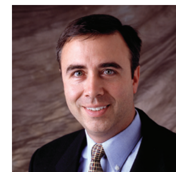
Service Management Report

A QUARTERLY E-NEWSLETTER FOR THE SERVICE EXECUTIVE • VOLUME I • SPRING 2007



Ask the Expert

Mike Landry, **Founder and Chief Technology Officer, Servigistics**

Why are leading companies now investing in their service businesses?

If service is important, why are processes still spread across disparate functions, essentially hampering service's success?

Why is service parts pricing gaining increased executive attention?

Do you have a service related question for Mike? If so, send it to him at asktheexpert@servigistics.com and it could be included in a future version of Service Management Report.

Q: Why are leading companies now investing in their service businesses?
A: Over the past year, we've conducted focus groups with executives from companies across diverse global industries during which we identified the following drivers of increased investment in service businesses:

- **Product Commoditization**: Shorter lifecycles, globalization, cost pressures and intense competition are making it increasingly difficult for manufacturers to remain competitive through product differentiation alone. Increasingly, service and support delivered after the sale serve as the drivers of revenue and customer loyalty rather than the sale of the product itself. As a result, forward thinking companies are investing in post-sales service as a source of competitive differentiation and customer intimacy.

- **Diminishing Product-based Margins:** While product-based margins diminish in maturing industries such as high tech, aerospace, motor vehicles and consumer and industrial products, service margins remain very healthy. In fact, in some sectors, service margins can be 30 to 200 percent greater than product margins. As a result, leading companies across diverse industries are investing in service as a new source of profit, demonstrating the power of service as a growth driver.

- **Lack of Service Technology Infrastructure**: Service-led growth requires effective collaboration across functions, new decision-making capabilities and the underlying integrated service technology infrastructure to support those processes – an approach the market is now referring to as Strategic Service Management. Executives who understand the power of this integrated approach are fundamentally shifting the way they view their service business. Rather than viewing it as a cost of doing business, they're viewing it as key profit driver and source of competitive differentiation

Q: If service is important, why are processes still spread across disparate functions, essentially hampering service's success?
A: Strategic Service Management is in its early stage of adoption, similar to other waves of business process transformation. Look at SCM, ERP, CRM – all of which began as disjointed business processes that were eventually integrated through the adoption of an underlying technology infrastructure.

Service is no different. The complex nature of post-sale service makes it very difficult to implement and sustain business transformation without the use of an integrated service technology infrastructure. Until recently, this technology was not

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Ask the Expert (continued)

available and line-of-business owners and CIO's were forced to "get by" and simply stitch together disparate service solutions and ERP functionality, which resulted in sub-optimized processes and value capture.

Leading companies increasingly understand that a fully integrated approach to service can be achieved only through a strategic service management solution — one that enables the integration, optimization and efficient management of their core service business processes. These include: service resource planning, customer commitment management, service partner management and service pricing management.

Q: Why is service part pricing gaining increased executive attention?

A: The reason is simple: Price increases usually reach the bottom line in one piece while the advantages of lower unit costs or higher sales volumes are diluted. Thus, for a company with 10 percent margins, a 10 percent price increase could produce a 100 percent increase in profit. While the process seems simple, less that 20 percent of companies are confident their current service parts pricing methodology is maximizing service parts revenue and gross profit.

According to a recent *Wall Street Journal* article, many U.S. manufacturers have struggled to raise product prices amid the growth of global competition and cost-cutting drives among customers. This has negatively impacted revenue and profits for U.S manufacturing, which contributes 12 percent to the U.S. gross domestic product.

In response, OEM's are around the globe are frantically searching for new profit opportunities and are finding them in unusual places – massive warehouses located around the world that house millions, or in some cases billions, of dollars in service parts. It's not common knowledge, but many manufacturers earn a significant amount of their revenue - not on the initial sale of their products - but on the service and parts they sell after the sale. Today, a surprising number of companies determine the price of their service parts through the use of a sub-optimal, "cost-plus" model for pricing service parts and miss significant revenue and profit opportunities. Cost plus methodologies derive price points by adding a percentage markup to the cost of every part. This is typically done with no regard for competitive prices or price elasticity, resulting in missed revenue and profit opportunities. Aberdeen Group recently uncovered the significant profit opportunities related to service parts pricing in a benchmark report titled Maximizing Profitability with Optimized Service Parts Pricing.

The Servigistics Pricing Solution enables companies to increase revenue and maximize service profitability through the management and optimization of service parts prices. The solution combines patented pricing methodologies, advanced optimization techniques and market adaptive business logic to provide service, finance and marketing professionals with the decision support information and tools required to capitalize on high-margin business opportunities.

The award winning and patented Servigistics Pricing is proven to help companies increase service and parts revenue 5 to 15 percent. With Servigistics Pricing, companies optimize prices based on competitive data, customer reaction to price changes, and part availability information. The Pricing Solution uses software, content and expertise to develop the best service parts pricing approach for your company.