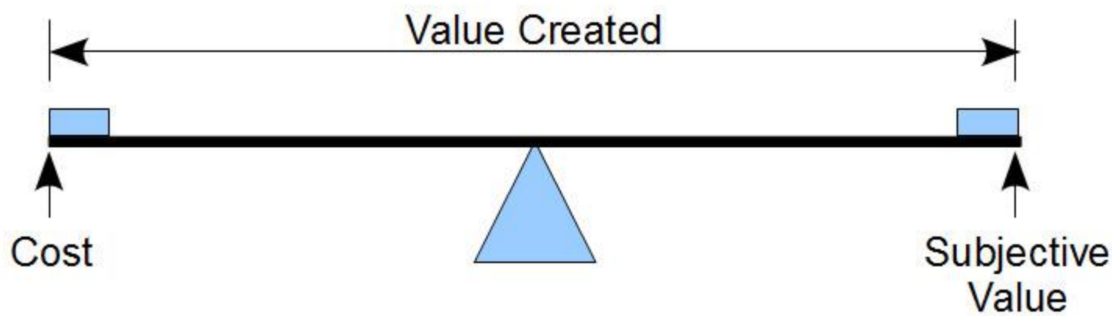
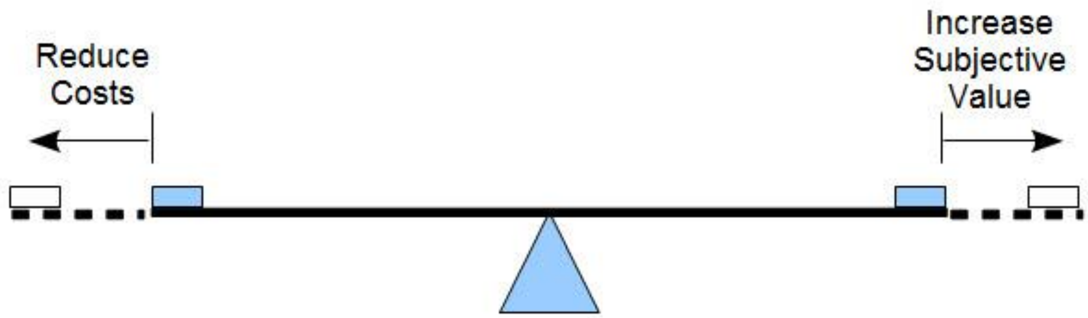
Managing Business Value Creation

Business at its most fundamental level is about creating value. Without value creation (a.k.a., a value proposition), a business is limited in what it offers to society, and will soon no longer exist due to Adam Smith's invisible hand. The reverse is also true in that a business that creates a lot of value should be successful within the market place. Value creation takes on many forms as I will discuss, but the first thing to realize is that value is a subjective quantity, and is dependent on the perceptions of the customer.

To study this further, let's create a system where the value created by a business is the plank used for a seesaw, with the seat on the left representing the business' per unit costs, and the seat on the right representing the customer's subjectively perceived value (per unit value) of the business' products or services.



Since the value created by the business is the entire length of the seesaw plank, there appears to be only two ways to increase the business' overall value creation (i.e., length of the seesaw plank): the first and most obvious is to increase the customer's perceived value of the business' product or service thus extending the plank to the right, and the second and less obvious is to reduce the business' costs, thus extending the plank to the left.



There are many ways to reduce the businesses costs, and here is a partial list of the more obvious ways:

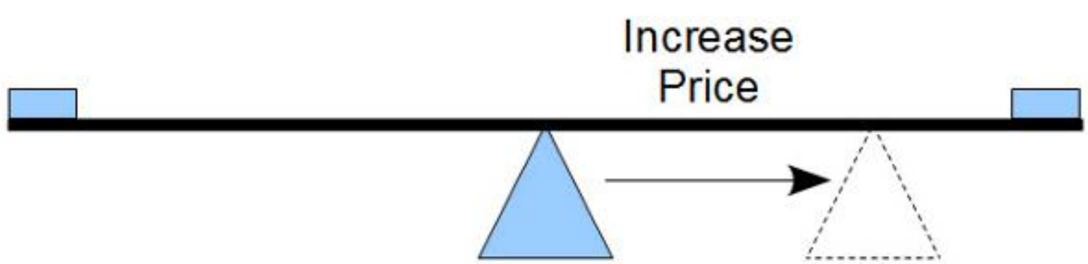
- Implement a six sigma/lean program to reduce waste / scrap, reduce inventories, improve quality of product or service, and improve efficiency resulting in more throughput and/or less overhead.
- Utilize design of experiment (DOE) techniques to capture the qualities most important to the customer, while minimizing the cost to deliver.
- Negotiate more aggressively with suppliers for reduced raw material costs.
- Relocate facilities to reduce transportation costs.
- Capture economies of scale where possible.
- Reduce learning curves through acquisition and/or knowledge sharing.
- Upgrade to more efficient equipment.
- Leverage fixed assets through automation (aka operating leverage).
- Optimize your CCC (cash conversion cycle).
- Obtain more favorable financing and optimize the company's WACC (weighted average cost of capital).
- Relocate to more favorable regulatory conditions, tax conditions, labor costs, and/or closer to raw materials sources, all to reduces costs.

Now lets move on to the customer's perceived value with a partial list of the more obvious means for increasing this:

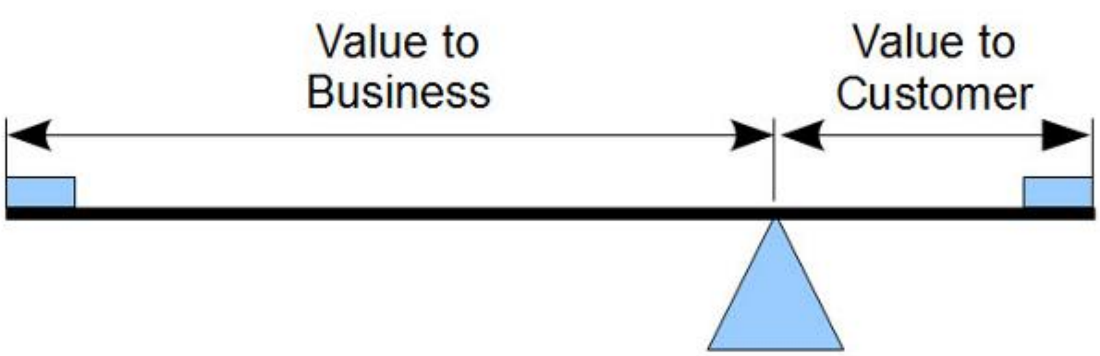
- Utilize surveys via conjoint analysis and cluster analysis to understand the various groups of customers that exist, and what they specifically value.
- Use focus groups and voice of the customer (VOC) interviews to test theories and to further develop a deeper understanding of your customer's needs / wants / pains.
- Conduct contextual research of financial reports, analyst reports, magazines, trade journals, newspapers, and internal customer service and sales databases. Combine this data to discover the bleeding edge (cutting edge) of the customer's needs / wants / pains. Also use this data to quantify the size of the market opportunity, competitors within the market space, your market penetration, and the growth rate of the market.
- Analyze of your business' true strengths and competitive advantages, and leverage these in your product and service offerings.
- Synthesize all of the data above to develop market and customer segmentation, then develop specific value propositions targeting each of these segments, utilizing your business' strengths and opportunities.
- Analyze product offerings, bundling lower valued products in with higher valued products for free or a reduced price, thus increasing the perceived value of the higher valued product, and if bundling substitute products, thus eliminating cannibalization of the higher valued product. Use contribution margin to analyze which products and services are profitable, and which are not, and either bundle or discontinue the non-profitable products and services.

- Use contribution margin to determine which customers are profitable, and which are not, eliminating the unprofitable customers. Look at the customer's total portfolio of products and services used with the business though in making this decision. The pareto principle holds true in that 20 percent of customers typically supply 80% of revenues, so make some logical choices of which customers to discontinue serving because they are not economically viable.
- Finally, launch marketing campaigns targeting key customers with soundly researched and focused messaging based upon the various research conducted above.

In summary, operations and finance play a role in the reduction of costs, and marketing plays a role in the creation of customer perceived value, but we have not yet touched on sales. Where sales comes into play is to push the fulcrum (i.e., the triangle supporting the seesaw) away from the business' cost side of the seesaw (i.e., left side of plank), towards the customer's perceived value (i.e., right side of plank).



If the length of the plank represents the value created by the business, then the point in which the fulcrum and plank meet represents the unit price of the business' product or service, with the section of plank to the left of this point representing the portion of total value created that is kept by the business, and the section of the plank to the right of this point representing the portion of total value created that is kept by the customer. Obviously the business would like to have their sales staff push the fulcrum as far to the right as possible.



By pushing down on the left side of the seesaw, you will see that much more leverage is obtained by having the fulcrum point pushed further to the right, and this is real financial leverage that is obtained by capturing more of the value that has been created by the business. The amount of value given to the customer, in return for the price paid by the customer must appear to be a fair deal to the customer or else the transaction will not occur. So sales' job must be to increase the perceived value as much as possible in the customer's mind, while increasing the price up to the maximum point acceptable to the customer for a transaction to occur.

The following is a partial list of the ways in which sales can achieve these goals:

- Sales should educate in the customer segments, their value propositions, and the product and service offerings and their target pricing.
- Collateral should be supplied to the sales staff that relays this consistent message – the customer's value proposition, and the business unique ability to fulfill this.
- Sales should maintain a database of their current and potential customers, and this database should be shared throughout the sales organization and the business. All knowledge known of a customer should readily be available to any employee who interfaces with the customer, and this same system should allow all customer interfacing employees to input their knowledge of their customer.
- The business must realize that they engage the customer not only at the point of sale, but at numerous other points along the customer's lifecycle, such as onboarding / set-up, training, customer service, and invoicing, and that each of these touch points must be coordinated and consistent in their messaging, and are an opportunity to enhance the customer's perception of the value they are receiving, and are additional opportunities to sell additional products and services to the customer.
- Implement a Solution Selling program. A good source for this is Keith Eades http://www.spisales.com. Solution selling is a process where you first learn your customer's needs, then create a vision in their mind of an end state which just happens to fit with your suite of product and service offerings. This is sometimes also called consultative selling or action selling – but in the end they are all the same thing.