QDI Strategies

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20/20 Vision for Marketing Breakthroughs

Value from a Clearer Market Vision:

Tools to Capture Greater Profit and Share

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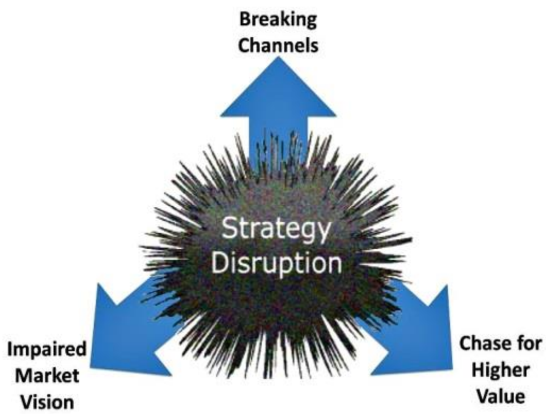
Rigorous Tools to Capture Profit and Share Opportunities

20/20 Vision for Marketing Breakthroughs

If you have been following the first four white papers in QDI's Market Disruption Forces and Strategies series, then you already know that forces exist that are breaking your channels and hindering your chase for higher value. Your ability to communicate and deliver value through your channels is at risk.



The following tools help you assess how your Designed and Perceived Value stack up against competition to enable you to see new profit and/or share opportunities. If you have taken a fresh look at your customers and distribution, this increased market insight has revealed one of the following value issues.

> *The following tools help you assess how you stack up against competition to enable you to see new profit and/or share opportunities.*

You need to increase the <u>Designed Value</u> you provide to your customers to win their business at the prices you desire.

Designed Value is the value <u>you plan</u> to deliver to customers. For example, in the automobile industry cars are designed to meet specific performance in crash tests standards. This is one element of the car's Designed Value. If the car does not meet the crash test performance criteria, then the engineers need to re-engineer the car to provide the Designed level of Value required by these tests.

Crash test performance is just one of the many value elements needed to provide overall customer value. For each of the performance elements that manufactures think is important to their customers, manufacturers need to meet a Designed Value level of performance.

Your Perceived Value is lower than it should be because the customer does not believe your value proposition.

Perceived Value is what the customer thinks he gets. For example, in the energy efficiency industry performance contracting has been around for years. However, many customers don't believe they will save as much as the vendors say. There are two reasons why the customer might not believe these savings projections:

1. The vendor has not effectively communicated the savings due to a lack of execution on the vendor's part
2. The vendor did not adequately design the offering to include the tools and processes that would enable the customer to prove that the savings are real

> *You can't capture the value you create if you can't clearly define that value and be sure it is superior to the customer's alternatives.*

In either case, the customer's perception of value will be less than the supplier had designed. One of the key questions for marketers is, "Which of the perception problems do I have?"

- Am I not effectively communicating my value?
- Have I not understood the customer well enough and therefore designed a value proposition that he sees as inferior?

Creating value requires designing products and services that provide customers value that is superior to their alternatives. Capturing value requires presence to your target customers, effectively communicating your value proposition, and then using pricing and your marketing programs to seize the economic value.

You can't capture the value you create if you can't clearly define that value and be sure it is superior to the customer's alternatives. In this white paper QDI introduces tools you can use to define and quantify your Designed Value and measure your perception of your Designed Value versus competitive alternatives.

In the marketplace, the only perception that matters is the customer's. As marketers we have to make decisions based on our own perceptions of how customers behave, what is important to them, and how they perceive our offerings and the offerings from our competitors. As we have discussed in previous white papers, the closer your perception is to market reality, the better decisions you will make.

Regardless of the quality of your perception, you have to make decisions. These tools will help you define and quantify your Designed Value versus competitive offerings.

You can use these tools with your internal marketing and sales teams to define and assess your value in product planning exercises. For sales organizations, learning how to increase the value customers perceive drives improvements in pricing (you don't leave money on the table), in marketing (clarity in the value you communicate), and in sales (closing with the right value proposition).

Value is about perception

The ultimate judge of your value is the customer. Thus, you need to strive to see value through his eyes.

Perception, what the buyer thinks, determines your value in the market. While most buyers do not have a formal scale to measure value, more and more buyers are moving in this direction. In addition, Quality programs implemented throughout the industry are focusing more and more on the "total cost," which looks at both the hard and soft costs and benefits of doing business with fewer suppliers. Likewise, more and more sales forces are teaching their salespeople how to sell the "total value" or "value-add" that they supply in the way of services and relationships.

> *The value the customer perceives is not only a function of the product, but also of the services associated with that product and the relationship/trust the customer has in the product and the supplier.*

Therefore, you also must see value from the customer's perceptions. Often the value he perceives is not only a function of the product you offer, but also of the service associated with that product and the relationship and trust he has in the product and his supplier. Accordingly, you need a more inclusive definition of value.

QDI's Creation Value Formula provides a framework for quantifying the total value customers perceive from your offering versus competitive offerings. The value a customer perceives is a function of his perception of benefits and costs**.**

$$\boxed{Value_P = B_P / \$C_T}$$

- **Benefits**
  - Product / Service
  - Service – ETDBW - Responsiveness
  - Relationship
  - Brand
- **Cost**
  - Purchase price
  - Buying and adoption cost
  - Risks

For each specific customer segment

The "Benefits" and "Costs" tables below show these value elements in more detail.

Benefit Components: The benefits a customer perceives reflect the product(s) he receives from you, the services he gets, and the relationships he has with people in your organization. In addition, the image that your brand portrays can be a benefit to the customer. Specifically, we define these components as:	
Product/Service	Functionality, fit (ease of use and adaptation), and form (ease of replacing the present product, service or function)
Service	Service ease of doing business together - service quality. Service empathy - customer perception that someone cares
Relations	Personal linkages to the supplier
Brand	The fit of your brand image with the customer's perception of risk and product suitability, i.e. are you a reliable supplier, and a leader in this product class.

Cost Components: The cost components include all the cost the customer incurs to do business with you. As such, some of these costs are represented by payments to you, some are represented as expenses within his business, and some of the costs are the risks he perceives in doing business with you. Specifically, the cost components are:	
Product Cost:	The amount the customer pays for the product, including special terms, delivery, etc.
Purchase and Adoption Costs	The cost the customer incurs to purchase, handle, store, own, and use your product. This includes all the traditional ownership costs as well as handling cost and adoption costs. The adoption costs include training, engineering, design, and installation that are associated with your product, particularly when they differ from other options.
Risk Cost	These costs are a function of the customer's risk tolerance and his perception of the costs and likelihood of problems related to your product. A simple example of risk cost would be the purchase of a PC. What is the risk of buying an off-brand of PC from a mail order house versus IBM, DELL or Compaq? What could possibly go wrong? What would these problems cost you? What is the likelihood that this could happen? Is this cost greater than the price difference between the off-brand and branded options?

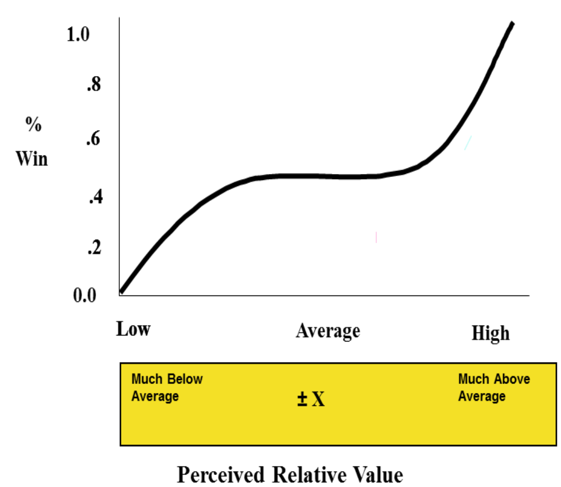
QDI's Value Creation formula looks at the drivers of customer value – the elements that define value and those that define costs. Using this formula you can calculate a Total Benefits score and a Total Costs score for your offering and competitive offerings.

You can translate these Benefits and Costs scores into a Relative Perceived Value score by comparing your score to your competitor's scores. Again, we need to reinforce the idea that these scores are your perception of what customers think. Once you have completed this exercise, you can test your assumptions in the market by tracking your performance or with research that is designed to specifically measure the value customers place on each of the benefit and cost criteria that you have built into the model and how they score you versus competition.

The concept of "close rate" represents the results of the customer's decision-making process. Close rates for a specific customer sale are either (1), a sale, or zero (0), no sale. The vertical axis represents the Close Rate, which ranges from 0 to 1.0 (or nothing to 100% of the time). This is a measure of how often you win the sale when presented.

Creating superior perceived value for the customer "wins" the business, resulting in a higher Close Rate

Close Rate



From our experience, this is a percentage that sales organizations can estimate. If you ask, they will tell you what percent of the time they win the sale when they are competing for the business. This number is often relatively close to what we find when we do research, however, it only relates to the sales transactions where your sales force is present. Much of the sales you lose were not presented to the customer, either because a third party was selling your product or because no one was offering your product at that sale.

As the chart above shows, the greater the Relative Perceived Value of an offering (which is shown on the horizontal axis), the higher the probability that the Close Rate will be a score of one (1). Over several transactions this probability becomes the percentage Close Rate for a specific competitor or offering.

The shape of the curve shows that if preference for your offering is low, then your close rate will be low. As preference increases, your close rate increases. It is important to understand that this relationship is not linear. Thus, your close rate does not go up proportionately for every point of increased Preference. The reason for this is that the consumer / buyer does not distinguish that precisely between offers. There is a great deal of inertia around his existing product or supplier he purchases from. Therefore, the "Close Rate Curve" goes flat when decision makers view products as about equal.

To improve close rate, the marketer needs to work on his value proposition as well as his channel's ability to communicate the value. Having a great value alone will not generate a great close rate.

How to Measure Value

The value assessment tools below are based on QDI's Value Assessment Workbook, which helps sales and marketing teams quantify their internal perceptions of the value they and their competitors provide customers.

QDI's VALUE ASSESSMENT WORKBOOK

The starting point is what you think the "Designed Value" is that you and your competitors provide.

Sales and marketing teams use the workbook to rigorously structure the product's Designed and Perceived Value versus competitive alternatives.

The VALUE ASSESSMENT WORKBOOK leads your through two exercises. The first is to define the value that each competitor creates (Designed Value) which includes the value criteria and value scores for each competitor. Do this by:

- Defining the BENEFITS customers receive
    - Defining the individual criteria that determine the BENEFITS that you provide to customers
    - Weighting the relative importance of each of these BENEFIT criteria
    - Scoring your performance versus your competitors on each BENEFIT criteria
- The second is to define the COST criteria and score your company versus your competitors
    - Defining the individual criteria that determine the COSTS that customers incur in purchasing this type of product
    - Weighting the relative importance of each of these COST criteria
    - Scoring your performance versus your competitors on each COST criteria
- In this exercise you are quantifying what you believe to be the "Designed Value" that each competitor in the market offers.

The second exercise is to quantify your Close Rate. This exercise:

- Translates the competitive benefits and costs scores into a set of Perceived Value Scores for each competitor. (Perception here is your best effort at estimating customer perception. This score is not their real Perceived Value score unless you have measured customer perception using the benefit and cost criteria and weights you have built into the value model.)

- The Close Rate Calculator then quantifies your Close Rate based on the number of competitors that are present at each sale.

Your Value Creation

QDI's Value Assessment Workbook helps marketers clearly define the elements that they believe drive customer value. The Benefits Calculator worksheet that is shown below asks the marketing team to define and quantify the benefits they believe the customer perceives in each of the four benefit categories. The discipline of clearly stating the importance of each category, benefits, the weights of the benefit, and your performance scores are the bases of the DESIGNED VALUE you deliver to customers. The insight that results from scoring your competitors' performance forces clarity in your pricing, marketing, or sales programs.

Benefits Category and Criteria Detail	Category Importance (Allocation of 100 Points)	Item Benefit Description - Detailed Description of Why This Is a Benefit and Quantification of Its Value	Benefit Criteria Weight (Allocation of 100 Points Across Detailed Benefits in Each Benefit Category)	Relative Performance (1 - 10 Scale where 10 is Best)			
Product				YOU	Competitor 1	Competitor 2	Competitor N
Detailed Product Benefit 1							
Detailed Product Benefit .... N							
Service							
Detailed Service Benefit 1							
Detailed Service Benefit .... N							
Relationship							
Detailed Relationship Benefit 1							
Detailed Relationship Benefit .... N							
Brand							
Detailed Brand Benefit 1							
Detailed Brand Benefit .... N							
Total Benefits Score							

The worksheet asks the team to:

1. List the benefits they think customers want in the BENEFIT column.
2. Allocate 100 points across the four benefit categories to weigh their relative importance to this customer segment in the CATEGORY IMPORTANCE column.

3. Define, in as much detail as possible, each specific benefit in the DESCRIPTION column. For example, in the product benefit column, you would list the key functional benefits the customer gets from the product or service you are marketing. In the service category, you may list “ease”.
4. Allocate 100 points across the criteria in each benefit category to weigh the relative importance to the customer of each criteria of doing business” or “speed of response” as key benefits in the BENEFIT CRITERIA WEIGHT column.
5. Score the performance you think you and your competitor deliver on each criterion in the Relative Performance Columns.

QDI’s Value Assessment Workbook leads your marketing team through a similar analysis of TOTAL COST your team believes the customer perceives he will incur with each competitive offering. Again, the accuracy of the Perceived Value Score is a function of your input data. If you have used customer inputs, your scores will be more consistent with what customers perceive. If not, the scores are your best estimates of customer perceptions.

Using these two scores BENEFITS and COSTS, the workbook calculates a Perceived Value score for each competitor (Value = Benefits / Costs).

QDI uses a proprietary formula to compute relative scores but for the purposes of this exercise simply divide your total value score by the sum of all the competitors (including your own) value score.

These Perceived Value Scores are then used to calculate a **CLOSE RATE** score for each competitor. Your CLOSE RATE is a measure of how successful your sales channels will be when they and their competitors effectively present their individual value propositions to customers. If your channels or your competitors fail to effectively communicate their value to customers, this will negatively impact their CLOSE RATES.

The Impact of Value

Now compare the calculated close rate with the close rate reported by the sales organization (either via your CRM system or anecdotally). This is a starting point to assess how well you are capturing the value you have designed into your offerings.

Using QDI's Value Assessment Workbook, you have now clarified and quantified the Designed Value you think you provide to customers. You now have a very solid benchmark to use to answer three key questions:

- **Are you leaving money on the table?**
    - Is the Designed Value you offer significantly greater than competitive alternatives?
        - Can you raise your prices?
        - If so, how much?
    - Or have you used your value advantage to maximize share? Are you capturing share equal to the value you are giving away?

- **Are marketing and sales clearly communicating the Designed Value?**
    - If the Designed Value you think you deliver is generating a higher CLOSE RATE than you actually achieve in the market, you may be failing to communicate this value.
        - Is this lack of communication making it more difficult to sell to a specific segment or gain the support of a specific influencer?
        - Do the marketing communications give the same weighting to each benefit that the team scored their relative importance? Does this lack of clarity

Clarity in how your Designed and Perceived values compare versus competitive alternatives will drive improved pricing, more effective marketing, and higher Close Rates.

hurt your close rate? Is this communication failure costing you pricing power?
        - How effectively are your channels communicating your value?
    - If the calculated close rate is less than your actual close rate you may have other problems:
        - Is your sales force using price instead of value to close the sale?
        - Have you misrepresented what customers value in your model?

- **Have you over-estimated your Designed Value?**
    - Are your benefits actually less valuable than you believe they are?
    - Are competitive offerings more valuable than you think?
    - How does your total cost versus competitors compare?
    - How does your brand score compare to competitors?
    - What must you change to establish superior value?

When trying to increase the value they offer, the issue for decision makers is to identify what part of the value equation they should fix. Should they increase benefits? Should they reduce costs? What can they do most effectively? The trap most marketers fail to consider is the interdependency. For example, downsizing reduces internal costs and allows a manufacturer to decrease prices to his customers. This reduces the customer's cost and increases his perceived value of the supplier's products or services. However, downsizing often also reduces the benefits, making it harder to do business with the supplier, disrupting long-term relationships and, therefore, reducing value to the customer.

The question in cutting internal costs is simply, "Will this change reduce or increase the value the customer perceives? And, will it change the value positively enough to change the customer's behavior?" The answer to these questions comes from an in depth understanding of the customer's perception of value.

If you are interested in QDI's Value Assessment Workbook, or assistance in capturing more of the value through pricing, share growth, and lower costs, contact QDI Strategies at the number below.

Where Clients Ask QDI for Help	
New Products / New Markets	Develop market insight to <u>speed</u> launch and ramp-up while <u>reducing the risks</u>
Channel Issues	Provide <u>clarity</u> regarding conflict, performance, and go-to-market options
Share Growth	Discover market drivers and determine <u>strategy opportunities</u>

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