Logistics and Customer Service in the Hospitality Industry

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Abstract

This article evaluates the statement that companies may increase efficiencies and profitability by segmenting their customer base in terms of importance, for the purpose of providing specialised services. We specifically refer to how customer segmentation compares to basic service as proposed by Bowersox and Closs and discuss the advantages and disadvantages of the basic service approach as well as the factors which have contributed to its success. We also discuss the background and current state of the customer service environment and provide an opinion of which approach to customer service is preferable.

INTRODUCTION

Terminology

Customer service is defined as a process for providing significant value-added benefits to the supply chain in a cost-effective way (Bowersox & Closs, 1996:66).

Basic service approach to customer service is the provision of a standardised service offering which is based on a specific level of availability, operational performance and reliability which is provided to all customers. (Bowersox & Closs, 1996:74)

Customer segmentation in a logistics context is the segmentation of customers into distinct groups, which are differentiated in terms of profitability, for the purpose of providing the appropriate level of service to each customer and to provide key customers with specialised services (Cottrill, 2007:9).

Trends in the Customer Service Environment from a Supply Chain Perspective

The purpose of this section is to give an overview of certain trends and issues that affect customer service in practice, from a logistical perspective. These issues are being discussed separate from the points to follow as they pertain to both basic service and customer segmentation. An important aspect of customer service is that the organisation’s customer service strategy must be aligned with organisational policy and goals in order to be successful.

There are many trends which are changing the way in which organisations are conducting their operations. In this section we will briefly discuss the main trends and changes which are taking place. Many of these trends are the result of the transition from an industrial to an information technology driven society. These trends will give us insight as to how logistics operations are changing, and if interpreted correctly can result in a competitive advantage for a firm (Bowersox, Closs & Skank, 2000:3).

Customer Service to Relationship Management

According to Bowersox and Closs (2000: 3); leading firms increasingly recognise that success hinges on establishing intimate relationships with key customers. This trend emphasises a movement towards more closely linked relationships with customers, allowing firms to provide customised levels of customer service. All customers do not have the same
service expectations and do not necessarily want or deserve the same overall level of performance (Bowersox et al., 2000:3). This statement further emphasizes the need to move from a transactional view of dealing with customers to a relationship based arrangement in order to better understand customer requirements. This will enable the organisation to anticipate and meet specific customer requirements as efficiently and effectively as possible.

Adversarial to Collaborative

The conflict between buyers and sellers arises as each party wants the best financial deal, and neither party trusts the other. This results in a highly inefficient supply chain. Collaboration results in a potentially vast increase in the efficiency of the supply chain as a result of decreased work duplication and redundancy. (Bowersox et al., 2000:4). Collaboration follows on from the previous point of relationship management, as relationship management is required to maintain supply chain collaboration.

Forecast to End cast

Many firms continue to forecast activity levels and events that other participants in the supply chain already know. (Bowersox et al., 2000:5). This issue follows on from collaboration, in that through collaboration and information sharing this inefficiency can be avoided and an overall supply chain policy can be developed that aims to improve the customer service given to the end consumer.

These trends seem to indicate that there is an overall shift from using an undifferentiated service approach on a transactional basis to customer segmentation and the use of a specialised service approach, as the move toward relationship management, collaboration and information sharing suggest.

Third Party Logistics Service Providers

A third party logistics provider (3PL) is a firm that provides logistics services to companies for part, or sometimes all of their supply chain activities. This process is known as outsourcing. Third party logistics providers specialise in integrated warehouse and transportation services that can be scaled and customised to meet customer requirements in terms of inventory availability, order cycle time as well as any specialised activities which may form part of the organisation’s operations (http://en.wikipedia.org/wiki/3pl).

The question must then be asked; why would a firm consider outsourcing? Some companies simply lack the expertise and ability to perform the logistics activities themselves. In this case the organization would more than likely choose to outsource its logistics functions to a 3PL. 3PLs allow firms to focus on their core competencies as the following example illustrates. Phoenix Brands has decided to outsource its transport and inventory activities to a 3PL, leaving their own management free to focus on manufacturing and marketing. Phoenix Brands, a consumer goods company is now able to maintain competitive levels of logistics service while focusing their resources on maintaining high levels of quality in their core functions. 3PLs also provide Enterprise Resource Planning (ERP) systems which allow the organisation to better collaborate and share information with its customers, enabling the firm to have access to relevant information on a real time basis for planning purposes (Macdonald et al., 2007:19).

The advantage to an organisation making use a 3PL is based on two characteristics of 3PLs; (1) 3PLs’ specialization in there respective areas of expertise, and (2) from their ability to achieve economies of scale in areas were a single firm would not have sufficient demand to achieve such scales. 3PLs are able to support both basic service and value-added service by providing specialised services to organisations according to their customers’ requirements, which results in effective customer service and a reduction in the cost of operations.

Fourth Party Logistics Service Providers

A further development in the evolution of the outsourcing process is the fourth party logistics service provider (4PL). The convergence of technology and rapid acceleration of capabilities have heightened the need for a overarching integrator for activities which span the entire supply chain (Kivinen & Lukka, 2000:23). This development gives rise to a new player in the supply chain, someone who has the knowledge, experience and expertise to oversee and coordinate the whole supply chain as one flowing unit.

Comparison of Basic Service and the Customer Segmentation Approach

Basic Service
Basic service addresses all aspects of customer service. To implement a basic service platform, it is necessary to specify the level of basic service commitment to customers in terms of availability, operational performance and reliability. The level of basic service that needs to be provided is related to the firm's overall marketing strategy and elements of the marketing mix which aim to achieve the organisation's long-term strategic goals (Bowersox & Closs, 1996:74).

Basic service is the minimum level of support provided to all customers which stresses that a firm should not deliberately violate its program by offering unique services or limiting service to selected customers. The critical decision lies in selecting profitable customers and to avoid providing a lower basic service to marginally profitable customers. (Bowersox & Closs, 1996:74)

Basic service must be implemented at least cost in order to increase the profitability of the organisation’s operations. If price is the main competitive feature in the market then firms should seek to differentiate themselves in terms of the value and quality of the services they offer and create competitive advantage through value creation (Bowersox & Closs, 1996:74). One of many examples of how firms could differentiate themselves from their competitors is through the provision of reverse logistics. Customers on average return about 6% of everything they buy. Firms need to consider this dimension of service when establishing a basic service level (Jayaraman, Vaidyanathan & Luo, 2007:56).

In order to be able to improve or maintain high levels of basic service quality, measurement of different basic service elements is critical.

The first element of basic service is availability which is the ability to have inventory when required by the customer. The attributes used to measure availability include aspects such as stock-out frequency, fill rate and orders shipped complete. Stock-out frequency is the probability that a stock-out will occur and the amount of times that demand exceeds product availability. Fill rates measure the impact and magnitude of stock-outs over a period of time. Orders shipped complete refer to how many times all the inventory that a customer has ordered is available (Bowersox & Closs, 1996:67-70).

The second element of basic service is operational performance involving aspects such as speed, consistency, flexibility and malfunctions/recoveries. Speed is the elapsed time from when order is placed until shipment arrival. Consistency is the firm's ability to perform at the expected delivery times over various performance cycles. Flexibility refers to the firm's ability to handle extraordinary customer service requests. Malfunctions will occur in the basic service program and firms will need programs to prevent and accommodate these special situations (Bowersox & Closs, 1996:70-71).

Reliability is the third element of basic service and looks at the ability to comply with levels of planned inventory availability and operational performance. The key to achieving logistics quality is measurement. The three aspects of measuring service quality include measurement variables, measurement units and measurement bases. Measurement variables are performance activities that represent items to be measured such as sales, orders and stock-outs measured over various periods. Measurement units are the selection of unit measures such as cases, units or dollars, for example to track and report stock-outs in both numbers of units and inventory dollars. The final consideration is the selected measurement base which defines how performance reporting is aggregated. (Bowersox & Closs, 1996:71-74)

Stock & Lambert (1993:102) suggest that it is essential that a firm adopt a customer service strategy that is based on customer needs, is consistent with overall marketing strategy, and advances the organisation's long-range profit objectives.

Cost/Revenue Trade-Offs can be use as a tool to determine how a change in customer service level affects profitability in terms of sales volume and cost (Stock & Lambert, 1993:105).

A Customer Service Audit is a critical method of obtaining information that firms can use to their advantage to develop or improve their basic service strategy.

The External Audit identifies elements customers believe to be important, how they perceive services provided by major vendors and which service variables are most important such as order cycle times, flexibility or orders shipped complete. This information is important in determining the base level of the basic service program in order to develop the program around customer expectations. (Stock & Lambert, 1993:110-111)
The Internal Audit will involve reviewing the firm’s current operations, by interviewing managers, in order to serve as a base for determining the firm’s internal level of performance and comparing it to the customer’s perception of service being provided. Managers will identify inconsistencies between service performance and customer perceptions from the obtained information in order to align the firm’s operational performance and customer perceptions (Stock & Lambert, 1993:117-118).

The next step of the Customer Service Audit would be to identify potential solutions, by comparing the firm’s own service performance levels with competitors (competitive benchmarking) and positioning the firm’s services in the market accordingly in terms of the relative performance and importance of specific operational variables (competitive position matrix and performance evaluation matrix). Firms must identify and take advantage of strategic opportunities which will be identified through this process (Stock & Lambert, 1993:118-124).

The final step is then to establish customer service levels which include setting standards, maintaining on-going performance measurements, communicating with all the employees responsible for implementing the customer service program, as well as establishing formal reporting structures to alert top management of any deviations from the set level of performance (Stock & Lambert, 1993:124).

Dell makes use of a high performance basic service program with an obsessive adherence to a clearly defined strategy and unwavering commitment to core values. Dick Hunter, vice president of Dell Americas Manufacturing and Distribution Operations, views Dells supply chain efficiencies as one component of a perpetual success engine which allows them to pass savings on to customers which drives demand and market share and subsequently helps suppliers drive their business (Hunter, 2005:34-39).

CUSTOMER SEGMENTATION

The aim of logistics is to satisfy the needs of customers. Business logistics contributes to an organisation’s success by providing customers with timely and accurate product delivery. Some argue that in order to meet that objective it is important to segment a firm’s customers. The marketing concept holds that to achieve organisational goals depends on determining the needs and wants of the target market and to allocate resources to meet those needs more efficiently and effectively than competitors. Thus the key strategic objective of the marketing function is to penetrate the identified market segments in order to generate profitable transactions for the firm’s long term wellbeing (Linford, 2003:37-38).

The process of customer segmentation may involve segmenting the market into different industries if the organisation’s customers are spread across diverse industries, for example the pharmaceutical industry; the automotive industry and the fast moving consumer goods (FMCG) industry. Performance indicators for each industry are then identified, for example, for the pharmaceutical industry a firm could focus on the following key performance areas: cold chain management for temperature sensitive medicines; batch trace ability and sensitive reserve logistics and disposable procedures. If the industry segmentation approach is followed then these industries are then further segmented into customer groupings that are characterised by similar requirements. Typical customer segments for the pharmaceutical industry include wholesalers, private hospitals and pharmacies (Linford, 2003:37-38). If the industry segmentation approach is not followed then segmentation will take place at the customer level.

A useful method to segment one’s customers is the ABC analysis, which is used to classify customers into different categories of profitability. The outcome of this method is for the firm to identify the most profitable customers in order to provide higher levels of customer service to those customers. The ultimate aim is to encourage repeat business from the customers that receive this higher level of commitment (Linford, 2003:37-38).

Each of these customer segments will have different service requirements, which will result in a differentiated customer service offering. These offerings will in turn enable a firm to differentiate itself from its competitors but more importantly help it provide specialised or value-added services to these segments (Linford, 2003:37-38).

Value-added services can be defined as additional services which are offered over and above the organisation’s basic service offering that brings added value to the total customer relationship and strengthens the revenue stream for both customer and supplier, thereby encouraging repeat sales and driving
purchases of additional products and services (Anon, 2002:16). When firms make use of the value-added service approach it is imperative that they do not treat all customers the same and therefore they must establish and understand the requirements of the different customer segments in order to design a service offering that matches the customer's requirements (Linford, 2003:37-38).

Five primary performance areas of value-added services that have been identified include:

Customer-Focused Value-Added Services offer buyers and sellers alternative ways to distribute their products using third-party specialists (Bowersox & Closs, 1996:80). Northern Telecom's customers now want them to inventory products, give them visibility to see the inventory so they can allocate against it, pick product, merge it with other equipment, label it the way they need it to be labelled so that it looks like its coming directly from them and also to comply with the recipients labelling requirements. All of these are performed by a third-party logistics provider, USCO Logistics Services Inc. (Harrington, 1998:52).

Promotion-Focused Value-Added Services involve the assembly of point-of-purchase displays coupled with a wide variety of other related services aimed at stimulating sales (Bowersox & Closs, 1996:80). Procter and Gamble holds promotions at supermarkets and convenience stores with price incentives that take the form of price promotions and discount coupons distributed by mail or in store (Barret & Steinert, 2004:62).

Manufacturing-Focused Value-Added Services involve unique product assortment and delivery to support manufacturing. Cross-Dock facilitator services provide advanced shipment notification, mixed store ready pallets, and enable precise delivery times (Bowersox & Closs, 1996:80).

Time-Focused Value-Added Services involve using specialists to sort, mix and sequence inventory prior to delivery. Exel Distribution mixes food manufacturer products to exact assortment required by retail food stores (Bowersox & Closs, 1996:81).

Basic Services Specialists may be used to provide day-to-day execution of all or part of a firm's customer service program. Roadway Logistics Service functions as a third-party service provider for Libbey-Owens-Ford Glass (LOF). Not only does Roadway perform transportation services and arranges for other carriers to handle segments of LOF's freight, but it also facilitates necessary administration and carrier payment using still another specialised service provider Cass Logistics Inc. (Bowersox & Closs, 1996:82).

From the above definition and the five primary areas it is clear that value-added services are customer-specific and involve the sharing of information between the company and the customer in order to successfully satisfy the customer's requirements.

Once a firm has segmented its customer base it is essential to collaborate with those customers in order to work toward a mutually beneficial relationship. According to Wadhwa, Khanda, Bhoon & Bibhushan, 2006:28; some of the benefits associated with supply-chain collaboration include:

- A reduction in inventory and personnel which results in a decrease in the associated costs.
- Better delivery performance through reduced cycle times.
- Increased sharing of information, ideas and technology allows the firm to increase the speed with which its new products reach the market.
- Collaboration with customers can result in a competitive advantage by allowing a firm to focus on its core competencies as a result of increased information sharing, which serves to strengthen the trust and interdependence between a firm and its customers. All of this helps the firm to focus on working toward goals of the supply chain and not individual companies.

All of these factors allow a firm to provide improved customer service.

Whilst the customer segmentation approach enables a firm to match service levels with its various customer segments, allowing it to allocate resources more effectively as well as maximise profitability, there are some disadvantages to this approach (Cottrill, 2007:9).

- There may be a reluctance to share information between companies in the supply chain for strategic competitive reasons (Cottrill, 2007:9).
- Inability of the firm's managers to reach a consensus with regard to the service levels provided to each
Providing value-added services results in the increased complexity of operations.

- The firm needs to understand and be prepared to go beyond its basic service to create customer satisfaction and facilitate long-term success. This requires a significant overall commitment that many firms may not be willing to take due to the associated risk and high investments (Bowersox & Closs, 1996:87).
- The costs of servicing small segments increases due to less opportunity to consolidate logistical volume for cost control. (Bowersox & Closs, 1996:64)

Given the discussion above, it is necessary to compare basic service to customer segmentation in order to determine the fundamental similarities and differences between them.

The basic service program is designed to meet specific customer requirements for low-cost, high quality, high volume product provided with minimal service and customer support. Basic service drives out cost and can improve the firm's profit margin by allowing a firm to standardise its products and services. Due to this standardisation, costs can be minimised as specialised service offerings are not offered to individual customers. With the basic service approach firms can provide a more predictable cycle time. Firms can also take advantage of consolidating volume, thereby reducing costs (Shulman & Allen, 2007:3-4). The customer segmentation approach is more complex than basic service as it is customer specific. This results in higher costs related to reduced batch sizes and specialised packaging and delivery circumstances as unique services are provided to different customers with unique requirements. Firms that offer value-added services therefore need to be flexible in terms of their operations, strategies and customer service decisions if they wish to successfully fulfil the objectives of the customer segmentation approach (Shulman & Allen, 2007:6-7).

The similarities between the two approaches are that they both aim to increase the profitability of the organisation by increasing the efficiency and effectiveness of operations. Both approaches aim to structure their operations to provide a product offering that meets their customers' requirements better than competitors in order to gain a competitive advantage.

Advantages and Disadvantages of the Basic Service Approach

Advantages

Standardisation of the Logistics Configuration

The use of a basic service approach to formulate a customer service strategy enables the organisation to devise standard operating procedures concerning activities such as transportation, warehousing and manufacturing. According to Dick Hunter (2005:34) vice president of Dell Americas Manufacturing and Distribution Operations, standard configurations keep costs low and enable Dell to forecast demand more accurately.

System-Wide Measurement and Improvement is Possible

A basic service approach requires an organisation to have standard performance measures in place in order to establish performance levels according to customer requirements as established by the Customer Service Audit (Stock & Lambert, 2001:110). This allows for a system-wide approach to measuring and reporting on the level of service being provided by the logistics operations of the firm. Being able to control performance on a system-wide level allows for problems and deviations from the set standards to be discovered and rectified and for costs to be controlled. Operational improvement initiatives as well as cost saving programs can also be implemented system-wide as a result. Procter & Gamble has implemented multi-echelon inventory (MEI) tools that have optimised inventory holding across their Beauty Care Products Division, reducing their total inventory holding by 3%-7% while maintaining inventory availability service levels above 99%, which will now be implemented across all their operations as a result of the MEI tools success (Kerr, 2008:24).

Scale Efficiencies

The basic service approach allows for economies of scale efficiencies to be realised as reduced service differentiation and standardised operations optimises shipping through full loads which reduces cost (Schulman & Allen, 2007:4). As a result of standardisation greater volumes of goods can
be moved through the distribution channel which also creates economies of scale.

**Reduced Complexity**

As the service offering is not differentiated and no value-added services are provided, the organisation can focus on developing core competencies and a clearly defined logistics strategy which will enable the firm to develop a competitive advantage through customer service. According to Keith Harrison, global product supply officer for P&G, Procter & Gamble have 3 priorities which they emphasise in their supply networks; forecasting demand, actionable visibility and agility (Anon, 2007:12). Dell has reduced costs and differentiated their business by focusing on the Direct Model as a logistics strategy, which is based on assembling IT equipment according to customer requirements and shipping directly to customers (Hoffman, 2007:12).

**Disadvantages**

**Segmentation of Customer Base Not Possible**

The use of a basic service approach does not allow for customers to be segmented according to profitability and specialised services to be offered as part of the organisation’s product offering as a basic level of service is provided to all the organisation’s customers (Bowersox & Closs, 1996:74). This precludes the ability to collaborate closely with key customers and provide specialised services in order to gain additional business and customer loyalty. The basic service approach also excludes marginally profitable customers which cannot be serviced efficiently at the basic service level. Both these implications suggest that potential revenue may be lost as a result of not offering a differentiated service to customers based on their profitability to the firm.

**Increasing Customer Expectations**

A basic service program creates certain customer expectations. Focusing on providing set levels of service to all customers creates the possibility that two firms in an industry may compete based on logistics competency and customer service which will lead to increasing customer expectations as the firms attempt to gain a competitive advantage by increasing the level of their basic service offering through shorter order cycle lead times and higher levels of inventory availability. This phenomenon increases logistics costs and puts pressure on the operations of the firm, constraining profitability (Bowersox & Closs, 1996:75).

**Success Factors**

A major factor which has determined the success of the basic service approach is the reduced complexity of operating at a set level of service across all the operations of the organisation. This allows the organisation to focus on its core competencies and develop a clearly defined customer service strategy which can be communicated and understood by the employees of the organisation, the members of the organisation’s supply chain and all the stakeholders involved in firm’s operations. Operational employees know what performance levels they are expected to achieve when carrying out the firm’s logistics activities and the marketing function and sales staff have a clear idea of the level of service they can offer to potential customers as part of the firm’s product offering. Reduced complexity also reduces the probability of errors occurring when performing specialised services to specific customers. The reduced level of communication and collaboration required between the organisation and its customers means fewer resources are devoted to determining customer expectations, as these expectations are established on a periodic basis as opposed to continually communicating with customers in order to establish their requirements.

Another success factor of this approach is attributed to the fact that the basic service level is applied across all the operations of the organisation and is provided to all customers (Bowersox & Closs, 1996:74). Companies set specific performance standards and metrics which are measured and compiled system-wide. This allows for logistics performance to be analyzed over time enabling senior management to determine how successfully the organisation is meeting customer expectations as well as determining the success of service improvement initiatives, such as Procter & Gamble’s implementation of the MEI tools. This ensures that a structured approach is taken when establishing and reassessing the level of service which is provided to customers, allowing the organisation to implement continuous improvement over time with the resultant benefits for the organisation and the supply chain.
CONCLUSION

The statement that companies may increase efficiencies and profitability by segmenting their customer base in terms of importance for providing specialised services may be considered valid provided that the conditions exist, which enable this approach to customer service to succeed. These conditions are however, fraught with problems. The required level of collaboration and information sharing necessary for this approach to succeed are difficult to achieve in practice because of factors such as flawed business information and a limited view of the entire supply chain. The lack of a common view of the customer base, caused by the gap between the marketing and sales functions and the supply chain managers, lead to perspectives which are different because of the inherent divisions and lack of cross functional communication which exists in many organisations. A lack of adequate analytical tools and an organisational structure which does not facilitate communication constrains the ability of the customer segmentation approach to provide increased efficiencies and profitability as this approach to customer service requires that customer profitability be clearly defined and agreed upon in order to provide value-added services accordingly. (Cottrill, 2007:9) Also the flexibility, agility and logistical competency required to successfully implement this strategy are not present in many organisations.

Given the existence of these challenges, the basic service approach may be a better alternative as the reduced complexity, standardisation and system-wide application of this approach increases its appeal to organisations which cannot achieve the level of information sharing, collaboration and flexibility which is a prerequisite for the customer segmentation approach. In the case of organisations lacking these competencies the basic service approach will provide greater efficiency and profitability than the customer segmentation approach.

REFERENCES


