

SERVITIZATION STRATEGY  
AND MANAGERIAL  
CONTROL

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STUDIES IN MANAGERIAL AND FINANCIAL  
ACCOUNTING

# SERVITIZATION STRATEGY AND MANAGERIAL CONTROL

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# CONTENTS

ABOUT THE AUTHORS	vii
INTRODUCTION	1
CHAPTER 1 THE SERVITIZATION OF MANUFACTURING: WHY AND HOW <i>Anna Pistoni and Lucrezia Songini</i>	5
CHAPTER 2 SERVITIZATION STRATEGY: KEY FEATURES AND IMPLEMENTATION ISSUES <i>Anna Pistoni and Lucrezia Songini</i>	37
CHAPTER 3 STRATEGIC MANAGERIAL CONTROL FOR SERVITIZATION STRATEGY <i>Anna Pistoni and Lucrezia Songini</i>	111
CHAPTER 4 CASE STUDIES <i>Anna Pistoni, Lucrezia Songini, Paolo Gaiardelli and Sara Pegoraro</i>	225
CONCLUSIONS	311

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# INTRODUCTION

In times of economic crisis, the manufacturer value chain is becoming less attractive as the demand for products is increasingly stagnating. Under such circumstances, companies are progressively becoming aware of the value associated with service offerings. Services provide a more constant income and higher profit margins; however, they also need less capital investments than goods.

Particularly in developed economies, the intense pressure on manufacturing organizations are driving many innovative manufacturers to differentiate their products by offering additional services. The traditional boundaries between manufacturing and service firms are breaking down across the globe. To survive, many manufacturing firms have to move beyond manufacturing and offer services and solutions, often delivered through their products, or at least in association with them. This strategy is called “servitization”; it encompasses new business models based on the product-service system (PSS).

From a practical perspective, companies are increasingly approaching servitization, changing their business model and aligning their strategy. A few examples of servitization strategy, and its main drivers and impacts, are highlighted below. Low oil prices have reduced the prices of raw materials for a number of sectors such as chemicals, rubber and plastics. Under the pressure of their customers, manufacturers in these industries have had to reduce also their selling prices, and consequently they have seen a margin decrease. Some companies have been responding to these heavy pressures on margins by refocusing their innovation activity, both maintaining a high level of process innovation and increasing the level of service innovation. The weight of companies in these sectors engaged in service innovation has rapidly increased from 17% in 2014 to 40% in 2015.<sup>1</sup> Since the 1990s, IBM started to follow a

strategy that can be considered a servitization of the business. According to the industry trend and in the light of his better understanding of customers' needs and ongoing business demand, IBM's CEO recognized that the market was shifting. Thus, he pushed the company to move up in the value chain from production of hardware and to reinvent itself as a provider of business solutions, based on a portfolio of consulting, delivery and implementation services, enterprise software, systems and financing.

There are several reasons why manufacturing firms should evolve strategic emphasis on services: the servitization strategy may provide financial opportunities, strategic opportunities as well as marketing opportunities. Companies find servitization as a way to increase value and differentiate themselves from competitors. Services are important sources of revenue for manufacturing firms especially when industries mature and the firms can no longer easily differentiate their products.

However, even though the positive impacts of servitization are convincing and promising, environmental arguments are compelling, and opportunities for manufacturers are very high, there is still a lot to be learnt by academics, practitioners and organizations.

The servitization of manufacturing is a growing and relevant area of research that in the last few years has attracted an increasing amount of attention in management, marketing and operations literature that mainly aims to explain why and how to servitize. However, a connection between academia and practice is essential to the foundation of this research to continue with its development and to contribute to improving the implementation of servitization strategies in companies.

Approaches from a variety of disciplines have led to insightful studies on the practical implications for businesses. Actually, the transition toward servitization is a complex and challenging process, requiring clear strategic thinking, devoted resources, planning tools and support mechanisms. If these aspects are not properly managed, the risks of failure are very high, as is well documented by empirical evidence. Several recent studies have showed that servitized firms sometimes generate higher revenues but deliver lower profits than pure manufacturing firms. Within those enterprises that might be interested in implementing a servitization strategy, the significant change in the system of gaining profit could deter producers from employing consistently this concept for the following main reasons: the lack of experience in structuring an organization to be competent at designing, making and delivering the new product-service offering; the limited experience in pricing the offering; and the fear of absorbing risks that were previously assumed by the customers.

This book, through both a theoretical and an empirical approach, aims to analyse the servitization phenomenon from a wide perspective, highlighting the main challenges that companies interested in servitization have to overcome, in order to successfully implement this strategy. Attention is specifically on managerial control mechanisms that can better support the servitization strategy.

The role and characteristics of managerial control for servitization are quite underdeveloped issues, both in research and in practice, notwithstanding that it may help in capturing the features of servitized firms and then modelling, measuring and evaluating their impact on corporate financial performance and its determinants. However, to support servitization strategies, managerial control mechanisms have to be designed and implemented consistently with the distinctive characteristics of servitized firms.

The book is organized into three theoretical chapters followed by the fourth chapter focused on empirical evidence. A final chapter presents some concluding remarks.

In Chapter 1, a framework of the servitization phenomenon is offered. After the analysis of the main definitions and content of servitization, relevant determinants that can explain why companies approach this kind of strategy are taken into consideration and discussed.

In Chapter 2, the main practical implications of servitization are analysed. They represent the relevant choices that a company has to make in order to successfully implement the servitization strategy, such as the service offering design, the organizational change, the cultural shift and financial implications.

Chapter 3 discusses managerial control systems and presents the specific mechanisms devoted to planning and monitoring of the key variables of the servitization strategy, both in the long term and in the short run. In the context of servitization, particularly important is the role of strategic cost management mechanisms. In fact, on the one hand, the servitized firm has to design a service offering able to be profitable during the whole product-service life cycle; on the other hand, they have to develop control mechanisms to monitor the short term profitability. In this chapter, we propose that servitized firms have to implement two main types of strategic managerial control mechanisms, and we present their role, characteristics and issues critical to implementation in servitized organizations.

In Chapter 4, some empirical evidence on both the servitization strategy and its impacts on the enterprises and managerial control systems for servitization is outlined. Four case studies are presented and discussed, from two main industries, the printing and photocopier sector and the automotive industry, which have pioneered the introduction of servitization and the

development of consistent managerial control systems. The final section of Chapter 4 deals with the servitization strategy in a specific sector, namely the heavy commercial vehicles (HCV) industry.

This volume may represent a useful tool for those companies interested in the development of successful servitization strategies and for scholars involved in research on this challenging, interesting and very up-to-date managerial topic.

In particular, it may be of interest for top management and middle management in charge of strategic and organizational issues as well organizational units such as supply chain, logistics, production, after sales and service, R&D, strategic planning and managerial control.

Interested companies comprise, but are not limited to, manufacturing firms operating especially in durable goods industries where the role of services is relevant to the product life cycle.

Consultants and practitioners involved in strategy, organization, manufacturing, operations, supply chain and managerial control may also find this volume interesting.

Among academics and researchers, people involved in many research fields such as strategy, strategic planning and managerial control, operations, supply chain, logistics, after sales and services, production, and R&D may be interested in this book.

Even though the volume represents the outcome of a joint work and combined efforts of the authors, the specific contribution of each author to each chapter is outlined below. In particular, Anna Pistoni has written Chapter 1 and Sections 2.1, 2.2, 2.3.1, 2.3.2.1, 2.3.3, 2.4, 2.5, 2.6, 3.3.2, 3.3.4, 3.4.3, 3.4.4, 4.2, 4.4, 4.6 and 4.9. Lucrezia Songini has written Sections 2.3.2.2, 2.3.2.3, 2.3.2.4, 3.1, 3.2, 3.3.1, 3.3.3, 3.4.1, 3.4.2, 3.5, 4.1, 4.3, 4.5, 4.7 (with Sara Pegoraro) and 4.8 (with Paolo Gaiardelli).

## NOTE

1. EEF The manufacturer organization (2015). *Innovation monitor*, <http://www.eef.org.uk>