

Customer  
Service  
Programme-  
Europe  
(CSP-E)

# Customer Service Pricing

# INPUT<sup>®</sup>



## CUSTOMER SERVICE PRICING

NOVEMBER 1986

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Research produced by  
INPUT  
41 Dover Street  
London W1X 3RB  
England  
01-493-9335

**Customer Service Programme - Europe (CSP-E)**

***Customer Service Pricing***

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## CUSTOMER SERVICE PRICING

### ABSTRACT

Customer service pricing is of vital importance to vendors. Though price is not the most important criterion to users, they do expect value for money and it must always be considered an important issue. At the same time, users are demanding increased system availability from vendors, and this has implications for service pricing.

To meet this challenge, vendors have begun to 'unbundle' their service contracts and establish a comprehensive set of services, paying more attention to user needs and marketing concerns. Marketing is the key to developing the ability to provide a wide variety of services pitched at precisely the price level that each user can pay.

This report examines from both the vendor and user viewpoints areas of major importance to pricing including service criteria, discounting, and payment of premiums.

This report contains 48 pages, including 15 exhibits.



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# CUSTOMER SERVICE PRICING

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## CUSTOMER SERVICE PRICING

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## I INTRODUCTION

### A. OBJECTIVES

- This report, Customer Service Pricing, is produced by INPUT as part of the 1986 Customer Service Programme in Europe.
- Pricing is always a key issue for vendors and often presents the cutting edge of management's decision-making role in marketing.
- The object of the report is to identify and analyse trends in service pricing as seen by both the vendor and the user. Important areas such as discounting, premiums, and pricing strategies are discussed.

### B. METHODOLOGY

- This report has resulted from INPUT's ongoing customer services research programme which during 1986 included over 800 user interviews conducted by telephone. This research covered a number of issues including attitudes towards customer services pricing.
- For this particular report, 12 major hardware vendors were also interviewed in order to ascertain their responses to a variety of questions regarding the setting of service prices.

- Additionally, 50 users were specifically questioned with regard to their attitudes on aspects of vendor pricing of service including discounting, premium services, and willingness to perform self-maintenance.
- INPUT would like to express its thanks to all those companies and individuals who participated in the research undertaken for this report.
- Enquiries and comments regarding this report and any related topics of interest are welcomed by INPUT.

### C. REPORT STRUCTURE

- The remaining chapters of this report are organised as follows:
  - Chapter II is an executive overview providing a summary of the contents of the entire report.
  - Chapter III discusses the perspective of the vendor regarding pricing strategies and attitudes towards discounts.
  - Chapter IV looks at the role of the user as a force in service pricing and user attitudes towards premium services and discounts.
  - Chapter V analyses apparent differences between user needs and the services provided by vendors.
  - Chapter VI summarises INPUT's conclusions.

## **II EXECUTIVE OVERVIEW**

- This Executive Overview is designed in a presentation format in order to:
  - Help the busy reader quickly review key research findings.
  - Provide a ready-to-go executive presentation, complete with script, to facilitate group communication.
- The key points of the entire report are summarised in Exhibits II-1 through II-6. On the left-hand page facing each exhibit is a script explaining its contents.

## A. MATURING OF THE CUSTOMER SERVICE MARKET

- The customer services market can be considered as having reached a mature stage as evidenced by slowing revenue growth, the presence of experienced and thus more demanding users, and the inevitable increased competitiveness of vendors.
- Under these circumstances, increased emphasis tends to be placed on additional services to augment basic offerings and also on pricing. Both of these are occurring in the customer services business.
- Vendors seek to develop additional service offerings both to improve their competitiveness and to generate extra revenues.
- More emphasis tends to be placed on marketing in order to be responsive to user needs in formulating the delivery of services.
- The notion of customer service as a cost centre has been replaced by the marketing-oriented approach of customer service as a revenue earner.
- Increased emphasis on pricing implies a reevaluation of pricing strategies.
- The emergence of independent maintenance companies has increased the pressure on vendors to pay increasing attention to competitive strategies in general and pricing in particular.
- It must also be recognised, however, that there are many users who are not price sensitive. It is these users who are most anxious to secure a high quality service and place a corresponding value on it.

## **MATURING OF THE CUSTOMER SERVICE MARKET**

- **Slowing Growth**
  - **Increased Competitiveness**
  - **Additional Services**
  - **Emphasis on Pricing**
-

## B. PRICE DISCOUNTING

- One response to increased competitiveness has been the selective use of discounting as a selling tool, although most vendors said that they did not officially operate discounting policies.
- In practice, discounting is in widespread use especially in volume sales. It is mostly used at the initial selling stage where substantial discounts are offered as inducements to purchase.
- Another aspect of discounting is vendor encouragement of users, by means of discounts, to take on more responsibility for self-maintenance. This can lead to substantial savings for both the user and the vendor.
- Users do not, however, always choose service price as a major criterion when deciding on a particular service vendor, and thus vendors can overestimate the size of discounts needed. Therefore, while vendors offer on average up to 50% discount for self-maintenance, users on average only expect about a 25% discount.
- The use of extended warranties is increasing. Extended warranties effectively allow a discount on maintenance prices by encouraging the notion of a long-term guarantee of service at a recognised level.
- It must be recognised, however, that users generally rank service quality higher than service price, so vendors must be careful that lower prices and discounts do not erode service quality.



## **PRICE DISCOUNTING**

- **Secure New Business**
  - **Encourage Self-Maintenance**
  - **Use of Extended Warranties**
-

### C. USER PURCHASING CRITERIA

- Hardware reliability remains the most important purchasing criteria overall. As computer technology has developed, users have come to expect increasing levels of reliability in their equipment.
- Users continue to place emphasis on the criterion of availability (or uptime) of the system. This, in turn, implies a high degree of importance to the levels of response and repair times on offer from the vendor.
- Overall quality of services and the price of services are rated by users as less important than response and repair service times.
- Different patterns of criteria prioritisation are evident in the customer services market. Independent maintenance companies selling initially on a low-price strategy have successfully exploited that segment of the market that places a high emphasis on the cost of service.



## USER PURCHASING CRITERIA

- Response Time
- Repair Time
- Quality of Service
- Price of Service

#### D. USER PERSPECTIVE

- Unbundling of the customer service offering tests the willingness of users to select additional service functions; for example, 'on-site spares' at extra cost.
- Around one-third of all users reported an interest in at least one particular service option; for example, remote diagnostics, standby coverage, or increased software support.
- These users report a willingness to pay a premium of about 12% over and above basic maintenance charges for such services.
- User self-maintenance was seen as an attractive option by around one-third of the users surveyed. Whilst vendors report a willingness to offer discounts of up to 50% for use of this approach, users indicated a willingness to participate for, on average, only a 25% discount.
- Users have expressed interest in the notion of a 'no-claims discount'. This would effectively produce a discount on a subsequent year's charges if there had been little or no take-up of service in the previous year.
- So far there has not been a great deal of response from the vendors to this idea.

## **USER PERSPECTIVE**

- **Service Premiums**
  - **Self-Maintenance**
  - **"No-Claims" Discount**
-

## E. CUSTOMER SERVICE PRICING TRENDS

- Users indicated a declining expectation in overall service pricing increases. Price increases averaged around 9% in 1985 and 7% in 1986, and are anticipated by users at 6% for 1987.
- INPUT expects vendors to continue implementing unbundling approaches in order to achieve increased price competitiveness and to maximise their operations revenue generation capability.
- Vendors must exploit to the maximum the willingness of some users to pay premiums for additional services.
- Attention must be paid to controlling discounting which is widely practiced despite vendor policies of apparent strict price control.
- Vendors must place more emphasis on assessing the value of services to their users when setting prices in order to maximise their revenue potential.
- In summary, as the market increases in competitiveness, the marketing approach will become more necessary, implying not only closer attention to user needs, but much greater emphasis on the pricing function within customer service.

## **CUSTOMER SERVICE PRICING TRENDS**

- **Declining Expectation for Price Increases**
  - **Unbundling**
  - **Premium Pricing**
  - **Discounting**
  - **More Emphasis on Pricing**
-



## F. USER DISSATISFACTION WITH CURRENT MAINTENANCE PRICES

- Users expressed varying degrees of dissatisfaction with the levels of maintenance prices that they pay.
- The most common complaint was simply that the level of maintenance received was too expensive. However, a number of users had specific reasons for dissatisfaction with maintenance pricing.
- The most frequently mentioned complaint was that maintenance pricing did not reflect the inherent reliability of the equipment. Consequently, this has led to users seeing a need for 'no-claims' discounts.
- The level of maintenance charges in relation to equipment cost was also a concern. A number of users commented that their support costs had not fallen in line with lower hardware costs.
- A lack of choice with regard to the supply of maintenance services was also a concern for some users. This must be seen as a warning for vendors of the continuing threat of third-party maintenance vendors.
- A few users questioned the justification for maintenance prices in view of the relatively poor services that they received. These comments basically related to the competence of the field engineers assigned to their installations.

## **USER DISSATISFACTION WITH CURRENT MAINTENANCE PRICES**

- **Equipment Reliability**
    - **"No Claims" Discount**
  - **Equipment Cost**
  - **Lack of Choice**
  - **Support Competence**
-





### III VENDOR PRICING APPROACHES

- All vendors agreed that revenues derived solely from hardware maintenance would continue to decline in real terms in the future. They all similarly agreed that the most profitable ways of generating additional revenues were likely to be through increases in software support and involvement in TPM.
- In addition, the efficient organisation of their service departments and coherent and comprehensive pricing strategies were seen to be the best routes to continued overall company profitability.
- In recent years, customer service has developed in its own right with the recognition of the potential profitability of service. Customer service is no longer merely an adjunct to sales and marketing but has produced its own marketing, advertising, and selling techniques.
- Previously, management viewed service as a cost centre and set their prices accordingly. It was seen as necessary that service costs should cover labour and spares costs.
- With the switch towards service as a profit centre, those same service organisations saw the need to improve the efficiency of their operations in order to satisfy increasing user sophistication.
- So service had to be sold and marketed, which in turn led to new overheads that service managers had never faced before.

- In addition, the emergence of independent maintenance companies has given a new competitive edge to the concept of service, especially, though not exclusively, in the issue of service pricing.

#### A. PRICING STRATEGIES

- Classical marketing theory recognises several pricing strategies. While each one varies in its emphasis, three main strands can be identified.
  - Cost-plus pricing.
  - Competitive pricing.
  - Perceived-value pricing.
- Cost-plus pricing attempts to cover the costs associated with providing the service, usually with a notional profit margin added. The principal feature is that the service should be self-financing. However, any pricing method that does not take into account current demand and competition is not likely to lead to the optimal price.
- In competitive pricing a company will base its prices largely on competitors' prices. This price might be the same, more, or less than the competitors'.
- The problem with this approach is that it is usually a reactive one, i.e., it only reflects back what is happening in the market rather than being an influencing force, although this may be tempered by a dominant market leader.
- Competitive pricing strategies whether in hardware, software, or service will lead to lower margins that are likely to harm smaller vendors since the lowest-cost producer will always win in this situation.

- Perceived-value pricing will be concerned with the user's perception of value rather than covering the costs of providing the service.
- A bank, for example, will place a different value on service for its vital data processing installations than a small company that uses PCs in a noncritical role.
- The danger here is that the vendor will undercharge for a service. The most difficult aspect of this strategy is actually estimating the value placed upon the service by the 'high-need' user.
- In the example of a bank, computer downtime may be costed at say \$100,000 a day; to that organisation that is the perceived value of the loss. If the service only costs \$1,000 a day then the vendor is leaving money on the table since the bank would be willing to pay a far higher sum to guarantee minimum disruption to its operation.
- In addition, a computer user may place little value on a service that is perceived as being cheap.
- In the real world most vendors adopt a combination of the first two strategies since it would appear to give the most flexibility both to the user and to the supplier.
- Exhibit III-1 shows the analysis of vendor responses to the question of the pricing strategies that they adopt. It can be seen that cost and competitive pricing were the most frequently mentioned.
- All the vendors interviewed admitted that pricing against the competition was not an official strategy, but nevertheless they expressed the view that they were obliged to adopt this approach if they were to both retain their market share and hopefully increase it.

**EXHIBIT III-1**

**VENDOR PRICING STRATEGIES**

<b>TYPE OF STRATEGY</b>	<b>NUMBER OF RESPONSES*</b>
<b>Cost Recovery Plus Profit Element</b>	<b>5</b>
<b>Competitive</b>	<b>3</b>
<b>Perceived Value</b>	<b>1</b>
<b>Combination</b>	<b>6</b>

\* Multiple Response Allowed

Total Number of Respondents: 12

## B. ATTITUDE TOWARDS DISCOUNTS

- All the vendors approached said that discounting as a selling tool was not official policy. However, they all went on to admit that in certain circumstances they would be prepared to permit discounting.
- Discounting may be used in two main situations.
  - At initial contract time.
  - At contract renewal time.
- It is important to state that as a tool discounting should not be used indiscriminately, but rather selectively and with the realisation of its likely anticipated future effects.
- In addition, vendors should be aware that users do not always choose service price as the main criterion for picking a particular service vendor but tend to place more emphasis on service quality.
- Exhibit III-2 shows an analysis of the types of discounting mentioned by vendors. At the top of the list is discounts for volume.
- In fact, this type of discount usually occurs during initial hardware sales negotiations where substantial discounts would be offered as inducements to purchase.
- Vendors also pointed out their differing attitudes to such discounts between users who had single or multiple vendor sites. In such cases where competition is not evident, i.e., a single vendor site, then the discount was not likely. On a multiple site, on the other hand, such discounts were readily available since competition was a real factor.



**EXHIBIT III-2**

**VENDOR ATTITUDES TOWARDS DISCOUNTS**

<b>TYPE OF DISCOUNT OFFERED</b>	<b>NUMBER OF RESPONSES*</b>
<b>Volume</b>	<b>10</b>
<b>User Self-Maintenance</b>	<b>6</b>
<b>Type of Contract</b>	<b>3</b>
<b>Competitive</b>	<b>2</b>
<b>Up-Front Payments</b>	<b>2</b>
<b>Other</b>	<b>2</b>

\* Multiple Response Allowed

Total Number of Respondents: 12

- Some vendors were keen to see users take more responsibility for their maintenance. This could be anything from user diagnostics to 'return to depot' services. In such cases, a user could expect discounts in the 40-50% range where vendors are keen to encourage user self-maintenance to reduce their servicing costs.
- The danger, of course, is that the user may come to believe that he can do all servicing himself even though it may not be in his best interests to do so.
- Some vendors allow discounts according to the type of contract held by the user. In this case, the vendor may attempt to actively encourage the user to take up a particular service.
- Part of this includes the whole question of warranties versus insurance. Vendors would like to see extended warranties for three main reasons:
  - It supplies money 'up-front' to the service organisation.
  - It locks in the user to the vendor.
  - It gives the user a long-term guarantee of service at a recognised level.
- The main disadvantage is that it also locks in the vendor to a set price and cannot take into account fluctuations that may be beyond the control of the vendor.
- Discounting can be market-driven, as for example has been the case for independent maintenance. The point is, however, that only a minority of users are so price sensitive that they will in fact switch service vendors on the price issue alone.

- Service quality generally ranks higher for users than service price, and a vendor should be able to contain the threat from independent maintenance companies by offering better service and more flexibility.
- Only two vendors said that they actively used competitive discounting to gain service contracts and they were both smaller organisations.
- Other types of discounting included:
  - A type of 'no-claims discount' for marginal use of a service already contracted.
  - Strategic discounting which involved targeting specific markets in order to quickly establish a market share.



## IV USER PERSPECTIVE

### A. SERVICE CRITERIA

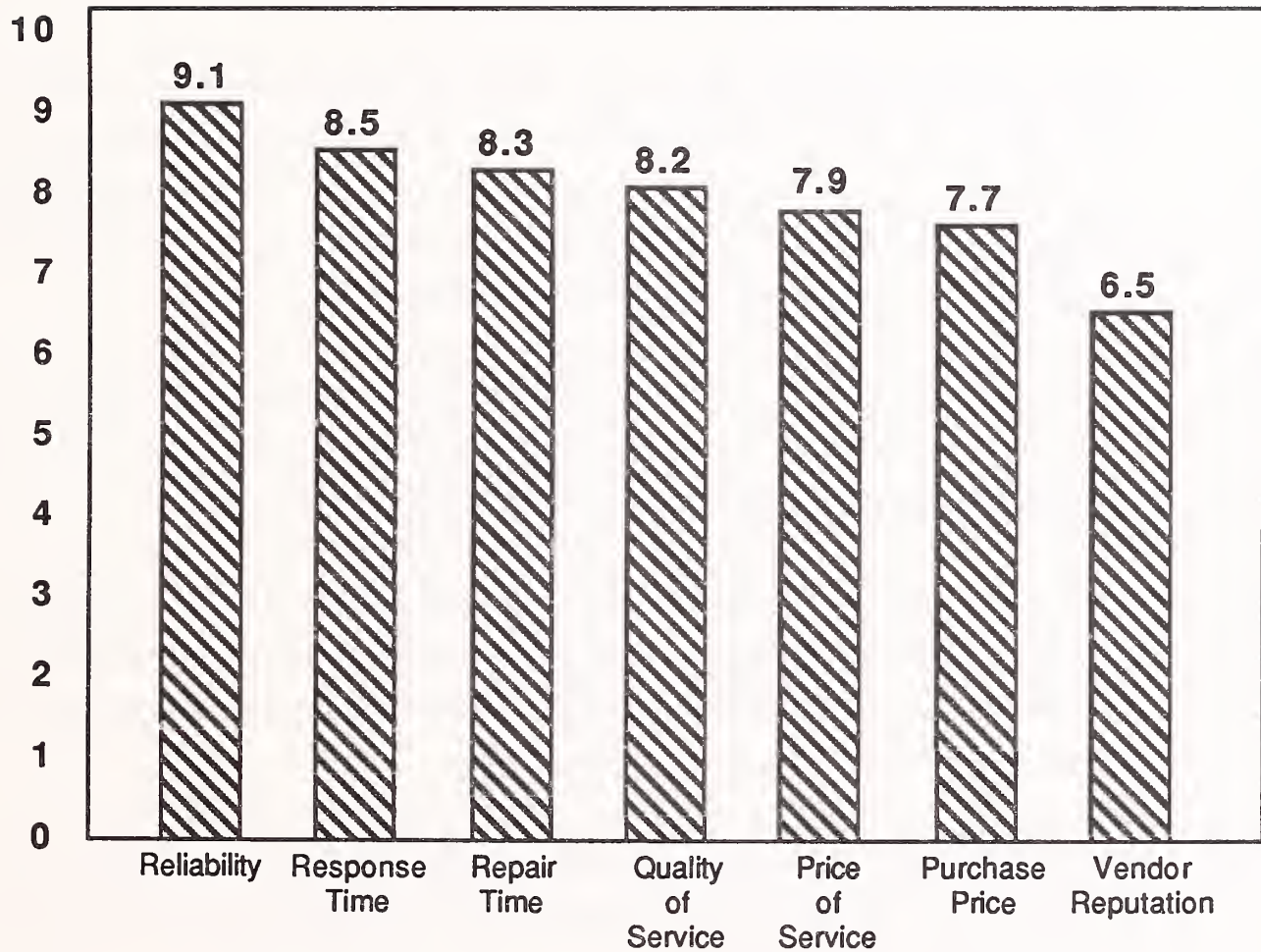
- Until recently, service was seen as a 'necessary evil', something that was needed when things went wrong and thus had negative connotations. This was assumed by both users and vendors.
- However, recently the notion of customer service as something to be marketed has emerged due to three main factors:
  - Increased user resistance to paying percentage service charges especially as the reliability of hardware has improved.
  - A move away from the notion of system fixing towards a comprehensive offering that would benefit the user in many different ways.
  - The growing importance of independent maintenance companies.
- In addition, users have been demanding more and more system availability or uptime, and as they get used to new, higher levels of uptime, so the demands increase.
- There are many reasons why a user will decide to purchase a particular piece of equipment and any subsequent maintenance contract. That set of decisions

is peculiar to that individual user, and no one user will have necessarily the same criteria as another.

- Evidently the decisions that have to be made when purchasing a mainframe are different from those when buying a PC, but nevertheless the user still has to be informed as to what is available in the marketplace that comes within his specification.
- Users were asked about the criteria they use when purchasing equipment. Exhibit IV-1 shows how, when asked to rate in order of importance various purchasing criteria, users rated reliability the most important.
- This is perhaps understandable since most users will want maximum use from their equipment and this implies maximum reliability.
- What is interesting, however, is how far down in importance comes the vendor's reputation as a criterion in the selection of equipment.
- The user's perception of the quality of service offered by the vendor is also important. It can be that what is perceived has a stronger influence than that which actually prevails.
- It is apparent that the price of service in itself is not that important since it was rated as only the fifth most important criteria. This is notable as TPM companies have tended to emphasise the price of service in their marketing activity.
- This is not to say that users are not interested in lower prices, but that other factors like response and repair times and, above all, reliability (for this read availability) are more important.
- Vendors should be aware, though, of user resistance to creeping price rises.

EXHIBIT IV-1

USER CRITERIA FOR SELECTING HARDWARE



PURCHASING CRITERIA

Number of Respondents: 50

Average Standard Error: 0.2

- It is also apparent from Exhibit IV-1 that users place response and repair times high on their list of attributes.
- Perhaps the lesson here is that it is not necessarily the price but the quality of service that is supplied that is the critical factor. The overall result of this analysis shows that, as may be contrary to popular belief, users in the main are not too price sensitive when it comes to the purchase of hardware and service. They place the reliability of their equipment above all else and regard the upkeep of that equipment as their prime objective.
- Vendor service organisations, on the other hand, face pressure from their management to increase profitability. Cost-cutting is one solution, although the effect on the user may then be to reduce the quality of service provided. Increasing prices alternatively have the reverse effect of driving users away (perhaps towards independent maintenance companies).
- The response has been to 'unbundle' services; that is, to offer a low entry-level price for all customers and then provide a 'menu' of premium services that can be marketed to users in need of such additional services.
- This enables users to effectively purchase exactly what they want in terms of service. Those who desire premium service and are not price-sensitive will willingly pay the extra necessary, while those users who only want the base service will be able to contract for that alone.
- What vendors have in fact discovered is that the services that they previously offered for free (within the main maintenance contract) can now be charged for to gain additional revenues.



## **B. PREMIUM SERVICES**

- Vendors have been unbundling the services 'package' in recent years in an attempt to provide the user with a 'menu' of services from which he can choose.
- Users were, therefore, asked whether they would be prepared in principle to pay for extra services like remote diagnostics and an on-site engineer.
- They were also asked about the level of premium they were prepared to pay for any such service.
- Exhibit IV-2 shows the analysis of user responses, indicating that the service most wanted by users is the provision of standby coverage; by this is meant either the use of another machine on-site or remotely, usually on the vendor's site.
- On average, though, users would only be willing to pay about 12% over and above their current maintenance charges.
- The other types of services quoted showed the premiums they would be willing to pay lay within the range of 10-14%.
- The premium that users would appear to be willing to pay for the provision of increased software support was the highest mentioned, averaging out at 14%.

EXHIBIT IV-2

USER NEEDS FOR PREMIUM SERVICES

REASON	NUMBER OF RESPONSES*	AVERAGE PREMIUM EXPECTED
PM During Non-Prime Hours	17	12%
Remote Diagnostics	16	10%
On-Site Spares	17	11%
Standby Coverage	21	12%
On-Site Engineer	16	13%
Increased Software Support	16	14%

\*Multiple responses allowed

Total Number of Respondents: 50

## C. USER ATTITUDES TOWARDS DISCOUNTS

### I. GENERAL CONCEPT

- Exhibit IV-3 shows an analysis of the response of users when questioned about possible discounts for a list of services and an indication of expected discounts.
- Heading the list is the fact that users appear to regard self-maintenance as grounds for expecting a discount (in this case about 26%).
- Upgrading to a new service category is reckoned by users to be worth about a 20% discount since it enables the supplier to eventually charge more for the new service in subsequent years.
- The non-use of a service implies that although a user may have paid for it, the user never made full use of it.
- This is interesting since it serves to underline comments that have been noted by INPUT concerning the non-use of services. It appears that a form of 'no-claims discount' is expected by users; this means a discount in the subsequent year if a service is not used the previous year.
- In fact, one major vendor operates a scheme whereby the subsequent year's maintenance contract, if similar to the previous year's, is reduced by 50% if a particular service was not used or was underused.
- As well as discounts for non-use, vendors also promote the idea of discounts to encourage use of a particular service.
- A typical example of a discount for using a service is in remote diagnostics. A recent INPUT study, Remote Disgnostics in European Customer Service,

**EXHIBIT IV-3**

**USER ATTITUDES TOWARDS DISCOUNTS**

<b>TYPE OF DISCOUNT</b>	<b>EXPECTED DISCOUNT</b>	<b>NUMBER EXPECTING DISCOUNT*</b>
<b>Self-Maintenance</b>	<b>26%</b>	<b>16</b>
<b>Up-Grading of Service</b>	<b>20%</b>	<b>14</b>
<b>For NOT Using a Service</b>	<b>18%</b>	<b>28</b>
<b>FOR Using a Service</b>	<b>12%</b>	<b>23</b>

\* Multiple Responses Allowed

Total Number of Respondents: 50



July 1986, showed one hardware vendor who gave users of remote diagnostics a discount of \$200 per month; however, those declining to use the service could expect to pay a premium of some 30% over their standard maintenance charges.

- Currently, vendors are anxious for users to take up remote diagnostics since it saves time and money for both parties. On the other hand, some users view remote diagnostics with suspicion, hence the need for discounts to encourage use.
- This is especially true for users where there may be a security problem due to sensitive data.
- This sample indicates that users find the idea of a discount for using a service an interesting one. However, it does not attract a correspondingly high anticipated discount, an average around 12%.
- This could be because users probably think that such a service is already built into their maintenance contract, so leaving little room for discount. Vendors of service could take advantage of this potential by further unbundling so that the user could see exactly what the maintenance contract offered.

## 2. USER SELF-MAINTENANCE

- Most vendors are keen for the user to be more involved in self-maintenance. This reduces vendor costs, enables the user to be more aware of the working of his equipment, and serves to generally reduce the time spent on call-outs.
- It has already been noted how the unbundling of the service contract has given vendors the opportunity to offer a wide variety of services, thus freeing users from the restrictions of (sometimes) unnecessary maintenance.

- This is not, however, a completely new approach since some vendors have traditionally offered a 'return to depot' service that implied lower rates. Users are not usually receptive to this form of self-maintenance.
- The issue of self-maintenance in general drew the highest expectation of discount--some 26%. In actual fact, vendor analysis (see Section III.B) indicates that vendors would be willing to offer a 40-50% discount for user self-maintenance.
- Increased user participation in the maintenance and support of equipment offers a number of advantages:
  - For those users who are price-sensitive, it provides a low-cost service option.
  - At the low end of the service market, it bolsters the vendor's position against attack from independent maintenance companies.
  - It can usefully attract new users who may later develop into premium clients.
  - It increases user awareness of the importance of service while leading, it can be argued, to lower price sensitivity.
- Exhibit IV-4, which indicates how far users are willing to perform self-maintenance, highlights four levels of participation.
- From this it can be seen that working with a support centre is the most popular method with an expected discount of some 24%. The other levels mentioned show a lower willingness to participate, but interestingly enough indicate a similar anticipated discount.

**EXHIBIT IV-4**

**USER WILLINGNESS TO BE INVOLVED IN SELF-MAINTENANCE**

<b>LEVEL OF PARTICIPATION</b>	<b>PERCENT WILLING</b>	<b>EXPECTED DISCOUNT</b>
<b>Work With a Support Centre</b>	<b>48%</b>	<b>24%</b>
<b>Install a Software Patch</b>	<b>45%</b>	<b>23%</b>
<b>Install Circuit Board/ Hardware Module</b>	<b>35%</b>	<b>24%</b>
<b>Deliver Equipment to a Service Centre</b>	<b>30%</b>	<b>25%</b>

Total Number of Respondents: 130

- It would appear that vendors should be most concerned about increasing the value of the service that they offer. If this means a mix of discounting and premium offerings, then that is the mix that must be made.
- Every user has a slightly different approach, and it should be the goal of a service organisation to fulfill that individual user's needs as effectively as possible.

## **V SERVICE PRICING AND MAINTENANCE CHARGES**

- The aim of service pricing must be to balance a number of potentially conflicting factors as economically and efficiently as possible since the service department comes under various pressures.
  - The overall company sees service as a profitable operation and obviously wants to keep it that way.
  - The sales function sees lower service prices as an aid to the sales of equipment.
  - Users desire improved service and competitive pricing.
- Thus, the service department has to provide for a variety of needs and should continually seek out new methods of doing so.
- Users, on the other hand, see maintenance charges simply as a cost that they have to bear to pay in respect of the level of service that is contracted to them.
- Of course, for every user there is a different standard--the degree of dependency on the equipment determining the extent to which the user relies on the vendor.

## A. VENDORS - AN HISTORICAL PERSPECTIVE

- The majority of those vendors interviewed agreed that the percentage of revenue derived from hardware maintenance is declining; nevertheless, the volume of business is increasing.
- There are several identifiable reasons for this:
  - More flexible service contracts.
  - A wider variety of services on offer than before.
  - Increasing revenue from software support.
  - Growth of the user base from increased hardware sales.
  - Specialised service demands from sophisticated users.
  - Improved efficiency and economies of scale from larger suppliers.
  - Competition from independent maintenance companies.
- Perhaps the most important innovation has been the unbundling of the service contract; where once a wide range of services were provided 'free' but at a cost, now vendors are offering a low-cost base level service with the option to increase to any other level at a recognised charge.
- This has three main advantages:
  - A base price offering can attract new users who are more price-sensitive.



- There is a different price for each service and the user can relate that to his own perceived value for that service.
- The whole idea of giving users a choice can only serve to enhance the image of the vendor as one who offers value for money.
- INPUT has noted a downward trend in prices for some of the reasons mentioned above, and those vendors who were approached for this report agreed about this.
- Therefore, a major objective must be to look for new ways to increase revenue and to further develop non-hardware maintenance activities.
- A prime candidate for this is in software support where there are increasing user service requirements and greater potential for revenue and profit.

## **B. USER EXPERIENCES WITH MAINTENANCE CHARGES**

- In INPUT's 1986 annual survey on customer satisfaction in Europe, users were questioned about their experiences of price changes during 1985 and what increases (if any) they anticipated for 1986 and 1987.
- Exhibit V-1 is an analysis of the responses to this question in the six European countries where the survey was carried out. What is interesting is the expected trend towards lower prices/increases.
- However, vendors must be careful not to lower service quality since, as was commented in Chapter IV, this is of key importance to users.

**EXHIBIT V-1**

**USER EXPERIENCES OF INCREASES IN MAINTENANCE PRICES  
AND ANTICIPATED INCREASES FOR 1987**

**(Average Increases in Percent)**

<b>COUNTRY</b>	<b>1985</b>	<b>1986</b>	<b>1987</b>
<b>France</b>	<b>7</b>	<b>5</b>	<b>5</b>
<b>Germany</b>	<b>6</b>	<b>5</b>	<b>6</b>
<b>Holland</b>	<b>8</b>	<b>5</b>	<b>5</b>
<b>Italy</b>	<b>12</b>	<b>10</b>	<b>8</b>
<b>Sweden</b>	<b>9</b>	<b>8</b>	<b>7</b>
<b>United Kingdom</b>	<b>9</b>	<b>8</b>	<b>7</b>
<b>Europe Total</b>	<b>8.6</b>	<b>7</b>	<b>6.3</b>

Average sample size for each year: 440

- In addition, users were asked about their level of satisfaction with their current maintenance charges. A significant number expressed dissatisfaction for a wide variety of reasons, not the least of which they thought that the vendor was not offering value for money. Exhibit V-2 gives some examples of this.
- The first reason falls under the generic title of 'too expensive', and this can cover many different aspects of that complaint.
  - Simply too expensive.
  - An imbalance between what is charged and what is received.
  - The quality of service does not warrant the price.
  - Difficult to justify the cost when compared to the usage of the equipment.
  - Often the price is non-negotiable.
  - Some items of equipment have a service charge that bears no relation to their purchase price.
- The other major complaint was that since hardware has become so much more reliable, maintenance costs do not yet reflect that improvement.
- In this respect, many users spoke of the idea of a 'no-claims discount' for subsequent year's maintenance charges. There were many reasons why this was felt to be justified:
  - A small number of faults do not warrant such high prices.
  - Very few breakdowns.

EXHIBIT V-2

**SOME REASONS FOR DISSATISFACTION WITH  
CURRENT MAINTENANCE PRICES**

REASON	NUMBER OF RESPONSES
"Too expensive for what we get"	95
"Reliability of hardware does not warrant the maintenance costs"	38
"Not good value for money"	14
"Competition is better"	14
"Tied too much to the manufacturer"	10
"The price of hardware is falling, so why doesn't maintenance"	9
"Increase in maintenance out of line with increase in inflation"	5
"Competence of supplier's Customer Engineer organization"	5

Total Number of Respondents: 135 (multiple responses allowed)

- The user pays for services that are never used.
  - The equipment is so reliable--almost maintenance-free.
  - Always having to pay the same price regardless of how often the service is used.
  - No relationship between the performance of the machine and the price of maintenance.
- Sometimes the reverse was true concerning reliability. Older equipment which cost more, relatively, still commanded the original higher maintenance charges because older machines need more maintenance.
  - Interestingly, some users said that they believed that the competition had more to offer. This could be part of the complaint that some users felt that they were too tied to the manufacturer and had little choice.
  - The argument here is that ultimately a user does have a choice, and this is what vendors realise when they attempt to tie in a user to a maintenance agreement.
  - Similarly, this is what TPM companies work on--the fact that if a user is dissatisfied enough, he will switch suppliers.
  - Another complaint was that since the price of hardware was falling, the price of maintenance should also fall--this presumably from those users whose service price was linked to the purchase price of their equipment.
  - It is now recognised by vendors that this type of pricing strategy (i.e., service costed as a percentage of equipment price) is difficult to sustain, as was discussed in Chapter III.



- Some users interviewed did suggest that they had a problem with the vendor's customer engineering organisation. There were several examples of this:
  - Often the customer engineer is not competent enough for the user.
  - The user feels that the engineer does not communicate properly, especially when fixes are being done remotely.
  - Sometimes the engineer gives the impression of being very busy when the user knows that this is not so.
  - There could be differing levels of engineer competence, so continuity was important.
  - The time taken compared to the seriousness of the fault was often at dispute.
  - The quality of workmanship could be criticised.
- Users who expressed dissatisfaction with their maintenance prices were then asked what they thought would be a reasonable average discount; their responses are analysed in Exhibit V-3.
- These responses show the variation between the different European country user groups and the degree of discount that users are expecting. In fact, without users taking on some aspects of self-maintenance, it is difficult to see how vendors could offer service prices at these levels.



**EXHIBIT V-3**

**AVERAGE DISCOUNT EXPECTED ON CURRENT MAINTENANCE PRICES\***

<b>COUNTRY</b>	<b>PERCENT OF DISCOUNT EXPECTED</b>	<b>PERCENT OF TOTAL SAMPLE</b>	<b>TOTAL SAMPLE SIZE</b>
<b>Belgium</b>	<b>17%</b>	<b>18%</b>	<b>28</b>
<b>France</b>	<b>30%</b>	<b>7%</b>	<b>168</b>
<b>Germany</b>	<b>31%</b>	<b>10%</b>	<b>160</b>
<b>Holland</b>	<b>30%</b>	<b>13%</b>	<b>79</b>
<b>Italy</b>	<b>32%</b>	<b>11%</b>	<b>116</b>
<b>Norway</b>	<b>32%</b>	<b>27%</b>	<b>26</b>
<b>Sweden</b>	<b>37%</b>	<b>14%</b>	<b>79</b>
<b>United Kingdom</b>	<b>37%</b>	<b>15%</b>	<b>158</b>
<b>Total Europe</b>	<b>31%</b>	<b>13%</b>	<b>814</b>

\*By those users who expressed dissatisfaction with their current maintenance charges.



## VI CONCLUSIONS

- In this research, both users and vendors responded to various questions regarding aspects of service pricing.
- On the one hand, users have indicated that pricing is not generally the most important consideration. Hardware reliability and response and repair times are considered to be the most critical issues.
- Nevertheless, pricing will always be an important issue and there will always be a proportion of users who are price sensitive.
- At the same time, users will expect increased levels of service as requirements for system availability increase.
- In addition, some users are willing to accept premium services with corresponding premium rates for increased service products. Similarly, some users would be interested in more self-maintenance, especially if it meant a discount on their current maintenance charges.
- Vendors, on the other hand, have responded with two main strategies:
  - Lower effective prices through the selective application of discounts.
  - Unbundling of service products.

- Those vendors that have managed to introduce flexibility into their service contract have found that they have been able to attract those users who are price sensitive as well as those users who can pay for premium services.
- Unbundling services can assist the vendor in two main ways:
  - It can provide a bulwark for the vendor against the attack from independent maintenance companies, especially at the lower end of the market.
  - It increases user awareness of the importance of service while leading to lower price-sensitivity.
- What are needed are new directions especially in the fields of marketing and advertising--communicating the message of service benefits to those that make the decisions and adapting the organisation of service departments in order to maximise the revenue potential from new service offerings.







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## Offices

### NORTH AMERICA

#### Headquarters

1943 Landings Drive  
Mountain View, CA 94043  
(415) 960-3990  
Telex 171407

#### New York

Parsippany Place Corp. Center  
Suite 201  
959 Route 46 East  
Parsippany, NJ 07054  
(201) 299-6999  
Telex 134630

#### Washington, D.C.

8298 C, Old Courthouse Rd.  
Vienna, VA 22180  
(703) 847-6870

### EUROPE

#### United Kingdom

INPUT  
41 Dover Street  
London W1X 3RB  
England  
01-493-9335  
Telex 27113

#### Italy

Nomos Sistema SRL  
20124 Milano  
Viale Vittorio Veneto 6  
Italy  
228140 and 225151  
Telex 321137

#### Sweden

Athena Konsult AB  
Box 22232  
S-104 22 Stockholm  
Sweden  
08-542025  
Telex 17041

### ASIA

#### Japan

ODS Corporation  
Dai-ni Kuyo Bldg.  
5-10-2, Minami-Aoyama  
Minato-ku,  
Tokyo 107  
Japan  
(03) 400-7090  
Telex 26487

