



Service Dominant Logic

As academics attempt to understand the rapidly changing world of modern marketing, a new theory tries to make sense of what is going on. Simon Young investigates.

Something is wrong with marketing. Or rather, there's something wrong with the way marketing is taught: it doesn't reflect reality. For 100 years or more, we've taught that marketing is about moving products from manufacturer to consumer. And yet common sense tells us it's about more than that. Instinctively we know that product-centred thinking gets in the way of what we should really be about.

Service-dominant logic is the academic world's attempt to understand what's really going on, and help us understand why what we're doing works – even when it breaks all the rules.

It started when Stephen Vargo went back to school. Vargo already had an MSc in Social Psychology before beginning a career in marketing and management. When he returned to academia 10 years ago, he chose to focus on services marketing, reflecting his real-world experience.

But things just didn't make sense. "Could we really be just reaching a service economy," he asks. "Could there be a separate services marketing and a goods marketing – does any of that make sense? Or are we somehow looking at the whole thing wrong?"

Vargo, now associate professor of marketing at the University of Hawaii's Shidler School of Business, did an in-depth analysis of the histori-

cal models used to explain markets. "What it kept pointing to is that goods, not service, are the anomaly," he says.

Vargo joined forces with Robert Lusch, head of marketing at the Eller College of Management in Arizona, then researching resource management. Together they built the framework of service-dominant logic, an underpinning logic to the way we see value, markets and marketing.

The pair released their first paper, "Evolving to a new dominant logic for marketing" in the *Journal of Marketing* in January 2004. While most papers present a finished theory, Vargo and Lusch broke with tradition to present a possibility, a work in progress.

Even more radically, the paper was accompanied by seven commentaries by top scholars, something unprecedented in the journal's history. "It immediately started to be a dialogue," says Vargo.

Many academics saw service-dominant logic as explaining something they'd sensed but not articulated.

Through 2004, service-dominant logic was the topic of panel discussions at marketing events in the United States and Europe. It came to New Zealand in November 2005, when

Ice Cream

Milind Malik uses a tasty example to teach his students service-dominant logic. The Manukau Institute of Technology senior lecturer in marketing encourages his students to imagine an ice cream.

"If you just sit and look at it, are you getting value from it?," he asks. "No, it just sits there and melts away. You get the value in using the product. That's the same with every product – value in use."

Malik has mixed responses from his students. "Some look at me like I'm crazy; others are really onto it," he says.



From 4 Ps to 10 FPs

If it's true, service-dominant logic renders the four Ps – the cornerstone of current marketing teaching – irrelevant.

However, service-dominant logic is not yet a theory, so it doesn't yet have any "how to's". Instead, it has a set of very interesting premises, called Foundational Premises (FPs) by Stephen Vargo and Robert Lusch, the academics who coined service-dominant logic.

They began with eight; now there are 10. Vargo says he can't stick with 10, ("because they get called commandments all the time!") so watch out for another FP soon.

Here they are, in their latest form:

FP1: Service is the fundamental basis of exchange.

It's about service, even when it seems to be about goods.

FP2: Indirect exchange masks the fundamental basis of exchange.

Goods, money and institutions seem like something different, but they're actually the same – exchanging service for service.

FP3: Goods are distribution mechanisms for service provision.

Goods are only valuable if you use them. Value comes from the service they provide.

FP4: Operant resources are the fundamental source of competitive advantage.

Operant means active, dynamic. Traditionally, economics and marketing have been about operand resources – resources that are acted on, like water, coal and gas. Service-dominant logic sees competitive advantage coming from operant resources, like skill, knowledge and expertise.

FP5: All economies are service economies.

While this seems self-explanatory, Vargo and Lusch get pretty tetchy if you try to call it 'services' economies. It's 'service' not 'services', because services sound like just another kind of goods. Service, on the other hand, is an underlying reality, becoming more and more apparent with increased specialisation and outsourcing.

FP6: The customer is always a co-creator of value.

In other words, you cannot create value in a vacuum. Instead, you do it in dialogue with your customer.

FP7: The enterprise cannot deliver value, but only offer value propositions.

This carries on from FP6. You can only create and deliver value once your customer has accepted your value proposition.

FP8: A service-centred view is inherently customer-oriented and relational.

When your customers have a say in how they are served, it only follows that your marketing will be customer oriented and relational. It can't not be!

FP9: All economic actors are resource integrators.

Nothing to do with George Clooney. An economic actor is someone who participates in the economy – in other words, all of us. A resource integrator is someone who brings resources together – usually thought of as the role of the company. This follows on from recent economic thought which acknowledges households and individuals are as much resource integrators as companies.

FP10: Value is always uniquely and phenomenologically determined by the beneficiary.

Phenomenology is not the study of poltergeists, but instead the way we see and understand things, regardless of objective reality.

So this last FP means each customer has their own way of determining exactly how valuable your product – sorry, service – is to them. It depends on a number of things, including the context in which your service is delivered. Customers also create their own meaning for the service you offer, which has implications for branding in the future.

As Waikato Management School marketing professor Richard Varey says, "How do we explain a brand if a valuation is by the customer? You can suggest or propose a brand, but you can't deliver or impose it on anyone. They'll make an evaluation of why it's important."

Otago University hosted the Otago Forum, a gathering of over a dozen international marketing academics, including Vargo and Lusch, to move the conversation forward and reach a better understanding of what was going on.

The forum also dominated a special issue of *Marketing Theory*, which featured papers presented at the forum and also asked the wider academic community to continue co-creating the future of marketing. As the editorial reported, "The emphasis over the three days [of

the forum] was on dialogue and interaction. While papers were presented, they were clearly starting points for discussion and continued dialogue."

In 2006, Vargo and Lusch published *Service-dominant logic: reactions, reflections and refinements*. The book was co-written by around 50 academics responding to the ideas in the original paper, including those who disagreed with Vargo and Lusch. You could say they were eating their own dog food. One of the foundational premises of the paper stated that the

value of service-dominant logic is in its open, collaborative effort.

Two academics who took up the invitation to respond and contribute a chapter were Richard Varey, professor of marketing at Waikato Management School, and David Ballantyne, associate professor of marketing at the University of Otago.

"David and I were just amazed when we saw this call for the book chapter," says Varey. "It absolutely gelled what we'd been doing for some time." Ballantyne's background was in re-



David Ballantyne.

In A Nutshell

There are two different logics we can use to look at how business works – goods-dominant or service-dominant. Goods-dominant thinking assumes firms exist to make and sell things, preferably tangible things (goods). Goods are produced away from the market, and standardised to ensure efficient production.

According to goods-dominant logic, value is created at the point of production, and delivered when the product is distributed. The value lies in the product itself. Services are either an add-on to goods, or an inferior type of goods. Why inferior? They're everything products shouldn't be – intangible, custom-made, fleeting, and production and consumption happen all at once.

Service-dominant logic, as presented by Vargo and Lusch, proposes that all business is about the exchange of service for service. They're not talking about the rise of a services economy; they're saying it's always been about service for service, even when it looked like manufactured goods. In service-dominant logic, goods are merely an appliance for service delivery, meaning every business – including yours – is a service business.

Vargo describes goods-dominant logic as "marketing to" customers, and service-dominant as "marketing with" customers.

It's something we've probably known for years – every advertising student knows that people don't buy drills, they buy holes. But while we understand that on an intuitive level, the structure and theory upon which our day-to-day jobs are based has goods built into it. Some major reconstruction is required, and Vargo and Lusch believe service-dominant logic is where it starts.

relationship marketing for 15 years, and Varey had published a series of textbooks on internal marketing, marketing communications and relationship marketing. Both academics had seen the need for a different approach to marketing.

"The idea was the firm providing service, rather than providing goods," says Varey. "It seemed like a simple, almost insignificant shift in thinking, but it's got profound implications."

Varey sees service-dominant logic as providing a central point of focus for other emerging marketing trends. "Relationship marketing, knowledge management, social responsibility – all those ideas seemed to come into clearer

connection if you put service, rather than distributing manufactured goods, as the purpose of the firm," says Varey.

For Ballantyne, too, Vargo and Lusch's original article brought together a lot of disparate parts. "It seemed to bring together service, relationships and two-way or interactive communication," he says. "It says the industrial revolution has come to a review point around the nature of service." If the nature of service is different from what we thought it was, it means other things might be different as well. For instance, branding, relationships, and managerial strategy.

Further north, Vargo and Lusch were also

ringing bells for academics at the University of Auckland's business school. Since 1996 the business school has participated in the contemporary marketing practices (CMP) programme, a worldwide study that asks executives about the big picture changes they're experiencing.

"What we were hearing from the ground up was, 'we're trying to change from a product-centric approach, but we're moving past that approach to something else – but we don't know what it is'," says Richard Brookes, deputy head of marketing at the Auckland University Business School. "The Vargo and Lusch paper just clicked when we read it."

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Who's Doing It?

Honda New Zealand

When Honda won the Supreme Award at the 2007 *NZ Marketing Magazine* Marketing Awards, the judges said Honda "epitomises the service-dominant logic of marketing", and that it was among a group of companies "rewriting the rules for product marketers".

They did it through a tight focus on the customer experience after purchase, designing the desired customer experience and adjusting the rest of their business to suit.

Such an undertaking doesn't happen overnight, but it does happen, as Honda's top sales results, and marketing award, shows. (See the full case study in *NZ Marketing Magazine* August 2007 issue, available online at www.marketingmag.co.nz.)

Interface

You may have seen this carpet manufacturer in the documentary film *The Corporation*. Waikato Management School's professor of marketing Richard Varey describes the company's leasing model.

"They lease you a carpet, maintain it, recycle it when it's worn out. You pay for the use of it," he says. "It's like leasing a car or a photocopier. They are still responsible for what happens to it when it's not in use."

Varey notes the bottom line for interface is not profit but efficiency. In the process of pursuing efficiency, profit arises naturally.

"They describe it as an alternative model – I'd say it's almost a service-dominant logic model," says Varey. "They produce carpets

which will enable customers to realise value, they're not going to simply deliver goods. That's what S-D L is all about."

Fisher & Paykel

"My wife's away in Australia at the moment," explains David Ballantyne, associate marketing professor at the University of Otago, "so I get to do things that blokes don't normally do, like playing with the buttons on the washing machine."

Ballantyne was impressed when he came to press the buttons on his Fisher & Paykel machine. "There's very little opportunity to make an error. It was organised around an intuitive logic," he says. "This is where a product really does become a service, because the service is valued in use."

Listening Post

Hamilton-based hi-fi shop Listening Post is a smaller-scale example of service-dominant logic, according to Varey. "They help their customers, through their expertise and knowledge, to experience the soul of the musician," says Varey. "The equipment they sell is just the means to do that."

Varey compares that approach with the approach of most department stores, where "you ask for a stereo and get a cardboard box with a price on it". Varey's more interested in how to realise the music in the best way possible.

"They've probably never heard of service-dominant logic, but they're serving their customers," he says.



Rod Brodie.

Rod Brodie, associate dean and co-founder of the CMP programme, says 80 to 90 percent of CMP respondents no longer saw a point to having a separate services course. Makes perfect sense if you see everything as service – not to be confused with "services".

"I initially wrestled with Steve a bit," says Brodie, "because the problem is that service is so close to the word services. Some of our distinguished colleagues, like Philip Kotler, think that's what we're saying." (See FP5 in box story, "From 4 Ps to 10 FPs".)

Service-dominant logic hasn't been confined to the academic world. In fact, all the academics involved acknowledge their job is most often to follow what's happening in the "real world" and provide understanding around that.

Vargo is now working with IBM in developing what they call service science. Through a happy accident, Vargo met Jim Spohrer, director of

Almaden Services Research at IBM's Almaden Research Centre.

"Spohrer somehow got hold of our article and sent us a note saying this stuff is foundational to the service science we're trying to create," says Vargo. They have now been collaborating for nearly two years.

The collaboration is extending to Auckland University's business school, which launched a postgraduate course in Services Science. Although it's called Services (not service) Science, it contains many of the ideas behind service-dominant logic.

It also contains the creative collision of disparate disciplines. IBM's corporate affairs manager in New Zealand, Debbie Noon, says service science combines hard and soft sciences. "You need to take into account the technology, of course, but you also need to take into account the socio-cultural context in which you oper-

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Dissenting Voices

Andrew Hughes, a marketing and management lecturer at the Australian National University, probably echoes the thoughts of many marketers when he says service-dominant logic isn't yet workable.

He asserts that because service-dominant logic doesn't describe in specific, measurable terms how it affects a company's bottom line, it's not yet roadworthy for use by marketers in the same way the 4 Ps are.

And Vargo doesn't claim it is a useable theory. "Service-dominant is a logic, a mindset, a lens, but not a theory," he says. "It could provide the foundation for a grand theory of exchange."

While some criticise the non-theory for being too theoretical, others say it hasn't gone far enough away from current product-based thinking. Griffith University's Sharon Shembri, one of the attendees of the 2005 Otago Forum, asserts that the logic, while true, doesn't go far enough. "A focus on the product as either goods or services negates any focus on how the customer experiences that product," she writes in *Marketing Theory*.

Vargo is quick to admit there is a necessary stage of transition needed for people to understand the new way of thinking. So while the old thinking led to promotion and the new thinking is dialogue, a transitional concept is integrated marketing communications.

On a bigger scale, the past was "to market", the present, transitional concept is "market to", and the eventual goal is "market with".

ate," says Noon. "That's what brings in what we call the human factor – psychology, how people communicate, how they perform, change management – because you can't introduce a new system or process unless you take into account the people who will use it."

Meanwhile, service-dominant logic has become part of the conversation in every research-active university marketing department, says Varey. "It's changing our curriculum or

giving us research projects we didn't think were important," he says. "It's such a big thing, we could go back and almost recast all the existing orthodox literature."


Varey predicts a large output of revised textbooks over the next two to three years, while Ballantyne says the concept should make its way into practitioner-land in a few years.

"I think it's just a bit early yet," he says. "It's hard for practitioners to make the connections.



Jim Spohrer.

It's a tightly structured theoretical piece." However he has no doubt service-dominant logic will eventually become mainstream thinking and practice. "The same thing happened with relationship marketing," he says. "Basically it was a sleeper for 10 years, then took off in the early '90s."

Back in the classroom, service-dominant logic is being taught alongside more traditional theories. Milind Malik, a senior lecturer at Manukau Institute of Technology, says he gets mixed reaction from his students when he presents the ice cream analogy (see box story: "Ice Cream"). "Students who read widely are always open to new ideas," he notes. "Students who stick to the textbook won't be." 

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If you do what you've always done, you'll get what you've always had.



The definition of 'brand management' has evolved. It will always encompass defining and promoting what a business stands for, but increasingly it also covers managing 'how' that business behaves and 'what' it delivers. In this context companies have five choices for managing their 'business brand':

1. Do nothing
2. Talk a lot but still do nothing
3. Commission expensive window dressing
4. Up the game – refocusing or extending what you offer
5. Break the game wide open...

Only the last two make sense from a business perspective. DNA is working with two New Zealand businesses that understand this.

Securing the future of an iconic New Zealand retail business

Tyres are usually a 'grudge' purchase, retailers compete on price in a tight market, and the major players invest heavily in TV advertising. Bridgestone New Zealand (Firestone's parent) needed to protect and grow Firestone's market-leading share in this environment.

A review of Firestone's market offering was undertaken. Key to this was the insight that customers increasingly expect more from the retail experience. Younger women and urban/metro groups in particular feel out of their 'comfort zone' in a workshop environment.

The actions required to meet these 'human' needs were captured in a brand definition that sets new performance benchmarks, because delivering a superior customer experience is the only way to build more positive, ongoing relationships. Tyres are still core business and price is fundamental, but Firestone must become more than a tyre workshop.

The answer lay in an extended 'combination' offering providing increased 'care' for customers and their vehicles:

- A True Retail Store Experience – better, more people-friendly environments.
- Vehicle Health – expanded product/service range to keep your vehicle healthy between mechanical servicing.

- Increased Service Delivery – the critical component.
- Evolved Firestone Brand Identity – telling the evolved story.

Roll-out is underway. Consumer research and sales figures are tracking well. John Staples, Bridgestone's General Manager Sales and Marketing is confident that "Firestone's expanded offering and evolved brand will secure the business's long term financial health... how long would Firestone maintain market leadership if it hadn't undertaken a process that literally tested and evolved the company's thinking?".

Reinventing a commodity exporter

Whangarei's Legacy Timber has been a building company, a pioneer of export timber mouldings and a supplier of beams for traditional Japanese housing. Most recently it manufactured clearwood edge glue laminate panels for DIY shelving products here, in Australia and Japan. However, vulnerability to exchange rate fluctuations was having an impact.

Legacy approached DNA having identified the need to get out of the 'commodity bind' where price is always the issue. Together we developed a strategy for Legacy to become a design-led ideas company offering 'unique' products.

These have been developed around potent consumer insights to ensure the development of ongoing brand relationships. We've also forged new channels to market, crafted a powerful brand platform and evolved integrated research, development and design capability – all of which has seen Legacy reinvented as a business that is the brand.

HOLD is the outcome – understanding the common human urge to collect 'stuff' (valuable, sentimentally significant objects, images and artworks) and display it as expression of self. HOLD offers a growing collection of innovative products for managing this 'stuff' in our lives. These include TAAPA, a diverse range of shelving layouts (made from sustainable wood) that can be customised to feature a surprisingly wide range of personal treasures, CAPTURE, a unique and flexible system for showcasing photo's and SHOW, a beautiful and functional wall mounted system for curating precious items, books, CDs etc.



Firestone – understanding the customer retail experience so it can become more than just a tyre workshop.

Test release through selected local retail outlets from late 2006 far exceeded expectations and the brand won a 2007 Best Product Design Award.

Significant orders have come from top-end US chain and design stores following HOLD's launch at two US trade shows. Hotel designers there have shown interest and the product is soon to feature on the Oprah Show and the HGTV Home Garden Show.

HOLD's recent launch in Paris also went well and negotiations are underway with top European and UK design stores. Product launch in Australia is currently being scoped and HOLD will feature at the Tokyo 100% Design Trade Fair in late October.

What choice does your business have – number four or number five?

If you'd like to explore how you can better meet customer needs or tackle changing market dynamics phone Nick Sampson on 09 375 1592 or Mike Meachen on 04 499 0828, or visit www.dna.co.nz

HOLD – escaping the 'commodity bind' has revolutionised a traditional family business. Hold's future is now about design-led product development based on 'human' needs.

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SHOW



CAPTURE



“The true joys in my life. My family and grandchildren.”