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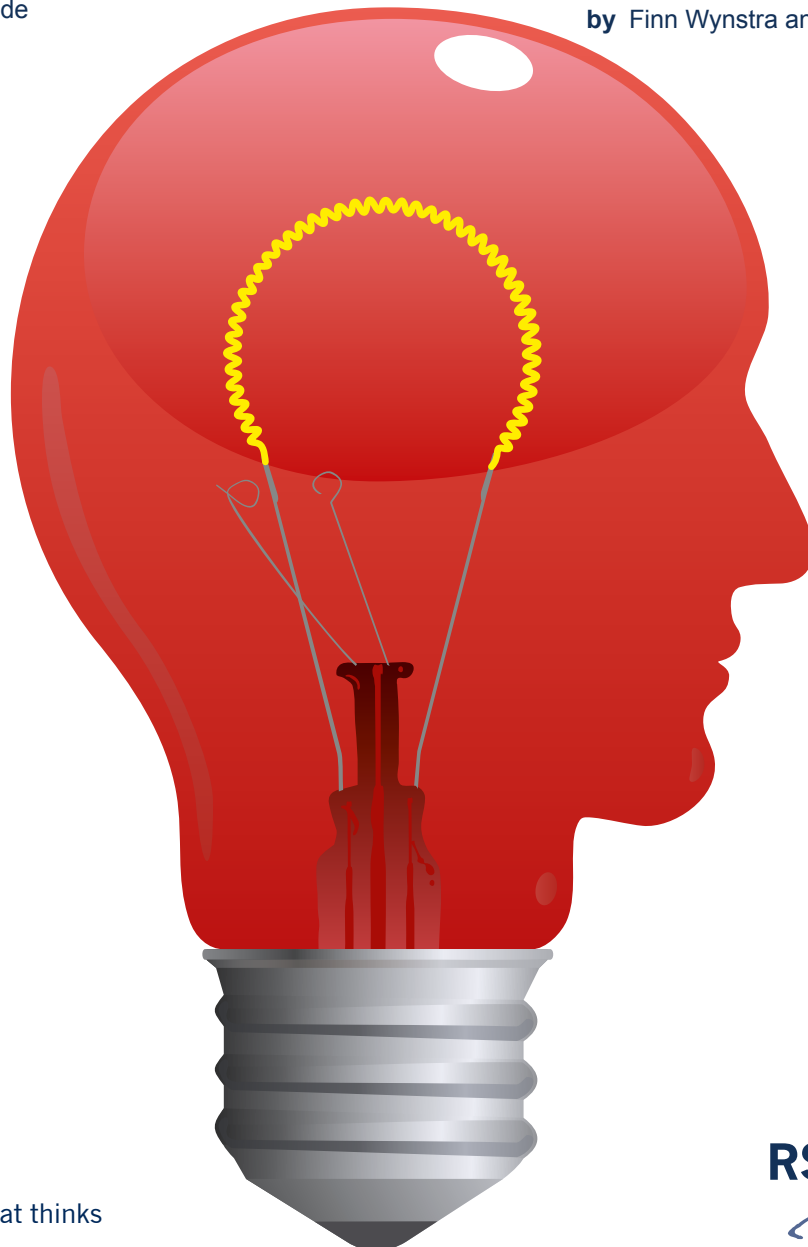
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The business school that thinks and lives in the future

Purchasing superior-value offerings effectively and successfully

By Finn Wynstra and James C. Anderson

In business markets price still plays a significant part in selling and buying decisions. Suppliers strive to get an equitable or fair return on the value of their offerings and buyers look for bargains and usually find them, thanks to over-eager suppliers. However, recent experiments show that there are other more effective and successful ways of selling without giving away too much value.

When selling superior value relative to the incumbent or next-best alternative offering, a supplier often tries to claim a portion of this by asking a price that is higher than either. At the same time, though, buyers' purchasing decisions are often based primarily on price, thus frequently tempting suppliers to give away some value to the customer – such as 10 per cent additional value for a price increase of only 7.5 per cent. One reason for this is that buyers may not be able to appreciate the superior value on offer. Another, more obvious reason is that discount or rebate giveaways are simpler and more concrete to comprehend, and come without risk to the buyer.

Although this is an essential part of customer-value management, remarkably little research has gone into understanding what would persuade business customers to purchase higher-value offerings that come with a higher-price tag – other than just a monetary give-away. In practice, suppliers competing at the high-end

with high-value offerings are not always good at demonstrating how this high-value they are selling could affect an individual customer. Instead these suppliers will focus, at best, on generic features and benefits.

To study the effects of alternative ways to promote high-value, high-price offerings, we conducted field experiments where we tested other key selling tactics to reduce “value ambiguity”. One such tactic is by providing “value evidence”, where suppliers document and demonstrate this superior value, and thus remove uncertainties and ambiguities in the minds of buyers. Suppliers can develop value evidence by conducting pilot studies of beta-test customers and documenting the results, or by using reference lists of key customers deploying this offering and related case studies. As the use of reference lists is obviously cheaper than conducting pilot studies with each new customer, it is useful to understand whether the first is equally effective in getting

customers to buy higher-value, higher-price offerings.

Realistic scenarios

We constructed 36 alternative-purchasing scenarios, built around the purchase of 10 KW/HP replacement motors. In each scenario, a manager has to choose a new motor from a selection of four products, varying in price and value. This choice is timely because, outside these scenarios, suppliers have actually started offering lines of premium-efficiency replacement motors. To simplify matters, the incumbent supplier always provides the incumbent (reference) offering, as well as the alternative products (this removes any ambiguity caused by having to change suppliers).

In addition to “value evidence” tactics, we introduced one other factor into our experiments: consequences of obtaining superior value. We studied this factor in two ways. First, by comparing the preferences of purchasing and maintenance managers, we were able to study the effects of functional responsibility. Second, in the scenarios we manipulated the kind of performance review and reward system in place (based on lower total cost of ownership, for example).

To help develop these experiments, we drew on past research in the USA and on two business roundtable



discussions with senior purchasing executives. These discussions were valuable in discussing the constructs and potential manipulations of them with purchasing executives from firms in a variety of business markets.

We conducted the experiments in the Netherlands and participants were purchasing and plant maintenance managers, who were also industry members of De Nederlandse Vereniging voor Inkoopmanagement (NEVI – Dutch Purchasing Management Association) and De Nederlandse Vereniging voor Doelmatig Onderhoud (NVDO – Dutch Maintenance Managers Association). Each manager, who could actually be responsible for acquiring such products for their company, was assigned one, randomly selected scenario for the experiments.

Focusing on value

Our experiments revealed that value evidence and incentive to change each received significant support as mechanisms to reduce uncertainty and ambiguity about superior value. There was strong empirical support that incentive to change operates as a threshold phenomenon. Suppliers are most likely to give away some of this incremental value to their customers (in discounts or rebates) as an enticement to select their offering over the incumbent supplier's or competitors'.

Such a give-away could be just the incentive customers are looking for, and thus warranted. However, the “give-away effect” is not linear. There is a threshold, beyond which buyers are indifferent to the incremental monetary incentives offered, and therefore there is no significant advantage to suppliers to give away more than that.

We also found that the results of pilot studies, when carefully designed and monitored, are effective in enabling suppliers and customers to identify the actual value in monetary terms buyers receive, such as lifetime cost-savings.

However, pilot studies (which involve financial costs to the supplier) were just as effective as creating reference customer lists, and documenting and developing related case studies as value evidence (low or no-cost alternatives). This should not come as a surprise. Customers often admire and respect some of their competitors, and having these respected companies as reference users can influence their own purchasing decision in a positive way.

Significant support was also found for performance review and reward. During the roundtables, one executive predicted that specific performance indicators and bonus targets would become increasingly salient for buyers. In fact, as management sees the need to measure the contribution suppliers and their offerings make in improving

the company's competitive advantage, buyers are coming increasingly under pressure to document all of this for evaluation purposes. In reacting to market and company demands, buyers are honing their purchasing skills and proficiency at making professional assessments of suppliers and the value of their offerings.

While no significant differences in purchase preferences were found for area of responsibility (purchasing managers versus maintenance managers), there is some indication that buyers in Anglo-Saxon economies, like the USA, are mostly interested in low-value, low-price offerings, unlike their Dutch counterparts, who were also interested in high-value, high-price ones. Perhaps this has something to do with looking at the bigger and longer-term business picture. In general, buyers from companies with a more strategic perspective on purchasing and supply management tend to look beyond short-term gains (such as price) and at the total cost of ownership, for example, making them more accepting of high-value, high-price offerings.

Key messages

While we must be cautious when using scenario-based experiments with purchasing and plant maintenance managers to generalise what occurs in actual business practice in diverse ►

Purchasing superior-value offerings effectively and successfully (continued)

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markets, several recommendations and observations can be drawn from our studies.

Looking at the consequences dimension, suppliers should be aware that in general customers are not primarily interested in low-price, low-

customer firms that embrace total cost of ownership as a business philosophy.

However, we direct our two main messages at suppliers. First, there is nothing wrong with suppliers giving away value to their buyers, but they should not overdo it because it is

greater value in exchange for supplier assistance in the data gathering and analysis as well as earlier access to these offerings. Additionally, suppliers can use the documented results to create reference customer lists and value case histories.

This leads us to a final piece of advice for suppliers: do not blame your customers if they tend to focus solely on price; after all, it is up to you to convince them otherwise. ■

“Purchasing managers are serious about quality offerings, even if it means a higher price.”

grade products. Although they are sceptical and critical of all offerings, even purchasing managers are serious about quality offerings, even if it means a higher price.

However, suppliers should also take into account the pressure purchasing and other customer managers face with performance reviews and rewards, and act accordingly. Customer managers reviewed and rewarded for staying within the established budget will likely have purchase intentions opposite to those reviewed and rewarded for lowering total cost of ownership. The former will pursue lower-value, lower-price offerings (as long as the offerings meet the minimum specifications); the latter will prefer higher-value, higher-price offerings. This suggests customer manager performance review and reward system as a segmentation variable, with suppliers targeting

not linear, which means that there is nothing to be gained beyond the critical threshold.

Second, suppliers should provide evidence of value through pilot studies, or even customer references and case studies, where possible, because these are the cheaper option. In fact, reference lists of respected competitors can be equally effective in persuading buyers to purchase higher-value, higher-price offerings. This suggests a two-stage strategy. Suppliers should conduct pilot programmes with beta-test customers to understand the value delivered by new or enhanced offerings. The results of the pilot programmes, when they are carefully designed and monitored, enable the supplier to document the actual value in monetary terms that the beta customers receive. Customers may be willing to cooperate in documenting the costs savings or

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