



*Back in 1962, Rolls Royce changed their business model for their aircraft engines. Instead of selling them as a product, they retained ownership and started leasing them. This way, they were able to monitor them consistently, perform maintenance more timely, increase their margins and offer their customers a more advanced product. In short; they Servitized.*

# Servitization:

## Shifting from products, to product service bundles in B2B

Whitepaper

Part 1/3: Introduction to Servitization

## Key takeaways

- Servitization is the new “normal”. Join the revolution, or be left behind.
- Servitization enables firms to stabilize revenues, smoothing out the peaks and troughs often involved with the sales of goods<sup>1,2</sup>
- Adding services to the product portfolio results in an average revenue growth of 30%.
- Companies that have opted to offer product-service bundles see an increase in customer retention and loyalty.
- At an organizational level servitizing requires a shift in mindset from product to customer that certainly adds complexity and requires risk management.

## Welcome to the servitization whitepaper series.

In part one of three, we will introduce the field of servitization. We will explore why servitization is important from a business and consumer perspective.

After having established why it is important to consider servitizing, a good starting point for any organization embarking on this journey is a clear understanding of the extent of servitization required. In part 2 of this whitepaper we will introduce a practical canvas to map servitization progress. Part 3 will provide guidelines on how to successfully achieve the mindset shift required to servitize.

## Customers do not want standalone products, they want solutions. Those solutions often require a combination of products and value-added services.

For the past 20 years, the provision of services has permeated almost every facet of industrial activity. When asked to give an example of great service, most people still refer to those received in “classic” service industries – hospitality, telecommunications, or finance to name a few. However, reality is that some of the best and most innovative services stem from companies that provide products. Case in point: Warby Parker, perhaps the most disruptive company in the eyewear industry, launched by promoting their free home “try-on” for the frames offered on its website. Customers no longer have to visit a brick-and-mortar store to try on or purchase frames.

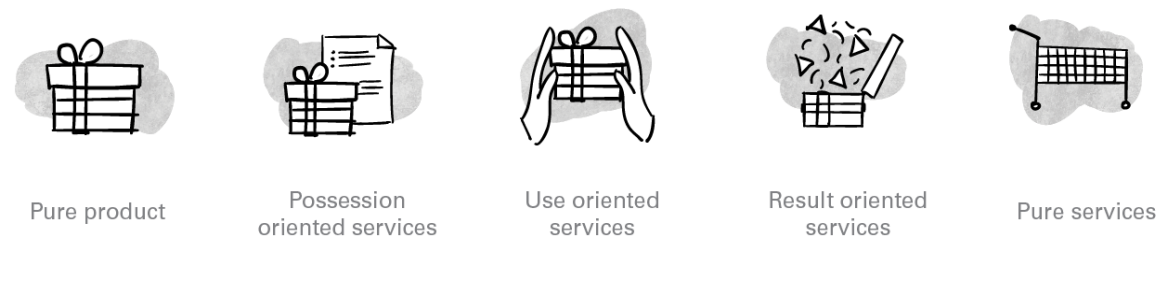
B2B companies have jumped on the bandwagon, shifting from providing products to bundling those products with services. Notable examples are Rolls-Royce “Power-by-the-Hour” and Xerox “Pay-per-Copy”. Each company has built its new business strategy around the services it could provide. This is “servitization” – the process through which companies, once focused solely on products, shift their strategies to a service-centered model.

The Rolls Royce service model, applying to its aircraft engines, charges the user by usage time. Xerox's new service model allows users to take advantage of the benefits of owning a copy machine, without having to own the machine itself.

Servitization is more than simply tacking on a product warranty. It is about bundling products and services in a way that creates shared value for the company and its customers.

## B2B Customers want solutions that provide support

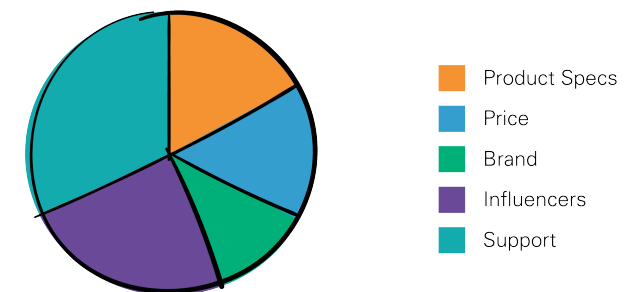
Increasingly the purchase of assets in B2B are based not only on quality or price (together representing one third of purchase decision<sup>3</sup>, see figure 2) but also on the accompanying support. Therefore the purchase of a product often comes with the management, maintenance and repair of that product. Offering a product-service bundle is a good way to alleviate some of the product-related burden, allowing customers to focus on their core capabilities while potentially reducing costs<sup>1,2</sup>. Successful servitization can help a client reduce costs by up to 25-30%<sup>4</sup>.



**Figure 1.**

Progressive stages of servitization. From left to right, companies provide solely products through bundles to solely service offers. For example, office furniture, car sharing and corporate entertainment.

In the example on the right, Rolls Royce fits as a use oriented service, and Xerox as a result oriented service.



**Figure 2.**

Customer's decision factors for technology products<sup>3</sup>.



## A product-service offering is appealing to customers for four reasons.

### Unburdening clients from product related activities

Customers demand peace of mind. A product-service proposition offers B2B customers the opportunity to focus on their core business, knowing that somebody else will take care of the maintenance and management of their assets.

*"I need a little bit of unburdening, a guarantee that it'll work."* – Client of servitized company in Lighting Industry

### Supporting clients to achieve key goals

A product-service offering provides the opportunity to shift role from supplier to trusted partner.

*"As a company we have targets on energy saving. Agreeing on an energy performance with our supplier is a mean to achieve our saving targets."*  
– Client of servitized company in Lighting Industry

### Focusing together on the end user experience

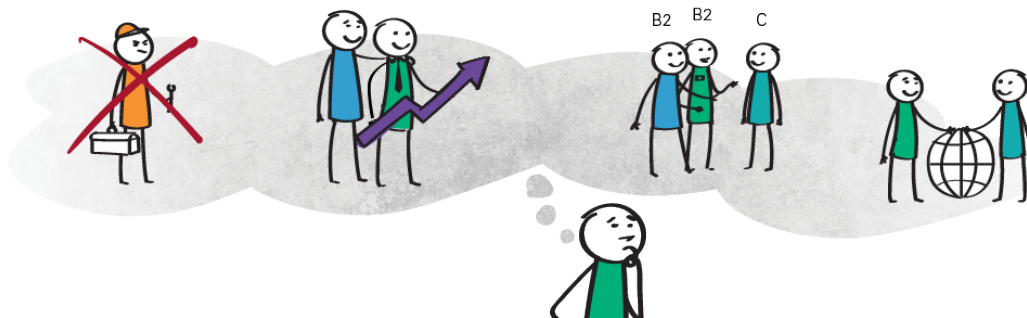
Being a trusted partner means supporting clients in providing the best solution for the final user. At the end of a B2B2C chain, there is always a human being.

*"If the new service is not tuned to our final users, then there is little point in adopting it."* – Client of servitized company in Lighting Industry

### Decreasing risk by sharing responsibilities

By taking ownership of installing, maintaining, repairing products, manufacturers help decrease the risk of failure for their customers.

*"The risk is no longer just ours but also for those who deliver the service. Because we say: this is the result that we want and how that is achieved, that is no longer my job but yours."* – Client of servitized company in Lighting Industry



## Building a better business through Servitization

Servitization is an avenue for improving business performance in four key areas: Clients, Competitive advantage, Economic<sup>5</sup> and Environmental.

### Client:

#### Offer a Relationship that is More than Transactional

Clients are demanding more. They increasingly require that their suppliers provide services alongside their products, and want those suppliers to manage any business activities related to those products<sup>2,6</sup>. This has been a catalyst for servitization, transforming the business-client interaction from pure transaction into a relationship. To survive, and thrive, businesses must now understand both how the client plans to use its products, as well as the client's goal for that use. Ultimately, businesses are called upon to understand what the client needs, and devise a proposition for meeting that need. This proposition goes far beyond the product itself. Moreover, servitization contributes to provide a way to create long-lasting client relationships<sup>7</sup>.

*"Continuity of the company is our motivation. Look, now we earn money by selling products but we think that our market will move to a different business model and if we do not follow...."*

– New Service Provider in Shipbuilding industry

#### Product + Service, Greater Perceived Value

Many complex products are incredibly expensive. While many clients understand the benefit of such products, few can

afford to acquire them. By retaining ownership of and charging the client periodically for the use of their products, a company can reduce the total cost of ownership of such products<sup>8,9</sup> through servitization. Such a system provides a way for the client to grow its business, and creates an incentive for the business to make a sustainable, high-quality product. By using the product as a tool to deliver a service, the bundle is far more valuable than the product alone<sup>10</sup>.

*"Our new customers do not have enough money to purchase a technically advanced system for 20.000 or 30.000 euro. But they do want to grow as a company. Well, then we will simply offer our systems as a service."*

New Service Provider in Horticulture Industry

### Environmental:

#### Sustainability is the Wave of the Future

Servitization is a potential solution to the supposed conflict between economic growth and environmental considerations<sup>11</sup>. By maintaining ownership of the product, the supplier can eliminate incentives to produce products that must be constantly replaced.

*"There is a good reason why we offer our big technical products as a service: it is sustainable. As a company we take ownership of the product, make sure it will not fall apart, because it is in our interest that we do not have to come by often. So we have to make sustainable products and that really fits our vision: do not create too much junk."*

– New Service Provider in Horticulture Industry





## Competitive advantage:

### Differentiate Your Brand by Offering Services

Product-service bundling is a way to create competitive advantage via market differentiation<sup>9</sup>. This is particularly relevant for companies in the European market, which have difficulty competing with their global competitors. Instead of investing in more precise automation or other product-related logistics, companies invest in knowledge and skills to develop offerings designed to improve the operations of their clients<sup>10</sup>. These offerings are typically entirely different than those of its competitors, though they might include a similar product. The focus is on a process tailored to the client, rather than on an asset - making the company unique.

*"If we can offer performance-based services, I think we are really unique in our market, we will be frontrunners."*

– New Service Provider in Shipbuilding industry



## Economic:

### Add Services, Increase Your Margins

By positioning the product as a tool of a larger service that provides value, a proposition is no longer evaluated on its quality and associated costs, but on its value for the client's overall process. Greater margin can be made on this value proposition. Adding services to the product portfolio results in revenue growth for the majority of businesses (60% of the respondents of the Barclays Corporate study: 'Servitization and the Future of UK Manufacturing: The power to help you succeed' September 2011) - with revenue increases of 25% to 50% for 25% of the companies. One study shows that bundling products and services can drive profitability growth of up to 5,3%. Furthermore, the revenue from services is more

consistent than that of products, resulting in a steadier financial situation for the business<sup>2</sup>.

*"The pure product projects have a relatively low profit margin: between 0-3%. Our service projects make healthy margins of up to 8%. That's high in our market."*

– New Service Provider in Construction Industry

## Join the revolution or be left behind

Servitization is a transformation that cannot be ignored. Shifting focus from products to service-product bundles brings benefits for both customers and businesses, virtually in any sector. To name a few of the benefits servitization can provide: stabilized and higher revenues, improved margins, increased customer retention and loyalty.

Although servitization brings substantial benefits to the business while being highly valued by customers, from an organizational perspective it might be challenging. Servitizing the business requires a fundamental shift of mindset from product to customer. This will have an impact on the way employees are trained and rewarded, as well as the way they work.

A good starting point for any organization embarking on this journey is a clear understanding of the extent of servitization required. In part 2 of this whitepaper we will introduce a practical canvas to map servitization progress. Part 3 will provide guidelines on how to successfully achieve the mindset shift.

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