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Michael Kleinaltenkamp
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Business Relationship Management and Marketing

Mastering Business Markets

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Springer Texts in Business and Economics

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Editors

Business Relationship Management and Marketing

Mastering Business Markets



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Preface

Economic value creation in business-to-business (B-to-B) markets by far surpasses value creation in the business-to-consumer (B-to-C) interface in many developed and emerging economies. In Germany as the most important European economy, the ratio is about three to one. Interestingly, this fact is barely reflected in how mainstream marketing scholars and professionals have treated the business-to-business realm; neglect may be the appropriate term. This is all the more astonishing since the paradigm shift from transactional to relational (B-to-C) marketing in the 1980s was nothing new to many B-to-B marketers.

For many organizations selling their products and services to other organizations, their customer relationships are one of their dearest assets. In our four books series “Mastering Business Markets”, the present volume touches upon all relevant questions B-to-B companies face with regard to the management of customer relationships and all marketing-related aspects within them.

We have divided the book into three parts: basic principles of business relationship management (Part I), analysis, goals, and strategies (Part II), and the implementation of business relationship management (Part III). Part I gives a thorough theoretical introduction based on both new institutional economics and behavioral B-to-B marketing theories. Part II is concerned with organization (re-)buying behavior, customer value and customer selection, and strategies within business relationship management. Finally, Part III provides tools and instruments to put business relationship management and marketing into practice: a chapter on the use of the classical marketing instruments within business relationships is followed by a reflection on how a B-to-B organization best organizes itself and its IT infrastructure to meet the challenges of business relationship management and marketing.

Since this book is based on the German language book “Geschäftsbeziehungsmanagement” but will be used in a newly created international Executive Education program, the China-Europe Executive Master of Business Marketing, we also deemed it worthwhile focusing on a special type of business relationships, those between organizations in Europe and China. Thus, Chap. 6 touches upon special questions that these intercultural relations bring with them.

As with every book, we have to say thanks to a number of people whose work was invaluable in finalizing this work. We thank all authors who contributed to this volume. Our sincere gratitude goes to our research associates Silvia

Stroe and Ilias Danatzis who managed the whole translation and editing process. The original translation was provided by A.C.T. Fachübersetzungen GmbH. At Springer, Dr. Prashanth Mahagaonkar served as our publishing editor. Finally, our research assistant Corinna Ebert rendered outstanding service to all layout works. Of course any remaining inconsistencies or mistakes are the lone responsibility of the editors.

Berlin, Germany
March 2014

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Part I

**Basic Principles of Business Relationship
Management**

Michael Kleinaltenkamp, Wulff Plinke, and Albrecht Söllner

1.1 Business Relationships as the Foundation of Business Relationship Management

1.1.1 The Business Relationship as a Competitive Marketing Task

Companies conduct business to achieve their objectives. They develop products and services, create markets, manufacture goods, choose business partners, submit bids and sell their products—all while dealing with the constant threat that other companies acting similarly (or even completely differently) may be more successful in attracting and enticing away their business partners. Of course, this game, which is known as **competition**, also offers opportunities—chances to close deals with new business partners who previously worked with other companies. When a company repeatedly does business with another company over an extended period, we generally refer to this as a “business relationship”.

This book deals with **marketing within business relationships**, primarily from the perspective of suppliers who then re-sell their products and services to other companies or government organizations (business-to-business marketing in sales markets).

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Marketing is intended to promote **customer benefits**, meaning to present the customer with an offer that he considers superior to those from other, relevant competitors. If there are no customer benefits, the customer will choose to do business with a competitor, the long-term result being a supplier's elimination from the competition. Thus, marketing can also be considered the **behavior scheme** of a supplier, intended to arm the company for survival amongst the competition. In this sense, marketing means taking action to ensure survival in the competitive environment, so to speak **individual competitive policy**. This includes all of the processes related to planning, coordination and controlling intended to help the supplier reach his competitive goals.

The premise on which the marketing concept is based is that a company that finds itself in a competition amongst suppliers can only survive if its **customers** make purchase decisions that provide the company with the required resources in the form of revenue. So marketing as a behavior scheme is geared towards offering the customer services that in turn induce the customer to grant the required services to the company (Pfeffer and Salancik 1978; Utzig 1996).

Marketing as a way to secure the resource "customer" can have many different shapes, depending on the structure of the competitive arena. The **competitive arena** is a certain specific manifestation of competition. This type of manifestation arises from the structure, sequence and result of competition. The competitive arena is a virtual arena as the supplier experiences it. It is not simply fateful but—in the case of an ongoing transaction—the result of decisions made by the supplier, competitors and even third parties. In the case of new business, the supplier has already decided to enter a certain field of competition with a certain offering, thus changing the balance between the existing suppliers and customers.

When defining the relevant arena, a supplier must be careful not to specify it too broadly or narrowly. It is certainly possible that a supplier battles competitors who are objectively not truly competitors or that the company does not have an overview of competitors who define "their" arena differently and may potentially be more successful as a result (Abell 1980; Backhaus and Schneider 2009). A supplier must establish various parameters to define the arena. These include the target customers, their quantity and the solutions they expect; the number of relevant competitors and their behavior scheme; the role of potential third parties; the rules of competition and the degree of success to which the suppliers aspire.

In the business-to-business field it is the norm that a supplier does not have only one customer for the products and services that he offers—just as a purchaser typically contracts with more than one supplier for the products and services that he purchases. A specific relationship between a supplier and a purchaser (the dyad) generally constitutes only a segment of all business relationship that the two parties live in (Refer to Fig. 1.1).

Thus, a specific business relationship is a potential definition of the competitive arena. The individual customer and the competitors that compete for the customer form the specific part of the market situation that is selected as the focus of competition of a supplier. **Marketing in business relationships** (synonymous with business relationship management, relationship marketing, relationship

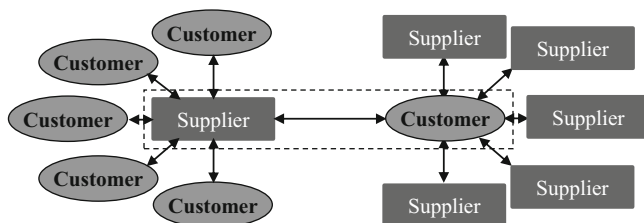


Fig. 1.1 Dyadic business relationship as part of supplier/purchaser relationships

management) is a behavior scheme that relies explicitly on the existence and the significance of **lasting** exchange relationships between **one** supplying company and **one** customer, and that focuses its marketing measures on the repurchase behavior of the customer. Horizontal business relationships (e.g. cooperations between competitors, alliances, cartels) are not discussed in this book. The subject is rather the processes of ongoing market exchange between a certain supplying and a certain purchasing company or: It is about managing **repurchasing** and **reselling**.

The subject of marketing in business relationships is one that has gained substantial significance in theory and in practice over the last few decades. The increase in relevance was triggered by fundamental changes in market processes that vastly changed the rules in these competitive arenas.

1.1.1.1 Changes in the Field of Technology

Such changes have been and are still apparent in the fields characterized by technical innovations. They affect the development and manufacturing processes as well as application processes. The most pertinent fields include information technology, communication technology, traffic engineering, aerospace technology and networking of various enabling technologies used in manufacturing and logistics systems.

The technical advances are joined—particularly in the business-to-business markets—by profound changes in **sales activities** and **procurement activities** related to systems and process technology. In strategic investment situations purchasers have absolute freedom of choice **before** committing to the technology-based system; however, once they have made the investment decisions, they feel a strong sense of being bound to the technology and/or the supplier. Decisions on technology investments cause customers to make far-reaching commitments that pre-determine future decisions.

It is not only technology that shapes this evolution: Distinctive, computer-supported networking between customers and suppliers is a sign of this new age. Just-in-time systems as extreme manifestation of networking and continuity of supply relationships are a form of technology-based cooperation and are a fundamental industrial standard today. Electronic ordering and invoicing systems are also parts of such systems. The business of complex systems for office organization, communication technology and factory automation has become increasingly important—these are all fields in which customers see themselves as locked into decisions

made earlier on the one hand and foster expectations as to the future benefits of certain technologies on the other hand. Both of these reasons have made long-term cooperation between suppliers and customers the predominant pattern.

Thus market transactions in the field of new technologies should not be viewed and interpreted as single transactions but largely as decisions on whole **conglomerates** of market transactions. This is why the suppliers' marketing strategies tend to be geared primarily towards one single customer (or a closely linked configuration of companies) and a sustainable solution to that customer's problems as well as towards customer and supplier both growing along with technological advances.

1.1.1.2 Changing in the Field of Marketing

Innovations in the field of technology are not the only catalyst for changing market processes. Another factor is changing strategic behavior patterns that develop as a result of the battle for competitive positions. Such patterns are not only a result of changing technology, they actually have an impact on the market process. This includes particularly evolving management and organizational structures within the company (e.g. lean management, business process re-engineering, outsourcing) as well as the general trend to consolidate while at the same time practicing division of labor in regard to global competition. In a time of **focusing on core competencies**, i.e. decreasing vertical manufacturing, the strategy of closer cooperation between suppliers and customers (e.g. in the form of simultaneous engineering or concurrent engineering) brings about substantial **procurement concentration**, with a declining number of suppliers per customer for a certain product. The increasing orders for research and development are another reason for close **cooperation** between suppliers and customers in these fields. A single customer can play such a significant role that he can himself represent a strategic business segment (e.g. an airline as customer of a catering supplier; a telecommunications company for a producer of communication technology).

Technical developments and changes in the field of marketing have caused us to observe a gradual narrowing of the market focus. Whereas it used to be the case that marketing concepts tended to apply the guideline of attempting to reach as many customers as possible with a certain range of products or services, nowadays the focus is on a single customer or a small number of customers along with a broadening of the problem solving perspective for the customer(s).

Carefully complied customer analysis and customer evaluation are applied to satisfy strategically important customers and groups of customers to the greatest extent possible. Figure 1.2 illustrates the correlation.

1.1.2 Definition of Business Relationship

In this section we consider a business relationship to be the consequence of market transactions between a supplier and a customer that is not random. "Not random" means that, on the part of the supplier and/or customer, there are reasons that either

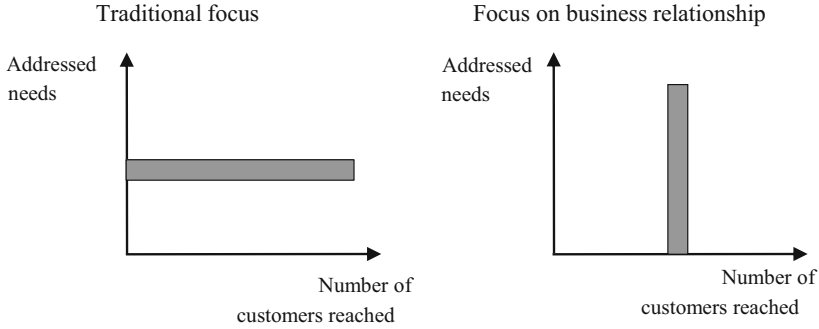


Fig. 1.2 Business relationship management—altered market focus. Source: Based on Rogers and Peppers (1994)

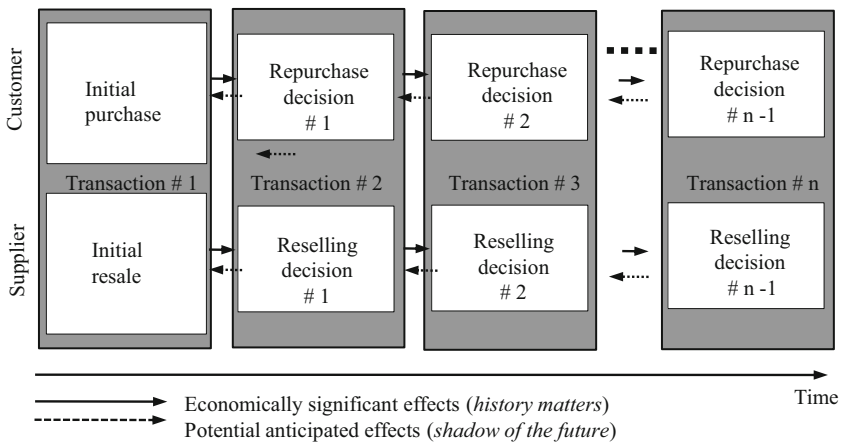


Fig. 1.3 Business relationship as a series of transactions

make systematic linking of market transactions seem sensible or necessary or that actually lead to linking. So a business relationship—as demonstrated in Fig. 1.3—can be seen as a series of market transactions between which there is an inner connection (Plinke 1989).

Every business relationship begins at the time of the first transaction: the initial purchase by the customer and the initial sale by the supplier. Once a business relationship has been established, it leads to a respective number of repurchase decisions on the part of the customer and reselling decisions for the supplier. The fact that this happens and that it is “not random” can be attributed to economically significant factors—which will be explained in more detail—on both sides. Such reasons can originate from past transactions (*history matters*) or due to potentially anticipated effects that do not become relevant until subsequent transactions occur (*shadow of the future*).

So in this sense—and to some extent in contrast to colloquial understanding—not every meeting of business people representing the supplier and purchaser can be considered a business relationship. Rather the focus of the previous definition is more on understanding the business relationship as a “relationship between businesses” in the sense of single market transactions conducted by identical partners, i.e. the same supplier and customer companies.

This does not mean that “relational” elements affecting the relationship between the negotiating parties are not relevant within such business transactions. This applies even more as the transactions in question become more “complicated,” meaning as more things need to be clarified, as the partial services related to the transactions grow, as the risk perceived by the involved parties increases, etc.

So for example, when a 3-year contract is entered for outsourcing all of a company’s IT infrastructure, and then later during the term of the contract, there are many aspects that have to be negotiated. And as a result of the contract many contacts are made between various persons at different levels of the hierarchy in both the supplier’s and the purchaser’s company. On the other hand, routine procurement of wearing parts can be triggered with an online order; processing and shipping are more or less automatic.

In scientific literature, these different (extreme) types of transactions are referred to as “discrete” (in the sense of “simple”) and “relational” (in the sense of “complex”). The respective features of the two types are shown in Fig. 1.4.

The characterizations clearly show that in relational transactions—as opposed to discrete transactions—relationships between the participants (social contacts, regular sharing of information, proactive and cooperative conflict solving processes, etc.) not only occur randomly, they are essential to mastering the wealth of tasks related to developing and processing the transactions. Nevertheless, such a complex and thus relational transaction can be a standalone transaction, not being dependent in any way on a business relationship.

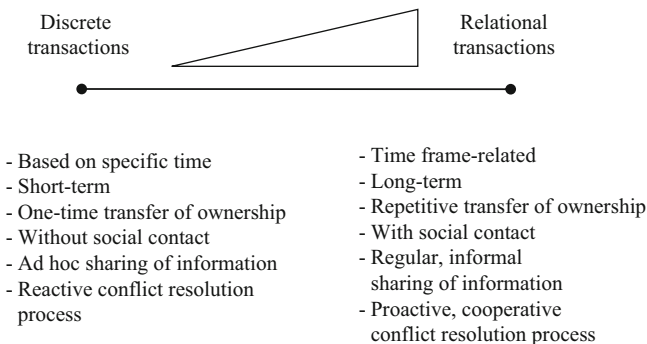


Fig. 1.4 Features of discrete and relational transactions. Source: Based on Macneil (1980), Werner (1997), Zimmer (2000)

It does not become a business relationship—in the sense understood here—until

- A second transaction follows the first and the second transaction was entered into because of the (positive) effect of the way in which the first transaction was completed or
- Such a transaction was preceded by another transaction, the course and result of which prompted the same partners to once again do business with one another.

Thus, there can be many different constellations of business relationships: Sometimes there can be a sequence of relatively simple (routine) transactions, sometimes a sequence of complex, long-term transactions, or a combination of simpler or more complex transactions that occur more or less alternately. It is easy to see that, depending on the shape of such constellations, the links between the various transactions can vary greatly in the level of distinction (Palmatier et al. 2006).

And the type of internal links can be vastly different as well. One can differentiate between one-sided and mutual commitments, and it is imperative to differentiate between the reference object of the internal link. Table 1.1 shows the ideal possible cases.

Commitments between suppliers and customers can come about based on the *object* of the transaction. This means that a **customer** is so convinced of the merits of a purchased product or service (or is more or less dependent on acquiring it) that the decision is made to purchase it again. Observed behavior patterns can be subsumed under the concepts of brand loyalty (one-sided commitment to a product brand), system loyalty (one-sided loyalty to a system architecture, e.g. Profibus) or loyalty to a technology (one-sided commitment to a technology, e.g. laser technology).

When a buying company is one-sided oriented, it means that the customer firm is loyal for reasons that best suit its own plans, regardless of the attitude or behavior of the selling company. For his part, a **selling company** can also be loyal, when in pursuing its own advantages it recognizes reasons to stay with one subject (e.g. certain core competencies and core products) and to thus commit one-sidedly to certain solution expectations. We refer to such commitments as

Table 1.1 Manifestations of business relationships

Reference object	Object reference	Personal reference	Company reference
One-sided commitment by purchaser	Brand loyalty System loyalty Loyalty to a technology	Personal loyalty	Store loyalty Supplier loyalty
One-sided commitment by purchaser	Problem loyalty	Personal loyalty	Customer loyalty
Mutual commitment	Reciprocal business relationship	Personal relationship	Business relationship, in the proper sense

problem loyalty. When the commitment is mutual, it may be based on a reciprocal business relationship, e.g. when an automobile manufacturer supplies the majority of the vehicle to a car rental company and, in return, has the rental company manage its own fleet (*fleet management*).

Commitment can also evolve from an affinity to or between **persons**, whereby there must again be differentiation between one-sided and mutual commitment. This is referred to as personal loyalty when it is related to the individuals of provider and/or a customer company; mutual affinity is referred to as personal relationships. The commonly used term is “business friendship.”

Finally, the **corporation as such** can be the reference object of a commitment, regardless of persons and specific products or technologies. When the commitment is one-sided **on the part of the purchaser**, supplier loyalty and store loyalty can be typecast (Wind 1966, 1970; Bubb and Van Rest 1973; Cunningham and Kettlewood 1976; Bonoma et al. 1977; Jarvis and Wilcox 1977; Mathews et al. 1977; Engelhardt 1979; Hannaford 1979). Supplier loyalty means that a customer prefers to choose the same supplier, regardless of the problem and the product in question. Accordingly, customer loyalty on the part of the supplier is a manifestation of the loyalty. Customer loyalty means that, based solely on own plans and independent of the attitude and behavior of the customer, the supplier is interested in continuing the supply relationship with this customer. Mutual commitments based on the respective partner company are to be typecast as **business relationships (in the proper sense)**.

There is obviously some overlap with these types. For example, loyalty to a company can certainly go along with loyalty to persons or products or services. However, this does not change the fact that there are commitments to companies that have no reference to persons or objects.

We will now examine the field in Table 1.2 that classifies the **business relationship in the proper sense** as a special type: Both parties have an interest in the relationship—which does not eliminate the possibility that reasons for and intensity of the commitments may be asymmetrical—and the reference object of the commitment is the company. The business relationship will be examined by the **type of internal link** between the transactions, looking at two dimensions: the situation of the relationship before the commitment occurs (*ex ante*) and the situation after (*ex post*); and the differentiation of whether the business relationship was planned or whether it evolved *de facto*. There are four potential states; refer to Table 1.2. The typology of the business relationships applies to both the supplier and the customer; however, for now we will examine only the customer.

Table 1.2 Attributes of business relationships

Attributes of business relationships in the proper sense	De facto business relationship	Planned business relationship
Ex ante situation	Case 1a Isolated transaction	Case 2a Strategic decision
Ex post situation	Case 1b Creeping commitment	Case 2b Lock-in effect

1.1.2.1 Case 1a

Cases 1a and 1b describe the **de-facto business relationship**. Such a relationship evolves unplanned and often unnoticed (Kleinaltenkamp 1993). Many aspects of this are conventional wisdom. First case 1a: A customer wants to begin a transaction with a supplier. S/he has no previous experience with this customer and expects no repercussions on future transactions—it is an isolated transaction. The customer's preference Z is the result of a simple comparison of the benefits of the two examined suppliers, S and SC . The preference $Z_{N/S}$ is simply the customer benefit that customer N reaps by choosing supplier S . The competitor SC represents the **comparison level** for evaluation of supplier S .

The de-facto business relationship (case 1a)

$$(1) \quad Z_{N/S} = (b_S - c_S) - (b_{SC} - c_{SC})$$

$$> \quad 0$$

with

$Z_{N/S}$ = Preference of customer N towards supplier S (customer benefit)

b_S ; b_{SC} = Benefit of transaction with S or SC

c_S ; c_{SC} = Cost of transaction with S or SC

The customer will initiate the transaction if Z is positive. There is no commitment and the customer feels free to choose the same supplier or a different one next time—s/he is flexible. However, the options become limited when we examine case 1b.

1.1.2.2 Case 1b

There has already been a preceding market transaction that occurred without the intention of entering into subsequent transactions. In this case, the determinants for a second potential repurchase decision are related to the customer's **experience** with the initial purchase. All of the elements in definition (1) were initially expectation values and now, as far as supplier S is concerned, are values based on experience. The simplest way to explain a repurchase is the confirmation of expectations by the experiences. Supplier S asserts the customer benefit **ceteris paribus** based on his or her own behavior, because the customer is **satisfied** with the purchase decision and does not change his or her opinion of the selected supplier.

In this case the way the customer evaluates the supplier generally changes—and these changes tend to reinforce the inclination to repurchase. A significant factor is the reduction in the **risk** of cost-benefit determination. When presented with the choice between two suppliers who otherwise appear to be equal, in the future the customer will prefer the supplier with the lower risk, meaning that the customer benefit increases based on the experience that is reflected as a decrease in risk.

Furthermore, the customer's **transaction costs** fall due to experiences: Routinization of decision making processes, which can be attributed to defined interfaces to suppliers, proven sample contracts and equally proven social relationships to the supplier, reduce

the efforts related to procurement in new transactions. **trust** as a component of the attitude towards to supplier is established. It can be claimed with a high degree of certainty that, the more complex the transactions, the more quickly and more comprehensively the effect of experience as reductions in transaction costs occurs.

So in comparison to case 1a, something has changes in case 1b, and it was completely unintentional. A **creeping commitment** has occurred in the timing, reducing the number of potential suppliers from the customer's point of view (*creeping commitment*, based on (Robinson et al. 1967)).

If in a de-facto business relationship it happens that, after one or more market transactions the expectations are not met for a specific market transaction, the result is **dissatisfaction**. Which conditions could cause a customer to switch suppliers or to be willing to repurchase? First of all, the customer will repurchase if the perceived discrepancy between expectations and experiences is less than the subjective value of the savings in transaction costs. A certain degree of **lethargy** on the part of the customer can play a role: One becomes accustomed to the supplier and does not run away just because one is dissatisfied in a single case.

If dissatisfaction grows, the existence of **switching costs** must now be taken into consideration to explain the repurchase behavior. The customer will feel that there is something that binds him or her to supplier S or, in other words, that it will cost him or her something to switch from S to SC.

Keep in mind that costs are not only monetary: Anything related to switching that the customer perceives as strenuous, unpleasant, risky or time-consuming is considered for this purpose to be a cost of switching (Refer to Sect. 4.2). In the case examined here, a certain type of switching costs is relevant: The experience gained with the current supplier becomes worthless, meaning getting to know one another, establishing trust, functioning together, etc. can be of value only with this supplier. When the customer switches suppliers, the learning curve for transaction costs is replaced by a new learning curve (Refer to Fig. 1.5). The hatched area symbolizes the value of the switching costs $c_{S/SC}$ in this case.

Thus definition (1) must be modified in regard to the costs and benefits of supplier S from expectation values to values based on experience and expanded to include the amount of the direct switching costs $c_{S/SC}$.

The de-facto business relationship (case 1b)

$$(2) \quad Z_{N/S} = \begin{matrix} (b_S - c_S) \\ > \\ 0 \end{matrix} - [(b_{SC} - c_{SC}) - c_{S/SC}]$$

with

$Z_{N/S}$ = Preference of customer N compared to supplier S (customer benefit)

b_S ; b_{SC} = Benefit of transaction with S or SC

c_S ; c_{SC} = Cost of transaction with S or SC

$c_{S/SC}$ = Direct costs of switching from supplier S to supplier SC

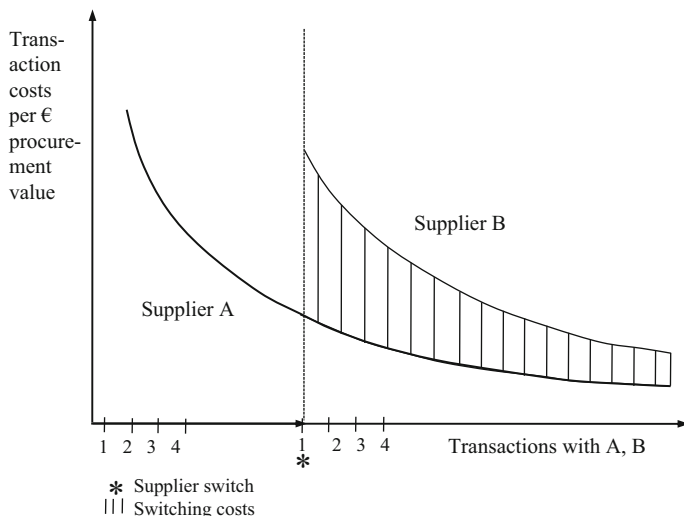


Fig. 1.5 Switching costs based on experience

If the equation (2) clearly differs from the value of (1) positively, the customer’s loyalty to the supplier has evolved creepingly. Along with effects of an experience of sustainable customer satisfaction, reduction of risk due to experience and the decrease in transaction costs, the switching costs may be reason enough for a customer to remain loyal to a supplier.

1.1.2.3 Case 2a

In the case of a planned business relationship, the customer (and generally the supplier as well) assumes from the start that cooperation will be long-term. It is clear to the participants that investments specific to the relationship will be incurred and that commitments will arise from which one can free oneself only by accepting the cost thereof. At the same time, one anticipates benefits that can result from entering into the business relationship. Such a decision making situation is considered by the customer to be **strategic**, when it results in far-reaching commitments that can vastly influence the chances of success, the costs and the flexibility of the customer. It is generally the sometimes extreme commitment that the customer feels to the business partner that is decisive. The customer firm often feels compelled to invest in hardware and software to be able to enter into a supplier-customer relationship—just think of **just-in-time** systems, joint development projects with the supplier or **value-adding** partnerships. This includes the choice of supplier when inventing in plant automation. The customer will take into consideration this restriction in flexibility for the assessments when beginning a

relationship with a supplier, meaning that the freedom that needs to be sacrificed must be compensated by appropriate—anticipated or expected—benefits of doing business with the supplier (Ulaga and Eggert 2006; Saab 2007). Before committing to a relationship, it is essential to estimate the benefits of the relationship as well as to assess the risks, meaning the damage that can result for failure to reap the benefits once the commitment has been made. The investments that the customer has made to initiate the supply relationship—and the anticipated values—must be considered to basically be lost when the supplier is switched; comparable investments must then be made for a different supplier. This raises the barriers that the customer faces to ending the business relationship accordingly.

The customer will make the commitment to S when the ex-ante analysis of the comparison to supplier SC indicates that a relationship with S is more beneficial. Because no choice has been made before the time of this decision, the two potential business relationships with S and SC are illustrated as simple net present value models. The customer's preference Z in relation to S is the difference between the two net present values, taking into consideration the respective specific investments in the business relationship. Since in an ex-ante situation the anticipated exit barriers appear the same as entry barriers, the preference for supplier S under the same conditions increases as the anticipated costs for switching from S to SC decrease (The opposite applies from SC to S). This is why the anticipated switching costs with a negative value must be considered.

$Z_{N/S}$ is the present value of the relationship with S minus the present value of the relationship with SC. If this value is greater than zero, the customer will choose S and enter into a relationship. To simplify the process, the probability of the alternatives S and SC is considered to be equal. This seems permissible since we are not dealing with a planning model but with the fundamental definition of the conditions for the success of business relationships.

The planned business relationship (case 2a)

$$(3) \quad Z_{N/S} = \begin{aligned} & \left[-A_{S0} + \sum (b_{St} - c_{St}) (1+i)^{-t} - \sum c_{S/SCt} (1+i)^{-t} \right] \\ & - \left[-A_{SC0} + \sum (b_{SCt} - c_{SCt}) (1+i)^{-t} - \sum c_{SC/St} (1+i)^{-t} \right] \\ & > 0 \end{aligned}$$

with

$-A_{S0}; -A_{SC0}$ = Investment in business relationship with S or SC in t_0

$b_{St}; b_{SCt}$ = Benefits of business relationship with S or SC in t

$c_{St}; c_{SCt}$ = Cost of business relationship with S or SC in t

$c_{S/SCt}; c_{SC/St}$ = Direct cost of switching from S to SC or from SC to S in t

i = Required rate of return

t = Planning period

This definition reveals the significance of long-term risk management in business relationships with strong dependencies. So for example, suppliers of computer-aided production technology must place particular emphasis on establishing trust

when acquiring new customers. They have to assure their customers that they can keep up with the latest technology over the long term. It becomes apparent that customer recognize and evaluate competitive advantages related not only to single market transactions but to business relationships as well.

1.1.2.4 Case 2b

When the decision has been made to choose supplier S, the result—based on Williamson (1985)—is the so-called “Lock-in effect”: The customer is loyal to the chosen suppliers, because a commitment has been made that makes it difficult to switch. The customer will remain loyal to this relationship as long as the “damage” in comparison to the net benefits is less than the now anticipated switching costs, meaning as long as the value $Z_{N/S}$ is greater than zero.

The planned business relationship (case 2b)

$$(4) Z_{N/S} = \frac{[\sum(b_{St} - c_{St})(1+i)^{-t}] - [\sum(b_{SCt} - c_{SCt})(1+i)^{-t}] + [\sum c_{S/SCt}(1+i)^{-t}]}{0}$$

with

$-A_{S0}; -A_{SC0}$ = Investment in business relationship with S or SC in t_0

$b_{St}; b_{SCt}$ = Benefits of business relationship with S or SC in t

$c_{St}; c_{SCt}$ = Cost of business relationship with S or SC in t

$c_{S/SCt}; c_{SC/St}$ = Direct cost of switching from S to SC or from SC to S in t

i = Required rate of return

t = Planning period

The customer’s flexibility is determined not only by experiences with the performance of the current supplier. Actually, factors outside of the supplier-purchaser dyad can change **expectations** related to benefits and costs, which in turn influence the decision of whether to stay with the supplier or to switch. Actions of competitors or additional competitors can change the comparison level for the current suppliers. Technological and structural developments can also change the customer’s attitude (evaluation of the benefits offered by the current supplier). Other exogenous factors such as new laws are also aspects that can have an influence.

As previously mentioned, the current examination of a dyadic supplier-purchaser relationship does not always correspond to actual conditions. Multi-level business relationships often exist (e.g. component supplier—system supplier—operator). And frequently several suppliers work together to solve a customer’s problem, which can lead to complex structures in business relationships. Another dimension that adds to the complexity is the multi-personality of the decision-making process in the organizations involved (Fließ 2000).

To summarize: A business relationship is a consequence of market transactions between a supplier and a purchaser that is not random. “Not random” means two things. Either there are reasons on the part of the supplier and/or customer that make

a planned link between market transactions appear practical or necessary (planned business relationship based on aspects of benefits or dependency). Then specific investments are made in the business relationship. Or there are reasons that de facto lead to a link (de-facto relationship, e.g. due to habit or learning processes). In such a case **values** emerge in the relationship that would result in a loss were the relationship to be dissolved. In both cases, the business relationship has a more or less positive significance for both parties (positive net benefit). Investments, accumulated and developed values, and significance are thus the general commitment forces that reflect the “internal link” between the repeated market transactions.

1.2 Internationalization of Business Relationships

A primary challenge to the management of business relationships is the increasing internationalization of such relationships. Paul Krugman, one of the most influential business journalists in the USA, emphasizes the potential of international division of labor (Krugman 1999). According to Krugman, the essence of globalization is not that an increasing number of participants have to share an existing economic pie. Rather globalization can generate additional prosperity by greater international division of labor. Globalization is understood in this sense as a process of expanding the potential for international division of labor, primarily by reducing the costs of communication and transport and by dismantling trade barriers. Globalization affects two areas: It provides many more ways to create value, offering more activities with which a company can create value for its customers, and it extends and expands the potential markets.

By merging production capacities in the course of specialization and division of labor, additional cost benefits and potential for prosperity can be realized. International division of labor and international trade immediately present two problems: Producers can concentrate on a limited product range and better economies of scale. This is enabled by international trade, which grants access to new markets. And consumers benefit from a wider range of available products. International division of labor and international trade offer consumers millions of product variations in the field of automobiles without excessively high price tags.

In addition to the prosperity promoted by the international cooperation, the intensive international **competition** is a source of growing prosperity for consumers. The process of globalization causes the number of suppliers and buyers to increase. Since in many markets more and more suppliers are competing for a scarce commodity that not all suppliers can have (the purchasing power of consumers), the competition tends to become fierce. Free trade impedes the establishment of national monopolies or cartels. Free access to the market is thus an effective agent in combating the establishment of market power on the supplier side. However, in recent years it can increasingly be observed that companies attempt to face the challenge of international competition with a global monopoly.

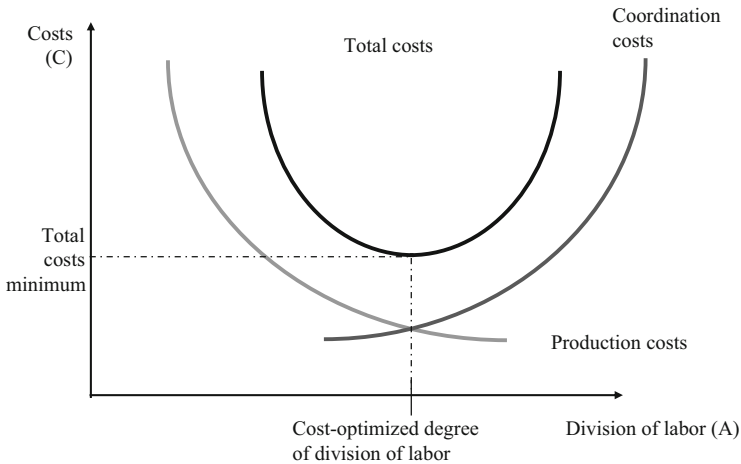


Fig. 1.6 Production and transaction costs as a function of the degree of division of labor

The process of globalization, which has accelerated steadily over recent years, is facilitated by a reduction in the coordination costs of international division of labor.

From the economic point of view, the degree of international division of labor is determined particularly by the transaction costs—meaning the cost of coordinating the division of labor (Refer to Chap. 2). As the division of labor increases, the transaction costs progress in exactly the opposite direction of the production costs (Refer to Fig. 1.6).

While the production costs decrease as the degree of division of labor between international business relationship partners increases due to the effects of specialization and economies of scale, the need for coordination and thus the transaction costs rise as division of labor increases.

The causes of a potential reduction in production costs due to international cooperation have become well known, primarily through the work of Adam Smith and David Ricardo (Söllner 2008). Even after many modifications and advancements of their work, the added benefits of cooperation can be attributed primarily to two main aspects:

1. The parties have different (absolute and comparative) cost items, making specialization and exchange of commodities beneficial.
2. The parties possess very different resources and capabilities. This makes it possible to increase the variety and quality of the solutions offered, meaning the products and services (Krugman 1999). This sometimes has far-reaching consequences for the (re)structuring of the respective value-added chain (Kleinaltenkamp 2007).

The generally rising transaction costs can be attributed primarily to the increasing complexity of international transactions. A few examples illustrating the

increased need for coordination in regard to international business relationships as opposed to domestic cooperative relationships are: cultural differences, different legal conditions, higher communication costs, national borders and isolated economic areas. Additional examples are easy to find.

When examining both transaction costs and production costs as a factor of the degree of division of labor, there is a point—the minimum of the total costs curve in the graph—at which an additional increase in international division of labor does not lead to a gain in prosperity. Thus transaction costs limit the expansion of international division of labor. At a certain point, intensifying international business relationships even more does not make sense, because the production cost advantages related to division of labor are consumed by higher transaction costs.

But in recent years there have been vastly different developments particularly in regard to transaction costs. On the one hand, new security risks have led to a rise in transaction costs (Brück and Schumacher 2004). On the other hand, advances in technology in the communication field, the decreasing cost of shipping, as well as political developments opening formerly closed markets have caused transaction costs to go down. This contributed to the permanent growth of various markets. In some branches it only makes sense to talk about a global market—in regard to the sales market as well as to procurement markets. This development is reflected in an unprecedented surge of **offshoring** and **outsourcing** (Pajak 2006) and in a complete re-design of companies' value chains.

There are actual many indications that the revolution in information and communication technologies enables completely new forms of cooperation for which neither place nor time overlap is required to perform various partial services. In fact, people from different places around the world can work together with no time restraints whatsoever. International business relationships, networks and virtual organizations as a special type of network are becoming more and more of a business reality. The dissolution of vertically integrated and diversified corporations into networks is described by Miles and Snow (1986) like this: *“Business functions such as product design and development, manufacturing, marketing, and distribution, typically conducted within a single organization, are performed by independent organizations within a network”* (Miles and Snow 1986).

According to Sydow (1992), **corporate networks** can be distinguished by close coordination amongst the network parties while still retaining legal and sometimes the economic independence (Sydow 1992).

A wealth of differently organized participants tend to gather around core corporations, which are in turn surrounded by many cooperative relationships with other participants. Corporate networks consisting of business relationships of differing intensity represent an opposite pole to forms of business organizations with long-term, defined restrictions between internal and external matters, strong locational ties and a relatively stable allocation of resources (Picot et al. 2003).

In light of such development, it becomes a central and new challenge to management to analyze the consequences of the output of goods and services in value-adding chains and networks when such goods and services are being produced in different places at different times and through a division of labor. To take

advantage of the opportunities presented by business relationships and networks, it is essential to critically examine the chances and risks of these new organizational principles.

As previously mentioned, the reduction in transaction costs resulting from the rapid advances in information and communication technology (I&C technology) have been the driving force in increasing internationalization of business relationships between companies and their networking of autonomous participants. This technological factor is reinforced by many other developments at different levels (Picot et al. 2003):

1. The level of the corporate environment
2. The level of the corporation's market relationships
3. The level of the organization and its members.

The question of location can be resolved at the **corporate environment** level not only by the rapid technological advances but also because of other changes driving progress. The development and promotion of business clusters as well as cross-border clusters are a measure applied in regional politics to offer an opportunity to promote economic survival in structurally weak areas (European Commission 1994).

At the **market relationships** level of a company, trends toward globalization not only offer opportunities for companies and participants to network, they virtually compel networking. The new market opportunities that companies have in international markets are countered by new competitive pressure. A company can meet this pressure by increasing its **innovative force** and improving its **cost efficiency**. The innovative force can be strengthened by including the best and most capable companies and people in the value-adding process. Since it is safe to assume that talent and readiness for action are not concentrated in one location but spread across different locations around the world, a corporation can increase its innovative capacity by networking the knowledge holders. In regard to cost efficiency, companies working as networks can achieve progress e.g. by consciously using regional differences in certain costs (wages, R&D costs, etc.) to their advantage when planning their cost positions. Different time zones, working hours, etc. can also effect additional acceleration. Cross-border division of labor is a unique challenge to suppliers and purchasers in this situation (Nguyen and Nguyen 2010). There are also different attitudes on the different forms of division of labor that can be attributed to the various cultures (Homburg et al. 2009) and (Andersen et al. 2009).

At the level of the **organization**, there are clear indications that members of the organizations—particularly those who are employees of an organization—now have greater demands and expectations of their employment. Especially the desire and the necessity to reconcile work and personal/family life have led employees to seek greater flexibility. New, networked organizational forms such as telework enable the employees' desire for greater flexibility and self-determination to

become a fundamental principle of the organization. This creates the conditions for more highly motivated employees and for attracting valuable new employees.

So at all three levels grounds can be found for the increasing significance of business relationships and corporate networks, including those taking place in an international context.

1.3 Responsibility in Business Relationships

Globalization and internationalization of the value-adding chains of many companies have created new opportunities for companies and consumers. At the same time, the discussion of morally appropriate corporate behavior has been taken up again. Especially the working conditions of foreign partners in business relationships have moved more and more into the public eye (Table 1.3).

Example 1: Catastrophic Conditions at Asian Suppliers to Motorola, Nokia and co

Famine wages, poisoning, 13-h shifts and 7-day weeks—according to a study conducted by the Dutch organization “Stichting Onderzoek Multinationale Ondernemingen” (Somo, Centre for Research on Multinational Corporations) on behalf of the EU commission, Dutch ministries and trade unions, the working conditions at some of the suppliers to the world’s largest mobile phone producers are catastrophic. Nokia (Finland), Motorola (USA), Samsung and Sony Ericsson purchase vast quantities from suppliers who force their employees to work under inhumane conditions. For example, the Chinese supplier Hivac Startech produces acrylic lenses for mobile phones of Motorola in the Special Economic Zone Shenzhen near Shanghai. There are no adequate measures available to protect the employees from the toxic substance n-hexane contained in the solution used to polish the lenses. Nine employees had to be treated in hospital for acute poisoning. According to Somo, one of the women had to have an abortion as a result of the poisoning. Joseph Wilde, one of the co-authors of the Somo study, is convinced that these distressing revelations are not isolated cases: “This is a fundamental problem of the entire mobile communications industry.” Pricing pressure in the industry and the resulting “complex supply chains” have caused even major corporations such as Nokia and Motorola to lose sight of their suppliers (Wendel 2006).

The general public as well as many consumers judge these and similar cases critically. This means that corporations and managers must examine the behavior of their business partners as intensively as they do their own. And it is definitely not easy for them to find their place in the field of tension between acceptance by society and increasing competitive pressure.

Table 1.3 Working conditions at mobile phone suppliers

Supplier companies (selection)	Customers	Hours per workday	Weekly wage in US dollars	Workdays per week
Hivac Startech (China)	Motorola	10–12	0.24	7
Giant Wireless (China)	Motorola	10–13	0.12 (2003) 0.44 (2006)	6–7
Kangyou Electronics (China)		10–13	0.33–0.37	7
LTEC (Thailand)	Nokia	12	0.32	7

Source: Wendel (2006)

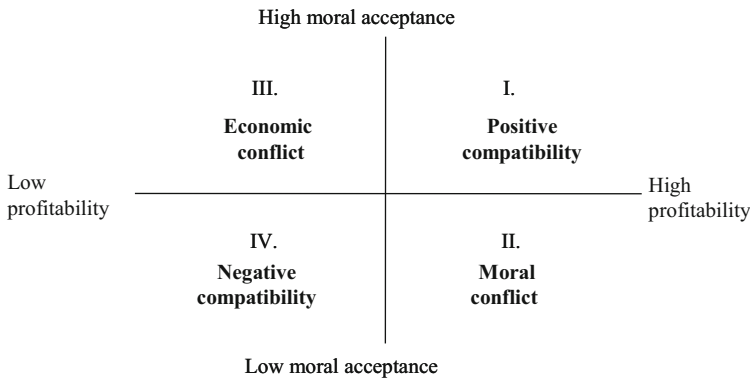


Fig. 1.7 Homann’s four-quadrant graph. Source: Based on Homann (1994, p. 116)

Karl Homann can contribute significantly to orientation in business relationship management with his findings. Homann recognizes the long-existing conflict between economic rationality and moral behavior and illustrates it clearly in his four-quadrant graph (Refer to Fig. 1.7). The two axes represent the effect of a certain corporate action—e.g. choosing a certain partner for a business relationship—in relation to the moral acceptance of the action as well as to the profitability of the acting corporation.

Quadrant I describes the case of a complementary relationship between moral behavior and economic success. This can potentially be the result of the economic regulatory framework demanding and enforcing morally correct behavior of all competitors, meaning that, when the rules are followed, there are no sanctions imposed that would have a detrimental effect economically. Or it can be the benefit of profitably “selling” moral behavior, e.g. by using it for effective advertising.

Quadrant II demonstrates a case in which corporate behavior—even when it is legal—does not reconcile with the moral expectations of a society. The company decides is this conflict for profit and against morals. This decision—to the extent that it is even substantiated—is usually justified by pointing out the competitive pressure. Critical news coverage—as in the case of Motorola—can cause

corporations to rethink their policies when they have a negative effect on profitability targets.

Like quadrant II, quadrant III represents a conflicting relationship between profitability and moral acceptance. However, in this case the company chose morals, thus rejecting profitability.

Quadrant IV stands for the case in which an action is neither accepted nor profitable. Withdrawal from the market is a probable strategy in this case (Homann 1994).

Homann's graph clearly demonstrates that moral behavior under conditions of strong competitive pressure can pose a problem for a company. A regulatory framework that consistently integrates and enforces moral requirements would resolve the conflict between morally correct behavior and economically rational behavior in a competitive environment. Such a framework would specify moral expectations as restrictions applicable to all market participants. Competition would occur as "plays" within the rules of the game and not as violation of moral standards. But, particularly in the international context, such a framework as the "systematic place of morals" (Homann 1994) is still far away. The countries have virtually no chance of effectively enforcing an economic framework on internationally operating corporations. This deficit is offset only partially by the rules of the game at the level of regional affiliations, by WTO rules or by monitoring by NGOs.

Thus, the conflicts demonstrated above as cases II and II will often occur in reality. Homann considers two types of strategies feasible as a reaction on the part of the corporations: The **competitive strategy** and the **regulatory policy strategy**.

The **competitive strategy** is aimed at showing moral behavior because the partners to the transaction prefer business partners with moral integrity or are potentially interested in such partners. This preference can relate to vastly different reference objects, such as products, production methods, emphasis on employees or environment, etc. It is principally about discovering opportunities for profit that are based on morally acceptable behavior. This would reconcile moral and economic goals (Homann 1994).

A concept such as **Corporate Social Responsibility** (CSR) can also be considered a competitive strategy. CSR means that companies behave in an ethical manner and, as "good citizens," accept responsibility for society that goes beyond the responsibility of their corporate activities. However, Homann believes that such a concept will be implemented only when it also means economic success for the respective company. "*No one can expect a company to accept severe economic disadvantages for its morally correct behavior, while competitors acting with fewer morals reap all the profits*" (Homann 1991).

Even when a competitive strategy is not feasible, corporations are not divested of their ethical responsibility. They are then obligated to point out the deficits of the existing framework with a **regulatory strategy** and to work towards abolishing such deficits (Homann 1994). One example of a regulatory strategy is the active support of the "Global Compact" initiative of the former general secretary of the United Nations, Kofi Annan (Söllner 2008).

Case Study: Nike

Nike is as successful company that designs, sells and markets sporting goods but does not produce the items themselves. It instead consistently takes advantage of the opportunities presented by the global division of labor. Nike's manufacturing has been completely outsourced. Sometimes there are isolated market transactions with external manufacturers, but often the company relies on long-term business relationships.

In the early 1990s, a campaign was initiated to damage the corporation's image: Nike was publicly sharply criticized for the working conditions imposed by its suppliers (Locke and Romis 2009):

After initial defensive reactions, in 1992 Nike became proactive and formulated a "Code of Conduct" that all of its suppliers had to sign and publicize within their companies. The code obligates suppliers to comply with certain standards regarding the environment, working conditions, health and safety in the workplace. To enforce the "Code of Conduct" at the suppliers' facilities, Nike conducted numerous training courses with suppliers. A team made up of 90 compliance officers in 21 countries was put together to monitor compliance with the "Code of Conduct." About 1,000 production managers work directly with the suppliers. All Nike employees responsible for production and compliance receive training on the Code of Conduct, particularly in regard to labor standards, intercultural awareness and Nike's program "Safety, Health, Attitudes of Management, People Investment and Environment" (SHAPE).

Three different audits at the suppliers' facilities are also performed. The three audits are: a basic SHAPE audit; a more extensive audit of management and working conditions (M-audit); and regular monitoring by the Fair Labor Association (FLA). The FLA is a certified non-profit multi-stakeholder organization that conducts independent external monitoring to assess compliance with relevant standards on the part of participating corporations.

Research results show that, on the one hand, Nike's suppliers perform above average in factory audits. At the same time, the investigations also reveal that the working conditions in the various supplier companies from one and the same country differ vastly, from exemplary companies to those that violate the standards.

Exercises

1. Define marketing in business relationships. To what extent does marketing in business relationships support the existence of a company in the market?

2. State and explain the essential catalysts for changes in market processes and explain how these catalysts have contributed to the increasing significance of marketing in business relationships.
3. Explain the difference between “discrete transactions” and “relational transactions.” What is the difference between the two types of transactions?
4. Explain the various reference objects of loyalty or commitment within a business relationship.
5. Explain the different types and the features of business relationships.
6. Explain how transaction costs affect the degree of international division of labor.
7. How can the lack of an economic framework affect a corporation’s behavior in the market? Refer specifically to the moral acceptance of behavior as well as to the company’s profit goals.

Nike Case Study

1. Discuss the benefits that may be reaped by Nike outsourcing its production.
2. How does management differ when Nike performs isolated market transactions with suppliers as opposed to transactions within close business relationships? List arguments and systematize them.
3. To what extent does management of moral standards belong to management of business relationships and networks? Compare Nike’s behavior to Homann’s approach and assess Nike’s course of action.

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Theoretical Perspectives of Business Relationships: Explanation and Configuration

2

Michael Kleinaltenkamp, Wulff Plinke, and Albrecht Söllner

2.1 Theoretical Approaches to Explaining Business Relationships: Classification

The first chapter of this book presents the business relationship as a form of exchange and sharing amongst companies. Without expressly mentioning it, this already includes various theoretical perspectives regarding the phenomenon “business relationship” as well as potential constellations. It is obvious that, depending on the theoretic perspective chosen, a business relationship can be explained in different ways and the subsequent recommended actions can also vary.

As this chapter will show, research approaches to marketing in business relationships are very heterogeneous (El-Ansary 2005). This chapter intends to create awareness for the significance of different theoretical perspectives in regard to the topic business relationship.

Initial approaches to business relationship management first occurred and were first mentioned in publications in the 1950s, in the course of the development of earlier forms of key account management. The essential element remains the strategic and organizational focus of a supplier on individual, important customers (e.g. on large corporations specializing in consumer goods retail; refer to Sect. 7.1).

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But the true beginnings of business relationship research can be found in the late 1970s and the 1980s (refer to various assessments of the development: Backhaus 1997; Christopher et al. 2002; Bruhn 2003). Initial studies examining this phenomenon were conducted in both industrial marketing (part of what is now referred to as business-to-business marketing) and in services marketing. These studies naturally focused on the considerations that tended to deal descriptively with the meaning of business relationships and with their definition (Levitt 1985; Diller and Kusterer 1988; Plinke 1989) as well as certain characteristics, e.g. phases of a business relationship (Jackson 1985a, b; Dwyer et al. 1987; Sethuraman et al. 1988).

Other studies were devoted to special aspects or features of industrial business relationships, such as the constellation of sales processes in this context (Spekman and Johnston 1986), just-in-time supply relationships (Frazier et al. 1988; O'Neal 1989) or issues concerning customer evaluation (Turnbull and Wilson 1989).

The work of the IMP group (*Industrial Marketing and Purchasing*) assumed great significance during this time (Ford 1978, 1980; Hallén and Wiedersheim-Paul 1979; Hakansson and Wootz 1979; Håkansson 1982). Their work is distinguished by the fact that they assume a network perspective, meaning that not only the dyadic relationships between supplier and customer are examined; instead, their analyses attempt to include the entirety of all direct and indirect delivery and supply relationships in which a supplier is involved.

While the studies mentioned above concentrated on the relationships existing between companies, the work performed in the field of service marketing focused more on the relationships of consumers who purchase and use services. Particular attention was paid to the interaction between customers and employees of a supplier company that takes place when a service is provided as well as to the effects of such interaction, e.g. in regard to customer satisfaction, repurchase behavior, etc. (Berry 1983; Gummesson 1987).

The field of business relationship management became firmly established during the 1990s, with the publication of multiple theoretical-conceptual studies (e.g. (Heide and John 1992; Möllner and Wilson 1992; Morgan and Hunt 1994; Söllner 1999) and of the first text books on the subject (e.g. Kleinaltenkamp and Plinke 1997; Gordon 1999; Peck et al. 1999).

Finally, research on business relationship management received an additional boost in the first decade of this century, with the development and propagation of customer relationship management (CRM) (e.g. Payne and Frow 2005; Hippner et al. 2011; refer to Chap. 8). This was due mainly to information technology systems, which allowed virtually all processes of business relationship management to be supported and to be more effectively and efficiently structured.

These approaches to business relationship management as well as those mentioned later in this chapter focused on two central issues:

1. Which factors cause business relationship partners to commit to each other?
2. Which behavioral effects and intentions emanate from the commitment to a business relationship?

The answers to these questions and the conclusions drawn from them—particularly in regard to the constellation of business relationship management—can be very different, depending on the theoretical focus chosen.

2.2 Behavioral Approaches

Articles related to the behavior science of business relationship research focus particularly on the effects that occur at the level of single individuals. They deal with the occurrence of commitments as well as with the resulting effects on repurchase behavior and certain behavioral intentions of individuals. The fundamental pattern of behavioral explanatory approaches is shown in Fig. 2.1. The illustration indicates that single measures to promote customer loyalty to a supplier stimulate emotion, motivation and even the attitude of the individual and influence the person’s inner psychological processes. The commitment that results is either strengthened or weakened, depending on whether positive or negative effects are triggered in these areas. This, in turn, affects the behavioral intentions as well as the actual behavior of a person in regard to repurchase (intention), cross-buying (intention) or recommendation (intention).

Concepts that explain individual aspects of the emergence of commitments and loyalty in this regard are the learning theories, the theory of perceived risk or the dissonance theory (Homburg and Bruhn 2008):

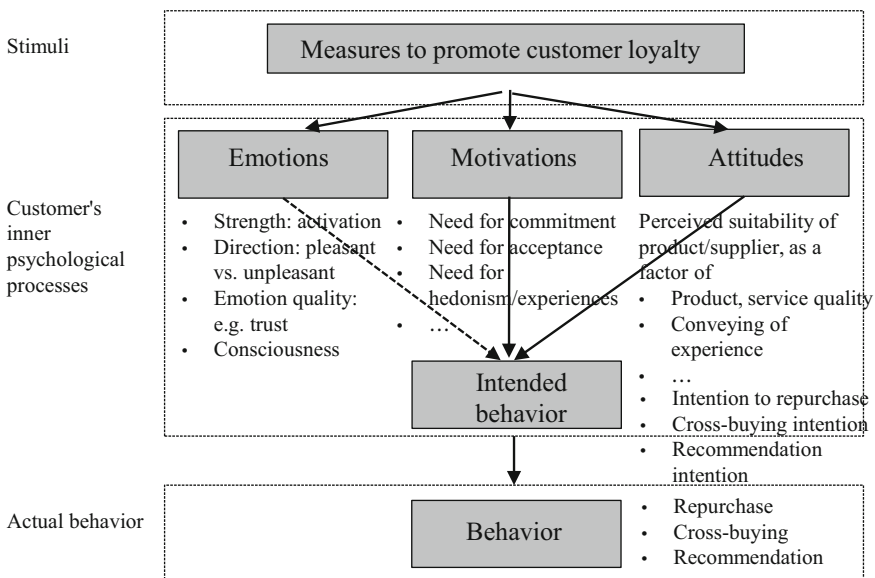


Fig. 2.1 Conceptualization of customer loyalty from a behavioral perspective. Source: Based on Weinberg and Terlutter (2003, p. 49)

- If, for example, the theory of learning by reinforcement is applied, beneficial past behavior is retained, while behavior that was not beneficial is relinquished or modified (Wilkie 1994; Engel et al. 1995). A customer's loyalty to a supplier always increases when the customer perceives a benefit from the business relationship or is satisfied with the relationship.
- The theory of perceived risk states that people attempt to minimize the risks that they perceive. Customer loyalty can occur in this sense, too, when customers adhere to their trusted and familiar purchase decisions and/or suppliers to minimize the risk of dissatisfaction (Hentschel 1991).
- The dissonance theory is based on the assumption that individuals strive for long-term equilibrium of their cognitive system (Festinger 1957). Reevaluation, additions or suppression are applied to attempt to abolish dissonance and to once again achieve inner equilibrium. If this is successful—in this case regarding purchase decisions made—it can lead to commitment to a supplier. If it is not successful, the intention to switch becomes stronger, resulting in a business relationship being terminated or not even entered into in the first place.

So the behavioral approaches offer insight that is relevant particularly to explaining individual behavior of customers in consumer goods markets. These approaches apply fundamentally to the behavior of persons dealing with (re)purchasing in companies as well. However, taken alone they are surely not significant, because they ignore some essential aspects of organizational purchasing processes. This particularly includes the effects of the cooperation of multiple persons in a (re) buying center as well as the fact that procurement decisions are made in an organizational environment geared towards making a profit (refer to Chap. 3). This last aspect has been especially relevant, as will be explained in the following section, to the significance that economic approaches based on cost-benefit as well as value aspects of business relationships have gained.

2.3 Social Psychological Scheme of Explanation: The Approach of Thibaut and Kelley

The social psychological theory by Thibaut and Kelley is another approach that was originally developed to explain individual behaviors but was then applied to organizational business relationships. It was designed to explain the occurrence of commitments amongst people in social groups. It is based on the theory that all human relationships are formed by comparing the costs and benefits of a relationship as well as the costs and benefits of other relationships in which they are involved (Thibaut and Kelley 1959). Although the concept was initially developed to explain individual human behavior from a non-economical perspective, the fact that it is based on cost-benefit considerations means that it can easily be applied to business relationships of companies. When this is done, a partner evaluates the results of a business relationship (RV) on the basis of two criteria. The first is the comparison level (CL) and is a measure of previous experiences. The experience

can have been gained from this business relationship or from a different one. Positive experiences increase the CL, while negative experiences decrease it. More recent experiences have a stronger effect on the CL than do older experiences. Situational influences also carry weight. So the CL is a measure of the **expectations** of the customer. The business relationship is perceived as “attractive” when the difference of costs and benefits of the relationship is greater than the CL. However, when the attractiveness of a relationship is determined in this way, it is not sufficient to be able to evaluate whether a partner will remain in a business relationship or not. This can be accomplished in the theory of Thibaut and Kelley by applying a second criterion, the Comparison Level for Alternatives (CL_{ALT}). This measure describes the ratio of benefits and costs in the best alternative business relationship that can possibly be achieved. By applying both CL and CL_{ALT} , a conclusion can be reached on the attractiveness of and dependency in the relationship. There are three different cases (refer to Fig. 2.2):

1. The current relationship is perceived as more attractive than the CL, meaning that the value RV also exceeds the attractive alternative relationship CL_{ALT} . Because of this alternative, the partner in the business relationship is not dependent (s/he can switch and is then still above the expectation benchmark).
2. The current relationship value RV is higher than the CL, making the relationship attractive. However, CL_{ALT} is below CL, so the business relationship partner has no attractive alternative in this case. S/he is dependent.
3. The current value RV of the business relationship is lower than the CL, making the relationship unattractive. Since CL_{ALT} is below the current value, switching would be detrimental to the business relationship partner, who is already in an unattractive situation. S/he is dependent in an unattractive relationship.

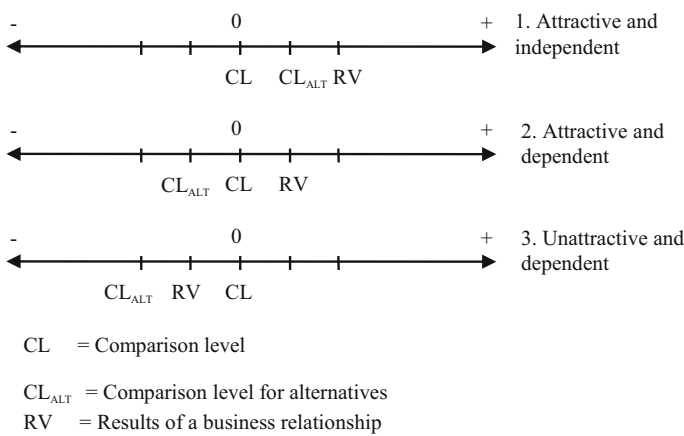
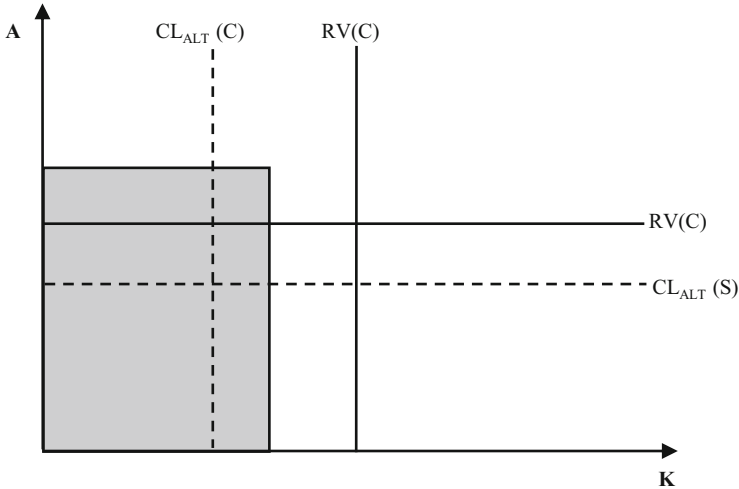


Fig. 2.2 Attractiveness of or and dependency in relationships. Source: Based on Herkner (1991, p. 398)



Legend: Refer to Figure 2.2

Fig. 2.3 Structure of dependency in a business relationship (example)

In the model of Thibaut and Kelley, attractiveness and dependency are the result of the difference between costs and benefits of an existing relationship, evaluated on the basis of the expectation benchmark for costs and benefits not specific to the relationship as well as on the specific benchmark of the cost-benefit ratio of a specific alternative. This means that, when defining costs and benefits, all of the cost components of the current business relationship as well as those related to switching the business relationship partner are considered.

(Un)attractiveness and (in)dependence can now also be used to describe the position of the two partners to one another, particularly in regard to business relationship management from the supplier's point of view (refer to Fig. 2.3).

In this example, the supplier S is in an unattractive business relationship [$RV(S)$ is less than $CL(S)$] and dependent as well [$CL_{ALT}(S)$ is even less than $RV(S)$]. Customer C, on the other hand, is in a relationship that is attractive for him [$RV(C)$ is greater than $CL(C)$], but is dependent, just like S [$CL_{ALT}(C)$ is less than $CL(C)$]: One sees a case of mutual dependency with asymmetrical distribution of attractiveness. These could offer starting points for business relationship management.

So this model offers fundamental insight into the reasons that persons or organizations enter into (business) relationships, remain in the relationships or strive to sever them. Essentially, this model states as the primary driver the costs and benefits of a relationship and as the fundamental behavior that participants can choose in this regard the options of switching and remaining in a relationship. The concepts explained in the following Sect. 2.4 are thus fine-tuning of this basic model. They concentrate sometimes more on costs, sometimes more on benefits or

the value of a relationship, or on the behavior or behavioral intentions resulting from a commitment.

2.4 Economic Indicators: Switching Costs and Relationship Value

2.4.1 Bonding Effects of Switching Costs

2.4.1.1 Investments Related to Business Relationships

In the definition of a business relationship, the internal link between transactions and investments that customers make to establish and maintain a business relationship played a decisive role. This does not necessarily have to be high one-time expenses at the beginning of a business relationship. Overcoming entry barriers to a business relationship (offensive as an out-supplier) and defending the position by a single customer (defense as in-supplier, refer to Chap. 5) are a strain on the supplier that show up as current expenses in his internal accounting. Irrespective of how they are treated for accounting purposes, these costs are considered to be an investment. The supplier takes a **long-term** view. He sees not only the initial transaction but also subsequent business that will amortize the expenses invested in the initial acquisition. Entry costs and costs relating to defending business relationships can thus be considered **investments**, their reference object being the relationship to a specific customer (Bursk 1979; Kleinaltenkamp and Ehret 2006; Ungruhe 2011).

An investment is the acceptance of a certain disadvantage in the present in anticipation of an uncertain benefit in the future (Schmidt 1983). This definition reveals a perspective adequate to solving the problem. All expenses that a supplier incurs that are not geared towards order acquisition of a specific market transaction but towards securing subsequent transactions to later cover the expenses should be considered investments. These expenses include accepting unplanned and unsecured **additional costs** (e.g. goodwill services, generous interpretation of contract ambiguities, favors, seminars for customer's employees, referrals, etc.) as well as the continued cost of directly maintaining the relationship (e.g. regular meetings of top management, trade fair contacts). A particularly important aspect of the investment is forgoing the complete utilization of pricing policy latitude for every single transaction, e.g. when a competitor experiences a supply shortage, when a customer causes his own scheduling bottleneck, etc. In such a situation a customer would have no choice but to accept the "skimming" of the price leeway, but it is very likely that the customer would develop a good memory and would attempt to decrease dependency in the future. So the total marketing effort invested by suppliers to establish and maintain individual business relationships can be interpreted as an investment in this sense. Thus marketing in business relationships is linked to a long-term perspective in which single transactions should always be seen as a means of generating new transactions with the same customer. The investing perspective is thus a key feature in differentiating transaction marketing from relationship marketing (refer to Sect. 5.1.2).

The fact that both the customer and the supplier can benefit from substantial investments in a business relationship brings up the issue of the **symmetry** of the commitments between supplier and customer. It is definitely possible that one of the two sides feels a greater sense of loyalty (meaning greater dependency) than the other, and there is a risk that the other side could exploit this (Söllner 1996; Kleinaltenkamp and Ehret 2006; refer to Sect. 2.2).

Dependency based on investments plays a decisive role in the approaches of New Institutional Economics. This field of research has been met with great interest since the 1970s, which can be attributed particularly to the early publications of Oliver E. Williamson (1975, 1985). Williamson, the most prominent proponent of the transaction costs theory, received the Nobel Prize in Economic Sciences in 2009 for his work in the coordination of transactions. The starting point of his research is the conviction that the core problem of economics, the organization of the activity of the economic entity, cannot be sensibly dealt with without examining the organizational costs (transaction costs). As Williamson sees it, the existence of business relationships is evidence that this type of coordination reduces transaction costs.

The question of why economic activities are actually realized by applying a wide range of coordination forms—besides market transaction and coordination within the company (hierarchy), there are many combined forms applied—can be explained with the transaction costs theory, pointing out differences between the transactions to be coordinated. For Williamson, the most important element of a transaction is the specificity of the related investments. Transactions can then be differentiated by whether or not they require long-term and specific commitment of resources. Williamson argues that it is the specific investments that can lead an economic entity to be caught up in a dependency (“lock-in” situation) and that, when combined with other factors (uncertainty, restricted rationality and opportunism), can cause coordination problems (Williamson 1975).

So dependency in transaction costs theory means remaining dependent on the **inputs** required for a transaction. It does not express dependency of an economic entity on specific services of a different economic entity. The specificity of an investment can be determined rather by looking at the value of the resource in a capacity other than the intended use, particularly in the best alternative use—in this case, a business relationship with a different partner. If the value of a resource in its original capacity is higher than in the best alternative use, the difference in value is referred to as quasi-rent. It results in a return that the specific resource can provide only in its originally intended capacity—in this case, the business relationship with the respective partner (Fig. 2.4). This applies equally to buyers and suppliers. So when a purchaser changes suppliers, he should ask himself how the value of a resource (e.g. a machine, an IT system, employee know-how) would change were he no longer to buy from the current supplier—the in-supplier. If this difference (the quasi-rent) is significant, he would be forced to accept great economic disadvantages were he to switch the supplier, which tends to result in remaining with the “old” supplier (left side of Fig. 2.4). The cost of switching, gauged as loss of value of the respective resources, would be too high.

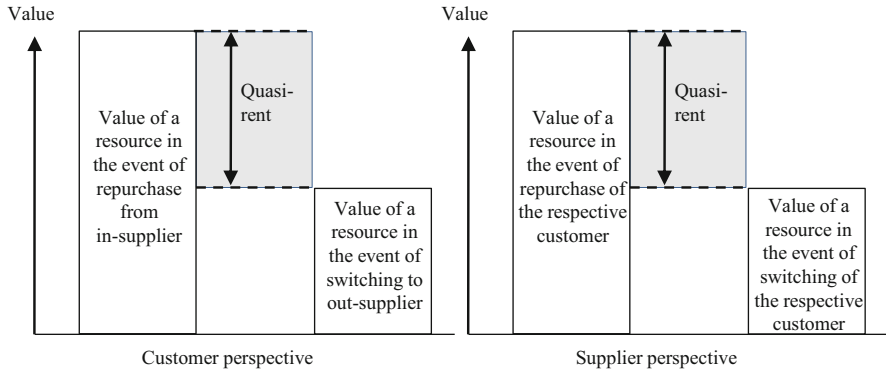


Fig. 2.4 Specificity-related losses when the intended utilization of a resource ceases

The same concept can be applied to a supplier with a customer considering or threatening to terminate the business relationship or with a customer he no longer wishes to do business with—for whatever reason. Here, too, the supplier must compare the value of his resources when the customer repurchases to the value in a situation in which the customer would have switched or would no longer be supplied (right side of Fig. 2.4). The greater the potential loss of the respective resources (machines and equipment, business processes, employee know-how, etc.) would be, the more likely the supplier is to make concessions for the customer in question—theoretically, until the quasi rent is exhausted—and the less economic sense it would make to cease supplying the customer. The cost of switching, caused by the loss of the customer and the associated loss of value of the company’s own resources, would be too high.

So the existence of high and specific investments justifies a commitment in two ways. On the one hand, the resource specificity forces the investor to realize the planned transaction(s) so that the investment can be amortized. On the other hand, the specificity substantiates a dependency based on the “good will” of the transaction partner: The partner could be tempted to dispute the quasi rent with the committed business partner by insisting on new negotiations (Butler and Baysinger 1983). It is precisely this good will on the part of an actual or potential business partner that Williamson rules out by assuming that humans are by nature opportunistic (using their own cunning and wits).

Differential analysis of specific investments is made easier with Williamson’s differentiation between four types of specificity (Williamson 1985). The list is not necessary complete and has been amended by Williamson himself (Williamson 1986). It also offers an initial analysis matrix to compile appropriated specific investments, which are a particularly influential factor in the economic approach to explaining loyalty.

- **Site specificity** means that the customer and the supplier made agreements tied to specific places and later relocation would be very costly or impossible. This

type of specificity can occur when e.g. a steel manufacturer builds a plant near the ore supplier or when a supplier to the automotive industry relocates to a new facility of the customer in a foreign country. Dependency results from the customer having no other transaction partners in this location.

- **Physical asset specificity** means that a customer adapts interfaces to the supplier, e.g. by acquiring certain equipment or implementing certain processes. Specific material goods can include communication equipment to link the supplier and purchaser, transport and storage facilities used by both parties, etc.
- **Dedicated assets** are the result of a company structuring its capacity exclusively for the cooperation with a certain market partner. Capacities are created in anticipation of a certain transaction volume. Were the transaction volume do not occur, there would be no other suitable use, even if the technical properties are unspecific.
- **Human asset specificity** means that knowledge related to the business relationship exists or is acquired. Human capital that is lost outside of the business relationship can be acquired e.g. through targeted training. It can just as well have resulted from earlier transaction and experiences with the partner—more or less as a by-product.

The phenomenon of specificity in combination with the problem of opportunism is thus essentially responsible for the safeguarding of resources having become such an important management task for many transactions. Since protecting from the risk of specificity on the market would lead to such high transaction costs, the transaction costs theory's standard solution to this problem is vertical integration. Integration of specific transactions is intended to utilize the controlling benefits of the "hierarchy" and thus to minimize transaction costs.

However, from the customer's and supplier's perspective, the vertical integration suggested by Williamson is generally not a viable option. It was particularly Picot (1991) who pointed out that barriers to integration can result primarily from financial restrictions and from a lack of know-how. The desire to stick to one's own core competencies can also be arguments against integration. And finally, such a step would mean that, in the case of downstream integration of a supplier, a company would become a competitor to its own customers; and were upstream integration of a customer to occur, the company would become a competitor to its own suppliers. In both cases this can generally lead to significant disadvantages. In light of this, close cooperation amongst business partners is a realistic alternative for cooperation as compared to the hierarchy option, especially—as Stinchcombe (1985) pointed out—taking into consideration the fact that many of the benefits of a hierarchy can also be achieved in close business relationships. However, it should be kept in mind that entering into a business relationship with the intention of protecting the required specific investments usually leads to additional specific investments being needed to establish the business relationship. The role that investments play in business relationships has already been emphasized in earlier publications on this topic (Johanson and Mattsson 1985; Plinke 1989). Specific investments have been cited as a central aspect of business relationships in many

other articles as well (Hallén et al. 1991; Heide 1994; Plinke 1997; Plinke and Söllner 1997; Söllner 1999). In this respect one can agree with Sheth and Parvatiyar (1994) when they emphasize that specificity is definitely not only a condition for entering into business relationships but is also the result of the decision to choose a close business relationship. Specific investments have far-reaching consequences for the relationship between suppliers and purchasers by sustainably affecting their negotiating situation.

Economists from the most varied schools of thought all acknowledge the significance of negotiating situations in which transactions are brokered. The number of potential suppliers and purchasers plays a decisive role in this aspect. If a customer has several potential suppliers to choose from, we refer to this as a situation of supplier competition. If there is only one supplier, a monopoly exists. The negotiations between the monopolist and the purchaser will differ vastly from the negotiations in the case of supplier competition.

By taking the specificity into consideration, Williamson succeeds in demonstrating that a situation of supplier competition does not necessarily have to remain in place. From the customer's perspective, the competitive situation upon conclusion of the contract can by all means change from a situation of complete supplier competition to a unilateral or bilateral monopoly. Whether or not the competitive situation changes in this way depends completely on the scope and specificity of the resource allocation resulting from conditions of the contract. If neither of the two parties makes investments, the next round of negotiations also takes place under the same conditions of supplier competition. If, on the other hand, specific investments are made, the competitive situation is "*fundamentally transformed*" (Williamson 1985, p. 61). As soon as the customer has made specific investments, competitors that were not included in the first round of negotiations are at a disadvantage in the second round compared to suppliers who were successful in the previous round. When the customer makes such specific investments that bind him to a certain supplier, barriers are erected for potential competitors, protecting the established business relationship.

Supplier investments can also effect a fundamental transformation. In many cases, the supplier in a business relationship will be forced to make investments that are sunk costs for him. Investments made by the supplier can also transform the market situation to a bilateral monopoly. On the one hand, supplier investments made under the assumption of an imperfect market are relevant, because new investment projects cannot always simply be financed. On the other hand, the calculation basis for the in-supplier's pricing is completely changed by the specific investments. While the resources to be expended are still completely disposable to the out-supplier and thus represent relevant costs to be covered, the resources already disposed of are sunk costs for the in-supplier because the investments are irreversible. The in-supplier company may possibly consider this in its pricing and remain below his full costs in the competitive situation. This situation alone can discourage potential out-suppliers from an offer and stabilize the monopoly situation.

When a customer invests in a business relationship, the investments—if they are specific—are irreversible. They substantiate switching costs and bind the customer to the successful supplier. While the supplier frequently achieves the essential marketing objective of customer loyalty (Diller 1996), the customer may experience stability and security and thus the transaction cost efficiency essential to performance of certain transactions. However, the price of this is forfeiting the corrective influence of competition and the acceptance of problems common to monopolies or bilateral monopolies. The loss of resources in the event of termination of a business relationship shifts the relationship of the customer to potential suppliers, and it changes the bilateral negotiating position towards the current business partner. This is due to the lack of replaceability of the successful supplier.

2.4.1.2 Direct Switching Costs

In addition to the costs that a business relationship partner incurs for loss in value of the invested resources, a supplier or a buyer switch can be prevented or hindered by the fact that its initiation and execution are difficult and costly. These direct switching costs include all “*anticipated, directly attributable costs to terminate the old and begin the new business relationship*” (Saab 2007, p. 122); based on (Adler 2003, p. 115). This includes not only monetary values but all other expenditures—such as time and effort—incurred from (potentially) switching as well. These cost components include expenditures (Saab 2007) for

- The termination of the existing relationship (*take down costs*), contract penalties or the time required for termination,
- the search for an alternative relationship (*search costs*), e.g. to collect and prepare information on suitable contract partners and
- establishing such an alternative relationship (*setup costs*), e.g. negotiations, coordination of organizational processes, introduction of new procedures, investments in equipment, training employees.

It follows that the costs mentioned here depend strongly on the level of knowledge of the participants on the existing and any potential alternative business relationships. The trust in an existing business partner as well as the satisfaction in regard to the partner are significant factors (Kühne 2008). If, for example, the trust in a current partner is high, the transaction costs for the initiation and execution of subsequent transactions are—sometimes drastically—reduced (Plötner 1995). One feels that the in-supplier can be trusted and that less activity is required to find information and to safeguard against later disadvantages. When little or nothing is known about an out-supplier, the exact opposite is the case, with the consequence that high direct switching costs are (or can be) incurred for a potential switch. It would be necessary to compile information on the quality of the goods and services supplied by the company in question, to check the creditworthiness and reliability of the potential partner, etc. And one would probably also have to expend considerable effort in drawing up contracts that protect against any opportunistic behavior on the part of the new partner. This last case clearly indicates that, by remaining in

the “old” business relationship with the in-supplier—sometimes substantial—direct switching costs can be avoided.

The same concept applies to the satisfaction felt in regard to a business partner. Satisfaction means “knowing what you have.” To find out whether the satisfaction would be comparable with a potential new partner, effort would have to be invested in seeking information such as references. Such efforts are also a source of direct switching costs and can make switching less likely or even prevent it.

The amount of the direct switching costs in a specific case is to a great extent a factor of the number and strength of other relationships in which the supplier and purchaser are participants. As previously mentioned (refer to Sect. 1.1), companies in business-to-business markets are generally involved in a greater number of parallel business relationships. Switching to a customer or supplier within such a group generally incurs fewer direct switching costs than establishing contact to a completely new business partner. In such a case switching in its own sense is not even necessary: One’s own situation can be improved by restructuring the procurement and/or customer portfolio. For example, a customer can put pressure on a supplier by reducing the delivery rate (*share of wallet*) or by temporarily not considering the supplier for deliveries (Janker 2004), because he will incur only minimal termination, search and/or setup costs, if at all (Saab 2007). This does not, however, affect the significance of direct switching costs as a loyalty factor. The amount of the costs is also a significant factor in the cases described above. The more alternatives a company has in its customer and supplier base, the lower are the switching costs, the less it is committed to a single partner with which it is in a business relationship and the greater is the probability that it could switch (Saab 2007).

2.4.2 Loyalty Effects of the Value of a Business Relationship

Concentrating transaction cost economics on transaction cost efficiency while strictly applying the concept of opportunism is, however, restrictive when attempting to analyze actual management situations. This was first explicitly expressed by Zajac and Olsen in 1993, when as part of their “Transactional Value Analysis” they argued that interorganizational business relationships are entered into primarily to achieve mutual benefits. Their findings indicate that business partners come to agreements that do not necessarily minimize transaction costs when the resulting cost disadvantages are at least balanced by the additional values created by the relationship (Zajac and Olsen 1993; Madhok 2000).

The significance of the business relationship value is also apparent in a series of studies that confirm that the value that the business relationship partners place on the relationship (*relationship value*) has become an essential if not the decisive factor for the initiation and success of business relationships as well as for the behavior of the partners in the business relationships (Krapfel et al. 1991; Anderson 1995; Wilson 1995; Wilson and Jantrania 1994; Tunder 2000; Cannon and Homburg 2001; Hogan and Armstrong 2001; Adler 2003; Walter et al. 2003). Wilson

Table 2.1 Dimensions of the business relationship value. Source: Based on Ulaga and Eggert (2006)

		Value dimensions	
		Relationship benefits	Relationship costs
Sources of value creation	Core offering	Product quality Delivery performance	Direct costs
	Sourcing process	Service support Personal interaction	Acquisition costs
	Customer operations	Supplier know-how Time-to-market	Operation costs

(2003, p. 176) expressed this clearly: “*Product value is not enough to win in the marketplace. Relationship value creation is critical to winning in the marketplace*”.

In this realm the relationship value model created by Ulaga and Eggert (2006) has attracted considerable attention. On the basis of theoretical preliminary considerations and a series of in-depth interviews, they identified six values perceived by customers in business relationships. Three of these values include cost aspects and three benefit aspects. They are each based on the actual core offering, the sourcing (procurement) process and the customer operations in which the products and services purchased from the supplier are used (refer to Table 2.1 and to Sect. 5.3.1).

Empirical examination of the model revealed that, in regard to assessing the value of a business relationship, the perceived benefits play a greater role than the perceived cost reductions. In regard to the significance of the individual dimensions, the study showed that the greatest value was placed on gains in benefits in the operations and sourcing areas as well as on production cost reductions (Ulaga and Eggert 2006).

The significance of the business relationship value is also apparent in the results of a more recent study geared towards the international marketplace. The analysis of a large number of cases in Argentina, Germany, New Zealand and South Korea indicated that, on both the supplier and purchaser sides, the business relationship value sometimes had a much stronger influence on the intended behavior of the partners involved than did the switching costs (Geiger et al. 2012).

2.4.3 Commitment in Business Relationships: Interaction of Business Relationship Value and Switching Costs

The previous section clearly indicates that cost as well as benefit or value aspects are the foundation of the loyalty of a business relationship partner. So it seemed and seems reasonable—as the Thibaut and Kelly model did—to combine the two approaches to be able to fully comprehend how commitments in business relationships come about.

These considerations can be plausibly phrased by saying that ultimately there are—“only”—two reasons why people remain in relationships: either because they want to or because they have to (Johnson 1982); quoted according to (Söllner 1993). The aspect of having to stay in the relationship stands for the switching costs, while wanting to represents the benefits gained from the relationship. This concept has been revived again and again for business relationship research and to explain commitments in this context (Söllner 1993; Plinke 1997; Bendapudi and Berry 1997; Gilliland and Bello 2002; Gounaris 2005; Liu 2006; De Ruyter et al. 2001; Saab 2007).

An initial approach that applies and pursues these thoughts is Söllner’s **commitment model** (1993). This model sees commitment as the perceived loyalty to one economic entity as opposed to another. An extension to this line of reasoning on the transaction costs theory is that the commitment is no longer attributed solely to the scope of specific investments. The extension includes the addition of the **specific contribution to the relationship** as an input category and—as previously mentioned (refer to Sect. 2.4)—the **success of the relationship** and the **relationship equity** as two output dimensions that also influence the customer’s perceived loyalty (refer to Fig. 2.5). Direct switching costs, on the other hand, are not considered.

Specific contributions include e.g. loyalty to the business partner and motivation to achieve the same objectives (Allen and Meyer 1990; Gundlach et al. 1995). It can evolve over the course of a business relationship with no planning whatsoever. And it can also be consciously created, e.g. by supporting interorganizational relationships with planned interpersonal relationships. The commitment dimension is a significant modification in relation to transaction cost economics. All conceivable components of the commitment dimension are fundamentally suitable for reducing the tendency of the involved parties to be opportunistic. However, when

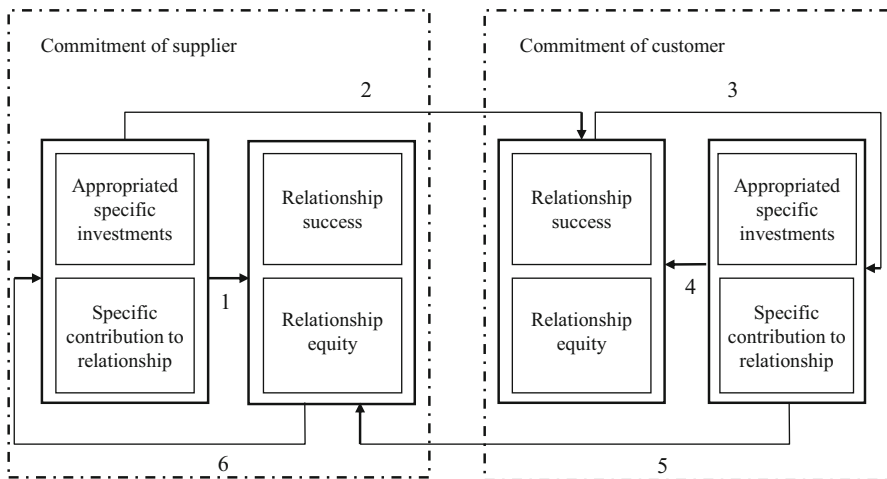


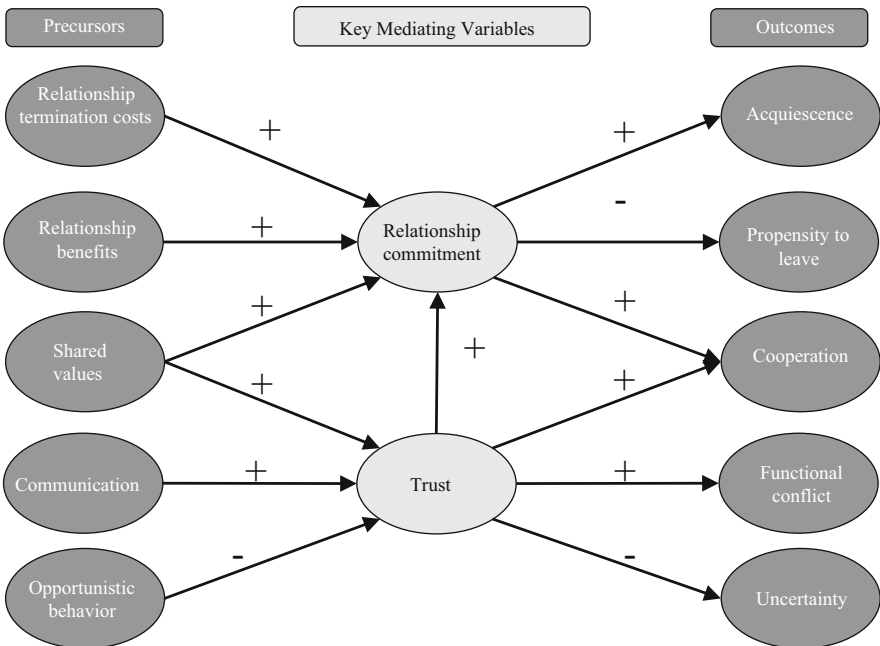
Fig. 2.5 Commitment in a business relationship (dyadic view). Source: Based on Söllner (1999)

this is acknowledged, opportunism is no longer about a given property; it is a variable that, depending on the specific application in the relationship, can manifest itself to varying degrees in the relationship.

The **relationship equity** reflects the question of how the success of the relationship is divided between the partners. A measure for the relationship equity can be the perceived comparability of the respective input-output ratio of the two partners. Particularly when it is examined dynamically, the perceived equity in a business relationship will have a strong impact on the further course of the relationship. Some authors now expand the contemplation to include the generally perceived quality of the relationship (Mysen and Svensson 2010).

While Söllner’s model focuses primarily on the economic factors leading to a commitment, Morgan and Hunt examine certain intended behaviors that can result from varying degrees of commitment in their commitment-trust model (refer to Fig. 2.6).

These factors include the willingness of a business relationship partner to meet the wishes or requirements of the other side (*acquiescence*), to terminate the relationship (*propensity to leave*) or to show a willingness to cooperate (*cooperation*). When determining the degree of commitment, not only the benefits of the business relationship (*relationship benefits* are examined, but also the anticipated



Legend:
 A "+" stands for a positive correlation, a "-" for a negative correlation between the respective variables. Sample reading: The higher the "relationship benefits," the higher is the "relationship commitment."

Fig. 2.6 Commitment-trust model. Source: Based on Morgan and Hunt (1994, p. 22)

cost of ending the relationship (*relationship termination costs* which also represent a portion of the direct switching costs. Values from which both partners in a business relationship benefit (*shared values*) are also seen as factors that impact commitment. In the model the commitment is seen as a value that provides a mediating influence between the initial and influencing factors (*precursors*) and the results of the business relationship (*outcomes*). The commitment itself is a dependent—in this case on stated influencing factors—variable that intervenes in the effect of the ultimately dependent variable—in this case the intended behavior.

Trust is also seen as a mediator effect in this model. It is also influenced by the shared values as well as by the way in which the partners have communicated with one another in the past (*communication*) and by the *opportunistic behavior* of the other side—or by the lack thereof. The degree of trust has an effect on the tendency to cooperate as well as on the extent to which conflicts can productively be used to successfully continue the business relationship (*functional conflict*). As the only factor that does not represent intended behavior, the authors see trust as influencing the *uncertainty* that a business relationship partner feels in regard to the integrity of his counterpart. And trust also has an impact on the commitment itself.

The model has attracted a wealth of attention in relevant literature and has become one of the most frequently quoted approaches. A point that warrants criticism is that the termination costs only factor in some of the switching costs. Neither the expenses incurred as direct costs for searching for an alternative relationship (*search costs*) and for establishing the relationship (*setup costs*) are not considered explicitly, nor are the sunk costs attributable to specific investments (refer to Sect. 2.4.1). They flow into the approach only indirectly and in different ways as mediating values through trust:

- Deep trust in an existing business relationship partner increases the “search costs” as well as the “setup costs” related to an alternative business relationship. This indicates that trust is a factor that impacts the amount of the direct switching costs.
- Opportunistic behavior poses a risk particularly with high specific investments. In this sense, non-opportunistic behavior that does not threaten the quasi-rent leads to low sunk costs and it increases trust in the business relationship partner. So trust is a value that is determined by the type of switching costs, the sunk costs.

Saab’s model (2007) is an approach that avoids the problem mentioned above and in which the influencing factors of the commitment are attributed to solely economic considerations, and it also takes into account the essential behavioral intentions. Based on thoughts of transaction cost as well as transaction benefit theory—and in accordance with the concepts explained previously—he sees a commitment as the result of the combination of relationship value and switching costs, whereby the latter is in turn composed of direct switching costs and sunk costs (refer to Fig. 2.7). As already explained, the sunk costs can be the result of

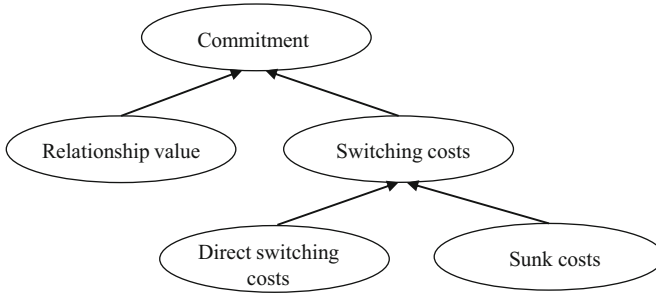


Fig. 2.7 Model of commitment in business relationships. Source: Based on Saab (2007)

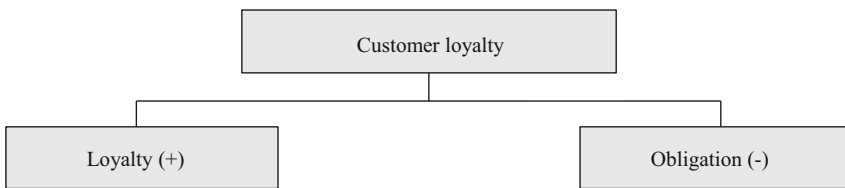


Fig. 2.8 Customer loyalty from the customer's perspective. Source: Based on Eggert (1999)

resources specific to the business relationship losing value from switching, meaning that the quasi-rent is at risk.

To determine the relevance of the model—previously tested successfully in the business-to-business field—to business relationship management, in his study the author also examined the intended behavior of the three commitment drivers—business relationship value, direct switching costs and sunk costs—that emanate from the supplier and the purchaser. He based his studies on findings including those by Eggert from a study in 1999—which was performed on consumer goods, however. This study also initially revealed that customer loyalty was determined ultimately by the factors “wanting to” and “having to.” A state in which for one customer the “wanting to” dominates is referred to by Eggert as—positively perceived—“loyalty,” while a state in which “having to” dominates is—negatively perceived—“lock-in” or obligation (refer to Fig. 2.8). What is interesting here is that customers feeling loyalty towards the supplier demonstrate more positive intended behavior than those that feel obligation. This is apparent in their lesser intention to switch, their greater willingness to express a recommendation and their greater willingness to intensify the business relationship, all while only minimally seeking alternative suppliers.

Saab's study reaches very similar conclusions (refer to Fig. 2.9): The higher the relationship value, direct switching costs and sunk costs are, the lower is the switching probability and the higher are the willingness to intensify the relationship and the relationship tolerance, meaning the inclination of a partner to be willing to accept a mistake made by the other side. The greater the relationship value, the less

		Effects				
		Switching probability	Willingness to intensify	Relationship tolerance	Search for alternatives	
					Search for other alternatives	Search for additional partners
Loyalty dimensions	Relationship value	-	+	+	-	-
	Direct switching costs	-	+	+	-	n.s
	Sunk costs	-	n.s	+	n.s	+

+ Positive correlation - Negative correlation n.s. Correlation not significant

Fig. 2.9 Effects of commitment dimensions on intended behavior. Source: Based on Saab (2007)

frequently a partner seeks alternatives or additional partners. This also applies to direct switching costs in regard to searching for alternatives. The higher the sunk costs, the more intensively additional partners are sought to reduce the dependency created by the specific investments. The previously mentioned international study indicated a similar tendency; however, it identified differences between the respective intentions of the supplier and buyer (Geiger et al. 2012). Another interesting revelation was that buyers and suppliers have different reasons for accepting commitments. The supplier weighs the disadvantages of dependency against the potential cost of acquiring new customers. The higher the latter are, the more likely the supplier is to commit to new purchasers or to the existing customer base. Buyers, on the other hand, see the loss of procurement freedom as a necessary condition to reducing costs incurred to maintain and manage a wide supplier base.

To summarize: The commitment or loyalty that a business relationship partner feels to another party is essentially influenced by two factors: the value of the business relationship (a positive factor) and the switching costs (a negative factor). The latter can be divided into direct switching costs attributed directly to a (possible) switch and costs that could be incurred due to a (looming) loss in value of own resources were a switch to occur (sunk costs). Depending on their manifestation, the loyalty drivers can significantly influence the behavior or intended behavior of the participants involved.

This does not provide a patented explanation for the establishment and duration of business relationships. At the same time, these considerations show the approaches for successful business relationship management. They logically consist of increasing the value of the relationships for the respective partner and/or increasing the switching costs that he would incur. This can happen by the customer being “tempted” or deeming it sensible to invest specifically in the business relationship, resulting in the incurrence of sunk costs. Also, an attempt can be made to increase the direct switching costs by making it more difficult to compare alternative business partners to one another. These fundamental constellations of

business relationship management are examined extensively in Chap. 5 of this book, from the in-supplier's as well as the out-supplier's point of view.

In addition to the two drivers of commitment, there are additional characteristics that can be characterized by a business relationship and must thus be considered for the analysis as well as for the constellation of business relationship management. We will examine these characteristics in the following chapters.

2.5 Other Economic Attributes of Business Relationships

2.5.1 Structural Attributes of a Business Relationship

Whenever commitments make suppliers or buyers feel dependent on their business partners, their inclination to seek or turn to alternatives increases. But whether or not a partner perceives the dependency resulting from the business relationship as disruptive depends not only on the value of the relationship and the switching costs but also on the **structure** of the commitment (Gundlach et al. 1995), meaning the question of whether the commitments are balanced or asymmetrical or whether they are perceived as such. It is safe to assume that a customer considers a potential dependency on the supplier to be much less disruptive when the supplier is similarly dependent on the business relationship.

When examining business relationships, it quickly becomes apparent that the construct commitment facilitates a wealth of structures. Even when only the appropriated specific investments and their simplified characterizations as “high” and “low” are examined, four cases can easily be differentiated (Table 2.2).

Cases 1 and 4 represent symmetrical input structures. In case 1, both parties have made high and specific investments. In contrast, in case 4 both parties have made only minimal specific investments. Cases 2 and 3 represent asymmetrical input structures in which either only the customer or only the supplier has made high specific investments.

The number of cases of different business relationship structures can be greatly increased by taking into consideration the structure of the other commitment dimensions or by using a finer scale to measure the commitment dimensions. Without getting into all of the possible constellations of business relationships, a few fundamental thoughts on the relevance of the structure of dependency relationships should be mentioned here:

Table 2.2 Structure of appropriated specific investments. Source: Based on Söllner (1999)

		Appropriated specific investments by the customer	
		High	Low
Appropriated specific investments by the supplier	High	1	2
	Low	3	4

- Besides the determinants of a company's dependency in a business relationship, the structural features of the business relationship should also be recognized when attempting to determine whether or not a customer perceives the dependency resulting from a business relationship as negative. Quite a few authors have emphasized the problems of one-sided investments in business relationships (Berry and Parasuraman 1991; Anderson and Weitz 1992; Morgan and Hunt 1994; Gundlach et al. 1995; Plinke and Söllner 1997; Kleinaltenkamp and Kühne 2002).
- Dependency that results from a certain commitment dimension—e.g. from specific investments—can be acceptable to a company when it is symmetrical dependency. Specific investments pose a lesser threat potential when both partners have made a commitment by making specific investments. Williamson (1985) refers to the necessity of exchanging hostages in this context. The same applies to output-related dependency. A customer who receives a unique service from his supplier will feel less threatened by this dependency when the supplier in the business relationship also experiences success that would not be as easily achievable in other business relationships.
- A symmetrical relationship structure will be the exception in most cases (Gummesson 1994). However, in these cases a dependency in one commitment dimension may be able to be compensated for by a partner's dependency in another commitment dimension. Heide and John (1988) talk about the opportunity to balance out specific investments in a business relationship by “offsetting investments” to establish good relationships with other members in the chain of purchasers.
- Dependency (based on investment or value) is acceptable to a company when in the business relationship standards of solidarity and justice are recognized as institutional guidelines by the independent company as well (Heide and John 1992; Kaufmann and Stern 1988; Söllner 1999). So the threat perceived by the customer is reduced by the supplier's specific stake in the relationship.

2.5.2 Process Attributes of a Business Relationship

By definition, business relationships are characterized by a certain stability. This does not, however, mean that the time sequence cannot be changed. And although the commitment dimensions described here are independent of one another, they are distinguished by different interactions. And the customer's behavior affects the supplier's commitment and vice versa. So, for example, specific investments made by the customer impact not only the customer's success in the relationship but that of the supplier as well: They increase the customer's switching costs. They stabilize the relationship and reduce the insecurity of the supplier (Ungruhe 2011). Conversely, a high specific investment in the relationship by the supplier can e.g. be a sign of a slight risk of opportunism on the part of the purchaser. And finally, perceived relationship equity will impact the future investments and the future contribution to the relationship of the parties involved.

The decisive factors in this view are the dynamic aspect and the possibility of a step-by-step establishment of commitment. The prerequisite for closely binding the customer may be for the supplier to also make a commitment. Since this process can occur in steps and reciprocally, a strong commitment can be established without a company being bound asymmetrically to a high degree at a certain time.

It is not necessary and probably also not possible that both parties are equally committed. The intention is rather to signal to the partner interest in the relationship by committing oneself. This creates the conditions under which the partner is willing to commit to a relationship or the committed partner does not attempt to reduce his dependency (Söllner 1993).

Examination of the process aspects of business relationships has led to the development of different phase models of business relationships, which will be taken up in Chap. 3 to analyze repurchase decisions and in Chap. 5 to develop strategies for business relationship management.

So converting from market coordination to relational coordination leads to activities that can be far-reaching. These activities are primarily geared towards obtaining the knowledge required to coordinate a transaction through a governance structure and to creating the organizational requirements for execution of relational exchange conditions. Particularly Walter (1998) describes how the required steps can become barriers in the evolution process. It should be noted that the organizational and individual requirements for the implementation of business relationship management vary from company to company (refer to Part III of this book). So converting to relational exchange relationships poses problems of varying degrees for the people in different companies.

Exercises

Case Study

Many automobile producers have moved their manufacturing facilities to foreign countries to save costs. According to a report in the German magazine ADAC Motorwelt, the Audi TT is made in Hungary, the Opel Astra in Belgium, England and Poland, the Porsche Boxster in Finland and the VW Polo in Spain and Slovakia. And manufacturers are also increasingly purchasing parts and components in foreign countries as the vertical range of manufacture decreases. The proportion of vehicle parts produced in Germany has fallen from 35 % in 1991 to 25 % in 2001. Parts and components are often procured from suppliers all around the world.

The Opel Vectra is a good example of this development. It is produced at the Rüsselsheim plant, opened in 2002. Figure 2.10 clearly demonstrates that the Vectra is a real “European,” with components from many different places.

The establishment of international business relationships and networks has brought Opel great potential advantages (refer to Chap. 1). But a cooperative relationship between a manufacturer like Opel and a potential supplier is definitely not easy. It is plagued by uncertainties. Manufacturers and suppliers negotiate early,

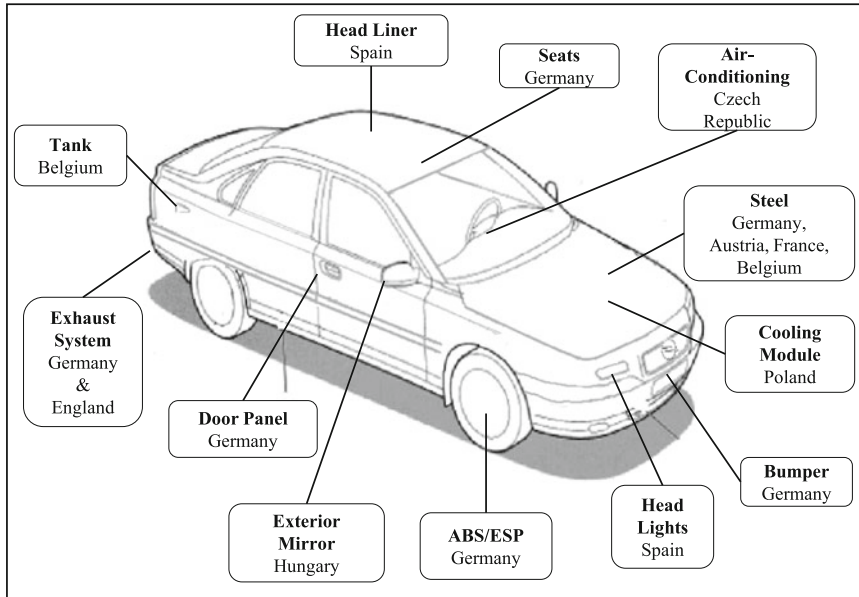


Fig. 2.10 The Opel Vectra and the origin of essential components. Source: Based on ADAC Motorwelt, 2/2007, p. 46f

meaning they discuss a service that is not yet in existence. Many issues cannot be definitely resolved: Does the supplier properly meet the expectations and what will be the actual cost-benefit ratio? Which roles do trade unions and strikes in the supplier's country play? If a bottleneck occurs, might a supplier in a foreign country give preference to customers in his home country?

The transaction is fraught with uncertainties for the supplier as well. The exclusive cooperation with the German manufacturer appears to be worthwhile at first glance. But how will the cooperation be over the long term? Will the forecast quantities be achieved, amortizing the required investments and producing profits? Will the manufacturer remain as cooperative as implied in initial discussions? Or is there a risk of an "extended workbench" occurring and having to accept prices that barely cover costs?

Discuss the risks that the potential benefits of the business relationship could endanger from the perspective of the manufacturer and his suppliers. Then consider how to manage the risk involved in business relationships.

Additional Exercises

1. Explain the fundamental pattern of customer loyalty from a behavioral perspective. Which concepts are you familiar with within this perspective that explain the origin of customer loyalty, and are these concepts sufficient to thoroughly explain the (re)purchasing behavior of companies?
2. Explain the social psychological approach of *Thibaut* and *Kelley* in light of the origin of organizational business relationships.
3. What is the main feature that differentiates transaction marketing from relationship marketing? What are the consequences for the commitment between the customer and the in-supplier?
4. Which different types of specificity do you know about?
5. Explain the components of switching costs that a purchaser incurs when changing the in-supplier.
6. What significance does the value of a business relationship hold for the loyalty between customer and in-supplier?
7. State and explain the commitment drivers in business relationships.
8. Differentiate the essential tasks of managing a business relationship in light of the individual replacement phases from the tasks of managing a market transaction.

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Part II

Analysis, Goals and Strategies of Business Relationship Management

Repeat Purchasing in Business Relationships

3

Frank Jacob

The previous section demonstrated why business relationships make up a separate topic of business-to-business marketing. Fundamental concepts were established and, based on theories, a model was formed. Basic conditions were also discussed. In this context, business relationships are seen as a special variation of the exchange and sharing between participants in the market. A special feature of the exchange and sharing within a business relationship is the fact that the customer repeatedly makes his purchase decision in favor of the same supplier—despite his free choice to change suppliers, if he so desires. We refer to this as repeat **purchasing behavior**. This part of the book focuses on the representation and explanation of the determinants of such repeat **purchasing behavior**.

A practical case will be presented and discussed to introduce this topic.

Example 1: Old New Partner

Handelsblatt, December 23, 2000—The Danish toy manufacturer Lego will once again be using SAP software for corporate management. It was only one year ago that Oracle, arch rival to the German company, was delighted to have snatched this European customer from SAP. Now the Americans are coming out on the short end again. This is good news—at least for SAP. After all, the Germans were always happy to advertise their affiliation with the well-known Lego logo.

But for the manufacturer of the building blocks, it was more of a bitter setback. This has little to do with the German software and much more to do with having changed IT suppliers twice within only ten months. Even in

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faraway Denmark, it is common knowledge that the implementation of completely new corporate software costs time and a lot of money. Data has to be prepared and processes changed—all of which involves risk. And taking this risk in a situation that is difficult anyway makes the decision to switch suppliers even harder. Maybe SAP should reconsider putting the name Lego back on its list of references.

The article reports on an exchange and competitive relationship between the supplier SAP, the customer Lego and the competitor Oracle—a relationship characterized by impressive dynamics. Evidently the customer Lego and the supplier SAP originally had a close relationship. However, this was not enduring, and it fell apart about 1 year before the time of reporting. At that time, Lego replaced its supplier SAP with the competitor Oracle. What is surprising though is the news that Lego left its new supplier Oracle and returned to its previous supplier SAP. None of the participants can really claim these happenings as a success. The Lego management committee will surely have to be prepared to explain to its board of directors why it took such a step back. The SAP sales department was fortunate to have been able to regain Lego as a customer, but they undoubtedly had difficult questions to answer from within their own company in the meantime. And the Oracle sales department suffered serious embarrassment for the short-lived prestige gained by supplying Lego. A rash explanation of these events could be to blame a lack of professionalism on the part of all participants. As we see it though, the problems were caused primarily by a lack of understanding the special aspects of the behavior of the market participants in business relationships. Such behavior definitely follows its own rules. The intention is to investigate the rules.

The purpose of examining purchase behavior is to find an explanation for purchase decisions. The distinctive feature of a—functioning—business relationship is that the customer repeatedly makes purchase decisions in favor of the same supplier and forfeits the opportunity to change suppliers. This means that the situation can be examined at two different levels: the explanation of the **repeat purchasing behavior** in the respective market transaction and the description of the business relationship in the time sequence. This differentiation provides the structure for our deliberations.

3.1 Repeat Purchasing and the Market Transaction

The understanding that a business relationship is the consequence of a sequence of market transactions that is not coincidental (Chap. 1) is the basis for our deliberations in this part as well. The central aspect of this is the individual market transaction between a supplier and a customer. As mentioned above, the intention is to explain the reasons why a customer enters over time into a series of transactions with the same supplier, although he has other alternatives available. In other words:

We want to explain repeat purchasing behavior. Once again, we will apply the exchange paradigm introduced in Chap. 1 as the basic concept. This means that the prerequisite for an exchange is the coming together of customer benefits and supplier benefits (Plinke 2000). Thorough understanding of the repeat purchasing as a consequence of the structure of the customer benefit is clearly instrumental to the success of the supplier's management behavior in an actual business relationship. Thus, intensive analysis of potential variations of the customer benefit and its significance for the occurrence of repeat purchasing is the focus of Sect. 3.1.1. Consideration of the supplier advantage reveals conclusions that help us understand the customer's repeat purchasing. Although this perspective is seldomly taken, we consider this representation to be essential in conjunction with the topic of business relationships. We apply an interaction paradigm for marketing purposes (Plinke 1991), and in Sect. 3.1.2 we will demonstrate how insight into the structure of the supplier advantage helps improve business relationship management in the actual markets.

3.1.1 Customer Benefit as a Determinant of Repeat Purchasing

Repeat purchasing is the result of certain constellations of the customer benefit. To develop an understanding of this concept, such constellations must be differentiated. The **bonding** plays a key role as a behavior determinant. The customer's repeat purchasing behavior can be differentiated in this sense by whether it would occur without the influence of such a bonding or whether the bonding was decisive (Bliemel and Eggert 1998). Repeat purchasing in which bonding is not a factor is founded either on the effect of the **core offering** or on the effect of the **ancillary services**. Bonding itself is attributed to economic causes or to the effect of rather psychological causes such as trust and commitment (Linke 2006). Trust and commitment as attitudes can be supported by all three of the other causes of repeat purchasing mentioned. Figure 3.1 offers an overview of the potential explanations of repeat purchasing as they can be attributed to the structure of the customer benefit. The outline of the following sections follows the classification shown.

3.1.1.1 Repeat Purchasing Caused by the Elements of Exchange

We see a core service of an offer to be the element of the service that are fundamentally (Kotler and Bliemel 2001) or substantially (Homburg and Krohmer 2003; Meffert 2000) suited to meeting the functional needs of the customer. These needs are characterized by the fact that they give the customer grounds to enter into exchange activities with suppliers. Ancillary services, on the other hand, can enhance the benefits of a core service, but alone they are not capable of meeting the functional needs of the customer (Meffert 2000). So they merely provide ancillary benefit. Both categories can promote repurchase.

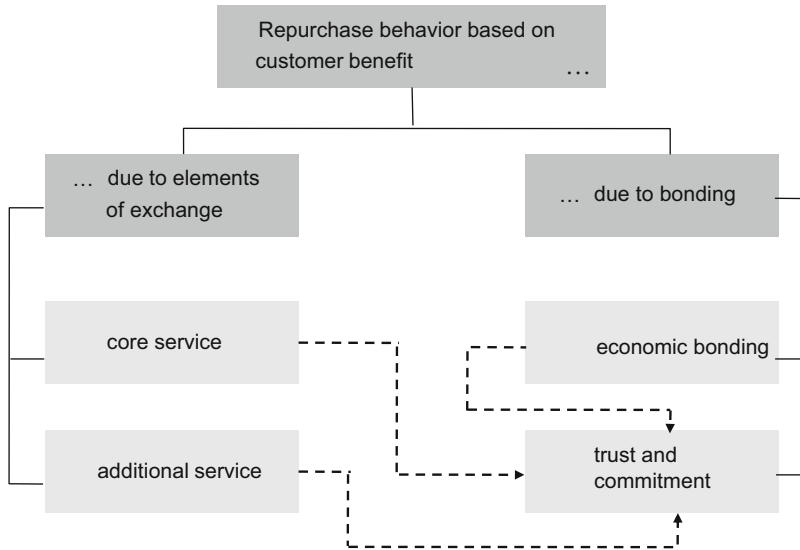


Fig. 3.1 Business relationship management—altered market focus. Source: Based on Jacob (2009)

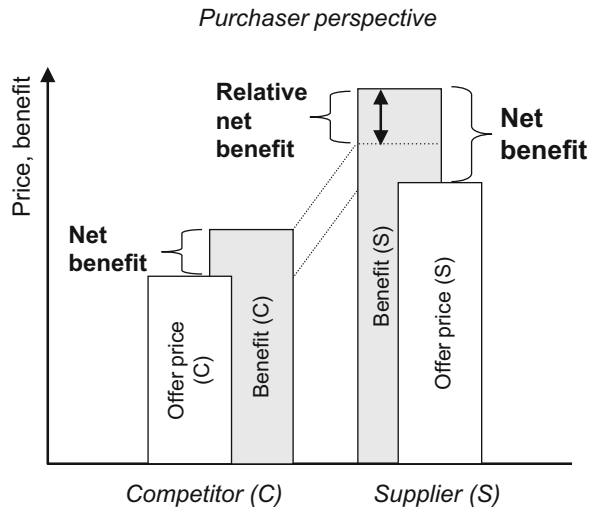
The Core Service as the Reason for Repeat Purchasing Behavior

The essential benefit for the customer is derived from the composition of the core service. In following our exchange argument in Chap. 1, benefit and price in turn form the central parameters for the composition of the customer benefit. If the supplier is successful in creating benefits to the customer on the basis of the core service, the customer will enter into the exchange with this supplier and not with a competitor. Figure 3.2 illustrates this correlation.

The customer has two offers to choose from: one from the focal supplier (S), the other from the competitor (C), which is in this case the most appealing alternative to supplier (S) for the customer. To even be considered by the customer, both offers must on their own demonstrate a positive **net benefit**, meaning that the anticipated benefit of the offer must exceed the price to be paid. But the customer will still only choose one of the offers, namely the one with the greatest net benefit. We refer to this difference as the **relative net benefit**. In the situation illustrated, such a relative net benefit favors supplier (S) over competitor (C) in the customer's favor and forms the basis for a customer benefit advantageous to the supplier (S). If the supplier is able to maintain this customer benefit over the long term, the customer will continue to favor this supplier over competitors (Bliemel and Eggert 1998; Meffert 2005), meaning that he will make future purchases from the supplier as subsequent transactions. So in this case repeat purchasing is the result of enduring, “simple” customer benefit. Plinke (1997) calls this a *de facto* business relationship.

An example of the significance of **de facto business relationships** in business markets is the empirically verifiable proportion of these regular customers in the customer base of the German mechanical engineering sector. Corresponding data

Fig. 3.2 Customer benefit as relative net benefit



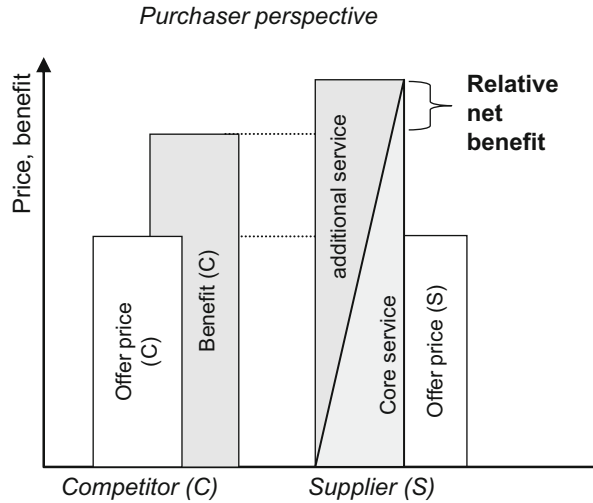
was discovered by the NIFA panel, which conducted specific research at the Ruhr-Universität Bochum from 1991 through 1997 (Jacob 2002). Over time, more than 40 % of all registered German mechanical engineering companies took part, which makes the study highly representative of the market. When the time span 1996 was examined, it was shown that an average of about 50 % of all of a mechanical engineering companies' customers are regular customers. The proportion of total sales generated from business with regular customers was determined to be around 75 %.

It should be noted, however, that repeat purchasing behavior is linked to the sustainability of customer benefit from the core service of the exchange relationship. If the structures of the exchange change, e.g. if a competitor increases the benefit of his offer to the customer or reduces the prices, the basis for repeat purchasing behavior is negated. Innovations, price changes or a stronger pace in the competition can affect switching. The customer will then immediately switch to the supplier making the most appealing offer (Bliemel and Eggert 1998). Thus repeat purchasing behavior is linked to the sustainable maintenance of the customer benefit in the exchange relationship; long-term security of the customer benefit must be the focus of the supplier.

Ancillary Services as the Reason for Repeat Purchasing

Ancillary services can take many different shapes, whereby the aspect referred to as customer service (Stauss 1991), often has particular significance (Meffert 2000). Examples of customer service are: technical and administrative customer support; ordering service; delivery; assembly; supply of spare parts; maintenance; repair, option to exchange a product; training and courses; hotlines; internet-based services; and also the availability of the supplier's distribution centers. Just like the core service, ancillary services change the exchange relationships (Reichheld

Fig. 3.3 Ancillary service and repeat purchasing behavior. Source: Based on Jacob (2009)



1993). Figure 3.3 offers a general overview of the effect of ancillary services on exchange relationships.

The illustration shows the situation in which the customer benefit favors the supplier (S)—a benefit resulting from the combined effect of core and ancillary services (Diller 2007). Just like a customer benefit based on a core service, such a customer benefit can motivate the customer to repeat purchasing. For this to happen, the supplier has to offer unique ancillary services or has to surpass competitors in regard to the quantity and quality of ancillary services. Once again, this repeat purchasing will endure only as long as the benefits of the exchange relationship favoring the supplier can be maintained. If the benefits of the relationship change, e.g. due to measures taken by the competitor, the customer will immediately change suppliers and cease repeat purchasing. However, it is often said that particularly ancillary services are harder for the competition to imitate than core services (Meffert 2000), and repeat purchasing founded on ancillary services is more resistant to competitors' measures than is repeat purchasing based on a core service.

As the following definition demonstrates, ancillary services implemented by the supplier for the express purpose of motivating the customer to repurchase are summarized by the term **Customer Relationship Management (CRM)**: “CRM is a customer-oriented corporate philosophy that, with the aid of modern information technology, attempts to build and solidify profitable customer relationships over the long term by applying comprehensive and differentiated marketing, sales and service concepts” (Hippner et al. 2001, p. 417). CRM is further specified in Fig. 3.4.

The illustration indicates that there are three dimensions of Customer Relationship Management (Hippner and Wilde 2005; Pritzl and Lauer 2003). Analytical CRM means that information related to the data object single customer is collected,

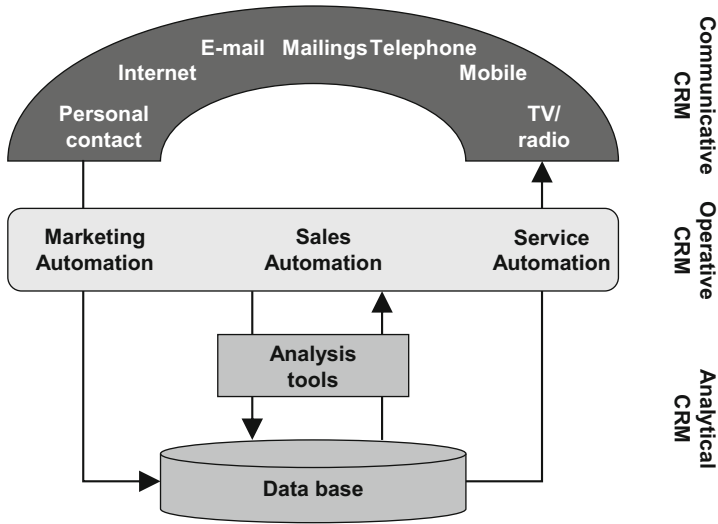


Fig. 3.4 CRM and the constellation of ancillary services. Source: Based on Hippner et al. (2001)

maintained and prepared for use. Tools used for analytical CRM are modern electronic databases as well as special tools for data analysis. These tools can be used to support operative CRM in the sense of marketing processes, sales processes and service processes. This enhances the impact of general advertising campaigns by directly addressing individual customers electronically. In sales, schedule management can be automated and thus improved. The user-friendly design of systems for E-commerce is a variation that improves service processes. But each operative CRM is always characterized by the use of modern technologies to communicate with the individual customer, meaning that communicative CRM must be named as an ancillary dimension. Figure 3.4 indicates the respective communication technologies. It must, however, be taken into consideration that especially these technologies are subject to vast dynamics right now. Example 2 uses a practical example to illustrate the effect of CRM as an ancillary service to the customer benefit.

Example 2: CRM in Material Sales

Bayer MaterialScience is a manufacturer and supplier of high-quality materials and is a global market leader in the field. A challenge faced by the sales department is the global and sometimes very nontransparent structure of its own customers. “Our old customer relationship management was distributed amongst about a dozen parts of old systems we had developed ourselves. We had to gather the required information from different databases and transaction systems. We saw the opportunity to achieve absolute

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transparency with a uniform CRM solution,” says Dietmar Gasch, head of Organization and Informations Systems for Bayer MaterialScience. The introduction of a uniform CRM system not only improved internal processes, it also generated direct benefits to the customers: “Using the web platform, customers can call up status information on orders and deliveries, download data sheets, safety information or certificates, or check the availability of the desired products any time they wish.” (Blache et al. 2005)

3.1.1.2 Repeat Buying Due to Bonding

While customers who repeatedly buy from the same supplier because of the core and ancillary services continue this behavior as long as the exchange relationship with the respective supplier remains beneficial, repeat buying based on bonding is resistant to such changes, at least in the short and middle term (Diller 2007; Pritzl and Lauer 2003). Relevant literature differentiates between a demand- or output based understanding of the term customer bonding and a supplier- or input-based understanding of the term (Diller 1996; Dittrich 2000). When describing customer bonding, demand-based describes customer behavior that leads to repurchase. In regard to the supplier, the term bonding summarizes all measures taken by the supplier intended to promote the customer’s behavior. So it would be correct to refer to customer bonding management (Weinberg and Terlutter 2005). We will initially apply a demand-based understanding of the term. Bonding in this sense can be attributed to economic effects on the one hand and to the attitude constructs trust and commitment on the other.

Economic Effects as the Reason for Customer Bonding

Bonding based on economic effects is referred to by Bliemel and Eggert (1998) as obligation—as opposed to bonding—of the customer. Economic obligations (lock-in) means that certain elements have to be considered in the exchange relationship that make it more difficult for the customer to change from his current supplier to a competitor. Individually, these elements can be about the impact of **specificity** and of **satisfaction** (Linke 2006).

Specificity as Switching Barrier

The term specificity was coined by Williamson (Williamson 1990) in the course of his contributions to the development of transaction cost economics. Specificity very generally describes a characteristic of resources. It means that the resources can only deliver their full benefits in a certain, specific context (Linke 2006). If the initial acquisition of the resources is linked to a payment, one refers to a specific investment. The difference between reaping the full benefits and reaping the benefits of the next-best alternative use is called the quasi rent (Linke 2006). Specificity becomes interesting to business relationships when the context deals

with the continuation of the exchange relationship with one and the same partner (Preß 1997). Specific resources can occur in the most varied shapes, which is clearly shown in Examples 3 and 4.

Example 3: Manufacturer Warranty for a New Car

When a consumer buys a new car, he generally purchases not only the vehicle but also the legal claim to its proper functioning for a certain length of time. Such a warranty is usually valid for three years. Special legal regulations allow manufacturers of motor vehicles to require to some extent that the regular maintenance and service work be performed in one of the manufacturer's authorized shops for the warranty to remain valid. So if the owner of a new vehicle wishes to retain the full warranty provided by the manufacturer, he cannot have any required maintenance performed by an independent garage. Upholding his legal claim to the warranty is tied to repeatedly buying maintenance services in an authorized shop.

Example 4: Frequent Flyer Cards

There are some very successful bonus programs in the airline industry, like Lufthansa's Miles and More program (Eisenächer 2005). Passengers can sign up for the program and then accumulate points every time they fly with the respective airline. When they reach a certain number of points, the points can be redeemed for an award, usually a free flight. However, an amount of points below the required minimum amount would lose its complete value, were the passenger to decide to no longer fly with that airline but to take advantage of offers from competitor airlines. So the value of the points can be maintained only by frequenting flights from the same airline in the future.

If the customer has made an investment specific to the supplier or if he has a resource specific to the supplier, the quasi rent should always be taken into consideration when evaluating the exchange relationships. It always makes the competitor's offer less attractive. After all, the investment or resources would be lost, were the customer to leave the context of the business relationship. As Fig. 3.5 shows, this effect of specific resources can shift the customer benefit in an exchange relationship (an alternative representation for the same situation can be found in (Plinke 1997). If without the influence of the specific resource there would be a customer benefit for the competitor, the existence of a specific resource would make it a disadvantage to the customer. Because specificity is a phenomenon that outlasts the individual transaction, it can form an enduring basis for repeat purchasing.

So inducing the customer to make specific investments can be a way to secure repeat buying. However, the effect of specific resources in securing repeat buying has limits. On the one hand, it must be taken into consideration that, as with most

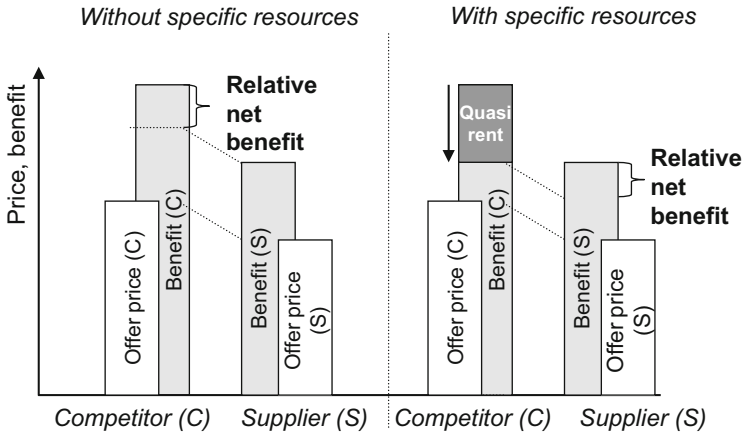


Fig. 3.5 Specificity in the exchange relationship. Source: Based on Jacob (2009)

resources, specific resources lose value over time (Dittrich 2000; Weiber and Adler 2003). If the age of a new car exceeds the warranty period in Example 3, the obligation imposed by the warranty to have maintenance and repairs performed at an authorized shop is no longer relevant. The same applies to the miles accumulated in the frequent flyer account in Example 4, once the points have been cashed in for an award. The passenger can then join and use a different airline's frequent flyer program, if he so chooses. But on the other hand Bliemel and Eggert (1998) point out that bonding in the sense of obligation (lock-in) is not in the customer's best interest. Lock-in signifies dependency, which poses a risk for the customer. So it can be expected that customers will demonstrate strong reactance to a supplier's attempts to induce the customer to make specific investments. These would be defensive reactions to internal or external restrictions. This is why marketers should promote specificity that leads to customer satisfaction (Dittrich 2000).

Satisfaction as Switching Barrier

Satisfaction always creates a bonding effect when, in an exchange situation, the offers of competitors seem to be uncertain. Uncertainty can be the result of uncertain elements related to benefit or price. The following example illustrates a specific type of uncertainty occurring in exchanges on business markets.

Example 5: Uncertainty in Exchanges Occurring on Business Markets

In its edition of November 4, 2009, no. 256, the newspaper *Frankfurter Allgemeine Zeitung* reports on page 17: Price increase in SAP maintenance—To the annoyance of its German customers, the software corporation SAP has raised the prices for standard maintenance. As the SAP user group DSAG stated, “In view of the current economic situation and to facilitate

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reverting to a trustful business relationship, a general suspension of the price increase would have been the right thing to do.” The group conjectures that the price increases for standard maintenance are intended to force the customers into the more expensive Enterprise Support. The quintessence of the dispute is the increase in maintenance costs planned last year, rising from 17 to 22 percent of the license fees. Revenue generated from maintenance is essential to the corporation, helping it to compensate for the slump in license fee revenue.

Opportunistic behavior, which the customer has to assume of all suppliers, can lead to an absence of benefits. Opportunism refers to conscious acceptance of a disadvantage for others with the intention of furthering one’s own best interest (Williamson 1990). SAP’s behavior in Example 5 can be interpreted as such, at least from the user’s or customer’s point of view. Transaction costs that the customer incurs due to measures intended to protect him from such opportunism, force up the price for the customer. The same is true for hidden prices, for ancillary services for which the necessity is not apparent until later, and for high maintenance and service costs that the customer is not informed of until after conclusion of the contract. Figure 3.6 shows how uncertainty impacts the perception of the net benefit of a single offer. It is especially apparent that the uncertainty shown poses a threat to the net benefit that the supplier anticipates from the offer.

In conjunction with Fig. 3.6, Fig. 3.7 offers a general explanation of how uncertainty can impact the customer benefit. We will first examine the left side of the illustration. Two competing offers—one from the focal supplier (S), the other from the competitor (C) who once again represents the best alternative to supplier (S)—are characterized by uncertainty. The net benefit of both offers—before the exchange—is endangered, because the customer cannot be certain about whether his expectations in regard to benefit and price will be met.

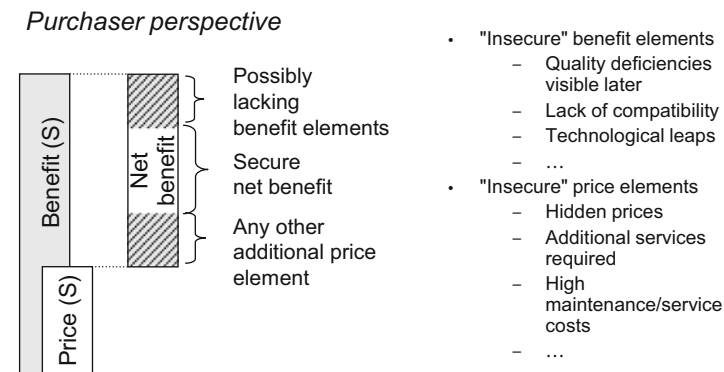


Fig. 3.6 Uncertain net benefit in the market transaction. Source: Based on Jacob (2009)

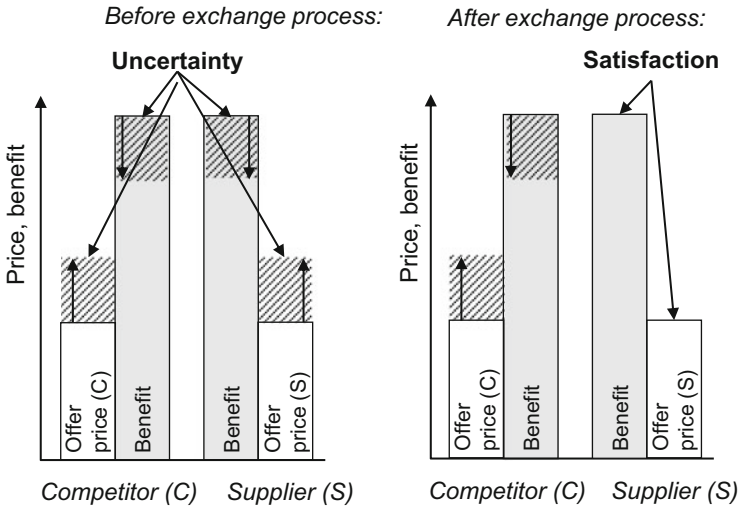


Fig. 3.7 Uncertainty and satisfaction as determinants of customer benefit. Source: Based on Jacob (2009)

The supplier who succeeds in achieving an exchange with the customer has the unique opportunity to deliver satisfaction and eliminate uncertainty with the constellation of the service offered. This happens by not displaying any opportunistic behavior and by performing the service as it was promised and as the customer expects. Transaction costs to overcome uncertainties are no longer incurred once the customer has experienced such satisfaction. A general overview of this principle can be seen on the right side of Fig. 3.7. Supplier (S) increases the benefits of his offer, while the competitor's offers continue to be impacted by uncertainty. This influence is enduring, because transactions with the competitors always pose the risk of disappointment—a risk to which the customer does not wish to expose himself (Dittrich 2000). So under the conditions described, satisfaction encourages the customer's repeat buying.

Example 6: Customer Relationships in the Logistics Field

In a press release, the company Deutsche Post DHL reports: DHL Express expedites complaint management—How good a customer relationship is particularly apparent when mistakes are made and the customer complains. The less bureaucracy the company shows in handling the complaint, the more enthusiastic is the customer. Since even the specialist for quick and reliable deliveries within the postal system cannot eliminate every potential error, complaint management is a high priority at DHL Express. A special service offered by DHL allows customers to specify the precise time that critical

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shipments are delivered to the recipient. If DHL Express cannot meet the delivery time, the customer is ensured a refund of the shipping costs. The customer has simply to call the service hotline. However, when customers were surveyed, it was revealed that they found the wait too long when they called the hotline. The source of the problem was quickly apparent: The service employees at the hotline were not authorized to decide whether or not the demanded refund was justified—even when the customer was obviously right. The hotline personnel have since been trained to evaluate complaints and decide on shipping cost refunds to regular customers. Subsequent customer surveys indicated much fewer complaints about delays. And customer satisfaction as well as the intention to remain a customer of DHL rose.

As these examples show, satisfaction is something that does not just happens on its own: The supplier has to act consciously to achieve it. The actions required to succeed in delivering customer satisfaction are summarized under the term satisfaction management. The basic functionality for this concept is supplied by the confirmation/disconfirmation paradigm (C/D) (Kaiser 2005; Krafft 1999). Accordingly, expectations and perceptions of the customer upon purchasing a product or using a service form the starting point for the development of satisfaction or dissatisfaction. In a subjective comparison process, the customer looks at the service as he expects it from the supplier on the one hand and the service as he actually perceives it on the other. Confirmation means that the perception meets the expectations. If the perceived actual service exceeds the anticipated service, it is referred to as positive disconfirmation. If, on the other hand, the actual service falls short of the expectation, it is negative disconfirmation. Confirmation and positive disconfirmation result in satisfaction, while negative disconfirmation leads to dissatisfaction. Figure 3.8 illustrates these correlations. So satisfaction can be classified as an attitude resulting from cognitive processes as well as from emotional elements (Foscht and Swoboda 2004; Steffenhagen 2004).

The C/D paradigm is applied as a management approach in the so-called GAP model by Zeithaml, Berry and Parasuraman (Hentschel 1990; Zeithaml et al. 1988). This model first cites the sources of expectations, and then shows the individual needs, experiences from the past, word-of-mouth communication with other market participants and the supplier's communications aimed at the customers. It also clearly indicates how the supplier's services develop and where the causes of non-fulfillment of expectations of the services lie—in other words, the gaps (Fig. 3.9).

Gap 1 indicates deficits in anticipating customer expectations. This deficit can be the result of errors in market research or of a lack of sensitivity to customer wishes on the part of service personnel. Gap 2 relates to errors in designing specifications to meet expectations. This can usually be attributed to poor internal communication. Gap 3 shows that poor implementation of specifications can also be a source of later dissatisfaction. This could be due to e.g. inadequate technical equipment of the

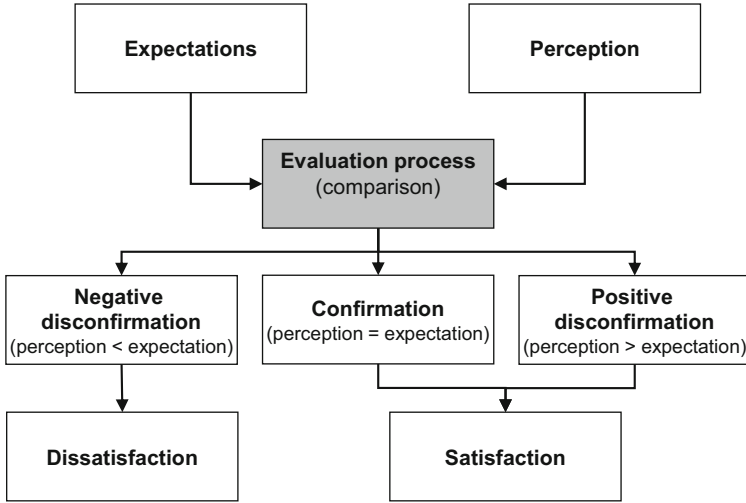


Fig. 3.8 The C/D paradigm. Source: Based on Foscht and Swoboda (2004)

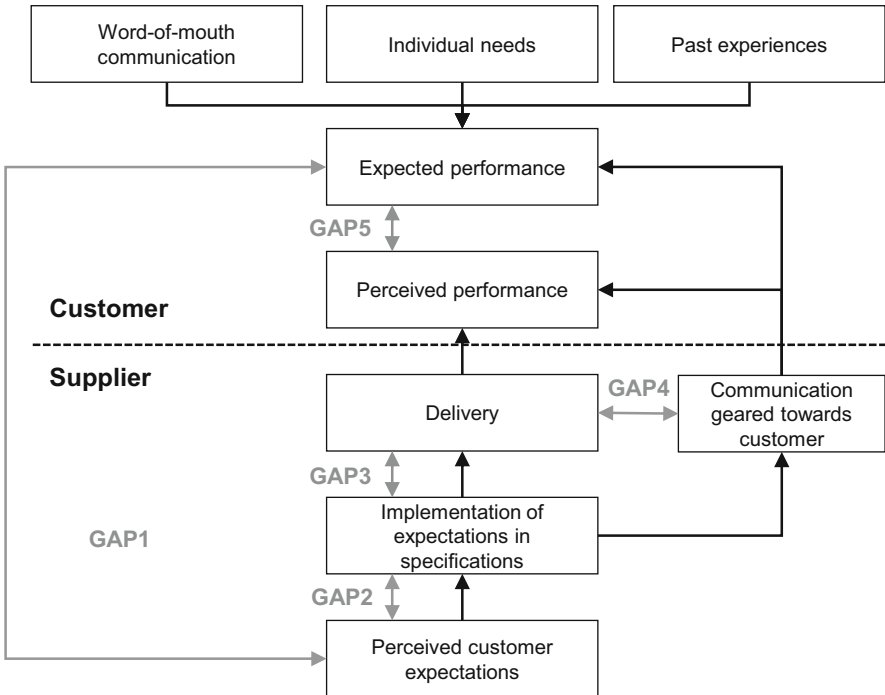


Fig. 3.9 The GAP model of customer satisfaction. Source: Based on Zeithaml et al. (1988)

supplier. Gap 4 illustrates the divergence between communicated service and the actual service rendered, whereby a higher service standard is communicated than rendered. This is generally referred to as “over-promising” and is caused by poor horizontal communication within the supplier company, e.g. between advertising and product management. Finally, gap 5 indicates the evaluation process of the customer and is the result of all preceding gaps.

In addition to the great degree of detail, another benefit of the GAP model is that, by examining the gaps, specific approaches can be found for practical management of customer satisfaction (Bruhn 2001; Kleinaltenkamp and Jacob 2006). Decision makers can see which sub-processes within the company need to be analyzed and potentially improved as well as monitored over the long term.

In published literature, satisfaction is often named as the central element determining customer bonding and thus ensuring repeat purchasing (Krafft 1999). Satisfaction is the root of a bonding effect to the extent that changes in the competitors’ offerings do not affect the decision of the customer as long as the market remains uncertain. This is the difference between repeat buying based on satisfaction as well as on specific resources and repeat buying based on core and ancillary services, where a change by the competitor in the exchange relationship immediately causes the customer to reconsider his choice of supplier. But it should also be pointed out that the bonding effect of satisfaction should be considered weaker when the number of competing offers is not characterized by uncertainty. If the customer can be certain that the services will be performed as expected, he can definitely assess all of the alternative offers, even if he has had no previous experience with the suppliers. Satisfaction then poses no more switching barriers. Confirmation of this can be found in studies performed in certain industries, proving that even customers prone to switching are highly to very highly satisfied with the original supplier (Reichheld 1993; Weinberg and Terlutter 2005). However, this insight does not absolve company decision makers from their obligation to assign utmost importance to satisfaction management.

Trust and Commitment as a Source of Customer Bonding

While customer bonding on the basis of economic effects is referred to as obligation or lock-in, **trust** and **commitment** lead to customer bonding in a merely positive sense (Bliemel and Eggert 1998). The repeat purchasing behavior that this bonding promotes is based on a customer’s positive and outstanding attitude regarding a single supplier (Plinke 1997; Weinberg and Terlutter 2005). The positive attitude is attributed to trust in the supplier and is manifested in commitment to the supplier. Thus trust and commitment are key factors of customer bonding in the sense of demand-based bonding (Bliemel and Eggert 1998; Bruhn 2001; Dittrich 2000).

We generally see trust as an expectation construct. The more specific understanding of the term in published literature is multi-faceted and more complex (Blomqvist 1997; Plötner 1995) definition is representative of how the term is understood: “*Trust is the expectation that a person or group of persons has not or will not act in an opportunistic manner in regard to a deliberate event, at least not towards the person extending the trust*” (Plötner 1995, p. 36). Thus trust is

characterized by the conscious relinquishing of supervisory measures (Linke 2006). In the sense of a (neo-) behavioral interpretation, the expectation construct trust arises from certain appealing factors or stimuli originating with the object of the expectation (supplier) and perceived by the person extending his trust (customer) (Preß 1997).

Commitment, on the other hand, expresses the intentional element of the positive and outstanding attitude of the customer towards the supplier. There are also diverse definitions and models for commitment (Söllner 1993). Moorman et al. (Moorman et al. 1992, p. 316) phrase it concisely: “*Commitment to the relationship is defined as an enduring desire to maintain a valued relationship.*” This includes the willingness to make short-term sacrifices (Dittrich 2000).

Example 7 demonstrates how a positive attitude based on trust and commitment can actually influence repeat purchasing.

Example 7: Bonding to Supplier When Purchasing an Automobile

The market research institutes Deutsche Automobil Treuhand GmbH (DAT) and Gesellschaft für Konsumforschung AG (GfK) regularly conduct studies to collect fundamental information on the development of the automobile market in Germany. The information is published in the DAT-Report. The study also identifies the degree of bonding to manufacturers when purchasing new and used vehicles. For the year 2005, it was determined that 45 % of used car buyers and 59 % of new car buyers were loyal to the manufacturer from which they purchased their last vehicle. Within sales of new cars, bonding to the manufacturer was more pronounced amongst buyers of German brands than those who chose foreign cars.

Trust and commitment make existing business relationships resistant to competitive measures. Similar to repeat based on satisfaction, repeat purchasing based on commitment and trust differs significantly from repeat purchasing on the basis of core and/or ancillary services. In the sense of an argument introduced by Plinke (2000), trust and commitment represent the emotional and conscious attitudes of the customer, which are reason to ignore competitors’ offers when evaluating the exchange relationship. So we can assume that the bonding (loyalty) effect based on trust and commitment is even stronger than that based on satisfaction. Figure 3.10 illustrates this understanding of the effect of trust and commitment using our basic exchange theory model. The pale area in the bar representing the competitor’s offer in a situation characterized by a customer’s trust and commitment signifies the mental “ignoring.”

Trust and commitment are established over time. They can emerge as a result of all of the other factors mentioned thus far that promote repeat purchasing—core services, ancillary services and economic switching barriers. So the triggers for repeat purchasing that we are dealing with here are not unrelated, which is clearly demonstrated in Fig. 3.1.

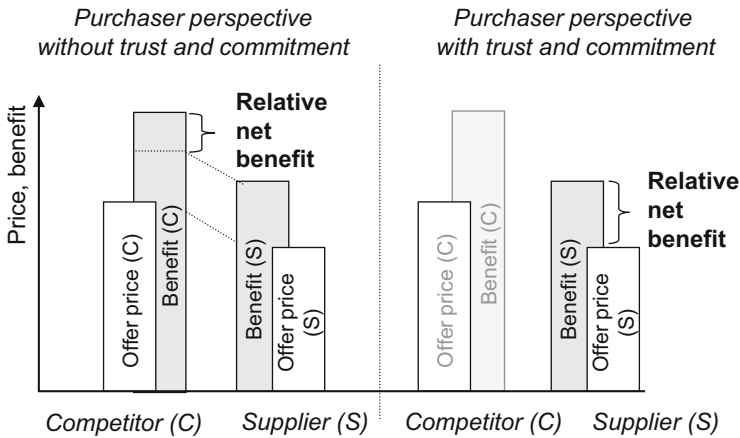


Fig. 3.10 Trust and commitment in an exchange relationship. Source: Based on Jacob (2009)

Trust as an expectation on the part of the customer is thus a behavioral determinant that can definitely be acknowledged as an emergent factor. This means that trust develops implicitly over time, without superficial intentions of the participants. The form and extent of trust always remain emergent or implicit. However, some fundamental correlations to active and systematic management of trust can still be posed. Measures to promote trust apply the effect of references, similarity, self-confidence and reciprocity (Plötner and Jacob 1996). The correlations will be explained briefly here.

The supplier's past transactions and projects are referred to as **references or referrals**. They become relevant to the aspect of trust when they prove that the trust that others placed in the supplier was not violated. This type of confirmation can also form the foundation for expectations of trustworthiness geared towards the future. To be able to maximize the benefit of their effect for a certain customer, the supplier should carefully select references before presenting them to the customer (Günter 1979).

The effect of **similarity** in establishing trust has been proven in a multitude of empirical studies (Crosby et al. 1990; Schoch 1969). Findings show that people tend to trust a counterpart in whom they see similarity. If a supplier would like to use this correlation to establish trust and business relationships, there are two fundamental ways to go about it:

- One method is to select only the target segments that are compatible with the supplier's customer contact personnel.
- The other way is to recruit employees who are similar to a specified segment of customers.

The consistency of the behavior of the person or group of persons to which the trust is extended is also an object of the expectations linked to the trust. Only

persons who behave consistently can be considered to be trustworthy. In contrast, inconsistent behavior leads to mistrust, because the behavior cannot be anticipated. One indicator of consistent behavior is a person's self-confidence (Plötner 1995). So we can assume a correlation between the trustworthiness of a supplier and the self-confidence of his employees at the interface to customers. Self-confidence is primarily a personality trait. If it is to be applied to promote trust in relationship management, self-confidence can be specified as a criterion in the selection of personnel who will be dealing with customers. However, self-confidence can be build up within certain limits. There is an approach from behavioral theory that states that self-confidence can be promoted applying an incentive system (Petermann 1996). The employee is confronted with tasks that he must master. If he is successful, he knows that his success is due to his own skills. The employee experiences a great degree of self-efficacy, which leads to confidence in himself. This approach is implemented in the course of leadership to directly promote self-confidence and thus indirectly establish customer trust.

The final principle for targeted management of trust is **reciprocity**. Quite a few authors (Plötner 1995) are convinced that a trusting relationship can only be based on a relationship of mutual trust or reciprocity. So one can expect trust from a counterpart only when one is willing to trust the counterpart. This thesis has been confirmed by experiments performed as part of game theory (Axelrod 1987). Reciprocity is fortified by repeated extension of trust by both parties. But despite the mutuality, one participant must still take the first step. The field of conflict studies (Osgood 1959) has offered suggestions on how a party interested in establishing trust can initiate a so-called spiral of trust. The steps are:

1. One's own interest in a trusting cooperation should be communicated
2. Then a signal of one's own initiative must be conveyed
3. The initiative should be implemented and
4. The counterpart should be invited to share in reciprocal behavior.

For relationship management, this means that trust management requires some preliminary work. This can take the form e.g. of offering a free consultation with no obligation. It is, however, important to restrict the scope of the preliminary work. After all, the principle of reciprocity implies *quid pro quo*. If the preliminary work is considerable, the customer may feel overwhelmed by the expectation. So reciprocity applies a policy of small steps towards establishing trust.

Table 3.1 summarizes these approaches for the management of trust in the context of relationship marketing.

3.1.2 Supplier Benefit as a Determinant of Repeat Purchasing

The previous sections dealt with uncertainty on the part of the supplier as an essential behavior determinant for the perception of a customer benefit on the part of the customer. In extreme cases, the customer may refrain completely from

Table 3.1 Management of trust

References	<ul style="list-style-type: none"> • Identification of references • Cooperation with references • Assurance of references to provide information
Similarity	<ul style="list-style-type: none"> • Similarity at the individual level • Similarity at the group level • Similarity at the corporate level
Self-confidence	<ul style="list-style-type: none"> • Self-confidence as trait required of new recruits • Establishment of incentive systems that reinforce behavior • Measures to increase the professional and social competence of employees
Reciprocity	<ul style="list-style-type: none"> • Initiation of spirals of trust • Promotion of leverage symmetry in the supplier/customer relationship

Source: Based on Plötner (1995)

the market exchange, because the conditions that he requires for a positive net benefit are no longer given. The supplier then has various measures on hand to eliminate uncertainty perceived by the customer and to once again ensure the conditions that facilitate an exchange. The supplier's intention to continue a business relationship plays a certain role with these measures. As we will show, such an intention is relevant to the structure of the supplier advantage. After explaining the fundamentals of contract theory, we will reveal this correlation.

3.1.2.1 Contract Theory

An initial approach to mastering the challenge posed by uncertainty perceived by the customer can be found in the legal system, where contracts are used as the respective instrument. Contracts are generally seen as a way to ensure safety and reliability for the contracting parties. Contract theory names three very general differentiations in the types of contracts, as shown in Table 3.2 (Macaulay 1963; Macneil 1978; Williamson 1979).

The classical contract is the standard form of a contract and attempts to find wording that covers all potential contingencies that could present a cause for uncertainty. Purchase contracts, rental contracts or service contracts generally follow the pattern of a classical contract. The rights and obligations of the contracting parties are explicitly specified. The classical contract always fulfills its function when all of the causes of potential uncertainty can be completely covered. But the increasing complexity of the conditions surrounding the market exchange makes this more and more questionable. Reference is made to the incompleteness of the classical type of contracts (Göbel 2002). This causes market participants to lose faith in the functionality of classical contracts. The neoclassical contract attempts to avoid this problem by no longer formulating the contingencies themselves but only the way in which they should be dealt with. Arbitration processes for handling conflicts between the contracting parties are specified. Appropriate clauses can be found in comprehensive contracts between the exchange partners in the capital goods sector. But once again the problem is that

Table 3.2 Types of contracts in contract theory

Type of contract	Classical contract	Neoclassical contract	Relational contract
Principle	Rights and obligations of the contracting parties are precisely formulated to cover all contingencies	Specification of arbitration process in the event of dispute	The contracting parties protect themselves by exchanging pledges
Problems	<ul style="list-style-type: none"> • Completeness of contract • Cost of contracts (wording and implementation) 	<ul style="list-style-type: none"> • Predictability of dispute • Cost of contracts (costs incurred to create contract and for arbitration) 	<ul style="list-style-type: none"> • Constellation of pledges • Effectiveness of pledges

this type of contract also remains incomplete. Relational contracts forgo completely an explicit wording and implicitly bind the parties to one another. This usually occurs by exchanging pledges. A pledge received by one of the two exchange partners protects from opportunistic behavior on the part of the other partner. Pledges can be exchanged formally, e.g. as a security guarantee. In this case a third party—frequently a financial institution—formally agrees to provide a sum of money or some other service when requested to do so by the holder of the guarantee. The holder can then take advantage of the guarantee when he considers previously agreed stipulations to have not been fulfilled. So the guarantee reduces the behavioral uncertainty that the holder could feel towards the bearer of the guarantee. However, formal guarantees to ensure that business relationships function properly tend to be uncommon in actual practice. But relational contracts can come about more informally. The so-called shadow of the future, with its implications for the development of business relationships, will be introduced here as a variation of relational contracts that is relevant to marketing purposes.

3.1.2.2 Business Relationships as Relational Contracts

To be able to explain how the “shadow of the future” functions as a determinant of repeat purchasing behavior, the supplier advantage must be explained as the counterpart to the customer benefit in the market transaction. Figure 3.11 shows this as a bar graph. It is apparent that the price is the element that links the customer perspective and the supplier perspective. While for the customer in the exchange the price represents the sacrifice to be made, for the supplier it is the incentive to participate in the transaction. But both the supplier (S) and the competitor (C) have to compare this price with the costs incurred to provide the service that is the object of the exchange. If the price is higher than the costs, the result is a profit. Over the long term, the supplier with the greatest profit has an advantage. So a positive difference in one’s own profit as compared to the profit of the competitors is considered a supplier advantage.

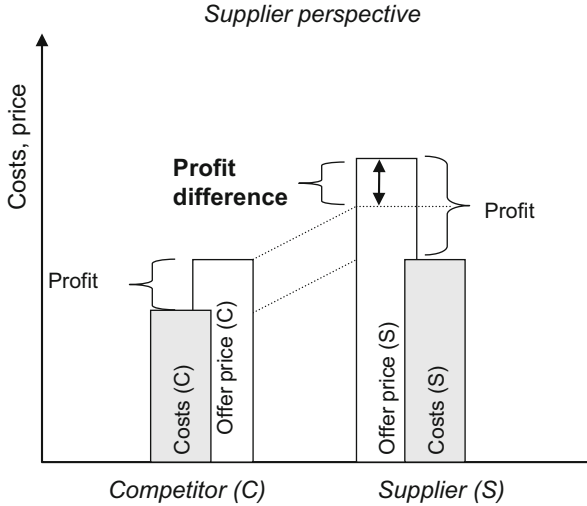


Fig. 3.11 Supplier advantage in market exchange

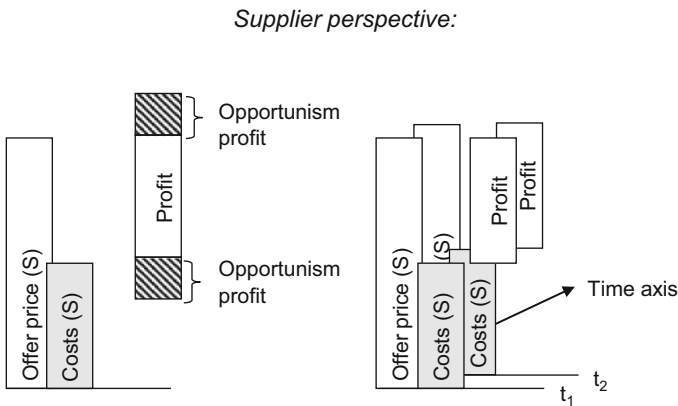


Fig. 3.12 Shadow of the future. Source: Based on Jacob (2009)

The left side of the next illustration, Fig. 3.12, shows how the reduction in net benefit that the customer perceives as caused by uncertainty impacts an increase in the supplier’s profit. Price increases and reductions in performance due to opportunistic actions harm the customer and can even benefit the supplier. For the supplier, price increases directly improve profit. Reductions in performance indirectly increase the supplier’s profit, because he can save costs when efforts are reduced. So in the short term, the supplier definitely has an incentive to act in an opportunistic manner when he has flexibility like that expressed in Example 5. After all, this

would increase profit and thus his leverage in the competition with other suppliers in his industry.

But as shown on the right side of Fig. 3.12 the supplier can relieve the customer of this uncertainty. This can succeed when the supplier can plausibly convey that short-term opportunism is not worthwhile because it poses a threat to profits from future transactions with the same supplier. After all, when a customer has once been disappointed by the supplier, it can hardly be expected that he will do business with the same supplier in the future. If the customer shares this insight into the structure of the supplier advantage, his remaining in a business relationship with the supplier becomes a pledge and overcomes any perceived risk of opportunism. The risk of losing future benefits of a business relationship dampens the attractiveness of short-term opportunistic behavior or short-term profit gained from opportunism. In game theory this principle is assigned the metaphor “shadow of the future (Axelrod 1987). So market transactions have to be properly prepared by the supplier by conveying to the customer his own dependency and his interest in a long-term relationship, as opposed to short-term benefits from opportunistic behavior. These efforts are apparent in the following practical example.

Example 8: Planning Tools for Software Consulting

For a long time now, the software company SAP has been cooperating successfully with software consultants who adapt software systems to the individual needs of the users. The largest German software consultant working with SAP is the Telekom subsidiary T-Systems. Upon announcement of the adoption of a new planning tool for the SAP software configuration, the company T-Systems in a press release quotes an executive of the supplier SAP:

“We are happy that, with the introduction of the ‘Run SAP’ method, T-Systems is eager to expand its long-term business relationship with SAP,” states Dr. Uwe Hommel, Executive Vice President of SAP AG. “T-Systems is one of the first SAP partners to introduce the concept of continuous operational procedures—a concept provided by Run SAP—to its application management services and hosting offers.”

In the example, both companies—supplier and customer—publicly express their mutual interest in continuing the business relationship. The continued existence of the business relationship is then more valuable than a short-term profit gained from opportunistic actions, particularly on the part of the supplier. Media reports clearly indicate that both parties recognize this. A “shadow of the future” manifests itself. Insights into these correlations and the awareness of the participants in the mutuality lead to a decrease in uncertainty for the customer and thus to repeat purchasing behavior.

So, repeat purchasing behavior itself is inherent to the repeat purchasing behavior. This effect does not stem from the history of a business relationship but from its

potential future (Jacob 2002). This effect arises from the structure of the supplier advantage and affects the customer benefit.

3.2 The Business Relationship over Time

Because of their special nature, repeat purchasing behavior and business relationships are temporal. However, we have thus far looked at them from a static perspective. This means we have developed an understanding of why customers in certain purchasing situations make a decision for the in-supplier and against the out-supplier. This insight is essential to current market actions of a supplier. But it is obvious that behavior should also be examined beyond the current purchasing situation. After all, marketing management includes not only the present but also a planning task that extends beyond. This planning task has to take into consideration the history of a business relationship and show the way into the future. This is what research on the life cycle of a business relationship deals with. It is also the topic of the next section.

3.2.1 The Life Cycle of a Business Relationship According to Dwyer et al.

The approach presented by Dwyer et al. (1987) is of fundamental significance to research on the life cycle of a business relationship. The approach should initially be seen as an analogy to the product life cycle and explains the ideal type of time sequence of a customer relationship (Stauss 2006). It differentiates between five phases of a business relationship (Preß 1997). The cycle begins with an initiation phase in which potential partners in a later business relationship get to know one another. The customer becomes aware of a supplier and the products and services offers, and then he deliberates entering into market transactions. For the supplier, this phase is important to demonstrating his attractiveness to the customer. This phase is followed by one of exploration, in which the potential partners look at the possibilities of purchasing and of a stronger commitment to one another. At this point, the force of the commitment remains relatively low though. The relationship should be considered as not yet solidified. However, the foundation for expansion of the cooperation between supplier and customer is established. This is the phase in which bonding arises, whether of an economic nature or on the basis of trust and commitment. Once these bonds have been consolidated, they can evolve—which, in the case of bonding, leads to greater satisfaction. When the market partners discern the value of the business relationship, the requirements for creating a “shadow of the future” have been met. But every business relationship is susceptible to the threat of dissolution. The initiative to terminate the relationship usually comes solely from the customer. The termination phase is always characterized by the fact that the requirements for the emergence of repeat purchasing behavior

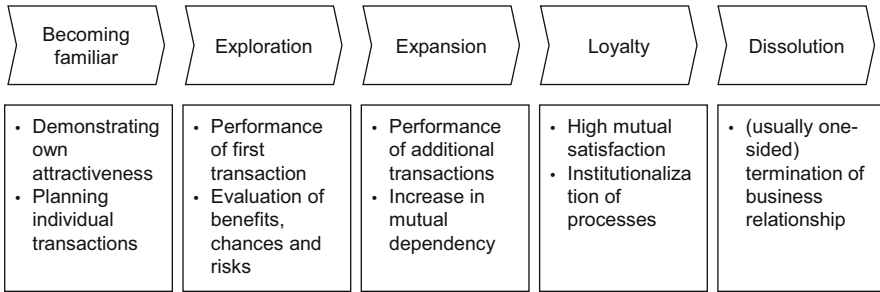


Fig. 3.13 Life cycle of a business relationship. Source: Based on Dwyer et al. (1987)

described in previous sections have fundamentally changed. Figure 3.13 offers an overview of the life cycle of a business relationship.

It should be noted that the course of a business relationship as shown in the illustration is the ideal. Practical market applications can deviate from this pattern at any point. This is why the deterministic character of the phase sequence shown is often criticized (Stauss 2006). It is also important to mention that the approach offers no assertion on the duration of a single phase; in actual practice, this is strongly dependent on the specific situation. Despite these constraints, the life cycle of a business relationship provides the foundation for derivation of specific fields of business relationship management (Diller 2005). These fields arise from the central challenges that the supplier faces in the various phases of a cycle.

3.2.2 Dynamic Consideration of the Life Cycle of a Business Relationship

Criticism of the deterministic character of the traditional model of the life cycle of a business relationship can be countered by refraining from the idea of a rigid sequence of the individual phases. So business relationships are characterized by an undecided course. Stauss (2006) to some extent presents a point of view in which he introduces to the stated phases of the life cycle of a business relationship a risk phase that can occur repeatedly at any time. For such a risk to be relevant, the customer must be considering terminating the relationship. So migration prevention management and customer recovery management are recommended as permanent tasks of business relationship management.

There are, however, more resolute approaches to considering the indecision of the course of business relationships; these refrain completely from claiming a phase sequence. These can be seen as a strategy in which there is differentiation only between an in-supplier and an out-supplier situation in a business relationship (Brown 1995). The in-supplier situation is distinguished by a business relationship between the customer and the focal supplier. In the out-supplier situation, the customer maintains a business relationship with one of the supplier's competitors. It was proven empirically that the customer's purchase behavior is decidedly

different in both situations. The in-supplier situation in principle supports the (positive) impact of a company's (good) reputation and/or a (positive) attitude regarding the offer extended by the business relationship partner. The correct term for this is moderator effect. So the in-supplier situation warrants e.g. efforts on the part of the supplier to establish good personal relationships between the sales personnel and the customer's personnel participating in procurement decisions. In the out-supplier situation, on the other hand, the customer tends to be influenced by stereotypes when forming his attitude. There is e.g. the risk that the customer associates the out-supplier's employees with the (usually negative) image of a "typical salesperson," which in turn has a detrimental impact on the attitude towards the out-supplier's offering. So the out-supplier should attempt to distract from such stereotypes.

The results of a study by Eggert et al. (2006) can be interpreted similarly. The object of the study was the way in which the customer's perception of a business partner's contribution to value creation for the customer changes over the course of a business relationship. The results indicate that, at the beginning of business relationships, the value contributed through improvement of procurement processes is usually paramount. Over time this becomes less and less an issue in a business relationship and is replaced by the perception of value-adding contributions in the production process. So it seems apparent that in-supplier marketing should focus on value-adding contributions to production processes, while out-supplier marketing should emphasize value-adding contributions to procurement processes instead.

3.3 Summary

This chapter has dealt with the determinants of purchase behavior in business relationships. It is characterized by repeat purchasing. Indicators of repeat purchasing behavior can be found in the structure of the customer benefit as well as in the structure of the supplier advantage. Regarding the customer benefit, it must be determined whether or not there are any relevant bonding effects. Repeat purchasing behavior without the influence of customer bonding can be attributed to the core service of an offer or to the ancillary services. Customer relationship management is the collective term for approaches that can precipitate repeat purchasing behavior by conscious configuration of ancillary services. Bonding can have economic or psychological roots. Economic commitment can be explained by the effect of specific resources in the customer's possession or by the effect of satisfaction in an environment of uncertainty. Psychological determinants of bonding and thus of repeat purchasing are trust and commitment, whereby the former is an expectation and the latter an intended action. The structure of the supplier advantage helps to explain repeat purchasing behavior when, seen from the perspective of a current purchase decision making situation, not only the past but also the future is taken into consideration. As "shadows of the future," business relationships represent relational contracts and are thus capable of reducing the perceived behavioral uncertainty of the parties to a business relationship. Finally, we expanded the

explanation of repeat purchasing from the consideration of a point in time to the consideration of a time period. The central concept here is the life cycle of a business relationship in its tradition or in a dynamic form.

Appendix

Exercises

1. What are the different levels of an exchange that can be considered the source of repeat purchasing behavior in business relationships? Which repeat purchasing behavior is more resistant to competition?
2. Explain the term “Customer Relationship Management” (CRM) and clarify its effect as an ancillary service on the customer benefit. What are the different dimensions of CRM?
3. Explain how specificity and satisfaction can act as switching barriers in business relationships!
4. Define the term satisfaction. Which factors impact the occurrence of satisfaction in business relationships?
5. What does the confirmation/disconfirmation paradigm imply?
6. Name and explain the central components and correlations of the GAP model according to Zeithaml et al. (1988)!
7. What are the essential differences between repeat purchasing behavior based on satisfaction and specific resources and repeat purchasing behavior based on core and ancillary services?
8. How is trust established in business relationships?
9. Which types of contracts do you know about? What are the main differences between the various types of contracts?
10. Explain the phases that business relationships can go through. What are the characteristics of the phases?
11. Which approaches to dynamic consideration of business relationships do you know?

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Michael Kleinaltenkamp

4.1 Fundamentals of Customer Evaluation

The establishment and cultivation of business relationships often require substantial resources. Every company that practices business relationship management asks itself if these investments are worthwhile, if the effort and expense required are balanced by revenues that are at least as high (Gupta and Lehmann 2005). The latter can be earned by the customer's company itself or just as well—at least partially—by other companies, provided that their purchase decisions are influenced by the behavior of the customer in which the supplier's investment was made. In light of this, the choice and selection of such “important” customers represents a major part of business relationship management.

So it comes as no surprise that a study commissioned by the task force “Development, Design, Sales” of the Verein Deutscher Ingenieure (VDI, Society of German Engineers) indicated that 70 % of those surveyed agreed with the statement that it is of strategic importance to better know the earning rate of the individual customer relationships (Krafft and Albers 1997; Krafft 1999). On the other hand, it is often lamented that customer evaluation is performed only superficially or on the basis of less meaningful criteria, such as customers' sales volume. Practical experience often confirms that the customers with the highest revenues are not exactly those who contribute most to the supplier's success. In many companies, the rule of thumb is that 80 % of sales can be attributed to 20 % of customers. But the 20 % generally do not generate 80 % of the contribution margin or even of the profit. It is often the relationships to the customers generating the most revenue that, upon closer examination, have to be classified as unprofitable (Plinke 1997).

So what determines a customer's value? Which criteria should or can be applied to determine the value of a single customer or a group of customers? The answers to

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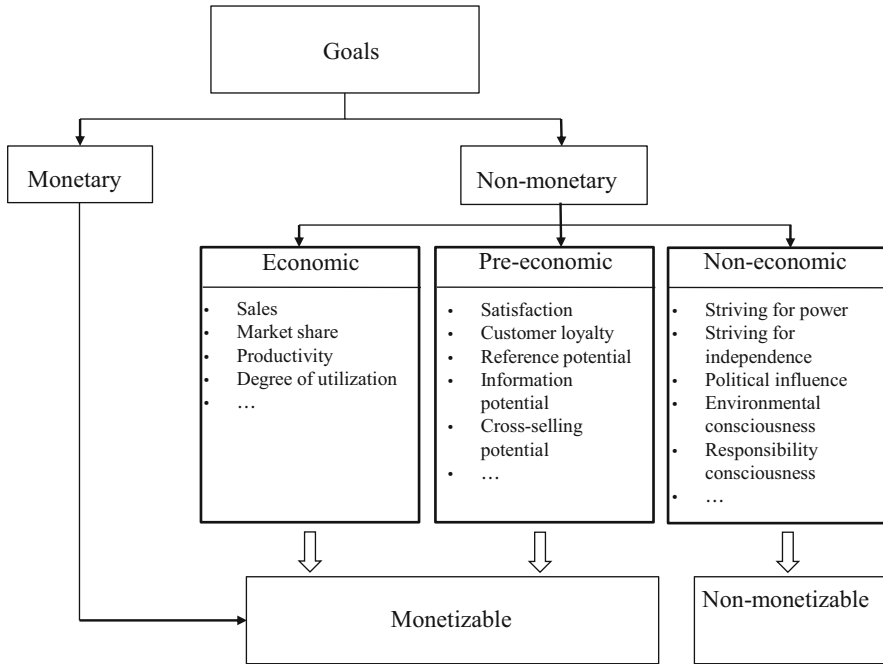


Fig. 4.1 General classification of goals for marketing purposes. Source: Based on Cornelsen (2000)

these questions are ultimately a factor of the goals that a company pursues with the business relationship management activities.

Potential goals are shown in Fig. 4.1—based on Krafft (1999) and Cornelsen (2000). They are classified first by whether the respective goals are of a monetary or non-monetary nature. The non-monetary objectives are further divided into those that can in principle be monetized and those that cannot. The first group includes all economic and pre-economic variables, while non-economic goals such as striving for power or independence can usually not be assigned a monetary value. Depending on the goals of a company's business relationship management activities, the value of an individual customer or a group of customers can be different, so other aspects must be considered or combined to assess the customer's value.

When this view is pursued, the customer value can be generally defined as a gauge of the direct and indirect contributions of a customer towards achieving the supplier's goals. So it represents the economic significance of a customer or group of customers for a supplier company (Cornelsen 2000).

Such a broad definition of the term customer value ultimately encompasses all monetary and non-monetary contributions of a customer that promote the supplier's success. To determine this value, it must be decided which specific criteria should be applied and whether single aspects or combinations of aspects should be

Table 4.1 Classification of customer value concept

Distinguishing criterion	Criteria	
	Object of evaluation	Single customers
Data base	Quantitative	Qualitative
Number of evaluation criteria	One-dimensional	Multi-dimensional
Monetization of evaluation criteria	Monetary	Non-monetary
Time period	Single period/static	Multiple periods/dynamic

Source: Based on Reinecke and Keller (2006)

considered. Table 4.1 offers an overview of various ways in which parameters for determining a customer's value can be differentiated. As the table shows, the value can refer to a single customer or a group of customers. It can be based on quantitative or qualitative data, include monetary or non-monetary aspects, and it can be static (for a single period) or dynamic (for multiple periods). Also, a customer evaluation concept can be sustained by one of these criteria or by several (one-dimensional vs. multi-dimensional).

As the name says, one-dimensional concepts for determining the customer value apply only a single criterion as the evaluation measure. Multi-dimensional models, on the other hand, attempt to better portray the complexity of the various possible contributions a customer can make to the value by integrating different parameters (Eggert 2006). This, however, creates special method-related problems: differently dimensioned values have to be combined to one comprehensive parameter.

The following section will first explain individual dimensions of customer evaluation, then go on to point out approaches that comprise the application of various criteria. Economic-quantitative gages are introduced first, then qualitative factors.

4.2 Criteria for Determining Customer Value

4.2.1 Economic-quantitative Gages of Customer Value

Table 4.2 summarizes the economic-quantitative parameters most important to the business-to-business sector as well as the hypotheses on which they are based in view of their impact on the customer value.

4.2.1.1 Revenue Analysis

The determination of the customer value based on the revenue generated with the customer (revenue analysis) remains the most common analysis method (Sect. 4.2.3). The customer value is calculated simply as the total of all amounts invoiced to a customer over a period—typically one year. When doing this, the customer's share of total revenue for the period is often determined, meaning the share of revenue generated by a customer. The customers are then frequently

Table 4.2 Economic gages of customer relevance

Name	Calculation	Premise
Revenue	Total of the contributions invoiced to the customer per period	The greater the revenue generated by this customer, the greater is the relevance of the customer
Customer's share of revenue	Revenue generated by this customer per period/total company revenue per period	The greater the share of revenue generated by this customer, the greater is his relevance for the supplier
Supplier's share of deliveries	Revenue generated by this customer per period/customer's total purchases in a product category	The greater the share of deliveries, the greater is the relevance of the supplier for the customer. These can provide indicators for possible ways to influence the customer
Contribution margin	Total revenue per period/total direct costs per period of all product-related costs, order-related costs and costs related directly to the customer	The greater the contribution margin, the greater are the resources that this customer provides to cover costs that this customer produces, and the greater is the relevance of this customer
Customer's share of contribution margin	Customer's contribution margin per period/total contribution margin per period	The greater the share of the contribution margin, the greater is the customer's relevance
Customer's contribution margin position (importance)	Customer's contribution margin per period/total contribution margin per period	The better the contribution margin position, the (relatively) greater is the relevance of the customer
Cash flow	Revenue inflow from this customer per period/revenue outflow for this customer per period	In the event of objectives geared towards liquidity: the greater the cash flow, the greater is the relevance of the customer
Customer's share of cash flow	Customer's cash flow per period/total cash flow per period	The greater the share of the cash flow, the greater is the customer's relevance
Capacity utilization	Quantity supplied per period/total capacity per period	The greater and more consistent the capacity utilization, the greater is the customer's relevance for setting objectives related to production planning with cost optimization

Source: Based on Plinke (1997)

classified as A, B or C customers based on these values. Figure 4.2 illustrates the results of such a so-called ABC analysis.

The x-axis of a coordinate system indicates the cumulative number of customers, and the y-axis shows the cumulative share of revenue generated by the respective customers. In the sample case depicted in Fig. 4.2, 85 % of the revenue is generated by 20 % of the customers. In this sense they represent the best customers—the A customers. The next 25 % of the customers generates another 10 % of revenue.

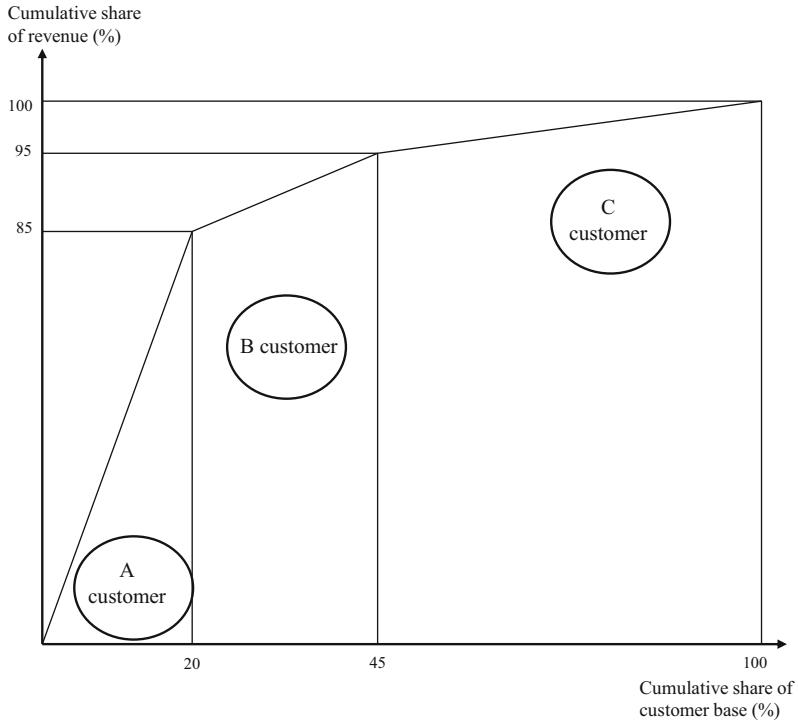


Fig. 4.2 Typical distribution of a company’s revenue amongst A, B and C customers

They are classified as B customers. The remaining 5 % of revenue comes from 65 % of the customers. These are the company’s C customers.

When the curve resulting from this type of analysis moves farther to the left, it means that the share of revenue generated by one or a few A customers is increasing. This means that when the customer or customers terminate the business relationship, the subsequent decline in the supplier’s revenue cannot be easily offset.

The fact that this method is common in business practice is due primarily to the ease with which the method can be applied as well as to the relative simplicity of procuring information (Cornelsen 2000). All of the information required can normally be obtained without much effort from the company’s accounting department. However, it should be kept in mind that, when analyzing revenue—just as with other criteria mentioned here (Table 4.2)—usually only individual periods are examined. Random events like overdue payments, invoicing of single large orders or seasonal fluctuations can have a critical effect on the analysis. Also, the degree of a business relationship’s maturity is not taken into consideration, so companies are evaluated in the same manner, regardless of the different maturity phases (Cornelsen 2000). The customer’s use of resources is also not considered when only the revenue is analyzed. So looking at only the revenue to evaluate a customer

does not seem adequate: the high revenue generated by a customer may sometimes be “expensive”—meaning that excessive costs for this specific customer were incurred.

4.2.1.2 Calculation of Customer Contribution Margin

One way to overcome the stated deficits of customer evaluation based solely on revenue is the calculation of the customer contribution margin. This method deducts the costs incurred by the customer, meaning the direct costs of the specific customer relationship, from the revenue generated by business with that customer (Rese 2006). The basic structure of such a calculation of customer contribution margin is shown in Fig. 4.3.

To be able to calculate the contribution margin in this way, it is essential that the data is organized properly. The relevant costs and revenue must be able to be clearly attributed to the individual customer (Köhler 2008). This is generally not a problem for the revenue. With proper accounting practices, the revenue generated by each customer is clear or can be easily discerned. The costs that can be attributed to individual customers are more difficult to allocate though. The reason for this is that particularly costs incurred for customer service—like those deducted from contribution margin II in Fig. 4.3—are in many cases posted as sales and administrative expenses. The result is that, in regard to the respective customer relationship, they are treated not as direct but as overhead costs.

	Gross customer revenue per period	
-		Decrease in revenue
=		Net customer revenue per period
-		Costs of products purchased by customer (variable piece costs according to product calculation, multiplied by purchase quantities)
=		Customer contribution margin I
-		Order costs directly attributed to customer (e.g. devices, shipping costs)
=		Customer contribution margin II
-		Visit costs directly attributed to customer (e.g. costs incurred to travel to customer)
-		Other customer related direct costs per period (e.g. salary of responsible key account manager; engineering aids; costs of mailings; interest on accounts receivable; for customers at the level of trade: Advertising cost subsidies, listing fees and similar payments)
=		Customer contribution margin III

Fig. 4.3 Basic structure of calculation of customer contribution margin. Source: Based on Köhler (2008)

This is not detrimental to the calculation of customer value, as long as there are no vast differences between customers and the amounts to be considered are not noteworthy. But if this is the case, such a calculation will lead to distortion of the customer contribution margins, because the customer relationships that incur (significantly) higher costs than the other appear in a more positive light, while all of the others appear more negative than they are.

The question arises whether in such cases the respective customer-specific costs, instead of being recorded as overhead, should be considered direct costs and billed to the customer. These are essentially “quasi overhead”, meaning customer-related direct costs treated as overhead for the company’s accounting purposes. They could actually be assigned to their source—in this case, individual customers. This is not done though, because the effort required to separately compile and allocate them tends to be avoided. As in all such cases, this decision should generally be made by weighing the costs and benefits. So the (potential) benefit of compiling the costs of a business relationship is opposed by the additional costs incurred for their separate recording and allocation (Rese 2006). Since it is particularly difficult to measure the stated benefit effect beforehand, a pragmatic way to solve this problem is to make random evaluations. If it turns out that there are great differences in the assessments of the individual customer relationships as compared to the results based on the allocation of overhead, converting to another method should be seriously considered. If this is not the case, the less precise but exact enough values can continue to be used.

A similar problem arises with economies of scope on the revenue side with calculation of the cost margin. They can exist on the one hand for a certain time period for the same customer relationship (1.) and on the other hand for a certain point in time in regard to relationships with several different customers (2.) (Engelhardt 1976).

1. In this case, calculation of the customer contribution margin typically considers the past and then only a single period thereof. It happens again and again in a period that a transaction with the customer in the course of a so-called “strategic project” occurs at conditions which are particularly beneficial to the customer. The intention is that the customer will become loyal to the supplier and the consequence will be additional business that will at least offset the expenses of the original transaction. When this is the case, the contribution margin of the respective order and thus the contribution margin for the period for this customer, which includes all of the project contribution margins of the respective period, is reduced. But the future revenue induced by the very favorable conditions are not recorded in the respective period, with the consequence that the respective customer contribution margin is actually calculated as too low. Conversely, the future customer contribution margins for the customer and period are assessed too high, because they are at least partially the result of diminished revenue granted the customer. So as long as planned contribution margins are not used for calculation purposes, the respective economies of scope are completely disregarded. However, it would be preferable to consider them in

regard to the goals and intentions of business relationship management, because in addition to the evaluation of earlier procedures, it is also and not least about planning and control of business relationship management future activities relating to individual customers.

2. When the relevant revenue is calculated, only the amounts invoiced to the customer are considered. For example, revenue resulting from the respective customer having made a recommendation to another customer is not included in the calculation, although it can be attributed to the respective customer. This presents a problem analog to recording the direct costs attributed to an individual customer relationship. The revenue treated as individual revenue is actually “overhead” revenue because it can be attributed to a common source: the behavior of a certain customer. Allocating them to multiple customer relationships is fundamentally a correct allocation to the source, so the order and customer contribution margins calculated this way at least partially reflect an incorrect image.

The problems described here can be solved with the implementation of a so-called pool calculation—which is not often applied in actual practice. With this method, the portion of the reduction in the contribution margin accepted in anticipation of future revenue with the same customer (case 1) or in anticipation of additional revenue with other customers (case 2) does not flow into the calculation of the customer contribution margin but is posted in a separate pool. This negative value represents the investment in the respective customer relationships (case 1) or in the relationships with other customers (case 2). Whether or not this was worthwhile should be apparent when the hoped for additional revenue is generated either by the same customer or by the other customers. But since at least part of the revenue can be attributed to the revenue reductions previously accepted to gain the business, part of the contribution margins achieved with the respective orders should not be assigned to the margins but be offset against the original investment, which was allocated to the pool. Practically speaking, this would mean that some of the order contribution margin would be credited to the respective pool—such as a certain percentage of the contribution margin over a certain time span. If the value that was originally negative would be at least offset by the contribution margin, it would be an indication that the investment was worthwhile and the company was correct in its assessment of the customer behavior. If this were not the case, it would be a clear signal that the respective presumptions and expectations were wrong; these findings could be used later.

However precisely a customer contribution is calculated, it can be used for an interesting analysis of the value of customer relationships when the revenue and the contribution margin of each customer are plotted on a two-dimensional graph. Figure 4.4 shows an example of this. To be able to reach further conclusions, the average revenue of all customers as well as the respective average contribution margin must be calculated. If lines are drawn at a 90° angle from both the x-axis and

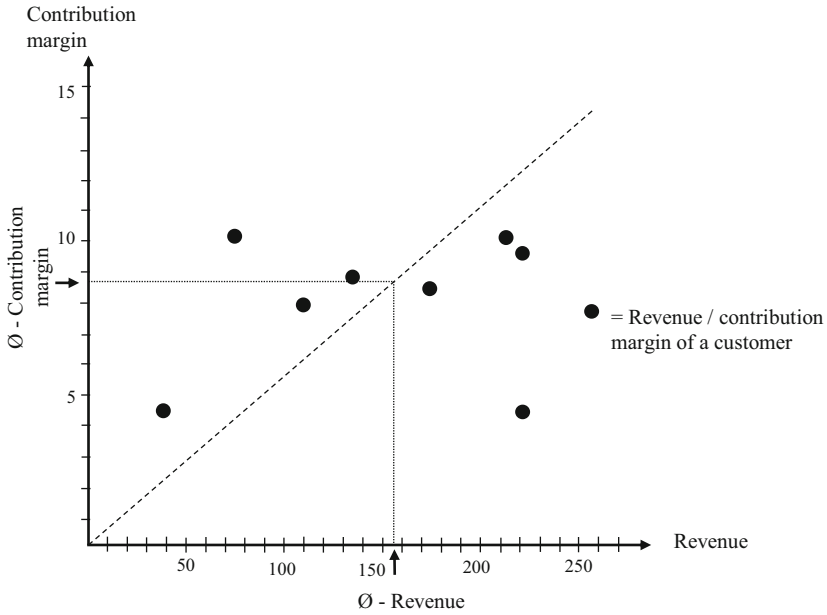


Fig. 4.4 Combined revenue/contribution margin analysis. Source: Based on Plinke (1997)

the y-axis, the intersection of the two lines is the point at which a customer would be plotted were the average revenue and the average contribution margin achieved. The line running from the zero point through this point thus represents all points at which precisely the average contribution margin is achieved when the respective revenues are met per revenue unit. All of the customers represented by the points below the lines are considered “bad” customers in this regard, because their contribution margins achieved per revenue unit are below average. It is the exact opposite for the points above the lines.

Interesting insights and questions arise from such an analysis: Why are the respective values so good for some customers and so bad for others? Do the “bad customers” primarily buy products with low product contribution margins? Do they always manage to get prices that are good for them? Is the cost of taking care of them higher than that of taking care of other customers? Which measures can be developed to improve the relevant values? etc.

4.2.1.3 Customer Lifetime Value

An approach that can solve at least some of the problems caused by applying the customer contribution margin is the use of the **Customer Lifetime Value (CLV)**. The basic idea is to look at a business relationship as an investment, which can then be accordingly evaluated with investment analysis methods. The CLV essentially expresses nothing more than the total of all (discounted) payments received and

payments made over the lifetime of the business relationship (*cash flows*) (Berger and Nasr 1998). The CLV can be determined in three different ways:

The CLV approach is generally a calculation method that applies the principles of dynamic investment analysis to customer relationships. There are two fundamental calculation methods: calculation of the potential CLV and calculation of the present CLV. The only difference between the two methods is the reference time.

1. To calculate the **potential (customer lifetime) value** the cash flows are added together without any modifications, e.g. undiscounted. The basic structure of the process is the same as that of the calculation of the customer contribution margin. The customer value determined in this way indicates the potential profit that can be made with a customer over the course of the period examined.
2. The **present (customer lifetime) value** is determined applying the principles of dynamic investment appraisal, which assumes that future payments are worth less than present payments. So future payments are discounted at a certain interest rate. The result of such a calculation is the net present value of all—considered—cash flows of a business relationship with a customer. The present value represents the CLV in its own sense and is the most common calculation method.
3. Finally, a **retention rate** can be included in the CLV. It indicates the probability that can be anticipated with the relevant future payments during the period in question. It can basically be any value between 0 (=termination of relationship) and 1 (=secure continuation of relationship). So the resulting **customer lifetime value with the retention rate** is the expected value of the future payments made and payments received in a business relationship.

The equation in Fig. 4.5 shows how to calculate the CLV in its own sense, meaning the net present value of a business relationship.

Specific determination of the CLV is generally faced with the following challenges:

$$NPV = \sum_{t=0}^n \frac{e_t - a_t}{(1+i)^t} = e_0 - a_0 + \frac{e_1 - a_1}{(1+i)} + \frac{e_2 - a_2}{(1+i)^2} + \dots + \frac{e_n - a_n}{(1+i)^n}$$

e_t = (Anticipated) payments into the business relationship in period t

a_t = (Anticipated) payments out of the business relationship in period t

i = Discount rate for discounting to a uniform reference time

t ... = Period ($t = 0, 1, 2, \dots, n$)

n = Duration of business relationship

Fig. 4.5 Calculation of net present value of a business relationship. Source: Based on Helm and Günter (2006)

1. First the relevant cash flows must be attributed causally to the customer, following the procedure for determining the customer contribution margin. In practice, problems with the implementation can occur because not all items can be precisely assigned. So often only the customer's direct amounts flow into the calculation (Rudolf-Sipötz 2001).
2. The second challenge is that the time frame for the examination must be specified, meaning how many periods flow into the calculation. One way to do this is to use the average duration of a company's business relationships (Helm and Günter 2006). But this can be a problem when the relationships extend over many years—which is not unusual. Then very high values would have to be included in the examination, with the consequence that payments made and payments received far into the future would also have to be considered. But since it gets more and more difficult to estimate such amounts the farther away they are, the validity of the examination would suffer.

Another method is to use as the consideration period the duration that the company typically uses as a planning horizon for strategic decisions. It is different in each branch or company, but three, five and ten years are common. In this way the evaluation and the management of business relationships would be synchronized with the company's strategic planning.

3. The third challenge is that an interest rate at which the cash flows are discounted must be determined. Different procedures can be chosen for this purpose. An approach pursuant to the objectives of business relationship management is to take the rate for the average cost of capital incurred by a company (*Weighted Average Cost of Capital [WACC]*). These are the costs that the company has for financing its activities with its own as well as borrowed capital (Kruschwitz 2000). Sometimes payments into the pension reserves are also taken into consideration; they can also be seen as costs incurred for business operation. So when a customer's CLV is exactly zero, the amount generated is precisely the amount needed to satisfy the claims of all of the company's investors resulting from financing of the respective customer activities. This means that customers with a negative CLV are those who reduce the company's value because the business performed with them does not cover the capital costs incurred for the transactions. Customers whose CLV is positive, on the other hand, contribute so much to a company's revenue that they generate an amount over and above that needed to cover capital costs. In this sense, they increase the company's value and can be considered "really" good customers.

Table 4.3 shows how the CLV is calculated, using as an example a company in the automation sector.

As in the example in Table 4.3, the CLV is typically calculated for a single business relationship. If this is not possible or is too complex due to the data availability situation, the value can be determined at the level of customer groups or segments (Kunschert 2009). Homburg and Daum (1997) recommend using the CLV as a negotiation tool for major customers. As the example shows, a negative

Table 4.3 Calculation of CLV with an automation company as an example

	1st year	2nd year	3rd year	4th year	5th year	Total
Gross revenue	2.0 mn	1.9 mn	1.8 mn	1.7 mn	1.6 mn	9 mn
Associated revenue	10,000	10,000	10,000	10,000	10,000	50,000
Manufacturing costs	1.6 mn	1,350,000	1,260,000	1,160,000	1,040,000	6,370,000
Sales costs	150,000	154,000	150,000	140,000	130,000	724,000
Sales support costs (logistics, etc.)	360,000	370,000	380,000	390,000	400,000	1,900,000
Surplus revenue per year	-100,000	36,000	20,000	20,000	40,000	16,000
Discounted surplus revenue (10 %)	-100,000	32,727	16,529	15,026	27,321	CLV = -8,397

Source: Based on Kunschert (2009)

CLV can serve as leverage to negotiate better conditions (Homburg and Daum 1997).

Case Study

A corporation in the automation sector is faced with the decision of accepting a framework agreement with a term of five years. The agreement guarantees an annual revenue, with the amount for the first year being 2 million euros. A price reduction of 100,000 euros is set for each subsequent year. A service contract is also to be signed, guaranteeing an annual income of 10,000 euros. To be able to assess the attractiveness of this framework agreement, the company is now estimating the manufacturing, sales and sales support costs that will be incurred. A discount rate of 10 % is set. The calculation of the Customer Lifetime Value in Table 4.3 on the basis of this example shows that, despite the positive cumulative surplus revenue, the CLV is negative (Kunschert 2009).

4.2.2 Non-monetary Gages of Customer Value

As previously mentioned, a customer's value to corporate practice consists rarely of only monetary values or those that can be monetized. Non-monetary or qualitative parameters can often be significant. These are more difficult to record and cannot be assessed as precisely. Such criteria are imposed and used along with quantitative parameters or in place of such parameters if there are no quantitative criteria available, or when it does seem sensible to impose them (Rieker 1995).

Qualitative criteria used to determine a customer's value can always be based on many different properties and behaviors of customers (Anderson et al. 1993; Ford and McDowell 1999; Wilson and Jantrania 1996). In principle, any of the customer's contributions to the supplier's goals related to the market or to customers can be taken into consideration (Fig. 4.1). So first the challenge is to select the properties that are relevant to the supplier company. There should be knowledge or at least conjecture on the correlation of the relevant variables to a customer's value. And because of the qualitative nature, one must be aware that the assessment of the relevant criteria is often necessarily subject to strong subjective factors (Günter 2006).

The non-monetary criteria most important to the business-to-business sector will be outlined in the following section. Approaches such as how these non-monetary properties can be combined with the mentioned economic-quantitative parameters in the course of multi-dimensional customer value analyses will then be described in Sect. 4.2.3.

All of the procedures described are basically analyses of potential. As the term implies, they examine anticipated values, not realized values. So customers who perform above average do not necessarily effect direct growth for the supplier

company (Cornelsen 2000). This is not the case until the respective potential has actually been tapped.

- Determination of the **potential for innovation** includes analysis of the capabilities that the customer has to promote the supplier's innovations (Rieker 1995). This is particularly of value to the supplier when it serves to reveal customer needs simmering in the market but for which no marketable solution exists. So-called "lead users" are particularly useful to the supplier for this purpose. They are characterized by having the need for a new solution much earlier than other purchasers and by being able to recognize and render the need more precisely (Rieker 1995). The potential for innovation of such a customer firm can also be an indication of whether it is inclined to adopt the supplier's innovations, thus serving as a reference for other customers.
- The **reference potential** or the **reference value** of a customer is determined by the "*number of potential customers that an existing customer can reach within a certain time based on recommendations and influence as well frequency and intensity of contact and the extent of his social relationship networks*" (Tomczak and Rudolf-Sipötz 2006, p. 135). In principle, a customer can pass along positive, neutral or even negative information on a supplier or the products and services offered. In the business-to-business sector, the reference value of a customer is often of such great interest because the services offered—due to the individual nature for a specific customer—do not yet exist at the time the order is placed and are thus difficult to evaluate. The uncertainties that this evokes can then be reduced by positive statements made by experienced customers. The more a customer supports a supplier in the acquisition of new customers or in the introduction of new products and services, the greater is his value to the supplier.
- An analysis of the **development potential** is to be used to determine the ways in which a customer firm can assert and develop itself in its markets in the future (Mach 1993). Many different factors of the customer company can play a role in this process. These factors include the competence of its management, production equipment and plants, the development potential of the business segments, the quality of marketing strategies as well as of the products offered by the customer company, the development of the its markets as well as of its own sales or business practices (Mach 1993; Rieker 1995).
- The purpose of an analysis of the **potential for cooperation** is to discover the extent to which a customer is willing to enter into joint activities with the supplier. The goal is to achieve synergies that e.g. arise from joint sales or research and development activities. From the supplier's point of view, this is appealing not least because such a cooperation can promote a customer's loyalty to the supplier (Rieker 1995).

These analyses can provide interesting findings on the value of individual customer relationships. However, it should be noted that, in the actual implementation of the stated methods for compiling quality properties of customer value, the

relevant criteria are not recorded or monitored in most of the controlling systems used by supplier companies (Gelbrich and Müller 2006). So actual performance of the analyses is often tedious and related to single cases, reducing the significance and applicability of the results.

4.2.3 Multi-dimensional Approaches to Determining Customer Value

4.2.3.1 Scoring Models

Scoring-based analyses of customer value normally combine qualitative and quantitative elements. Scoring processes are basically models of a relatively simple mathematic structure that can be differentiated in many ways and can be adapted to different purposes—in this case, the evaluation of customers.

This is the typical procedure for creating a scoring model to evaluate customers (Table 4.4):

- First a list of all criteria relevant to customer evaluation must be compiled (column 1).
- The second step is to weight the criteria by their significance (column 2), whereby the sum of the individual weights is one or 100 %.
- Then each customer is evaluated in regard to each criterion and assigned a score (columns 3–6, left). Different scales can be used for the evaluation (the value range is 1–5 in the example). The higher the assigned score, the stronger is the criterion for the specific customer. Inverse scales can also be used. For example, a higher score for customer care expenditure is equivalent to lower expenditure for customer care.
- All of the scores are then multiplied by the corresponding weighting factor (column 3–6, right).
- Finally, the weighted scores are added up to produce the total score of the customer (total lines in columns 3–13). It represents the customer value determined in this sense.

Which factors are considered important, how many criteria are applied and how they are weighted is always open. It can and should be discussed by the supplier company using this process. Comparing different opinions on the individual aspects as well as bringing about a consensus on this topic offer good opportunities to share knowledge about individual customers that already exists within the company as well as knowledge on awareness of what is considered important or not. This allows information on individual customers or groups of customers to be improved and enhanced.

One should nonetheless be aware of the strengths, weaknesses and limits of scoring models. First of all, scoring models depend greatly on subjective assessments. This applies to the weighting factors as well as to the scores. Another limitation or assumption when calculating customer values with the scoring process

Table 4.4 Example of a scoring model for customer evaluation

(1)	(2)	(3)		(4)		(5)		(6)	
		Customer ID							
		40,592		40,070		40,033		40,237	
Evaluation criteria	Weighting factor	Points	wtd.	Points	wtd.	Points	wtd.	Points	wtd.
1. Revenue									
Rank accdg. to ABC analysis	0.200	3	0.60	3	0.60	3	0.60	3	0.60
Revenue development	0.050	4	0.20	4	0.20	2	0.10	3	0.15
2. Sales processing									
Order regularity	0.010	4	0.04	4	0.04	3	0.03	2	0.02
Share of revenue by order	0.030	4	0.12	3	0.09	1	0.03	1	0.03
Payment morale	0.050	4	0.20	5	0.25	5	0.25	3	0.15
Support expenditure sales reps	0.045	1	0.05	3	0.14	3	0.14	3	0.14
Support expenditure office	0.045	2	0.09	2	0.09	3	0.14	3	0.14
3. Influence on employment									
Product group 1	0.060	3	0.18	1	0.06	3	0.18	3	0.18
Product group 2	0.010	1	0.01	1	0.01	1	0.01	1	0.01
Product group 3	0.030	3	0.09	3	0.09	3	0.09	4	0.12
Product group 4	0.050	3	0.15	4	0.20	3	0.15	1	0.05
4. Customer development									
Market position	0.050	5	0.25	4	0.20	5	0.25	5	0.25
Market development	0.050	5	0.25	4	0.20	4	0.20	5	0.25
Customer growth	0.050	5	0.25	3	0.15	3	0.15	2	0.10
5. Competition factors									
Relative competitive position	0.025	3	0.08	3	0.08	3	0.08	3	0.08
Relative share of deliveries	0.025	4	0.10	4	0.10	4	0.10	4	0.10
Switching barriers	0.050	4	0.20	3	0.15	2	0.10	3	0.15

6. General criteria

Customer's potential for cooperation	0.030	5	0.15	3	0.09	3	0.09	3	0.09	3	0.09
Reference potential	0.100	3	0.30	3	0.30	3	0.30	3	0.30	4	0.40
Strain on manufacturing due to special deadlines	0.040	1	0.04	3	0.12	3	0.12	3	0.12	3	0.12
Total	1.00		3.34		3.15		3.10		3.10		3.12

Source: Based on Plinke (1997)

is that adding up the weighted scores implies that the evaluation criteria are independent. In reality, this is generally not the case though. The individual properties actually correlate with one another, meaning that they are not independent of one another in their manifestation. So a customer who requires intensive care is generally the source of high care expenditure for the sales reps as well as for the office. In such a case a high value in one of the two categories always means a similarly high value in the other category. Because both values are used, the expenditure for customer care is allocated twice to some extent. This then leads to some distortions, such as overestimating or underestimating certain criteria applied to calculate customer values.

As long as one is aware of their limitations, scoring processes can be considered very flexible and simple-to-use instruments for the evaluation of customers. Particularly when used regularly—about once a year—they can reveal interesting insight into the status and development of business relationships with individual customers.

4.2.3.2 Customer Portfolios

Like the scoring models, customer portfolios are also a form of customer value analysis in which multiple criteria can be considered for the evaluation at the same time. The distinctive feature of customer portfolio analysis is less the determination of the values that flow into it than the way in which the results are displayed. Also, recommendations can be derived relatively simply from the positions of individual customers within the portfolio; these recommendations offer at least an initial starting point for designing customer-based strategies. Because of the easy traceability and the fact that the respective circumstances are clearly shown, customer portfolios have come to enjoy wide acceptance, despite the fact that they contain no unequivocally quantifiable results.

Ultimately, the goal of customer portfolio analysis is less the assessment of individual customers and more an optimal composition of the customer base. It is more an examination of the structure—including and especially for large quantities of customers (Dubinsky and Ingram 1984; Fiocca 1982; Johnson and Selnes 2004). Nevertheless, customer portfolio analysis is also used to evaluate individual customers in the business-to-business sector, especially because the number of customers is easily manageable in this field, which in turn enables them to be assigned to a portfolio (Cornelsen 2000). Several customers can nonetheless be combined to customer segments and then evaluated together.

The structure of customer portfolios is the same as that of business portfolios. Both types of analysis are based on the fundamental concept of portfolio theory by Markowitz (1952), whereby financial assets should be evaluated looking at two dimensions: their anticipated return and the associated risk. The individual customers and the business relationships established with them are viewed in this sense as investments, which are evaluated in regard to their future intrinsic value. On the one hand, criteria are applied that typically—*analog to the return on an investment*—serve as an indication of the future attractiveness of the customers. On the other hand, the position of one's own company in the eyes of the customer is compared to the position of one or more major competitors as seen by the same

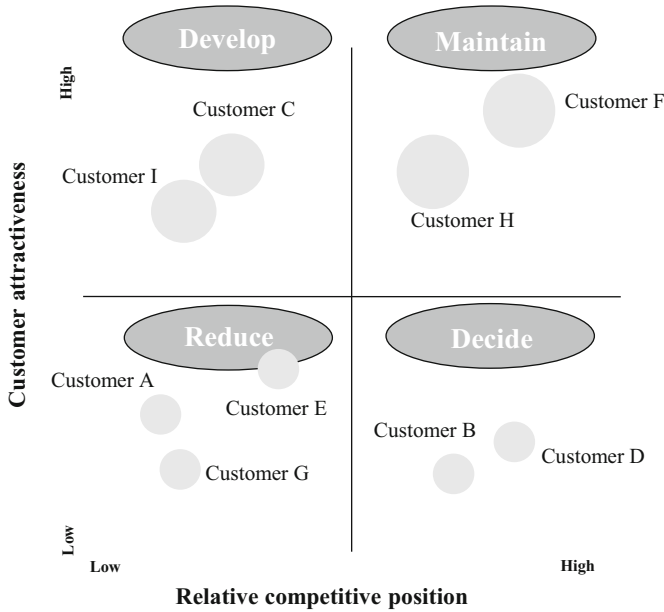


Fig. 4.6 Customer attractiveness/relative supplier position portfolio

customers. This relative competitive position reflects to some extent the risks associated with the respective business relationship: If one’s own position is relatively strong, the earnings in the respective business relationship can probably be realized more easily than when one’s position is weaker. But as with the scoring process, there are ultimately no fixed guidelines regarding the criteria and dimensions to be applied. The choice thereof is a factor of the specific situation, the goal of the analysis and the relevant technical requirements for data acquisition and analysis.

Figure 4.6 shows an example of a customer attractiveness/relative supplier position portfolio. The customer attractiveness, plotted along the vertical axis, can be measured by factors such as revenue, contribution margin, anticipated growth of customer, price elasticity, cross-selling potential, entry barriers, customers’ reputation, stability of business, etc. Parameters such as the relative share of wallet, cost and location advantages, financial power or product advantages, etc. as compared to the major competitor(s) can flow into the evaluation of the relative competitive position. The individual total values (scores) are typically determined using scoring models (previous section).

When performing the evaluation, it is important—similar to application of the scoring process—to ensure that the dimensions are independent, preventing systematic distortion and thus double evaluations of individual criteria. To avoid this risk, Kuhlmann (2001) recommends that one of the dimensions should include internal criteria and the other external criteria. Internal criteria means those that the

supplier can influence, like the relative share of deliveries. External criteria refers to values upon which the supplier company has no influence, e.g. the growth rate of the customer market.

The customers are plotted as a circle in the matrix according to their respective evaluations, whereby the size of the circle represents the revenue currently generated by the customer.

As Fig. 4.6 shows, the four quadrants of the matrix can also be assigned standard strategies for the constellation of business relationship management. Customers who are highly attractive and whose companies enjoy a strong competitive position should continue to be developed. Customers who are particularly attractive but with whom the supplier company has a weaker position than the competitors should at least be retained. Relationships to customers who are not particularly attractive and with whom one's own standing as a supplier is weaker should be reduced or perhaps even completely relinquished. And with customers who assign a high position to the supplier but who are otherwise not particularly attractive, a decision should be made as to how the business relationship should evolve in the future. If their attractiveness can be increased in the future—in whichever way—the relationships with them should be cultivated or even intensified. If not, it makes sense to decrease the business relationship activities or to even give up the relationship.

Deriving from standard strategies in such a way on the basis of a customer's position in a portfolio should definitely be viewed critically (Cornelsen 2000). A customer portfolio is initially a static model that reflects the assessment of business models at a certain point in time. This poses a certain contradiction to the dynamic character of business relationships, and there is a risk that the significance of the customers will be evaluated incorrectly over the course of time. Also, the analysis normally includes only the current customer base, not taking into consideration the need to acquire new customers. Because of the undifferentiated approach and the weak theoretic reasoning, Kunschert (2009) and Plinke (1997) categorically dismiss deriving such recommendations solely on the basis of a portfolio analysis. They suggest using customer portfolios only for purposes of analysis (Plinke 1997). All the same, the standard strategies outlined here provide at least initial indications of how relationships to individual customers should be designed (Kunschert 2009). Basing a business relationship strategy solely on such an evaluation would, however, surely be very risky and inexpedient because of the inherent reduction in information.

4.2.4 Practical Application of Different Customer Evaluation Methods

In a study conducted in early 2000, Tomczak and Rudolf-Sipötz (2006) analyzed which of the customer evaluation methods introduced here are actually used in corporate practice. It was apparent that companies still use the "traditional," easy to implement methods most frequently. Despite the stated deficiencies in the method, ABC analysis based on revenue is still the dominant choice. A welcomed

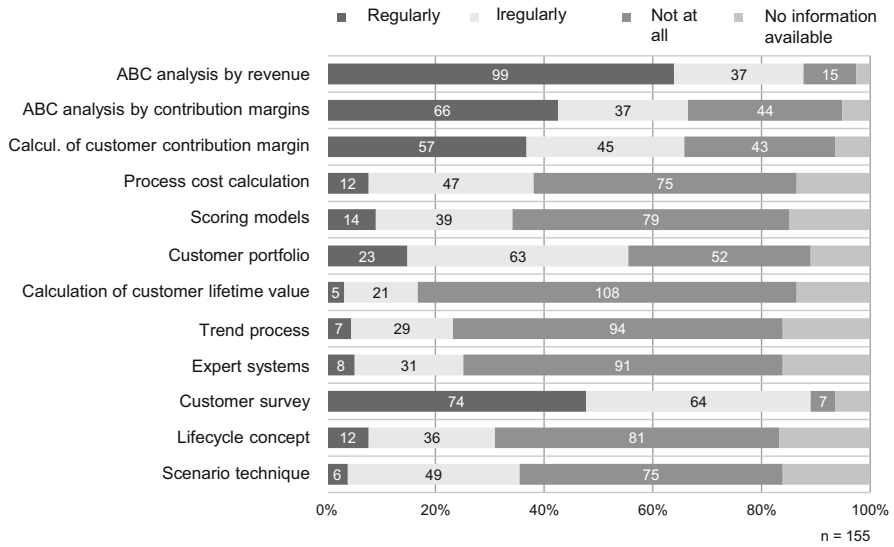


Fig. 4.7 Frequency of use of customer evaluation methods. Source: Based on Tomczak and Rudolf-Sipötz (2006)

development is that the use of the calculation of the customer contribution margin or of ABC analysis based on customer contribution margins has become much more widespread. Figure 4.7 shows in detail how frequently the individual evaluation methods are used.

4.3 Customer Value Controlling

When business relationship management activities are viewed as investments intended to effect return flows of at least the same amount through business with the customers, examining only random points of the customer value—such as at the beginning of the customer relationship—does not seem to make sense. To be able to meet the goals of business relationship management, it is rather essential to examine the long-term development of customer values and to continuously monitor the extent to which identified potential for success is actually achieved. Customer value controlling in this sense should include activities that plan, control and monitor customers’ potential for success (Reinecke and Keller 2006). This comprises the following tasks (Table 4.5):

- The purpose of **planning** is to identify customer potential, in order to be able to select those customers that appear to be the most profitable for the company over the long term and to prioritize customers in regard to the treatment with which to provide them. If this process reveals unprofitable customers or groups of customers, the business relationships can be terminated (Sect. 5.4). Alternately,

Table 4.5 Planning, control and monitoring of customer's potential for success

Phase	Procedure	Goal
Planning	Prioritization of customers	Identification of customer potential
Control	Resource allocation in regard to customer value	Maximizing customer potential
Monitoring	Comparison of anticipated customer values	Effectiveness of potential maximization

Source: Based on Reinecke and Keller (2006)

additional investments in the business relationship can be considered, with the goal of once again making these customers profitable partners for the supplier.

- **Control** is intended to implement measures that realize the identified customer potential. A company's resources available for purposes of business relationship management are applied as best suited to the determined customer value, whereby the attractive customers or groups of customers should of course be the main focus.
- Finally, **monitoring** looks at the extent to which the aspired for customer potential was actually effectively utilized by the company. It is essential to continuously compare the customer values to the company's goals and to react to different situations as needed. Changes can be attributed to external causes, e.g. to different competitive conditions on customer markets or recent technological innovations. Internal causes can be the result of improved customer relationships or better internal opportunities to maximize customer potential (Reinecke and Keller 2006).

Although the fundamental challenges and tasks of comprehensive controlling of customer value are known, it is seldom actually practiced. The reason for this is that the controlling systems and procedures are still strongly oriented on the conditions and requirements of internal accounting. On the other hand, gages and procedures related to the customer and to the market are only rarely examined or implemented. In the sense of customer- and market-oriented corporate management, many companies have an enormous potential for improvement for which the previously described criteria and methods can be used.

Appendix

Exercises

1. State criteria that can be applied to determine customer value!
2. Explain the concept of revenue analysis and the classification of the customer base in A, B and C customers. Why does using the revenue analysis not seem sufficient? What should be taken into consideration with revenue analysis?

3. Explain the structure of calculation of the customer contribution margin. What can be problematic when compiling customer-specific costs?
4. What is the problem with calculation of the contribution margin when there are economies of scope on the revenue side?
5. Explain the concept of “pool calculation.” What are the advantages of “pool calculation”?
6. In which ways can the Customer Lifetime Value (CLV) be determined? How do they differ from one another?
7. Describe typical challenges faced when determining the CLV!
8. What are non-monetary parameters of customer value? Which manifestations of analysis of potential are there, and how do they differ from one another?
9. Describe the procedure for scoring-based customer analyses. What are the disadvantages of scoring-based customer analyses?
10. What is the difference between customer portfolios and scoring models? Explain the structure of a customer portfolio by giving an example. How can the independence of the dimensions be ensured?
11. What does customer value controlling mean, and into which phases is the customer’s potential for success divided?

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5.1 Strategic Tasks of Business Relationship Management

The conclusion of the second part of our book deals with strategies used in business relationship management. Based on a clear understanding of customer behavior—which in business relationships is primarily repurchase behavior (Chap. 3)—as well as of customer evaluation and selection (Chap. 4), this chapter will discuss the general thrust of business dealings within business relationship management. As we will see, the time-related as well as the competition-related embeddedness of a business relationship play a crucial role.

5.1.1 Strategy in Business Relationship Management as a Task Between Competitive and Marketing Strategy

So far, we have become familiar with business relationship management as a special type of supplier-customer interaction in the marketplace. The previous two chapters were dedicated to intensive analysis of repurchase behavior and customer evaluation. This chapter will deal with the implementation of business relationship management. This could lead the reader to believe that business relationship management is primarily an operative management task geared towards applying a certain range of marketing activities. The extent to which the operative component of business relationship management has to be accompanied by a strategic perspective is the subject of this chapter.

But what is a strategic perspective? What distinguishes strategic decisions? According to (Plinke 2002), they are “*economic decisions that bear the distinction of being particularly significant to a company in regard to both time and content*”

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(p. 7). They impact the company's future development and competitiveness. The following three examples clearly point out the extent to which this applies to decisions made in the course of business relationship management:

Example 1

Company A is a first tier supplier in the automotive industry. The company's few direct customers are automobile manufacturers, so-called OEMs (original equipment manufacturer who regularly develop new series and then produce them for several years. It is common practice to first install technological innovations in the higher-quality series, e.g. Mercedes Benz S class or BMW 7 series. When designing a new series, an OEM often announces a competition for the new concept, with the goal of choosing one or two suppliers for certain vehicle models or systems. If A has thus far not been a customer of the OEM C, a successful bid in the competition to supply the respective system could mean entry into a business relationship with C. Then A's production is not only ensured of a base load over years, the company also has an important reference with which to attract other OEMs. With this new customer relationship, A can plausibly position itself as a quality leader.

Example 2

The case with supplier B, a producer of corporate software, is somewhat different. The company's proprietary solution for a certain clientele has grown organically. It often occurs that, despite additional modules and expansions, such solutions reach their limits. New systems have to be introduced from time and time, and they are not always compatible with the old systems. If B then plans a technological leap that would no longer allow downward compatibility—for example, to appeal to a larger circle of potential customers with a new platform and much less expensive components—the bonding effects of the old system in regard to existing business relationships would no longer apply.

Example 3

The situation with D, a German manufacturer of semiconductors, is different from A and B. D supplies manufacturing technology and process solutions for the semiconductor industry. This industry is characterized by a rapid technology cycle. According to "Moore's Law" (Moore 1965), the computing capacity of a semiconductor component doubles every 2 years. For D's

(continued)

customers to be able to promptly supply their own customers at the beginning of every new generation of technology, they need the newest manufacturing technology as quickly as possible. To facilitate this, the semiconductor manufacturer has to integrate various initial investments. D's initial investments are as much a part of this as the investments made by the American company P. In addition, both companies use various services supplied by the other company. D and P recently announced a strategic partnership. With the integration of their respective capabilities on the one hand and their joint cooperation with nearby universities and research facilities on the other, both companies anticipate faster and more comprehensive solutions for the semiconductor industry.

In the first two examples, decisions made in the course of business relationship management have a significant impact on the economic viability of the company. In Example 1, taking advantage of a strategic window paves the way to entering into a new business relationship. For supplier A, this is a rare opportunity for organic growth in an industry in which supplier-customer relationships tend to be rigid. Also, A can use the new business relationship as a reference for top technology. The superiority of the special supplier system can be demonstrated, making A a more attractive partner for other OEMs as well. In contrast, the technological leap in Example 2 B poses the threat of harming or even terminating business relationships without entering into new relationships of the same scope and volume.

The situation in Example 3 is a little different. The customer relationships of D and of P are characterized by enormous time competition. This time competition is a continuous threat to the viability of the semiconductor manufacturer, as many bankruptcies have clearly demonstrated over the years. Thus, many of D's and P's business relationships are in danger. Besides the relationships with their customers, D and P have a relationship with one another. It is distinguished by their mutual supplier-customer relationship, but also by the fact that both companies supply similar customers. With the planned cooperation, D and P intend to gain a head start and then pass along the benefits to their customers. Both companies use their network to not only ensure the survival of their customers but also to secure and expand their own business relationships with customers. This, too, is a supplier decision intended to be more competitive in business relationships.

All of the examples are about obtaining or defending a competitive advantage. Achieving a competitive advantage is generally viewed as the foremost task of competitive strategy (Kleinaltenkamp 2002). There are two fundamental alternatives to achieving a competitive advantage: A supplier can offer his customers a less expensive or a better solution to a problem. These concepts are referred to as price leadership and quality leadership. Some authors point out a third strategy option: Porter (1980) talks about a niche strategy differentiated by the degree of market penetration, while Backhaus and Schneider (2009) deem the dimension of time to be essential and cite time leadership as the third generic

strategy. What all of the generic strategy options have in common is that they are all organizationally established at the level of a strategic business segment (Kleinaltenkamp and Fließ 2002).

Although the concept of marketing as a mindset of market-oriented corporate management has asserted itself amongst marketing researchers (Backhaus and Schneider 2009; Homburg and Krohmer 2009), marketing in companies is still considered a corporate function. Therefore some authors differentiate the marketing strategy from the competitive strategy, e.g. Kleinaltenkamp and Fließ (2002). These two authors are convinced that the marketing strategy comprises “*the entire process of the selection and targeted application of marketing instruments. (. . .) Moreover [the activities of the marketing strategy] provide the framework for all measures related to business relationship management that aim to establish or maintain a business relationship*” (p. 237).

Strategic decisions in business relationship management, depending on their manifestation, are positioned somewhere between these two strategy interpretations. Decisions in the course of business relationship management contribute significantly to the pursuit of various options regarding competitive strategy or even enable this in the first place. On the other hand, decisions related to competitive strategy impact the implementation of business relationship management, thus affecting the marketing strategy.

The three examples clearly reveal both facets. In the first case, A’s entering into a business relationship with OEM C can lead to A being viewed by C’s competitors as a quality leader for the system being considered. This is an essential prerequisite for obtaining a competitive advantage (Backhaus and Voeth 2010, whereby the authors talk about a comparative competitive advantage). So when A is successful in entering into a business relationship with C, he has successfully accomplished a significant competitive move. The second case is different: With his new system platform that no longer possesses downward compatibility, software supplier B is pursuing a price leadership strategy. B loses the bonding effects of the previous system and thus has to think about how to maintain the existing business relationships or if he can afford to forfeit some of his existing business relationships. So a decision relating to competitive strategy has an effect on the marketing strategy. Both influences can be detected in the third example. Intensifying their relationship with one another with a technology partnership creates a basis on which D and P can assert their time leadership. This is in turn reflected in the constellation of the business relationships to both companies’ customers. If D and P are successful in achieving their competitive position, the value of the relationships to the customers increases for the customers as well. This consolidates the business relationships.

So when business relationship management helps to reply to competitive strategic questions, it warrants discussing the extent to which our navigator, the competitive advantage (Plinke 2000), is applicable. A particular question is whether our understanding of a business relationship means that the contents of the concept have to be more narrowly specified or modified. The following section deals with this question.

5.1.2 Competitive Advantage in the Context of Business Relationship Management

According to Plinke (2000), the competitive advantage of a supplier S consists of a customer-based component and a supplier-based component. The customer-based component is the customer benefit, reflected in the relative net benefit. Supplier S reaps such a benefit when customer C favors S’s offering over a similar competitive offer from S’s competitor SC. It is assumed that, to assess the relative net benefit, all significant benefit and cost components of the two competing offers perceived by the customer are taken into consideration. So the relative net benefit is the effectiveness advantage of supplier S (Backhaus and Voeth 2010). S can achieve the relative net benefit of customer C by providing C with a greater benefit than SC, by generating lower costs than SC or by combining cost and benefit elements that reinforce one another or compensate for one another.

The supplier advantage, on the other hand, describes the efficiency dimension of the competitive advantage. Supplier S has a supplier advantage when he is able to economically provide the customer benefit. S should make a profit in the short term. Over the long term, S’s profit should be greater than that of SC to be able to defend the competitive advantage. If S were to make a lesser profit than SC over the long term, SC could implement cost reductions to change the cost difference between the offers to the customer and potentially eliminate S’s customer benefit as compared to SC. Figure 5.1 shows the key elements of the competitive advantage.

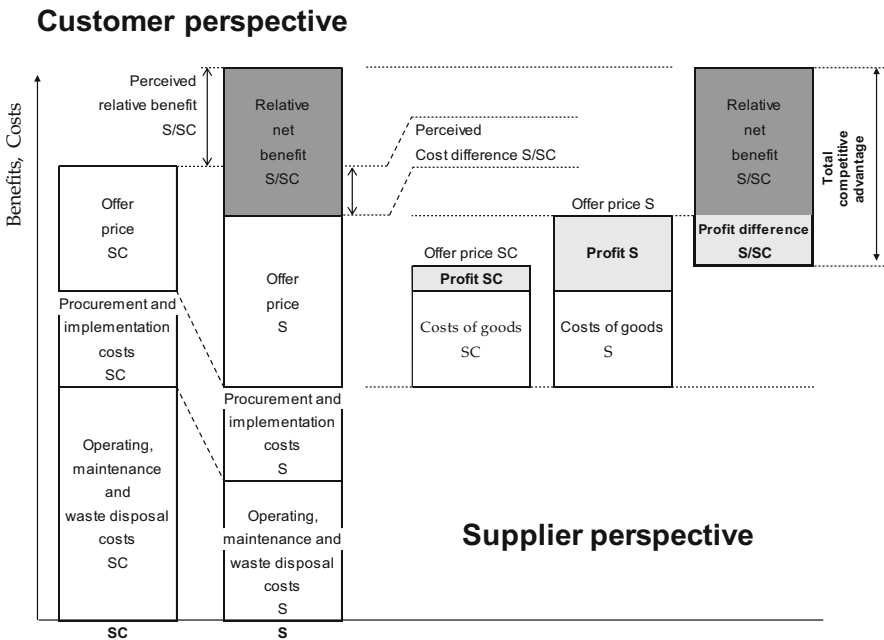


Fig. 5.1 Example of a competitive advantage. Source: Based on Plinke (2000)

As we have already discussed, the competitive advantage serves as a fundamental instrument that a company uses to navigate all market-related strategy deliberations. However, if one examines this navigator more closely, it becomes obvious that the fundamental logic of achieving a competitive advantage is implicitly related to transactions, the market (segment) and the point in time.

The **transaction as the object of reference** is reflected in the fact that, in demonstrating a competitive advantage, the benefits of a transaction become plausible to both the customer and the supplier. When customer C reaps a greater net benefit from a transaction with supplier S than from a transaction with an alternative supplier SC and supplier S makes a profit on the transaction, the transaction comes about. Supplier S then has a competitive advantage (with the customer).

But since it is only in special cases that a supplier can cover all of the costs of goods sold from a single transaction, e.g. in the project business (Backhaus and Voeth 2010; Plinke 1998), in all other cases the portrayal of the competitive advantage is always **related to the target market (segment)**, meaning the aggregate of the current and potential customers of the respective supplier. The supplier company cannot work such as to cover all fixed costs and generate a profit until all of the customers have been carefully examined. The higher a supplier's fixed costs are, the stronger is the influence of the total number of customers on the existence of a supplier advantage.

In addition to the reference to the transaction and the market segment, the basic discussion of a competitive advantage reveals the **reference to a specific point in time**. It is often pointed out that a competitive advantage should be defendable and thus stable in regard to time, meaning it should always be recognizable when customer and supplier benefits are analyzed at different times (Plinke 2000; Backhaus and Voeth 2010); this view remains comparative-static though.

The preceding chapters of this book have revealed that business relationship management is based on

- Business relationships, not on isolated transactions
- Individual customers, not on markets or market segments and
- Time periods, not points in time.

For the construct competitive advantage to be able to be utilized as a navigation instrument for business relationship management as well, the competitive advantage properties discussed above will be specified and corrected in detail here.

The first correction is needed in regard to the reference to a transaction. As discussed in Chap. 1, the business relationship is the consequence of transactions that have an internal relationship with one another. To be able to properly discuss the competitive advantage, it is important to know whether, from the supplier and customer point of view, the business relationship is a *de facto* or a planned relationship.

Figure 5.2 shows the various possibilities. The benefits that the supplier has from the relationship are clearly a factor of how the exchange relationship (transaction

How the supplier has to view the competitive advantage		Customer's view at the beginning of a later business relationship	
		<i>Transaction orientation (de facto business relationship)</i>	<i>Planned business relationship</i>
Supplier's view at the beginning of a later business relationship	<i>Transaction orientation (de facto business relationship)</i>	Customer benefit: static Supplier advantage: static 1	Customer benefit: dynamic Supplier advantage: static 3
	<i>Planned business relationship</i>	Customer benefit: static Supplier advantage: dynamic 4	Customer benefit: dynamic Supplier advantage: dynamic 2

Fig. 5.2 Supplier's view of the competitive advantage in business relationships

vs. relationship orientation) is viewed by both the supplier and the customer at the beginning of the business relationship.

If at the beginning of a potential business relationship both parties assume they will perform a transaction with one another without planning a business relationship (quadrant 1), the supplier's point of view is static: In the above transaction, his offer must be effective, meaning that the customer receives a relative net benefit greater than that of a comparable offer from a competitor. Also, the supplier should ensure that he makes a profit with this transaction, thus realizing a supplier advantage as a result of the transaction. Consideration of the benefit is a cost-benefit calculation for both sides. So the supplier must invest effort in his marketing activities to ensure that the potential customer clearly realizes the benefits of the transaction.

The opposite case would thus be a business relationship planned by both sides (quadrant 2). In this case the customer's as well as the supplier's considerations of the benefits are based not on the costs and benefits of a single transaction at a specific point in time but on the entire time period of the planned business relationship. This means that the cost-benefit calculation applied thus far becomes an investment decision (Hogan 2001): A customer benefit exists when the customer C ascribes to the future business relationship with supplier S a higher present value (refer to Chap. 4, where the reverse point of view—the value of the business relationship for the supplier—is reflected as the customer lifetime value) than to a relationship with the competitor SC. This means that the discounted, cumulative returns from this business relationship are higher than those from an alternative business relationship. Likewise, S has a supplier advantage when the present value of the business relationship for S is positive. Since this is an investment decision, for the supplier it frequently means higher costs than revenue at the beginning of the planned business relationship. But the costs are overcompensated later due to the

long time horizon. As we can see, the customer and supplier advantage arise from dynamic consideration in this case. For the supplier, this means that he has to gear his marketing strategies towards pointing out to the customer the added value of a business relationship, not of the single transaction.

Between these two poles, there are two alternatives for which the customer and supplier point of view differ at the beginning of a potential business relationship. If the customer considers the exchange relationship a planned business relationship but the supplier is focused more on the transaction (quadrant 3), only examination of the customer benefit is subject to a dynamic calculation, while the supplier advantage is viewed statically. So the customer wishes to enter into a business relationship and the supplier has his doubts. Consequently, the question arises as to whether this situation should even be included in a book about business relationship management: After all, the supplier has no intention of entering into a business relationship. If only the beginning of a business relationship were the topic of this book, the answer would clearly be no. When looking at the issue of potential termination of an existing business relationship by the supplier, we will encounter the considerations in this quadrant of the matrix again. It can be stated that the marketing activities of the supplier could be geared towards demonstrating the advantages of a business relationship for the customer. But it is essential to point out that a supplier advantage can be realized with every single transaction.

The fourth case is the one most commonly encountered in corporate reality. While the potential customer is focusing on the benefits of a transaction at the beginning of a business relationship, the supplier is already thinking about a long-term business relationship. This is justified by the fact that the supplier's costs incurred for customer acquisition are vastly higher than those incurred for customer (Reichheld and Sasser 1990). In regard to marketing strategies, for the supplier this means that he has to convey to potential customers the benefits of the transaction. He will make at least some investments that could ideally lead to the exchange relationship with the customer becoming a business relationship. After all, he sees his supplier benefit as dynamic: It is important to him that the customer proves to be profitable over the course of the business relationship, not necessarily with the first transaction.

As already mentioned, differentiating between the static or the dynamic perspective of the competitive advantage is important not only at the beginning of a business relationship. Over the course of a business relationship, various parameters affecting the competitive advantage of a supplier change. So the next section will focus on strategic analysis in the context of business relationship management, enabling the parameters to be identified and described in detail.

5.1.3 Strategic Analysis in the Context of Business Relationship Management

Discussion of the competitive advantage showed that at least three objects must be closely examined to determine the advantage: The situation of the customer, the

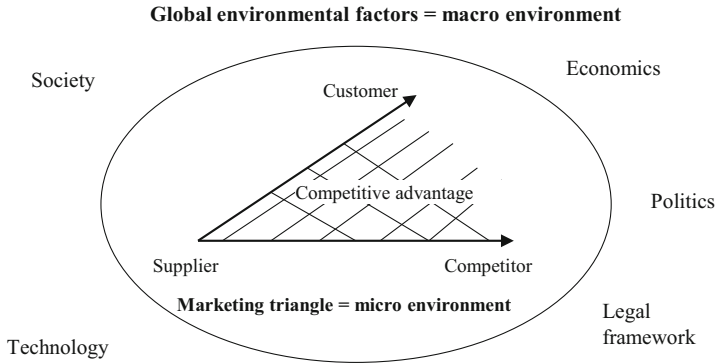


Fig. 5.3 Strategic analysis. Source: Based on Homburg and Krohmer (2009)

state of competition and the capabilities of one's own company. These three poles form the marketing triangle (Backhaus and Voeth 2010) within which the competitive advantage can be determined. But since none of the three poles can be examined in isolation and there is much interaction with the environment, the strategic analysis is supported by analysis of the global corporate environment (Homburg and Krohmer 2009). The analysis includes examination of social, macroeconomic, political, legal and technological developments. Figure 5.3 shows the general strategic analysis task for marketing.

These analysis tasks of course also apply to companies whose marketing activities are dedicated particularly to long-term business relationships. The tasks generally required have already been discussed elsewhere (Kleinaltenkamp 2002). Thus only two aspects of analysis will be handled in detail here—aspects that are of particular relevance to strategic considerations in business relationship management. The first aspect has to do with the time dimension of business relationship management. As the previous section explained, the competitive advantage can be viewed statically as well as dynamically. Particularly with the dynamic view, the time of consideration plays a decisive role in the market behavior of the participants. So we need to look more closely at the phases of business relationship management. Examination of the reciprocal effects of a business relationship with its environment is deemed particularly significant. The following two sections are dedicated to these special analysis tasks.

5.1.3.1 Phases of Business Relationship Management

Phase models have been used for analysis purposes in marketing science and practice for a long time. The product life cycle, shown in Fig. 5.4, is a particularly prominent concept. Expanding on the adoption and diffusion of innovation (Rogers 2003), the concept describes how a product is disseminated in the market. It implies that every product, in the modified form of the model, or even entire markets pass through certain life cycle phases. The phases have different sales and profit potentials. The basic form of the model differentiates between introduction, growth,

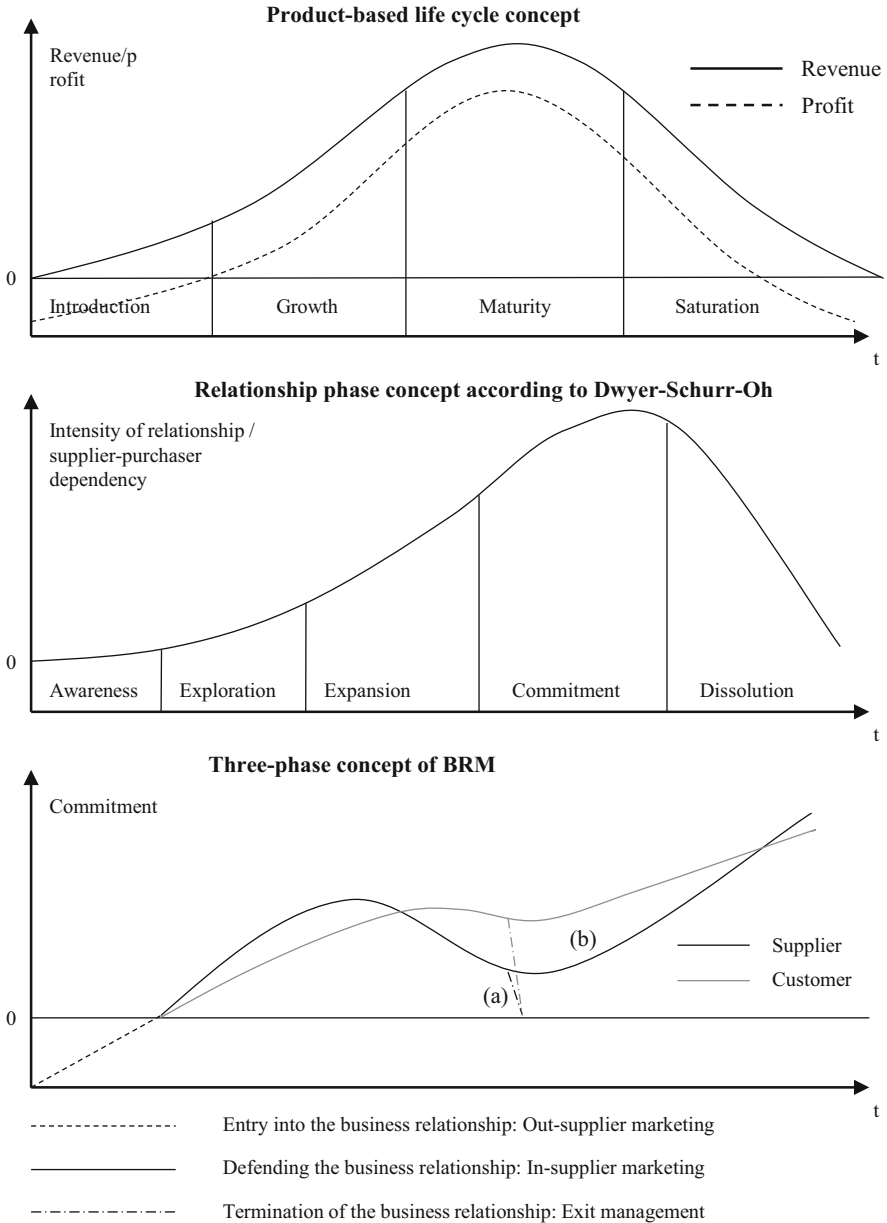


Fig. 5.4 Phase concepts in marketing

maturity and saturation. The individual phases are often described following the dimensions market growth, market potential, market shares, stability of market shares, number of competitors, customer loyalty, entry barriers and technology

(Homburg and Krohmer 2009). Certain standard strategic assertions can be made based on the different phases of the life cycle. Specifically, program structure analysis can be performed to classify a supplier's product portfolio in different life cycle phases on the basis of the model. It serves to check for a balanced mix of products in the various life cycle phases.

One aspect of the life cycle concept that is sometimes criticized is the simplicity of the course of the curves. They reflect merely an ideal course. Other courses could also be empirically proven. The time continues to be used as the sole explanatory variable. This implies that the sales are subject to a certain regularity over which the company has not influence. In regard to business relationship management, the concept has two significant weaknesses. On the one hand it is product-based and on the other solely supplier-based. A business relationship can be founded on one product, but often there are several products involved, especially in a long-term relationship. Also it is dyadic, so a single supplier viewpoint is inadequate.

The relationship model propagated by Dwyer et al. (1987) has been applied instead, particularly in US American marketing science. This is the concept shown in the second graph in Fig. 5.4. The model describes the typical course of a relational exchange between supplier and customer. The authors differentiate between five phases: awareness, exploration, expansion, commitment and dissolution. In the awareness phase, the two parties become aware of one another, but all actions are one-sided. According to the model, the parties begin to interact with one another during the exploration phase. This phase is divided into five sub-phases: attraction, communication and negotiations, development and application of power, development of standards and formation of expectations. The initial transactions occur here. In the positive case, a certain degree of trust and satisfaction is established on the part of both partners, facilitating entry into the third phase. This phase contains the same sub-phases as phase 2, except that the parties accept greater risks and increase their mutual dependency. The fourth phase, commitment, is the point at which the exchange partners reach the greatest relationship intensity. The commitment phase is characterized by a high degree of specific investments by both parties (*inputs*), by sustainability and by consistency/predictability. The last phase is dissolution. While the establishment of a relationship requires activities by both parties, dissolution is usually initiated by one party. In describing the final phase, the model's authors use the analogy of dissolving a personal relationship. An intrapsychic phase, in which one party evaluates its own satisfaction, finds it to be negative and decides to terminate the relationship, is followed by an interactive phase. The parties negotiate the modalities of the dissolution during this phase, before making the dissolution public in the social phase. The process is completed with a phase of social and mental recovery on both sides.

The phase concept developed by Dwyer et al. (1987) brought about substantial added value in describing market exchanges between economic participants, in that relational elements were compared to the purely economic cost-benefit calculation of economic theory. And as opposed to the life cycle model, it is not formulated from the supplier viewpoint and does not have a single product as its object. However, it attempts to describe relationships between companies and consumers

as well as those between companies. So the object examined is always implicitly the person as the economic participant and not the company. This may explain why trust and satisfaction, two variables from social psychology, are emphasized as special “bonding agents” between the parties. As the foundation for their theory, the model’s authors apply the classic writings of social exchange theory. This is why they refer to a relationship as early as the first phase of a relationship, although this is not the case in our interpretation of a business relationship. The inevitability of relationship termination also contradicts our understanding of business relationships as well as the reality in which e.g. the business relationship between Bosch and Mercedes-Benz (and its predecessor corporation) has existed since the early twentieth century and shows no signs whatsoever of coming to an end. But the most crucial aspect of applying the model in marketing practice may be primarily its descriptive nature. In particular, phase-based implications for business relationship management are missing.

Instead, we suggest a phase model that is explicitly geared towards action and takes into consideration different courses of business relationships. It is illustrated as number III in Fig. 5.4. It shows the supplier’s view (black line) as well as the customer’s (gray line) and differentiates between the three phases of a business relationship: entry, defense and termination. The model assumes that some business relationships are terminated (case a), but that many business relationships have no foreseeable end (case b). The demands that these three phases place on business relationship management are vastly different.

In the entry phase (simple dotted line), a supplier (black line) attempts to demonstrate to the potential business partner the benefits of a transaction (in case of de facto business relationships from the customer’s perspective) and the benefits of a business relationship with this supplier. So the supplier has to focus particularly on generating and communicating a customer benefit. This is especially difficult when the potential customer has a business relationship with a direct competitor and the relationship poses high exit barriers for the customer. If the supplier is active in a relatively stable market, his primary analysis task in this phase is to identify strategic windows for entry into a relationship to even be able to create a customer benefit. Depending on the customer’s orientation, sometimes the static view of the customer benefit and sometimes the dynamic view must be taken. Section 5.2 is devoted to these analysis and marketing tasks.

The customer and supplier are in the actual business relationship by the time they enter the defending phase. The commitment of the partners to one another is determined by the relationship value and switching costs for the customer and by the customer lifetime value (Chap. 4) and the switching costs for the supplier. Both dimensions are concretizations of customer benefit and supplier advantage in the case of business relationship management. As long as the business relationship remains beneficial to the supplier, he should attempt to control the business relationship such that the customer also has no reason to terminate the relationship. Then the dimensions relationship value and switching costs are available to him for marketing actions (Saab 2007). The associated analysis and marketing tasks will be discussed in Sect. 5.3.

The termination phase can occur at any time in an existing business relationship in which the commitment between the two partners has reached a low point. It can be initiated by the customer or by the supplier. In our case we will assume the perspective of the supplier to examine the circumstances under which a supplier should terminate a business relationship. The reasons for this step include economic, organizational and technological factors. Possible reasons for the termination can be attributed to customer value, meaning the dynamically viewed supplier advantage, to customer behavior, or to shifting of the fit between customer needs and supplier services. Section 5.4 will deal with this topic.

5.1.3.2 Reciprocal Effects of Business Relationships with Their Environment

In addition to the phases in which business relationship management should take on a different appearance, considerations from a strategic viewpoint regarding reciprocal effects of business relationships with their environment play a special role.

On the one hand, the environment can be the market as a micro environment. Business relationships between the supplier and other customers or between customers and competitors are then of particular interest. It is important to examine different parallel business relationships that a supplier has, because there can be positive as well as negative reciprocal effects between these business relationships. In an industry in which supplier services demand a high degree of customer trust, establishing and expanding a business relationship with customer 1 can be an essential reference for the supplier. It is only the successful business relationship of the supplier with customer 1 that makes the supplier's promised performance plausible to customer 2 and makes him an interesting business partner. The situation is different when a supplier's customers fear that the supplier is using resources that give the existing business relationship value in other business relationships as well. These resources might even have been developed jointly in the course of the business relationship, e.g. a special logistics concept or new production technology. In such cases the supplier has to decide whether to forfeit competing business relationships or to find a way to convince parallel business partners that their rights are not being infringed upon by activities with competitors. Questions about handling parallel business relationships will be examined in depth in Sect. 5.5.1.

On the other hand, the macro environment can also be factor, e.g. as societal, political, legal, economic or technological developments. In regard to the first factors, especially developments towards good governance have impacted business relationship management over the last decade. For example, many large corporations have introduced codes of conduct that narrowly specify how their own employees can accept gratuities. This gives a supplier much less leeway in personal relationships. The corruption scandals of recent years and having to deal with them have led many companies to implement much more stringent transparency measures. For some companies, this has led to terminating or examining existing business relationships (Schmitt 2010). Besides these factors, we are interested especially in economic and technological developments that can be utilized to benefit a supplier's business relationships. This happens often by a supplier using

relationships with other business partners to strengthen his own business relationships with customers (Anderson et al. 1994). By using his network, he can e.g. integrate technological innovations in his offering, providing customers with greater value. Section 5.5.2 deals with this strategic component.

5.2 Entry into the Business Relationship: Out-Supplier Marketing

There are two consecutive steps that a supplier takes when he plans to enter into a business relationship: First he identifies strategic windows, and second he selects entry concepts appropriate to the type of business relationship to be entered. As discussed in Sect. 5.1.2, the customer calculation differs by whether or not the potential customer in aiming for a business relationship right from the start. From a marketing strategic perspective, the supplier has to provide the potential customer with different information needed to make a decision.

5.2.1 Strategic Windows

Example 4: Flying Against the Trend

The year 2009 was not a good one for the aviation industry. Lufthansa reported 89 % less operative profit than in 2008. Media reports claimed that British Airways was on the brink of bankruptcy several times. Air Berlin, in previous years treated as a potential candidate for bankruptcy or takeover was able to largely avoid this trend. What happened?

The financial crisis beginning in 2008 was the dawn of hard times for many companies. In Germany it was only with the aid of government support such as reduced-time pay that widespread layoffs could be avoided, particularly in the manufacturing industry. The result was strict austerity for most companies. This was apparent in business travel, which fell sharply. Long trips were replaced by teleconferences and travel guidelines became more stringent.

These measures hit a certain group of business travelers—flying business class on Monday morning and on Thursday or Friday evening on domestic or European routes—particularly hard: management consultants and auditors. One reaction to the financial crisis by the three largest consulting firms in Europe—McKinsey & Company, The Boston Consulting Group and Roland Berger Strategy Consultants—was to refrain from or limit business class on shorter flights, thus saving costs. And the travel departments and consultants were instructed to book the cheaper rate when comparable times could be found for the same route. The consultants—who used to be able to specify the

(continued)

exact flight time and airline and did not need to look at the price—were now restricted in their choices: Instead of their favored airline Lufthansa—the miles flown on business trips and collected in the customer loyalty program Miles & More were allowed to be used for personal travel—they often had to fly on the cheaper Air Berlin flight.

These trips were made appealing to the consultants. With a change in service, Air Berlin was able to establish a real business relationship with certain business customers or to intensify existing relationships. This included a blanket agreement with Roland Berger Strategy Consultants, granting all of the firm's employees silver status on Air Berlin. This status allowed higher baggage limits, guaranteed a seat in the front section of the plane to be able to deplane more quickly, granted preferential check-in and security treatment (the so-called fast lane) and a few other benefits. Besides the ticket prices that are lower than those of Lufthansa, Air Berlin granted the customer company additional discounts. In return, the consulting firm agreed to a quota of flights to be booked on Air Berlin. With the right offers to the right customers at the right time, Air Berlin used a difficult economic situation to increase its domestic market share and emerge from the crisis stronger than before. Roland Berger Strategy Consultants' quota to be met on Air Berlin flights continues to apply even now that business class is permitted again (Unknown 2010).

As Example 4 demonstrates, the timing can be crucial when it comes to entering into or intensifying a business relationship. Abell (1978) coined the term **strategic window** to express this phenomenon. He uses the term to express the time frame within which the special demands of the market offer an optimum fit for a company's resources and capabilities. These times when the fit is right should be used by suppliers to best serve the respective market.

In the case of business relationship management, the respective market can be a single potential customer, such as when the supplier is a component supplier to the automotive industry. But it can also consist of multiple customers and thus multiple potential business relationships, like in the introductory example, or the market can be many customers as is the case with suppliers of system technology, e.g. operating systems. In all of the cases, strategic windows for business relationships are characterized by the fact that the bonding effect of existing relationships between potential customers and competitors is particularly weak during these periods.

Typical situations in which the bonding effect in existing relationships is lower include the following (Backhaus and Voeth 2010; Schlüter 2000):

- Product launch, change in model or significant product variation by an OEM
- Contracts that are expiring or have been terminated due to conflicts in an existing business relationship

- Technological leap by a competing system supplier (e.g. software) that does not possess consistent downward compatibility
- Fundamental change in the sourcing strategy of potential customers due to internal or external changes in the corporation
- Shift in the market balance due to the exit of competitors (supplier shake-out) and consequential end of business relationships with their partners

In addition to constellations in which existing business relationships can be replaced or supplemented with new ones, situations are of course also conceivable in which completely new business relationships can evolve from a new way to solve a problem. This is always the case when innovations from the macro environment re-define the competitive arenas. Such innovations can be of a political-legal nature, such as deregulation in the energy, telecommunication or transport sector. They are often the result of technological innovations that enable certain business relationship models in the first place. The second case will be illustrated later in Example 7, “Brushes and rollers no longer needed for facades,” in Sect. 5.5.2.

Because of the fundamental bonding effect of existing business relationships between competitors and potential customers, observing and promptly identifying strategic windows is one of the most pressing strategic tasks of business relationship management. This task has to do with strategic foresight (Slaughter 1998). Companies must learn to detect even weak signals in their environment in time to be able to recognize such strategic windows (Ansoff 1979). To ensure that this actually happens, the identification of strategic windows should be a firmly anchored organizational task in the company. There are two ways that are particularly well suited: If the company or business unit has its own staff department for (competitive) strategy planning, it makes sense to assign this special task of strategic foresight to the department. Otherwise assigning the task to the marketing or sales manager would also be an option.

A complementary task to detecting weak signals in the company’s environment is to examine the company’s own capabilities and resources to determine if they can be used to take advantage of the strategic window. Depending on how potential new customers see the company, this can mean that the supplier company must be able to generate and communicate a static or dynamic customer benefit. The next two sections will discuss ways to generate such a customer benefit.

Finally, using Example 4, utilization of a strategic window will be demonstrated again. As a result of influences from the macro environment (dramatic decline in the overall economic situation), business travel habits of former airline customers have changed greatly. Many of the corporate customers of the airlines became more price-conscious and eliminated privileges previously granted to their employees, such as flying business class. So for the large consulting firms, for example, this meant a fundamental change in the sourcing strategy, which was met with some internal resistance. For Air Berlin, on the other hand, a strategic window opened. Business travelers previously allowed to fly business class did not consider Air Berlin, because it does not offer business class on short-haul and medium-haul flights. But since Air Berlin flies with about the same frequency as Lufthansa, at

least on many of the domestic routes, and offers a much lower ticket price, customer demands and Air Berlin's corporate resources suddenly went together much better. With additional offers tailored to the customers' needs, such as the silver card for all of the consulting firm's employees, Air Berlin was able to generate a true customer benefit for the consulting firms and break open virtually closed business relationships that had existed for years.

5.2.2 Entering into Business Relationships Not Planned (De Facto) by the Customer

As discussed in Sect. 5.1.2, there is a wealth of supplier-customer relationships in which the supplier is seeking a long-term business relationship right from the start but the customer's focus is on the single transaction. If the supplier wishes to successfully enter into such a business relationship, it is advisable for him to assume the customer's transactional view. In regard to the customer benefit that has to be generated and communicated, this means that the customer must perceive supplier A's offering as providing greater net benefit than the comparable offering by the competing supplier SC. Only then will the potential customer be willing to make an initial purchase.

So what does the supplier have to do? A glance at the information economics provides the general direction (Weiber and Adler 1995). A customer is exposed to a series of uncertainties related to his purchase decision, particularly in regard to quality and price of the offering. Supplier offerings can be classified by the potential to reduce uncertainty. Search goods are offerings for which the uncertainties can be greatly reduced by searching for information before making the purchase decision. Many properties of physical products fall into this category. Experience goods, on the other hand, are offerings for which the quality and price uncertainties cannot be reduced or eliminated until after the customer has made the purchase. This includes most services (as opposed to goods). Credence goods are offerings for which the customer cannot at all reduce uncertainties. They generally cannot be verified and are only revealed in exceptional cases. An example of this is a structure in which cracks appear 5 years after construction is completed, e.g. because the stability of the building ground was not properly assessed and part of the building has begun to shift.

There are different strategies available to a customer to reduce uncertainty before a purchase. Figure 5.5 provides an overview of the strategies. To limit uncertainty concerning search qualities, the customer can practice a strategy of offering-related information search. However, since experience qualities and credence qualities cannot be verified until after the purchase if at all, a customer has to rely on signals as a substitute for information. These are heuristics, meaning abbreviated decision-making rules that allow conclusions to be drawn about certain supplier and offer properties but do not guarantee them. A brand name, a corporate image or a certain price level are mentioned as such signals in publications. Weiber and Adler (1995) differentiate between information substitutes based on a single

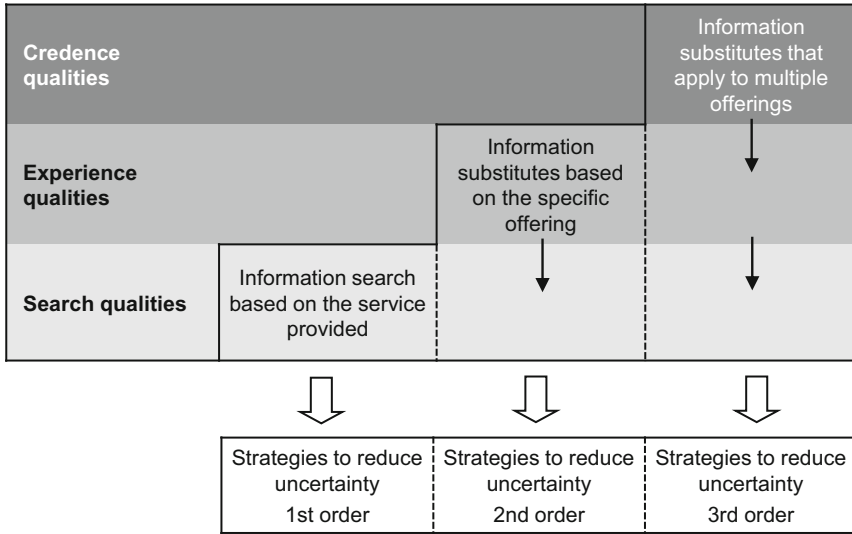


Fig. 5.5 Strategies to reduce uncertainty from the customer’s perspective. Source: Based on Weiber and Adler (1995)

offering or based on multiple offerings, depending on whether the uncertainties that can be reduced are related primarily to experience qualities or credence qualities.

Since the customer rationale for an unplanned business relationship is initially geared towards the transaction, it can be assumed that search qualities play a greater role than in relationships planned by the customer, while the opposite is true for experience and credence qualities. So the better equipped the supplier is to support the potential customer’s search for information, the more likely it is that an initial purchase will occur.

There must be differentiation regarding relevance of the information and the respective manifestation. If, for example, a potential customer is interested particularly in the physical quality of the product, the respective quality information (as opposed to information on price and delivery) should primarily be made available to him (relevance of information). Of course, the information has to persuade the customer that the supplier’s offer is superior to that of the competitor (contents of information). For the OEM supplier business, Backhaus and Voeth (2010) consider the dimensions quality, price, time and place to be offering features regarding which a supplier has to credibly convey that the customer’s demands are better met with his offering than that of the competition. A supplier can use all of the possibilities offered by the marketing toolbox (Kleinaltenkamp and Jacob 2006). This includes providing essential information on offering features (always relative to the competitor), e.g. with

- Product specifications incl. provable minimum requirements
- Quality certificates

- Cost-benefit calculators
- Price assurances, possibly incl. assurance of the (proportional) coverage of the customer's switching costs in the event of a system switch
- Relevant information on the organizational structure (locations, contact persons)
- Relevant information on process organization (logistics, adherence to schedules)
- Depending on the type of offering, the supplier will have to provide substantial information substitutes such as warranties or references. The following Example 5 shows how search and experience qualities can be credibly conveyed:

Example 5: Individual Taste

International Flavors and Fragrances Inc. creates fragrances for industrial purposes. The company develops and manufactures products for industrial customers, e.g. in the food industry, who use the aromas in their production processes. Through the use of toolkits, International Flavors and Fragrances Inc. was able to include the customer in the innovation process and at the same time give the customer a reason to subsequently order the products. The customer can use the toolkit to search for the desired scent solution. Once he has identified it, he sends the desired scent to International Flavors and Fragrances Inc. The company then develops a suggestion for technical production implementation and gives the customer a sample. After a correction loop, the customer can immediately place an order for the desired fragrance. (Backhaus and Voeth 2010).

For the initial purchase to become a real business relationship, the supplier has to ensure that the newly acquired customer sees reasons to purchase again from the supplier. These reasons can either be specifically created by the supplier, or they can evolve during the course of the transaction and later, unrelated transactions. The reasons created by the supplier include service/product customization, product-related services, loyalty programs or system lock-in (refer to Chap. 6). The reasons attributed to repeated exchange are particularly relational variables such as customer satisfaction, trust and well established processes in completing transactions. This is especially relevant in stable business relationships in which differences in the performance level of suppliers are minimal like those between accounting firms and their clients (Hougaard and Bjerre 2009). Only some of the relational variables can be managed by the supplier, but e.g. professional complaint management (Stauss 2010, Sect. 6.4.1) can prevent restrictions of these relational variables from occurring.

5.2.3 Entering into Business Relationships Planned by Both Parties

In contrast to business relationships not originally planned by the customer, where becoming committed to one supplier occurs slowly, the customer takes a different view from the start when he is planning on establishing a business relationship. He is aware that, with the beginning of a business relationship, he is committing to a supplier. It may not be possible to give up the relationship until the mid-term future,

and it could involve heavy losses. This means that the anticipated time period of the future exchange relationship is much longer. The potential customer may be able to reduce his uncertainties in regard to the search qualities of the service exchange by actively seeking information at the beginning of the business relationship. This means that the strategies to reduce uncertainties resulting from search qualities discussed in the previous section are also applicable to planned business relationships. Because the relationship is intended to be long-term, as the planned duration increases, the customer focuses more on the experience and credence qualities. Figure 5.6 illustrates the general relationship. While uncertainties related to search, experience and credence qualities are similarly pronounced in a business relationship planned to be short, with a longer business relationship the experience qualities and even more so the credence qualities of the planned, repeated exchange of transactions play a greater role. This can be attributed particularly to increasing uncertainties pertaining to the environment when a longer time horizon is planned.

The purchaser will only choose the business relationship if the supplier is better capable of conveying the experience and credence qualities of a potential business relationship with the aid of suitable information substitutes than is the competitor. This is equivalent to conveying the customer benefit from a dynamic perspective.

Weiber and Adler (1995) claim that information substitutes based on the service provided can reduce uncertainties attributed to experience qualities. They differentiate between directly and indirectly effective information substitutes. Directly effective information can be e.g. warranties or a contract that regulates anticipated future events. Information substitutes that work indirectly, on the other hand, can be price (as surrogate for quality), product-related advertising, product brands and references based on performance.

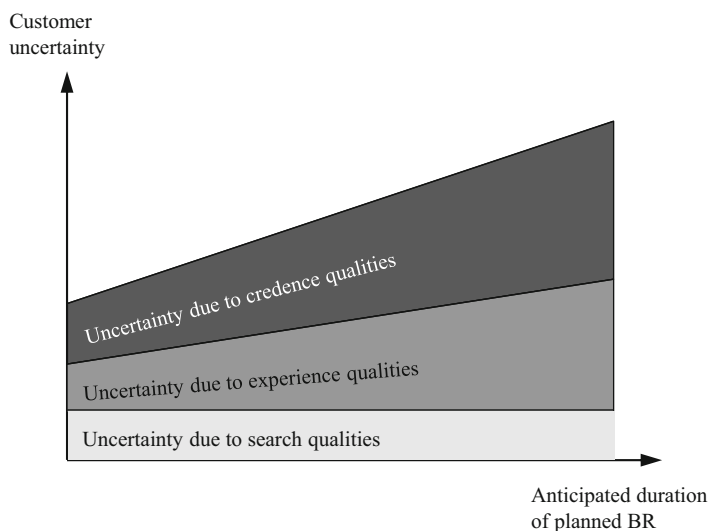


Fig. 5.6 Customer uncertainty as a factor of planned duration of a business relationship

Information substitutes that apply to multiple services help to reduce uncertainties attributable to credence qualities. The level of awareness of a company and the company's reputation play a significant role. A supplier's reputation is the result of experiences of his customers thus far and other interaction partners, whereby the experiences do not necessarily have to be those of potential customers. It is assumed that future transactions and business relationships with this supplier will be similar to those that have already taken place. So a potential customer relies on the supplier's reputation and expects that the supplier will act in the same way towards him as he has in the past when interacting with others. A customer's assessment of a supplier's reliability is influenced by information on the development of the supplier's financial situation, the strategy he pursues and his legal form, as well as his hiring and human resources policies and his efforts in regard to sustainability. Thus a company that markets its services to a high degree within business relationships is well advised not to underestimate these more global indicators of his business. From a strategic perspective, these indicators can serve to reduce the customer's uncertainty resulting from credence qualities.

In addition to the reduction of uncertainties, the supplier has to take into consideration another factor in his calculation to generate such a dynamic customer benefit: the previous business relationship of the customer which he might terminate in an extreme case or which can lose significance through establishment of a new, parallel business relationship. As we have already seen, it is easiest for the supplier to utilize a strategic window to approach potential customers at a moment in which the switching costs are as low as possible.

5.3 Defending the Business Relationship: In-Supplier Marketing

In the phase model of business relationship management, defending a business relationship is the most important and most frequent situation. As long as a supplier enjoys a supplier advantage from an existing business relationship or the switching costs associated with terminating the relationship do not make economic sense, he will endeavor to defend the existing business relationship. While earlier research discussed particularly the bonding effect of specific investments and the associated switching costs as the reason that a customer remains in a business relationship (Plinke 1997; Söllner 1993), more recent studies proclaim that, from the customer's point of view, the value dimension of a relationship is primarily responsible for a customer not switching to a different supplier (Eggert 1999; Geiger et al. 2012; Saab 2007). Therefore customers prefer remaining in a business relationship when they want to as opposed to when they have to. The dimension of the customer's switching costs should not be neglected though. Sometimes the two dimensions cannot be unequivocally separated, such as when specific investments on the part of the customer have to occur before the relationship value can increase (Kleinaltenkamp and Ehret 2006). Nevertheless, both dimensions offer essential approaches to defending a business relationship.

5.3.1 Increasing Relationship Value

When does a customer consider a business relationship to be valuable? Which factors contribute to the value? Ulaga and Eggert (2006) pursue these questions in their exploratory examination of corporate purchasing managers in various industries. They identify three different aspects that a supplier can focus on to increase the relationship value for a customer (Ulaga and Eggert 2006):

- Improvement of the core offering
- Improvement of the procurement and interaction process
- Enhancement of operations of customer

Benefit and cost components are assigned to each of these aspects; the components can serve as design approaches.

5.3.1.1 Improvement of the Core Offering

Improvement of the core offering has to do primarily with the **original product quality**. This of course means compliance with the customer's technical specifications (meeting quality demands). These specifications must be fulfilled over time though (quality consistency). If problems occur in this regard, suppliers are best advised to work with customer teams to find a long-term solution. It should be kept in mind that, to be able to evaluate the parameters meeting quality demands and quality consistency, a benchmark—usually based on customer expectations—is needed. Customer expectations change over time though. This is particularly true for goods having to do with information and telecommunication technology: The technological advances of the last 30 years have radically changed customer demands. Such goods often possess characteristics of a system, meaning they are linked to a system architecture to produce a customer benefit (Backhaus and Voeth 2010). Because of system lock-in, the customer is often forced to stay with a system supplier to be able to utilize new services. But to ensure that the bonding effect of such a system is not lost, a system producer is well advised to provide the technological advances needed to meet customer needs within the system that arise over time—so the supplier should be aware of meeting quality demands and ensuring quality consistency.

The following Example 6 illustrates the extent to which the customer's quality demands in regard to the core offering of the supplier can be influenced by the supplier:

Example 6: From Product Partner to Process Partner

The Lenze group, with 3,000 employees worldwide, is a major German supplier of automation technology. The product range includes servo drives, motors, couplings and brakes, but also complete drive systems. By applying

(continued)

“value engineering,” a customer-specific, process-based concept that considers all cost and benefit components of the customer process when calculating a customer benefit, the customer’s perception of quality changes from that of a product partner to that of a process and problem solution partner.

With the aid of this concept, Lenze was able to save EUR 12,500 with a procurement volume of EUR 100,000 for one of its A customers in the textile industry. However, these savings were possible only when the entire job—previously divided amongst three different suppliers—was taken over by Lenze. The total amount saved could be attributed to optimized dimensioning (EUR 4,000), simplified component assembly (EUR 5,000), process improvement (EUR 2,500), and quicker commissioning through proper training (EUR 1,000).

Lenze was able to emerge as a problem solver due to (a) traditionally existing mechanical engineering and drive design competence, guaranteeing the best possible design and dimensioning for the customer’s problem. Another contributing factor is a scalable product and service program (b) that facilitates low-cost as well as high-end solutions. And finally, individual customer solutions could be supplied through the acquisition of completely ready-to-install components from only a few suppliers (c).

Customers also expect their main suppliers to provide a **continuous improvement process**. This is the only way that a supplier can increase the relationship value by offering a core service that really is superior. Such a continuous improvement process can occur only on the part of the supplier or as a partnership between the customer and the supplier. The latter can often be found as R&D cooperations for new series in the OEM supplier business (Backhaus and Voeth 2010).

In addition to the product quality of the core offering, the associated **supply performance** is also significant in the customer’s value perception. **Adherence to schedules** is interpreted as the supplier meeting agreed delivery dates. **Delivery precision** describes the customer’s expectation that each delivery contains the exact supplier services that the customer wishes to have. Due to increasing coordination of value-adding processes involving multiple companies and the associated logistics concepts such as just-in-time delivery, a supplier’s delivery performance is becoming more and more relevant. The reduction of intermediate storage facilities at many steps of the value-adding process means that producing companies have lower costs of capital employed. If a supplier cannot maintain the promised supply performance in such a value-adding chain, the consequence will be high losses to the supplier and the customer due to production failure. So adherence to schedules and delivery precision should be considered the minimum requirements. A supplier’s **supply flexibility**, meaning his ability to implement short-term changes in the scope and date of deliveries, greatly enhances his value in a business relationship.

In the automotive industry, the supply performance of a supplier depends strongly on his location—being close to the customer guarantees advantages. In the early 1990s, the average distance of an independent supplier to Toyota from its customer was about one fifth the distance of external suppliers to General Motors. In addition, Toyota suppliers had five times as many deliveries, three times as much personal contact and 25 times as many guest engineers at the customer's facilities than did General Motors (Dyer 2000).

Of course every supplier offering has its price, generating costs for the customer and thus decreasing the customer benefit. Contrary to this, the price as payment for the service performed is crucial in determining the supplier benefit for the supplier. So the price should be considered by the customer to be fair. In industries in which contracts tend to extend over many years, factors that can contribute to the customer feeling that he is paying a fair price include an **annual discount** expected by the customer and (partial) **passing on of cost savings** that the supplier has benefited from. Customers also often expect their main supplier to match a competitor's lower price when the service is the same.

5.3.1.2 Improvement of the Procurement and Interaction Process

Continuous improvement of the procurement and interaction process includes supporting service activities in addition to the core offering (service support). Industrial customers particularly value the supplier's **reaction speed** to customer requests. The more complex the transactions within a business relationship are, the more difficult it is for both sides to anticipate every contingency. So misunderstandings should at least be expected. But if a customer can always rely on his supplier reacting promptly to any difficulties that occur, this can be considered to be an additional value driver in the business relationship. A second crucial component of service support is **information management**. When the customer's wishes change frequently, the speed at which information is made available is important. Customers also see the scope of information as important, whereby this often means more details.

A third, own element of service support is when the supplier takes over activities that the customer previously performed himself (**outsourcing**). The supplier then becomes an outsourcing partner to the customer. Examples of this are when the supplier takes over storage (vendor managed inventory) or assembly of preliminary products to build modules. Introduction of simplified order handling using electronic ordering systems or the supplier taking over **quality assurance tasks** (inspection of incoming goods) are also services that increase the value of the relationship.

An essential requirement for efficient and smooth cooperation between the supplier and customer companies is the constellation of the personal relationship between the persons at the two companies who are communicating with one another. It has been apparent since earlier studies that choosing a sales employee with similar personality traits to those of the purchasing manager he communicates with leads to greater sales success than when their personalities are different (Evans 1963; Schoch 1969). If in addition to their professional relationship the

communication partners from the supplier and customer companies develop a **personal relationship** of mutual regard and understanding, it becomes easier to understand the customer's objectives and to find quicker and better solutions to the customer's problems. Such personal relationships can be promoted with different relationship nurturing instruments such as fireside chats, invitations to sporting events, etc. But recently especially larger corporations have introduced stricter rules (codes of conduct) for the acceptance of personal gratuities from suppliers. For such personal relationships to be able to evolve, it is essential that both sides have a certain **stability over time of customer contact personnel**.

5.3.1.3 Enhancement Operations of Customer

Improving the customer operations may be the greatest area in which to generate enduring relationship value. Potential starting points for increasing value are the product development process and the customer's production process.

Value creation and enhancement during the product development process of a customer includes the supplier's participation in management processes such as target costing and simultaneous engineering. **Target costing** is a comprehensive process that develops new products based on market needs. The products are designed to meet the product features demanded by the market at prices that the market tolerates (Seidenschwarz 1993). After deducting a profit margin for the supplier, target costs are specified as guidelines that the design and development of the product must comply with. Since target costing is used especially for products manufactured in series and the depth of added value has decreased over the last few years for OEMs, integrating the important suppliers in such a process is seen by the OEMs as being more and more important. **Simultaneous engineering** describes the process of parallel, interlinked product development on the part of the supplier and the customer (Bochtler and Laufenberg 1995). By bringing previously upstream and downstream development steps into parallel, the customer gains a time-related advantage. The organizational coordination required for this development concept, e.g. a uniform development platform for internal cooperation and working with other companies, serves to avoid discontinuity of media, transmission errors and incompatibilities (Backhaus and Voeth 2010). **Rapid prototyping** can also give the customer time-related advantages, thus increasing the relationship value (Halfmann and Holzmann 2003; Weiber et al. 2006). When a supplier is capable of quickly producing simple prototypes, the customer and the supplier can use the prototypes to quickly make improvements, thus reducing the total time-to-market for the customer's products.

Increasing the relationship value by improving the customer's production process is facilitated primarily by the customer saving costs. For example, based on existing products of the customer, a **supplier suggestion scheme** can be used to identify and eliminate dispensable steps in the customer's production process. If the supplier has a wide customer base, solutions successful in the industries of the other customers may serve as creative suggestions for the production process of the customer in question. Such suggestions on how to improve processes can include

e.g. operating models that help to save maintenance and repair expense as well as warranty and tool costs.

Regardless of specific process improvements in R&D and the customer's production, such suppliers provide customers with a special value that the customers can rely on when they need **technical problem solving skills**. The technical solution sought does not have to be related to other transactions between the business partners.

5.3.2 Increasing Customer's Switching Costs

A customer's switching costs are the dimension of loyalty that to a certain degree force a customer to remain in a business relationship with a supplier. According to Saab (2007) they can be characterized as direct switching costs and sunk costs of investments attributed to specific relationships.

A customer's **direct switching costs** are those that are incurred to terminate a business relationship (termination expenses), to seek a new business partner (search costs) and to establish a new business relationship (setup costs). These costs cannot be interpreted as strictly economic values, they should also be seen as the monetary equivalent of psychological and social expenses (Rieker 1995). To put this into perspective, it must also be noted that direct switching costs are incurred in full only when a customer procures a certain service exclusively from one supplier. If this is not the case, the customer will incur nominal or no search and setup costs. So the influence that a supplier has on a customer's direct switching costs is limited. At least in the case of long-term business relationships governed by a contract, it may make sense for the supplier to include in the blanket agreement **penalties** for premature termination of the supply relationship (Backhaus and Voeth 2010).

The customer incurs **switching costs related to relationship-specific investments** when relationship-specific investments have not yet been depreciated. They are referred to as sunk costs (Saab 2007). This is the most common case in the system business, where the customer consciously ties himself to a supplier for a certain time (payback period). Sunk costs are incurred e.g. when a company has purchased from a supplier planning software with various optional extension modules. After expansion of the business, this software system no longer meets the customer's requirements and must be replaced with a new, more powerful system provided by a different supplier. The portion of the original software that has not yet been depreciated is considered sunk costs for the customer. To generate switching costs for the customer due to sunk costs, a supplier basically has several dimensions of specific investments available to choose from. These are site specificity, asset specificity, human capital specificity and time specificity. So the supplier's goal should be to get the customer to invest along these dimensions specifically for the relationship. If for example the customer has to pay for special training required for his employees to be able to use the supplier's service, the switching costs along human capital specificity increase. An information technology network specifically for the relationship, e.g. a tailored ordering system

(hardware and/or software, processes) that the customer at least partially pays for increases switching costs for asset specificity.

In conclusion, however, it should be pointed out that a supplier has limited possibilities to influence sunk costs through relationship-specific investments made by the customer.

5.4 Termination of a Business Relationship by the Supplier: Exit Management

Although it is generally assumed that a business relationship is an asset to a supplier and retaining customers makes greater economic sense than new acquisitions (Reichheld and Sasser 1990), the question has arisen repeatedly over the last 10 years as to whether this supposed wisdom applies unconditionally. The answer is no. The focus shifts to a different question instead: Under which conditions is it more beneficial to the supplier to terminate an existing business relationship than to continue to pursue it? The consequences of terminating the business relationship must be considered as well. This leads to the question of which ways of terminating a business relationship best highlight the positive aspects while playing down the negative effects. These considerations will be examined in the following section.

5.4.1 Termination of a Business Relationship: Reasons and Consequences

In our phase model of business relationship management, we showed the business relationship as a “going concern” of a B2B supplier. So the ideal business relationship does not end once it is firmly established. Rather the business partners again and again renew their connection and both benefit from it. Such a pattern can be observed between important suppliers to the automotive industry and the OEMs, who have business relationships spanning decades.

Besides the various reasons that might induce a customer to terminate a business relationship, such as when, due to technological leaps, his needs can be better or less expensively met by a different supplier, there are also reasons that can prompt a supplier to end a business relationship. Three of the customer’s reasons are of particular relevance to the supplier:

- Customer value
- Customer behavior
- Customer needs

5.4.1.1 Customer Value as a Reason for Termination

According to a recent study performed by Haenlein and Kaplan (2009), introduction of customer relationship management (CRM) systems in many companies have made it much easier—or even possible in the first place—to evaluate customers

without unreasonable effort (Haenlein and Kaplan 2009). Such evaluations of individual customers revealed to companies in different sectors such as retail banking (Haenlein et al. 2006), logistics (Niraj et al. 2001) and the metalworking industry (Bowman and Narayandas 2004) that between 20 and 30 % of their customer relationships were not profitable. These findings are confirmed by practitioners (Karle 2008).

But companies should apply their resources in the most profitable and efficient way. Since for marketing purposes a customer relationship can be seen as an investment made by the supplier, a company should regularly examine its business relationships to determine which ones it should continue to pursue and which it should give up for economic reasons. “*Not all customers are worth attracting and keeping*” (Rust et al. 2000, p. 187). The various measures of customer value were discussed in Chap. 4 of this book. Ideally, the decision as to whether a business relationship should be continued or not from the supplier’s perspective should be made on the basis of the customer lifetime value (CLV). The CLV ideally reflects not only the anticipated monetary benefit of a business relationship but also the resource potential (reference, information, cooperation and synergy potential) of the respective customer (Tomczak and Rudolf-Sipötz 2006). If for reasons related to information technology or other operative limitations the CLV is not available to a company as a present- or future-oriented measure, other indicators should be used to determine the customer value. One example of such an indicator is a customer-specific contribution margin in conjunction with qualitative assessments of the respective customer’s reference and information potential. In contrast, categorizing customers by revenue, which many companies do, is misleading (Karle 2008).

Regardless of the metric used to measure the customer value, the decision of whether the supplier should terminate a business relationship with a low or negative customer value is comparable to a portfolio decision (Lucco 2008): By ridding the customer portfolio of unprofitable or less valuable customers, resources are freed up to be invested in promising business relationships (Johnson and Selnes 2004). For example, the real option approach can be used to support such decision (Haenlein and Kaplan 2009).

5.4.1.2 Customer Behavior as a Reason for Termination

Besides customer value, the specific customer behavior can be a second crucial reason for a supplier to terminate a business relationship. Since on-going problematic customer behavior impairs the customer value as well, it is impossible to completely separate these two termination reasons. Often over time problematic behavior begins first, and then the customer value is affected. This is why an entire section is dedicated to customer behavior.

Bumbacher (2000) initiates investigations into this topic and identifies three groups of problematic customers: (1) troublemakers and benefit finaglers, (2) those not fully accountable and (3) potential lawbreakers.

One distinctive characteristic of **troublemakers and benefit finaglers** is that they make aggressive price demands that are completely disproportionate to the service purchased (Tomczak et al. 2000). These demands can be expressed as

stipulating close delivery dates, expecting additional service free of charge or being unwilling to participate in creating the service (Kleinaltenkamp and Ehret 2006). Another typical trait of troublemakers and benefit finaglers is their poor payment behavior (Gawantka 2006). A company expends a disproportional amount of its resources on the conditions posed by such customers, leading to a loss in customer value when the problematic behavior persists. And excessively dealing with such customers can result in less time and personnel available for other customer relationships, so the others are neglected. When this type of customer behavior occurs, the company should quickly decide the tolerance level for such behavior and determine when it would make sense to terminate the business relationship.

People who are temporarily limited in their ability to judge, communicate and act due to their mental state are considered to be **not fully accountable** (Bumbacher 2000). These people play only a minor role for business relationships between companies.

Potential lawbreakers are customers who act in a way that is counter to the law in business relationships. The bank robbers, thieves and vengeful persons that Bumbacher (2000) originally meant are not relevant in the context of business relationship management to industrial customers. The significance of this category increases however, when it includes customers or suppliers who violate or have violated anti-corruption laws. As many cases reported in the media have shown, maintaining business relationships with customers who even convey the appearance of being involved in corruption in their supply relationships can be seriously detrimental to a supplier company's chances of survival. For example, after the corruption scandals at the industrial service provider Ferrostaal AG in Essen became known on the spring of 2010, essential customers such as Thyssen-Krupp or the currency printer Giesecke-Devrient scrutinized or even terminated their business relationship with Ferrostaal (Fasse and Murphy 2010; Schmitt 2010).

5.4.1.3 Changed Fit Between Customer Needs and Supplier Service

A third reason for terminating a business relationship is when the customer's needs can be the result of changed customer needs or of different offerings by the supplier. An example of a supplier terminating a business relationship because of changed customer needs could be when the customer wishes to reduce his number of suppliers and thus requests a substantially wider delivery range from a previous B supplier who does not have the capacity to do this.

The second case often occurs when a supplier company chooses a new strategic focus. It can happen that the customer needs and the supplier services are no longer compatible when the main business purpose changes as well as in the event of divestment of corporate units/parts of the company that were essential to maintaining the respective business relationships. However, since such corporate strategy steps are decided at the highest level of a company's decision hierarchy, business relationship management plays only an executive and advisory role in this type of termination.

Regardless of which side of the fit of customer needs and supplier services has changed, this reason for termination of a business relationship is the least

problematic. The supplier may be the first to consider terminating the business relationship, but sooner or later the customer would also have recognized that a continuation is not in his best interest.

5.4.1.4 Consequences of Supplier Terminating a Business Relationship

A supplier terminates a business relationship for certain reasons. These reasons are ultimately of an economic nature, meaning that before termination of a business relationship, a positive effect on utilization of resources and thus on the company's success is anticipated. The improvement is to be achieved by using the resources previously expended for unprofitable customers or those who are difficult to serve to instead better satisfy profitable customers or to acquire new ones (Alajoutsijärvi et al. 2000; Johnson and Selnes 2004). The extent to which this increase in profitability is actually achieved and not depleted e.g. by costs incurred for disputes associated with terminated business relationships (Giller and Matear 2001) is ultimately strongly impacted by how exit management is implemented.

From the customer's viewpoint, termination of business relationships with undesired customers can trigger different reactions. The assumption thus far has been that this practice could lead to spiraling **negative word of mouth (WOM)** (Haenlein et al. 2006). Customers whose business relationship was terminated by the supplier could damage the supplier's reputation with negative propaganda. Amongst the supplier's current customers, this could cause some of them to terminate their business relationship with the supplier. And potential new customers may be more inclined to perform transactions and possibly enter into a business relationship with a competitor.

But on the other hand, exactly the opposite effect can happen: Existing customers perceive their supplier to be serious, increasing the resources expended for his profitable and valued customers. The few empirical studies that examined whether WOM has positive or negative effects for the supplier when the supplier terminates a relationship revealed that both occurred (Haenlein and Kaplan 2009, 2010).

5.4.2 Communication Strategies to Terminate a Business Relationship

When a company decides to end a business relationship, it is confronted with a choice of communication strategies. Falling back on research on dissolving personal relationships, Alajoutsijärvi et al. (2000) developed a typology of potential communication strategies, shown in Table 5.1.

They examine various communication strategies according to the dimensions of directness (indirect, direct) and interpersonal/interorganizational orientation (partner-oriented, self-oriented). Indirect strategies are those that do not explicitly communicate to the partner the wish to terminate the business relationship, but instead the supplier's behavior changes in a way that makes it apparent to the

Table 5.1 Communication strategies to terminate a business relationship

		Partner-oriented	Self-oriented
Indirect	Disguised exit	Pseudo de-escalation	Cost escalation, signaling
	Silent exit	Fading away	Withdrawal
Direct	Communicated exit	Negotiated farewell	Fait accompli, attributional conflict
	Revocable exit	Mutual state of relationship talk	Diverging state-of relationship talk
	Voice	Changing the relationship	Changing the partner

Source: Based on Alajoutsijärvi et al. (2000)

customer that a continuation of the business relationship is not desired. Indirect strategies can be either disguised or silent.

Pseudo-deescalation (partner-oriented) is when the supplier expresses to the customer the wish to change the business relationship but he actually means termination. This way he gives the customer's company and the negotiating person a way to save face. **Cost escalation** and **Signaling** are, on the other hand, self-oriented concealment strategies. Cost-escalations are one-sided supplier activities intended to make transactions so expensive or otherwise unattractive to the customer that the customer refrains from continuing the business relationship. The supplier can increase prices, invoice services previously provided free of charge, or change delivery conditions to payment in advance when the customer's poor payment behavior is a crucial reason for terminating the business relationship. In contrast, signaling means conveying to the company through third parties from the two companies' environment or through the media that the supplier is no longer interested in continuing the business relationship.

Fading away and withdrawal are two of the indirect, tacit communication strategies. **Fading away** means that both parties implicitly understand that the business relationship has ended, but neither party addresses it openly. The benefit of this solution is that there is no intention to harm the partner and the partner can save face. With **withdrawal**, the supplier expresses his intentions by changing his behavior. Less frequent and less open communication are signs of such an approach.

With direct communication strategies to terminate a business relationship, the object to be communicated—termination of the business relationship—is made explicit. If the supplier company intends by all means to end the relationship (communicated exit), this can happen either by communicating accomplished facts (fait accompli solution) or by a kind of **negotiated farewell**. In the first case, it is likely that culprits will be sought and blame placed, and that costly legal disputes regarding responsibility for and modalities of the termination will arise. For exactly this reason, some companies have begun to include an arbitration clause in their contracts when they enter into a business relationship. An arbitration court can settle disputes more quickly and less expensively than ordinary courts. But if both parties realize that dissolution of the business relationship is unavoidable, a negotiated farewell can save both parties time, money and bother.

If the supplier company is willing to maintain the business relationship despite a change in his business partner's behavior, the communication is considered a **revocable exit strategy**. Alajoutsijärvi, Möller and Tähtinen (2000) call the partner-oriented approach "*consensual discussions on the state of the business relationship*" (Alajoutsijärvi et al. 2000, p. 1275), because the purchaser attempts to include new insight on the customer in his assessment of the situation. In the case of **one-sided discussions on the state of the business relationship** on the other hand, the supplier without stating his motives asks his customer to change his behavior under threat of terminating the relationship.

In addition to indirect and direct communication strategies to terminate the business relationship, Alajoutsijärvi et al. (2000) include the voice strategy in their classification. The focus here is not on dissolution of the business relationship but on avoiding conflicts that have occurred in the business relationship. So it will not further occupy us at this point.

Which of these communication strategies a company should choose is strongly dependent on the external circumstances, on the reason for terminating the business relationship and on the potential consequences. These consequences affect the technical and legal course of the relationship as well as the ripple effect, which determines the manner in which the separation is perceived by third parties (other customers, cooperation partners, suppliers, employees, etc.). If a supplier has a limited number of customers, an elegant, partner-oriented termination is more important than for a supplier who has many customers. This also applies when the customer plays a relatively significant role in the supplier's network with his other business partners. Negative WOM that may result from a messy separation is weighted higher in this situation than when the relationship with an insignificant customer is terminated. When choosing between direct and indirect communication strategies, the cultural background of the companies involved plays an important role in regard to the effectiveness and consequences of the strategies. Especially in cultures in which it is essential to save face, indirect strategies are beneficial (Günthner 1993; Shi 2003). Another criterion in the decision on whether to pursue direct or indirect strategies is the urgency of termination: Only the direct alternatives ensure quick termination. If the supplier's corporate network is relatively small and close-knit, meaning that the acting persons will encounter one another again and again in various functions over the course of their professional lives—this is the case in the paper industry—partner-oriented communication strategies are more appropriate in that they minimize the negative reputation effects for all of the parties involved.

5.5 Business Relationships and the Corporate Network

Another task of business relationship management, in addition to phase-specific management of the business relationship itself, is the consideration of factors outside of the business relationship. The last section of this chapter deals with two types of such factors: influences between competing business relationships and

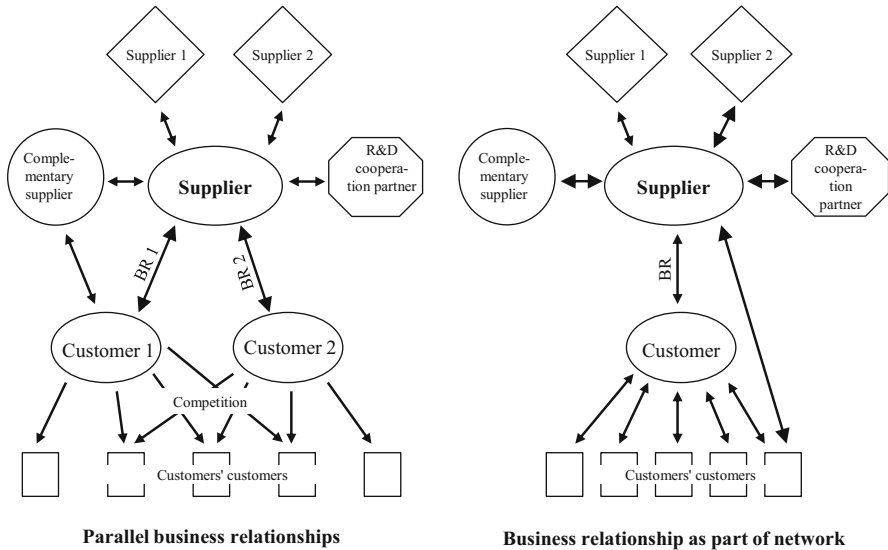


Fig. 5.7 Parallel business relationships and the business relationship as part of the network

the effect of network participants (cooperation partners, suppliers) in the business relationship examined. Figure 5.7 illustrates both cases.

5.5.1 The Business Relationship as Part of the Corporate Network: Handling Parallel Business Relationships

From a strategic perspective, three sets of issue play an essential role when examining parallel business relationships:

- Prioritization of customers/business relationships when resource bottlenecks occur
- Protection of relationship-specific values
- Decision on either/or business relationships

These will be explained in detail.

5.5.1.1 Prioritization of Customers When Resource Bottlenecks Occur

As we saw in the discussion on a supplier terminating business relationships, the decision on priority handling of business relationships is significant for the supplier company’s efficiency of resource utilization. Basically, the business relationships of the greatest value to the company should be granted the most time and effort.

For standard operation, meaning regular business without great environmental impact, internal segmentation of business relationships makes sense. The

segmentation determines how much attention a customer should generally receive. Segmentation can be founded e.g. on an ABC analysis (Chap. 4) based on CLV or the contribution margin. Depending on the homogeneity of the customer structure, it may be beneficial to take into consideration certain specifics of the customer's industry when allocating resources. So for a machine tool manufacturer it may make sense to give the same care to a medium-sized customer in the chemical industry with a high need for customization as to a very large automotive customer with a high customer value and low customization. Without the business e.g. of the chemicals customers, the company would record a loss, while the automotive customers ensure secure, long-term capacity utilization. Competitive relationships at the company's own market stage as well as at the customer's market stage should be taken into consideration when prioritizing individual customers.

A special situation can occur in regard to handling parallel business relationships when a company experiences a bottleneck for its own core service at the purchaser level. This was the case, for example, on the global market for industrial gas turbines and compressors from 2006 through 2008. Because of capacity bottlenecks in manufacturing, customers who wished to purchase these capital goods had to wait over 2 years for delivery of their orders. A similar phenomenon could be observed in the market for high-purity silicium, the basic material used to produce photovoltaic cells, where the demand soared to an unprecedented level. Following the global financial crisis in 2007–2009, many suppliers to the automobile market were not capable of meeting the leap in demand that came in 2010–2011. In such a situation, a supplier is faced with the decision of how much of his service he offers to which customers.

Prioritizing customers when there is a bottleneck of the core service requires especially prudent behavior. It is particularly crucial that the method chosen promotes understanding for the supplier's behavior on the part of the most important customers during and after the bottleneck, so the business relationships are not harmed. Customers should feel that they are being treated fairly. So short-term opportunistic utilization of a temporary advantage in the supplier market is usually ruled out.

Figure 5.8 shows our suggestion for a prioritization process that is as consistent as possible for all customers and applies the same decision-making criteria. These criteria can include the (higher) price for the core service, consideration of certain clauses in existing contracts, the customer value (CLV), the duration of the business relationship so far, the customer's willingness to make relationship-specific investments or certain external factors.¹ When a supplier begins negotiating greater delivery quantities with his various customers, these previously specified criteria

¹ This would be the case in the event of a global epidemic like swine flu in the winter of 2009/2010, when a large quantity of vaccine has to be produced in a very short time and the vaccine manufacturers were dependent on a shortage of primary product for their production. The manufacturer of the primary products could not afford to apply different criteria to serving his customers in such a situation; public pressure would force him to grant priority delivery to the vaccine producer.

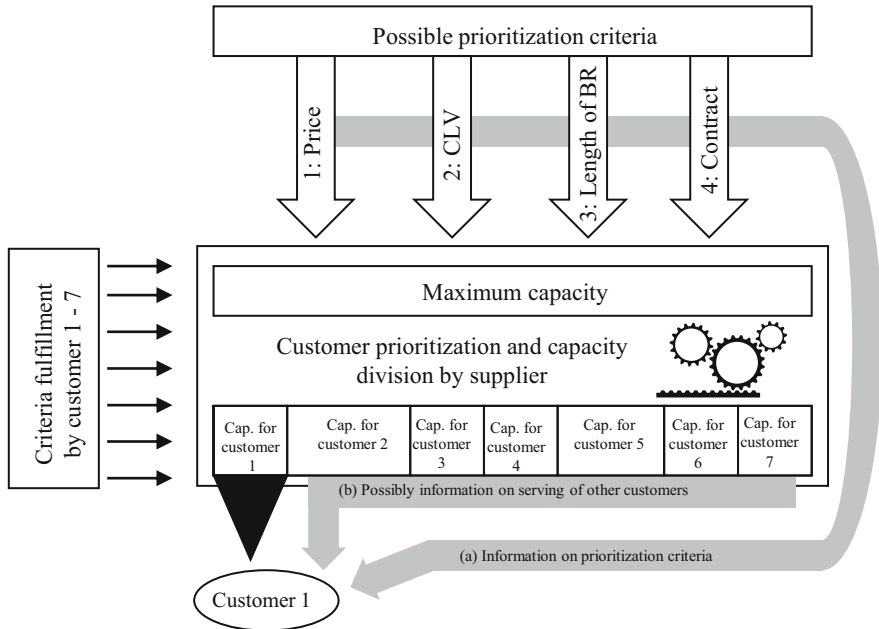


Fig. 5.8 Prioritization for temporary supply bottlenecks

should serve as the guiding principles for the supplier and should always be complied with. Depending on the extent to which a customer meets the respective criteria (left side of the illustration), he should receive more or less of the requested core service (center of the illustration).

To ensure that the customer perceives that he is being dealt with fairly (Kumar et al. 1995) and that despite the fundamentally unsatisfactory situation the customer is ultimately being satisfied, the applied prioritization criteria should be revealed. Then the customer can understand why he was being treated the way he was. When there is greater market transparency, it may be beneficial to explicitly explain the degree to which the quantities demanded by other customers were satisfied, giving the customer a means for comparison. Both measures are intended to diminish customer expectations and to ultimately make the customer more satisfied with his own treatment (Churchill and Surprenant 1982).

5.5.1.2 Protection of Relationship-Specific Values

One feature of particularly intense business relationships is that often values are created that are beneficial to both partners in the business relationship but that are also of use to at least one of the partners—often the supplier—in other business relationships. This is the case, for example, when a pulp producer works with a selected paper manufacturing customer, having a joint engineering team optimize his manufacturing process and paper machines such that the paper manufacturer realizes significant savings in the production process. Often a contract is written up,

specifying that such savings are shared by the partners involved. So for the pulp manufacturer, the savings are an additional source of revenue. In addition, after the project the supplier could attempt to use the knowledge on the production process gained in cooperation with this one customer in other business relationships with the customer's competitors. This is of course not in the customer's best interest. Taking into consideration the cost of the project, the customer would only agree to the project if the supplier assures him credible exclusiveness. The know-how obtained through the cooperation should remain exclusively in this business relationship, at least for a certain time.

A supplier of industrial goods and services will usually have to implement both external and internal measures to achieve this. The effectiveness of the measures determines whether or not his customers will agree to such value-generating projects.

External measures are all those that the supplier takes at the company's boundaries, particularly in regard to the customer. The primary measure is the respective cooperation contract, which clearly specifies the partners' rights and obligations, whereby special attention is paid to the intellectual property generated by the cooperation. For example, it should be determined who the owner is of patentable inventions. It is also common practice to have all employees involved in the project sign non-disclosure agreements (NDA) covering all customer and project information. Another measure could be information technology barriers, designed such that the supplier's personnel can only gain access to the customer's IT systems to the extent that is essential to the project.

Depending on the type of business, an internal measure could be construction of so-called Chinese walls, imaginary boundaries for information available in different parts of the company but that should under no circumstances whatsoever be brought together. This is the case e.g. in the banking sector or with consulting firms when the supplier has two competing customers. Internal grace periods before employees can change jobs are also internal measures.

5.5.1.3 Either/or Business Relationships

In rare cases suppliers who do business primarily within business relationships are faced with a difficult choice: The business relationship with customer 1 precludes a continuing relationship with customer 2, because 1 and 2 are fierce competitors. If this is to be feared, the supplier is faced with the competitive strategic task of choosing one of the two business relationships. Not only criteria related to customer value should be considered, all elements of the strategic analysis should be examined. The environmental relations of the potential business relationships as well as the effects on competitors and on current and potential customers should be assessed.

5.5.2 The Corporate Network as Part of the Business Relationship: Value Creation Through Collaboration

With the development of modern marketing concepts, there has been a transition from the sale of products to the offering of solutions in many industrial goods markets (Cova and Salle 2008). Because many companies have evolved from product sellers to solution providers, the significance of other participants in the companies’ environment has shifted: The company in question can contribute many of the competencies required for the solution only through cooperation with other value-adding partners. Thus the company’s network takes on a more and more significant role for its own customer relationships. In a paper on the state of business relationship management, Hunt et al. (2006) go as far as to state the following: “*Network competition best describes the current situation in the auto industry*” (p. 75). Similar tendencies can be detected in the textile, telecommunications and energy sectors (Kleinaltenkamp and Ehret 2006).

The partner network has two central functions for a supplier company: First, it impacts the company’s innovation capacity (Gemünden et al. 1996). This is reflected in the business relationships to the supplier’s customers by a greater customer benefit resulting from improved products and processes. Second, the network significantly affects the ability of a supplier to establish business relationships in an unknown market (Holm et al. 1999).

5.5.2.1 Partnerships for Innovations

The various types of innovation partners are shown in Fig. 5.9.

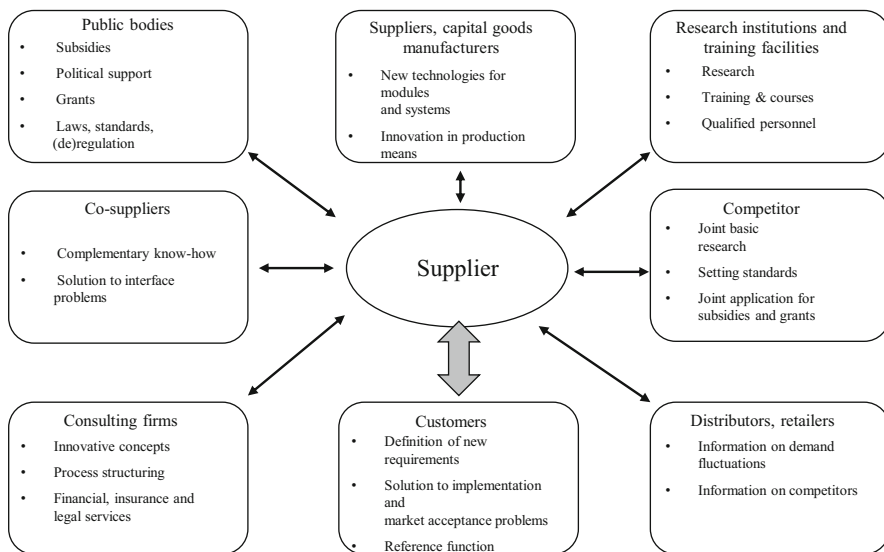


Fig. 5.9 Network partnerships and their contribution to a business relationship. Source: Based on Gemünden et al. (1996)

As we can see, a company can look in many very different directions to find the right partners to help strengthen its own business relationships. Following the illustration clockwise, these include **consulting firms and pure service providers**. With their professionals ranging from consulting engineers and economic and tax consultants to financial advisors, market researchers and management consultants, they can cover any facet of consulting services needed. They contribute innovative concepts, such as transfers from other industries. Sometimes it is their services that make customer benefit in a business relationship feasible in the first place. In a collaboration between AKP Electrical, a manufacturer of control technology and equipment for power supply and transmission, and the Metaglas plant in Bagnols (France), AKP was only successful in getting a large order for the complete overhaul of the power supply to the Metaglas factory because the company cooperated with the engineering firm Rossi. It was only by working together that they were able to convince Metaglas of the necessity of overhauling and then present the offer that Metaglas chose (Cova and Salle 2008).

Co-suppliers contribute to a company's innovation capacity by integrating complementary services previously supplied separately and combining them to form superior comprehensive services. An example: To strengthen its own business relationships with customers from the paper industry, the BASF AG business unit Paper Chemicals has been working closely since 2003 with the pigment manufacturer Omya and the paper machine manufacturer Voith, both of which have similar customers. The goal is to improve the paper quality and reduce the manufacturing costs for the customer (Fasihi 2003). Example 7 also demonstrates how cooperative technology development increases value for the customers and the companies involved.

Example 7: Brushes and Rollers No Longer Needed for Facades

Despite mechanization in many construction-related fields, many tasks have remained in the realm of manual labor, such as painting building facades. This has traditionally been done with brushes and rollers, which—taking into consideration the rising cost of labor—offers a great potential for savings. Because of side effects resulting from different sized droplets, spray systems had not yet been able to penetrate the market.

All of this was to change with the Nespri system, winner of multiple awards since 2005. The system was developed in a cooperation between the painting equipment manufacturer J. Wagner GmbH and the largest European building paint manufacturer Caparol. With its innovative pump and nozzle technology, the new system achieves an optimized droplet size—the result of “airless atomization.” The atomizing device and the paint are precisely attuned to one another. The advantages of this system are: uniform application of the paint; no spray mist emissions and little effort required for full

(continued)

coverage; high working speed and ergonomic working posture; little waste; and significant overall savings for the customers in the handicraft industry.

Because of the system lock-in—the basic equipment costs about EUR 7,000—Wagner as well as Caparol achieved much greater customer loyalty in the handicraft industry. This would not have been possible with the old technology (roller and brush). The substantial customer benefits make collaborative tapping of global markets appear realistic. And both partners benefit from the sharing of know-how as well as from more efficient sales achieved by dovetailing their distribution channels (Garber 2007).

Public bodies can also act as partners in a network. This has to do with political support for the development of new technologies on the one hand. But it can also mean the establishment of business relationships into new markets, potentially granting a supplier greater credibility. The case of the Swedish telecommunications manufacturer Ericsson, who decided to work on a Japanese standardization committee in order to establish a business relationship with the Japanese cellular service provider Tokyo Digital Phone (Holm et al. 1999) is an example of how public entities can be used as partners.

Technological cooperation as partners with one's **own suppliers** is a classic case in the automotive industry. Since OEMs have drastically reduced their number of suppliers over the last 20 years, the direct suppliers now have to cover a much wider range of offerings. To be able to offer their customers innovations, they are forced to become partners in innovation collaborations with their own suppliers. Without the collaboration between Hella (supplier of headlight systems) and Osram (manufacturer of illuminant systems) it is hard to imagine that the diode lamp would ever have been developed.

Collaboration between companies and **educational and research facilities** can be beneficial from a technological as well as a management perspective. From a technological perspective, cooperative research at universities or other research facilities (an example in Germany is the Fraunhofer-Institut) can offer a less expensive or better way to develop technology, which in turn strengthens existing business relationships. Examples of such collaborations are the T-Labs of Deutsche Telekom with the Technische Universität Berlin, and Siemens' cooperations with the Technische Universität Munich and the Universität Linz. It may also be beneficial to conduct training sessions and further education offerings with a fixed higher education partner (Alajoutsijärvi et al. 2000) who may be able to give training geared towards the specific business relationship.

Even collaborations with **competitors** as partners can make sense and have significant impact on one's own business relationships. This necessity becomes particularly apparent when new standards have to be set in a market with direct or indirect network effects (e.g. telecommunication, transport, IT software) (Hardenacke 2005). Fundamental research and tapping a market new to both parties are ways to potentially collaborate with competitors.

Finally, distributors such as logistics service providers and commercial enterprises should be named as potentially important sources of information on customers and competitors.

5.5.2.2 Partnerships for Market Access

While partnerships focusing on innovation are primarily intended to strengthen existing customer relationships, partnerships for tapping new markets are established with the intention of entering into new business relationships.

There are various types of reasons for such partnerships. When entering a market in a new country, **legal aspects** often play a vital role. In China and in some Mideastern countries (Qatar, Oman), a foreign corporation cannot found a local company in which it holds 100 % of the shares. Instead, it must establish a joint venture with a local partner if it intends to do more than simply export to the country. The problem is similar when national legislation dictates local content laws, meaning that a certain proportion of a final product must originate in the respective country. In the automotive industry, for example, this regularly means that European suppliers to European OEMs are forced to cooperate with local partners when they enter foreign markets (China, India, South Africa). This was the case for BOD Defense, manufacturer of military systems and its European partners SPP and TBC, who formed local partnerships, such as that with the University of Sydney, to be able to establish a business relationship with the Australian armed forces (Cova and Salle 2008). Local content requirements were an issue here, too.

But even when legal requirements do not force such relationships, cooperation with local partners can be beneficial for **cultural reasons**. In the example mentioned above, where Ericsson and Tokyo Digital Phone established a business relationship to construct and operate cellular phone infrastructure, the customer had reservations about Ericsson's ability to provide enough qualified employees with the required language skills. This is why the customer required that Ericsson find a Japanese partner, which ended up being Toshiba (Holm et al. 1999).

Exercises

1. Which are the different generic strategy options to achieve a competitive advantage?
2. What is the difference between a competitive strategy and a marketing strategy? How can strategic decisions be categorized in business relationship management?
3. Name and explain the components that make up the competitive advantage!
4. Explain potential time perspectives of the competitive advantage at the beginning of a business relationship from the supplier's viewpoint!
5. Explain the three-phase concept of business relationship management and compare it to other phase concepts in marketing!
6. Discuss the term "strategic window"!

7. How can supplier offerings be classified by the potential to reduce uncertainty? Which strategies for reducing uncertainty are available to the customer?
8. State and explain the individual ways in which a supplier can increase the relationship value for a customer!
9. Differentiate between direct switching costs and switching costs related to relationship-specific investments! From the supplier's perspective, how can they be increased?
10. Which central reasons for a supplier to terminate a business relationship have you learned about? Describe the consequences of such a termination for the supplier and for the customer!
11. Explain the direct and indirect communication strategies available to a company to terminate a business relationship!
12. How can customers be prioritized in the event of temporary supply bottlenecks such that they feel they are being treated fairly?
13. Name and explain the different types of innovation partners available to a supplier company within his network!

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Business Relationship Management and Marketing in a European-Chinese Context

6

Alexander Tirpitz and Miaomiao Zhu

6.1 Introduction

Since the Chinese government started its *Going Global Policy* (*zou chu qu* 走出去) in 2001, Chinese companies have become an important and increasingly visible source of foreign direct investment (FDI) in the world (UNCTAD 2006, 2010). In 2011, Mainland China had estimated global outward FDI stocks of over 365 billion USD and FDI outflows of over 65 billion USD. Compared to the almost 400 billion USD of FDI outflows from the United States it might seem negligible, but it is already significantly more than Germany's FDI outflows of 54 billion USD in 2011 (UNCTAD 2012, p. 169 ff.). Moreover, a survey of UNCTAD among Investment Promotion Agencies (IPA) revealed that China was regarded as the most promising investor home economy for global FDI in 2012–2014 (UNCTAD 2012, p. 21). In consequence, Chinese firms become integral business participants in developed Western economies. Thus, Western management executives are increasingly challenged with building and sustaining business relationships with Chinese players not only in China but also outside of China, e. g. in the European Union (EU). At the same time, Chinese firms need to adapt to the cultural environment of these countries and the way business is conducted, as Western firms had to do earlier when entering the Chinese market.

Business behavior of Chinese refers to cultural rules and norms mainly rooted in Confucianism. One of these cultural rules is the strong reliance on personal relationships, also known as *guanxi*. As a mixture of personal and professional relationships implying certain obligations, *guanxi* determines success in private as well as in business and influences the way Chinese perceive business relationships (Yang 1994). But *guanxi* is not the only factor influencing the behavior of Chinese in business: From a more holistic perspective Confucian values as outlined in the

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book of rites and the commonly known strategic wisdom of Chinese military strategists like Sunzi (*sunzi bingfa*—The Art of War by Sunzi; for an English translation see Sun Tzu et al. (1963)) and Tan Daoji (*sanshiliuji. miben bingfa*—36 stratagems: the secret book of the art of war; for a German discussion of the 36 stratagems see e.g., Senger (1992)) do also play an important role.

The Western approach to business relationships is comparatively clinical and rationality-oriented (Wong and Leung, 2001). Assumptions, expectations and behavioral patterns of Chinese and Western businessmen hence differ heavily. Since Casnir (1999, p. 107) states that changes or adaptations on the part of all participating individuals are prerequisite for meaningful and mutually beneficial intercultural communication, this chapter outlines major cultural differences between European countries and China as well as their respective business cultures and provides approaches to the management of European-Chinese business relationships.

6.2 The Role of Culture in Business Relationships

6.2.1 What Is Culture?

In order to understand the impact of culture on business relationships, it is important to have an understanding of what culture is. Culture can best be understood as “*a giant, extraordinary complex, subtle computer. Its programs guide the actions and responses of human beings in every walk of life.*” (Hall and Hall 1990, p. 3). Hence, culture can be referred to as the “*software of the mind*” (Hofstede and Hofstede 2009, p. 3).

Three layers of culture are commonly distinguished (Schein 1983, 2010):

- Artifacts (e.g., behavior or explicit hierarchies)
- Espoused values (e.g., norms and rules)
- Underlying basic assumptions (views of the world etc.)

Whilst artifacts are easily observed and espoused values can be figured out, it is much harder to understand the underlying assumptions of a specific culture. Therefore, different researchers (e.g., Kluckhohn and Strodtbeck 1961; Hofstede 2001; House et al. 2004) derived cultural dimensions displaying these basic assumptions. In the following section some of these approaches are outlined and implications for business practice are derived.

When talking about European-Chinese business relationships, not only the national culture of China but also the organizational culture of our business partners is of interest to us.

Organizational culture, then, is the pattern of basic assumptions that a given group has invented, discovered, or developed in learning to cope with its problems of external adaptation and internal integration—a pattern of assumptions that has worked well enough

to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think, and feel in relation to those problems. (Schein 1983, p. 14).

With regard to external adaptation we need to bear in mind that Chinese enterprises, especially the ones located in the developed regions of the Chinese East coast and the special economic areas, are increasingly influenced by Western business values and practices. In consequence, business practice is changing and Chinese subordinates in the aforementioned areas, for instance, tend to prefer cooperative leadership rather than the traditionally applied paternalistic style (Waldkirch 2009).

Hence, the subsequently presented concepts on cultural dimensions, which help to identify the underlying basic assumptions, provide general guidance. However, since these concepts concentrate on national culture, their relevance for a particular business relationship might differ from case to case.

6.2.2 Concepts of Culture and Cultural Distance

Various attempts to categorize cultures according to specific dimensions have been undertaken so far. An early attempt that has been used as a basis for many others is the social anthropologist approach of Kluckhohn and Strodtbeck (1961) that outlines six basic value orientations in which cultures differ:

- Relationship to nature
- Beliefs about human nature
- Relationship between people
- Nature of human activity
- Conception of space
- Orientation of time

Among the more business-oriented attempts to reveal global cultural differences Hofstede's (2001) study on cultural dimensions and the more recent GLOBE project (e. g. Chhokar et al. 2007; House et al. 2004) received outstanding attention in research and in practice. Therefore, we are going to focus on these two concepts in order to point out major differences between Europeans and Chinese and derive managerial implications for business marketing. Further, we will take the work of Hall (Hall 1973; Hall and Hall 1984, 1990) on intercultural communication into account.

6.2.2.1 Hofstede's Culture's Consequences

Hofstede's model consists of five cultural dimensions. Each of these five dimensions represents a universal value orientation that can be specified for different national cultures. The first four dimensions (Power Distance, Masculinity, Individualism, Uncertainty Avoidance) were derived from a large-scale survey among employees of IBM subsidiaries in different countries. The fifth dimension (Long-term Orientation) that derived from the Chinese Value Survey was added

later in order to account for general differences in the underlying value concepts of Eastern and Western cultures (Hofstede and Hofstede 2009).

- Power Distance (PDI) is the extent to which the less powerful members of institutions and organizations within a specific national culture expect and accept that power is distributed unequally (Hofstede 2001; Hofstede and Hofstede 2009).
- Individualism (INV) is the degree of interdependence maintained among the members of a specific society (Hofstede 2001; Hofstede and Hofstede 2009).
- Masculinity (MAS) measures in how far gender roles within a specific culture are clearly distinct with men being assertive and achievement oriented and women being rather humane and relationship oriented (masculine) or if men and women are both expected to be humane oriented and less assertive (feminine) (Hofstede 2001; Hofstede and Hofstede 2009).
- Uncertainty Avoidance (UAI) accounts for the extent to which members of a specific culture feel threatened by ambiguous or unknown situations and have created beliefs and institutions that try to avoid these (Hofstede 2001; Hofstede and Hofstede 2009).
- Long-term Orientation (LTO) is defined as the extent to which a society shows a pragmatic future-oriented perspective rather than a past-oriented or present-oriented short-term point of view (Hofstede 2001; Hofstede and Hofstede 2009).

6.2.2.2 GLOBE Study

The more recent GLOBE (Global Leadership and Organizational Behavior Effectiveness) (House 2006; House et al. 2004) project used Hofstede's dimensions, but also extended them to the following:

- Individualism-Collectivism is separated into two individual dimensions:
 - Institutional collectivism: *“degree to which organizational and societal institutional practices encourage and reward collective distribution of resources and collective action”* (House et al. 2004, p. 30)
 - In-group collectivism: *“degree to which individuals express pride, loyalty and cohesiveness in their organizations or families”* (House et al. 2004, p. 30)
- Masculinity has been substituted by
 - Assertiveness: *“degree to which individuals in organizations or societies are assertive, confrontational, and aggressive in social relationships”* (House et al. 2004, p. 30)
 - Gender egalitarianism: *“extent to which an organization or a society minimizes gender role differences”* (House et al. 2004, p. 30)
- Humane orientation: *“degree to which individuals in organizations or societies encourage and reward individuals for being fair, altruistic, friendly, generous, caring, and kind to others”* (House et al. 2004, p. 30)
- Future orientation: *“degree to which individuals in organizations or societies engage in future-oriented behaviors such as planning, investing in the future, and delaying gratification”* (House et al. 2004, p. 30)

- Performance orientation: “*extent to which an organization or society encourages and rewards group members for performance improvement and excellence*” (House et al. 2004, p. 30)

Much more interesting than the fact that GLOBE identified further dimensions, is the project’s approach to ask for values (*Should Be*) as well as for practices (*As Is*). For China this revealed, for instance, large discrepancies concerning the actual (practice) Power Distance and as it should be (value). This indicates that Chinese managers are rather tolerant towards unequal power distribution in society, but do call for more equality anyway. The GLOBE authors (Fu et al. 2007) do explain this by the internal (traditional Chinese values) and external forces (Western influences) contemporary China is facing. Thus, Chinese managers seem to undergo changes in their value orientations that have to be taken into consideration for European-Chinese business relationships, as well.

6.2.2.3 Use of These Models

Somehow appearing in all of these frameworks, *individualism-collectivism* and *power distance* seem to be dimensions with an outstanding notion in understanding cultural variations (Thomas 2008).

The dimension *individualism-collectivism* has been broadly discussed and received utmost attention by many researchers (Berry et al. 2011; Genkova 2012; Singelis et al. 1995). As Pornpitakpan (1999) shows, this dimension or its representation in a certain culture respectively is also important for the perception of adaptive behavior within intercultural business relationships. Following his findings, collectivist cultures might perceive a high degree of adaptation of their business partners as positive, individualist cultures as rather negative. In consequence, an adaptive approach to business relationships is more likely to be successful for Westerners, whereas Chinese should avoid too heavy adaptation.

An extension of the *individualism-collectivism* dimension, that needs to be considered in the context of business relationships with Chinese, is furthermore the one of *horizontal* and *vertical individualism* or *collectivism* respectively (Singelis et al. 1995).

Vertical collectivism includes perceiving the self as a part (or an aspect) of a collective and accepting inequalities within the collective. Horizontal collectivism includes perceiving the self as a part of the collective, but seeing all members of the collective as the same; thus equality is stressed. Vertical individualism includes the conception of an autonomous individual and acceptance of inequality. Horizontal individualism includes the conception of an autonomous individual and emphasis on equality (Singelis et al. 1995, p. 240).

Not identically but rather similar is GLOBE’s distinction between *societal* and *in-group collectivism*. Considered together with the representation of the *power distance* dimension in all the above-cited models, different European and Chinese understandings of how resources and power should be distributed can be revealed. In intercultural business relationships variations in these cultural dimensions might

Table 6.1 Outline of potential cultural impacts on business relationships

Hofstede	GLOBE	Potential impact on . . .
Collectivism vs. individualism	Institutional collectivism	Status of buyer and seller Perception of degree of adaptation (Pornpitakpan 1999)
	In-group collectivism	
Power distance	Power distance	Status of buyer and seller
Long-term orientation	Future orientation	Perception and understanding of success in a business relationship
Uncertainty avoidance	Uncertainty avoidance	Instruments applied in business relationships (e.g., contracts)
Masculinity vs. femininity	Gender egalitarianism	Status of women in business Competitive vs. cooperative attitude towards business relationships Negotiation behavior (Lügger et al. 2014)
	Assertiveness	
	Performance orientation	
	Humane orientation	

Source: Based on Rothlauf 2012

lead to different roles, status allocations and performance expectations among buyers and sellers.

The following table puts the dimensions of Hofstede and GLOBE in relation to each other and outlines potential impacts on European-Chinese business relationships (Table 6.1).

In addition, based on Hofstede's cultural dimensions, the cultural distance between to cultures can be assessed by means of an index (Kogut and Singh 1988; Shenkar 2001). Admittedly, the cultural distance index is only meaningful as a very broad comparison at the national level and care has to be taken in its interpretation (Thomas 2008). However, it has been shown that cultural distance, e.g., has an impact on the choice foreign market entry mode (Kogut and Singh 1988). Furthermore, the index indicates a large cultural distance and hence many potential pitfalls within European-Chinese business relationships.

However, as Casmir (1999, p. 101) states:

Nowhere did such conceptual models explain or help us understand how, why and when individuals overcame their differences in actual intercultural dialogic interactions.

Thus, these models should serve as a starting point for understanding cultural differences. Situational and individual factors of the actual business relationship, e.g. industry norms or the educational background and personal experiences of the interacting managers need consideration. As already stated above, Chinese businesspeople are increasingly influenced by Western business practices in terms of international standards, regulations, etc. Western practitioners doing business with China are often provided with cross-cultural training or coaching by their companies. Furthermore, Western businesspeople increasingly emphasize relationships and cooperation and seem to move in the direction of Guanxi-type

systems throughout the twenty-first century (Lovett et al. 1999). However, differences will certainly remain and rapid cultural convergence must not be expected (Ronen and Shenkar 2013).

6.2.3 Cross-Cultural Communication

Since “*Culture is Communication*” (Hall and Hall 1990, p. 3) it is not only important to understand universal cultural value orientations and differences deriving from these as outlined above. It is furthermore essential to be aware of different communication patterns applied by Westerners and Chinese.

Hall and Hall (1990) propose to divide communication into three parts:

- Words as the medium of business, politics and diplomacy
- Material things as indicators of power and status
- Behavior representing people’s feelings and techniques for avoiding confrontation

This division of communication indicates that not only the spoken word but also material things and behavior have to be taken into account when interpreting communication, especially in an intercultural context. Therefore, Hall and Hall (1990) point out that communication differs between cultures with regard to the following aspects.

6.2.3.1 High Versus Low Context

Most Western cultures can be defined as being cultures of low-context communication, whereas China is one of high-context.

A high-context (HC) communication or message is one in which most of the information is either in the physical context or internalized in the person, while very little is in the coded, explicit, transmitted part of the message. A low-context (LC) communication is just the opposite; i.e., the mass of the information is vested in the explicit code. Twins who have grown up together can and do communicate more economically (HC) than two lawyers in a courtroom during trial (LC), a mathematician programming a computer, two politicians drafting legislation, two administrators writing regulation, or a child trying to explain to his mother why he got into a fight. (Hall 1989, p. 91).

The different positions Westerners and Chinese hold on the high-low-context-continuum do regularly show in business meetings or negotiations. While Western European executives, especially Germans, tend to communicate in a very direct, explicit way, Chinese do usually communicate rather implicitly, indirectly. For instance, Chinese would never express criticism or the refusal of an offer directly, but indirectly by stopping the negotiation or simply not getting back to the potential business partner. This behavior can be explained by traditional Chinese values like *harmony* and *face*, which will be outlined below.

6.2.3.2 Space

The perception of space is also determined by culture. Space and related boundaries begin with an individual's physical boundary (skin), continue with one's personal space and end with one's territory.

Territoriality is especially developed in the Germans who tend to occupy places and possessions and label them "mine". Furthermore, in business, e. g., office space indicates power and status.

The personal space of a person, usually described as an invisible bubble around him or her, determines how much distance people keep from each other. A Penetration of this private zone makes people feel uncomfortable or even being offended. For Northern Europeans this comfort zones is generally quite large, whereas it is much smaller in the South of Europe as well as in Asia. Moreover, space does also include auditory, olfactory, thermal or kinesthetic screening and not only visual. For instance, Germans tend to feel easily disturbed by loud noise, whereas this is usually not the case for Chinese.

In consequence, the appropriate distance that has to be kept to strangers and business partners differs significantly and executives have to be aware of the communicative notion of space in order to avoid misinterpretations (Hall and Hall 1990, p. 10 ff.). For instance, Chinese tend to avoid body contact like handshakes or hugs, but they do usually not feel uncomfortable if they have to stay close to strangers in an elevator or public bus. Contrary, Western Europeans tend to feel rather uncomfortable in a crowded elevator or bus, but are usually used to body contact with acquaintances, friends and family members.

6.2.3.3 Time

According to Hall and Hall (1990) especially the cultural determined time systems of monochronic and polychronic time are relevant to international business.

In monochronic cultures, time is experienced and used in a linear way - comparable to a road extending from the past into the future. Monochronic time is divided quite naturally into segments; it is scheduled and compartmentalized, making it possible for a person to concentrate on one thing at a time. In a monochronic system, the schedule may take priority above all else and be treated as sacred and unalterable (Hall and Hall 1990, p. 13).

Northwestern European countries like Germany are monochronic cultures. And everyone who attended business meetings with Germans knows that they do highly appreciate punctuality and strict schedules. In contrast, Asian cultures like China are polychronic time systems.

Polychronic time is characterized by the simultaneous occurrence of many things and by a great involvement with people. There is more emphasis on completing human transactions than on holding to schedules. For example, two polychronic Latins conversing on a street corner would likely opt to be late for their next appointment rather than abruptly terminate their conversation before its natural conclusion. Polychronic time is experienced as much less tangible than monochronic time and can better be compared to a single point than to a road (Hall and Hall 1990, p. 14).

Table 6.2 Patterns distinguishing monochronic and polychronic time systems

Monochronic people	Polychronic people
Do one thing at a time	Do many things at once
Concentrate on the job	Are highly distractible and subject to interruptions
Take time commitments (deadlines, schedules) seriously	Consider time commitments an objective to be achieved, if possible
Are low-context and need information	Are high-context and already have information
Are committed to the job	Are committed to people and human relationships
Adhere religiously to plans	Change plans often and easily
Are concerned about not disturbing others, follow rules of privacy and consideration	Are more concerned with those who are closely related (family, friends, close business associates) than with privacy
Show great respect for private property, seldom borrow or lend	Borrow or lend things often and easily
Emphasize promptness	Base promptness on the relationship
Are accustomed to short-term relationships	Have strong tendency to build lifetime relationships

Source: Based on Hall and Hall (1990)

The following table contrasts monochronic and polychronic time systems by exemplifying aspects of the respective behavioral patterns (Table 6.2).

Thus, when communicating in a cross-cultural setting the involved parties have to be aware of the culturally determined frame of references of either party. Drawing on different aspects of (cross-cultural) communication, Browaeys and Price (2011) suggest a model of cross-cultural communication that takes into account the knowledge, experience, norms and values and assumptions as the frames of reference of the communicating parties. Furthermore, they outline four key communication filters (verbal and non-verbal language, style of thinking and communicating, stereotypes, relationships), which influence the way an intended message is received by either party. Consequently, it is not only necessary to understand basic assumptions, norms and values, and communication patterns, but also the notion of relationships (Fig. 6.1).

6.2.4 Cultural Differences Between Europe and China

In a European-Chinese business context several cultural differences occur, especially when we take into account that there is not one European culture, but several national cultures to be considered. Figure 6.2 depicts cultural differences between selected European countries and China as scored on the Hofstede dimensions.

For Germany and China this reveals big differences in the underlying basic assumptions that manifest in values and artifacts. While we have the same score in Masculinity (MAS), there are big differences in all the other dimensions:

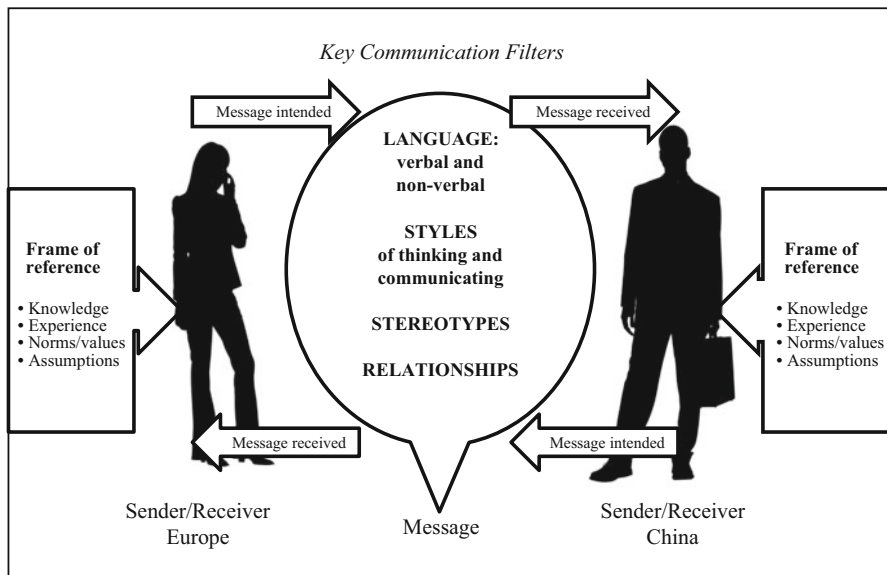


Fig. 6.1 Model of cross-cultural communication. Source: Based on Browaeys and Price (2011, p. 276)

- Germany scores rather low in Power Distance (PDI), China rather high.
- Germany scores rather high in Individualism (INV), China rather low.
- Germany scores rather high in Uncertainty Avoidance (UAI), China rather low.
- Germany scores rather low in Long-term Orientation (LTO), China extremely high.

Despite the differences between the Chinese culture and the selected European ones, the Hofstede scores do also reveal the aforementioned substantial differences between these European national cultures. The GLOBE study even identified different cultural clusters within Europe (Chhokar et al. 2007, p. 13), which share similar values: Nordic Europe (Denmark, Finland, Sweden), Germanic Europe (Austria, Germany, Netherlands, German-speaking Switzerland), Eastern Europe (Albania, Georgia, Greece, Hungary, Kazakhstan, Poland, Russia, Slovenia) and Latin Europe (France, Israel, Italy, Portugal, Spain, French-speaking Switzerland). Hall and Hall (1990) do also describe certain differences in the way, for instance, Germans and French communicate even though they are neighboring countries. Chinese doing business with Europeans need to be prepared to find different cultural settings in each country and not one common European culture. Europe shares historical events and a common cultural basis, e.g. Romanic language roots. At the same time there is also a wide range of separating historical events, like World War I and World War II, leading to different self-perceptions and basic assumptions.

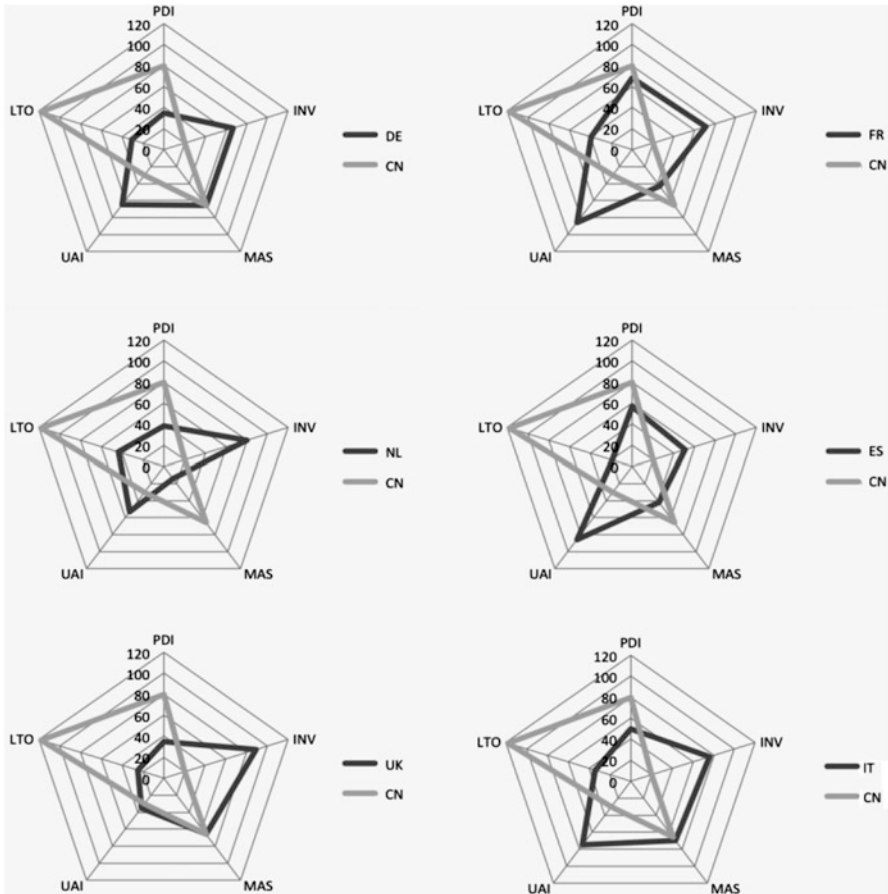


Fig. 6.2 Comparison of selected European countries and China based on the Hofstede dimensions (DE Germany, FR France, NL Netherlands, ES Spain, UK United Kingdom, IT Italy). Source: Based on Hofstede 2001

Furthermore, the GLOBE study (Chhokar et al. 2007; House et al. 2004) helps us to better understand changes occurring in European and Chinese cultures, since not only practices (*As Is*) but also Values (*Should Be*) have been measured. In some dimensions this reveals huge discrepancies and hence recent changes in cultural aspirations. The following figure depicts the GLOBE scores for China and for Germany (West) as one of the major economies in Europe (Fig. 6.3).

By comparing the *As Is*- and *Should Be*-scores for Germany, Brodbeck and Frese (2007) come to the conclusion that German managers “would like to get rid of the many rules, regulations and constraints” (p. 163), “wish to abandon the traditional “tough on the person” approach” (p. 163), feel too little performance orientation in their society and show a “*Zeitgeist of Consolidation*” (p. 163) with regard to future orientation. Furthermore, Germany ranks low on the Collectivism dimensions and

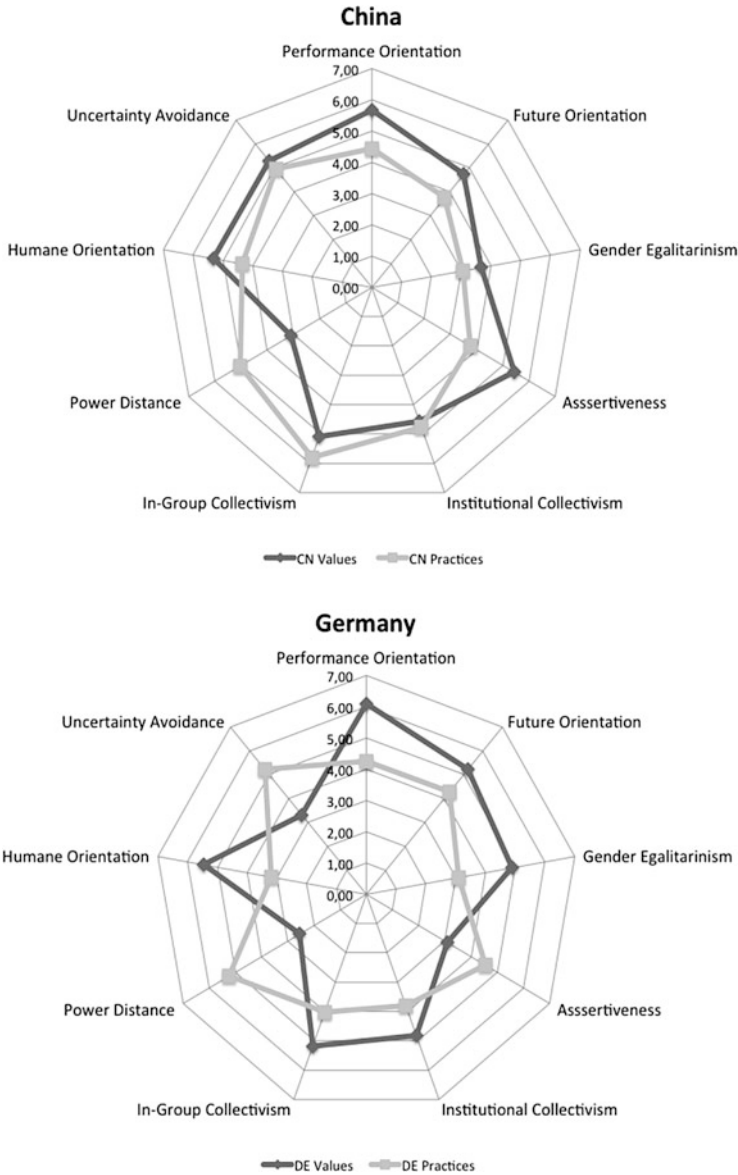


Fig. 6.3 Values (*Should Be*) and Practices (*As Is*) in Germany (West) (DE) and China (CN). Source: GLOBE study, Based on House et al. (2004)

the differences between values and practices reflect the “*ideal of a “Gemeinschaft” and the social welfare state in Germany*” (p. 164). On the other hand, since “*humane orientation is seen to be taken care of by state institutions*”, “*Getting the task done, minimizing errors, and achieving high-quality standards seem to be*

more important at work than compassion and interpersonal relationships” (p. 165). In addition, Gender Egalitarianism is highly favored in Germany, but not practiced in the same way yet. This strong aspiration of Germans for more Gender Egalitarianism only recently led to a government’s decision to introduce a women’s quota for supervisory boards of listed companies from 2016.

For China the comparison of *As Is*- and *Should Be*-scores has been done by Fu et al. (2007). For Performance Orientation Chinese rank rather high, but the discrepancy between *As Is* and *Should Be* are low compared to other countries. Fu et al.’s (2007, p. 888) explanation is that “*Chinese people think good performance is already highly encouraged*” and that “*the Chinese being more collectivistic, may not like extreme emphasis on encouraging individual performance*”. In contrast to Hofstede’s long-term orientation, China ranks middle for *As Is*-Future Orientation and very low for *Should Be*-Future Orientation, since “*the current situation in China discourages people to think long-term.*” (p. 888). Assertiveness shows a high discrepancy between the rather low *As Is*-score and quite high *Should Be*-score. According to Fu et al. (2007) this could be explained by the still prevalent notion of *guanxi*, *mianzi* and *renqing* (see Sect. 6.3.2) on the one hand, and the rapid societal changes and high uncertainty requiring Chinese to be more assertive on the other hand. The scores for Institutional and In-Group Collectivism confirm China being a very collectivistic culture. However, the slight differences between *As Is* and *Should Be* reflect that these traditional values are challenged in the workplace as well as in private and “*Individual contributions are now being acknowledged and rewarded*” (p. 890). Due to its state of economical development, China still ranks low on Gender Egalitarianism. In contrast to Hofstede’s low score on Uncertainty Avoidance, Chinese score rather high on the GLOBE dimension of Uncertainty Avoidance. Fu et al. (2007) explanation is the traditional Chinese value of order. The even higher *Should Be*-score “*reflects the anxiety caused by the unprecedented changes going on in China*” (p. 891). The discrepancy between the value of Humane Orientation and its practice reveals once again the changes China is undergoing. The traditional values related to Humane Orientation are “*challenged by realities and people there find it increasingly important to be assertive and aggressive in order to survive*” (p. 892).

With reference to the models on cultural dimensions and intercultural communication, the following table summarizes general differences between most Western European countries and Eastern and Southern countries like China (Table 6.3).

Culture or the cultural system sets borders for the entities of the individual and the group by defining what belongs to the culture and what does not (Zick 2010, p. 539 f.). Differences between cultures as the aforementioned make adaptation necessary in case that (business) interaction occurs. Thus, the objective of business partners in a cross-cultural setting should be mutual adaptation followed by the establishment of a relational or third culture (Casnrir, 1999). Therefore, selected approaches to cross-cultural business relationship management—in a European-Chinese context—will be outlined in the Sect. 6.4.

Table 6.3 Cultural differences in (communication) behavior of Chinese and Westerners

Characteristic	Low-context/Individualistic (e.g. Western Europe, USA)	High-context/Collectivistic (e.g. Japan, China, Saudi Arabia)
Communication and Language	Explicit, direct	Implicit, indirect
Sense of Self and Space	Informal handshakes	Formal bows and handshakes
Dress and Appearance	Dress for individual success, wide variety	Indication of position in society, religious rule
Food and Eating Habits	Eating is a necessity, fast food	Eating is social event
Time Consciousness	Linear, exact, promptness is valued, time = money	Elastic, relative, time spent on enjoyment, time = relationships
Family and Friends	Nuclear family, self-oriented, value youth	Extended family, other oriented, loyalty and responsibility, respect for old age
Values and Norms	Independence, confrontation and constructive conflict	Group conformity, harmony
Beliefs and Attitudes	Egalitarian, challenge authority, individuals control destiny, gender equity	Hierarchical, respect for authority, individuals accept destiny, gender roles
Mental Process and Learning	Linear, logical sequential, problem solving	Lateral, holistic, simultaneous, accepting life's difficulties
Business/Work Habits	Deal oriented ('quickly getting down to business'), rewards based in achievement, work has value	Relationship oriented ('first you make a friend, then you make a deal'), rewards based on seniority, work is a necessity

Source: Based on Hollensen (2011)

6.3 Cross-Cultural Differences in Business Relationship Management and Marketing

A first approach to business policy and relationship marketing in Europe could be seen in Niccolò Machiavelli's pamphlet *Il Principe* (approx. 1513). Despite the fact that this work is mainly an advice on how to rule an empire, many parallels can be drawn to modern marketing and management (cf. Thomas 2000). Albeit many of his thoughts seem rather unethical, Machiavelli's emphasis on loyalty is a plea for relationship rather than transaction orientation (Thomas 2000). Hence, Machiavelli's pamphlet received broad attention among business practitioners as a source of strategic inspiration, which displays in many books on how to apply Machiavelli's thoughts in business (e.g., Phillips 2010). However, since Machiavelli's ideas do reflect strategies that are more typical for high Power Distance countries (Hofstede 2001, p. 116), his thoughts are far from being general knowledge or strategic basis of European business marketing professionals. For Chinese executives, in contrast, the ancient stratagems of *Sun Zi* (Sun Tzu et al. 1963) are commonly known and applied in daily business (see Sect. 6.3.2).

These strategies do also imply the use of deception and tactics like bait, illusion and fakery, what might be regarded as unethical from a Western perspective but has to be accepted and understood objectively when doing business with Chinese (Wong and Leung 2001).

This outlines already one major difference between the Chinese and the Western approach to business relationships: The Western one is rather clinical and based on trust, bonds, fairness and power dependence. The Chinese approach involves Confucian values like *renqing* (favor or norm of reciprocity), harmony and *guanxi* (personal ties) as well as stratagems. Wong, et al. (2007) refer to this as mind-orientation and heart-orientation, respectively.

6.3.1 Key Factors in Western Business Relationships

Relationship marketing (or relationship management) is “*a philosophy of doing business, a strategic orientation that focuses on keeping and improving relationships with current customers rather than on acquiring new customers*” (Zeithaml, et al. 2006, p. 176). Although the focuses of relationship marketing are retention and/or relationships in both west and east, the western relationship marketing is a totally different system than in China, and there are some major factors that western business practitioners believe can greatly influence establishing, maintaining and succeeding business relationships. Hence, we briefly explain these factors and their impacts on western business relationships in this section to show the different ways of dealing with business relationships between the west and China.

6.3.1.1 Trust

Trust is not only essential for building successful business relationships, but is also important for enhancing business performance. It has thus attracted a great deal of attention in inter-organizational research (e.g., Doney et al. 2007; Doney et al. 1997; Gounaris 2005; Morgan and Hunt 1944; Siguaw et al. 1998; Sirdeshmukh et al. 2002) as well as in other research fields, such as social psychology (e.g., Lewicki and Bunker 1995) and sociology (e.g., Williamson 1991).

There are two dimensions of trust: credibility (or honesty/integrity) and benevolence. Credibility is the expectation that the partner’s word or written statement is reliable, while benevolence refers to the extent to which a firm is genuinely interested in the other’s welfare and is motivated to seek mutual gain. Here is a most commonly cited definition of trust.

Trust is the perceived credibility and benevolence of a target of trust (e. g., Doney et al. 1997, p. 36).

Although it is a belief held by one party, trust implies an interaction between two parties, meaning that the belief should actually be based on the other’s certain words or behavior. In other words, a firm’s trust is engendered by the other firm’s trustworthiness, or at least the other firm’s believed trustworthiness. The definition

describes such reflection by using the word “perceived.”, which also shows that trust contains both subjective and objective characteristics.

The key effects of trust on inter-organizational relationships determine its important position in a business marketing context. It is suggested that trust promotes long-term relationships and higher-level cooperation (e.g., Morgan and Hunt 1944), enhances competitiveness, commitment and satisfaction (e.g., Anderson and Narus 1990), and reduces conflict and opportunism (e.g., Pfeffer and Salancik 1978). On the other hand, the central role of trust also motivates marketing theorists, who are working on its antecedents.

The nature of trust, which Doney et al. (1997), lies in the two following points. First, in spite of the disagreement about whether organizations can be targets of trust, mainstream literature on trust suggests that trust does exist on the organization level. Second, the operation of trust stems from the vulnerability of decision makers (trustors) and their decision outcomes—uncertainty that is important to the trustor. Hence, the effects of trust concentrate on building long-term relationships/orientation to avoid such risk (e.g., Dwyer et al. 1987).

6.3.1.2 Bonds (Western Networks)

As common ties that unite people and groups in human societies, bonds have been investigated by sociologists since the 1970s. Their relational nature and key effects on increasing relational attachments have gradually come to be valued in business marketing over the last 20 years, which is why bonds have been studied in some B2B literature as a relational factor, but are rarely thoroughly researched as a main construct. Smith (1998, p. 78) defines bonds as:

The psychological, emotional, economic, or physical attachments in a relationship that were fostered by association and interaction and served to bind parties together under relational exchange.

Previous research conceptualizes three types of bonds that serve to bind firms to business relationships: social bonds, structural bonds, and functional bonds. Social bonds refer to “*the personal ties or linkages forged during interaction at work*” (Smith 1998, p.78). Functional bonds are “*the multiplicity of economic, performance, or instrumental ties or linkages that serve to promote continuity in a relationship.*” Structural bonds are “*ties relating to the structure, governance, and institutionalization of norms in a relationship*” (Smith 1998, p. 79).

Most prior studies in business marketing have only focused on social bonds and found that social bonds could positively influence trust, commitment, satisfaction, and relationship quality in exchange relationships (e.g., Cater and Zabkar 2009; Mavondo and Rodrigo 2001). A few have researched the other types of bonds and investigated their effects on trust and relational performance (Gounaris 2005; Lin et al. 2003) or different effects on commitment in different cultures (e.g., Williams et al. 1998). Smith (1998) also examined the antecedents of all the types of bonds and demonstrated that communication, cooperation, and relationalism could help to foster bonds.

6.3.1.3 Fairness

As a “*human hunger or thirst*” (cited in Cohen 1986, p. 1), fairness is listed as one of the ethical values for marketers (American Marketing Association 2012). Fairness plays a critical role in business relationships. Fairness research in the business context started as early as the 1980s, however, it was quite short and limited compared with the long study histories and fruitful outcomes in other disciplines of the humanities and social sciences. Since the publication of the classic paper by Kumar et al. in 1995, more and more marketing scholars have been inspired by the work and recognize the importance of fairness. Research is now rapidly increasing with many notable works (e.g., Jap 2001; Brown et al. 2006).

According to Scheer (2008) fairness can be defined as follows:

Fairness is an evaluation that one's condition, outcomes, and/or treatment are appropriate when judged against relevant standards held by the evaluator.

Fairness is “*endlessly resilient*” (Pitkin, 1981, p.348), because its nature is cognitive, subjective, and sometimes egocentric. First, fairness is a perceptual cognition that does not necessarily have to be “*reality*” in the “*truth world*” (Folger and Cropanzano 1998, p. XV) or an “*‘objective’ reality as conceived by a competent, impartial observer*” (Deutsch 1985, p. 12). Second, the principles of fairness or value involved were only dependent on the evaluator’s choices and opinions (e.g., Lerner 1974; Deutsch 1975). Finally, in academia, the object of fairness research is one’s fairness *perception* rather than the “*truth.*” As Azar and Darvishi (2011, p. 7365) stated: “*An act is ‘just’ because someone thinks it is.*” This again underscores that a cognitive perception is all fairness theorists ask for.

Two points need to be made. First, fairness concerns one’s “*condition*” at the same level of outcomes and treatment, which implies that the outcomes and treatment received should first be in accordance with one’s status quo. This particularly applies in complex business circumstances in which firms usually have different marketing roles and tend to behave based on them (Cateora 1983). Second, the definition stresses that not just one standard is used for fairness evaluations. In other words, it indicates that fairness also varies according to the application of different rules.

Distributive fairness and procedural fairness are defined contextually in business marketing. Distributive fairness refers to a firm’s “*perception of the fairness of earnings and other outcomes that it receives from its relationship*” with its partner. Procedural fairness, on the other hand, is defined as the perception of the fairness of a firm’s procedures and processes in relation to its partners (Kumar et al. 1995, p. 55).

For so many years, fairness research in the B2B field has been focused on answering the same question: How does perceived (un)fairness impact business relationships? The research puts a great deal of emphasis on this from the perspectives of both fairness and unfairness. Direct effects include that a fair distribution is positively related to channel members’ satisfaction and performance, negatively related to conflict between them. A fair perception enhances long-term orientation and relational behaviors (Griffith et al. 2006; Brown et al. 2006), while

unfairness tends to generate hostility, conflict, and opportunism in business relationships (Kaufmann and Stern 1988; Samaha et al. 2011). Moreover, unfairness also causes negative reactions; firms feel angry when they receive negative, inequitable outcomes (Scheer et al. 2003).

According to previous literature, fairness also has indirect outcomes. For instance, Kumar et al. (1995) found that as the outcomes received from the relationship increase, the importance of distributive fairness on the relationship quality increases, while in long-term relationships, procedural fairness is more important than distributive fairness.

Finally, (un)fairness itself acts as a moderator in business relationships. Cui et al. (2007) demonstrated that in a fair channel relationship coordination could be achieved by using a constant wholesale price. On the other hand, it has been identified that conflict and opportunism slightly decrease a channel member's outcomes if the perceived unfairness is low (Samaha et al. 2011). In addition, they also found that perceived unfairness strengthened the negative effects of conflict and opportunism on cooperation and flexibility.

6.3.1.4 Power and Interdependence

It is a well-established tradition that inter-organizational literature includes dependence as a major relational factor. As most of the dependence research is based on Emerson's (1962) classical power-dependence theory, dependence has been defined very consistently. This means that dependency implicitly resides in the other's power and "*the dependence of actor P over actor O is (1) directly proportional to P's motivational investment in goals mediated by O, and (2) inversely proportional to the availability of those goals to P outside of the O-P relation*" (Emerson 1962, p. 32). The definition below is the more general and widely applied one in prior marketing literature, which was made by Frazier in 1983 (p. 71):

Dependence refers to a firm's need to maintain the business relationships in order to achieve desired goals.

In B2B relationships, both interdependence/bilateral dependence (mutual dependence of both partners) and asymmetric dependence/unilateral dependence (imbalance between partner's dependence) exist.

The antecedents of both interdependence and asymmetric dependence have not been extensively studied. Commitment and trust have been argued to have consequences on interdependence (El-Ansary 1975), however, there is comment that the effects are not significant (Palmatier et al. 2007).

Generally speaking, interdependence has been shown to have a positive effect on business relationships. To be more specific, interdependence is considered to positively influence exchange performance, collaborative communication, commitment, and trust (e.g., Kumar et al. 1995; Palmatier et al. 2007) and could promote the use of legal contracts and contract enforcement (Antia and Frazier 2001; Cai et al. 2009).

Dependence asymmetry is more often investigated in B2B marketing research. In most cases, dependence asymmetry has been viewed as the comparative level of

each firm's dependence (e.g., Gundlach and Cadotte 1994). In other words, dependence imbalance in business relationships is no longer the concern; instead, scholars only consider one firm's dependence state regardless of its partner's. This work will only concentrate on this logic of asymmetric dependence conceptualization. The term dependence will be used for short.

A range of dependence effects has been found in business relationships. Some papers have shown that dependence undermines trust in benevolence (Eggert and Ulaga 2010), leads to the use of coercive strategies, and reduces the willingness to compromise (Gundlach and Cadotte 1994). Others suggest that it is positively related to the cooperation intentions (Andaleeb 1995) and relational loyalty (Scheer et al. 2010).

Of course, the above mentioned factors are not the whole picture of the western relationship marketing. However, they present the western way of understandings of business relationships and how to deal with them, which also make a clear distinction from the Chinese thinking that is provided in the next section.

6.3.2 Key Factors in Chinese Business Relationships

China has to be considered as a unique research object in the context of business marketing (Chinese Theory of Business Marketing) (Wang and Song 2011). Therefore, we want to call attention to the unique phenomenon of *guanxi*, also referred to as the Chinese way of relationship marketing (Arias 1998; Yau et al. 2000) and related values like harmony and face.

6.3.2.1 Confucian Values and the Notion of Guanxi

The Chinese society is one of high Power Distance as a result of the idea of *Kong Zi* (孔子 Confucius) that an unequal distribution of power is necessary for a stable society (Hofstede 2001). *Kong Zi* defined the five basic relationships (*wu lun* 五伦) implying mutual obligations and responsibility for the involved parties (master—follower; father—son; elder brother—younger brother; husband—wife; senior friend—junior friend). In consequence, Chinese do also have a specific understanding of the notion of personal ties (*guanxi*) in business relationships. As a mixture of personal and professional relationships implying certain obligations, these personal ties determine success in private as well as in business and influences the way Chinese perceive business relationships (Yang 1994).

Whilst Western relationship marketing is rather universalistic and impersonal, *guanxi* is particularistic and personal (Arias 1998; Hwang 1987; Lee and Humphreys 2007) and “*can be seen as unifying what Western bourgeois relationships separate: material exchange and affectionate feelings*” (Kipnis 1997, p. 24).

Different authors (Arias 1998; Park and Luo 2001) argue that while a successful transaction is a precondition for a good (personal) relationship in Western economies, good *guanxi* is often a precondition for a successful transaction in China.

The word guanxi (pronounced guan-shee) means literally “a relationship” between objects, forces, or persons. When it is used to refer to relationships between people, not only can it be applied to husband-wife, kinship, and friendship relations, it can also have the sense of “social connections,” dyadic relationships that are based implicitly (rather than explicitly) on mutual interest and benefit. Once guanxi is established between two people, each can ask a favor of the other with the expectation that the debt incurred will be repaid sometime in the future (Yang 1994, p. 1 f.).

There are mainly two streams of *guanxi* research (Heberer 2003; Kipnis 1997): One interpreting *guanxi* primarily as Confucian culture essence and another rather economic, political and social science stream seeing *guanxi* primarily as a practical adaptation to communist socioeconomic structures. Thus, the perception and behavior of Chinese within business relationships should best be understood as a result of both, cultural values and environmental factors, since the contemporary “*Chinese society is a blend of old and new cultural values*” (Wong and Leung 2001, p. 111).

The Chinese term *guanxi* (关系) can be translated as “personal connections” or “personal relationships” and refers to interpersonal relationships that are vital to conduct successful business transactions in a Chinese environment (Hwang 1987; Kiong and Kee 1998).

Guanxi is often described as a Chinese way of relationship marketing (e.g., Yau et al. 2000), albeit certain differences between *guanxi* and relationship marketing can be identified (Wang 2007). *Guanxi* is transferable among parties, reciprocal and intangible, and utilitarian rather than emotional (Park and Luo 2001; Arias 1998). Since *guanxi* is a special form of long-term oriented personal relationships built upon a set of shared *guanxi* bases (e. g., kinship, regional provenance or membership in an association) and, even more important, reciprocal obligations among individuals, relationship does not necessarily mean *guanxi* (Kiong and Kee 1998; Arias 1998; Wang 2007).

The construct of *guanxi* is deeply rooted in Chinese culture and Confucianism (Park and Luo 2001), but nevertheless it is not a unique Chinese phenomenon. Strong emphasis on personal relationships in business is also known from other cultures like Japan or Russia (Hwang 1987; Arias 1998; Ledeneva 2008). However, in its specific form *guanxi* is a product of Chinese culture and environmental factors that influence the way business is conducted.

According to Hwang (1987) *guanxi* is a relationship of mixed ties, meaning *guanxi* is neither solely expressive as bonds among family members nor exclusively instrumental as transactions among strangers. These mixed ties involve the use of *renqing* (reciprocal exchange of favors) and *mianzi* (face) to influence others’ behavior. Thus, *guanxi* means also sustaining each other’s reputation and social status (Arias 1998).

Furthermore, *guanxi* can be understood as a system of concentric circles with individuals being either located in the center or the periphery depending on the distance of the relationship and the degree of trust (Yang 1994; Park and Luo 2001). “*That is, the more inner circle the guanxi party is located on, the smaller the psychological distance between the guanxi partner and the self, the better the*

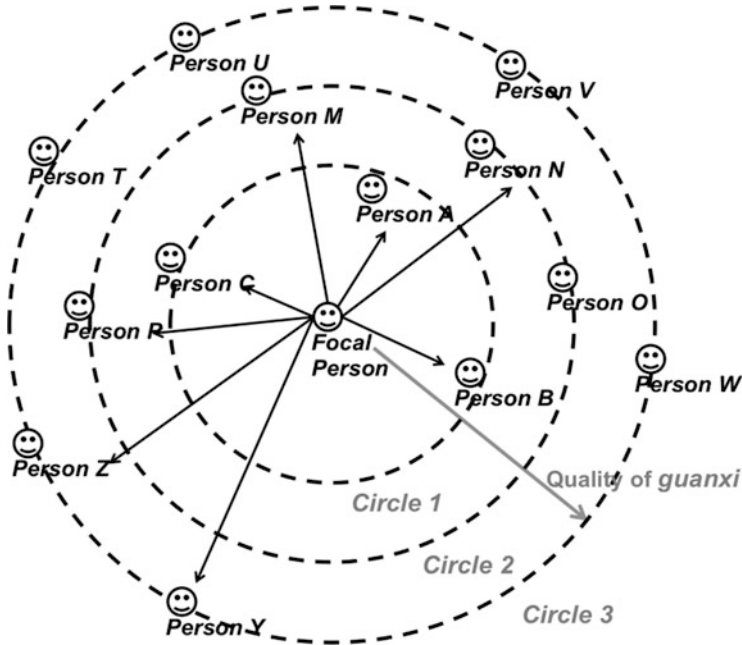


Fig. 6.4 A person's Guanxi-network with different levels of relationship quality. Source: Based on Chen and Chen (2004, p. 312)

guanxi quality is." (Chen and Chen 2004, p. 312). The degree of *guanxi* between two individuals determines the extent to which social resources are exchanged between them (Fig. 6.4) (Hwang 1987).

As the establishment of *guanxi* relationships in Chinese society usually involves "altercasting", i. e. forcing a potential relationship partner into his or her role, individuals in a *guanxi* network face a complex role duality, being both passive followers of social norms in predetermined relationships and active initiators of voluntary relationships. Once the relationship is basically established, one has to follow the rule of *renqing*, reciprocating received gifts or favors. These gifts or favors are not expected being repaid immediately, but when time of need has come. In addition, the rule of *renqing* implies that favors owed to someone increase in value compared to the once received favor (Hwang 1987; Yang 1994; Park and Luo 2001). Against this background, involvement in *guanxi* always implies the risk of being involved in corruption, if relationships are not only used to facilitate business exchange, but to circumvent legal barriers (Dunfee and Warren 2001).

Thus, and in line with Plinke's definition of a business relationship (see Chap. 1), we propose the following definition for *guanxi* with regard to business marketing:

Guanxi indicates a series of personal interactions, which are internally interlinked with each other, implying certain obligations and favors, and might be related to business but also to private. Hence, in contrast to business relationship management, guanxi is rather holistic, because business transactions are part of it, but not necessarily its core.

Originally, a *guanxi* perspective is limited to social relationships (Arias 1998). However, Lee and Humphreys (2007, p. 451) “define *guanxi* as a corporate culture that has a strong emphasis on the relationships between business partners for achieving mutual benefits and involves the use of personal and/or inter-firm connections to secure favors in the long run.” Thus, due to the transferability of *guanxi*, there is also a number of works on *guanxi* on the organizational level (Park and Luo 2001; Arias 1998; Mavondo and Rodrigo 2001; Yang et al. 2012). In line with these works and especially the one of Chen et al. (2011) *guanxi* could also be understood as a certain business strategy or practice that facilitates good relationships in terms of cooperation, long-term orientation and performance among companies. Accordingly, Wong and colleagues (Wong and Leung 2001; Wong et al. 2007) developed a comprehensive *guanxi* management model.

6.3.2.2 Elements of Guanxi-Relationships

As a rather complex phenomenon *guanxi* is a higher order construct (Yen et al. 2011), based upon a set of different constructs. These constructs determine the degree of *guanxi* one develops within the social interaction with other individuals, and thus, one’s position within a *guanxi* network.

Typically, it is suggested that *guanxi* is built upon *ganqing* (emotional affection), *renqing* (favor or social norm of reciprocity) and *xinren* or *xinyong* (trust or social credit) (Hwang 1987; Wang 2007; Yen et al. 2011). Recently, Yen et al. (2011) introduced an empirically tested instrument to measure the degree of a business relationship’s *guanxi* (in particular, the *guanxi* maintained between the representatives of the respective firms). The so-called GRX-scale builds upon the three aforementioned Chinese constructs of *ganqing*, *renqing* and *xinren*. Some authors also mention *mianzi* (face) as an important factor influencing *guanxi*, but, vice versa, also being influenced by *guanxi* (Hwang 1987). Due to the overall importance of *mianzi* within the Chinese culture and within intercultural interaction, it should definitely be included into the understanding of *guanxi* as a business strategy.

In the following, an attempt to define the aforementioned constructs and their mutual interdependencies is undertaken. This shall lead to a better understanding of how *guanxi* works and how Western companies might utilize it.

***mianzi* 面子 (Face)**

mianzi is an intangible form of social currency and personal status that is determined by a person’s post, credibility, honesty, reputation, power, income, or network. An individual’s *mianzi* can be described as the perceived social position and prestige in one’s *guanxi* network. Other things being equal, a *guanxi* relationship becomes stronger if one’s partner has superior *mianzi*. Therefore, saving one’s own as well as the face of persons in one’s *guanxi* network is crucial for the maintenance, extension and utilization of *guanxi*. Hence, a complex interdependency between *guanxi* and *mianzi* can be realized: The quality and quantity of one’s personal relationships (*guanxi*) influences one’s *mianzi* (perceived overall social status), and vice versa (Hwang 1987; Park and Luo 2001). Thus, *mianzi* received in a relationship leads to

defensiveness mechanisms towards outsiders of the relationship network (Wong and Leung, 2001).

renqing 人情 (Norm of Reciprocity and Exchange of Favors)

renqing is a complex construct implying (1) empathy, (2) an incalculable resource that is used in social exchange, and (3) an informal social norm of reciprocity by which *guanxi* networks are developed, maintained and utilized for mutual benefit as well as one's personal advantage. Violating the norm of reciprocal obligations leads to a loss of face (*mianzi*) and consequently even to a loss of *guanxi* (Hwang 1987; Wang 2007; Park and Luo 2001).

The *renqing* rules set behavioral norms guiding exchange parties based on face-saving and mutual insurance rather than the belief of exchange partners' integrity and honesty (Wang 2007). Hwang (1987) describes the interdependency between doing *renqing*, anticipating the payback of *renqing*, repaying *renqing* and face and *guanxi* as the dilemma of *renqing*: It is nearly impossible to repay a debt in *renqing* due to its subjectiveness and the value spiral (Hwang 1987).

ganqing 感情 (Emotional Affection)

ganqing implies personal feeling and emotional attachment between interacting parties. It plays a key role in maintaining and enhancing a *guanxi* relationship and makes impersonal business relationship more personal (Wang 2007). Multiple *guanxi* bases—such as memberships, regional provenance, etc.—help to enhance social interaction and thus *ganqing* through a feeling of shared commonalities (Kiong and Kee 1998). For developing *ganqing* an ongoing social interaction is of paramount importance. This does usually involve wining-and-dining and the exchange of gifts (Yang 1994).

xinren 信任 or **xinyong** 信用 (Personal Trust or Social Credit)

Within the literature some authors refer to *xinren* and some to *xinyong* as a dimension of *guanxi*. Whilst both could simply be translated as trust, semantically there is an important difference. Literally, *xinyong* means credibility, i. e. it is more objective and based upon the trustworthiness perceived by a social group. *Xinren*, literally meaning (personal) trust, is much more subjective and can be based upon affection and a personal believe in someone. Thus, Yen et al. (2011, p. 100) argue that “*In Chinese, one would only have xinren with the other party, in so far as the other party is evaluated as having good xinyong (credibility). It literally says that one should only trust a person who is trustworthy.*”

Mere trust or *xinren* is not sufficient to develop and sustain long-term relationships. While Western societies rely on contracts or partners' benevolence, Chinese rely on the rule of *renqing* and *mianzi* (Wang 2007). Leung et al. (2005) provide empirical evidence that Chinese emphasize on *xinyong* on a personal level rather than satisfaction on the organizational level to build a partnership relationship. This is in line with Kiong and Kee (1998) who found for Chinese traders in Singapore and Malaysia transactions building on *xinyong* are intrinsically higher

valued than those building on impersonal laws. Thus, if *guanxi* exists verbal *xinyong* based contracts are desired by Chinese.

6.3.2.3 Harmony

As one of the fundamental Confucian values, harmony is widely regarded as a commonly shared principle to guide interactions among individuals and groups in China. Most Chinese people strongly believe that pursuing harmony is quite essential in social life (Yang 1994). It is highly valued and deeply rooted in the everyday life for thousands of years. Here are two examples: The three halls, the heart of the Outer Court of the Forbidden City, in which the Ming and Qing emperors held courts and hosted imperial ceremonies, were named as the [Hall of Supreme Harmony](#) (太和殿), the [Hall of Central Harmony](#) (中和殿), and the [Hall of Preserving Harmony](#) (保和殿). And in contemporary China, the central government uses “constructing a harmonious society” as a political slogan.

Harmony, in Chinese, can be literally translated as He (和), describing a peaceful and/or united state. A great deal of Chinese idioms repeatedly stress the idea of harmony, such as Yi He Wei Gui (harmony is most precious; 以和为贵), He Er Bu Tong (gentlemen will be in harmony with each other despite their differences; 和而不同), He Qi Sheng Cai (harmony brings wealth, 和气生财), and so on. The last idiom has been extensively recognized and valued by businesspeople since ancient times, meaning that it has also been a long history of harmony being a guideline in business practice (e.g., Leung 1988; Zhang and Zhang 2013).

Sociologists found that “the ultimate goal of the concerned parties is to maintain a harmonious atmosphere,” (Zhang and Zhang 2013) and anything that destroys harmony will lead to anxiety in Chinese social life (Yang 1994). In the meanwhile, some theories are focused on the important role harmony played in conflict resolution. Gabrenya and Hwang (1996) demonstrated that Chinese tended to avoid conflict by tolerating interpersonal disagreements and transgressions. Similarly in the business context, where research also shows that Chinese managers strongly prefer negotiation and mediation to adjudication when resolving conflicts compared to their American counterparts (Leung 1988). On the other hand, harmony significantly influences *guanxi*, which is also a key value of Confucianism (see Sect. 6.3.3.1). People are more likely to cherish harmony with the ones whom they have good *guanxi* with to make it stable (Zhang and Zhang 2013). Another example is Chinese use the phrase, “breaking the face” (撕破脸) to express that harmony is jeopardized, showing the close relationship between harmony and face (*mianzi*). From this perspective, harmony is used for giving *mianzi* and maintaining *guanxi* in social interactions.

In China, the value of harmony is highly respected. Once the inter-personal/inter-organizational harmony is destroyed, it will have negative influence on the whole relationship, even worse, some relationships might hardly ever recover. It is common that the Chinese “*appear to pursue harmony for harmony’s sake*” (Zhang and Zhang 2013, p. 102), it is thus still necessary to safeguard harmony even if it is in a very superficial way. Therefore, Western practitioners need to be cautious with manifest conflicts when dealing with Chinese businessmen.

6.3.2.4 The Stratagems of Sun Zi

In addition to the concepts of *guanxi* and harmony, the stratagems outlined by Sun Zi in *The Art of War* are always prevalent in a Chinese business context. *The Art of War* was written between 515–512 BC by Sun Tzu (Sun Zi, 孙子), a high-ranking Chinese military general, strategist and tactician. It is the earliest military treaties in the world, and the most influential military work in Asia “*where the common people knew it by name*” (Sawyer 2007, p. 149).

The book is a general “guideline” for fighting a war in 13 detailed aspects of warfare, including Detail Assessment and Planning, (始计), Waging War (作战), Strategic Attack (谋攻), Disposition of the Army (军形), Forces (兵势), Illusion and Reality (虚实), Military Maneuvers (军争), Variations and Adaptability (九变), Movement and Development of Troops (行军), Terrain/Situational Positioning (地形), The Nine Battlegrounds (九地), Attacking with Fire (火攻), and Intelligence and Espionage (用间) (translated by Wee 2003; Wing 1988). A unity of opposites is presented in the book, based on the Yin-Yang concept from *I Ching* or *Classic of Changes* (Zhouyi 《周易》). The following seemingly opposite or contrary forces that are interconnected and interdependent are discussed throughout the book: Hardness-Softness (刚柔), Strength-Weakness (强弱), Illusion-Reality (虚实), Host-Guest (主客), Self-Opponent (彼己), Attack-Defense (攻防), Gains-Losses (利害), Victory-Defeat (胜败) and Direction-Indirection (奇正).

The book has not only influenced Eastern and Western military thinking, but also had a great impact on business tactics, legal strategies and beyond. Some ideas emphasized by Sun Tzu, such as to position an army based on both objective conditions and the subjective beliefs of other competitive actors, and to respond quickly and appropriately to changing conditions are particularly valued within business contexts (Michaelson, 2001). On the other hand, much of the text is about how to fight wars without actually having to do battle, it therefore finds applications as a training guide for many competitive contexts that do not involve actual combat—the business context is one of them. The book is also popular among Western management executives and Japanese corporations who have turned to it for inspiration and suggestion on how to be successful in competitive business contexts. (e.g., Krause 1995; McNeilly 1996). Nevertheless, it is only one book of thousands of recommended strategic books in the Western business world. The situation is absolutely different in China. The basic principles and stratagems of this book are so deeply rooted in everyone’s heart for centuries that they turned to idioms and are even prevalently used in modern daily life, such as 后发先至 (enticing the enemy to take a long and circuitous route, and though starting after him, to contrive to reach the goal before him, shows knowledge of the artifice of deviation), 避实击虚 (to avoid what is strong and to strike at what is weak), 兵不厌诈 (All warfare is based on deception), 不战而屈人之兵 (The supreme art of war is to subdue the enemy without fighting), and so on. It is therefore not surprising that the Chinese negotiators “*embraces a mixture of different roles together: ‘Maoist bureaucrat in learning’, ‘Confucian gentleman’, and ‘Sun Tzu-like strategist.’*” (Fang 2006, p. 54). In conclusion, the *Art of War* is on the required reading book list of nearly every key executive, in order to be 知己知彼,百战不殆 (if you know your

enemies and know yourself, you can win a hundred battles without a single loss), it is very essential to know this work when dealing with Chinese businessmen.

6.3.3 Differences Between Guanxi and Western Relationship Marketing

Whilst relationship marketing is universalistic and impersonal, *guanxi* is particularistic and personal. Hence, relationship marketing networks are relatively open to any exchange partners who follow the rules, whereas a *guanxi* network is an exclusive circle of members. However, *guanxi* and relationship marketing also share certain commonalities: Both are based on mutual understanding, cooperation and a certain long-term orientation. But they differ significantly in their underlying exchange principles: Legality and rules in relationship marketing and morality and social norms in *guanxi* (Arias 1998; Wang 2007). It is even suggested that *guanxi* unites long-term relationship orientation and short-term transaction orientation due to its mixed nature (Hwang 1987; Arias 1998; Lee and Humphreys 2007). Different authors (Park and Luo 2001; Arias 1998) argue that while a successful transaction is a precondition for a good relationship in Western economies, good *guanxi* is often a precondition for a transaction in China. *“In short, the contrasts lie in a major difference in management philosophy: there is a preference in the West for ‘Mind’ management, while in China more emphasis is placed on the ‘Heart’”* (Wong et al. 2007 p. 877). The following table outlines these two management philosophies.

Wong and Leung (2001) consequently summarize the main differences between Western approaches and Chinese approaches to business relationships as depicted in the following figure (Fig. 6.5).

6.4 Approaches to the Management of Sino-European Business Relationships

The above-outlined differences in Western and Chinese business relationships make it necessary to develop an approach that facilitates mutual understanding and adaptation. Generally, this can be achieved by (1) a thorough gap analysis resulting in market research and educational measures for businesspeople, which help to close the gap or minimize the cultural distance, respectively, and ideally lead to (2) attempts by either party to build a relational, third culture or (3) an adaptation to the Chinese way of relationship marketing by mutual building of *guanxi*. Additionally, for Chinese businesspeople adaptation to the Western, often more transaction-oriented way of business relationship marketing would be imaginable. This would involve a more direct, explicit behavior. However, it is much easier for businesspeople from high-context, relationship-oriented cultures to move towards a low-context, more explicit way of doing business (Hall 1989). Furthermore, Western businesspeople increasingly emphasize relationships and

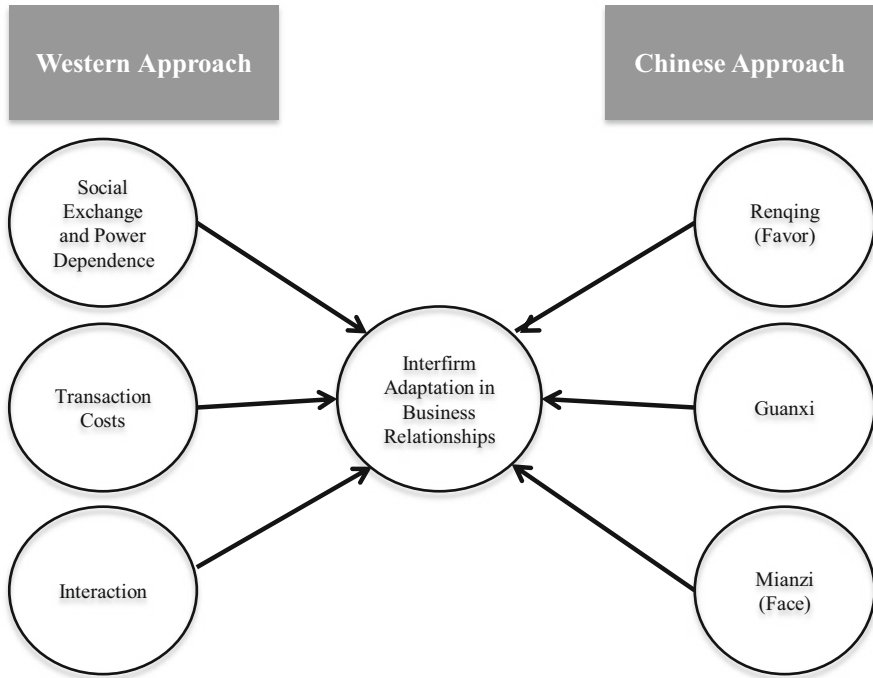


Fig. 6.5 Western and Chinese approaches to interfirm adaptation in business relationships. Source: Based on Wong et al. (2007, p. 33)

cooperation and seem to move in the direction of Guanxi-type systems throughout the twenty-first century (Lovett et al. 1999). Therefore, we do not put emphasis on that approach in the following sections.

6.4.1 Gap Analysis in a Cross-Cultural Negotiation

As already indicated above, the cultural distance (i.e., different basic assumptions, norms and values, behavioral and communicative patterns) between European cultures and Chinese culture is what makes adaptation necessary for the sake of mutual understanding and successful negotiations and business relationships. Therefore, Hollensen (2011, p. 665ff.) suggests to start with a gap analysis when it comes to cross-cultural negotiations and the initiation of business relationships. Such an analysis has to take the national and organizational culture of either party involved into account in order to assess the cultural distance (Gap 1). Furthermore, potential adaptations due to a shared business culture and the resulting actual behavior of the buyer and the seller have to be considered. The actual gap being identified between the interacting managers (Gap 2) can be closed by means of market research and education for salespeople. The latter should be reflected in a

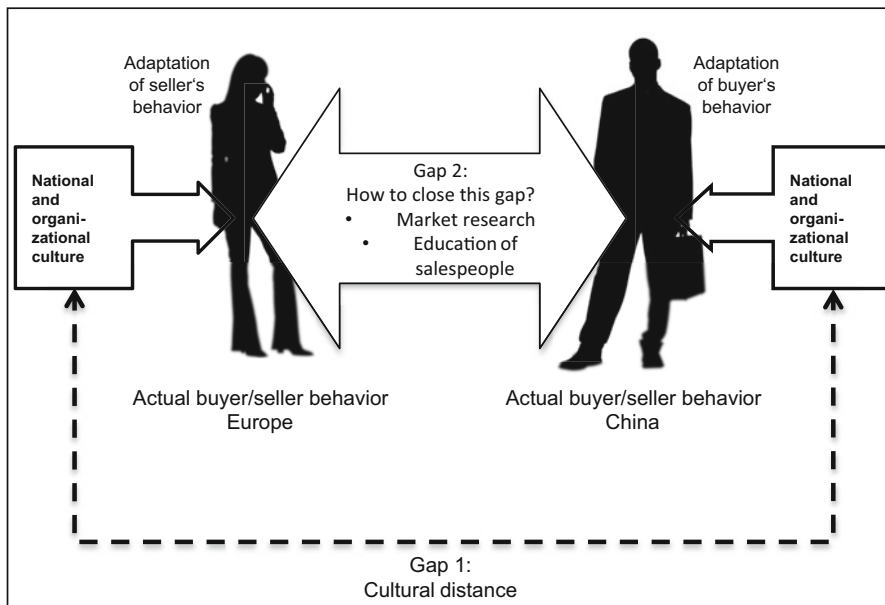


Fig. 6.6 Gap analysis in a cross-cultural negotiation. Source: Based on Hollensen (2011, p. 666)

long-term oriented, sustainable human resource development program. Such a program ideally leads to the salespeople's ability to build relational cultures (see Sect. 6.4.2) or to adapt to the Chinese way of relationship management (see Sect. 6.4.3) (Fig. 6.6).

The following figure depicts the process of a cross-cultural gap analysis.

6.4.2 Mutual Adaptation by Third-Culture Building

In industries with high requirements for global integration but rather low requirements for local responsiveness, so-called global industries, the existence of a globally integrated business culture is likely, since these companies have to apply an integration strategy regarding the targeted markets as well (Bartlett and Ghoshal 2002; Macharzina and Wolf 2010). For European-Chinese business relationships taking place in these industries, it is vital to understand how integration happens and a relational culture can be built, since Casnir (1999, p. 107) assumes *“that meaningful, beneficial intercultural communication requires changes or adaptations on the part of all participating individuals, and that such changes are not easy”*. Thus, he suggests a Third-Culture Building Model that represents the dynamic process of developing a unique relational culture by mutual adaptations. This model contains four phases, in which shared *“standards, value systems, ongoing personal relationships, interdependence and possibly new language components”* (Casnir, 1999, p. 108 f.) emerge. Within the theory of acculturation,

that is mainly applied in migration contexts, this approach corresponds to an integration strategy (i. a., Berry et al. 2011; Zick, 2010). In a business context, for the example of corporate mergers an integration approach is seen as favorable strategy (Malekzadeh and Nahavandi 1990). Hence, third-culture building as described by Casmir (1999) can also be applied to European-Chinese business relationships:

Contact (Phase 1): This phase represents the initial contact of European and Chinese businesspeople or organizations with each other. Since this contact might be the result of an unsolicited inquiry, it will not necessarily lead to further interaction. Reasons for the end of the contact may be rooted in a lack of resources, low intercultural competence, individual fears of dealing with foreign companies or specific corporate policies.

Need and Interaction (Phase 2): If the parties perceive the initial contact as being related to their mutual economic needs (i. e., they are generally interested in the establishment of a business relationship), further contacts follow. However, if there is no such perception of mutual benefits from the contact, the contact may also end here.

While no further steps may be taken towards building a third-culture, the decision could be quite abrupt or arbitrary (caused by fear, anger or intervention of others within a given culture) on the part of even one participant, or it could be based on limited opportunities, over time, for communicative interaction. (Casmir 1999, p. 110)

In case that the interaction and communication continues, a need for change or adaptation on both sides will emerge. At this stage it is of high importance that the involved parties are not only aware of this necessary mutual adaptation but also able to actively build and organize such a process. This would be the case if a former gap analysis has led to educational measures.

Dependence (Phase 3): At this stage and as a result of the former and ongoing interaction the involved parties do already depend on one another in order to achieve mutual benefits. Therefore, the building of a third-culture starts by negotiating behavioral rules, acceptable outcomes and roles within the relationship.

Third-Culture Interdependence (Phase 4): By ongoing dialogic communication and on the basis of interdependence, the involved parties can develop and maintain a third-culture. Therefore, businesspeople and organizations have to accept that mutual benefits can best be achieved through cooperative behavior. *“In effect, the beneficial continuation of the process becomes dependent on relationship and trust-building during mutual efforts to organize an ongoing communicative interactional process.”* (Casmir 1999, p. 111) Consequently, third-culture building requires businesspeople in a European-Chinese setting to have a deep understanding of cultural differences concerning values and communicative behavior.

Figure 6.7 depicts Casmir’s Third-Culture Building Model and its different stages.

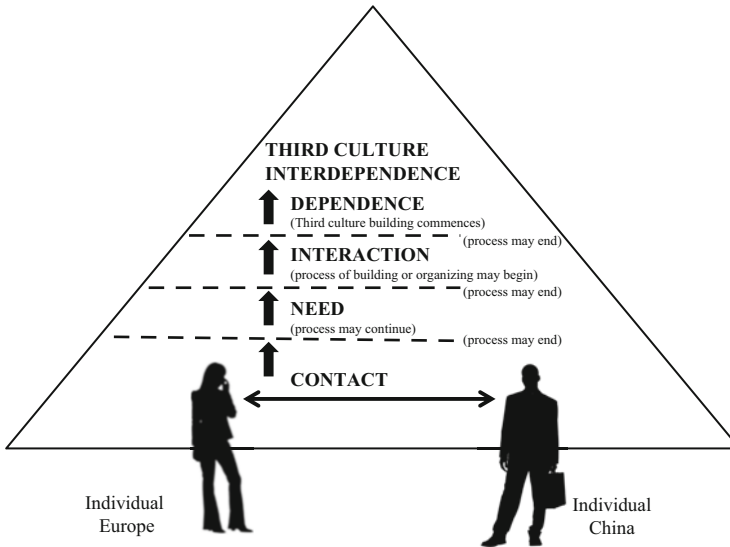


Fig. 6.7 Dialogic communication model of third-culture building. Source: Based on Casnrir (1999, p. 109)

6.4.3 Comprehensive Guanxi Model by Wong and Leung

In some cases, especially when the business relationship is taking place in China or the Chinese organization is an important and powerful buyer of the European one, a *guanxi*-oriented relationship marketing approach could be favorable.

The expectation is that a foreigner, when doing business in China, would integrate into the rules and understand different expectations and returns. Failure to do so is deemed to be 'not enough of a friend'. Therefore, a foreigner needs to know the ways that a Chinese uses to ask favours in the level of delicacy and understands that he always feels more free to ask favours. (Wong et al. 2007, p. 885)

For such European-Chinese business relationships Wong and colleagues came up with a comprehensive *guanxi* model (Wong and Leung 2001; for a brief version see Wong et al. 2007), which “attempts to account for differences in Western and Chinese views and to provide a holistic perspective to balance or explain the apparently conflicting views” (Wong and Leung 2001, p. 106). This model contains five basic elements building a strategic *guanxi* management process (Wong and Leung 2001):

1. Analysis of the changing relationship context: This phase applies the so-called SPACE-approach in order to understand the system (macroeconomic, political and legal environment), changes in the societal environment, the personalism related to family and kin networks, the individual self by employing empathy and the adaptation of business organizations as a result of synergy, pragmatism,

commitment of each party and empathy inside members of a given network (Wong and Leung 2001).

- Market intelligence in the form of *guanxi* perceptual positioning: This phase is to get a better understanding of the positioning of *guanxi* in order to plan marketing measures. Therefore, Wong and Leung (2001, p. 126) suggest a progression abbreviated DFAT (dependence, favor, adaptation, trust) and explain:

The order of the letters represents the progression from dependence to trust. Owing to dependence on another party, one party may attempt to minimize the risk of uncertainty by exchanging favor with other members inside the guanxi network. If the exchange is productive, the members will continue adapting their behavior to accommodate the weakness of the other party. This adaptation process eventually leads to mutual trust. The DFAT concept does not require any absolute sequence or a causal link, because there are too many variables in the real world.

Related to each of the DFAT-constructs and the respective degree of adaptation is a certain status within a *guanxi* relationship: unadapted outsider (fencer), adapted outsider (fiancé), unadapted insider (new friend), adapted insider (old friend). This status affects the *guanxi* interaction process between the involved business organizations. In analogy to a love couple the interaction process related to the status is described as *beware* (fencer), *benefit* (fiancé), *belonging* (new friend) and *beloved* (old friend). Thus, being aware of one’s status in a business relationship helps to implement the right marketing strategy. Furthermore, there are different routes of going through these status stages in order to establish and maintain good *guanxi*. The perceptual map of Wong and Leung (2001) depicts the different status stages according to the level of interaction and adaptation and respective routes towards the status of an old friend, i. e. a business relationship of mutual interdependence and trust.

- Guanxi* strategies: Fig. 6.8 outlines that there are different routes towards good *guanxi* (old friend): The I-route (F1-F4), the L-route (F1-F3-F4) and the Z-route (F1-F3-F2-F4). In addition to the depicted three routes there are two more routes

Fig. 6.8 Guanxi positioning map and development routes. Source: Based on Wong and Leung (2001, p. 117)

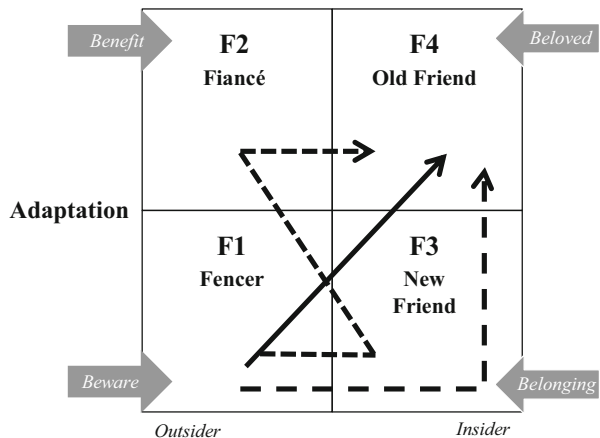


Table 6.4 Major dimensions behind Chinese business relationship building

Dimension	Mind	Heart
Face and favor-exchange		
Negotiation behaviour	Based on concept of profit motive	Based on concept of reputation and future interest
Social bonding	Mutuality	Face saving
Favoritism	Less favoritism, limited obligation and equal give-and-take	More favoritism, lifelong obligation and maybe less equality at the starting stage
Flexibility		
Role expectation	Explicit	Implicit
Role boundaries	Within the pre-determined role expectations	Beyond the existing role expectations
Cooperation and continuity dependency of cooperation	Based on the concept of conflict resolution and profit motive	Based on the concept of harmony, flexibility and may emphasize social objectives
Guiding principle in shared- value	Less emphasis on social closeness and friendship (based on legality and rule)	More emphasis on friendship (based on morality and social norms)
Involvement in continuity	Economic	Affective
Commitment	Based on calculated risks	Based on social sanction and personal network
Type of commitment	Calculated commitment	Affective commitment

Source: Based on Wong et al. (2007, p. 882)

(F1-F2-F4 and F1-F2-F3-F4). Ideally, the short I-route is taken. However, this is not always possible due to several factors related to the relationship context and the *guanxi* implementation process.

4. Implementation of *guanxi* management: The implementation of a certain *guanxi* strategy has to take the different perceptions of relationships in the West and in China into account (Wong and Leung 2001, p. 106 ff.). This means the complex interaction of mind and heart approaches as contrasted in Table 6.4. On the mind side, association and bonding of the key persons of the respective organizations lead to commitment of either party. On the heart side, empathy for the other party's needs and face-giving and face-saving lead to defensiveness, i. e. a mechanism of mistrust towards persons outside of the *guanxi* network and a clear distinction between outsiders and insiders. The "*two major concepts, commitment and defensiveness, are "self-contradictory" because commitment implies responsibility but defensiveness implies responsibility avoidance*" (Wong and Leung 2001, p. 109). These two opposing poles are combined and create the dynamic of *guanxi*-based relationship management. However, in case of conflict between mind and heart, Chinese will usually follow their heart and give preference to those who are already members of their network. Leung

et al. (1996) found accordingly that especially communication activities and daily operations, e. g. maintenance of a good relationship network, identification of correct China contacts, on-site visits to China contacts or monitoring market trends, are vital for *guanxi* building and business development in China. In contrary, the identified, for instance, lack of communication with China contacts, lack of contact network, lack of updated market information or change of key players during negotiations as key factors leading to a failed business deal in China.

5. *Guanxi* evaluation in adaptation and performance: Furthermore, but not necessarily eventual, the *guanxi* management process involves an evaluation of the adaptation and performance within the specific business relationships. Therefore, a continuous context analysis (see SPACE-approach above) has to be undertaken. In that way, potential changes like new government regulations or changing key contacts can be identified, their impact can be assessed and measures can be taken to adjust the degree of adaptation and consequently the performance.

The comprehensive *guanxi*-model of Wong and Leung (2001) helps Westerners to analyze and manage business relationships with Chinese by providing an overview of the different interrelated perspectives on a potential European-Chinese buyer-seller-relationship.

6.5 Managerial Implications for Doing Business in China

6.5.1 Contemporary Business Culture in China

The Chinese culture, particularly the Chinese business culture, is experiencing unprecedented changes over the past three decades due to the transition from a centrally planned towards a market economy. On the one hand, traditional Chinese business customs are mixed together with the Western ones, for example, the application of *guanxi* and military treatise to relational marketing management. On the other hand, the Chinese business culture is also strongly influenced by Western cultures (e.g., Bailey et al. 1997). International business rules and laws/regulations are highly respected and increasingly applied. Business deals, which used to be nailed by a gentlemen's agreement between the ones with a close *guanxi*-relationship are increasingly replaced by contract agreements. The situation that "a businessman's one oral promise is worth one thousand ponds of gold" (a Chinese idiom, 一诺千金) is therefore no longer the case in business. In addition, the provinces/regions have various customs and traditions within China, their economic developments are also highly imbalanced. Marketers should not assume the existence of within-country homogeneity (Wang 2013), and individual

approaches/strategies are thus recommended to be used when interacting with firms from different regions of China.

6.5.2 Relational Marketing “Package” in China

As previously discussed in the third section, *guanxi*, harmony and military treaties/stratagems can never be overstressed. In fact, these three factors interact with each other and serve systematically as a whole Chinese relational marketing “package”. *Guanxi* could be regarded as a technique or tool that can help initiate and maintain business relationships. When an inter-organizational/inter-personal relationship is built, a harmonious atmosphere is needed to maintain and deepen the relationship. Harmony is even more important when disagreement exists, and conflicts should be best avoided and cautiously handled. The Chinese believe “to be courteous before the use of force” (先礼后兵), pointing out that destroying harmony is always the second choice in China. Once harmony is jeopardized, whoever should take the blame, emotional feelings (*ganqing*) are hurt, faces (*mianzi*) are lost, and it is incredibly difficult to repair them afterwards.

6.5.3 Business Strategies in China

The Art of War provides strategies in B2B relationships. It seems like a paradox that on the one hand, firms should keep good *guanxi* and be harmonious with their business partners; On the other hand, they are supposed to use strategies on them, while it is not. In fact, *guanxi* and harmony themselves can be regarded as strategies. From a broader perspective, all the efforts placed on building *guanxi* and safeguarding harmony are actually implemented softly as structured strategies aiming at smoothing business and gaining more benefits from relationships. From a narrower perspective, many strategies directly convey the ideas of building *guanxi* and safeguarding harmony in order to confuse the counterparts, such as 笑里藏刀 (hiding a dagger in a smile, one of the thirty-six stratagems), 合纵连横 (first allying with some of the opponents to fight the strongest, and then breaking the alliance and fighting the rest) and so on. Of course, such strategies are not long-term oriented, and a lame use of them could be relatively easy to detect, therefore they should be carefully exerted to avoid negative effects on *xinren* (trust), *ganqing* (emotional affection) and harmony.

6.6 Summary

The primary aim of this chapter is to illustrate the essential role of culture in business relationship marketing, especially when the cultural distance is as great as in the case of Europe and China. Shifting away from acquisitions/transactions toward retention/relationships, relationship marketing and management puts great

emphasis on businesspeople and organizations, and their behaviors and interactions. Consequently, substantive knowledge about the culturally determined behavioral patterns and values of foreign business partners is invaluable for businesspeople involved in international business.

Against the context of European-Chinese business relationships, major concepts of cultural values and their representation in business as well as differences in cross-cultural communication were outlined. A comparison of selected European countries like Germany and China along these general values and communication patterns revealed differences in, for instance, hierarchy and group orientation and explicit vs. implicit communication. With regard to business relationships, key factors facilitating Western business relationships like trust and fairness and their counterparts of the Chinese *guanxi*-system like face and harmony were juxtaposed. *Guanxi* has been shown to be the common behavioral pattern guiding business interactions in the Chinese world; harmony is the atmosphere that all business parties should preserve and face needs to be given and saved by all means. Furthermore, commonly known and applied military strategies (stratagems) are supposed to be used by Chinese when it is necessary to keep the business in an optimal position even though *guanxi* and harmony are given.

Finally, three selected approaches for the management of European-Chinese business relationships were introduced and explained. These approaches point out the notion of mutual adaptation and understanding for cross-cultural business relationships to succeed.

Appendix

Exercises

1. Explain what culture is and why it matters to business relationships!
2. In what ways do the Chinese culture and European cultures like Germany differ? What are potential impacts on business interaction deriving from these differences?
3. Explain the notion of context, space and time in an intercultural communication situation! Outline specific differences of Western and Eastern cultures!
4. Describe the Western understanding of business relationships and contrast it to the Chinese one!
5. Comment on the statement “Guanxi is unethical and nothing more than corruption”!
6. Explain how a gap analysis in cross-cultural negotiations works!
7. When should companies follow a third-culture building approach in cross-cultural business relationships?
8. Explain the comprehensive *guanxi* management model of Wong and Leung and outline implications for doing business in China!
9. Explain the relationships among *Guanxi*, Harmony and Sun Tzu Stratagems when dealing with Chinese business partners.

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Part III

Implementation of Business Relationship Management

Ingmar Geiger and Michael Kleinaltenkamp

7.1 Introduction

“The customer is king.” This is not only the guiding principle of marketing, it is also a common everyday phrase—and it could serve as the motto for external implementation of business relationship management. In the first two parts of our book, we penetrated the theory of business relationship management, then we introduced its analysis and planning tasks. The third part of the book and especially this Chap. 6 are dedicated to the implementation of business relationship management. What can and should a company do to create value for its customers? What should a company do to defend its own business relationships from the competition? How can they be made profitable?

The business relationship management instruments introduced in this chapter are intended to fill the effectiveness dimension of the business relationship management—meaning the creation of customer value—with ideas and life. The issue of efficiency and thus generation of a supplier advantage are covered in Chap. 3. Following this introduction, we will concentrate on the four instrumental aspects of marketing (product, distribution, communication and pricing policies) to present and discuss approaches for generating and maintaining customer value. It should be noted that the four aspects sometimes overlap significantly: The focus of marketing in business relationship management is the customer, not a single product. It is also important to point out that the portrayal in this chapter refers primarily to the management of existing business relationships. Other, additional instruments may be needed to establish new business relationships (Bruhn 2007).

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7.1.1 Customer Loyalty as the Objective of Instrument Application

As we saw in the previous Chap. 5, the strategic goal of an existing, profitable business relationship is to preserve and defend the relationship. So the basic concept is to bind the customer to the company. The fundamental ways to achieve this are by maintaining or **increasing the value for the customer** and by **creating switching costs for the customer**. Empirical research increasingly shows that customers are particularly prone to become and remain loyal if the value of the relationship is right for them and not because they feel compelled to remain in a business relationship because of high switching costs (Geiger et al. 2012; Saab 2007).

In regard to the value for the customer, three approaches were presented in Sect. 5.3.1: improvement of the core product, improvement of the procurement and interaction process and enhancement of customer operations, whereby benefit and cost aspects can be improved for the customer in all three areas. Three aspects are particularly relevant:

- Reference object: As we saw in Chap. 3, a company can facilitate an increase in value for the customer at the level of an individual transaction as well as at the level of the business relationship (Chap. 3).
- Reference to competition: Generating a customer benefit is always based on the service offered by the competition (Cannon and Homburg 2001; Ulaga and Eggert 2006). So it is not a company's job to satisfy a customer 100 % but simply to offer more value than a competitor would.
- Reference to time period: Because loyalty is time-related in nature, maintaining the status quo is not enough to achieve a long-term customer benefit. Loyalty is founded on a business relationship over a time span, and it must be developed again and again.

The instruments presented here should be considered examples of ways to achieve customer loyalty. Because of the vast differences in technology and business processes in modern business-to-business markets, the business relationship management instruments explained here can only be considered exemplary. However, they offer a general understanding of the vast possibilities and directions for the instrumental constellation of a business relationship. This is especially pertinent in that a broad empirical study of the effectiveness of various instruments and specifically their impact on a company's financial success is still missing in different contexts (Palmatier et al. 2006b).

7.1.2 Secondary Effects of Instrument Application to the Supplier Company

Since in business relationship management the object of the marketing efforts is the individual customer and the goal is to find a solution to meet his needs and solve his

problems within the business relationship, instruments from different instrumental fields of marketing are often merged to form an overall package of measures. In cases in which the business relationships are particularly intensive, it happens again and again that close **cooperations between customer and supplier** arise (Kleinaltenkamp 1997). These are necessary on the one hand to achieve the planned customer benefit. On the other hand, they often lead to the supplier achieving **additional benefits** for himself besides the payment agreed for his services.

When it comes to a supplier's product policies, these benefits frequently take the shape of **know how accrual** gained through cooperation with the customer. In light of longer development times and increasing development costs for products, shorter product life cycles and higher flop rates of innovations, the knowledge and capabilities collected with important customers can be essential to a company's survival. We will go into this in detail in Sect. 7.2.4.4, when we introduce the lead user concept.

In regard to communication policies, especially in light of the development of the mobile internet and the propagation of social media in business-to-business fields, **communication-based cooperation with customers** is more important than ever to the supplier. When different customers share their experiences with the supplier's offerings, e.g. in so-called user groups or in internet forums, the supplier company can use this type of information as a means of communication. For example, when users of a product share information with one another, it appears more credible than when the supplier conveys the same information (Carl 2008). If such exchanges take place in a publicly accessible forum, the supplier can tell other customers about the forum, thus diminishing uncertainties in regard to use of the product. On the other hand, communication-based cooperation with customers offers an opportunity to collect information for market research purposes, e.g. with regard to planning new products, prices and distribution channels. The user group as a potential type of communication-based cooperation with customers will be examined in Sect. 7.4.3.

7.2 Instruments of Product Policies

Although modern business-to-business markets offer a much wider range of services than ever and there can be no "one size fits all" solution for product policies, a few developments can still be detected that apply equally to many offerings within business relationships. These developments can in turn serve as the starting point when considering how to design a supplier's specific product policies to maintain customer benefits. So in this section we will focus on the development from product to solution supplier (Sect. 7.2.1), service/product customization and customer integration (Sect. 7.2.2), cross-selling (Sect. 7.2.3) and the meaning of product-related services (Sect. 7.2.4).

7.2.1 From Product Supplier to Solution Supplier

As they were searching for ways to achieve competitive advantages in the 1980s and 1990s, corporate managers focused more and more on firm's purchasing functions. As **valuation creation activities shifted increasingly to component suppliers**, the own contribution to value creation drastically decreased for many companies that were previously strongly vertically integrated. However, the number of component suppliers also increased, which in turn led to high costs for dealing with so many component suppliers. This is why many companies decreased their number of component suppliers and strengthened their ties to the remaining suppliers, purchasing more extensive products and services from them (Kalwani and Narayandas 1995). For the structure in the automotive industry, this meant the construction of a supplier pyramid (Backhaus and Voeth 2010): The OEM is at the top of the pyramid. He purchases essential systems from his first-tier suppliers and has some of them installed directly by the suppliers. The numerous second-tier suppliers needed for the systems, on the other hand, have nothing directly to do with the OEM anymore.

This phenomenon has significantly changed the entire structure of the industry, and it can be observed in many other industries as well. Companies that used to focus on certain (physical) products have moved away from marketing only the core product. They have come to realize that customers are not primarily interested in a product or service but that they are seeking a solution to their problems. Suppliers attempt to meet this demand by offering **solutions** instead of products or services (Storbacka et al. 2011). Solutions are comprised of a combination of physical products and services as well as their application in a common process to create value between the supplier and the customer. This often leads to the supplier becoming deeply integrated in the customer's value-adding process (Cova and Salle 2008), which ideally creates value for the customer and definitely increases his switching costs. Example 1 shows how the introduction of such a solution creates value for the supplier and the purchaser.

Example 1: Management of C-parts by Würth Industrie Service for Liebherr

In the mid-1990s, the Würth group, which originated from a wholesaler for screws and nuts founded in 1945, established the business segment Würth Industrie Service. The intention was to offer industrial customers comprehensive solutions. At the same time, Liebherr, one of the world's largest manufacturers of construction equipment, was planning to standardize the management of C-parts throughout the corporation and introduce a kanban system for their provision and allocation. C-parts are low-value items, the procurement cost of which is very high in relation to the value of the goods. Screw and plug fittings, dowels and clamps, and chemical-technical products are good examples. Würth Industrie Service was ultimately awarded the

(continued)

contract to implement the C-parts management system. It makes sure that the 120,000 kanban containers at 15 Liebherr plants around the world are never empty. Liebherr has over 10,000 different C-parts on hand in the quantities needed. Würth supplies Liebherr with over 200 million of these parts every year. The processes and logistics are continuously optimized, ensuring that the prices, assortment, quality and scheduling remain at a satisfactory level. In addition to high customer loyalty, this partnership has brought Würth Industrie Service a dramatic advance in knowledge and extensive access to the construction machinery market. The next steps intended to expand the partnership include technical consulting and development by Würth Industrie Service (Hermes 2011).

For many companies, offering such system solutions is a steep challenge. Looking back over time, it is apparent that especially major manufacturers of physical products added services to their portfolios and successively became a system supplier. IBM, General Electric and Nokia are good examples of this (Davies et al. 2007). This put IBM in a position in the early 1990s where it could on its own offer its business customers solutions that included hardware, software and all of the supporting services. This reflects the case of the **pure system supplier**. However, for many smaller companies such vertical integration is not feasible; for them it makes more sense to act as a **system integrator**, purchasing the required components from others and then coordinating and integrating them themselves. Figure 7.1 shows the differences.

Table 7.1 illustrates the respective benefits of implementing solution offerings as a system supplier or system integrator.

In the actual corporate world, there are of course a wealth of hybrids between the prototype models shown here. Besides careful consideration of the make-or-buy decisions regarding the components of an offered solution, for many companies the pricing policies for such solutions seem to pose an important challenge. Many customers realize the value of the solution offered, but the suppliers are sometimes not able to translate this into greater willingness-to-pay (Bonnemeier et al. 2010).

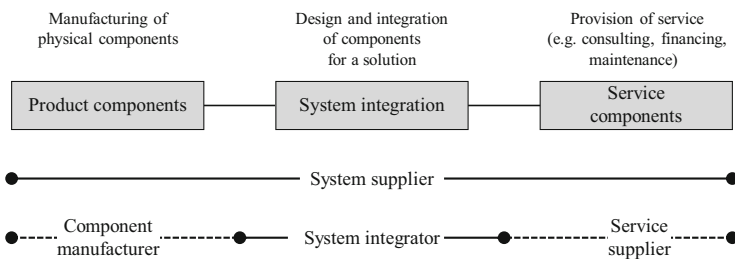


Fig. 7.1 Fields of activities of system supplier and system integrator. Source: Based on Davies et al. (2007)

Table 7.1 Comparison of system supplier and system integrator offerings

Advantages of a pure system supplier	Advantages of a pure system integrator
Control of all components of the solution offered	Integrator of externally acquired parts and components
One stop shopping: profound knowledge of own technology and system architecture	The entire range of technology: Clear understanding of competing standards and system architectures
Standardized components and possibly own interface standards	Modular components and standardized interfaces
Vertically integrated: backwards to physical products, forwards to services	Specialized: precise knowledge of system and component level
Reduced transaction costs and internal transfer prices	Market price advantages by comparing competing component suppliers
Coordination of internal departments and areas	System integrator works in a network of component suppliers
Reliable delivery of all solution components	Access to leading suppliers of components and skills
Stable and enduring organizational structures	Flexible time-limited organization tailored to meet the customer's needs
Extensive know-how in the product field and after sales service	Core competencies in system integration and product management
Bundled products of standardized components at a bundled price	Sale of single components and skills or those integrated to form a system solution

Source: Based on Davies et al. (2007)

7.2.2 Service/Product Customization and Customer Integration

A company's transitioning from being a pure product or service supplier to becoming a solution provider is accompanied by **customization of the offering**, meaning the solution tailored to meet the customer's needs. For example, in the fiercely competitive market for large medical equipment such as magnetic resonance imaging, Siemens sees itself as a solution supplier. In addition to the actual device, the company offers various services (Kotler et al. 2007): Construction advice for the rooms needed to house the equipment, equipment installation, training of operating personnel, financing offers, 24-h repair service, online troubleshooting and much more. However, from this vast range of additional services, Siemens offers each hospital only the services that it actually needs. The respective solution package is always designed to meet the individual wishes of the customers.

This requires that the customer contribute his own resources for the supplier to be able to offer his service. Such **customer resources** can be information, persons, objects, rights or nominal goods that the supplier temporarily provides. The customer to some extent becomes integrated in the manufacturer's service creation process. Figure 7.2 demonstrates the principle of **customer integration**.

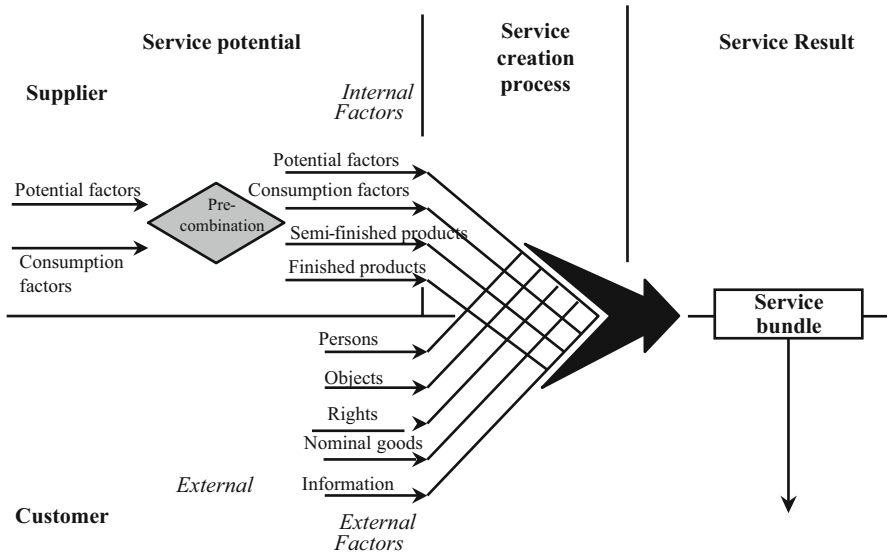


Fig. 7.2 Integrative service creation. Source: Based on Kleinaltenkamp (2008, p. 434)

In regard to the integration of the customer's resources, there are four potential cases, differing from one another in regard to time and location (Kleinaltenkamp et al. 2004). In the first case, the supplier implements resources over the long term with the customer, typical e.g. for transportation networks or repair centers. In the second case, the supplier's resources are applied only temporarily by the customer and then taken back once the service has been created. Maintenance and service work are examples of this. In the third case the customer relocates his resources and the service is created at the supplier's facility, e.g. when ships or airplanes are serviced. The last case allows the resources to be merged virtually, like remote diagnosis and maintenance. Figure 7.3 shows the different types of resource integration.

The way in which resources are integrated is often determined by technical aspects, such as when the supplier's or customer's resources are immovable. If this is not the case, effectiveness and efficiency factors are decisive, whereby virtual creation of services can demonstrate its advantages.

Because the customer is more integrated in the service creation process, a transaction that proceeds successfully for both parties leads to **bonding effects**. These effects are the result of switching costs incurred by the customer for the transactions on the one hand. On the other hand they result from learning processes experienced by the supplier.

Switching costs that the customer incurs through customer integration can be attributed to having gained the customer's trust and to resource specificity of factors related to the customer (Kleinaltenkamp 2008).

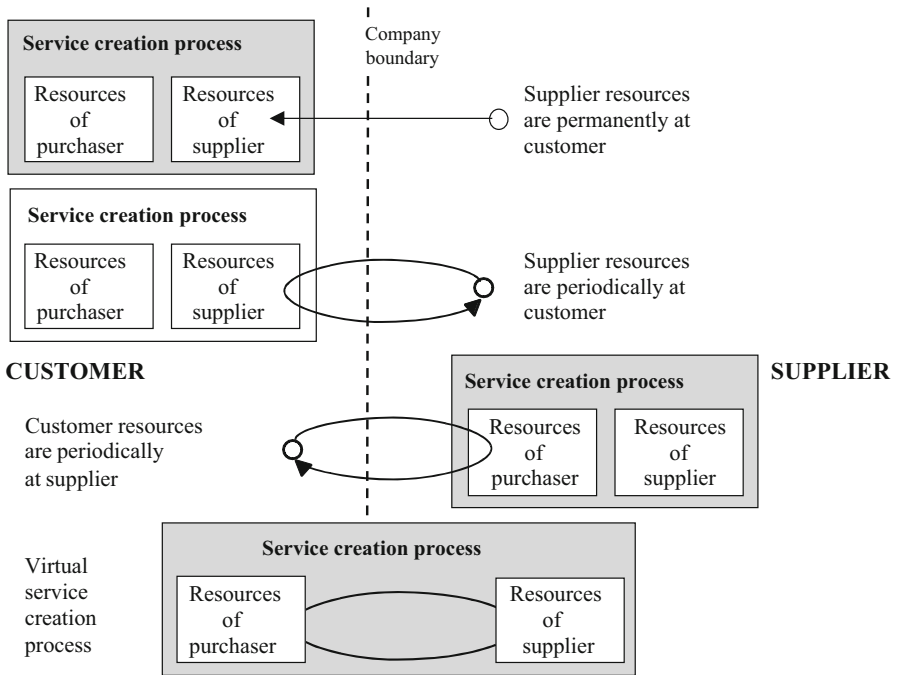


Fig. 7.3 Resource integration in the individual creation of service. Source: Based on Kleinaltenkamp et al. (2004, p. 632)

When an individual solution is to be created, the customer often cannot determine yet upon conclusion of the contract whether the supplier really can provide the solution that the customer expects. The essential risk is that, when the service is created, the production factors required of the customer (primarily information, but also persons, rights and objects) are not or cannot be completely provided, leading to faults in service creation. So the solution supplier has to strive to minimize the **risk perceived by the customer** ahead of such a transaction. If a supplier has already performed previous transactions with this customer, which is common in business relationships, and he has managed integration of customer factors well, the customer's trust in this supplier (in-supplier) will most likely be greater than the trust he would have in an out-supplier. So the supplier's goal should be to integrate external factors, particularly information required from the customer. Instruments such as those included in Table 7.2 are well suited to this purpose.

If services specific to one customer are planned to extend over a longer period, such as those described in Example 1 between Würth Industrie Service and Liebherr, customers are often encouraged or even obligated to make specific investments in the business relationship with the supplier themselves. A classic example of this is the establishment of remote data transmission with application-specific software; this is common with just-in-time supply agreements. A customer does not reap the maximum benefit of such **specific investments in a business**

Table 7.2 Selected instruments for obtaining information related to single customers

	Information needs	Information media	Gathering information		
			Interface constellation	Communication channels	
Partial approaches	<ul style="list-style-type: none"> • Specifications from customer (problem concept, required effectiveness, use concept, “whats”) • Specifications from supplier (solution concept, required objects, technology concept, “how”) 	<ul style="list-style-type: none"> • Buying center analysis • Promoter model • Value chain engineering 	<ul style="list-style-type: none"> • Cooperation approach (team building) • Qualification approach (employee qualification) • Organization approach (application engineering) 	<p><i>Data collection</i></p> <ul style="list-style-type: none"> • On-site presence • Exchange of samples • Exchange of personnel <p><i>Information transfer:</i></p> <ul style="list-style-type: none"> • Public networks • Terminals 	<ul style="list-style-type: none"> • Blueprinting
Comprehensive approaches	<ul style="list-style-type: none"> • Simultaneous engineering • Total quality management (TQM) • Quality function deployment (QFD) 				

Source: Based on Weiber and Jacob (2000)

relationship until subsequent transactions with the supplier occur. In an alternative supply relationship, such investments would have to be made all over again. So if a supplier is successful in expanding customer integration as a prerequisite for even better solutions to include specific investments, the business relationship becomes even stronger.

In addition to an increase in the customer's switching costs, successful customer integration also leads to **learning processes for the supplier** (Kleinaltenkamp and Dahlke 2006). In the course of creating a service, the supplier inevitably gains insight into certain circumstances surrounding the customer, into problems and also potential approaches to solving the problems. Especially in sectors in which customer integration is essential, e.g. management consulting, further transactions between the supplier and the customer are frequently the result of the supplier identifying problematic issues in the course of creating a service and then presenting a solution to the customer. The knowledge that the supplier gains through customer integration can be used to create better and even more individualized solutions for future transactions as well as to streamline customer integration processes (Kleinaltenkamp 2008).

7.2.3 Cross-selling

One possible first step from being a product supplier to becoming a solution supplier is **cross-selling**. With cross-selling, customers are offered additional physical products and services besides those already being purchased from the supplier. The intention of cross-selling is to achieve sales to an existing customer that affect multiple offers (Homburg and Schäfer 2006). For the customer, benefits can include preferential treatment by the supplier and cost reductions due to a decrease on the side of the total supplier base.

By practicing cross-selling, companies hope to create **growth opportunities** in otherwise stagnant markets by increasing the supplier share with their own customers; this is considered easier than acquiring new customers (Kamakura et al. 1991). Another aspect that makes cross-selling attractive is that the achieved revenue increases generally go along with disproportionately lower cost increases. Publications also point out the mutual positive effect of customer loyalty and cross-selling (Reinartz et al. 2008).

In light of this, it is even more amazing that the cross-selling potential has been utilized only inadequately in many industries. According to an empirical study by Schäfer (2002), companies in the chemical and the mechanical engineering sector exploit only 32.6 and 34.9 % of the cross-selling potential—and they are amongst the forerunners (Homburg and Schäfer 2006).

Cross-selling always begins with the customer's **needs for additional services**. It is irrelevant whether these are previously unmet needs or needs that have been met by a different supplier in the past. The supplier needs to reveal the customer's unmet needs, especially latent needs, meaning that the customer has recognized the problem but has not found an acceptable solution. If the customer's needs for cross-

selling services have so far been met by other suppliers, cross-selling endeavors are comparable to predatory competition.

In regard to the timing of cross-selling, additional services can be offered at the same time as the original service as well as deferred. As current examples in consumer marketing have shown (e.g. when a customer buys a sandwich at a rest area, he is asked if he would like coffee to go along with it), cross-selling does not always require a business relationship, although such a relationship does facilitate cross-selling (Reinartz et al. 2008). However, a relation between the original service and the additional offer is necessary in the business-to-business sector. Whether or not the additional service is something that is already part of the supplier's assortment is irrelevant to cross-selling, as long as an additionally revealed need of the customer can be met (Homburg and Schäfer 2006). Such a case is similar to the constellation of the system integrator introduced in Sect. 7.2.1.

While the specific constellation of cross-selling, particularly the additional services offered, are very different in different industries and companies, preliminary empirical findings have revealed generally applicable success factors that promote successful cross-selling in the field of sales and business relationship management (Homburg and Schäfer 2006). These include:

- Product customization
- In-depth knowledge of the customer's business processes
- Frequent contact with the customer to offer support when problems arise
- Frequent contact with the customer to provide information on new products
- Frequent contact with the customer to determine his wishes
- Frequent contact with the customer to determine changes in his needs
- Frequent contact with the customer to detect potential for optimizing the business relationship
- Frequent contact with the customer to measure customer satisfaction.

7.2.4 Product-related Services

As the previous sections stated, it is often product-related services that open the door to a supplier, allowing the supplier to be seen as a problem solver and to be successful in cross-selling. The vast diversity of today's business-to-business markets makes it impossible to list and characterize all of the services (Belz et al. 1997). Figure 7.4 offers an overview of the broad range of product-related services.

This section will examine **product-related services** that can be used in various industries as instruments of business relationship management. After-sales service is the most closely related to a physical core product, while the services discussed subsequently can be considered value-added services.

The quality of the product-related services has a considerable effect on the benefit that the customer perceives from the business relationship (Homburg et al. 2005; Menon et al. 2005). In addition to maintaining minimum service quality

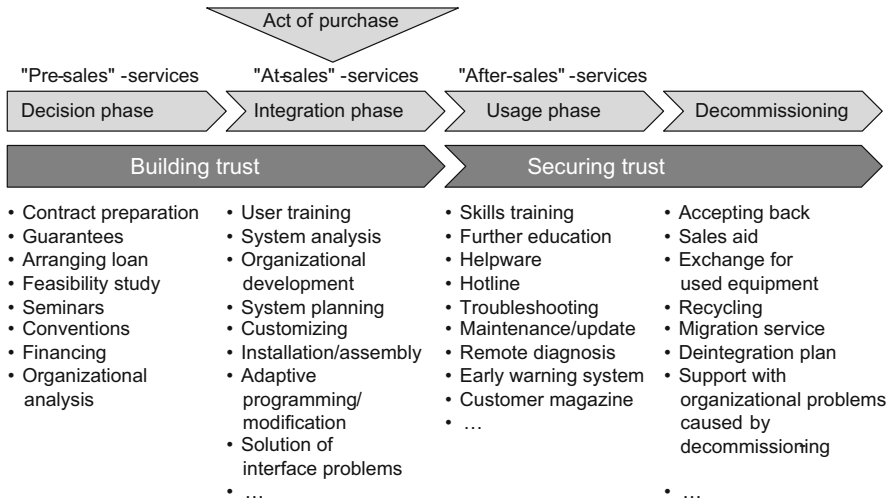


Fig. 7.4 System components of services. Source: Based on Wimmer and Zerr (1995)

standards, it is important that the supplier charge the customer for the product-related services (Ploetner 2008).

7.2.4.1 After-Sales Service

The first logical reaction to the call for product-related services to complement a core product and achieve stronger customer loyalty is to establish and expand **after-sales service**. Empirical studies show that, for all companies in the manufacturing industry, after sales service account for only about 25 % of revenue but for about 40–50 % of profit (Kim et al. 2007).

We consider after sales service as such to include all services required to facilitate use of the core offering, often a physical core product, and to minimize potential problems. Such services generally include installation and commissioning, provision of spare parts and technical guidance on product use, maintenance and warranties (Asugman et al. 1997). Some authors consider all product-related services to be after-sales service (Baumbach and Müller 1997); we wish to refrain from this concept.

Although some components of after-sales service have become standard and the customer expects to receive them free of charge (Morschett 2006), others provide an opportunity for particularly **high rates of return**: This is the case when the customer is more interested in supply availability and the reaction time for services (maintenance, troubleshooting, delivery of spare parts) than in the price (Baumbach and Müller 1997). This preference usually prevails when the customer uses the core product intensively (e.g. metal cutting machine tool or a software system) and its failure would mean substantially higher downtime expenses elsewhere. To provide complete coverage for any problems that may arise, many suppliers now offer their customers **full service contracts** as shown in Fig. 7.5.

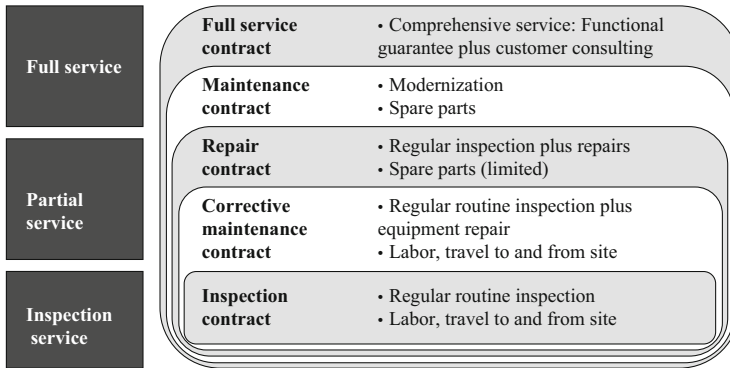


Fig. 7.5 Classification of after sales service contracts. Source: Based on Baumbach and Müller (1997)

When after-sales service includes the provision of services, it should be kept in mind that suppliers of industrial commodities often need other capabilities and that their competitors are others than those of OEMs. This includes particularly service logistics, technology and distribution (Baumbach and Müller 1997). For example, quick and reliable spare parts logistics is a fundamental requirement of efficient after-sales service. While national and regional after-sales offers have now reached a satisfactory level for most customers, this does not seem to be consistently the case with **international business relationships** (Asugman et al. 1997; Morschett 2006). The preferred method for achieving the service level in these business relationships as well often first involves external partners (Morschett 2006), similar to what can be seen in Fig. 7.1 in case of the system integrator.

As with all product-related services, pricing is a critical aspect of after-sales service itself. While fixed price contracts or cost-based agreements based on the provision of individual services as the basis for the compensation used to be common, nowadays so-called **performance contracting** is becoming more prevalent (Kim et al. 2007). With this concept, it is not the performed service that serves as the basis for the price but a pre-defined result of the service (Sect. 7.5.2). Such performance contracting requires the supplier to be in complete control of his processes, but it makes the documentation processes associated with provision of the service easier and reduces fluctuations in payments. For the customer, performance contracting means lower risk: The costs are set from the start, and the supplier is responsible for maintaining proper functioning of the core offering purchased. When this is accompanied by changes in the ownership structure of the production means, e.g. when ownership of spare parts is not transferred to the customer until the parts are needed, the customer can reduce his current assets and save capital costs.

7.2.4.2 Customer Training

Training as a product-related service consists primarily of the transfer from supplier to customer of information, know-how and suggestions for optimization of procurement or use of a product (Beutin 2008). In many cases the customer does not expect training and thus does not miss it. It does, however, give the supplier the opportunity to distinguish himself from the competition and establish true customer loyalty. The following Example 2 reveals how Goodyear was successful in doing this in the business relationship with tire dealers when it came to spare parts.

Example 2: Distance Learning at Goodyear

The US American tire manufacturer Goodyear was one of the first companies to use distance learning as a way to gain customer loyalty. Applying the method, Goodyear taught the tire fitters of its spare parts sales partners how to best mount its own tires. Until that point, the fitters preferred to mount tires for which they were thoroughly familiar with the installation process—and the new Goodyear tires were cast aside. Once the fitters had completed training, sales of Goodyear tires in the spare parts business rose significantly (unknown 2008).

When planning such **training contents**, one place to start is with all of the steps involved in the **use of a product**, whereby customers often have a difficult time with secondary aspects of use like occupational safety, as demonstrated by practical examples (Beyer 1998).

If a supplier decides to implement a training program for his customers, Llopis et al. (2006) suggest careful planning of the following aspects:

- Goals of the training program
- Selection of the customer's employees to be trained
- Duration and schedule of the training program
- Location of the training program
- Profiles of trainers needed
- Training methods
- Evaluation of the training program
- Pricing of the training program

Despite the great practical relevance of suppliers training their customers, marketing studies have dealt very little with this topic, so substantiated empirical findings have yet to be presented. One of the few empirical studies was, however, able to show that training programs for customers are particularly effective when they are designed to meet the needs expressed by the customer beforehand (Chow et al. 2008). So a training program not tailored to the customer's specific needs is much less effective.

7.2.4.3 Consulting on Improvement of Process and Quality

Besides customer training, **consulting on improvement of processes and quality** is especially effective in strengthening a business relationship. The basic concept is that the supplier and the customer use their respective and common skills to optimize the processes or quality in the customer's value creation. **Teams consisting of members from different companies** are often formed, reflecting the special capabilities of the participating partners (Stock 2006). The following Example 3 demonstrates how such a process improvement can occur.

Example 3: Optimizing Shipping Logistics at ThyssenKrupp Steel Europe

ThyssenKrupp Steel AG (TKS) is one of the global leaders in the manufacturing of high-quality flat steel, supplied primarily to the automotive industry. To ship its products to about 2,100 customers around the world as well as to provide raw materials to produce the steel, TKS works with Deutsch Bahn (DB, the German railroad company). DB uses flat cars developed especially for the steel industry to transport the TKS steel products. TKS and DB work together closely on optimizing TKS's inbound and outbound logistics and they conduct regular workshops as well. The marked improvement in quality in regard to order processing and information flow between the two companies was achieved with the implementation of the internet tool Rail Service Online. It facilitates status messages in realtime, ensuring a high degree of transparency in the shipping process (Jakubzig 2009).

Approaches to such process and quality improvements can be found in all of the customer's relevant **value-adding processes**. Suppliers and customers in many industries, e.g. in the automotive or paper industry, apply similar production technologies, such that any knowledge leads the supplier may have can be used to improve the customer's processes. Know-how transfer the other way around is also conceivable, such as when a component supplier is asked to participate in an automobile manufacturer's target costing project (see Sect. 5.3.1.3).

An important supplier decision when suggesting such process and quality improvement projects is the **structure of compensation**. In industries with fierce competition amongst suppliers, it may make sense for a supplier to implement such measures free of charge as a means to defend the business relationship. However, it is not advisable to do this in less competitive sectors; this could lead to the customer expecting regular "freebies." In cases in which the customer is basically open to this type of cooperation but is skeptical about the value of the additional services, **cost/benefit sharing models** have gained in popularity.

7.2.4.4 Lead User Concepts and Innovation Support

The last product-related service we will introduce here is the lead user concept, which represents close cooperation between supplier and customer with the goal of joint innovation. In contrast to the other product-related services, for which, put

simply, the principle of “service for payment” applies, with lead user cooperation both sides contribute their special skills, and an exchange of “service for service” comes about. For the supplier, a lead user cooperation can serve as an instrument to promote customer loyalty, but it is also intended to increase the company’s competitiveness as it relates to other customers.

According to the principles of the product life cycle concept as well as adoption and diffusion theory, the time at which purchasers in a relevant market are ready and willing to “adopt” a product—meaning to buy and use it—that is innovative to them varies (Kleinaltenkamp and Fließ 2002). Users who accept an innovative product first are referred to as **innovators**. Because of their early experiences with a product or with the first modifications to a product, they are of particular importance to the supplier. They serve as role models for subsequent customers and can provide a supplier with essential information that he can use for further marketing his innovative service. This relationship illustrated by the graph in Fig. 7.6, is the starting point of the **lead user concept**.

The term **lead user** was coined by Eric von Hippel (Hippel 1986). He defines lead users as follows (Hippel 1986): Lead users are customers or users of products, systems and/or services,

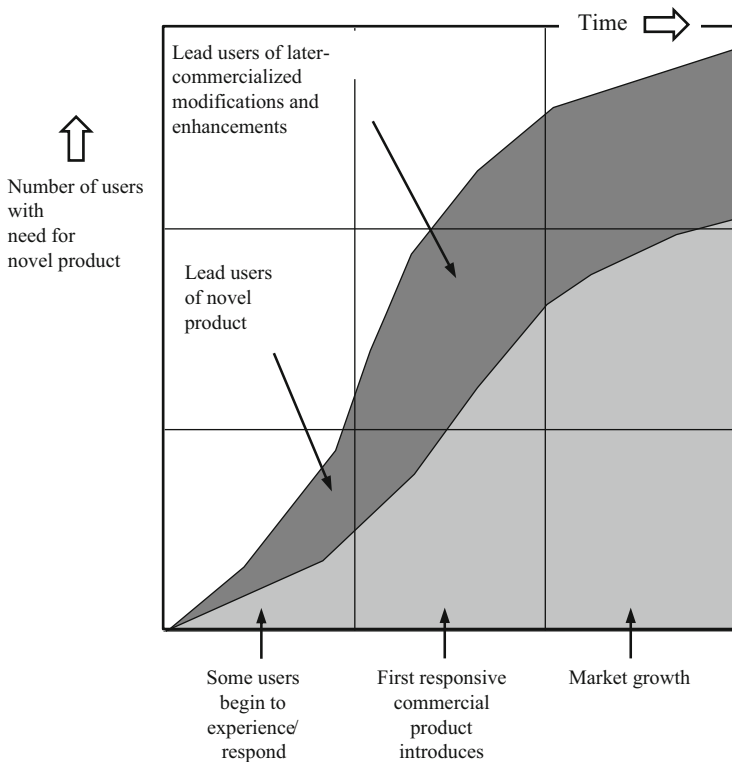


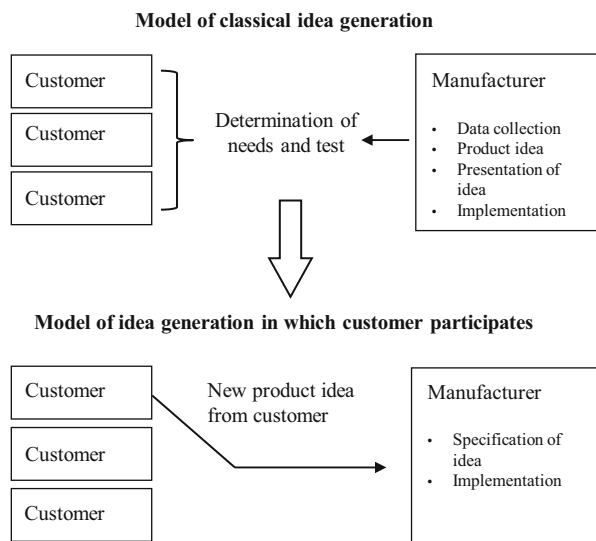
Fig. 7.6 Lead user in the product life cycle. Source: Based on Hippel (1986, p. 797)

- whose current needs can be considered exemplary for the future development of the overall demand in a market,
- who anticipate a substantial benefit from satisfying a certain need, making them more likely to provide data to meet this need,
- who have often implemented their own innovations intended to develop solutions to their problems and
- who are so interested in finding a solution that they frequently develop their own prototypes.

Von Hippel claims that customer demonstrating these traits are predestined to contribute to suppliers’ productivity increase in the development of new products in rapidly evolving markets in the business-to-business sector. This assessment is based on the assumption that customers with pertinent experience in future markets are better able to define future needs than customers—or even the supplier himself—without the relevant experience. It can also be assumed that customers who anticipate great benefit from a potential solution will make every effort to propagate the required knowledge and to develop the product concepts needed (Hippel 1986).

A hallmark of lead user cooperation amongst companies is that it extends well beyond the usual indirect way in which a supplier collects information, e.g. through market research surveys, as well as beyond the implementation of a product that the supplier would achieve on his own. A stronger, more targeted cooperation with leading suppliers can thus be summarized as changing from the “classical model of product idea generation” to the “model of customer contribution to product ideas”—a model from which the customer reaps benefits through participation (Fig. 7.7).

Fig. 7.7 Lead user cooperation transition from the classical model to the model of customer contribution to product ideas. Source: Based on Hippel (1978, p. 40)



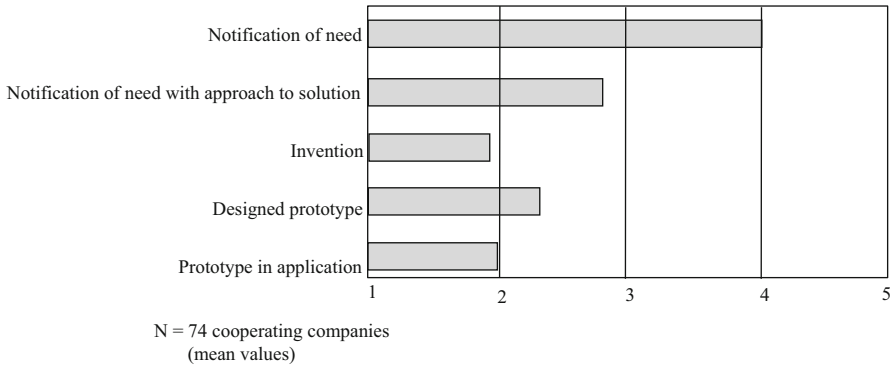


Fig. 7.8 Degree and frequency of customer initiative. Source: Based on (Kleinaltenkamp and Staudt 1991)

Empirical studies have shown that lead user cooperations are particularly prevalent in the field of research and development (Strothmann et al. 1979; Zörgiebel 1983; Kleinaltenkamp and Staudt 1991). The fact that manufacturers and users work together to develop solutions to problems does not say anything about the intensity of the cooperation though. An empirical study revealed obvious differences in regard to the extent and frequency of customer initiative. The “mere” notification of a need most often occurred before the type of notification in which a user has already designed an approach to a solution (Fig. 7.8).

This illustration clearly indicates the varying degrees of customer initiative in cooperation with a manufacturer. The two extremes are a **manufacturer-dominated innovation process** in which the producer controls all R&D, production and marketing activities, and a **user-dominated innovation process** in which the user handles all essential subtasks except for production (Fig. 7.9).

Cooperation with a lead user creates effects that happen before as well as after introduction of the new product. In positive cases, such a cooperation prior to introduction of a new product leads to an accelerated innovation process and a decrease in market entry barriers; synergies between manufacturers and lead users can be utilized to shorten product development time, attain a higher level of technology and reduce the cost of R&D applications. It is often precisely these effects that make entry into a market or earlier entry even possible. These correlations were confirmed in a series of empirical studies examining the most varied product and technological fields (Kirchmann 1994):

The R&D projects that Biegel examined also showed that success rates and contribution margins were much higher for developments initiated by the customer than for developments created by the supplier alone. And the cost of R&D was much higher for the supplier’s own creations than it was for projects initiated by the customer and was inverse to the success rate (Biegel 1988).

Among other findings, a study by Kirchmann revealed that cooperations with users have effects after introduction of the new product as well. This is because they

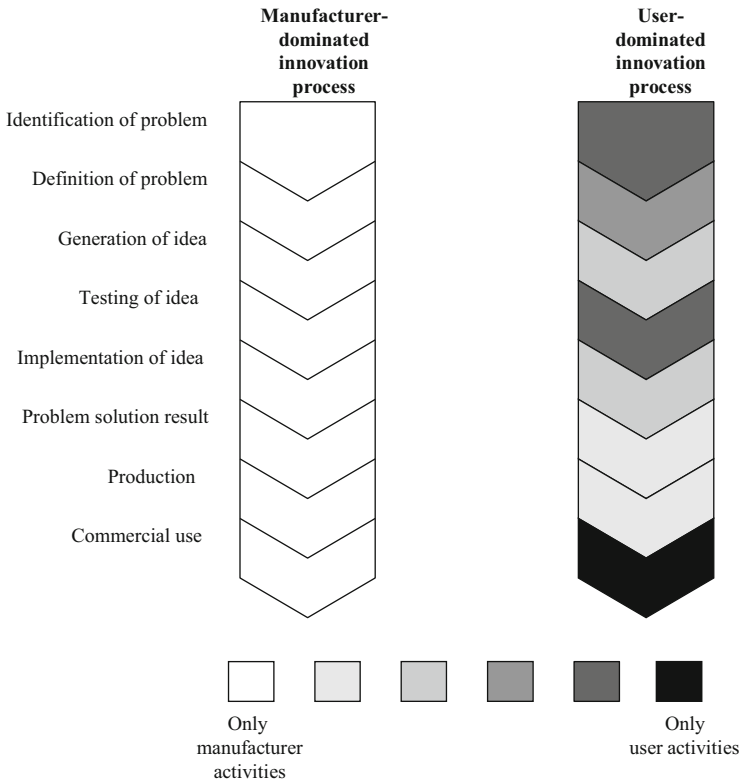
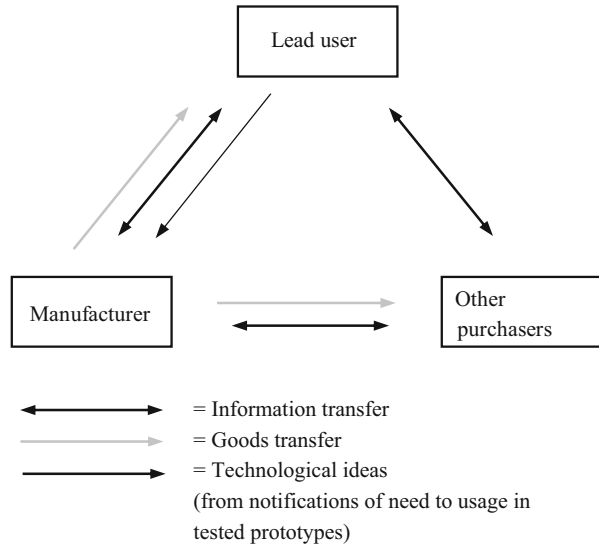


Fig. 7.9 Manufacturer-dominated and user-dominated innovation process. Source: Based on Kleinaltenkamp and Staudt (1991, p. 66)

contribute to improving adoption of a new product beyond just the circle of the lead user(s) (Kirchmann 1994).

Such an effect can be the result of a reduction in the risk associated with use of the product perceived by other potential customers. This can occur when lead users play an essential role in the flow of information to other purchasers by e.g. reporting in brochures or even in face-to-face discussions on their experiences with an installed **reference system** (Günter 1982), or when such a system is used for demonstrations for other customers. The impact can be amplified when a lead user becomes an opinion leader for other (potential) users. Then the customer can not only witness the functionality and quality of the product or production results, it also becomes easier to assess the product financially and to detect potential restructuring that may be required. In this respect the adoption processes are simplified or shortened even for users who are not part of a cooperation with the supplier, so working together successfully with lead users accelerates the diffusion of new products. The projects that Biegel examined also confirmed the positive impact of a cooperation with lead users after the new product was launched. It

Fig. 7.10 Potential impact of a lead user from a manufacturer's point of view. Source: Based on Kleinaltenkamp and Staudt (1991)



emerged that projects initiated by the customer were implemented much more quickly than a supplier's "own" creations (Biegel 1988). Another empirical study conducted at 3 M showed that products developed with the aid of the lead user concept generated revenue eight times higher than comparable innovations developed in a traditional innovation process (Lilien et al. 2002).

So from the point of view of a manufacturer in the business-to-business sector, the most appealing cooperation partners are users with a high **potential for innovation**, meaning a positive effect in regard to speed of the R&D process and to successful implementation of a new product, as well as a high **reference potential** for other customers in the target group to which the supplier aspires (Fig. 7.10).

Hence, the features mentioned here should be applied as selection criteria when choosing and approaching potential lead users.

Since it is also a fact that companies with long-term business relationships with their customers benefit from a significantly higher number of customer initiatives, it follows that consistent maintenance of the relationships with such interesting customers can make it easier to initiate lead user cooperations and can lead to greater success.

7.3 Instruments of Distribution Policies

Distribution policy is the second area of instrumental business relationship management that we will examine. These instruments are also intended to create a customer benefit that motivates the customer to remain in the business relationship. Therefore the two instruments introduced here are examples of tools that increase

customer loyalty. We will focus on **efficient consumer response** (Sect. 7.3.1) and **just-in-time delivery** (Sect. 7.3.2). While efficient consumer response emphasizes cooperation between a manufacturer and a retailer (some authors see it as a special type of just-in-time delivery; refer to Germain et al. 1994), just-in-time delivery refers primarily to business relationships between component suppliers and manufacturers. What both instruments have in common is that they require specific investments by the supplier and the customer and that they develop a strong impact on customer loyalty.

7.3.1 Efficient Consumer Response

The concept of efficient consumer response (ECR) dates back to an initiative by trading companies and manufacturers of brand-name products in the USA in 1992. The intention was to provide an opportunity to avoid the increasing competitive pressure from discounters and to reproduce the success of other cooperation models (Lietke 2009).

ECR can be interpreted as “*a comprehensive management concept on the basis of vertical cooperation between industry and trade, with the goal of more efficiently satisfying consumer needs*” (Seifert 2006, p. 52). The term covers customer (marketing) processes as well as supplier (particularly logistics) processes as shown in Table 7.3.

Implementation and coordination of the ECR sub-processes is based primarily on the establishment of a common IT architecture, which—in addition to the customer and supplier processes—is the third essential element of ECR (Corsten and Kumar 2005). The significance of information technology is apparent in the following Example 4.

Example 4: Efficient Consumer Response at dm

“With its specially created extranet, the German drug store chain ‘dm drogerie markt GmbH & Co KG’ in Karlsruhe allows its industry partners and suppliers to access its data warehouse and view current numbers anytime. This open information policy helps manufacturers to plan better. It ensures that shelves are well stocked, offers insight into tops and flops and is a valuable marketing aid. Consumers, manufacturers and the retail chain all benefit equally.” (Hermes 2009).

Various empirical studies offer insight into the prerequisites and success factors for successful implementation of an ECR cooperation. A study by Corsten and Kumar (2005) revealed that **specific investments** made by the supplier, followed by the deployment of **cross-functional teams** to implement ECR as well as the use of appropriate incentive systems had the greatest influence on a successful ECR cooperation. Seifert (2006) study, on the other hand, identifies as the requirements

Table 7.3 Sub-processes of ECR

	Sub-process	Goal of sub-process
By the customer (marketing)	Efficient product (development &) introduction (EPI)	Development and introduction of new products designed to meet customer needs
	Efficient promotion (EP)	Harmonization of promotion activities between manufacturers and retailers by communicating the benefit to consumers
	Efficient store assortment (ESA)	Provision of a complete, consumer-oriented, shopping-friendly assortment
By the supplier (especially logistics)	Efficient replenishment (ER)	Maintaining adequate stock; optimizing warehouse restocking by sharing delivery responsibilities
	Efficient operating standards (EOS)	Optimizing operative logistics by coordinating and standardizing flow of goods
	Efficient administration and systems (EAS)	Optimizing flow of documents and information; optimizing IT network and data warehouse
	Efficient sourcing (ES)	Optimizing flow-based pull systems by integrating upstream suppliers
	Efficient controlling (EC)	Optimizing billing and forecast systems (with the introduction of collaborative planning forecasting and replenishment - CPFR, activity-based accounting, realtime controlling)

Source: Based on Lietke (2009, p. 14)

for successful implementation of ECR: **involvement of top management**; mutual **trust** between the ECR partners, early successes; continuous measurement of the ECR success; the use of modern information technology and cost accounting methods; proximity to customers; change in the organizational structure; and employee training (Lietke 2009).

An **increase in the supplier's economic performance** as well as improved competitive capabilities were determined to be the effect of an ECR cooperation (Corsten and Kumar 2005). However, this study indicated that the supplier perceived an **impression of inequitable distribution of burden and benefit** in the business relationship; the impression was less pronounced when the supplier and dealer felt mutual trust. Therefore the supplier's participation in an ECR cooperation with a retail partner may intensify the business relationship between the two partners, but distribution aspects resulting from the cooperation should be trustfully regulated to the satisfaction of both partners.

7.3.2 Just-in-Time Delivery

In addition to cooperations with trading companies as part of ECR, suppliers can secure the business relationship by entering into cooperations with an emphasis on

distribution with manufacturers of the immediately downstream market level. An example can be found in the cooperations between component suppliers and assembly plants as part of **just-in-time delivery** (JIT component suppliers) in the **automotive industry**; the concept is becoming more common in other industries as well (Bernard 1996).

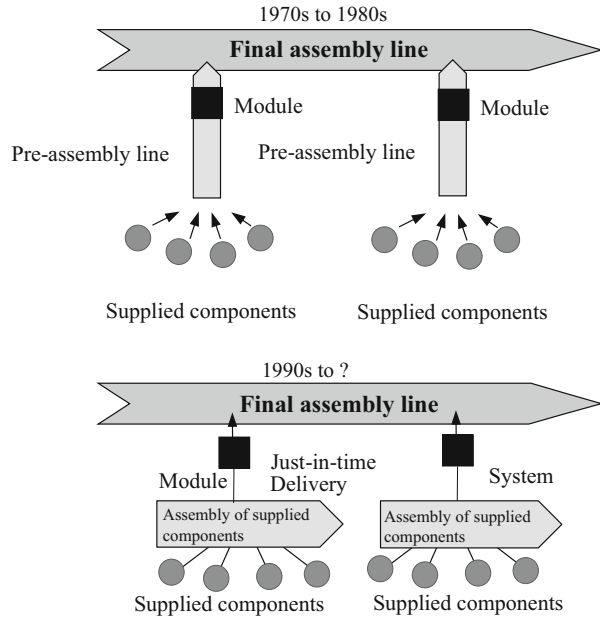
The fundamental idea of JIT delivery is to streamline supply chains and to eliminate intermediate storage facilities by providing the component supplier products when they are needed for production. To achieve this, the component supplier has to make every effort to avoid mistakes and to achieve 100 % perfection, meaning that he cannot deliver any faulty, incomplete or delayed products. To be able to achieve this from an organizational aspect, JIT delivery often entails maintaining several small intermediate storage facilities along the supply chain, using EDI (electronic data interchange) systems between businesses, and transferring supporting processes such as quality assurance to the responsibility of the supplier (Bernard 1996; Germain et al. 1994). This reconfiguration of the responsibilities between customer and component supplier is accompanied by changes in the organizational structure of the component supplier. As the empirical study by Green and Inman (2006) shows, successful application of JIT delivery is possible only when cross-functional and cross-departmental cooperation (integration) are strengthened, when performance monitoring is intensified, and when the degree of specialization is increased.

The essential catalyst for the development of this type of delivery has been the constantly changing market and competitive conditions in the European automotive industry in recent years, which has led to a fundamental evolution in the procurement behavior of automobile manufacturers. While the European automotive industry was characterized primarily by mass-produced, mostly standard products well into the 1980s, this concept that had been applied successfully for many years was increasingly displaced in the 1990s by various forms of “lean” production (Krafcik 1988; Womack et al. 1990). The concept of mass production was pushed to its “natural limits” by increasingly short development and production times and the market-induced demands for smaller but more differentiated series at the lowest cost possible (Pine 1993). In addition to this came the introduction of new types of vehicles as well as a wider range of special features and technical innovations, triggering a drastic rise in the number of interfaces that automobile manufacturers have to coordinate and leading to overly complex structures and processes.

A way out of this situation came in the restructuring of procurement, from the traditional, adversative acquisition of parts to the purchasing of highly aggregated modules and systems. The fundamental idea of **module and system procurement** in this context is to decrease complexity by reducing the vertical range of manufacturing as well as the number of directly supplying companies, thus disentangling the value-adding steps and making them more manageable (Fig. 7.11).

In contrast to traditional procurement of individual parts from different suppliers, module and system procurement means that the parts previously acquired separately are aggregated to pre-assembled, ready-to-install functional groups.

Fig. 7.11 Disentangling value-adding steps. Source: Based on Kleinaltenkamp and Wolters (1997)



Modules differ from systems in that vehicle manufacturers design and develop them and component suppliers produce them. System procurement is additionally characterized by the supplier adding significant value to development, production and logistics (Wolters 1994). It allows the component suppliers as well as the automobile manufacturers to greatly increase their efficiency, which can be attributed primarily to the following causes (Kleinaltenkamp and Wolters 1997):

- The transfer of supplier know-how or tapping of additional potential for development and innovation on the part of manufacturers due to close and early cooperation with the system suppliers during the concept phase
- Utilization of design-to-cost potentials by adapting sub-groups to the component supplier's manufacturing conditions
- Intensive communication between component suppliers and assembly plant, thus stabilizing the business relationship, reducing the number of coordination problems, accelerating the solution finding process and leading to an overall lower number of changes before the series run
- **Transaction cost** savings (initiation, agreement, processing, assimilation and supervision costs) by drastically reducing the number of direct suppliers
- Transfer of extensive assembly tasks to the system supplier by procuring complete, pre-assembled systems, thus tapping cost reduction potential in personnel, production and logistics
- Reduction of customer care and coordination expenses as well the cost of quality control by transferring responsibility for the system to the supplier.

Table 7.4 System procurement's net effects of rationalization

	Benefits to manufacturers	Benefits to component suppliers	Net effect of rationalization
Research and development	<ul style="list-style-type: none"> • Specialization in core competencies • Fewer modifications (e.g. tools) • Quick solution • Reduction in engineering capacities 	<ul style="list-style-type: none"> • Specialization in core competencies • Better utilization of special equipment • Better utilization of carry-over parts • Designs ready to be manufactured 	<ul style="list-style-type: none"> • Reduced development times • Better-engineered products • Lower development costs • Reduction in personnel expenditures
Procurement	<ul style="list-style-type: none"> • Reduction in suppliers • Fewer part numbers • Less purchasing personnel 	<ul style="list-style-type: none"> • Greater processing volume • More economic utilization • Better utilization of information systems 	<ul style="list-style-type: none"> • Reduction in personnel expenditures • Reduction in material costs
Production and logistics	<ul style="list-style-type: none"> • Reduction in pre-assembly • Less potential for errors (assembly) • Reduction in number of storage facilities • Less floor space required • Reduction in logistics interfaces (e.g. incoming deliveries) 	<ul style="list-style-type: none"> • Larger batches • Better capacity planning and utilization 	<ul style="list-style-type: none"> • Economies of scale • Lower quality assurance costs • Reduction in personnel expenditures • Learning curve effects • Lower cost of capital employed • Better product and process quality

Source: Based on Kleinaltenkamp and Wolters (1997)

The cross-company benefits of **system procurement** mentioned above can be illustrated with an analysis of the net effects of rationalization (Table 7.4). While system procurement means that the automobile manufacturer is able to decrease costs in all functional areas, it also means that the system supplier's expenses rise initially due to the expansion of his scope of services. However, examination of the total costs shows that the relative cost increase to the system suppliers is 20–30 % lower than the savings to the vehicle manufacturer (Wolters 1995). This can be attributed to fewer redundancies, economies of scale and learning curve effects, and to wage benefits for the suppliers. Furthermore, the system supplier benefits from greater entrepreneurial autonomy and a longer term planning horizon, which has a positive impact on strategic planning and enables him to promptly adapt corporate structures to current market demands. Establishment of a JIT system with a customer often means that the supplier's share of delivery to this customer rises substantially or, in the case of single sourcing, increases to 100 % (Bernard 1996).

System procurement inevitably creates a close commitment between component suppliers and assembly plants, and both sides are required to make substantial investments in resources specifically for the business relationship. In addition to “soft” forms of coordination such as **trust**, **satisfaction**, etc. (Chap. 3), new types of cooperation between the parties become a fundamental necessity. The system supplier faces the challenge of presenting the customer with an offering that not only meets the quality demands of the customer and is in agreement with his price expectations, the offering must also be adapted to the time at which the customer expects delivery. Added to this is the expectation that the offering will be continuously and dynamically adapted to the evolving situation and external discontinuities. Freiling (1995) points out that such a cooperation is possible only with far-reaching reorganizational measures on the part of the component supplier as well as within the cooperation between the component suppliers and the assembly plant (Freiling 1995).

A **JIT cooperation** is well-suited as a monitoring and control system for the type of partnership described here—a partnership that goes well beyond the normative guidelines of the traditional JIT concepts (Backhaus and Meyer 1990). The JIT cooperation is based on the concept that the customer will suffer disadvantages if a product or service is provided too early or too late. So a JIT offering is based on a specified offering being provided at a precise time, whereby the range of services offered is not limited to logistical aspects (Freiling 1995). It is apparent that, when a service is created applying JIT factors, the process is founded on reliability and stability. In customer companies, the JIT cooperation is often coupled with other lean production concepts such as kanban systems, total quality management and quality function deployment (Bernard 1996; Inman et al. 2011; Piercy and Morgan 1997; Zelbst et al. 2010). On the basis of the term **co-makership**, coined by Merli (1991), a JIT cooperation is characterized by the following attributes:

- The basis of the companies’ cooperation is a long-term **contractual commitment**.
- The component supplier is responsible for developing functionally definable assemblies and is integrated in the development process early.
- A wide range of development and production tasks is assigned to the component supplier, who then performs the tasks on his own and assumes the full warranty.
- The supplier delivers the procured items when they are needed for production, and the customer does not need to store them temporarily for inspection.
- The manufacturer supports the component supplier with training and consulting, facilitating ongoing improvement of prices and quality.
- The manufacturer and component supplier continuously share information on enhancing products and processes.

Table 7.5 System supplier tasks in potential areas of cooperation of a JIT cooperation

Development of supplied parts	Serial delivery of supplied parts	Delivery of spare parts	Taking back old parts
<ul style="list-style-type: none"> • New development of supplied parts • Continued development of supplied parts 	<ul style="list-style-type: none"> • Procurement of primary material • Production • Distribution • Installation in the final product 	<ul style="list-style-type: none"> • Provision of spare parts • Installation support 	<ul style="list-style-type: none"> • Logistics of retrieving old parts • Scrapping or recycling

Source: Based on Freiling (1995, p. 286)

Table 7.5 provides an overview of the resulting areas of cooperation of a **just-in-time cooperation**.

When choosing suitable cooperation partners, a vehicle manufacturer will generally base his selection on past experience with current and potential component suppliers. Only suppliers who have proven to be reliable business partners and who have a solid reputation are considered as potential cooperation partners. When assessing the range of services offered by the component supplier, the following criteria are often examined (Freiling 1995):

- Consistent performance, providing conclusions on the reliability of the component supplier's providing service to the assembly plant at the right time
- Effectiveness in the sense of the component supplier's willingness to accept orders from the assembly plant
- Quality of the service, which offers insight into how many deliveries have not met customer requirements
- Component supplier's willingness to provide information that indicates to the assembly plant the degree of transparency of the workflow
- Flexibility (of service/performance) as an indicator of the component supplier's ability to react to the assembly plants request—sometimes on short notice—for modifications.

Thus a supplier attempting to gain a customer in the automotive industry as a cooperation partner should consider these assessment variables to be the target variables of his marketing activities, and his strategic and operative measures should be designed to meet these objectives.

Although JIT delivery has become more popular and gained a strong following over the past two decades, it cannot be considered a cure-all for cooperation within value-adding chains. In looking back over 20 years of JIT practice and research, Polito and Watson (2006) see the following problems and limitations for the implementation of JIT cooperations (Table 7.6).

Table 7.6 Limitations of JIT delivery

Problems with JIT systems	
Economic situation & demand	<ul style="list-style-type: none"> • Strong fluctuations in raw materials prices • Fluctuations in availability of capital, especially for medium-sized companies due to economic cycle • (Strongly) fluctuating demand
Logistics	<ul style="list-style-type: none"> • Great distance between supplier and JIT customer • Capacity of transport system • Global sourcing (purchasing supplier services worldwide) • Being forced to use expensive air freight instead of less costly means of transportation (esp. maritime shipping) to meet short-term demand (e.g. in the global textile industry), leading to loss of cost benefits of JIT
Organizational requirements	<ul style="list-style-type: none"> • Decreasing availability of suitable personnel • Inappropriate organizational structures, such as distinctive hierarchies and limited accountability of employees • Ill-suited incentive systems (e.g. piece-work payment)
Cost-accounting systems	<ul style="list-style-type: none"> • Monthly or quarterly reporting periods not suited to continuous, long-term improvement processes of JIT cooperation • Common performance indicators reflect only plan deviations, not the actual reasons; this can sabotage efforts made as part of a JIT cooperation
Small company	<ul style="list-style-type: none"> • Cost disadvantages regarding supplied products due to smaller quantities purchased • No control over inclusion of own component suppliers on JIT system • Difficulty recruiting qualified personnel for JIT implementation

Source: Based on Polito and Watson 2006

7.4 Instruments of Communication Policies

While the objective of the instruments of product and distribution policies to strengthen the business relationship is primarily to expand the services utilized within a business relationship, the instruments of communication policies focus on controlling the customer's perception of his benefit. Recapping: The customer benefit anticipated from a business relationship is always geared towards the customer's perception, not towards neutrally or objectively phrased criteria. The following sections will introduce three concepts as examples of communicative support of a business relationship. The concepts can more or less be considered communication policies, since the focus is on sharing information with the customer.

7.4.1 Complaint Management

Business relationships free of faults on the part of the supplier are a noble goal, but they are not to be found in the real world. When an **error** occurs in the processing of

a transaction within a business relationship, it poses both a risk and an opportunity for the supplier. If he reacts properly to such a failure, **customer satisfaction** can be restored or even increased (Smith and Bolton 1998). If he does not, the worst case would be termination of the business relationship as well as negative consequences through bad references expressed to current and potential customers. So good **complaint management** is an essential means of protecting the business relationship and possibly even strengthening it.

The following subordinate targets are regularly pursued with complaint management (Stauss 2008):

- Achievement of complaint satisfaction
- Prevention of costs attributed to other types of reactions of dissatisfied customers, such as changing suppliers, involving the media, and negative word of mouth (WOM)
- Implementation and clarification of a customer-based corporate strategy
- Creation of additional acquisition effects by influencing (positive) WOM
- Evaluation and use of information gleaned from complaints
- Reduction in internal and external cost of errors

To be able to use complaint management to transform transaction dissatisfaction to complaint satisfaction, it is essential that a supplier create the proper **channels** for dissatisfied customers, where filed complaints can be properly registered and processed, and the customer receives an appropriate reaction. Various tasks are needed to best utilize the information contained in complaints. The individual steps in the process of direct and indirect complaint management can be seen in Fig. 7.12.

An empirical study by Homburg and Fürst (2005) revealed that, in regard to the organization of complaint management, an adequate degree of formalization (clearly defined processes and responsibilities) as well as a certain flexibility (particularly in B2B companies) are needed to implement effective complaint management.

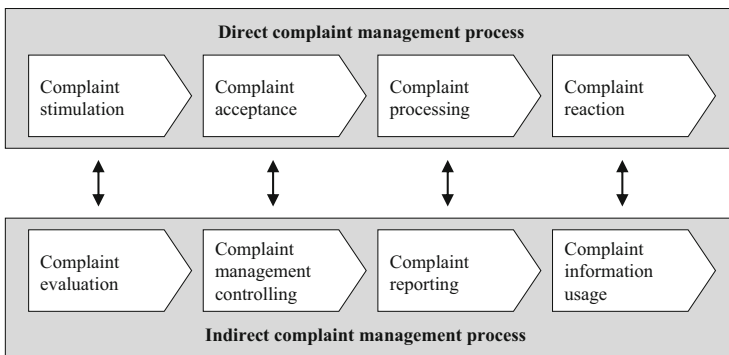


Fig. 7.12 Complaint management process. Source: Based on Stauss (2008)

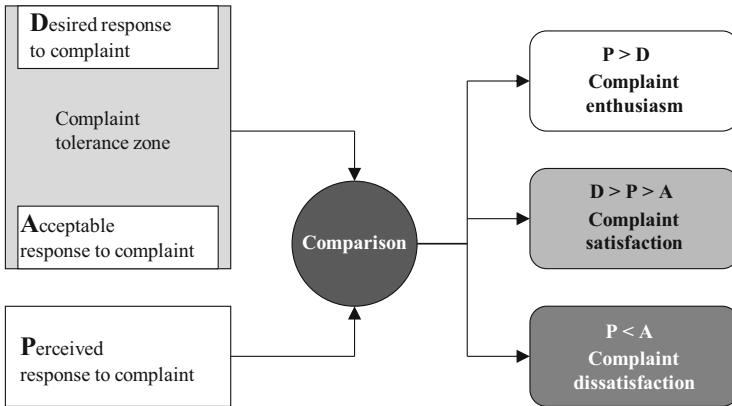


Fig. 7.13 Development of complaint (dis)satisfaction. Source: Based on Stauss (2008)

The customer's reaction to how the supplier processes complaints has been relatively well researched empirically; it follows the **expectancy disconfirmation paradigm** (Churchill and Surprenant 1982): The customer weighs the perceived response to a complaint against the response he expected. If the balance is zero or positive, the result is **complaint satisfaction**, otherwise it is **complaint dissatisfaction**. The expectations that customers have of a response to a complaint do not follow a uniform standard; they are more of a **tolerance zone for responses to complaints**, somewhere between an acceptable response and a desired response to a complaint (Stauss 2008). The desired response to a complaint is the normative, ideal expectation standard, meaning the expectation of how a supplier should react to a customer complaint. The acceptable response, on the other hand, is the minimum level at which a response to a complaint is perceived as tolerable. Depending on how the response to the complaint is perceived by the customer in relation to the tolerance zone, the customer will experience complaint satisfaction, dissatisfaction or enthusiasm. Figure 7.13 illustrates the correlations.

Another variable examined in this context is the presumed response to a complaint. Depending on certain factors, customers form an image of how a supplier might respond to their complaint. This presumed response then affects what they would consider to be an acceptable response to the complaint.

When the factors affecting the response to a complaint are examined individually, there are factors that determine the complaint tolerance zone as well as factors related to the perception of the response to the complaint. The following factors are determinants of the complaint tolerance zone:

- Understanding of one's role: The stronger the customer's perception of himself as a customer to be courted is, the higher his expectations tend to be
- Relevance of problem: As the problem that triggered the complaint becomes more relevant, the expectations of the response to the complaint rise
- Perceived fault of supplier

- Explicit and implicit promise to react
- Previous complaint experiences
- WOM from other customers

In regard to the perception of the **response to the complaint**, one can differentiate between the two dimensions **result of the complaint** and **complaint process**. The result of the complaint is evaluated on the basis of how appropriate and fair it is, while the complaint process is evaluated based on the factors accessibility, quality of interaction (friendliness, politeness, helpfulness, initiative, empathy, reliability) and reaction speed (Stauss 2008).

If by implementing a complaint management system when he makes mistakes the supplier is successful in accomplishing an appropriate reaction to the complaint, complaint satisfaction can increase a customer's overall satisfaction with a business relationship, possibly even surpassing the level from before the problem occurred (Smith and Bolton 1998). So adequate complaint management has an indirectly positive effect on customer loyalty due to customer satisfaction as well as a direct effect, as shown in the empirical study by Alvarez et al. (2011). Furthermore, complaint satisfaction and enthusiasm can lead to a positive WOM effect; customers tell others about their positive experiences (Gelbrich and Roschk 2011; Rothenberger et al. 2008).

7.4.2 Strengthening the Personal Relationships Between Supplier and Customer Personnel

Although this book deals with the management of business relationships between companies, these business relationships are still initiated, maintained and sometimes dissolved by people. The persons involved do much more than fill a pre-defined role; if this were the case, most business relationships could be computerized (Bagozzi 2006). Persons involved in the business relationship behave to a certain degree as business people and to a certain degree as friendly human beings (Heide and Wathne 2006). Specifically, employees of the supplier company establish personal relationships of different types with employees of the customer company (Beverland 2001). On the one hand, this type of relationship is needed to process transactions between the companies in the business relationship. But some such relationships go deeper and have secondary effects on the business relationship between the supplier and customer company. Business friendships between persons working for the supplier and for the customer are the extreme case (Beverland 2001; Price and Arnould 1999). However, even less intensive personal relationships have a positive impact on the business relationship as compared to human interaction focused only on the transaction, particularly in regard to the sharing of information and thus communication between the companies.

Palmatier et al. (2007) demonstrate in their empirical study that a customer company's relationship to a certain sales representative has a positive effect on revenue, effectiveness of sales and the customer's willingness-to-pay, while to the

supplier company only influences the willingness-to-pay. It should be noted that these results were obtained in an environment in which switching costs were relatively low for both sides. Another empirical study, conducted in the financial sector (B2B), revealed that measures designed to strengthen the personal relationship between supplier and customer personnel (invitations to meals, small gifts, invitations to entertainment events; a special status for the customer; privileged information) had a much stronger impact on customer profitability than did performance rewards or pricing measures (Palmatier et al. 2006a). The high expenditures observed in actual practice for such primarily atmospheric measures indicate that the personal relationship between personnel at the two companies is considered important.

Guenzi and Georges (2010) claim that the significance of the personal relationship differs by industry and is all the more important:

- as the credence qualities of the core service increase,
- as the focus of the core product on people grows (e.g. consulting),
- as the contact time per customer contact lengthens,
- as the degree of product/service customization increases,
- as the degree of discretion rises (e.g. legal advice),
- as the focus from physical products, to services and processes.

Beverland (2001) points out that, particularly in sectors in which there are multiple suppliers of one core service for which the features and price barely differ from one another (management consulting, auditing, legal advice), it is the personal relationship between the customer's and the supplier's personnel that is decisive in choosing or rejecting a business relationship between customer and supplier companies (Gwinner et al. 1998; Price and Arnould 1999). In such industries, the customer's loyalty is less to a company than to a representative of the company, e.g. the partner in a consulting firm. It should be pointed out though that the service relationship between the companies must be good before the personal relationship can prosper; only then can the business relationship benefit from the personal relationship (Beverland 2001).

So what can a supplier company do to promote good relationships at the personal level of its own and the customer's employees? To be able to reply to this question, another question must also be considered: What are the traits of good personal relationships in a business relationship context? According to Gremler and Gwinner (2000), they are characterized by familiarity, attentiveness and care, friendship, trust and rapport, whereby rapport and friendship in this context have received more attention in research.

Gremler and Gwinner (2000) define **rapport** between supplier and customer personnel as the perception of pleasant interaction with one's counterpart, marked by an internal connection between the two interacting participants. To use a common phrase, rapport means "the chemistry's right" between the participants. Rapport between supplier and customer personnel is fostered by similar philosophies as well as similar personal values and empathy (Campbell

et al. 2006). One way for a supplier company to promote rapport and thus good personal relationships between his employees and those of his customer is to allow similar employees to interact with one another. The **similarity** can be based on a content or formal dimension (e.g. same functional background, same level in the corporate hierarchy), or it can be have a personal-relational dimension (originating from the same region, similar interests; Steward et al. 2010). **Frequent contact** also fosters rapport between supplier and customer personnel (Beverland 2001). After all, a certain indirect role is assigned to the job satisfaction of the supplier's sales reps. Their satisfaction has a positive impact on their efforts to help customers, which in turn causes the customer's personnel to gain a positive impression of the sales reps (Bradford et al. 2009).

Rapport between the supplier's and the customer's employees is good for the supplier company in several ways: It makes the customer more **tolerant** when the supplier makes a mistake, and the consequences of a transaction causing dissatisfaction are not as severe (Campbell et al. 2006). So rapport supports complaint management. Rapport was also shown to have positive effects on **customer satisfaction**, **customer loyalty** and the **probability of recommendation** (Grewler and Gwinner 2000; Guenzi and Georges 2010).

While rapport to some extent constitutes the establishment of a personal relationship between supplier and customer personnel, a **business friendship** represents the extreme case of personal relationships. Between these two poles there is a progression of the strength of the personal relationship, the manifestation of which is based on different variables. Whether the customer is looking for a close or not-so-close personal relationship depends primarily on the personality of the customer's employee (Beverland 2001; Swan et al. 2001). According to Swan et al. (2001), the strength of a personal relationship between the supplier's and the customer's employees depends on the strength of

- personal familiarity,
- conversations about things other than business topics,
- common leisure interests and
- the sales rep's actions as an advocate and ambassador for the customer within his own company.

The authors identify three types of relationships that can exist; business friends, co-workers and business acquaintances. Business friendships are characterized by social support, sharing of thoughts and great personal candor (self-revelation) between the parties involved (Price and Arnould 1999). For personal relationships to transition to business friendships, factors that promote rapport must be accompanied by other influenceable conditions (Price and Arnould 1999):

- Structural opportunities for social interaction (meals, activities together)
- Common environments
- Common ground regarding values, standards, lifestyles and personality traits
- Friendliness

Similarity and mutual affection as well as mutual dependency in regard to achieving goals help to create business friendships (Price and Arnould 1999), whereby these factors can be controlled minimally or not at all. To be able to best utilize personal relationships for the good of the supplier company, even when individual employees of the customer change jobs, Beverland (2001) suggests establishing person relationships with multiple persons within the customer's organization (Beverland 2001). It should, however, be kept in mind that various scandals and a general trend towards greater corporate transparency have led to pronounced reinforcement of legal and well as corporate **compliance regulations** in recent years. So measures intended to fortify the personal relationship between supplier and customer personnel should always keep an eye on applicable regulations (Price and Arnould 1999).

However, such measures to strengthen the personal relationship are still worthwhile, because they have many effects. For the customer's employees with a personal relationship to employees of another company, the benefits of such a relationship can be social (friendship, personal recognition), psychological (less risk, greater feeling of security) and economic (faster service) (Gwinner et al. 1998). Broader, unprompted **sharing of business-related information** is linked to good personal relationships (Swan et al. 2001). Personal relationships can also help to better understand the **personal motives of individuals** in the customer's company. This is important because personal motives may influence behavior in a business relationship, such as when the relationship can have an impact on a person's career (Beverland 2001). And the fundamental trust felt towards the supplier company improves, which in turn is positive for the supplier company when problems occur (Beverland 2001), e.g. when delivery obligations are not met. The benefits of the personal bond also have an indirect or direct positive impact (through satisfaction and commitment) on customer loyalty and the tendency to make recommendation to others (Henning-Thurau et al. 2002).

7.4.3 Cooperations with User Groups

While complaint management and measures intended to fortify personal relationships extend well beyond direct and indirect communication with the customer, communication itself is much more the focus for the user groups introduced here.

User groups are primarily bodies of computer and system technology users that arose as the respective technologies became common. Their original purpose was to create a forum where people from the various fields of application could exchange ideas, share their experiences with certain systems and system technologies, and discuss problems they had encountered (Rothschild 1988; Kleinaltenkamp 1993; Erichsson 1993). CAD field specifically: Strothmann and Kliche (1989). User groups are also a way to establish contact with users of **system technologies** who have experience with the supplier's products and services and who are willing to invite other users to visit their applications. People seeking information tend to

Table 7.7 Distribution of information gleaned from user groups

Function	Distribution of information			
	Always	Occasionally	Never	Not specified
Technical management	42 %	35 %	6 %	17 %
Network communication	34 %	27 %	8 %	31 %
Management information system	26 %	20 %	11 %	43 %
Research & development	17 %	23 %	13 %	47 %
Business management	11 %	33 %	20 %	36 %
Training/further education	11 %	23 %	16 %	50 %
Consulting	10 %	15 %	17 %	58 %
Administration	4 %	19 %	27 %	50 %
Production	4 %	11 %	22 %	63 %
Marketing/sales	4 %	8 %	25 %	63 %
Purchasing	4 %	10 %	23 %	63 %
Market research	4 %	10 %	23 %	63 %

Absolute basis: 436

Source: Based on Erichsson (1993, p. 166)

believe that they will more readily learn about negative experiences with a supplier when they choose the **reference company** themselves than as opposed to when the supplier suggests the company to visit.

The work of such bodies of users focuses increasingly on the issue of technical **interface standardization**, no longer looking at the work of a single supplier but at that of multiple suppliers. The reason is that various users were and still are of the opinion that their position has to be represented longer term and more clearly, thus inducing the manufacturers to adapt to uniform standards and to support them (unknown 1986). On the other hand, users' passive behavior is often criticized, and without their participation any attempt to achieve international standards is fruitless. The executive committees of the user groups see overcoming this passiveness as their ultimate objective. They intend to do this by raising awareness amongst users and expanding user group channels (unknown 1987). To achieve their objectives, such user groups "feed" suggestions to national and international standardization bodies—which is why they are called **feeder groups**—or they act as **pressure groups**, attempting to support the enforcement of existing standards. One way this happens is that the members coerce manufacturers into applying the respective specifications by their choice of purchasing divisions and their market power.

The significance of user groups as an informational instrument for entire user companies as well as for individual persons within the company is revealed in an empirical study that examines, among other things, how the information gained from user groups is passed along in the respective company (Erichsson 1993). The study clearly indicated that it is particularly technical management that benefits from the findings: It receives information on the knowledge gained from user group meetings always in 42 % of the cases and occasionally in 35 % of the cases (Table 7.7).

Table 7.8 Roles in purchase decision processes as perceived by user group members

Roles in decision process for computer technologies	Absolute frequency	Frequency as percentage
Preparation of information	256	58 %
Initiation of decision process	225	51 %
Definition of department requirements	224	51 %
Definition of specification	223	51 %
Evaluation of supplier	207	47 %
Advising of those involved in decision	192	44 %
Evaluation of product types	192	44 %
Approval of purchase	94	21 %
Decision	87	20 %
Absolute basis: 429		

Source: Based on Erichsson (1993, p. 176)

Another noteworthy discovery was that the corporate representatives active in the user groups have significant influence on purchase decision processes—or at least that is their perception. Of those surveyed, 58 % said that they prepare information needed to make purchase decisions, and 51 % claimed that they initiate decision making processes and determine department needs and specifications. And almost half of those who replied stated that they were involved in evaluating the suppliers, advising the decision makers and assessing product types (Table 7.8).

Based on the results presented earlier, it comes as no surprise that users participating in gatherings see themselves above all as serving an informational purpose. Sharing information at conferences and the impulses gained in workshops are essential factors. Equally important are the better opportunities that user groups provide in gaining an overview of the market as well as the fact that user groups are a source of information relevant to investment decisions (Fig. 7.14).

So for customers in certain industries, user groups are an essential instrument to gaining access to information in experiences that other users or customers have had with the services provided by certain suppliers. And if this really the case, the question arises as to whether and to what extent a supplier can influence the respective information flows to his benefit by cooperating with user groups.

When user groups are involved in a supplier's communication strategy like this, the supplier has two fundamental possibilities: either pursue a cooperation with an existing, user-initiated user group or found a user group himself.

7.4.3.1 Cooperation with User-initiated User Groups

The essential requirement for cooperation with user groups arising from an initiative by users is that the user groups and their members are willing to work together with a supplier. So when initiating and participating in a user group cooperation of this type, it is important to bear in mind that the members consider the primary benefits of a user group to be the sharing of information with other members, maintaining personal contact with others and solving specific problems that may

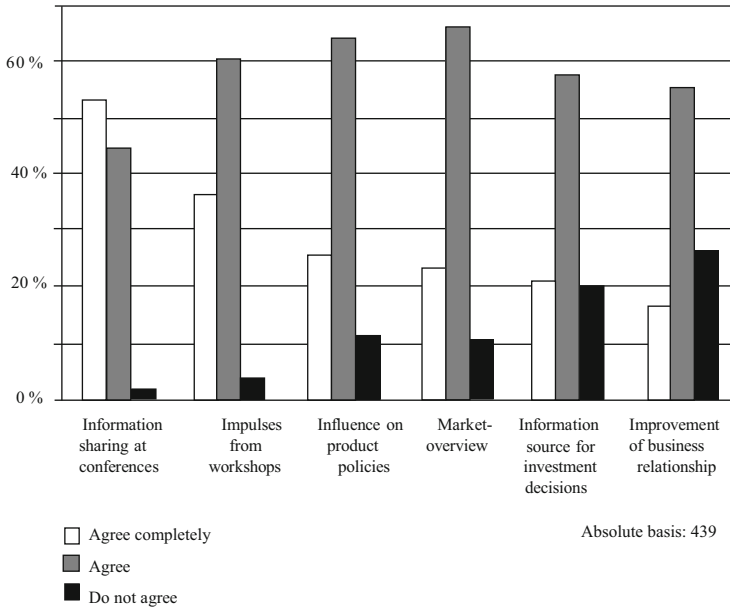


Fig. 7.14 Functions of user groups as perceived by users. Source: Based on Erichsson (1993, p. 182)

occur in workshops (Erichsson 1993). But since user groups are self-organized bodies, a key focus of the users and especially of their functionaries is to develop and implement a range of services based on member needs, thus binding active members and attracting new ones (Erichsson 1993). Thus an essential approach to successful cooperation with a user group is to support the user group to the greatest extent possible in precisely these points. There are different ways to express this support, e.g. by making certain technological or business know-how available exclusively to members of the user group, or by providing financial support for user group events by paying the fee for an invited guest speaker (Erichsson 1993). An empirical study of this behavior determined that suppliers were able to establish a partnership-like relationship with these and similar measures (Erichsson 1993).

When these efforts are met with success, the result is a vast opportunity to benefit from a substantial multiplier effect in regard to the supplier’s image. The great benefit of such activities is that, because of the constellation of the user groups and the internal information activities of the user group members, there is very little scatter loss (Erichsson 1993). Also, because of their function, their position in the hierarchy and their significance to investment and decision making processes, user group members can be considered **opinion leaders** (Kawasaki 1990) whose judgment is significant and credible to decision makers within their own company and in other companies as well. Thus the proper cooperation with a user group can be a means to targeted and trouble-free communication policy towards substantial segments of the potential customer base.

Cooperations with user groups can also be expected to have a positive impact on the image of the products and services offered as well as those of the supplier company. Such effects can be achieved in different ways at user group events, such as: independent consultants pointing out the advantages of their products in the course of their presentations; product developers being able to immediately answer any technical questions that come up; high-ranking company representatives seeking personal contact to members of the user group, etc. (Erichsson 1993).

At the same time though, the limitations of such cooperations should be kept in mind. They are primarily the result of the fact that user groups are simply user bodies. Despite the willingness to cooperate, user group events usually do not allow suppliers to engage in sales promotion in their own interest; this is usually contrary to the primary objectives of user bodies. It is also important to keep in mind that user group conferences generally take place only once or twice per year, so a supplier's time frame for conveying information is definitely limited.

7.4.3.2 Cooperation with Supplier-Initiated User Groups

Another way to cooperate with user groups is to not wait until users initiate the founding but to initiate or establish such a user body as a supplier. It is conceivable to scatter user groups across different regions, inviting representatives of customer companies relevant to the supplier's target groups to join. At the regular gatherings, organized by the supplier, selected suppliers can be invited to present their specific experiences; discussions can take place with corporate experts from the fields of product management, development, sales, customer service and quality assurance; and participants can have a chance to share their experiences. Also, individual users can be surveyed at regular intervals, asking them about new needs, their experiences with products or general satisfaction with the supplier and the supplier's employees. The circle of participants can be examined to possibly identify customers who could serve as potential **pilot users** for new products or as participants in a **lead user project**.

Furthermore, such focus groups do not necessarily have to be permanently institutionalized, they can just as well be brought together for specific cases or one time only—this would, however, diminish the distinction as a cooperation. Such events are referred to as **customer focus groups**, focus groups, forums or customer conferences (Günter 1996). Essential topics related to customer-supplier relationships are discussed with selected customers at such gatherings. The focus is generally on customer satisfaction, open and hidden complaints, and ways to improve the business relationships (Günter 1996).

7.5 Instruments of Pricing Policies

The last section of this chapter deals with the pricing policies of a company and explains how the pricing policies can promote customer loyalty in a business relationship. For this to be possible, it is essential to abolish the apparent contradiction that supplier and customer must be antagonistic towards one another in regard

to price. We will do this in the following Sect 7.5.1, before discussing two specific ways to secure the business relationship with certain pricing instruments.

7.5.1 How Pricing Policies Promote Customer Loyalty

In classical microeconomics, the price of an item is the sole criterion in the decision to purchase or not to purchase. This means that the buyer’s interest and the seller’s interest are exactly opposite. However, microeconomics are based on homogeneous goods, which are virtually non-existent in modern business-to-business markets and even less so in markets in which business relationships are the standard transaction model. So comparing offerings provided by different suppliers from the customer’s perspectives using only the price as a gage is misleading. Actually, the definition of the price and thus of the approaches for pricing policy must contain a **price numerator (payment)** as well as a **price denominator** (Plinke and Söllner 2006). The price-performance ratio becomes the focus of considerations.

Particularly the most recent behavioral research on pricing has shown that, from the purchaser’s point of view, the price not only serves an economic purpose as “currency” for a transaction, but rather the customer’s complex **price perception** determines whether or not a transaction comes about (Homburg and Koschate 2005a, b). The perception is influenced by information collection, evaluation and storage, which, taken together, bring about a certain purchase and usage behavior. Figure 7.15 shows the fundamental relationships and examples of influencing factors.

One type of price perception that has become common particularly amongst industrial customers is the concept of **product life cycle costs** or the **total cost of ownership (TCO)**. When assessing the price of a product, the customer compares the price for the core offering, e.g. the initial cost of a machine tool, to all of the follow-up costs for the use of the capital good over its lifetime (Diller 2008a). In the

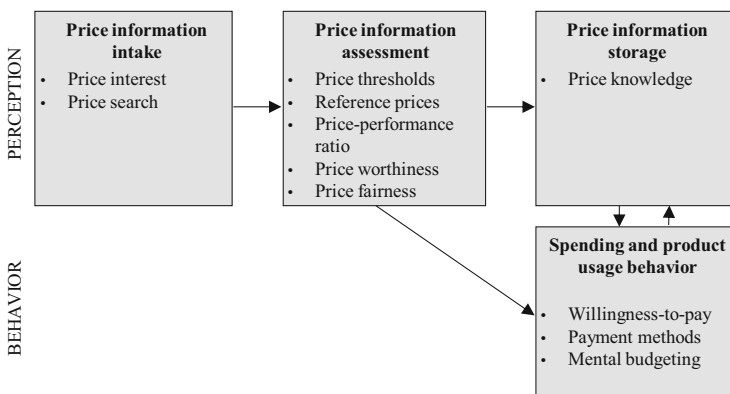


Fig. 7.15 Price perception and usage behavior from the perspective of behavioral science. Source: Based on Homburg and Krohmer (2009, p. 679)

case of the machine tool, this includes incidental expenses related to the acquisition (e.g. transport, connection to existing systems), the costs of spare parts and maintenance, operating expenses for energy and tool consumption as well as potential “negative costs” related to the resale value of the machine. So from the customer’s point of view, the relevant price should include all cost and benefit elements of the service marketed within the business relationship. Thus from the customer’s point of view, approaches to pricing policy intended to promote customer loyalty can in principle be found in all cost and benefit elements (Diller 2008a). The following aspects of uncertainty and capital employed illustrate such approaches.

Particularly when it comes to durable capital goods, often marketed within business relationships, the cost components of the TCO that can be anticipated in the future are tainted with **uncertainty** and difficult for the customer to plan. This uncertainty is comprised of environmentally induced factors (e.g. development of energy prices, capital costs) on the one hand and uncertainty intrinsic to the business relationship (e.g. development of spare parts prices) on the other. Minimizing such uncertainty can be a goal of pricing policy that leads to greater customer loyalty.

Another example is the **capital employed**, which for the customer is linked to many capital goods. Purchasing the capital good may be definitely worthwhile for the customer over the depreciation period, but he may not be able to raise the amount required for the investment at the time. If the supplier can successfully offer creative financing options along with the core product, the customer’s price perception focus may shift from the (prohibitive) purchase price to a monthly (doable) rate. This type of **financial engineering** has become an eminently important instrument of pricing policy in many sectors, one example being the General Electric corporation, a proponent of this concept for many years now.

The following Sect. 7.5.2 reveals how uncertainty regarding TCO as well as capital employed can be used to the benefit of pricing policies that promote customer loyalty. But first we will examine the various mechanisms with which instruments of pricing policy can increase customer loyalty and which role different parameters of price perception play therein.

When studying mechanisms intended to promote customer loyalty applying instruments of pricing policy, Diller (2008a) differentiates between **bought customer loyalty** and **trust-based loyalty**. He considers **bought customer loyalty** to be loyalty generated by the supplier offering price incentives within the business relationship that allow the customer to decrease his TCO. These include e.g. bulk discounts or bonus agreements that apply when the customer purchases a certain minimum quantity per year. While these instruments can facilitate the desired sales and revenue effects, they are highly questionable in regard to the profitability of the supplier company. When compared to other instruments of business relationship management, they performed the worst, e.g. in the empirical study conducted by Palmatier et al. (2006b), and had no positive impact on profitability related to single customers. Interestingly, such instruments of pricing policy directly affect the price numerator, meaning the payment.

Trust-based customer loyalty with the aid of pricing policy instruments, on the other hand, is based not on short-term measures related primarily to the price

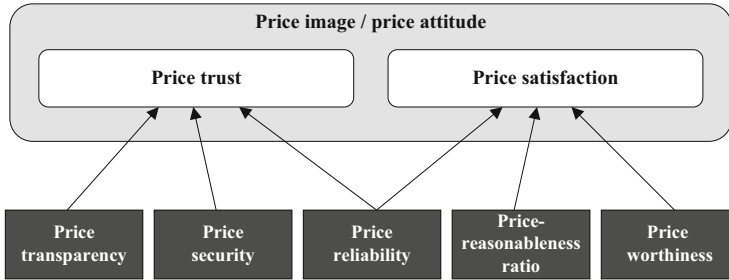


Fig. 7.16 Segments of price perception of trust-based customer loyalty. Source: Based on Diller (2008a)

numerator, but on a global positive perception of the price image. According to Diller (2008a) the **price image** is comprised of the price trust and the price satisfaction, which are in turn influenced by additional factors, as shown in Fig. 7.16.

So to create a positive price image, a supplier’s goal has to be to ensure **price trust** as well as **price satisfaction**. The respective drivers of these two variables facilitate this. Price transparency is the clarity of price information in regard to the price numerator and the price denominator, while price reliability provides information on how reliable or unreliable the individual components of the price are from a TCO perspective. Price reliability can be considered to mean that the prices stated when the contract was concluded still apply (Diller 2008b). Price reasonableness is perceived when the price-performance ratio of an offer is assessed as better than a reference value, such as a comparable value from a competitor; price worthiness indicates whether the price-performance ratio over all is “right” for the customer (Homburg and Krohmer 2009). The best instruments for creating a positive price image and thus promoting trust-based customer loyalty are those that bear on both the price numerator and the price denominator.

7.5.2 Choice of Price Denominator

For many customers of business-to-business suppliers, the purchased offerings are the actual production means. In such cases the role of the offering as a “means to an end” is out of the question. In the traditional view of a business venture, such capital goods represented production factors considered to be property of the company and to have their own value. While this interpretation meant that a customer company wished to purchase a machine tool, in many companies the thought process evolved to where it was not ownership of the machine that benefited the customer but usage of the machine.

In the first approach, purchase, the focus is on the machine tool, meaning **the physical product as the price denominator**. However, in this case the customer must anticipate many additional and uncertain cost components of the TCO.

If the customer takes the second view of a supplier of capital goods, it is no longer beneficial to offer the physical product and thus the price denominator but to offer to provide a service instead: Then the customer would no longer pay for the property but for the service received instead. In this case a **service becomes the price denominator**, not the physical product needed to perform the service. This has several benefits to the customer: Previously fixed costs (machine depreciation) become variable (only the service is paid for), and previously uncertain costs (maintenance, repair, spare parts) become calculable. Then every dimension of price trust is influenced positively. The company Hilti, manufacturer of professional electronic traditional tools (hammer drills, saws, etc.), is exemplary in its implementation of this concept. Hilti offers its key accounts a so-called fleet model, in which Hilti provides a defined fleet for a fixed monthly fee. Hilti takes care of the complete management of the fleet (stock control, implementation assessment, maintenance management, spare parts management, etc.). The customer no longer pays to purchase and manage the equipment, he only pays for the equipment to be available for his use (Diller 2008a).

Particularly innovative companies are going a step farther: Instead of the input of a service, they choose the **service output as the price denominator**. In this case only the service is paid for—in our example, the actual cutting performed. This allows suppliers to achieve a maximum reduction in uncertainty and the greatest flexibility possible in their contribution to added value for the customer. Kemppe, a Finnish supplier of welding machines, was very successful in this endeavor. By partially changing over to supplying the service “welding hours” instead of selling the actual equipment, revenue and profitability rose markedly. The next step planned is to offer “welding seams by the meter.”

Another successful example is the wind energy company Enercon:

Example 5: Enercon Wind Energy

“Enercon, number three in the world and technology leader in wind energy, is going one step farther and is sharing its customers’ entrepreneurial risk. The Enercon Partner Concept gives customers the assurance of consistently high wind turbine availability for the first 12 years. From servicing to safety inspections, maintenance and repairs, all eventualities are covered by one contract. The customers readily embrace this offer. More than 85 % of customers sign an EPC agreement. The fees for the service contract are based on the annual wind turbine output. So in pricing its service contracts, Enercon shares the entrepreneurial risk. Enercon absorbs half of the service fee for the first 6 years of the contract (Simon and Fassnacht 2009).”

So the last step in changing from a price denominator is to transition from service output to **effect of performance**. In this case the fee for the service is not based on what the supplier did for the customer but on the effect that the service had for the customer. For example, contracts for consulting services do not charge by the day. Instead, the agreed fee is a pre-defined fraction of the increase in revenue or

Table 7.9 Choice of price denominator

Price denominator	Determination	Customer's uncertainties
Physical product	Purchase price	Durability: Repair, maintenance, spare parts costs <ul style="list-style-type: none"> • Secondary usage costs (energy, personnel, etc.) • Intensity of usage • Usage performance • Effect of performance
Availability of service	Price as a factor of use	<ul style="list-style-type: none"> • Potential secondary usage costs (energy, personnel, etc.) • Potential intensity of usage • Usage performance • Effect of performance
Usage of service	Price dependent on service level	<ul style="list-style-type: none"> • Effect of performance
Result of service	Price dependent on result	

cost savings. It is important with such contingent contracts (The fee is linked to the **fulfillment of a performance condition**), however, to set incentives that encourage achieving the performance that are compatible for both parties (Thompson 2005). Table 7.9 provides an overview of the choice of price denominator.

7.5.3 Price Modules and Terms and Conditions Systems

Besides offering different price denominators to increase customer loyalty, the introduction of a systematic **price module concept** is particularly advantageous for B2B suppliers with many different service components. Such modular systems precisely define and price the various partial services (Diller 2008a). The customer can choose the service modules and thus the price modules. So price modules promote customization of services, but without blundering into the trap of unpaid “over-engineering” in which the customer receives services that he may not even want and that include additional services free of charge. A price module system grants the customer price transparency, because the price of each partial service is known. When assembling price modules, it is important to ensure consistency between the prices of the individual service components, whereby the price consistency can originate from customer-based or supplier based comparison logic. It should be kept in mind that there tends to be greater pricing leeway with less frequently demanded and regarded partial services, while more popular partial services and prices with a stronger customer focus should be priced more competitively. Consistency of modular pricing systems includes periodic price adjustment and communicating the new prices.

In addition to pricing of all partial services, modular pricing systems also offer **bundled prices** when service packages of a certain size are chosen. This is a way

for the supplier to positively influence the perception of the price-performance ratio, because the bundled price is a better deal than the sum of the single prices.

If for whatever reasons modular pricing systems cannot be consistently implemented and bundled prices are more the rule, performance-based **terms & condition systems** can ensure that the perception of the price image is positively affected. Conditions are certain circumstances that, when the customer complies with them, reduce the price for a supplier service. The following are examples of such conditions (Diller 2008a):

- Purchase volume (e.g. bulk discounts, volume bonuses)
- Time of purchase (e.g. trade fair discount)
- Terms of payment (e.g. remuneration for collection, early payment discount, period allowed for payment)
- Logistics parameters (e.g. pallets, place of delivery)

All variables in which at least one of the two sides detects a service deserving of a price reduction can basically be considered as reference points for such conditions (Diller 2008a).

Like modular pricing systems, terms and conditions systems are intended to improve a supplier's fundamental price image without "buying" customer loyalty. So here, too, it is essential to look at the overall effect of the terms & conditions system and to grant discounts only in areas in which the customer is particularly aware of the discount.

Exercises

1. Describe the ultimate goal of using instruments in business relationship management!
2. State your view on the following: In business-to-business marketing there is always a "one-size-fits-all" solution for the offering!
3. What is the difference between a "system supplier" and a "system integrator"? Discuss the advantages and disadvantages of the different types of solution offerings!
4. Describe the concept of integrative service creation! Explain why this leads to bonding effects between the transaction partners!
5. What does "cross-selling" mean and which factors promote successful "cross-selling"?
6. Describe areas of product-related services! Explain specifically the lead user concept!
7. Explain the term "efficient consumer response"!
8. Explain the term "just-in-time delivery"! Include an explanation of the net effects of rationalization of system procurement!
9. How do the instruments of communication policy differ from those of service and distribution policy?

10. Describe the complaint management process and state the subordinate goals pursued with complaint management!
11. Which determinants of the complaint tolerance zone are you familiar with?
12. Describe the two ways in which the supplier can include user groups in communication strategy!
13. Which types of price perception do you know about in regard to pricing policy instruments? Briefly describe the processes.
14. Describe the segments of price perception of trust-based customer loyalty!

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8.1 Organization of a Business Relationship Management

8.1.1 Fundamentals of a Customer-based Organizational Structure

When the wealth of tasks that are required in business relationship management is considered, one wonders how they can all be successfully implemented in a company. An essential cornerstone of the implementation of business relationship management in a supplier company is to ensure that the organizational prerequisites are in place. This can occur in very different ways. Ultimately the goal is to have one central address where all activities having to do with relationships to important customers come together in one uniform responsibility. This is usually associated with organizational institutionalization, whereby the departments and persons involved are generally referred to as **key account management** or similar.

Variations of key account management have been practiced in Germany since the early 1970s, particularly in the food industry. Among the first companies to apply this concept were *Henkel KGaA* and *Master Foods* (Diller 1989). But the origin of the concept was actually much earlier. Tosdal (1950) made the suggestion in the USA to grant individual important customers the status of “national account”, “(. . .) which buys a large quantity of product” (Tosdal 1950, p. 179). This type of national account management was practiced in the 1960s by more than 250 companies in the USA, all operating in the business-to-business sector. The National Account Marketing Association was founded in 1965 in New York. Its members at the time included General Electric, Xerox, IBM, Uniroyal and 3M. Although key account management grew out of the business-to-business sector, for a long time it was much more prevalent in the consumer goods industry (Knetsch 1990; Diller 1988; Thomas 1987). This is due to the fact that the respective

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companies were and still are dealing with trading companies as their direct customers, so there were business-to-business relationships. But in recent years it has become more and more common that other companies in the business-to-business sector, meaning those not supplying trading companies, implement some type of key account management (Homburg et al. 2000).

The essential tasks of such a key account position or department include:

- Gathering and evaluation of information on individual customers
- Conception of strategies to maintain and foster relationships
- Planning and possibly the implementation of measures to maintain and foster relationships—the measures being those targeted towards customers as well as those that affect the company’s internal operations
- Controlling of operative measures intended to maintain and foster relationships
- Consultations and negotiations with employees of the respective customer company.

An example of the type of information that should be compiled on important customers in this regard can be seen in Table 8.1, a process used by IBM for this purpose.

Figure 8.1 also shows an example of the summary of a customer strategy as it is applied by the company Freudenberg Dichtung- und Schwingungstechnik. The illustration does not only show the revenue and supplier share goals that the supplier would like to achieve for his various products (CHG, PTFE, etc.) with

Table 8.1 Important information on key accounts. Source: Based on IBM

Contents	Brief description
Customer overview	Name, address, number of employees, revenue, profit, financial situation, sector(s), etc. Market position, competitors, cooperation partners, trends in direct environment, critical success factors, strategies, etc. Customer’s respective business units, current and planned projects, etc.
Customer environment/ history	Solutions implemented by the customer so far, own as well as those of competitors, respective proportion of relevant total budget Relevant procurement budget Own orders received and lost
Relationship coverage Organization charts	Description of buying center Description of (business and personal) interests of individual persons Own evaluation from customer’s point of view Expectations of cooperation from customer’s point of view
Business plan	Own visions, strategies and projects Own contact persons
Opportunity plan	Information on process to identify and assess individual projects
Global account revenue	Information on globally operating key accounts

	Position today	Position in 2004 → Strategic Targets	Position in 2008 → Strategic Targets	Main Competitors + how to attack them
Sales in Mio. €	49	55 1. CHG 20 % market share on diesel engines 2. PTFE engine seals 70 % market share 3. Brake hoses additional 2.1 mio. € 4. Encoder businesses 60 % market share on xxx and xxx engines	65 1. Package sealing xxx engine xxx 2. RWDS on xxx engine xxx 3. CHG 50 % market share on diesel engines 4. Brake hoses additional business 4.5 Mio. €	1. CHG: xxx Attack on diesel engine with technical performance and cost reduction 2. Engine seals: xxx Attack with technical advantage on PTFE second generation and RWDS 3. Trans seals: xxx Attack with new Kombi seals 4. VSS: xxx Attack with low cost on xxx engine 5. Brake hoses: xxx Attack with high level technical performance on new complex BH for future cars
Market Share in %	51	59 1. Finalize the development of low cost CHG for diesel engines 2. Best in class service during the ramp up with PTFE seals 3. Develop high hardness VSS flange for xxx engine 4. Finalize the development and the industrialization of Hall effect encoder	70	
Necessary actions to achieve the targets				
Necessary success factors at xxx which should be improved at FDS				

Fig. 8.1 Overview of a sample customer strategy. Source: Based on Freudenberg Dichtungs- und Schwingungstechnik

the respective customer, it also points out the activities that the various divisions have to perform or implement within the company to achieve these goals.

Because of the vastly different market and intra-organizational circumstances and challenges, very different manifestations of key account management, the related tasks and the constellation of the respective positions and departments can be found in actual practice (Homburg et al. 2000; Zupancic 2008). They range from sales tasks related to single customers to positions or departments with specific responsibilities and even to divisions segmented by customer, with their own procurement, R&D, production, etc. In small and medium-sized companies, it is often sales managers or members of corporate management who take care of key customers. The following section will explain the different constellations of key account management, with the corresponding conditions for application as well as advantages and disadvantages. There will be differentiation between fundamental and special organizational options (Rieker 1995).

- The term **fundamental organizational options** designates the significance and propagation of business relationship management as a leadership concept within the organization. It is not about assigning a certain position or department to a place in the organizational structure but about spreading relationship management throughout workflow management.
- **Special organizational options**, on the other hand, deal with the specific constellation and outfitting of positions or department bearing responsibility for relationship management.

8.1.2 Fundamental Alternatives of a Customer-based Organizational Structure

A company has four fundamental alternatives for a customer-based organization (Shapiro and Moriarty 1984):

- Foregoing introduction despite the concept being sensible
- Relationship management as “part-time program”
- Partial introduction in one area of the company and
- Introduction throughout the company.

8.1.2.1 Foregoing Introduction of Institutionalized Relationship Management

After learning about all the reasons for and challenges of business relationship management, it may come as a surprise that a company could consider not implementing a customer-based organization. But the consideration should at least be part of the decision making process. Although the company may demonstrate the need for such activities, there may be good reasons for not doing so. This can be the case especially when the required human or financial resources are not and cannot be made available. In cases in which the position towards the customer cannot be improved and there may actually be the risk of individual customers

attempting to take advantage of the increased attention to their needs to achieve price concessions (Shapiro and Moriarty 1984), a supplier can or should consider refraining from implementation despite the general necessity thereof.

8.1.2.2 Relationship Management as an “Part-time Program”

The second possibility, “part-time” relationship management means that taking care of single, important customers poses an additional “task” for an employee. The decision to implement this type of relationship management is usually characterized by the size of the company, the available human resources, the relationship complexity and the related need for coordination, the number of customers relevant for relationship management and their geographic locations (Sidow 1993; Shapiro and Moriarty 1984; Pegram 1972).

Such a part-time program is especially popular amongst smaller and medium-sized companies, because no new jobs need be created. Maintaining and fostering the relationships with customers is taken care of by sales and marketing managers or by the owner or members of corporate management. They look after important customers in addition to performing their regular tasks.

Relationship management as a part-time task is perceived to have several advantages and disadvantages, which must be balanced against one another for each individual case:

- Such a solution surely makes sense when the “part-time relationship managers” have a relatively high position in the corporate hierarchy. They can then ensure that tasks relevant to the relationship are definitely performed. Especially when a company has only a few key customers, this is a way to coordinate goals and strategies related to single customers and to ensure that the general corporate goals and strategies are met.
- The disadvantage of this alternative is the inherent costs. Such a part-time program can only allegedly be considered an economic type of organization of business relationship management. Since the employee taking care of the key customers is usually in a relatively high—and thus well-paying—position within the corporation and must deal with the specific tasks and problems having to do with relationship management in addition to his many other important tasks, the activities related to customer care are not always given the proper diligence. And when the key customers are geographically far removed from where the part-time relationship manager is located, there is also the risk that direct customer contact will occur only rarely. It can also happen that an executive is not willing to deal with issues that seem minor to him but are important to the customer, e.g. missing instruction manuals.

So “part-time relationship management” is fundamentally an explicit way of taking care of important customers. However, its use can lead to the objectives of business relationship management being achieved only partially or not at all. This becomes more and more problematic as more key customers are cared for in this way. If the “part-time relationship manager” is not a manager, there is a substantial

risk that, because of his lack of power within the organization, he may not be able to assert himself. So “part-time relationship management” should be considered only when no other specific resources can be made available and this approach seems to promise greater success than completely foregoing organizational implementation of business relationship management.

8.1.2.3 Relationship Management as a Full-time Job

As opposed to the variations described above, business relationship management can also be implemented “full-time,” meaning as positions or departments created especially for this purpose—such as key account management—and it can be implemented partially or throughout the company.

- **Partial employment of relationship management** means that (only) certain areas of the company implement relationship management. The responsibility for implementation as well as integration in the management structure lies with the respective areas.
- **Corporate-wide relationship management**, on the other hand, means that the concept is implemented throughout the company and business relationship management becomes a comprehensive leadership strategy.

In both of these cases, key account management can be located just about anywhere within a company. There are three possible variations:

1. Integration across an entire company level
2. Integration in divisions or corporate divisions
3. Integration in units within corporate divisions, which may exist as e.g. strategic business units (SBUs) or single profit centers.

When multiple key account positions or departments exist in parallel in different divisions of a company, problems can occur when the respective institutions are responsible for one and the same customer. It is also important to remember that, for the relevant positions or departments to be able to act in the best interest of the respective business relationship partner, they have to be able to drastically or at least significantly influence the departments responsible for creating the services to be provided to the key customers. To be able to sensibly implement relationship management in regard to an important customer at this level, the SBU should—ideally—have its own R&D, production, sales, etc. (Churchill et al. 1985b; Shapiro and Moriarty 1984).

If a key customer makes procurements beyond the SBU, additional internal coordination is generally required. So it makes sense to establish business relationship management at the division level, particularly when the division includes centralized areas such as R&D, production or sales. Another benefit of incorporating the concept into a sales department centralized for the division is that when relationship management is introduced for the first time, it can be seen as a continuation of existing activities (Shapiro and Moriarty 1984). Such an

organizational connection also contributes to all key customers within the division being treated more or less equally, granting the supplier a consistent image for others. Important customers can no longer be considered a part of the SBUs, the “SBU egotism” when meeting demands beyond the SBU is reduced and the potential to design system offers increases. The advantage of dissolving the division—and at the same time a disadvantage—is the greater range of tasks. After all, key account management has to maintain an overview of all relevant services in the division, which increases complexity within the supplier’s system.

The same applies to the fourth possibility, placing relationship management at the corporate level. Here, too, the extent should be determined to which tasks that affect business relationships should occur in or be coordinated amongst multiple divisions. The potential to create system solutions that affect multiple divisions would be an aspect that makes uniform relationship management at the corporate level favorable. The greater internal and external leverage that can be expected leads to significant benefits of a solution at the corporate level. An added benefit is that behavior geared toward the customer is typically promoted throughout the company in regard to considering the needs of key customers, because the product orientation common to SBUs and divisions is attenuated (Shapiro and Moriarty 1984). The disadvantage of this alternative is that it is highly complex.

The advantages and disadvantages stated here occur particularly when a company has only one important customer. The more key accounts there are, the less likely it is that customer-oriented behavior is actually practiced with this variation; it is difficult to explicitly focus on a large number of important customers.

So in summary it can be said that deciding where to place customer-based organizational units requires a compromise. Each of the four alternatives described has advantages and disadvantages that, depending on the market constellation and circumstances within the company, are more or less relevant and have to be taken into consideration when assessing the specific organizational options.

8.1.3 Assigning Key Account Management to a Position in the Organizational Structure

8.1.3.1 Fundamental Options for Assigning Key Account Management to a Position in the Organizational Structure

The various organizational options are intended to find the best place for and constellation of key account management within the organizational structure of the supplier company. The level of the overall organization or the area in which the positions or departments should be placed must be decided, and the authority to make decisions and issue directives must be specified. The degree of authority to make decisions and issue directives has a major impact on what key account management can do within the respective company for important customers. Decision making model may be of help to this end (Wengler 2006).

There are different ways to create a position: a key account management position or department can be placed with a staff, in the line or in a matrix organization. The

abundance of the organizational forms that exist today can be systematized by the number of dimensions on which the structure is based. Following this concept, one-dimensional and multi-dimensional organizational forms can be differentiated:

- **One-dimensional organizational forms** are structured applying only a single criterion at one level of the hierarchy.
- With **multi-dimensional organizational forms**, at least two structuring criteria are applied together.

And, in turn, both organizational possibilities can take on different variations. The two most important one-dimensional organizational forms of key account management are to integrate it in the **line organization** or in a **line-and-staff organization**. The most common multi-dimensional structure is the **matrix organization**.

Figure 8.2 shows the six different ways in which key account management can be integrated into a corporate organization. The illustration is not intended to represent a real organizational form; it serves only as an example. In the illustration, key account management is shown as being possible at all levels of the organization, which could never be the case in reality. It could also never be integrated as a staff function and a line function at the same time. The illustration shows a company that, below the executive level, consists of (product-based) divisions at the top, then independent functional areas at the second level and geographic regions at the third level. This facilitates discussion of the effects of these three structural criteria, which are often related in practice, on key account management. Neither other staff unit nor functional area is considered, and activities are not differentiated by domestic or international. Interconnections between the areas are not considered. Neither are temporary organizational forms such as project organizations, task groups, management groups or general quality circles. Other cross-division functions such as controlling, quality management and environmental management are also not included.

8.1.3.2 Key Account Management as a Staff Function

Staff units support line entities, from which the staff positions derive their tasks or which assign the tasks to the staff. They generally prepare decisions but do not have the authority to make decisions themselves. When key account management is a staff unit, it is assigned to a managing position, e.g. corporate or sales management.

The tasks of such a staff unit are essentially limited to information gathering and planning activities. Coordination measures that require managerial authority must be directed by a higher-ranking position. In such a case key account management is restricted to providing conceptual and analytical preparatory work and to possibly monitoring implementation.

In actual practice it can happen that key account management is not able to assert itself with the required business relationship management measures when dealing with supervisors and other departments and areas. This can in turn lead to internal conflict and subsequently to frustration on the part of the person attempting to

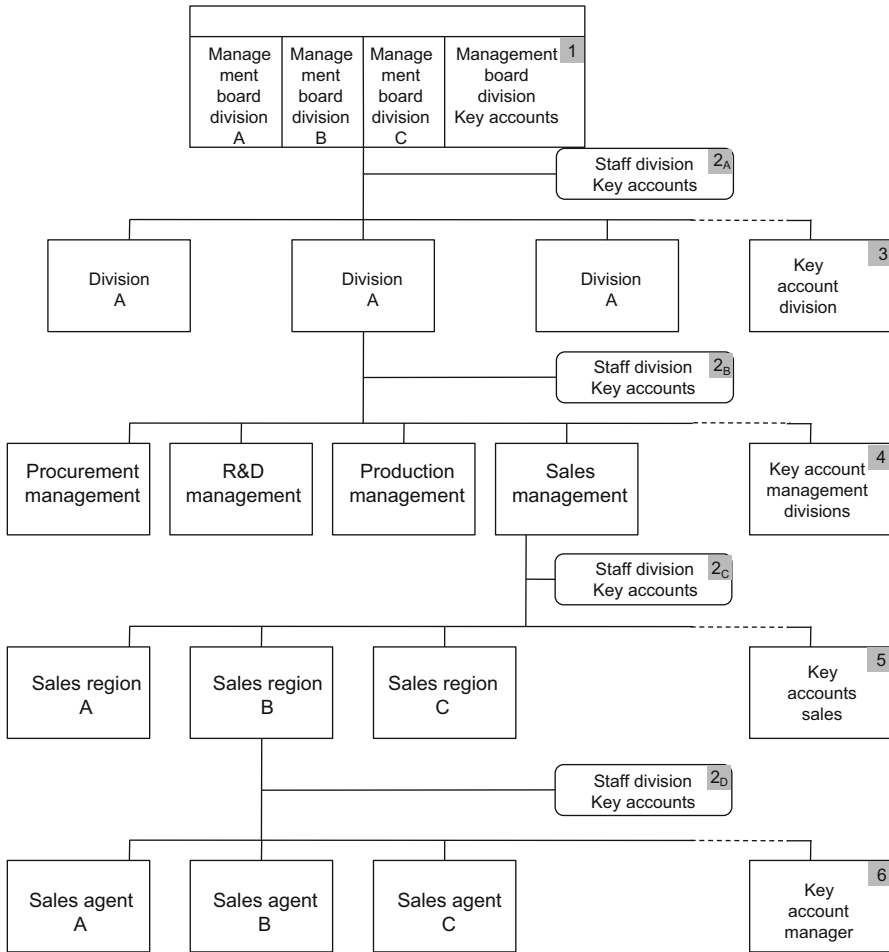


Fig. 8.2 Potential integration alternatives for a “key account management” position or department

execute the tasks—and on the part of the customer as well. It can be concluded that key account management is not well suited to implementing the tasks related to relationship management (Sidow 1993; Wolter 1985).

There are, however, variations in which key account management as staff could be conceivable. Assignment to a higher position in the hierarchy may make sense, such as variations 2A to 2C in Fig. 8.2, under the condition that the respective position supports key account management unconditionally. If key account management is assigned to an executive who is willing to implement all measures in compliance with business relationship management, key account management itself is not as dependent on having its own position of power. However, this variation is conceivable when there is only one or very few important customers.

Appointing a **staff unit as key account management** under the circumstances described above can also—depending on the size and complexity of the corporation—occur under a division manager or, when the sales and marketing manager has a strong position, under his leadership.

A key account management staff unit can only be successful when the next-higher line position has the authority within the corporation and the division to support the business relationship management orientation across all relevant departments and is also willing to do so.

The same applies in regard to externally geared key account management tasks. When key account management has to deal with many aspects that require coordination with the customer, it is especially important that its authority is “visible” externally. If a key account management staff cannot assert itself internally and cannot e.g. decide on price advantages to be granted to customers, it loses credibility in the eyes of important customers. Furthermore, subordination of the key account management staff to the division level or lower would make sense only when the key account receives services exclusively from this division. Even assigning the key account to the division for which it is most important can be seen as problematic. On the one hand, this could lead to a conflict of interest for the key account management since it is assigned to only one division; and on the other hand it can become more difficult to exert influence on other divisions. Since key account management is intended to give the supplier organization a coherent appearance, it would make sense to relegate it to the division level only when there are absolutely no market interdependencies. And since high fluctuation in staff might happen, the potential to establish long-term (personal) relationships is limited.

So key account management as a staff unit generally exhibits relative distinct differentiation, whereby the focus of specialization is on analysis, planning and monitoring tasks, while the implementation is greatly dependent on the supervisor (Schreyögg 2003). This can make it more difficult for key account management to be integrated in the corporation, and the key account management cannot achieve integration alone in these variations. The disadvantages of key account management being organized as a staff unit lead to the conclusion that this organizational form is advisable only in exceptional cases. This could be the case when the staff unit is established temporarily in preparation for later implementation as a line function.

8.1.3.3 Key Account Management as a Line Function

Line units are where execution takes place. They follow the principle of task placement and are characterized by clear seniority and subordination. So in such a case key account management is a true line entity between its own supervisor and the subsequent departments—to the extent that there are such departments. In this regard key account management can be the highest or just as well the last link in the chain.

Such an organizational unit should fundamentally be placed at the level of the company at which control can best be exercised over the tasks required for business

relationship management over the long term. The larger the unit is, the more resources there are available for the activities—and the greater are the internal coordination requirements and the more difficult it is to promote (single) customer-oriented behavior on the part of all employees.

Management Board Division “Key Accounts”

The highest place in the hierarchy where key account management can be integrated is variation 1 in Fig. 8.2. Establishing “key accounts” as a management board division can be beneficial particularly in the following cases:

- Small or medium-sized companies with only very few key customers who are so important that such priority treatment is expedient. Such “key account management at the highest level” would oblige the important customers’ need for high-ranking contacts. The challenge, however, is that the persons involved are willing and capable to meet all of the partial requirements related to business relationship management. This includes e.g. initiating, maintaining and fostering internal and external contacts as well as the willingness to personally deal with complaints from key accounts. So this type of key account management requires that the position and the “self-image” of a board member or executive of a company can be harmonized with the tasks of a key account manager.
- A second possibility, which is much easier to implement, is that an appropriate board or corporate management department act as the highest authority of an executive committee or of a clearing house for all of the company’s key account management units. In such a case the role of the management board division “key account management” would be limited to coordination of the various key account management positions in the divisions and regions as well as to intervention in individual cases, e.g. when consultation of a higher order is required. Such a variation is beneficial e.g. when there is a large number of key accounts purchasing various services from the different divisions. The advantage would be that the highest level has an overview of the key accounts and coordination of various functions can occur at that level. This ensures that the required business relationship management measures, which may be different for important customers, can be reconciled with the company’s resources. Coordinating the corporate strategy with the strategies followed for single important customers can be more easily effected in this case as well.

Both applications of variation 1 can be beneficial, taking into consideration the stated conditions when relationship management is assigned a high enough priority. Such a position can also be advantageous in regard to communication with customers, when the person occupying the position can be called in e.g. when a high-ranking representative is needed to deal with the key account. So the function of a “key account management” board member is comparable to that of a “sponsor”, who (personally) intervenes only in exceptional cases but who maintains an overview and control of the entire situation (Shapiro and Moriarty 1982).

Key Account Division

Another variation of organization integration of key account management is to assign it to a division or strategic business unit responsible for caring for all important customers. This means that such a unit performs not only sales and marketing functions but also has its own manufacturing, R&D, procurement and other functions (Shapiro and Moriarty 1984). This type of key account management is promising particularly when

1. Learning curve effects in production play a subordinate role, so establishment of own production has no negative effects on the unit costs of important customers
2. Important customers purchase completely different services than other customers, meaning that synergies are negligible or services have to be created individually
3. Key customers expect a completely different scope of services, making it possible to clearly differentiate when the service is created
4. Coordination between R&D, production and sales is essential to achieving the objectives of business relationship management, such that, without the direct influence on these departments and without their knowledge of the significance of the customers, successful implementation of business relationship management is endangered and/or
5. Key customers provide so many resources that a separate division or own SBU is justified.

If, on the other hand, there are no market interdependencies between the divisions, key account management can basically be assigned to a single division. There are two different possibilities, shown as variations 4 and 5 in Fig. 8.2.

Division Key Account Management

Variation 4 represents stand-alone division key account management. In this variation the sales manager, as well as the management levels of the other functional areas are at the same level in the hierarchy as key account management. So, important customer and those that are less important are taken care of within the division, but in different and very separate ways. The advantages and disadvantages of this organizational variation are similar to those of a separate division for key accounts.

Particular relevance is assigned to the process for identifying and assessing the attractiveness of important customers (Chap. 4). The question as to whether the marketing department or the sales department—if they exist as two distinct departments—should be responsible for selection of the key accounts should be decided as a factor of the significance of the marketing department and of which department will later be responsible for key accounts. If, for instance, the marketing department is a staff function that deals primarily with marketing services such as market research and advertising, and the sales department is later to take responsibility, marketing should surely be consulted but the decision should ultimately be made by sales. If, on the other hand, marketing is considered an integration function

geared towards market-oriented corporate management, the strategic significance of key accounts would mean that it makes sense for marketing to decide on identifying them. If sales is to be responsible for later customer care, the department should definitely be heavily involved to quickly anticipate any resistance.

Criteria and their assessment should not only come from these two areas though. It has already been pointed out that relationship management requires significant input and cooperation from all areas of the company. This is why it is important that as many areas as possible be involved in identifying potential key accounts. For example, the customer's technological leadership and willingness to cooperate on R&D may be of particular relevance to the R&D department, while accounting may be more interested in a customer's creditworthiness and cash flow and procurement sees development of joint recycling strategies as an essential aspect. Consulting all of the departments and areas may make the identification process more drawn out and complex, but it promotes a different type of identification process that, from the point of view of key account management, is of particular importance: identification with the key customer. A department actively involved in selecting such a key customer will get to know the customer's company better and will thus be in a better position to recognize its significance and to act in a customer-oriented manner.

When variation 4 is implemented, a conflict can occur when customers are selected who should later receive special care as key accounts. If sales management is consulted to identify important customers, it is safe to assume that sales will (later) be interested in "normal customers" and that not all interesting and possibly profitable customers will be handed over to key account management. So a "two-class society" could evolve within the division, whereby one "class" is responsible for the key customers and the other for the other customers. This can also impact the relationship to the other areas within the division. If the structure shown in Fig. 8.2 is applied, the functions such as R&D, production, etc. may be subjected to—sometimes contradictory—demands of sales management and of key account management. They might both attempt to make their fulfillment a priority in regard to the needs of their customers. With this variation, key account management's opportunities to contribute to initiation and constellation of customer benefits could be marked by a permanent conflict with the sales department or manager, who becomes an internal competitor to key account management with its own claims, wishes and demands. This could be particularly problematic when division key account management does not have the same access to certain resources. If, for example, customer service is positioned under the leadership of sales management, this area—essential to after-sales marketing with respect to the key account—can cause difficulties.

The benefits of this variation can surely be attributed to the relatively strong position of power that key account management has as well as to the potential to concentrate on the key customers within the division. And the relatively high position in the hierarchy facilitates access to the required assets. However, when variation 4 is seen as a whole, the problems and potential conflicts outweigh the possible positive effects. This alternative can fail particularly as a result of resource interdependencies, internal animosities and demarcation difficulties.

Sales Area “Key Accounts”

Although the internal position of power of key account management is lower in variation 5, it appears more likely that, with all other conditions being equal, this variation is better able to implement business relationship management overall. The problematic conflict between general sales organization and key account management is mostly avoided. The position of sales management is stronger in variation 5 than in variation 4, because it has responsibility for all customers. Due to the respective customers' significance to the company's success and thus to the success of sales, and due to sales management's position of power, it seems plausible that key account management would receive pronounced support from the higher-ranking position. The uniform appearance thus facilitated strengthens the position over other functional areas more so than does variation 4. So the chances of successful implementation of business relationship management can be considered to be good with this variation. However, variation 5 is highly dependent on sales management's position of power.

Key Account Management in the Sales Area

The last possibility is to assign key account management to the same level of the hierarchy as a (regional) sales representative. So it is not until the lowest level of the hierarchy that there is a distinction between key customers and other customers in regard to customer care.

Placing key account management here is surely the simplest variation from the implementation point of view, because no fundamental restructuring is needed. But this benefit is also the greatest disadvantage: key account management at this level is marked by little hierarchical power, restricted access to higher levels and all other functions, and poor visibility. It is very difficult for this type of key account management to assert itself internally. And external visibility is low, because key account management at this level of the hierarchy is perceived by the key customers as having a relatively low status. Because it is assigned to a sales region, the power of the person responsible for key account management is limited as well. So this type of organization can be successful only when the following requirements are fulfilled (Shapiro and Moriarty 1984):

1. The company has a large quantity of locally important customers and thus a great need for key account management positions to care for single customers. The advantage of variation 6 is that it is easy to implement.
2. Key account management tasks are clearly defined. Only limited flexibility is needed to perform the tasks.
3. There are no market interdependencies between the sales regions in regard to key accounts.
4. There is only minimal need for conflict resolution mechanisms, substantiated particularly by points 2 and 3.
5. The sales department's culture of cooperation, meaning the high value it places on working together, is pronounced.

6. Sales possesses mature and proven management systems, such as information and complaint management systems.
7. Support needed from other areas is primarily of a local nature, e.g. service personnel or administration.

If, however, the tasks resulting from the demands placed on relationship management are very complex and hard to plan, or if the customers are too important, it does not make sense to assign their care to this level.

Key Account Management in the Matrix Organization

Finally, the advantages and disadvantages of integrating key account management in a multi-dimensional organization will be discussed. The most notable form of such an organizational constellation is the **matrix organization**, in which one position is placed under two other, higher-ranking organizational units having equal rights. When key account management is organized as a matrix, one of these two dimensions is determined by the key customer. The second dimension is usually formed by a function-related or object-related organizational unit. The benefit of this organizational form is the dual view of product or function point of view and the customer's point of view. So the risk of a dominant perspective addressed with line organization is eliminated. And the greatest problem with staff organization, the discrepancy between competence and responsibility, is much less prevalent. If, however, key account management cannot assert itself against the second tier of management and is seen only as a customer-based coordination point, it cannot be considered superior to the staff function (Schreyögg 2003). Another potential benefit can be the short and direct communication routes. Suggested improvements or ideas for new products that key account management receives from customers can quickly be conveyed to product management. However, because the two dimensions have equal rights, substantial effort is required for communication. There are many interfaces between key account management and product and function management—interfaces characterized by the fact that the competencies and responsibilities of the two management levels overlap one another. So the goal of the two performance levels should be to utilize their competencies and responsibilities to reach joint decisions. Since there is no hierarchical differentiation between the two dimensions, and product or function management has the same rights as key account management, this would require team work between the dimension managers. In practical applications, however, power struggles often ensue, lasting until one level proves itself dominant over the other.

So key account management can be considered beneficial in a matrix organization, only when the conflicts between the two levels are minimal.

8.1.4 Composition of the Positions and Departments Responsible for Key Account Management

As the previous sections have demonstrated, key account management can be put into practice at different levels of a company, assigned to different supervisors and implemented in different areas of the company. But to determine the exact location, a supplier company should strategically consider the result it wishes to achieve by implementing key account management. In addition to the actual integration of key account management in the supplier organization, the exact composition of the positions and departments can impact how business relationship management is actually implemented when dealing with important customers. Designing such a position includes defining

- Its responsibility
- Its authority and
- Its obligations.

These features of the position's compositions must be carefully examined as to how they support achieving strategic objectives, with the intention of avoiding the common problem of discrepancy between responsibility and hierarchical position and thus the authority to assert certain goals (Gaitanides et al. 1991).

In this context responsibility designates the scope of duties that key account management is supposed to perform. Such duties can be differentiated between (Gaitanides et al. 1991)

- Responsibility for action
- Responsibility for results and
- Managerial responsibility.

Key account management can meet its responsibilities only when it is in a position to grant internal and external consent, to make concessions and to organize negotiations and courses of action. This is also referred to as internal competence and external competence, whereby **internal competence** means internal decision making and managerial authority, and **external competence** the decision making discretion when dealing with customers (Gaitanides et al. 1991).

These include key account management's rights to negotiate, reach agreements, issue instructions, participate and supervise—all of which must be clearly specified. For clarification and simplification purposes, the term “managerial authority” will be used to designate internal competences and the term “decision making authority” to designate external competences.

The tasks, responsibility and competence of key account management should follow a matching principle, meaning they should correlate with one another. If this is not the case, it could lead to customers perceiving key account management as “bothersome”, because it is not in a position to make commitments and implement them (Gaitanides et al. 1991). If key account management does not have sufficient

decision making authority, it cannot act as a relevant dialog partner for the customer and promise him customer benefits. Too little managerial authority can make it difficult to achieve the goals of business relationship management, because the relevant areas of the company do not feel obligated to comply with the specifications of key account management.

If key account management's position is such that it can wield power, it can "force" implementation of the goals of business relationship management. But if the internal departments have the same or more power, or if there are no direct power relationships, key account management can only try to motivate the departments to participate in integrated creation of customer benefits. Approaches can be found first of all by influencing the participants' intrinsic motivation, such that creating customer benefits becomes an internal obligation to them. Examples of this are

- Cooperation in designing and setting goals
- Working together to define key customers
- Becoming aware of the customer's problems by visiting his plant or
- Incorporation in the selling center.

Additional possibilities can be found by influencing extrinsic motivation of the participants, e.g. by

- Granting bonuses based on customer satisfaction to sales and service employees
- Granting bonuses for meeting deadlines and quality requirements of key accounts in the production area or
- Approving research budget by the market success of innovations.

The third task is to define the **duties** of key account management that have to be performed in the constellation of such a position or department. The main duties are to realize each customer's commitment potential and the resulting tasks. Key account management as "supporter of relationship management based on individual customers" deals with the relationship with an important customer. The extent and focus of the tasks is greatly dependent on the **complexity of the relationship** to be considered between the supplier and the purchaser. It is influenced primarily by the complexity of the environment relevant to both parties, by the coordination problems resulting from the vast number of connections between the companies, and by the consequent need for information and communication.

Environmental complexity is based on exogenous variables such as the unpredictability and uncertainty of the environment or environmental dynamics. The focus of consideration though is not mastering the complexity of the environment but mastering the complexity of the relationship between the supplying companies and the key customer.

The **complexity of the relationship** is also impacted by the complexity of the company relevant to the relationship, the complexity of the key customers relevant

to the relationship and the complexity of the offering (Shapiro and Moriarty 1980; also Köhler 1984; Weitz and Anderson 1981; Zeithaml et al. 1988).

- The **complexity of offering** can depend on many different aspects. These can include the type of offering (raw material, parts, components, systems, etc.), their degree of standardization and customization, the proportion of the service component, the degree to which the customer is included in creation of the service, potential system lock-in, quality requirements and many other aspects (Shapiro and Moriarty 1980). The complexity of the offering can have an impact on the company's internal coordination requirements as well as on customer-related coordination requirements, depending on whether actual service creation or inclusion of the customer is the focus of service definition and justification.
- The **complexity of the supplier** can be based on size, organizational form, number of levels in the corporate hierarchy, interdependencies and differentiation between the departments, corporate culture, degree of resource egotism, size and geographic distance of corporate units, regional distribution (regional/national/international) of the production facilities and sales offices relevant for the customer, etc. The greater the **supplier complexity** relevant for the relationship, the more difficult it is to internally coordinate the various tasks of business relationship management.
- Indicators of **complexity of the customer** can be affiliation with certain branches, customer's regional propagation (regional/national/international) (for an example, refer to Zupancic and Tomczak 2004), degree of centralization of procurement, etc. The greater the **customer complexity** relevant for the relationship, the more difficult it is to coordinate business relationship management tasks geared towards the specific customer.

All of these criteria can affect the complexity of the relationship between the supplier and the key customer, whereby it can be assumed that the overall task becomes more extensive as the relationship increases in complexity. The range of tasks becomes greater as the number of exchange relationships between different departments or business units increases, on the part of both the supplier and the purchaser, and as the services exchanged increase and become more heterogeneous.

The more functional areas and hierarchical levels in the corporation are affected by the relationship with the key customer, the greater is the need to implement business relationship management more extensively within the corporation and to have the support of top management to be able to be successful (Guesalaga 2007). If it is implemented in only part of the company and/or only to a certain level in the corporate hierarchy but other areas and levels are also relevant for the customer, "control" of the various activities is limited.

8.2 Key Account Manager Requirements

In addition to having an organizational structure suited to key account management and a corresponding constellation of the position of the key account manager, the right person must be selected to fill this essential role (Müller and Ivens 2011). Much more is generally expected of a key account manager than of a regular sales employee (Guenzi et al. 2007). Key accounts are a company's most important customers and have to be treated and cared for properly by the supplier. For such customers, the most important contact should be the respective key account manager (Guenzi et al. 2007). The key account manager takes care of essential communication with the customer company and is the primary contact person for all technical and business questions. He is responsible not only for ensuring that the current business relationship runs smoothly, he must also be able to detect additional potential for expanding the partnership or warning signals that the business relationship may be endangered. So publications and practical applications specify essential requirements that the key account manager as a person has to meet; however, these requirements are not always adequately fulfilled (Guenzi et al. 2007).

The requirements include social competencies (capability to interact with others) and personality traits, analytical and conceptional skills, and expertise (Homburg and Krohmer 2009). Since the key account manager is usually the essential interface between the supplier and customer companies, his social competence along with his personality traits play a prominent role. But much is also expected in regard to analytical-conceptional capabilities as well as expertise.

8.2.1 Social Competence

A key account manager's social competence includes particularly the following properties, which he needs when dealing with the customer's employees as well as those of his own company (Homburg and Krohmer 2009):

- **Intuition/empathy**

The key account manager especially has to be able to understand the customer's actual interests, even when these are not explicitly expressed or when the interests differ from the key account manager's initial impression (Mayer and Greenberg 2006).

- **Communication skills**

The key account manager is often the main information conduit from the customer to the company and vice versa. So communication skills are needed to collect and distribute the right information to the right place at the right time. For information that he brings into the company, this can mean e.g. entering the information in the CRM system and making it accessible to the employees who need it. If the key account manager is head of a key account management team,

he should be able to promote decentralized communication between members of the team (Sect. 8.3.2.2).

- **Adaptability and flexibility** when interacting with other people
As described in Chap. 1 of this book, many business relationships take place in an international context. This means that supplier companies and customer companies may have different national cultures and business customs. So it is absolutely essential that a key account manager be able to adapt and react to such differences, always complying with legal stipulations, of course. The degree of adaptability seems to be positively influenced by the experience and education level of the key account manager (Ulaga and Sharma 2001).
- **Capacity for teamwork**
In most cases, key account management can be successful only when both the supplier and the customer have specialists working part time on business relationship management or when key account management is always implemented by a team. In both companies, these people can be research and development employees, production engineers, programmers, quality managers or attorneys. Such employees often have different professional backgrounds, so the key account manager must be able to adapt to the respective communication customs as well as to understand and sometimes interpret the technical language. A key account manager's capacity for the required teamwork also includes leadership skills and conflict management skills (Lambe et al. 2009). He must also be in a position to know which experts or specialists have to be consulted for which issues (Steward et al. 2010).
- **Assertiveness**
It is very important that a key account manager be able to assert himself within his own company. Inquiries and orders from the customer that the supplier can fundamentally deal with may need to be prioritized in relation to other tasks in the supplier company to be able to fill orders as promised to the customer. Determination and initiative are often essential to the key account manager. The degree to which the key account manager can assert himself is strongly dependent on where and how key account management is anchored in the corporation and on internal competencies and processes, but his personal disposition also plays an essential role (Ivens and Pardo 2008).

8.2.2 Personality Traits

In addition to social competencies, a key account manager's personality traits are also essential to mastering his tasks. Personality traits are considered to be aspects of a person's personality that do not change over time. It has been shown many times that they influence a company's sales performance (Churchill et al. 1985a). The field of psychology differentiates between five fundamental dimensions of personality traits—the so-called “big five” (Digman 1990): conscientiousness, agreeableness, emotional stability (or neuroticism as the opposite pole), openness and extraversion (opposite pole: introversion). Since a key account manager is in a

position with a great amount of responsibility, he should demonstrate a high degree of all five personality traits. Aspects of conscientiousness such as personal integrity and reliability are required for a good relationship at the personal level between the key account manager and the people he deals with within the customer's company. Since the key account manager serves as the most important interface between the supplier and the customer company, he should be able to deal with many different people. He should also be able to handle conflicts and tension inherent to this interface position, and he should demonstrate emotional stability. A certain degree of openness ensures that the key account manager is open to creative ideas and recognizes approaches to solve a customer's problems. Extraversion is expressed in forceful action and approaching other people—traits that a key account manager should definitely possess.

8.2.3 Analytical-conceptual Capabilities

Because of the great degree of responsibility associated with caring for a company's important customers, it is essential that a key account manager have a great deal of analytical-conceptual skills. These are general, cognitive capabilities. When confronted with new tasks, the key account manager should be able to quickly structure them well and solve them. A high degree of analytical-conceptual skills is reflected in intellectual capacity (processing speed, memory, creativity, processing capacity) and special problem solving techniques. The skills can be figural-visual, verbal or numeric (Homburg and Krohmer 2009). Analytical-conceptual skills can be learned to a certain degree, e.g. by acquiring certain creativity, structural and decision-making techniques.

8.2.4 Expertise on Customer and Business

As the most important contact person for the customer as well as an essential source of information for the other functions within the supplier company, the key account manager must possess a wealth of solid expertise. In addition to general knowledge of business, technical and legal aspects and general managerial skills, it is particularly important that the key account manager be well informed on matters related to the customer and the specific business.

Among other aspects, this expertise includes knowledge of the following areas (Homburg and Krohmer 2009):

- Market and sector conditions and customs
- Customer's general business operations: strategic focus and economic situation, sales and procurement markets, plans for the future
- Organization of customer's company: structures, persons, processes, communication channels

- Cooperation with the customer: solutions to problems from within own company (technological, organizational, financial), critical aspects of cooperation, potential for expanding cooperation, indications that the business relationship may need to be examined
- Problem solving skills of competition and realistic assessment of own standing as supplier to the customer
- Own organization, particularly structures and persons (experts, specialists) to quickly and competently deal with customer inquiries and orders
- Fundamental technical aspects of the own offering to the customer.

Some of the expertise that a key account manager needs can be acquired through specific training or learned directly through practicing a profession, but some is based on experience. The wealth of required expertise on the customer as well as one's own organization means that it makes sense to develop a marketing or sales employee to fill the position of key account manager instead of hiring someone to directly take the position. This strategy is a common career path in many industries (Homburg and Krohmer 2009).

An example of this can be found in the pharmaceutical industry, where future key account managers are sometimes inducted into the position (taking responsibility for two to four large global customers) by accompanying the current job holder for a year before ultimately taking over the position alone. This is intended to ensure that the knowledge related to the customer as well as to the supplier is passed from the old to the new key account manager and the new key account manager can establish a similar reputation towards the customer as his predecessor had.

This procedure meets the need for continuity in key positions between the supplier and customer company; depending on the branch, the bonding effect to a certain person in the supplier company, often the key account manager, should not be neglected (Palmatier et al. 2007). In some service sectors the loss of a key account manager or a person acting in this capacity can mean the loss of the customer, e.g. in management consulting or auditing. So for companies with stable business relationships, it is worth offering the key account manager incentives to remain in the position for a long time (Palmatier et al. 2007).

An exception that occurs once in a while, particularly when the supplier and customer have a very close partnership, is that the key account manager goes to work for the customer's company. When this happens with the consent of both companies, the loss of the key account manager may have positive effects, such as even better cooperation with the customer.

8.3 Key Account Management Teams

As the course of this book has made clear, business relationship management is a complex task that can only rarely be mastered by a single person within a company. So institutionalized business relationship management in the form of key account management has one key account manager, but he is often supported by a key

account management team (KAM team). Jones et al. summarized the state of knowledge at the time as: “*Key accounts are predominantly served by some sort of team by supplier personnel*” (Jones et al. 2005a, p. 181). Besides the key account manager, such teams frequently include employees from marketing, production, quality management, logistics and accounting (Homburg et al. 2002).

Unlike the constellation of a selling center, which is often put together ad hoc, the composition of a key account management team is generally stable (Moon and Strong 1994). So the customer’s employees deal with the same supplier employees over a long period of time.

Some of the properties of a KAM team (Ahearne et al. 2010) are that:

- It consists of single persons that see themselves as a social unit and are viewed like this by outsiders as well
- These people depend on one another in their tasks
- The team is part of a larger organization
- The members develop a sense of community or esprit de corps and seek synergies with other members of the team
- An attempt is made to enable greater performance than would be possible through single persons. This is achieved by better balancing work packages, improving information flow and increasing motivation with mutual coaching and feedback.

Like a key account manager, a KAM team is responsible for a certain customer. It is in charge of developing and implementing the business relationship strategy for the customer (Moon and Strong 1994). Because of the various contact points with the customer company, in regard to the hierarchy level as well as to functional responsibilities, the main goal of a KAM team is to develop and grow a strong relationship with the customer (Moon and Strong 1994).

While customer service teams and KAM teams have been around for a while, it is only in the last fifteen years that academic research has begun to look closely at the effects of KAM teams and their success factors. We are now going to examine the reasons for establishing KAM teams (Sect. 8.3.1), the anticipated positive effects (Sect. 8.3.3) and the success factors identified thus far (Sect. 8.3.2).

As Fig. 8.3 shows, the effects of KAM teams as well as the success factors that influence them are located at both the team level and at the level of the overall organization.

8.3.1 Reasons for Establishing Key Account Management Teams

The increased use of KAM teams over the last two decades can be attributed to developments in the competitive environment, in both the customer company and the supplier company.

Jones et al. (2005) see KAM teams as a way to counter the rise in competitive pressure. Perry et al. (1999) also focus on the competitive environment when they

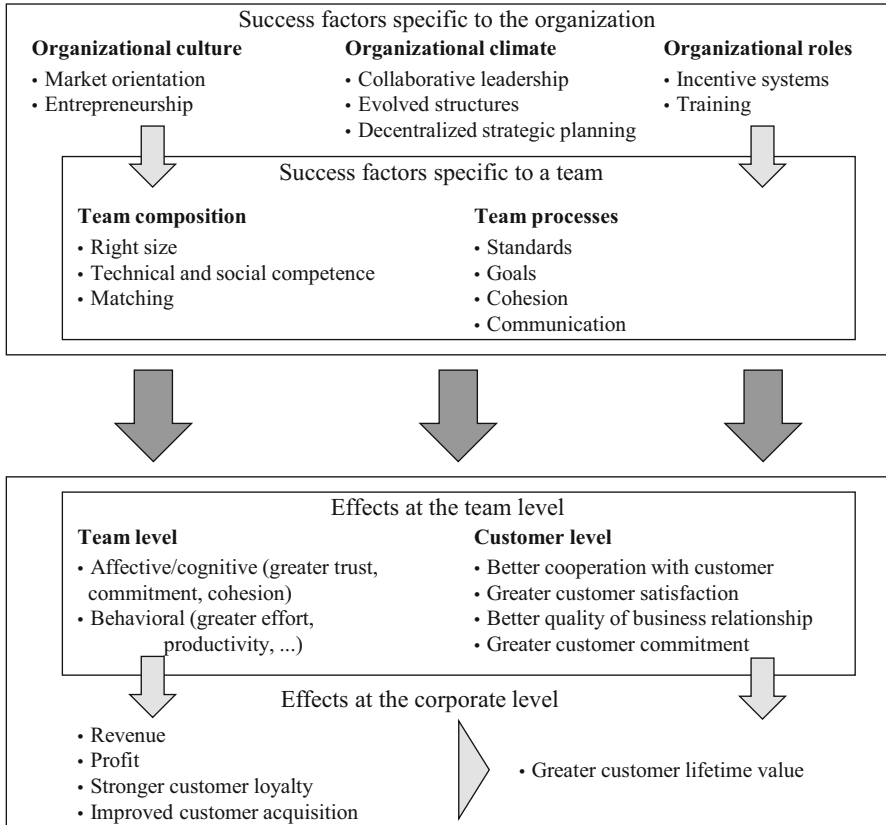


Fig. 8.3 Success factors and effects of KAM teams

talk about quickly changing environments and customer demands, changes in the technological environment and globalization of customers and competitors (Jones et al. 2005).

An empirical study by Jackson et al. (1999) on the use of sales teams instead of single persons reveals that teams are employed when

- The customer purchases a complex product for the first time
- The customer needs a lot of information
- The key account requires special attention
- Multiple persons are involved in the purchase decision
- The specific transaction represents a high volume for the supplier company
- The specific product is new to the key account manager's responsibilities or
- The complexity of the offer of products and services exceeds the cognitive capacities of a single person from the supplier company (Jackson et al. 2010).

On the customer's part, new customer demands and changing customer contact patterns, such as electronic supplier-customer interfaces, have led to more KAM teams (Dixon et al. 2002).

Supplier companies ultimately have high expectations of the implementation of KAM teams. With the diffusion of the customer lifetime value concept (CLV, Chap. 4), KAM teams are seen as a way to intensify the business relationship with a customer (Perry et al. 1999) and to thus increase the CLV (Jones et al. 2005). This is to be accomplished with better strategy coordination, more cross-selling and better solutions for the customers (Ahearne et al. 2010). And the concept of relatively autonomous teams goes well with the abolishment of hierarchies, evident in many companies (Perry et al. 1999). Selling teams also contribute to better knowledge management within the organization: information on customers is collected, distributed and used more effectively with technology-supported CRM (Arnett and Badrinarayanan 2005).

Thus there are many reasons to employ KAM teams. So now the question is: which specific effects should be achieved and what are the requirements to make this possible?

8.3.2 Success Determinants of KAM Teams

Although there are many diverse reasons for introducing KAM teams and this phenomenon of business relationship management can be seen more and more in practice, simply implementing KAM teams cannot guarantee that the related performance targets will be met. Research rather shows that certain factors can promote or impede the success of KAM teams. Such success factors can be located at the level of the overall organization as basic parameters. If these basic parameters require the use of KAM teams, other determinants at the team level play a crucial role in KAM teams fulfilling the hopes set in them.

As Lambe et al. (2009) point out in two empirical studies, this is still only very rarely the case. Poor team management, lack of training and team members without the essential skills prevent the set objectives from being reached. This is why the following sections are dedicated to the examination of the factors that make a KAM team successful.

8.3.2.1 Success Factors Specific to the Organization

The following factors are requirements or essential conditions for KAM teams to be successful. They apply to the entire organization of the supplier company. Jones et al. (2005) differentiate between the organizational culture, the organizational climate and the organizational processes (Jones et al. 2005), whereby they refer to publications on market orientation (Kohli and Jaworski 1990; Slater and Narver 1995).

An organization that values and promotes teamwork is particularly important to successful establishment of KAM teams (Jones et al. 2005). This can happen best in a "learning organization." According to Slater and Narver (1995), such an

organization is characterized by two special features of organizational culture—market orientation and entrepreneurship—and by three elements of the organizational climate: encouraging leadership, evolved structures and decentralized decision making.

Organizational Culture

As they relate to KAM teams, two aspects of organizational culture deserve special attention: market orientation and entrepreneurship. Kohli and Jaworski (1990) see **market orientation** as consisting of three basic processes that occur in the entire market-oriented organization more or less as permanent background processes: collection and generation of market intelligence, dissemination of this knowledge throughout all departments and levels of the hierarchy, and a willingness (responsiveness) throughout the organization to react to the knowledge. So the market orientation is the part of the corporate culture that ensures that the company acts in a way that promotes creation and maintenance of true customer and supplier benefits. So the market orientation serves as a guideline for (further) development of a company's offerings and of the future focus of its organization. The emphasis is always on generating a high customer benefit for one's own customers without losing sight of the supplier advantage. Since the customer benefit is always gaged from the customer's point of view and his requirements are constantly evolving, a market-oriented company has to keep up with changes and learn from the customers (Jones et al. 2005).

When KAM teams work in a market-oriented company, it is easier for the team members to see their own work through the customer's eyes. They are able to recognize dependencies between different functional areas that are essential to finding a better solution for the customer. For example, when the introduction of a new logistics concept is being planned, the logistics expert from the KAM team would be better able to detect in discussions with the customer that, for the customer, quality assurance aspects will be affected. He could in turn easily talk about this with the quality manager in the KAM team, because both team members, independently of their functional responsibilities, aim to offer the customer an optimum solution. In an organization that is less market-oriented and is structured e.g. strongly by function, such processes would cause more friction in a KAM teams and, in the worst case, have a negative impact on the customer.

The second important basic parameter of organizational culture besides market orientation that favors employment of KAM teams is **entrepreneurship**. Entrepreneurship (sometimes called "intrapreneurship" when entrepreneurship within or outwards from a corporation is meant (Jones et al. 2005), whereby we focus on both meanings here) is expressed by proactive action, a certain risk tolerance, receptiveness to innovation and an active aversion to bureaucracy (Slater and Narver 1995). Entrepreneurship within a corporation is manifested by entrepreneurial companies recognizing and creatively utilizing market and innovation opportunities. This includes, on the one hand, completely new business activities (new services, new customers) and, on the other, constant monitoring and transformation of existing business relationships with innovations (Jones et al. 2005). The principle of trial

and error is often applied in this process. Higher learning ability is attributed to an organizational culture characterized by entrepreneurship. Entrepreneurial organizations are frequently those that first introduce an innovation to the market and reap higher profits this way.

In entrepreneurial companies KAM teams have the job of detecting even weak signals from customers and turning them into new and creative solutions. In an entrepreneurial company, KAM teams are set up as entrepreneurial units with the necessary skills, resources and flexibility to be able to easily react to new customer demands.

Organizational Climate

While a company's culture grows organically over an extended time and is difficult to change, aspects of the organizational climate are more tangible and easier to modify. These include responsiveness and support of an organization, the leadership style practiced, the type of relationships within the organization and the type of conflict management (Jones et al. 2005). According to Slater and Narver (1995), the following aspects of the organizational climate are central to the establishment of a market-oriented, learning organization:

- Facilitative/collaborative leadership
- Organic/evolved structure
- Decentralized strategic planning.

Facilitative leadership is a leadership style in which the supervisor acts less as an expert instructing his employees on how to perform their tasks and more as a coach, motivating and supporting his employees. A key account manager who practices such a collaborative, facilitative leadership style sensitizes his team members and customers alike to topics that may become important in the future and grants his team adequate access to all essential information. He facilitates an open-minded and trusting climate in the KAM team and supports cooperation amongst the team members. When contemplating important decisions, such as expanding the KAM team or assigning roles within the team, such a key account manager asks for the opinions of the team members or allows the team to participate in the decision making process (Jones et al. 2005).

Evolved structures are used to pursue a high degree of adaptability. This happens with informal processes, decentralized decision making authority and a relatively low degree of specialization. Evolved structures always range between the requirements of stability and flexibility, between clarity and order on the one side and spontaneity and responsiveness on the other. Companies that do justice to both poles are characterized by open communication paths, personal responsibility of the employees, getting things done and frequent decision making with group consensus (Jones et al. 2005).

Evolved structures in KAM lead to KAM teams being able to make decisions towards the customer themselves, roles and responsibilities in the team having gradual transitions, and team members frequently communicating laterally to all

important sides. A KAM with evolved structures can react more quickly and flexibly to changed market needs, because changes are announced more quickly and disseminated throughout the organization, and the KAM team can ultimately react more quickly (Jones et al. 2005).

Collaborative leadership and evolved structures should be supplemented with **decentralized strategic planning**. Although strategic planning is generally considered difficult in turbulent environments, Mintzberg (1994) claims that decentralized planning is better suited to mid-term planning in environments without major turbulence (Mintzberg 1994). So ongoing planning should take place decentralized in the KAM teams. The KAM team is generally closest to the market situation and can react the fastest. But it should also be responsible within the organization for planning in regard to the respective key account. Such responsibility also promotes the KAM team's esprit de corps and its willingness to change (Jones et al. 2005).

Organizational Rules and Procedures

Organizational rules and procedures are essential, modifiable management parameters and serve to regulate the activities of employees, departments, subsidiaries or whole parts of the corporation (Jones et al. 2005, and in the following, the publications quoted there). These can include certain uniform communication routines, a uniform external appearance of members of the corporation or a code of conduct that clearly defines behavior in certain situations. One purpose of rules and procedures is to simplify cooperation beyond certain borders (e.g. between departments, between subsidiaries, towards the customer). Rules and procedures can be more standardized when a company's surroundings are quieter and more certain; they have to be more flexible in uncertain, quickly evolving surroundings. Since KAM teams care for single customers with individual requirements, they have to be granted certain flexibility in regard to rules and procedures.

The most important management parameters in regard to KAM teams include

- Amount and structure of compensation, whereby the type of variable remuneration is significant
- Mechanisms to reward and recognize employee efforts
- Training and further education
- Allocation of time and monetary resources and
- The duration of membership in a KAM team (Jones et al. 2005).

The variable portion of compensation as well as other reward and recognition mechanisms are intended to increase employee motivation in a way that causes the employee to try even harder to reach goals (Fließ 2006). Improved achievement of objectives could be reflected in greater customer satisfaction, higher revenue, lower transaction costs, a higher customer contribution margin or achieving certain functional-technical goals. Achievement of objectives can be a factor of certain desirable behaviors.

Incentives and rewards can be linked either to reaching certain goals or to a certain behavior (Krafft 1999). When deciding whether to base the **incentive systems** on achieving an objective or on behavior, the degree to which the respective employee or KAM team can influence the goal should be a criterion for consideration. The more achieving an objective (e.g. increasing customer satisfaction or the customer contribution margin, etc.) depends on other people or departments, the more important it is that the incentive system contains behavior-based components. If an incentive system based on reaching an objective is possible, the choice of target parameters is crucial: although increasing sales to a customer (as a value that is easy to measure) is still often set as the goal for a key account manager, economic factors favor the use of a customer contribution margin or CLV as the target value (Chap. 4). This is the only way to reconcile the employee's incentives and the company's goals. It is also advantageous to use "soft factors" such as customer satisfaction as performance indicators in reward systems. These early indicators can point out potential problems that would not show up until later as lower customer contribution margins, were they not remedied promptly. IBM, for example, uses customer satisfaction as an indicator for bonuses (Dwyer and Tanner 2009).

In modern reward systems, components based on behavior and on achieving objectives are balanced and are implemented in a balanced score card with the appropriate controlling systems (Homburg and Krohmer 2009). We will not get into a detailed discussion of incentive and motivation systems here (for more information, refer e.g. to Fließ 2006). Instead the special features of incentive systems as they relate to KAM teams will be examined.

Conventional incentive systems can be problematic for KAM teams when the different members of the team are pursuing separate, individual goals. Members of a KAM team are often also linked to a functional organization (e.g. R&D, production, engineering, quality management) and can have conflicting objectives because of the other responsibilities. So one suggestion originating from organizational research is to no longer define goals and create incentives for single persons but to do so at the team level (Gomez-Mejia and Balkin 1991; Jones et al. 2005). If it is not possible to do this monetarily, non-monetary rewards such as team dinners or events are effective ways to maintain team motivation.

After incentive systems, properly **training** KAM teams is the next most important aspect to the teams' success. Henke et al. (1993) observed that the members of cross-functional teams are often selected well, but they then receive little or no training to improve the team's work. KAM teams should regularly participate in training and coaching measures. Among other benefits, they will learn to better understand the specific skills of the other team members, their roles and the team processes and goals (Jones et al. 2005).

Adequate **time and resource allocation** is amongst the essential management parameters for a successful KAM team. It is particularly important for part-time members of the KAM team that their membership in a KAM team and the inherent time factor be specified in their job description. Otherwise these team members may end up with additional work/responsibilities due to ambiguous jurisdiction. It goes

without saying that a KAM team should be equipped with the necessary financial resources.

In regard to the **duration of membership in a KAM team**, Jones et al. (2005) argue that, on the one hand, continuity is important to the customer; but on the other hand, working too long in a team with the same composition poses a risk that the team's performance will deteriorate. This is caused by declining creativity and communication. So they advocate changing the makeup of KAM teams at regular intervals.

8.3.2.2 Success Factors Specific to a Team

While the success determinants of KAM teams examined thus far are located at the level of the overall organization, the next two sections will deal with two important aspects at the team level. In keeping with the classification of Helfert and Gemünden (2005) as well as Arnett and Badrinarayanan (2005) we will differentiate between team composition and team processes.

Team Composition

When putting together a KAM team, quantitative as well as qualitative aspects should be taken into consideration. In regard to the **size of the KAM team**, Helfert and Gemünden (2005) say: as large as necessary and as small as possible. If the team is too small, it cannot meet the wide range of customer demands over the long term and will miss opportunities to expand the relationship. If the team is too big though, the amount of coordination required increases disproportionately and the dedication of the individual members falls.

In regard to the qualitative aspects of the team composition, Helfert and Gemünden (2005) differentiate between certain technical/functional and social competencies that must be covered by a KAM team.

The **technical competencies** include:

- Technical skills:
The KAM team must be able to tell the customers about the precise performance specifications of the offer and, when necessary, to provide training; to understand the customer's technical requirements; and to initiate the proper adaptations to meet the customer's needs. In close partnerships, this includes understanding the customer's research and development process, production and quality management. Depending on the type of customer relationship, a KAM team may need several members to cover the full range of technical skills required.
- Legal skills to compose contractual regulations
- Networking skills to be able to utilize relationships with third parties to benefit the business relationship (Sect. 5.5.2).
- Knowledge gained from experience with other business relationships.

The study by Homburg et al. (2002) revealed that companies employing such cross-functional teams had the most successful KAM. There is a correlation

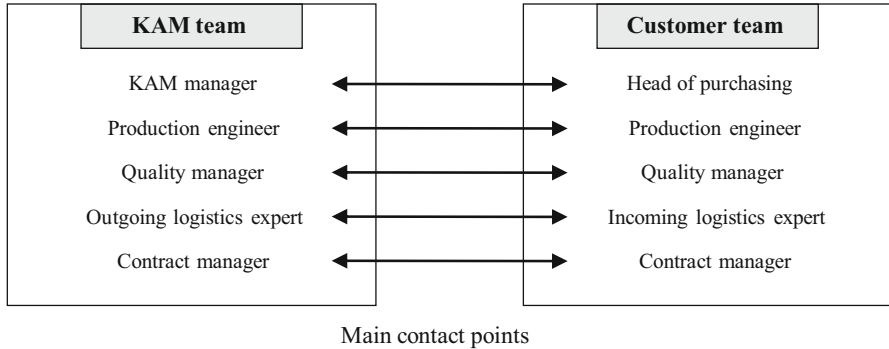


Fig. 8.4 Matching KAM team. Source: Based on Arnett and Badrinarayanan (2005)

between cross-functional population of a KAM team and, among other factors, quicker learning and better coordination (Arnett and Badrinarayanan 2005).

The **social competencies** include the qualities described in Sect. 8.2.1 (empathy, communication skills, adaptability, capacity for teamwork, assertiveness), as well as a sense of justice and the capacity for cooperation (Helfert and Gemünden 2005) and the ability to practice collaborative leadership: “As products become more complex, firms’ use of cross-functional teams means that salespeople must stay on top of multiple learning curves and must exercise inclusive leadership skills while keeping their teams’ focus on customer needs and wants” (Jackson et al. 2010, p. 402).

Arnett and Badrinarayanan (2005) point out another essential aspect in regard to the qualitative composition. When possible, the KAM should **match the customer’s team**. Since intensive business relationships hinge upon regular and intensive sharing of information, technology, related services and ideas between various employees, the exchange should take place through the interfaces best suited to this purpose. For example, engineers from the two companies can deal with design topics, while the logistics experts handle transport and storage aspects. When the KAM team is matching the customer team, it is helpful to observe the respective hierarchies and decision making authority in both companies. Figure 8.4 illustrates a matching KAM team.

Team Processes

Team processes are phenomena that occur as a result of the interaction within the team. They can inspire or impede the team’s success. Team standards, team objectives, team cohesion and team communication have emerged as particularly important (Helfert and Gemünden 2005).

Team standards are a team’s common beliefs on proper behavior, attitudes and perceptions in regard to things important to the team. Important aspects to KAM teams are particularly consensus regarding role allocation (Deeter-Schmelz and Ramsey 1995), interpretation of information and its significance to the business as

well the way in which strategy is implemented (Jones et al. 2005). Agreement on common approaches to certain tasks as well as tolerance for different learning orientations and styles are also mentioned. Constructive behavior in the event of conflict within the team is especially important (Dixon et al. 2002). Helfert and Gemünden (2005) postulate that both the absolute manifestation of a standard and the strict compliance with the standard by the entire team can positively impact team effectiveness.

Team objectives describe a desirable future state of reality in regard to the KAM team's activities, thus defining the purpose of team cooperation (Helfert and Gemünden 2005). This is why it is important that the team members have the same goals and pursue a common mission (Jones et al. 2005). Specifically, it must be ensured that corporate processes and incentive systems do not lead to conflicting objectives for the individual members (Sect. 8.3.2.1). To achieve the greatest team effectiveness, the team objectives should be clear, challenging, specific and, when possible, measurable. Such team goals have a motivating, coordinating function and they reduce conflict; they also contribute to better task performance by the team (Helfert and Gemünden 2005).

Team cohesion in a KAM team is the commitment of the team members to the group and its tasks (Smith and Barclay 1993). Particularly when strongly interdependent tasks are worked on in the team, which is often the case with KAM teams, team cohesion seems to have a strong positive impact on team effectiveness (Gully et al. 1995) Team cohesion can be of a social nature or be a factor of the task (Chang and Bordia 2001). While social cohesion is a result of the team members' personality traits, task-based cohesion is evoked by pursuing common goals and working on joint tasks. Various empirical studies have shown that team cohesion based on tasks has a stronger impact on team effectiveness than does social (Helfert and Gemünden 2005).

Another essential team process is **team communication** within KAM teams. Regular sharing of information within the team as well as into and out of the team (e.g. sharing with other units in one's own company, with the customer's company, with individual employees of the customer's company or with the corporate environment) is a *conditio sine qua non* to achieving the KAM objectives. Figure 8.5 shows the KAM team's most important communication relationships. The small circles represent individual members of the team. When the quality of communication is high, team members actively share information e.g. on changes in the corporate environment or changes related to the customer. They also demand feedback, request support and discuss any mistakes they may have made (Jones et al. 2005). Consensus is reached more quickly when team meetings are held frequently (Ahearne et al. 2010). Helfert and Gemünden (2005) sum up these aspects under the term communication intensity and continue to discuss different communication patterns that are better or worse for the effectiveness of KAM teams. It emerged that decentralized communication is better than central communication: the team members should communicate directly with the respective dialog partners and not with one or multiple central person(s).

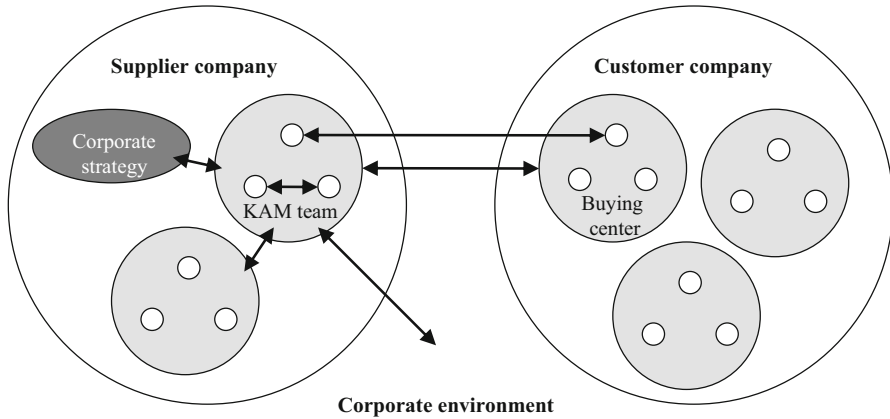


Fig. 8.5 Essential communication relationships of the KAM team. Source: Based on Jones et al. (2005)

8.3.3 Effects of Successful KAM Teams

Introduction of KAM teams is of course linked to certain goals regarding effectiveness and efficiency of relationship management towards the customer. When both organizational and team-specific success factors are present, the following effects can be expected at the team and organization level.

8.3.3.1 Effects at the Team Level

Both team effects and customer-specific effects can be observed in successful KAM teams.

Effects commonly mentioned include greater trust amongst KAM team members, stronger commitment to the team and company, higher satisfaction and greater self-esteem of the individual team members (Perry et al. 1999). Group cohesion also increases over time in successful teams. Another observation of the effects at the team level is that they are reinforced by team processes that progress positively and can be negative when processes progress negatively (Dixon et al. 2002). The behavior of individual team members is positively impacted when the success factors mentioned above are given: The degree of effort expended, the quality and quantity of communication and task coordination, productivity and the performance of certain tasks all improve, while absences decrease (Perry et al. 1999). And such KAM teams are perceived by managers as being more effective.

These positive repercussions in the KAM team are also reflected in the customer. When KAM teams are successful, the degree of cooperation with the customer often rises (Arnett et al. 2005), so the business relationship intensifies. This is accompanied by greater customer satisfaction and better assessment of the quality of the business relationship by the customer (Perry et al. 1999). And the customer's commitment to the business relationship strengthens in this context.

8.3.3.2 Effects at the Corporate Level

Although effects at the KAM team level are relatively easy to capture and serve as a good indication of the effectiveness of a KAM team, the ultimate purpose of establishing KAM teams is to grant the supplier company an economic benefit. So KAM teams must give the company a measurable advantage. At the corporate level, KAM teams promise higher revenue and profit, stronger customer loyalty and better customer acquisition (Perry et al. 1999). Ultimately, the effects at the corporate level are that the value of the business relationship for the supplier company increases and with it the customer lifetime value (Arnett et al. 2005). Nowadays tracing the revenue and sales rates attributed to the KAM team is a common way to check the effects of KAM team employment at the corporate level (Jackson et al. 2010).

Despite all the hopes associated with KAM teams, it happens much too frequently that the anticipated effects at the corporate level are not achieved, as Lambe et al. (2009) report, citing various practical, empirical studies. To actually achieve the desired effects, adequate attention has to be given to KAM team management and particularly to the organizational and team-specific requirements.

8.4 Control and Supervision of Business Relationship Management

Sections 8.1–8.3 of this chapter have focused primarily on planning aspects related to the internal implementation of business relationship management. For example, the following questions were answered: how should business relationship management be organized? Which people are needed for business relationship management and which working conditions should these people expect? The information conveyed in these sections form the foundation for successful implementation of business relationship management.

The time aspect of business relationship management was only slightly touched upon though. Business relationships change, some end and new ones are established. Mistakes are made, and companies learn from good examples. So the view of implementation of business relationship management must also have a dynamic component. This final section of Chap. 7 is intended to provide the dynamic perspective, whereby reference will be made to concepts introduced in other parts of this book.

Figure 8.6 shows business relationship management as a control loop that clearly illustrates the dynamic aspects mentioned. In engineering applications, the goal of such a loop is to keep a technical process (controlled system) stable enough that the desired control variable is optimized over the time period in question. Different stabilizers are used to compensate for changes to the control variable caused by disturbances.

In business relationship management, the market process in the customer's company represents the controlled system affected by different disturbances and for which the output is to be optimized over time. Possible control variables can be

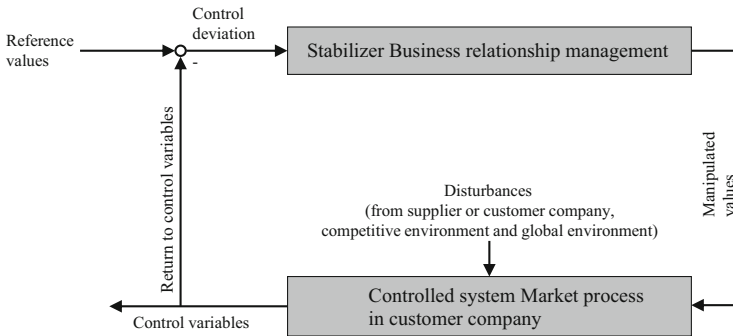


Fig. 8.6 Business relationship management as a loop. Source: Based on Plinke (2000)

e.g. customer satisfaction, the supplier share of customer deliveries (share of wallet), the customer contribution margin or the customer value (Chap. 4). To optimize these variables using the stabilizer business relationship management, they must first be specified as goals of business relationship management and thus reference values. This may seem obvious at first glance. At second glance, however, problems become apparent. These are the result of conflicts between the objectives, such as between revenue and contribution margin in a business relationship. We will look more closely at the reference values in Sect. 8.4.1.

Chapters 5, 6 and 8 of this book provide information on how business relationship management can act as a stabilizer and thus generate the required manipulated value. When the proper decisions are made and implemented, business relationship management is capable of correcting a potential control deviation at a certain point in time t_0 .

Disturbances can be any developments in the supplier, customer or competitor company as well as factors from the global political, social, economic and technological environment. These disturbances affect development of the business relationship with the customer company between the times t_0 and t_1 , often causing the control variables at time t_1 to take on a different value than the supplier company wanted at time t_0 . Even if the following point seems as trivial as paying special attention to the reference values, it is extremely significant: as a return to the control variables. Business relationship management may intervene and act (only at the time t_1) when the goals and results diverge (reference and control variable) only when the results of actions part of business relationship management (regulator that produces the manipulated value) and the subsequent behavior of the controlled system, including its reactions to the potential disturbances, can be attributed to coordination with the goals of business relationship management, meaning that business relationship management is constantly monitored. When monitoring occurs in the course of business relationship management, the various control parameters, changing at varying speeds, as well as their interrelation should be examined. Section 8.4.2 is dedicated to monitoring of business relationship management.

8.4.1 Controlling Business Relationship Management

Since business relationship management is a form of market cultivation and not a goal in itself, the question should be posed as to which control parameters should be applied to leadership of a company. While the purest form of the shareholder value approach focuses on the one-dimensional overall objective of increasing the corporate value, the stakeholder value approach emphasizes long-term viability of the company and keeps in mind the interests of all stakeholders. The marketing perspective interprets the essence of both approaches to mean that marketing activities should be geared towards generating the highest possible customer value (in the sense of a customer's value to the supplier company) for all customers, which then leads to a higher corporate value (Wiesel et al. 2008). The customer lifetime value (CLV) of every customer should be optimized for this purpose. This top-down perspective requires that the business relationship management control parameters be aligned with the company's economic goals.

Economic parameters (CLV, contribution margins, costs), however, are often located at the end of the chain of action in which the most varied events can have occurred and have led to these variables being as pronounced as observed. Because it is downstream in regard to time, controlling business relationship management solely with economic parameters is not appropriate. **Perception and behavior parameters**, such as customer satisfaction or the activity level with the customer, should rather be used as control parameters as well. These parameters are much closer to the actual business activities and can thus be influenced more directly. So it is beneficial to apply a mixture of control variables that meet different requirements. This can occur e.g. in the form of a balanced scorecard (BSC) (Homburg and Krohmer 2009).

When taken all together, they should meet the following—not always consistent—criteria:

- Geared towards the corporate goals: aligning the control parameters to the corporate goals (corporate value, profit, capacity, etc.) sets the direction for business relationship management.
- Proximity to cause and potential to exert influence: control parameters can be influenced only when parameters are selected that can be allocated to certain business actions, allowing any undesirable developments to be corrected.
- Relevance to future: although the actual control parameters are values from the present and the past, the control parameters used should be effectively measurable and thus relevant to the future. This is the only way to ensure that they can be influenced and business relationship management can specify developments instead of chasing after them.
- Compatibility of incentives: if certain incentives are linked to the control parameters of business relationship management, e.g. if bonuses paid to the key account manager depend on them, the control parameters should be compatible with the corporate goals to avoid setting individual misguided incentives.

- **Unequivocal and sturdy measurement:** to ensure that nominal values and actual values can be compared and to facilitate comparisons over time, the type of measurement must be precisely specified. And the extent to which measurement can be influenced should be revealed to prevent any potential conflicts of interest.
- **Measurement requiring little effort:** a control and monitoring system generates costs on its own. To keep these costs to a minimum, the control parameters implemented in the system should be able to be measured at the lowest cost possible.

The following section will introduce essential economic control parameters as well as control parameters based on behavior and perception. An overview of the different control parameters selected and their tendency to fulfill the above criteria can be seen in Table 8.2.

In addition to selecting control parameters suitable for business relationship management, specifying the target values (nominal values) in regard to the parameters is a requirement of systematic controlling. The degree of the goals as well as the time in which the goals are to be met should be precisely specified. And the person(s) responsible for meeting the goals should be clearly stated.

8.4.1.1 Economic Control Parameters

We already learned about the **customer lifetime value** (CLV) as a control parameter in Chap. 4. It is based on a future-oriented assessment of each business relationship, which takes into consideration the directly anticipated and discounted cash flow of a certain customer as well as—depending on the model applied—positive and negative economies of scope, such as the future reference and information value of a customer. If a company in a business relationship generates a high CLV, this is an indication of a pronounced competitive advantage. A positive aspect of CLV is that it is a control parameter that is based on the company's comprehensive, future goals. However, it is difficult to measure, in regard to both the structure of the measuring instruments (e.g. setting the period to be examined and the interest rate) and measurement or estimation of individual variables (cash flow forecasts, value of references and information, customer-specific costs). Values calculated in this way are much less reliable than other performance indicators. The CLV is susceptible to being consciously “cosmetically recalculated.” Despite its theoretic advantages, the CLV is suitable for controlling business relationship management only in companies capable of dealing with the difficulties mentioned.

A more manageable control parameter at the financial level is the **customer-specific contribution margin** (Chap. 4). Measurement of the current customer-specific contribution margin is based on the past and can reveal changes in the business relationship only well after their occurrence, but it is also geared towards the corporate goals. It is more difficult to measure than the **customer-specific revenue**, because **customer-specific costs** have to be determined for the calculation. Determining the costs that can be attributed to a single customer is often difficult, because especially sales and customer care costs are often recorded as

Table 8.2 Selected control parameters of business relationship management

	Criteria							
	Control parameters	Geared towards the corporate goals	Proximity to cause/potential to exert influence	Relevance to future:	Compatibility of incentives	Unequivocal/sturdy measurement	Measurement requiring little effort	
Economic parameters	Customer lifetime value	+++	--	+++	++	---	---	
	Customer-specific contribution margin	++	0	0	++	0	0	
	Customer-specific revenue	+	0	0	-	+++	++	
	Customer-specific costs	+	0	0	0	0	0	
Perception and behavior parameters	Share of wallet	+	0	+	0	+	0	
	Customer's payment behavior	+	0	+	0	+++	+	
	Own supply performance	+	+++	+	++	+	0	
	Number and type of customer contacts	+	+++	+	++	+	0	
	Number and type of projects with customer	+	++	+	++	0	0	
	Customer satisfaction	+	++	+	+	+	+	-

overhead. In contrast, customer-specific revenue can be clearly measured without substantial effort, so many companies apply this method despite the associated problems of setting incentives as a control parameter. In comparison to the CLV, the variables contribution margin, revenue and costs are much easier to implement in a conventional cost accounting system and are more resistant to factors that influence measurement. But, because they are based on the past, these variables cannot be used to reflect e.g. investments in a customer that are considered costs for accounting purposes. The economic variables discussed in Chap. 4 can of course also be used in addition to these control parameters.

8.4.1.2 Control Parameters Based on Behavior and Perception

While the economic control parameters indicate the financial results or the projection of results of the actual business cooperation, control parameters based on behavior and perception assess the cooperation itself. So they are highly susceptible to influence and can usually be measured pretty explicitly. From the customer's point of view, the **supplier share of wallet** can serve as a global indicator of the significance of a business relationship. As a control parameter, this value is particularly interesting in regard to the development over time: if the supplier share of wallet falls repeatedly, this can be taken as a clear indication that one no longer has a competitive advantage with this customer and efforts should be made to gain an advantage again. But since measuring the supplier share of wallet requires information on the customer's other supply relationships, which may need to be estimated, it is not an easy value to measure. **Payment behavior** is another indicator for a business relationship's future potential (Hermes 2011) and can be applied as an early warning signal. It is easy to measure by comparing the terms of payment and actual receipt of payment.

In regard to one's own performance in the business relationship, it is beneficial to compare actual to agreed **supply performance**. Depending on the type of business, factors such as adherence to schedules, quality assurance results of customer's inspection of incoming goods or the number of complaints can be used as indicators. These variables are amongst those that can be most easily influenced, making them particularly relevant for ongoing monitoring of the business relationship. Also, they can be unequivocally measured with little effort, as long as the indicators required are clearly defined such that they can also be used in incentive systems.

When a CRM system or sales information system is used, **types and quantity of customer contacts** can also be kept track of. Essential information that can be gained includes e.g. which of the supplier's employees talked to which of the customer's employees, and what they talked about when. Special attention should be paid to customer complaints and the notation on how they were treated (Homberg and Fürst 2005).

Apart from daily business, the **types and quantity of projects with the customer** play a significant role. Projects often serve to intensify the business relationship and to create additional value for both sides. They promote the future security of the business relationship and can be defined as goals for individual employees or

the entire KAM team, and they can generate incentive. But since each case is different, measuring this value can be problematic.

The last—yet very important—indicator for controlling a business relationship is **customer satisfaction**. It represents a global quality indicator for the business relationship and offers a comparison between expectations and perception of the business relationship (Chap. 3). To be able to use this as a reliable control parameter, it is essential to first determine how the data is collected and who is surveyed. To avoid replies biased by social desirability, customer satisfaction surveys should be conducted by third parties. So measuring this variable always incurs costs.

8.4.2 Monitoring Business Relationship Management

These **target/performance comparisons** based on the past should not be limited to comparison. The respective controlling bodies (e.g. KAM team) should rather attempt to discover related contents and reasons for why the control parameters developed in the way they did. The reasons may be found in one's own company or the customer's company, or related to the competition or the environment. Corrective measures can be introduced and implemented only when the causes of a certain development of the control parameters are revealed. When investigating the reasons for certain manifestations, it is worthwhile to use control parameters that are not equidistant from daily operation and to survey the parameters at different intervals: for example, an increase in the number of customer complaints can serve as an indication that the next survey will show a decrease in customer satisfaction if countermeasures are not immediately implemented. Customer satisfaction is often a preliminary indicator for the development of customer value, which may be expressed in a greater willingness to pay (Homburg et al. 2005) and ultimately higher profitability for the supplier company (Anderson et al. 1994).

In addition to comparing target and performance values—which are based on the past—**monitoring** business relationship management also includes anticipating future developments and adapting business relationship management to accommodate them (Steinmann and Schreyögg 2005). It is beneficial to monitor at regular intervals and to apply elements of **strategic foresight**. Quantitative as well as qualitative information should be used, such as long-term market/industry developments that may arise from changes in the technological environment. Scenario analyses are especially useful when there has been substantial upheaval in the corporate environment (Cornelius et al. 2005). Dwyer and Tanner (2009) suggest conducting an annual marketing audit for monitoring purposes. In the course of such an audit, the values determined for business relationship management control should be analyzed in regard to their time sequence as well, because some developments and correlations are not revealed when only a point in time is examined.

Exercises

1. State reasons in favor of introducing key account management in a company as an organizational form.
2. Explain the term “part-time relationship management.” Which criteria speak for and which against the fundamental organizational option key account management?
3. Weigh the pros and cons of introducing “part-time relationship management” and “full-time relationship management.” Which criteria would you examine in designing the constellation?
4. Which subdivisions of “full-time relationship management” are you familiar with?
5. What is the correlation between key account management and the formation of “strategic business units”? Explain potential conflicts.
6. When does it make sense to set up key account management as a staff unit?
7. When does it make sense to set up key account management as a management board division?
8. Which conditions support establishment of key account management as corporate divisions?
9. Explain how the complexity of the business relationship affects how business relationship management is designed.
10. Explain why, when business relationship management is successful, greater demands are placed on the key account manager than on a common sales employee.
11. Which determinants of successful employment of key account management teams at the organizational level are you familiar with?
12. Which team-specific success factors should be kept in mind when employing key account management teams?
13. Why should control of business relationship management not be based solely on economic variables? Which other control variables may make sense?
14. Which criteria should business relationship management control parameters fulfill? Explain them.
15. Which future-oriented ways to monitor business relationship management are you familiar with? Compare them to those based on the past.

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Martin Gersch

9.1 CRM: Terms and Fundamentals

9.1.1 Object of CRM

The term customer relationship management (CRM) emphasizes the use of Information Technology (IT) for targeted analysis, planning and makeup of business relationships with individual purchasers/customers (business relationship management). CRM is a management concept as well as a technological concept that utilizes application systems to support business processes for business relationship management (Laudon et al. 2010; Leußer et al. 2011).

As part of comprehensive development, the economic expectations in regard to usefulness of available microdata (Kroenke 2013; Shapiro and Varian 1998; Zerdick et al. 2001), are changing as a result of the information technological (r) evolution and digital convergence taking place for years now, particularly in regard to the ability to compile, evaluate and link data as well as use it commercially. In this sense, CRM is a specification of the approaches on the use of information technology (Mertens 2010) for companies in regard to potential and existing business relationships to individual purchasers/customers.

9.1.1.1 CRM: New IT Conditions for Old Ideas?!

Neither the fundamental ideas of business relationship management nor the concepts and methods that go with it are really new. They have been in use for a long time, sometimes without explicit names and sometimes in conjunction with evolving catchwords (e.g. business relationship management, relationship management, one-to-one marketing) (Bruhn 2007; Gersch 1998; Helmke et al. 2008; Hippner 2006; Sexauer 2002).

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For centuries now economic actors have suspected the different values of customers, observed different behavior in individuals, formed implicit or explicit customer groups and taken these assessments into consideration when designing their strategies and sales policy instruments. It has been possible for a long time as well to apply evaluations of available data with statistical methods to forming groups with similar properties in regard to selected criteria and/or forming and testing assumptions about the effect of strategies and sales policy instruments (**market segmentation**, Freter 2008).

However, the following aspects have changed the basic conditions, requirements and prospects of success of business relationship management so fundamentally that the **CRM euphoria** observed for a while becomes absolutely understandable:

More intensive competition with inherent pressure on the companies induces the companies to keep looking for potential improvement that could lead to competitive advantages. It was no later than the studies of the 1990s (Peppers and Rogers 1997; Reichheld and Sasser 1990; Reichheld 1993) that revealed the different meaning of customers, in regard to costs as well as to revenue, and explained a greater awareness in science and in practice in regard to differentiated analysis, planning and control of the relationship to individual customers using terms such as “**relationship management**” and “**business relationship management**.”

Dramatically fast-paced developments in information technology beginning the 1990s (Laudon et al. 2010) as well as particularly the use of the internet beginning in 1995 in conjunction with terms such as “electronic business” and “electronic commerce” (Gersch 2010) changed the basic conditions and possibilities of business relationship management in many ways. Examples of changes or completely new potentials that promoted greater attention to **customer relationship management** (CRM) include:

- Digitalization and cross-linkage of service creation, transaction and administrative processes with respective differentiation of data availability. The explosive growth in the use of online media (Infratest 2009; Laudon and Kraver 2010) along value-chains (Gersch 2010) as well as between individuals (employees and/or consumers: web 2.0; social networks) are relevant here.
- Increasing the availability of better technical ways to store and process mass data (explosion in performance) along with continuously falling costs for storage, evaluation and transmission of data (Weiber 2002).
- Availability of integrated CRM software systems, acting as “technological enablers” to open new ways to manage customer relationships (Leußer et al. 2011).
- Continued development of concepts for systematic and targeted use of evolving IT capacities as the framework of business relationship management, particularly for individual collection, analysis and use of data related to single customers. In combination with concepts that increase flexibility, such as modular design and “mass customization” (Pine 1993; Piller 1998, 2001), the prerequisites for customizing the offering at a cost comparable to mass production emerged successively.

9.1.1.2 Examples of Successful CRM Applications

The impressive economic success of customer relationship management can be seen in the developments of the companies stated here as examples. Some of them use other catchwords to describe their strategies, but they all base their strategies strongly on the elements of CRM described here. At the same time, it becomes apparent that the approaches can be very different. This will be discussed in this section as well:

Satisloh AG Guidance and support for sales reps of a typical machinery and equipment manufacturer using a mobile sales information system, not only facilitating more efficient preparation and reviewing of customer visits but also serving as aids for sales talks with IT-supported product configurators. Offers are put together to meet the customer's needs during consultations. The strategic goals of the supplier's business relationship management are taken into consideration, e.g. in regard to individual goals with the customer or special conditions (Weidner 2007).

Audi AG CRM as a component of decided campaign management in which e.g. customers considered relevant and attractive are targeted for involvement when a new vehicle is introduced. Selected customers are invited to special events before the vehicle is launched and are kept updated throughout the course of the campaign. CRM includes not only supplier measures, it also coordinates corresponding dealer activities.

Last.fm Internet radio services such as Last.fm and, as bandwidth increases, other internet-based media offerings (like tape.tv or Putpat), especially for movies, take advantage of forming "affinity groups." Based on the music, clip and/or movie preferences they have demonstrated as well on their observed digital behavior, customers are assigned to groups of persons with similar traits. This information can be used very successfully e.g. to customize the core offering and utilize "cross-selling" or "up-selling" potentials, and it can be used for targeted communication policy and use of data by third parties. The following explanations will expand on this.

Amazon Largest E-commerce company in the world (by revenue). The company expanded its original assortment of books and media long ago and now offers a nearly complete range of products through mail-order (incl. furniture, fashion and food). It also has marketplace and community functionalities. Recommendations from other customers based on their past purchases (e.g. verbal recommendations "Customers who bought this item also bought. . ." or star ratings and comment/blog functionalities) are particularly well known. This is only the use of customer data that is perceived by the customers. Amazon actually applies a broad range of the CRM potentials described here.

Otto Rapid growth to become second-largest E-commerce company in the world (by revenue). The company took central approaches formerly used in traditional business models and consistently adapted them to new technologies. These approaches include the analysis of multi-channel customers who are especially economically attractive as well as the formation of customer affinity groups on the basis of behavior data—generated from various online and offline contact channels—relevant to purchasing and used in an appropriate combination.

Google, Facebook & Co Wide-ranging collection and subsequent linking of differentiated personal master data and usage data on the most varied applications and services. This forms the foundation for differentiated user profiles. One use for these profiles is e.g. to offer services tailored to an individual's needs via the platforms and, as a non-monetary service in return, to generate microdata on the persons. The user profiles can also form the basis for targeted offerings to third parties. As Eric Schmidt, CEO of Google stated: *"We know more or less who you are, what you are interested in and who your friends are"* Unknown (2010)

To examine the focus of this contribution, the **capital goods sector**, the possibilities that CRM offers will be explained using primarily German pharmaceutical wholesalers as an example. This industry has been using the information gained from its central position in the value chain for decades to target its business relationships with pharmacies. It is important to point out that its core service (supplying the common assortment to pharmacies, particularly prescription medications (Rx)) cannot be digitalized.

9.1.2 Subtasks of CRM

Publications on customer relationship management commonly subdivide the topic to operative, analytical, strategic and communicative CRM (as examples for others: (Hilbert 2009; Hippner and Wilde 2008; Hippner 2010; Laudon et al. 2010; Leußer et al. 2011; Rentzmann et al. 2011)). Figure 9.1 provides a systematic overview and shows the relationships between the subtasks of CRM.

9.1.2.1 Operative Customer Relationship Management

Operative customer relationship management (oCRM) includes all of the operative support services required to perform business processes related to business relationship management of a company. These include particularly the following aspects:

- **Linkage and coordination of all corporate divisions with customer contact:** Operative CRM is comprised of all areas that, as so-called "front office", have direct contact with the customer. This typically includes sales and services, whose activities are in turn usually supported by their own specialized application systems (e.g. sales or service information systems). In addition to the

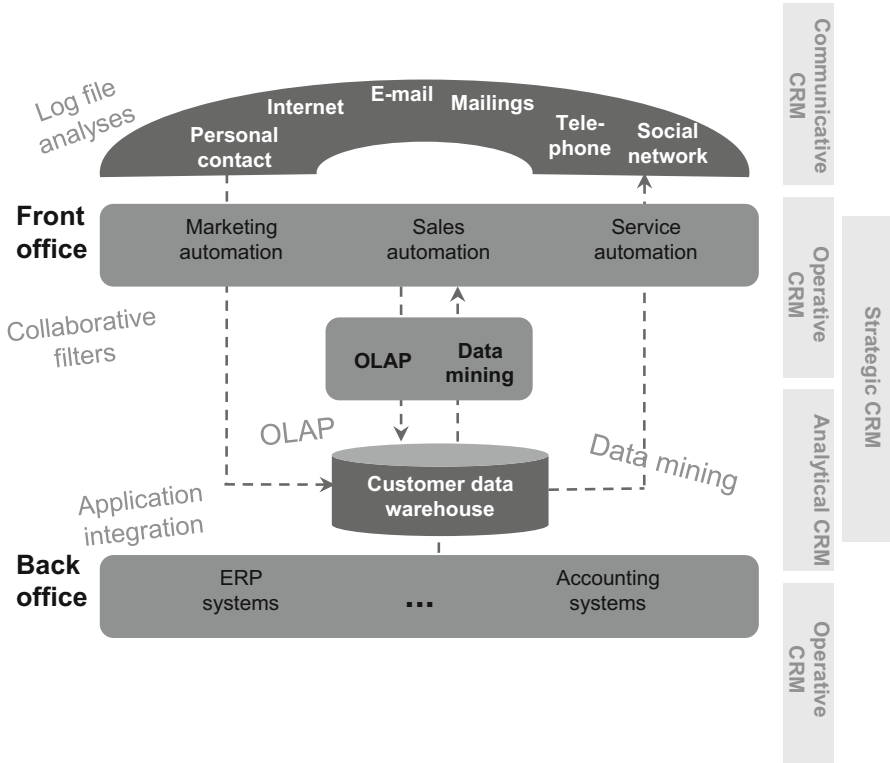


Fig. 9.1 Subtasks of customer relationship management. Source: Based on Hippner and Wilde (2008)

customer-related data generated from the operative business, relevant customer-related data is usually considered from all of the other direct channels to the customer (so-called “touch points”). It is already apparent that such customer contacts generally occur through a wide variety of media, only some of which are available as digitalized data and capable of integrated application systems.

• **Integration of customer-related data in a customer data warehouse:**

In most CRM application concepts, a so-called customer data warehouse takes over the central technical functions of mining, aggregating and providing the data on the individual customers gained from the various business processes and corporate divisions (Becker and Knackstedet 2011). A data warehouse is a corporate-wide concept. It is a logically central storage space that provides a uniform and consistent data base to help specialists and managers from all relevant divisions and levels in decision making. This data pool is stored and managed separately from the operative databases (Gabriel et al. 2009). Separating data analysis from the operative systems ensures that daily business is not hindered by the vast processing power required for analysis applications (Hippner et al. 2006). Because of the steep integration challenge (Sect. 9.2.2.1)

and the necessity to overcome technical, syntax, semantic and pragmatic standards between the application subsystems (Gersch 1998), partially redundant data storage usually has to be accepted (Schelp 2010).

- **Coordination of all corporate divisions with customer-related data and linkage to back office application systems:** In addition to the direct customer touch points, there are many other corporate processes in which data on individual customers that may be relevant to business relationship management is generate or used. Some examples: accounting, with data on individual payment behavior and payment references; managers, with their personal contacts to the customer's employees; and/or logistics and production area, with information on availability of goods and current production planning. When a comprehensive CRM approach is applied (Sect. 9.3), these business processes are also tied into the CRM concept. To avoid isolated solutions, the CRM system has to be linked to the company's central back office application as well (Helmke et al. 2008). Depending on the company's IT system architecture, these are usually ERP (enterprise resource planning) systems, production planning and control systems (especially in the manufacturing industry) and/or inventory control systems (retail) (Mertens 2009).

9.1.2.2 Analytical Customer Relationship Management

Analytical customer relationship management (aCRM) uses the data aggregated in oCRM and evaluates them in regard to specific problems and decisions. Ideally, the fundamental ideas of a continuous learning process can be realized with the aid of technical support (Hippner et al. 2006), a process coined "learning relationship" by Peppers and Rogers back in 1997. Because of the rapid technological development described earlier, there has been a dramatic increase since the beginning of this century in the fundamental options of collecting and analytically preparing microdata. Especially "cloud computing" as well as "in-memory" opportunities make technical (not organizational and/or legal!) performance and capacity restrictions virtually obsolete (Laudon et al. 2010).

In addition to the creation of standard reports for specialists and managers in customer relationship management mentioned earlier, "KDD" or "data mining" and "OLAP" applications are used for aCRM to generate information relevant to problem solving and decision making from the data stock of the customer data warehouse.

KDD stands for "**knowledge discovery in databases**" and designates the process required to detect previously unknown and potentially useful correlations in large quantities of data (Düsing 2010). Data mining is often interpreted as a step in comprehensive KDD, which includes the entire process as well the preparation and evaluation of data (Gluchowski et al. 2008). **Data mining** in this interpretation focuses completely on the actual discovery of previously unknown structures and correlations, using selected analysis methods that will be referred to later (Sect. 9.1.1.2).

On-line analytical processing (OLAP) is a software technology based on multi-dimensional data stock, intended to grant specialists and managers quick,

interactive and diverse access to relevant and consistent data (Gabriel et al. 2009). It is usually made up of relevant gages and performance indicators (e.g. sales, revenue, costs, contribution margins, market shares, regions, etc.) that are prepared and presented as a multi-dimensional data cube. Following these dimensions, the gages can—depending on the question/issue—be drilled down or rolled up, diced or sliced (Chamoni 1998; Hippner et al. 2006; Hippner and Wilde 2008). The emphasis is on dynamic and multi-dimensional analyses of historical and consolidated data stocks, which are especially well suited to verifying a priori hypotheses. The user interfaces, operated intuitively, are a particularly useful feature that enables management and technical departments—usually via data warehouse applications—to access various data sources within the company and outside of it. OLAP tools often tempt users to perform ad hoc analyses of specific problems. In contrast to tabular, statistical standard reporting, these analyses facilitate “playful” discoveries, specification and tracing of abnormalities and spontaneous questions (Hippner and Wilde 2008). When experienced users can interactively modify hypotheses with an OLAP system, the available multi-dimensional complexity quickly exceeds the limits of intuitive perception. This manual search for correlations should ideally be supplemented with the systematic discovery of new correlations in the course of data mining.

9.1.2.3 Strategic Customer Relationship Management (sCRM)

Applying the findings gained through aCRM, it is the job of strategic customer relationship management to make fundamental decisions related to business relationship management (Chaps. 4 and 5) and to then monitor its effect over time, making adjustments as necessary. Depending on where sCRM is anchored in the corporation, it can include particularly the following tasks:

- Continuous analysis and, when necessary, moving business relationship management to a different part of the organization (reflection/meta level).
- Formation, analysis, prioritization and selection of customers (or customer groups) deemed relevant.
- Formulation and specification of individual goals for each prioritized business relationship or each differentiated type of business relationship.
- Decision on individual constellation of business relationships and realized offerings, on business processes (Merzenich et al. 2011), on conditions and, when appropriate, on investments in the business relationships that affect multiple transactions.
- Coordination with other areas to create the organizational and technical conditions needed for efficient realization of individual business relationships (e.g. modular strategies or principles of mass customization).
- Decision on performing special actions related to business relationship management. These can include e.g. campaigns to acquire new customers with certain qualities, reactivation of “dormant business relationships” or active reclaiming of lost customers.

9.1.2.4 Communicative Customer Relationship Management

Communicative CRM (cCRM) implements both internal and external communication in business relationship management. With internal communication, it is essential to ensure that not only the data needed is extracted but that all of the decisions made in the course of sCRM can be applied again to all operative implementations. So the persons responsible for performing single tasks must have the proper specifications with regard to the overall customer-related strategy. This means for example that the specifications created e.g. for offerings or price conditions have to be effective for each customer at the customer touch points (e.g. sales reps or call center) as well as in the production plant. When a customer contacts the call center, these individual specifications must be applied just as they are in preparing personal conversations at different levels of the corporate hierarchy or in more or less generously handling a complaint in the service area.

External communication focuses primarily on coordination and agreement of communication of the individuals responsible for tasks and functions related to the customer. Decisions made as part of sCRM must be implemented as coordinated and agreed behavior by those responsible for tasks and functions, ensuring that, from the customer's view point, the supplier's overall communication is coherent and consistent.

Figure 9.2 gives an overview of the complex tasks of customer relationship management.

9.1.3 Goals of CRM

The main objectives of CRM are the utilization of new technical ways to support traditional **subtasks of business relationship management**. These subtasks can be characterized as (Gersch 1998):

- Analysis and selection of suitable business relationship partners (future, current and possibly former partners to be reactivated).
- Specific objectives for each separate business relationship
- Targeted design of each business relationship
- Permanent monitoring and control of the portfolio consisting of all business relationships but also of each individual relationship.

From an economic point of view, customer relationship management and the inherent customization of offerings have no intrinsic value. The central approaches are selective customer loyalty, securing or even increasing revenue, and improving the efficiency of activities required for this purpose (Gersch 1998). A differentiated performance analysis, often attempted with simplified cost-benefit analysis, should serve as a benchmark. This is typically intended to prove that the benefit generated by customer relationship management justifies the incurred costs (Chap. 4. To find out more about the fundamental problems of performance analysis of CRM applications, refer to Sect. 9.2.2.2).

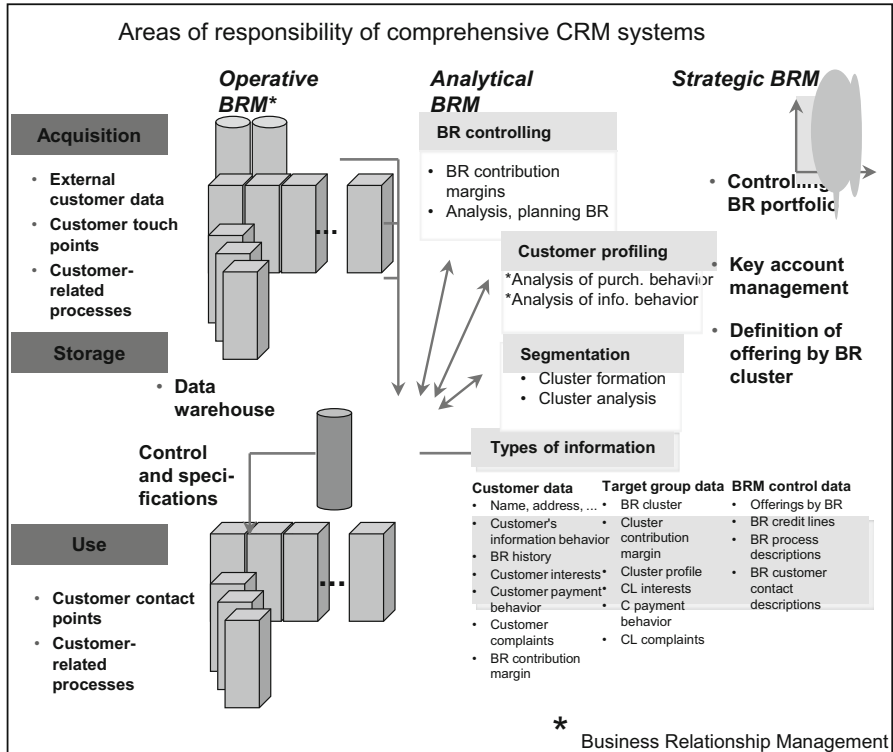


Fig. 9.2 Tasks of customer relationship management

Benefits of CRM are generally considered to be a selective increase in customer loyalty on the part of customers considered to be economically attractive as well as the chance to secure or even increase revenue. The aspects related to revenue are usually assumed to be associated with greater price willingness of the purchaser for customized bundled services, falling price elasticity for the customer over the course of the business relationship and/or an increase in the proportion of the supplier's revenue generated by customer spending (by concentrating the purchaser's procurement within one of the supplier's categories (potential for intensification) as well as by so-called "cross selling" or "up-selling", Hippner 2006; Laudon et al. 2010). If it is not possible to express this information as absolute values (for information on problems of cross-selling/cross-buying analyses, refer to Rese et al. 2008), an attempt is usually made to compare the assumed revenue developments without CRM measures as part of considerations on opportunism. Indirect benefit effects of single purchasers are emphasized as increasing customer value in addition to these direct revenue effects (Günter and Helm 2011; Hippner 2006). Indirect effects include particularly the reference potential, e.g. of opinion leaders in attractive purchaser segments, the information potential of typical customers, including lead users (Hippel 1986; Kleinaltenkamp

and Dahlke 2006), and the potential for cooperation (e.g. access to lacking resources and/or personal networks, Günter 2006).

In regard to the **costs of CRM**, the expense incurred to create the infrastructure required, the additional costs resulting from collection, analysis and evaluation of data, any customization of service creation and the offering are all considered to contribute to increasing costs (for more on overhead and costs attributed to individual customers, refer to Reckenfelderbäumer and Welling 2006). In contrast, CRM also has effects that reduce costs, e.g. more efficient communication processes, less scatter loss or potential outsourcing to regular customers of partial services provided by the supplier.

The information technology developments explained in Sect. 9.1.1 and the resulting changes in the basic conditions and the constellation options lead to the assumption that there are positive effects on both the benefit aspects and cost aspects. It is becoming increasingly interesting economically for more and more companies to investigate the potential uses of customer relationship management for their scope of activities, even in cases in which their former circumstances made it appear the CRM was not a promising course of action for them.

So the generally worded objectives of CRM are becoming a strategic option worth considering for more and more suppliers. The fundamental goals of CRM outlined here—depending on the basic conditions and the strategic direction of CRM—are specified in coordinated **subordinate targets of customer relationship management**. These targets relate e.g. to the following aspects:

- Long-term commitment of profitable customers or establishment and reinforcement of profitable customer relationships. The means to an end here is primarily to secure adequate customer satisfaction of the current and future customers deemed attractive (Hippner 2006, 2010; Hippner and Wilde 2008), the secondary intention being targeted design of additional loyalty factors (e.g. legal, technological or psychological loyalty elements) (Gersch 1998).
- Reclaiming and reinforcing former customer relationships that are assumed to be potentially profitable in the long term (Helmke et al. 2008).
- Typical subordinate goals for individual subtasks of CRM (Sexauer and Wellner 2008):
 - Improvement of customer selection
 - Addressing individual customer requests
 - Rationalization of in-house sales department and sales reps, possibly with simultaneous
 - Focus on and improved coordination of communication and sales activities
 - Effective and more efficient order processing (as well as other sub-processes of customer care and sales activities) by liberation from and/or automation of administrative routines
 - Early detection of potentially attractive new customers or of “dwindling” or “broken off” business relationships.

9.2 CRM at a Crossroads?!

9.2.1 CRM Euphoria and Disenchantment in Practice

Beginning in the mid-1990s customer relationship management became a real fashion trend in both scientific literature (especially in the marketing field and then later in information systems) and in actual practice. In retrospect, it can be labeled downright “CRM euphoria.” It was one of the few IT-related topics that captured the attention of the highest tiers of management.

Actual practical experience, a wealth of reports from corporations and relevant empirical studies all show that a certain disillusionment has begun to set in (Helmke et al. 2008; Schaller et al. 2006; Sexauer and Wellner 2008). Besides the many detailed reports, the following aspects have proven to be primary **sources of this disenchantment**:

- Unrealistic expectations as to the potential benefits, along with inadequate consistency and focus on goals related to planning and realization of CRM implementation suited to the respective company.
- Underestimated complexity of CRM implementations, particularly regarding instating the technical, organizational and HR requirements for an “integrated CRM concept” to be able to achieve the desired effects.
- Difficulty of creating an adequately discriminating performance analysis of CRM plans such that it actually influences the behavior of those responsible for decision making.

Before we talk about CRM scenarios that can realistically be implemented in Sect. 9.3, the following sections will examine these challenges.

9.2.2 (Unrealistic) Expectations Versus Underestimated Prerequisites for CRM

9.2.2.1 Underestimated Prerequisites for Integrated CRM Systems

The initial description of customer relationship management emphasized that it is an “integrated concept” and an “integrated information system” (Laudon et al. 2010; Leußer et al. 2011), which becomes apparent after learning about the subtasks of CRM, particularly aCRM. Integration always has technical implications as well as organizational and HR-related implications that are at least sometimes relevant.

The **technical aspects of integration** can be vastly simplified by differentiating between “connectivity” as a fundamental requirement for linking information systems and different degrees of “compatibility”; together they form the basic prerequisite for potential manifestations of integration (Gabriel et al. 2002; Mertens 2009; Weiber and Zühlke 2005). In very general terms, integration means connecting people, tasks and possibly technology to form a coherent whole, with

Requirements for (inter-organizational) cross-linking and integration

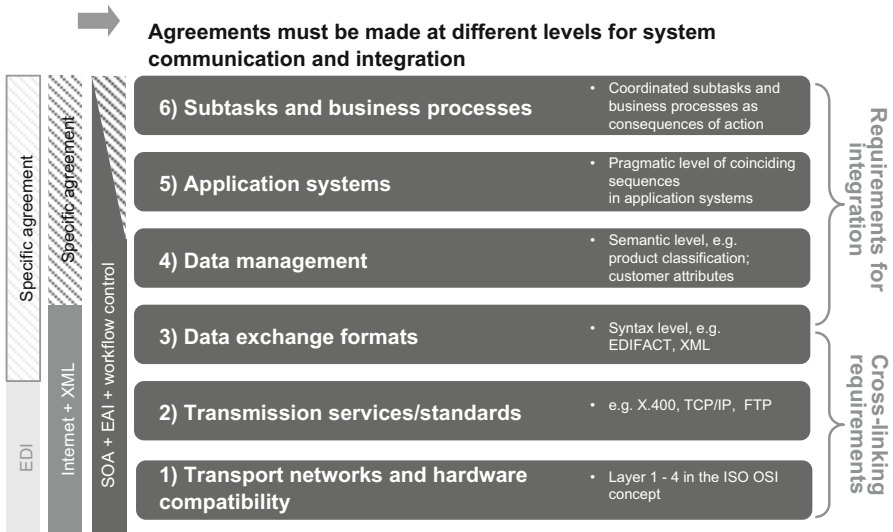


Fig. 9.3 Prerequisite for cross-linking and integration. Source: Based on Gersch (1998) and Weiber and Zühlke (2005)

the intention of combating the functional, process and departmental limitations resulting from division of labor and specialization (Laudon et al. 2010). Mertens (2009) claims that there are several dimensions to integration (based e.g. on the object of integration (data, functions, objects, processes, methods, programs), the direction of integration (vertical, horizontal, lateral) or the extent of integration (division, covering multiple functions or processes, internal or between companies). **Cross-linking** in this case means only the technical, physical link between different members of the organization, organizational units and the respective application systems used, with the objective of working in a coordinated and cooperative manner (e.g. as a network for sharing data). **Integration** is the subsequent coordination and possibly merging of technical systems, processes, structures and tasks between the various members and units of an organization and/or organizations. Beyond the predominantly technical aspects of networks, the syntax, semantics and pragmatic levels of compatibility are essential for integration to actually work (detailed information on integration: Gabriel et al. 2002; Gabriel and Beier 2003; Mertens 2009); for the **syntax, semantics and pragmatic level of compatibility**, especially Gersch (1998) and Fig. 9.3.

- The syntax level of compatibility addresses the physical nature of characters and their identification as data in the semiotic sense. This is usually assured by using formats like HTML, XML or EDIFACT to exchange data.
- The semantic level of compatibility specifies the unequivocal definition of the contents and meanings of characters and messages as the central task of data

management. It is important that terms such as “customer net price” and “customer value” always have exactly the same contents and definitions.

- The pragmatic level of compatibility deals with the coordination of action and reaction patterns as compatible business processes that can be consistently or sporadically supported by IT-based application systems.

When it comes to organizational aspects of integration, the following aspects are typically relevant particularly for operative CRM (similar to Hippner et al. 2006; Hippner 2010; Laudon et al. 2010):

- Multitude of touch points to customers with the need to be synchronized and supported.
- Multitude of contact partners, contact media and interaction channels to the customer to be integrated, usually through several functions, departments and different persons.
- IT-based information systems often only partially support these touch points, accrued customer data and the resulting customer histories.
- When customer contacts and customer-related processes are already supported digitally, it is usually with different information systems that are frequently not linked and are surely not integrated.

Sexauer (2001) was one of the first to focus on the **HR aspects of integration**. All of the technical and organizational measures can only create the conditions to provide an implemented CRM system that serves as a tool for the functionaries and decision makers. The central aspect of success is the acceptance of the CRM implications for the respective tasks and functions, especially when costs and benefits seem to be distributed unevenly amongst the functional areas. Depending on the CRM concept, this can affect not only operative tasks perceived as “pointless extra work” but can also cause detachment from the accustomed goals,—often focused on individual functions or tasks—processes and routines for achieving these goals (e.g. changing incentive payments in sales from “number of new contracts” to differentiated CRM subordinate targets, such as “number of new contracts with customers with certain properties,” “compiling and maintaining customer data also available to other divisions”). So it has proven crucial to success to frame the essential change in behavior with a suitable CRM implementation strategy, consisting e.g. of appropriate training and informational measures, modification of the incentive systems in compliance with clearly defined CRM subordinate goals (as specification of a CRM target pyramid) and clear and concise descriptions of tasks and processes.

To meet the demand for implementation of the fully “integrated CRM information system”—a demand that is easy to put into words but difficult to comprehensively and consistently meet—there are many conceivable solutions, all of which require a wide range of conditions and substantial investments before the CRM idea can be thoroughly put into practice and integrated, whereby it is supported by IT:

- CRM as a function in a central system: implementation of the required CRM functionalities in a central IT system (e.g. ERP or management information system) used by all relevant departments and functionaries.
- CRM as a supplemental module: addition to a company's existing infrastructure—which has usually grown successively and is heterogeneous—initially as an autonomous CRM module, consisting of a customer data warehouse and being integrated into the existing IT landscape via import and export interfaces (overview of 63 CRM software solutions, (Hippner et al. 2009).

As explained in detail in Sect. 9.3, “selective or focused CRM applications” are most common right now. These applications concentrate on (sometimes only at first) selected functions and application systems, not lastly because it has been revealed that the technical and organizational requirements for realizing a comprehensive and integrated CRM system demand investments and modification projects that are nearly impossible to quantify—and even rough estimates are of an amount that is unacceptable in relation to the anticipated benefits. Especially established companies with an IT system and process landscape that has grown over many years and is typically heterogeneous tend to choose the route of focused implementation of a CRM strategy, possibly combining it with a successive migration strategy when replacement investments are required, thus expanding CRM integration step by step.

9.2.2.2 Problems Associated with CRM Performance Analysis

As with all courses of action, customer relationship management and the associated investments are subject to performance analysis. The performance analysis is initially an evaluation/forecast of future effects, and as implementation progresses, it increasingly takes on the character of specific targets and inspection specifications. The special problems of CRM performance analysis are explained here on the basis of the general discussion with respect to information systems (Arens 2004; Gersch 1998; Schumann 1992, 1993; Uebel 2008):

- Multi-dimensionality of goals:
As the discussion of the goals of CRM in Sect. 9.1.3 revealed, CRM approaches typically pursue not just a single goal but several at the same time. It is not at all necessary that the various goals be equally relevant. No performance analysis can ever thoroughly consider all objectives—and surely not when there are multiple objectives with different weighting.
- Gage problems with systemization of economic effects:
One pivotal problem is finding a suitable indicator (or multiple indicators) that enables unequivocal comparison or modification of the efficiency of alternative courses of action and constellation alternatives. Although at first glance it may seem sensible to choose revenue and costs as the relevant indicators, it quickly becomes apparent that neither on the cost side nor the revenue side can all effects of CRM be unequivocally compiled. Furthermore, the respective cost and revenue classifications are specific to each company and are

subject to interpretation (Uebel 2008). And it also wouldn't be possible to classify all of the relevant effects by cost and revenue. There are typically several effects to be recorded only qualitatively (such as resulting flexibility, greater market transparency, faster decision making, etc.) but that should at least be considered as complements.

- Abstraction of situational and individual influencing factors on CRM effects
To substantiate the performance analysis, it has to be embedded in the specific situational circumstances of an individual company. On the other hand, comparison over a period of time and/or of multiple participants requires a certain degree of generalization. With the complexity of CRM concepts it comes as no surprise that controversy comes up again and again as to whether the measured or assumed effects in individual cases can be attributed to certain basic conditions. If this were the case, it would make a sweeping generalization impossible, specifically in regard to detailed findings. The challenge here is to choose an abstraction level that seems appropriate.
- (Lack of) consideration of linkage and integration effects:
The challenge, closely related to the previous point, is that CRM applications are typically realized by different functional areas, departments, procedures and IT subsystems, each contributing its part from the division of labor. A suitable excerpt must be chosen for the performance analysis and the comparison of benefits of courses of action performed for this excerpt. Established functional, departmental or IT system limitations are typically applied, and available basic information (e.g. from accounting/controllers) is taken into consideration as well. It happens regularly that reciprocal effects have to be ignored, between segments examined separately as well as between subsystems considered and not considered in the analysis.
- Observance of benefit effects distributed geographically, time-wise and/or institutionally:
Both positive and negative effects of potential CRM implementations typically occur at different times and are sometimes delayed. Seen from the cost side, this can be considered by factoring in one-time and current expenses (e.g. total cost of ownership with CRM systems, Laudon et al. 2010), but it is much more difficult e.g. when the resulting revenue is considered. In this context it is important to emphasize that the success of CRM can be observed only over the mid to long term (Hippner 2006). Which revenue effects are implied and which proportion is attributed to a CRM system? The ramifications can be seen in different locations and throughout the institution, which in turn leads to identification, evaluation and attribution problems. If advantages and disadvantages become apparent in different areas of authority (possibly at different times and with the attribution problems described), this will usually lead to analyses being discussed with a great deal of controversy.
- Uncertainty and innovation problems:
It must be kept in mind that CRM systems, like all information systems, have no objective, ex ante specifiable value (Picot et al. 2003; Uebel 2008). This means that really only specific implementations of CRM systems have effects

that can be compared, or hypothetical scenarios and those based extensively on assumptions have to be accepted. Then there is grave uncertainty about the actual occurrence of assumed effects as well as about the actual development of assumed conditions or the occurrence of surprises. This problem becomes even more critical with innovative implementations of CRM systems that are not “only” substitutive improvement of existing processes, structures and services but actually form and justify new ones. The limitations of attempting to quantify potential effects quickly become apparent, and it can be claimed that actual uncertainty is concealed by “pseudo-precision”. On the other hand, competing project proposals will in practice have to consider comparison figures/indicators (depending on the method applied, e.g. internal discounting, project contribution margin or ROI).

- Necessity of comprehensive consideration and solution of attribution problems: As already mentioned, CRM implementations are not restricted to technical realizations, they also require organizational and HR changes and adjustments. So performance analysis may not single out isolated aspects. It is, however, always difficult to determine the limits of causality, which effects can and should be attributed to the individual CRM concept. Expanding the analysis meets the demands for comprehensiveness, but at the same time the analysis effort, the unavoidable uncertainty of prognoses and the attribution problems increase dramatically.

In light of the challenges only hinted at here as well as the impossibility of “correct and complete” evaluation of the efficiency of CRM implementations, the following impressions—apparent in the evaluation of relevant publications as well as in observations and empirical studies of actual practice—are not surprising:

- Diversity and contention of methods: In accordance with the fundamental alternatives of analyzing the performance of IT systems, all conceivable manifestations and combinations of methods come up in discussions of CRM systems (Gersch 1998; Schumann 1992, 1993). These methods range from procedures for determining the effects (including cost-benefit analyses, process analyses, efficiency chains) and one-dimensional or multi-dimensional methods to economically assess the conjectured ramifications (such as investment appraisals, full-cost accounting and marginal costing, process cost accounting as well as scoring models, efficiency analyses and comparison of arguments and potential, Reckenfelderbäumer and Welling 2006) to more complex combined methods (Uebel 2008) that sometimes include different methods to determine uncertainty (such as sensitivity analyses, probability calculations, scenario technique). Brilliant controversial discussions on the “correctness” of the method chosen in comparison to other methods can ensue.
- Decisions having to be made with minimal information on the inherent risks and a tendency towards limited CRM implementations: In light of the complexity of comprehensive CRM concepts and the problems related to analyzing their profitability, it comes as no surprise that, because of

the unavoidable errors, simple procedures with a marked tendency toward aggregation are commonly used (Laudon et al. 2010; Sexauer and Wellner 2008). Examples of parameters used include: number of repeat purchasers, cost per customer service call, reduction in customers changing to other suppliers or various conversion rates, e.g. in the sense of interested parties becoming purchasers and then repeat purchasers. Sometimes an explicit methodical examination is omitted and the “convictions” of top management tip the scale. Since this, too, requires justification, the tendency becomes stronger to implement isolated CRM applications that can be realized with a relatively low budget, because performance analysis methods that can be easily substantiated (e.g. ROI) seem easy to justify. This effect tends to become stronger when middle management of a company is responsible to top management for CRM projects.

- **Disenchantment and CRM disappointment:**
The actual results often come as a surprise. They are perceived as much more negative, which can usually be attributed to originally optimistic assumptions, underestimated complexity or a limited analysis environment. This leads to the premature yet bold judgment that CRM usually does not meet expectations. (Laudon et al. 2010; Schaller et al. 2006).

9.3 CRM Development Scenarios

Simply put, there are two potential scenarios for the development of CRM that simultaneously systematize the courses of actions for companies considering CRM as a new strategic option:

- Focus on subtasks deemed realistic: companies begin the implementation of CRM with single, clearly defined subtasks. Hippner et al. (2006) refer to this as “selective CRM systems” as opposed to “integrative CRM systems”.
- Realization of comprehensively integrated CRM concepts that serve as a consistent anchor for the corporate strategy and integrate all relevant subtasks and functional areas to the greatest extent possible.

9.3.1 CRM Development Scenario 1: Focus on Realistic Subtasks

9.3.1.1 Examples of Selective CRM Applications

The wealth of selective CRM applications described in publications and observed in actual practice (Weidner 2007) can be categorized by different aspects by focusing on the subtasks. They can be categorized e.g. by:

- Phases of the customer life cycle: CRM concepts can focus on single subtasks over the course of the so-called customer life cycle (Hippner 2006; Hippner and Wilde 2008; Wimmer and Göb 2006). These include e.g. systematic

management of interests during the “initiation phase” of a business relationship or revitalization management to identify, analyze and rejuvenate business relationships with economically attractive customers that used to work well.

- Marketing instruments: Weiber (2006) differentiates between focusing on the course of communication, product, distribution and/or pricing policy; he claims that multiple, combined instruments can also be addressed. These include e.g. modular design/mass customization strategies as part of pricing policy, facilitating individual offerings suited to the customer’s needs.
- Measures that are part of customer processing: Helmke et al. (2008) distinguish such measures along the typical phases of customer processing. These include e.g. concepts for individual customer support during the information phase, all the way to after-sales service.
- Functional areas/corporate departments: Laudon et al. (2010) differentiate between selective CRM applications by the specialized departments sales, marketing and customer service. Examples of CRM application are customer and order management in sales, campaign and event management in marketing, and customer satisfaction management in customer service.
- Technical realization: Selective CRM approaches, often in conjunction with another systematization criterion, are differentiated by information technological aspects in at least two respects:
 - Locating CRM functionality in the IT system infrastructure of a company: CRM implementations here include those as an integral component of fundamental back office systems (e.g. of ERP or inventory control systems), as extensions of focused information systems (e.g. existing sales information systems) or as specialized CRM information systems selectively linked to established subsystems (Hippner et al. 2009).
 - Use of certain techniques to resolve CRM subtasks: these include considerations that emphasize e.g. the potential of multi-dimensional databases, new data mining methods or convergent, IP-based information and communication technologies as the basis for so-called customer interaction centers (CIC) to deal with CRM tasks (Hippner et al. 2006).

Because there are so many selective CRM applications, it is fruitless to even attempt to offer a complete overview. Using a few examples, the main approaches of typical partial approaches to CRM will be described.

Customer-related Sales Information Systems

These applications are characterized as part of operative and analytical CRM, often bearing different names like CAS (computer aided selling), (Sexauer and Wellner 2008), sales automation (Hippner et al. 2006) or SIS (sales information system), (Laudon et al. 2010). The emphasis is on supporting sales, particularly in efficiently performing the individual tasks associated with managing customer relationships. The most common applications are related to supporting sales staff in dealing with administrative, analytical and contact-related tasks before, during and after customer contacts (Hippner et al. 2006).

The **administrative tasks of the SIS** include scheduling appointments and planning routes for sales reps, compiling call reports or consolidating sales overviews. But effectiveness and efficiency can also be increased by simplifying travel expense claims, maintaining customer data, or target planning and budgeting individual business relationships. In addition to systematic evaluations in the form of standard reports, the **analytical tasks** of the SIS with increasing frequency include OLAP applications that help sales staff with flexible and problem-oriented analyses to prepare for and follow up customer contacts. Some of the standard analyses are: “lost order analyses” (analysis of all activities/offers that did not result in a contract), “sales cycle analyses” (analysis of purchasing histories and notation of replacement times in order to facilitate proactive approach) and “sleeping relationship analyses” (analysis of formerly active business relationships in regard to the causes of absent/declining subsequent transactions). The **contact-related tasks of SIS** are functionalities that support planning and execution of the actual customer contacts. These include e.g. electronic product catalogs, possibly with argument and configuration aids for customized offerings (sometimes based on experiences with customers of the same purchaser type or on the saved and assessed purchasing history of the specific customer) or conversation guidelines that help steer the content and course of phone calls with customers. Also refer to the implementation achieved by Satisloh AG, a supplier from the machinery and equipment manufacturing sector. With its mobile SIS, the company provided its sales reps with product configurators for use during sales talks.

From a technical viewpoint, integrated OLAP applications as well as combinations of different stationary and mobile terminals hold great potential for supporting sales reps in their work. And they are also an ideal way to improve coordination between sales reps and in-house staff and to mesh sales with other functional areas of the company.

A good example of strategies efficiently enabled by focused CRM application is so-called **campaign management**, in which several areas of responsibility (particularly marketing and sales) coordinate their actions (here and later: Hippner et al. 2006). The emphasis is on presenting to the right customer the right information and offering, in the right communication style, through the right communication channels at the right time in the course of the business relationship. Sales becomes part of comprehensive campaign planning, campaign control and campaign evaluation.

- **Campaign planning:** This includes especially: defining the goal of the campaign (e.g. increasing the revenue generated by regular customers by cross-selling or up-selling, reviving “dormant” business relationships), selecting the target group and specifying relevant selection criteria, combining communication channels as best suited to a certain type of customer or even to a specific customer, and clearly defining the campaign process. This ensures that each person responsible for a task is assigned unequivocal responsibility and specifications for single sub-processes.

- **Campaign control:** Usually with the aid of a campaign management system, previously planned sequences of actions are triggered and their implementation controlled in a coordinated manner as specified by the criteria/indicators dictated during campaign planning. These include alternative contact sequence planning and communication rules. Without the proper campaign rules, complex, multi-level campaigns would not be controllable and would lead to inconsistencies and irritation from the customer's point of view. It is also important to watch the reciprocal effects with other sales measures and campaigns. If the customer is approached too frequently by different contact persons addressing different topics, the contact can be perceived as "aggravating" or "too much". As Weidner (2007) made clear in the example of Audi AG's rollout of the Q7, campaign control can be achieved as a joint effort with cooperation between producers and dealers; a similar example is the Top Drive system by BMW AG, (Mertens 2009).
- **Campaign evaluation:** Customers' reactions are comprehensively and systematically fed to the customer data warehouse, thus facilitating the basic concept of "learning business relationships" (Peppers and Rogers 1997). Analysis of different alternative contact routes is of particular relevance (does contact initiated by the sales department trigger research, an inquiry or even an order in the online shop or call center shortly thereafter?). One goal of the impact study is to examine the action/reaction consequences to generate information relevant for action, in regard to continuation and control of the current campaign as well as in regard to the analysis of individual business relationships and the formation of customer types with similar reaction patterns. Then via the customer data warehouse this creates a foundation for future activities.

Data Mining Analyses of Customer-related Data

Data mining applications, considered to be promising new technologies to support customer relationship management, are a popular topic discussed in detail in publications and used more and more frequently in practice.

Generally speaking, data mining can be characterized as one of several potential approaches to data analysis, serving as a particularly good way to discover and confirm previously unknown information, structures, rules and patterns in large quantities of "Big Data" (Chamoni et al. 2010; Gluchowski et al. 2008; Hippner et al. 2011; Laudon et al. 2010; Neckel and Knobloch 2005). This makes data mining a crucial component of comprehensive concepts such as "business intelligence" (Dittmar and Ossendoth 2010). In regard to CRM, terms can be found such as "customer intelligence" (Wimmer and Göb 2006) or knowledge discovery in databases (Düsing 2010).

In customer relationship management, data mining becomes a part of analytical CRM. The multi-dimensional data compiled and kept in a customer data warehouse as part of oCRM forms the starting point for data mining. When the essential quality requirements are met, data from internal or external sources can be combined (Neckel and Knobloch 2005); or from of market research and internal corporate data collection (Wimmer and Göb 2006). In contrast to online analytical processing

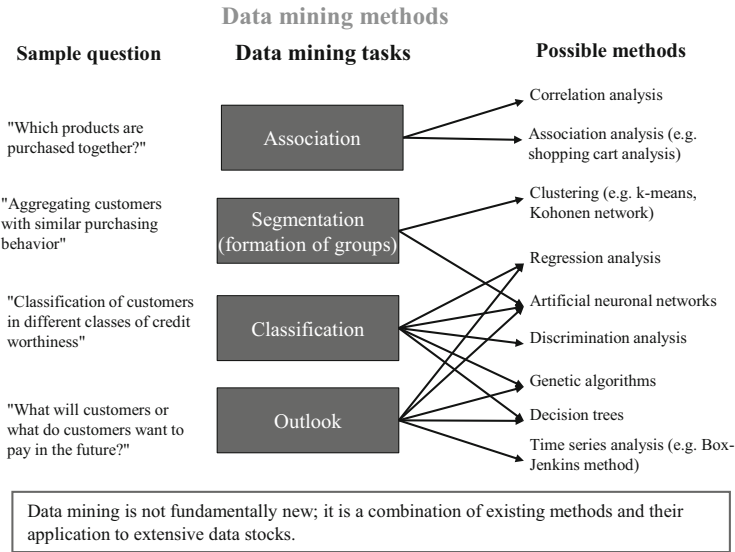


Fig. 9.4 Data mining methods and typical “research” questions. Source: Based on Chamoni et al. (2010)

(OLAP), data mining does not require prior assumptions and hypotheses regarding causal correlations to be developed. Identifying these from the data stock is a central task of data mining. The term “mining” is intended to conjure the image of panning for gold in vast, unknown quantities of stone and project it onto the evaluation of large amounts of data (Zerdick et al. 2001).

Data mining applications use commonly known, analytical and statistical methods that—with expanding technical capacity—can be applied to increasingly large data quantities, sometimes even automatically. The following fundamental types of potential problems are particularly relevant as **data mining tasks** (Chamoni et al. 2010; Hippner and Wilde 2008):

- Association: discovery of correlations/precepts between objects
- Formation of groups: revelation of similar patterns or formation of groups with similar characteristics
- Classification: allocation of objects to created classes
- Outlook: forecast of unknown/future characteristics of objects

Based on the findings of Chamoni et al. (2010), Fig. 9.4 offers an overview of typical data mining methods and provides examples of the questions addressed.

In regard to the use of data mining as part of aCRM, the wide range of conceivable uses is obvious. Two examples will briefly demonstrate this (for many more detailed examples, refer to Neckel and Knobloch (2005)

Management of Interests Combined with Customer Segmentation by Behavior Data

When generating contacts to potential customers or selecting inquiries received, there is a certain “information dilemma” in regard to the goals of business relationship management. Generally no historical, internal data related to transactions can be available on the potential customer/interests (Haas 2011; Hippner 2010; Weiber 2002). However, the prediction of the conjectured customer value of the potential customers or interested parties can be greatly improved by forming so-called “similarity/affinity groups”. The foundation for such groups can be a segmentation of current customers, using data gathered on their communication and purchase behavior as well as the customer value manifested over time. Applying the increasing volume of data distinguished throughout the various phases of the customer life cycle, it may be possible to hypothetically assign new interested parties to a similarity group with only minimal data available. And as the data availability increases, e.g. in regard to communication and interaction of a potential or first-time customer, it may be possible to improve the quality of the prediction step by step. The findings on typical customer traits gleaned from the similarity groups deemed attractive can be used to proactively initiate contact, thus acquiring new customers possessing the traits considered to be promising.

Proactive Recovery Management

The affinity groups described above can help to greatly improve the prospects of recovery management in business relationships (Hippner 2010; Hippner and Wilde 2008; Neckel and Knobloch 2005; Schöler 2011). In addition to better analysis methods to examine the selection of which relationships with current/previous customers would benefit from recovery measures in light of the potential customer value of this type of customer, the following aspects are also possible as part of proactive recovery management:

- When looking at **whether** recovery is worthwhile, data gained from comparable recovery attempts with similar customers can be analyzed and serve as a basis in deciding **how** recovery should be approached. The broader the data base available for this purpose is, the greater is the predictability of implementing recovery measures that are suited to the type of customer and that increase both efficiency and effectiveness. Analysis of the “cross-selling” and/or “up-selling” potential (Laudon et al. 2010) of the reclaimed customers can lead to greater intensity and higher value of the revitalized/renewed business relationships.
- Recovery management becomes proactive when indicators hinting at problems are identified and continuously observed before a business relationship is broken off. Then the supplier has the opportunity to intensify/revitalize the relationship with a customer presumed to be attractive before the relationship can be terminated. With these data mining approaches, it seems that the technical possibilities described by Reichheld (1993) are now available to consistently and actively utilize the relative benefits of managing existing or threatened

business relationships as opposed to the more common approach of attempting to generate new customers and new purchases.

- In regard to the usefulness of data mining approaches as part of aCRM, the following aspects are important:
- Internal customer data from any number of sources can be supplemented and combined with external data. However, the quality and relevance of the data base from oCRM as a basis for aCRM should be critically examined (Hippner 2010; Wimmer and Göb 2006).
- Data mining is not equally relevant to all aCRM issues and is not always superior to other analysis methods (Hippner and Wilde 2008; Neckel and Knobloch 2005). Benefits can be divined particularly when large, multi-dimensional data quantities become available for which there were previously insufficient conjectures on relevant causal correlations and patterns.
- While numerical data has made up the bulk of analysis objects so far, better methods (e.g. “text mining” are being developed to allow text or other “fuzzy” data to be considered in potential analyses, Gluchowski et al. 2008).
- With increasing digitalization and networking within E-business (Gersch 2010), the availability of data (digital traces) that users leave at different touch points and through different activities has exploded. In addition to “web log mining”/ “web usage mining” (Gluchowski et al. 2008), which has been practiced for a while now, information such as geographic and environmental data of individual times of use is successively becoming available via mobile terminals. In addition, web 2.0 applications generate a flood of data that cannot be managed manually (Laudon et al. 2010). Here, too, extensively automated analysis approaches promise interesting results, e.g. in regard to usage processes on the customer side that would not otherwise be detected and in regard to (dis)satisfaction or suggestions for improvement during use. Successively expanding the multi-dimensional data base this way promises interesting analysis possibilities, but is also increases the risk of loss of quality and relevance.

Collaborative Filters as “Automated Learning Relationships”

The process described above of using the available individual purchase and opinion data to build affinity groups as clusters of heterogeneous customers to form homogeneous groups is being used more and more frequently in the pricing and product policies of offerings. It serves to generate extensively automated recommendations and to customize the offering. This is discussed in publications particularly under the terms “**recommendation systems**” or “**collaborative filters**” (Ansari 2000; Lee and Kwon 2008; Zerdick et al. 2001).

Figure 9.5 outlines the fundamental principle that automates the idea of “learning relationships” by Peppers and Rogers (1997): “*A Learning relationship (...) gets smarter and smarter with every individual interaction. [The one-to-one enterprise gets experience with each individual customer]”. “Surfing the feedback-loop (...) the customer tells the company about certain need, you can ‘look’ at the customer during the online information/buying process and you can learn from the customer feedback ((un-)satisfaction, complaints...). ...Every interaction and*

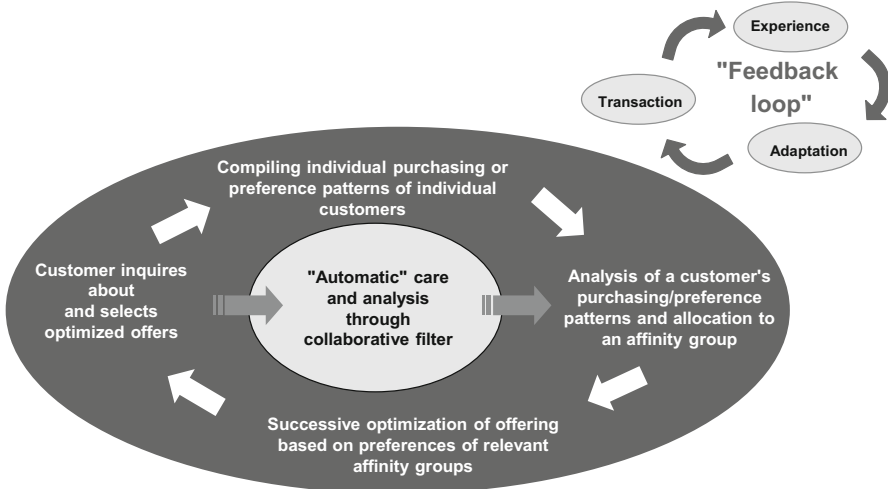


Fig. 9.5 Collaborative filters and the “feedback loop”. Source: Based on Zerdick et al. (2001)

modification improves your ability to fit your product to the particular customer. Even if a competitor offers the same type of customization and interaction, the customer won't be able to enjoy the same level of convenience without taking the time to 'reteach' the competitor the lessons your company has already learned.” (Peppers and Rogers 1997, p. 251).

While collaborative filters and recommendation systems were initially relevant when supplying completely digitalized offerings (e.g. Last.fm, Putpat, Yahoo, Google), the approach is being implemented with increasing frequency by suppliers whose offering core is made up of physical products (e.g. Amazon or Baur Versand (Weidner 2007)). A brief description of each application in specific offerings demonstrates the potential of “automated learning relationships”:

Last.fm/Putpat These media suppliers serve as an example for a series of comparable offerings of individualized music (www.last.fm) and music videos (www.putpat.tv). Once a personal account has been set up, the user states e.g. his five favorite groups. This serves as the basis for allocation to affinity groups with a similar taste in music. Then, for as long as he wants, the user can hear or see pieces of music that are a “surprise” to him: the selection is put together individually, but the order cannot be changed. Each piece can be evaluated and/or turned off before it is over. The more usage and evaluation processes there are, the greater is the precision of the fundamental formation of affinity groups and of the assignment of individual users to homogeneous groups with a similar taste in music. So the user is presented with a series of pieces that are new to him, but they have all received a positive evaluation from users with a similar taste in music. Because of the high degree of correlation between taste in music and features relevant to purchase behavior of other offerings, an “economically interesting” data base emerges. The

business system operators use the data e.g. for targeted marketing communication offers for third-party suppliers and—when legal stipulations permit—sell the data to other companies.

Amazon/Baur Versand Interested parties and customers can use the personalized online offerings of dealers by logging in. They are then offered easier use, accompanying services and other conveniences (e.g. remembering order data, invoicing after delivery, preferential conditions and “personal recommendations”). Personalization allows the supplier to individually analyze the behavior “observed” in regard to individual interaction and transaction processes—including those that cover multiple touch points and communication channels—and to save any feedback, complaints, etc. expressed. Also, the customer’s behavior can be compared to the sales policy instrument applied by the supplier, leading to higher and higher precision of individual and especially affinity group-based hypotheses on probable action and reaction patterns. Suppliers generally use the resulting data base in many directions. Typical uses include general and/or personal recommendations, which the customer recognizes as such (“Customers who were interested in this item also looked at . . .”; “Are you familiar with this item?”). Customers usually do not notice the successive customization of the offerings. It basically becomes feasible to offer every customer a customized view of the company’s offerings at different touch points, including individual conditions. This also successively creates an “economically valuable” data base that typically forms the origin of addition revenue streams for the supplier.

Coordination of Customer Touch Points and Interaction Channels

To master all the subtasks that are part of CRM, it is imperative to coordinate the different ways in which to interact with potential, current and former customers via the increasing number of touch points and channels. This helps to create as coherent an image of the customers as possible for the various (partial) functionaries within the company (*one face of the customer*), while at the same time achieving coordinated communication with the customer (*one face to the customer*) (Hippner et al. 2006; Weidner 2007, applying Vivil’s example).

If in addition to the traditional personal contacts (e.g. branch offices, service stations and field service) call centers are established to facilitate efficient and effective telephone contact, these partial approaches—with increasing customization of the offering, more complex service offerings and a greater number of touch points—are no longer sufficient to achieve the described goals of CRM.

Both in publications and in actual practice, so-called **customer interaction centers** (CIC) seem to be the reaction that meets the increasing demands for coordination and interaction. Agreement and coordination of parallel or sequential, of linked or unlinked, of supplier-initiated or purchaser-initiated interaction at various touch points is especially important to business systems that typically have multiple (alternative or combined) contact and sales channels (as well as the respective multi-channel strategies), (Schögel et al. 2011). Customer interaction

centers are intended to take care of precisely this task as part of operative and communicative CRM. This applies to supplier strategies that tend to allow the customer to choose the combination of interaction channels he is comfortable with as well as to strategies with which the supplier sees himself in a more proactive role in designing and controlling the business relationship.

Publications emphasize these aspects of customer interaction centers:

- Selection and integration of supporting interaction channels:
A supplier has to make a fundamental decision as to which interaction channels he offers and supports or does not offer and support. In addition to the traditionally dominant personal touch points, the number of media-supported interaction channels (e.g. internet websites, social media, information offerings on mobile internet, E-mail, text messaging) is increasing. The CIC becomes the central place—or at least plays a supporting role—where interaction with the customer is realized and e.g. documented in the customer data warehouse.
- Increased efficiency and effectiveness through IT-supported functionalities:
The CIC can in principle be the starting point for so-called “outbound functionalities” (company seeking contact to customer, e.g. as part of sales or service campaigns) as well as coordinator or body responsible for “inbound functionalities” (customer initiating contact, e.g. inquiries, making appointments, filing complaints). The necessity of a coordinated approach to different alternative or combinable touch points was pointed out in the previous sections. In oCRM, IT-based functionalities are increasingly supporting tasks typical for customer interaction centers, (Hippner et al. 2006), e.g.:
 - Pre-selection of customer inquiries: subsystems such as “computer telephony integration” (CTI), “interactive voice response” (IVR) or “skill based routines” (SBR) take care of e.g. sorting inquiries by various topics, replying to simple requests for information (sometimes programmed), program-supported compiling of basic information (e.g. master data or job numbers), capacity-based assignment of inquiries to available CIC agents, also taking into consideration the respective skills required to solve a problem when assigning the problem to an agent.
 - Support of actual interaction processes: the CIC agents are given not only all of the required customer-related data (ideally covering the entire customer history from all contact channels) in prepared/condensed shape (including linkage to documents that may or may not be relevant, such as invoices, minutes of meetings or previous inquiries), they can also use e.g. so-called “scriptings” (conversation guidelines) to help them with specific discussions.
- Reflexive CRM with consistent workflow planning and continuous tracking of CIC activities:
The basis for coordinated constellation of customer interaction is typically workflow management systems that facilitate systematic planning (especially sequencing), analysis and control of required but typically distributed

sub-processes (Laudon et al. 2010). Such systems enable e.g. analysis of customer interaction center activities (e.g. with continuous analysis of parameters considered relevant, such as defect rates, length and consequences of conversations or greater customer satisfaction after customer contact) as well as definition and control of escalation paths when certain entry requirements are met (e.g. unacceptable waiting, angering of A customers).

Particularly the developments in the field of customer interaction centers serve as a good example that focused CRM approaches are a way to effect substantial improvement. Weidner (2007) reports, for example, that, with the proper strategy, Vivil was able to achieve substantial operative increases in efficiency in its contact with retailers (e.g. by increasing the net duration of conversation per hour by 20 %, increasing the qualified dialing attempts by more than 40 %), (Weidner 2007).

9.3.1.2 Potential Reasons for Successful Focusing

Considering the aspects discussed thus far, the results of empirical studies, some indicating substantial preponderance of focused CRM applications, come as no surprise (Gottwald and Karlstetter 2010; Sexauer and Wellner 2008). The empirical studies reveal the following aspects that explain why selective CRM approaches focusing on individual subtasks are clearly favored over comprehensive CRM implementations and are found much more frequently in practical applications. The causes (especially complexity of CRM implementations, scope of requirements for integration, fundamental problems of adequately differentiated performance analysis) discussed repeatedly in the previous chapters are reflected here:

- Strong leverage for subtasks:
Especially when companies have not considered and implemented any CRM strategies yet, even revising individual subtasks effects leverage in regard to potential increases in effectiveness and/or efficiency.
- Adequate predictability and controllability:
The complexity resulting from subtasks and the potential follow-up costs seem to the decision maker to be easier to predict and control.
- Career boost with “quick wins”:
Closely related is the location of the specific CRM responsibility, especially at the level of middle management. The associated obligation to provide justification and proof to superiors typically promotes projects for which the economic success can be more precisely and reliably analyzed. So-called “quick wins” tend to benefit careers more than complex, comprehensive projects.
- Benchmarks and standardized sub-activities as “lessons learned”:
The CRM offering available on the market (especially consulting but also software products) is based primarily on the vast experience gained from many single, focused projects. It promises convincing results in the short-term to mid-term, e.g. by adapting proven business processes or making other organizational adjustments.

Even though these aspects tend to promote a focused CRM strategy, this should not be interpreted as a hidden indication that a comprehensive, integrated CRM strategy would actually be better. Focused approaches can be just the right way to achieve relatively great improvements, to increase the awareness and acceptance of CRM strategies and/or to have the courage to introduce a long-term, step-by-step migration strategy. Particularly the frequently underestimated prerequisites for a comprehensive CRM concept make an (initially) focused procedure seen reasonable. The following section demonstrates one of the rare examples of comprehensive CRM strategy implementations.

9.3.2 CRM Development Scenario 2: E-Business as Breakthrough for Integrative CRM?!

9.3.2.1 Comprehensive Management of “Cross-linked Business Relationships” Using the German Pharmaceutical Market as an Example

In contrast to the more focused approaches of selective CRM, there are also examples in which participants interpret customer relationship management as the essence of their strategy and attempt to comprehensively realize the described possibilities of CRM throughout several or even all activity and functional areas in a coordinated and systematic manner (Helmke et al. 2008).

The special opportunities but also the challenges associated with this will be explained in this section using the business relationship management practiced for decades by the pharmaceutical wholesalers on the German pharmaceuticals market.

Structure of the German Pharmaceutical Market

After decades of structural consistency in one of the most strictly regulated “markets”¹ in Germany, the health care reforms that went into effect beginning in 2004 led to the first noticeable changes, evident as innovative business models (e.g. mail order sales of medications, franchise pharmacy systems, blistering packaging especially for individual patients and/or multi-channel strategies for integrated supply geared towards target groups) and modified business systems (e.g. vertical integration between pharmaceutical wholesalers and pharmacies,

¹ The quotation marks used only this once signalize a controversy between practice and science as to whether, due to the strict regulations of the German mobile pharmaceutical market, this can even be considered a market in the classic sense. Despite the distinction between e.g. use, product selection and payment (such as the interaction between patients, physician and health insurance in the field of prescription medications) that is not a common feature of a market and despite strict regulation of competition between all participants at the various levels of the value-adding process, the German monopoly commission and others see the pharmaceutical sector as a market with special features worthy of consideration that has or should have competitive elements (Monopolkommission 2006; Wirtschaftsforschung 2010).

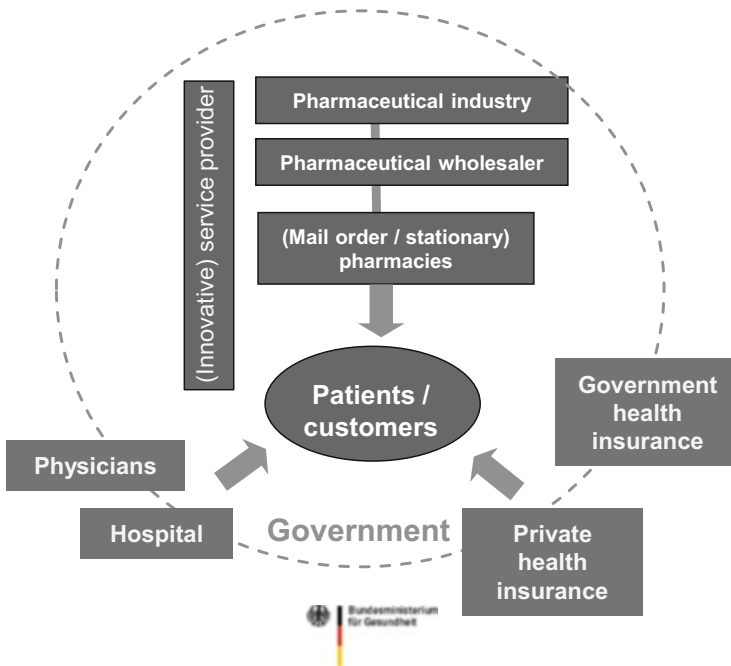


Fig. 9.6 Structure of the German pharmaceutical market. Source: Based on Kunz (2001)

direct delivery to pharmacies and sometimes to end users by the pharmaceutical industry).

The three-level sector structure in Fig. 9.6 shows a value chain, still applicable today, characterized primarily by the following benchmark data:

- Over 1,000 pharmaceutical companies offer about 60,000 medications on the German market, some of which by German law require a prescription (so-called Rx products) and/or must be sold in a pharmacy (over-the counter products), (BPI 2010; Wirtschaftsforschung 2010). Approval for these products follows regulations that change over time but are all-encompassing, the purpose of the regulations being to attempt to meet social challenges (e.g. demographic developments, financial restrictions, medical advances) and political objectives (such as access for all to the best medical care without direct social discrimination or fear of lack of care).
- Eighteen pharmaceutical wholesalers, some of them nationwide, have taken on a central mediator function to overcome geographic, time-related, quantitative (once in a while qualitative) and informational tensions between manufacturing and use. The so-called “one-stop shops” make deliveries to pharmacies of all of the products offered (about 120,000, including sideline and peripheral assortment) up to five times a day. Due to government regulation and phases in of intensive concentration and pricing out of competitors, the pharmaceutical

wholesalers' share of value added in Germany fell to 4.9 % (down 0.2 percentage points over 2007; refer here and later to: ABDA 2010 (BPI 2010)); the other groups involved were able to achieve the following shares of value added: pharmaceutical industry 65.2 % (+1.2 percentage points over 2007); government remained stable at 16 % (value-added tax) and pharmacies 14.9 % (−1 percentage point over 2007). Most of the large pharmaceutical wholesalers are active on the global market as well and pursue individual European strategies that have to be adapted to the regulations of the respective national pharmaceutical markets. In addition to economies of scale in purchasing and logistics, in many countries—when the local laws permit—clear vertical integration tendencies can be detected. The pharmaceutical wholesalers initiate and control particularly cooperation with pharmacies or even operate so-called “pharmacy chains” as branch retailers. Because of the “Mehr- und Fremdbesitzverbot” (prohibition on third-party and multiple ownership of pharmacies in Germany), this is not (yet) possible in Germany (MKG 2010). This law specifies that a German pharmacy must be legally and economically an independent entity and (just since the health care modernization act of 2004) may not operate more than four pharmacies (main pharmacy and up to three “branch pharmacies”), all located near one another. Although in 2004–2009 it looked as if the prohibition on third-party and multiple ownership of pharmacies in Germany could be abolished, a notable verdict issued by the European Court of Justice in May 2009 confirmed that the German law was compatible with European competition law (MKG 2010). This at least delayed the surmised tendency towards “industrialization” of the German mobile pharmaceutical market. However, there is still a strong presence—over 100—of horizontal and vertical forms of cooperation (EPC 2010), frequently involving a pharmaceutical wholesaler.

- For the first time in decades, in 2009 the number of “public pharmacies”² in Germany fell by 54 (−0.25 %) to 21,548 pharmacies (incl. branch pharmacies, Apothekenverbände 2009). Since the health care modernization act of 2005 permitted branch pharmacies, their number has risen to 3,224 in 2009. Through 2009, 2,677 permits for mail order pharmacies had been granted (Buse 2010), only about 2 % of which achieve transaction figures relevant to the market (>1,000 shipments/day, (Schloh 2010). This has so far had no effect whatsoever on the relatively high supply density in Germany of 3,800 inhabitants per pharmacy (EU 15 average: 5800, EU 25 average: 4400 (Apothekenverbände 2009; Haucap 2010). The total revenue of German pharmacies in 2009 was 39.8 billion € (without VAT). The average revenue of a stationary pharmacy in 2009 was 1.82 million € (VFA 2010), whereby there are vast differences between the pharmacies in regard to revenue and profitability (55.8 % of pharmacies achieve revenue of less than 1.5 million €/year; 19.3 % more than 2 million €/year). The

² Only so-called “public pharmacies,” which sell to consumers and are considered part of the mobile sector of health care, will be examined here. There are some exclusions to this, e.g. hospital pharmacies in the stationary sector.

pattern over time indicates a shift from smaller pharmacies to pharmacies with higher revenue (Apothekenverbände 2009). When compared to other industries, the steady rise in revenue as well as the return on sales can be seen as being much more attractive than those of other industries. German law dictates that every licensed pharmacy in Germany (pharmacies with an operating permit pursuant to §2 of the German pharmacy act) must be able to supply all prescription medications within a reasonable time. The pharmaceutical wholesalers take over the critical logistical function of ensuring that the common delivery time in Germany of only a few hours for over 120,000 potential products is met (Großhandels 2011). More evident than the absolute quantity are the structural shifts as a result of mail order pharmacies and other types of pharmacies. These still have to have a stationary, bricks-and-mortar store that is part of the mandatory emergency and night duty system. Mail order medications accounted for about 2.5 % of revenue in 2009, but this figure is growing at an annual rate of around 20–25 % per year, primarily in the OTC sector (OTC market share in 2009 approx. 8 % (Buse 2010; Voigt 2009). In addition to mail order sales, the complex forms of cooperation have promoted the tendency to specialize within the pharmacy sector. These trends are apparent e.g. in the differentiation of competition parameters and in the significance to revenue of different items in the assortment. Pharmacy offerings are generally classified into the areas of Rx (30.8 billion € in 2009; Apothekenverbände 2009), OTC (4.7 billion € in 2009; Apothekenverbände 2009) and the so-called “free choice area” (2.0 billion € in 2009; Apothekenverbände 2009) as well as home care products (1.7 billion € in 2009; Apothekenverbände 2009), all of which can be accompanied and supplemented by the most varied pharmaceutical services. The free choice area is limited in Germany to a defined range of “other products normally sold in pharmacies” (Bundestag 2010). The extent of this range has grown over recent years, but it is still the subject of intensive and controversial disagreement between various interest groups. Prescription products traditionally accounted for 90 % or more of revenue in pharmacies—something that has changed drastically, depending on the location and strategy of the pharmacies. Some pharmacy cooperations, e.g. DocMorris (a multi-channel supplier that has been taken over by the German pharmaceutical wholesaler Celesio and turned to a franchise concept, or easyApotheke) see their strengths in a consistent focus on trade strategies from other markets, like category management or establishment of trademarks and their own brands in the OTC and free choice areas (Voigt 2009). In 2009, the free choice area accounted for 30–45 % of the revenue of some pharmacies.

It is still common that a pharmacy is supplied by three different pharmaceutical wholesalers, and the shares of revenue of the three typically differ greatly. The regular or main supplier bundles approx. 60–70 % of the purchasing volume, the second supplier 15–20 % and the third up to 10 %. In addition—and, depending on the strategic orientation of the pharmacy, with increasing significance—the pharmacies maintain business relationships with industrial partners and/or other

wholesalers (especially for the special and free choice range). German pharmaceutical wholesalers have always applied intensive business relationship management to counter potential exclusion and substitution strategies in their dealings with the individual pharmacies (Engelhardt and Gersch 1995; Gersch 1998, 1999, 2004). The great significance of digitalization and networking in the value-adding structures described here is one of the reasons that German pharmaceutical wholesalers can be considered a pioneer in CRM applications. This will be explained more in the following section. Because although the German pharmaceutical market has its peculiarities, its strategies can be considered exemplary and interesting for other branches.

CRM Strategies of German Pharmaceutical Wholesalers

As is common with trading companies, computerized inventory control systems in conjunction with enterprise resource planning (ERP) form the backbone of IT infrastructures. This is also the case with German pharmaceutical wholesalers.

The great significance of the security of the medications supply as well as the relative planning reliability due to strict regimentation, the margins that can still be achieved in the market and the favorable organizational and technical requirements have made the German pharmaceutical market a pioneer in cross-company digitalization and networking. Transactions between pharmacies, pharmaceutical wholesalers and the pharmaceutical industry have been happening with electronic data exchange (EDA/EDI) online and without human-human or human-machine interaction (Gersch 1998) for over 30 years now—long before terms like E-business or E-commerce became popular (Gersch 2010). Computer-supported inventory and transaction data for each article is available at every step of the value-adding process, such that—without these terms being actively used in this sector—concepts discussed in other branches like supply chain management (SCM) or efficient consumer response (ECR) have been applied for a long time to the special features of this market and have proven highly effective.

Although this overall performance of the system is unimaginable without pharmaceutical wholesalers, the wholesalers have feared increasing disintermediation and re-intermediation for years, primarily regarding economically attractive target groups and/or products with traditionally and/or future high profit margins. Furthermore, the diverging economic significance of individual pharmacies, which has always been taken into account, is increased by the structural changes mentioned above, along with greater differentiation and some degree of specialization of the pharmacies. Pharmaceutical wholesalers have differentiated for many years between the pharmacies, applying various approaches and instruments of **customer relationship management**. Some interesting aspects thereof will be described here as examples:

aCRM as Strategy Requirement

With a combination of delivery and sales force service, particularly the pharmaceutical wholesalers offering the full product range have a comprehensive and detailed data base in regard to the individual pharmacies, at least to those with which they

have a delivery relationship. This forms the basis of analytical customer relationship management. The customer data warehouse is constantly receiving data on orders and delivery—precise information on items and exact times, updated daily. The data is based on individual pharmacies and provides a clear picture of the flow of goods, indirectly and supplemented by other data sources (e.g. sales information system), as well as of cost and revenue flows, the pharmacist's strategic behavior and/or business developments over time. A detailed comparison of the individual pharmacies in regard to their current and potential customer value can be created on the basis of the performance indicator systems that the pharmaceutical wholesalers have as well as external systems (Wirtschaftsforschung 2010). This forms the basis for strategic CRM decisions related to the constellation of business relationships with certain types of pharmacies and individual pharmacies and the basis for detailed planning, constellation and control of local, regional or national sales strategies as well as strategies for specific topics or groups in regard to how they affect the use of sales policy instruments (from the pharmaceutical industry side and from the pharmaceutical wholesaler and/or pharmacy (cooperations) side). In addition to the s/o/cCRM possibilities mentioned above, almost all pharmaceutical wholesalers use their data for things like establishing their own brands, for offering category management strategies (to the industry as well as to pharmacies) and/or for arranging infomediary/market research services for third parties.

sCRM as a Requirement for oCRM and cCRM of Multi-channel Strategies

Depending on the relevant circumstances and strategic position selected, pharmaceutical wholesalers use the advantageous conditions of analytical CRM for the various procedures in strategic CRM. So there are vast differences between cooperative pharmaceutical wholesalers (e.g. NOWEDA) owned by the pharmacies they supply, pharmaceutical wholesalers owned by sector participants (e.g. ANZAG, which changed owners in 2010: Gehe/Celesio, Sancorp, Phoenix and others sold their shares to the new majority shareholder Alliance Boots from Great Britain) and pharmaceutical wholesalers with an obligation to shareholder value (Phoenix, e.g. towards the majority shareholders in the Merckle family, Celesio towards Gehe and Haniel).

All pharmaceutical wholesalers base their decisions on detailed customer value analysis, which includes classification of pharmacies by individual criteria that, depending on the pharmaceutical wholesaler strategy applied, can vary in their strategic attractiveness and significance. If the pharmaceutical wholesaler is interested in forming a "cooperation and chain," it will try to have the closest relationships possible by law with the pharmacies that seem essential or well suited to the cooperation, looking at regional and local aspects in this determination. Individual pharmaceutical wholesalers see an opportunity in the coordination of cooperative multi-channel concepts that can be attractive in various ways with the participation of a large number of pharmacies: for the pharmaceutical industry, there are better chances of systematically and comprehensively finding marketing and sales partners for entire regions or target groups that cover multiple distribution channels (particularly stationary and mail order). For the individual pharmacies,

this means access to delivery conditions and marketing concepts that would not be possible for a single pharmacy on its own. Classic individual stationary pharmacies can then offer their customers e.g. professional online information or even E-commerce functionalities or decentralized home delivery service. The pharmaceutical wholesaler can also benefit from single pharmacies serving e.g. as opinion leaders and lead users, or even simply because the single pharmacies are particularly important precisely because of their profitability. In regard to other pharmacies that do not seem conducive to a selected strategic concept or stand out e.g. due to inefficient conditions and/or behavior (such as unattractive location or unsuitable equipment/configuration of the pharmacy, de facto thwarting of marketing strategies or lack of entrepreneurial skill amongst personnel, fluctuating, small order quantities of unattractive items from the product range, difficult logistical conditions), goals for the specific business relationship are formulated that can specify supplying the pharmacy only under certain conditions or even include terminating the relationship. An individual goal, combined with certain basic requirements, is specified for each pharmacy and serves as the basis for operative and communicative CRM.

For the pharmaceutical wholesaler, communicative CRM is typically a combination of personal relationships and coordinated communication policy measures flanked by distribution and price policy measures as part of operative CRM. Each pharmacy receives basic care and attention from the sales reps as well as from the management level of the regional sales and logistics centers. The managers are responsible for ongoing analysis and control of business relationships as well as for the operative constellation of the business relationship to the pharmacies, and—after coordination with central marketing departments that the larger pharmaceutical wholesalers may have—they use this information for actual implementation. A fully integrated customer information system is typically used to coordinate the different persons and measures. The system is linked via the customer data warehouse to the computer-supported inventory control system and e.g. to the ERP system-based functions accounting and controlling. The customer information system provides the responsible persons—graded by their access rights—with not only all of the available data and histories on individual customers, it also contains goals and specifications for the current and future actions having to do with the specific relationship. These range from granting individual delivery conditions (especially different types of discounts and terms of payment) to individual cases of facilitating or directly supporting individual projects of pharmacies, e.g. with a suitable financing model. The reasons for this range from a new opening or modernization of the pharmacy to forms of differentiating campaign management. The pharmaceutical wholesaler sometimes acts as the middleman for single pharmaceutical manufacturers to accompany, monitor and possibly control the operative implementation of actions that the sales force has facilitated for the pharmacies. The importance is increasing of commercial and private label strategies of the pharmaceutical wholesaler, who makes agreements with selected pharmacies—especially in the high-margin OTC assortments but also in the free-

choice assortment—that increase profitability and also promote the benefits of customer loyalty.

The competition for especially attractive existing locations and for new locations and concepts becomes fiercer. An increase particularly in various constellations of pharmacy cooperations (EPC 2010) poses a threat to pharmaceutical wholesalers of losing previously attractive strategic positions in the value-chain. Some pharmaceutical wholesalers are reacting with their own chain/cooperation concepts, while others seek to position themselves as a “neutral partner” or “friend of owner-operated pharmacies.” But customer relationship management is always the strategic foundation for defending the positions in the pharmaceutical branch that have evolved over decades.

9.3.2.2 Digitalization, Cross-linkage and System Integration Promote More Comprehensive CRM

Increasing digitalization and cross-linkage of all internal and business processes and those occurring between companies (in regard to E-business/E-commerce (Gersch 2010); in regard to diffusion rates (Infratest 2009) is possible only with better connectivity, cross-linkage and integration of the most varied operational information systems (Mertens 2009). New architectural concepts (such as **service-oriented architectures** (SOA), Gomez 2010), and developments like “**Software-as-a-service**” (Buxmann 2010) or **Web 2.0- applications** as the foundation of **social networks** (Lackes and Siepermann 2010) promote successive convergence processes, meaning technical as well as organizational merging of previously separate technologies and the applications and concepts based on the technologies. The technology and technical skills required to compile, save, evaluate and use individual data in different manners is becoming simpler and less expensive all the time.

These self-reinforcing technical mechanisms (left loop in Fig. 9.7) at the same time promote increasing customization within the strategies of single companies at the market level. Among other factors, this impacts the expectations of current and potential customers as well as the perception of competitors in regard to relevant competition parameters (right loop in Fig. 9.7).

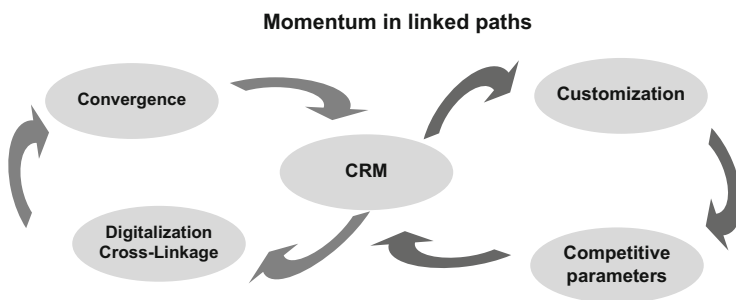


Fig. 9.7 Momentum from “linked paths”

Path dependencies (Sydow et al. 2009) suggest momentum on both the technical side and the market side (linked paths) that tends to promote development towards greater and greater propagation of CRM strategies. However, this process of “**eTransformation**” takes more time and is not as straightforward as it was thought to be in the early phases of E-business (Gersch 2004, 2010).

Conclusion

The interim “CRM euphoria” has given way to more realistic experiences as to which forms of customer relationship management seem to make sense economically. It continues to be apparent that rapid technological developments mean that the fundamental benefits of business relationship management are becoming an interesting strategic option for more and more companies. Nothing has changed so far in regard to the fundamental concepts of business relationship management (and is not anticipated in the foreseeable future). The rapidly developing implementation and utilization possibilities have changed dramatically, and the success of various participants has caused CRM skeptics to sit up and take notice.

Besides individual attempts to implement comprehensive, completely “integrated CRM concepts” right from the start, it is becoming more common to favor selective CRM solutions, with clear and predictable investment risks, focused on selected segments and partial issues. If—depending on the collected experiences and the development of relevant basic conditions—this occurs with the intention of successively expanding the CRM strategy to other functional

Attempt to define CRM

CRM is a ...:

- **Customer-oriented management approach that**, with the aid of
- **customer-oriented information systems**
- enables collection, presentation and use of **customer knowledge**. It also applies a
- **comprehensive orientation** of all corporate activities towards **customer processes**, thus pursuing
- **initiation, control and monitoring** of individualized and
- long-term **profitable customer relationships**.

... Interface topic:

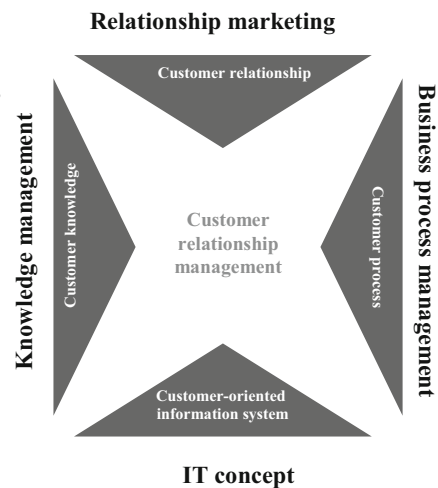


Fig. 9.8 Characterization of CRM. Source: Based on Sexauer (2002)

Theory: CRM is not a completed tool.
Many essential requirements have to be considered!

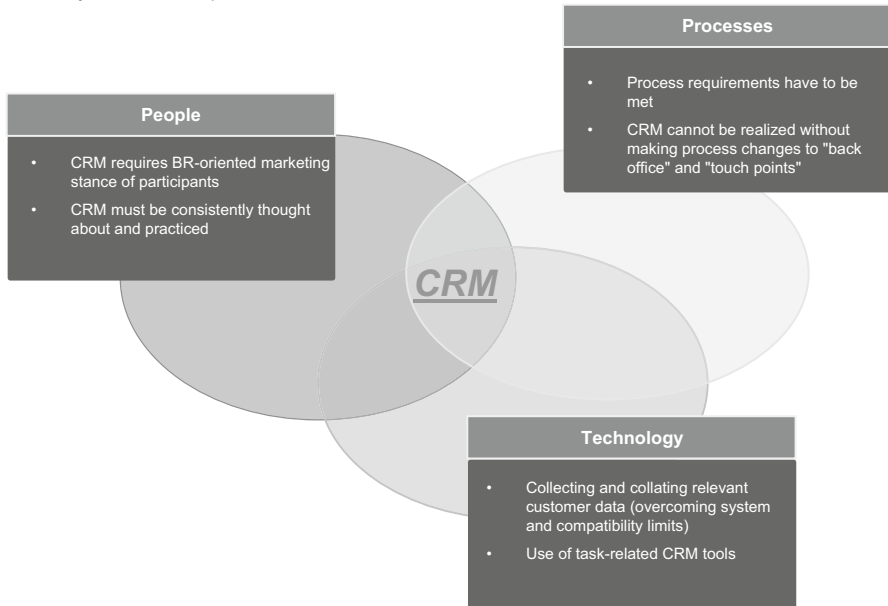


Fig. 9.9 Relevant dimensions of CRM implementation

areas and departments, many promising migration strategies emerge, which must of course meet the technical, organizational and HR requirements for integrative CRM discussed in this contribution. There can be no “one-size-fits-all” assessments as to “which type” and “how much” CRM are right for a company. Each company will have to find its own individual development and migration path. Despite the difficulties of adequately and precisely evaluating performance, more and more companies are choosing this path.

CRM can under no circumstances be reduced to the implementation of relevant software solutions. The definition provided by Sexauer (2002) and his justified characterization of CRM as an interface topic (Fig. 9.8) clearly emphasize that only orchestration of the aspects stated in Fig. 9.9 can ensure success.

Appendix

Exercises

1. Describe the basic conditions that enable the use of customer relationship management (CRM) to be successful. To what extent does IT development play a crucial role?

2. Explain the connections and dependencies between operative and analytical CRM.
3. Compare and explain the cost and benefit aspects of CRM.
4. Explain the HR aspects of integrating CRM and offer potential solutions using a CRM implementation strategy.
5. Discuss the potential of CRM when the sales force uses mobile or stationary terminals.
6. Explain the uses of CRM applications in regard to campaign management.
7. Illustrate the use of CRM by means of the so-called “feedback loop”.
8. Describe the possibilities of customer interaction centers as they relate to inbound and outbound activities.

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