



**Phil Anderson** is a Client Director at Ashridge. He teaches, consults and leads research in service operations focusing on process improvement, the impact of people and culture and operational excellence.

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Email: [phil.anderson@ashridge.org.uk](mailto:phil.anderson@ashridge.org.uk)



**Malcolm Locke** is a Director of Everymind, a strategy and management development consultancy. He is an Ashridge MBA alumnus.

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Email: [malcolm.locke@everymind.co.uk](mailto:malcolm.locke@everymind.co.uk)

# Jumping off the service excellence bandwagon

**It's increasingly hard for companies to differentiate themselves through service excellence. However, Phil Anderson and Malcolm Locke share research that demonstrates how operational excellence is a strategic option for sustainable success – for those brave enough to jump off the bandwagon.**

As Diane entered the boardroom she just caught the end of her CEO's closing remarks: "... so, in conclusion, differentiating ourselves on service should be our aim for the coming year." As her colleagues filed out, she overheard some of their comments.

"What are you going to do?" said one. "Well, for a start, we're going to build relationships with customers in our call centres instead of monitoring call duration times. What about you?"

"Interesting, I'm going to spend time working on ensuring our fulfilment operation enhances their on-time delivery."

Another was heard to say, "I'm going to develop all my customer contact people to be fully conversant across all products."

Diane was confused: three different definitions of improved customer service – furthermore, all their competitors were following the same service excellence approach.

## The value disciplines theory

The message of *The Discipline of Market Leaders*<sup>1</sup> is that no company can succeed today by being all things to all people. It must instead find a unique value that can deliver to a chosen market. Value disciplines are the desirable ways in which a company can combine its operating model and value proposition to be the best in its markets. Three distinct value disciplines are defined:

*Operational excellence* – provide products and services at the best price and with the least inconvenience through focus on cost management and operational effectiveness, eg Dell and Wal-Mart.

*Customer intimacy* – deliver what specific customers want by cultivating deep and lasting relationships, eg The Ritz Carlton and Airborne Express.

*Product leadership* – offer the best products through focus on innovation, eg Intel and Nike.

To be successful a company must relentlessly focus on one value discipline, such that it is the best in that area, while being at least industry average in the other two disciplines.

Sound familiar? Have you thought of jumping off the service excellence 'bandwagon'? Operational excellence could be the answer for you – it has been for others. Opodo, Tesco and IKEA have and the results are impressive. Opodo, an online travel agent launched only three years ago, now attracts and handles over 15 million customers every month across Europe. Tesco dominates UK grocery retail with 29% market share. IKEA has averaged revenue growth of 20% per annum for the past eight years.

When we asked service company executives about their organisation's strategy, service excellence was the main aim for most. But, how can individual companies differentiate if everyone is operating with the same approach? We believe pursuing operational excellence as a strategic focus provides that opportunity.

### Operational excellence vs. service excellence

Operational excellence is one of three fundamental ways of creating shareholder value identified by Treacy and Wiersema in their book *The Discipline of Market Leaders*<sup>1</sup>. The authors argue that only companies that relentlessly pursue one of three value disciplines – *operational excellence*, *customer intimacy*, or *product leadership* – will succeed.

Operationally excellent service companies provide their services at the lowest cost and highest convenience for their customers: low price and hassle free service. The retailer Zara and fast food company McDonald's are examples.

In contrast, customer intimate (or service excellence) companies cultivate relationships with their customers and strive to satisfy their unique needs. They travel the extra mile for their selectively chosen clients. The bespoke holiday agent Powder Byrne is an example, as are Airborne Express, BUPA, and The Ritz Carlton.

Whilst service excellence is about striving to exceed customer expectations, operational excellence is about delivering an acceptable service at the lowest total cost. **Figure 1** below, is based on our research, supported by findings from both the Ashridge MBA Alumni Conference attended by 80 executives in November 2004, and from discussions with our colleague Tony Cram – Ashridge faculty member, specialising in Customer Relationship Management.

**Figure 1.**

Operational excellence vs. service excellence



## How to be operationally excellent?

Increasing demand from both consumers and business customers for speed, convenience and price competitiveness suggests that operational excellence is a strong option for service businesses.

However there is a lack of guidance for service companies on how to achieve operational excellence. Much is written about service excellence and about operational excellence in manufacturing industries, where it is a well-embedded approach. But there is very little literature devoted to the subject of operational excellence in services.

We undertook research to help fill this gap. Our aim was to provide guidance to the many service companies we came across who were keen to jump off the service excellence bandwagon and do something different. Following a modified systematic review<sup>2</sup> of the literature of some 200 articles, a survey of more than 40 companies and in-depth interviews with seven operationally excellent service organisations, we are confident we can offer assistance.

We identified 35 characteristics of operationally excellent service organisations (OESOs). All 35 play a role in contributing to the operational excellence of an organisation. To view a full list of these characteristics, please visit [www.ashridge.com/360](http://www.ashridge.com/360). For the purposes of this article, we have picked out the six most important clusters of characteristics and illustrated them with examples of best practice from operationally excellent firms.

## 1. Strategic management

The fundamental strategic framework for OESOs consists of lowering cost and increasing quality. The two are not mutually exclusive. Increasing quality can drive out

cost through fewer errors and less waste as exemplified by Toyota. There is a virtuous strategic cycle for OESOs of lower costs resulting in lower prices that attract customers and increase sales productivity. easyJet, Amazon and parts of UBS adopt this policy to great effect.

Strategic management is carried out in a centralised, standardised and directed way with top-down control. The management team set strategy and review it frequently. Strategic messages are carefully crafted and communicated to all members of the organisation. From this, job responsibilities and objectives are clearly defined.

OESOs use simple strategic messages to communicate to their staff the importance of lower costs and higher quality. One investment bank we contacted as part of our research tells their staff to take the bus not the tube. Many use the popular mantra of "Think of it as your money – would you still spend it?" The message in a fast growing, online, logistics company is "every touch counts".

## 2. Cost management

Finding cost advantages is a continual process. It is important that the finance and operations team work closely together. They must jointly understand the business, cost structure and opportunities to reduce costs. Prerequisites that underpin effective collaboration include: team working; effective accounting systems; and accountants with good business and process knowledge<sup>3</sup>.

At Opodo senior business managers check that staff have taken the cheapest deals for business travel every month. They also monitor staff phone usage to ensure they are not misusing company phone accounts. Another investment bank we contacted said that they were being asked to commit to an 8% reduction in costs year on year.

## 3. Quality mindset and management

Quality mindset and management processes are at the heart of OESO success. Quality management supports cost reduction and the efficiency and quality of service delivery. There are numerous approaches. Many have been proven in manufacturing and are catching on in services.

**Lean thinking\*** is one of the most relevant approaches for all types of services but is not practised by the companies we researched. It is simple to understand, inexpensive to implement and can deliver stunning results. The US life insurer Jefferson Pilot reduced application turnaround time by 40%, increased sales by 60% and reduced labour costs by 25% as a result of applying lean thinking to the processing of new insurance quotes and applications<sup>4</sup>.

Operations innovation is another approach<sup>5</sup>. Some recommend step-changes in operations excellence in order to sustain competitive advantage. Progressive Insurance, a US motor insurer, grew revenue seven-fold in a decade by reinventing the claims handling process. Claimants can reach a Progressive representative 24 hours a day and adjusters, who work from mobile claims vans, will inspect a damaged vehicle within nine hours. This compares to the industry average of seven to ten days. Significant cost savings and customer loyalty trends have resulted. In contrast others, most notably Toyota, rely on continuous improvement for their operations innovation.

Some service companies have adopted **six sigma\*\***, the 'zero defects' approach to quality pioneered by Motorola and GE. The banks Citigroup and Bank of America are among them. One investment bank we spoke to thought that six sigma provides powerful analytics and a robust process.

However they are sceptical whether the return on investment justifies the level of input. They currently tolerate a 5% error rate in data. Although they should do better it is questionable as to whether the potential gains warrant investment to achieve zero errors. Other companies are using lean and six sigma together. They use lean thinking first to reduce waste and then six sigma to solve chronic underlying problems.<sup>6</sup>

A quality mindset is critical to the success of operational excellence. An example from the IT department of a global information provider is that when an IT hitch occurs in one country they will proactively check that the same hitch will not appear in all the other countries in which they operate. This avoids costly and wasteful downtime. Opodo gets the right mindset by telling staff to treat customers how they themselves expect to be treated by their payroll department. On time, in full, with no errors.

Technology is another critical factor in quality management. It can support breakthrough process performance improvements and reduce costs. However it can cause new problems and be very expensive. Consequently, OESOs are cautious about implementing new technology. They apply lean thinking first to ensure existing processes are optimised before considering IT investment. They will only invest in IT if there is a clear case for it and they will acquire what is absolutely necessary. No bells and whistles. Our research shows that they will acquire a proven technology rather than build something in-house.

## 4. Performance measurement and management

Measurement is pursued with religious zeal in OESOs. The commandment followed is that you can't improve or control what you

don't measure. Measurement is mainly focused on productivity, process performance improvement, cost saving and customer satisfaction. Measures are monitored and reported frequently, eg as often as several times a day for key performance indicators. The senior management team of the UK's largest electronics retailer receives sales figures by text in the morning and afternoon of every day. The figures are discussed and any necessary changes made the following day. A major international insurance company we contacted uses a 'dashboard' of data that provides real-time statistics on a host of business performance measures. Relevant measures are shared with all relevant staff in order to stimulate the desired behaviour and performance. The customer service directors in the call centre operations of Opodo and BUPA Insurance told us that it is essential that performance measures are posted for all to see, so that the customer service agents can understand the centre's impact on their customers and can take ownership for the response.

We asked all the companies who took part in our research for the most important measures they monitor on a regular basis. The top four metrics that emerged reflect their operational excellence focus (Figure 2). Finding 'profitability' at the top is no surprise. It's the prime goal for all for-profit organisations. More interestingly, perhaps, customer satisfaction is second and is seen as an essential measure for operational excellence. Service companies need to understand and shape their customers' expectations and focus relentlessly on achieving satisfaction by delivering to those expectations. Nothing less and nothing more.

Managing the performance of cost reduction initiatives is critical. Measuring process efficiency is key to understanding how service delivery processes can be improved. Performance measurement is worthless unless the company uses the measures to drive progress in activities that will deliver real bottom line improvements.

OESOs should also be fanatical about benchmarking. Our surveyed companies were generally poor at benchmarking. Several said that they collected data, but few actually considered benchmarking their processes. Opodo is an exception. It benchmarks against competitors and relevant 'best in class' service providers every month, monitors the trends and acts on the results.

## 5. Structure

OESOs structure themselves to be streamlined and agile. Streamlining reduces costs and increases the speed of service delivery. Agility also allows costs to be controlled and allows them to respond quickly to market changes.

They streamline themselves by outsourcing any process that does not add value to the customer or provide competitive advantage. The operations managers at one investment bank we spoke with need to justify why processes have not been outsourced rather than the other way round.

Organising workflow around processes rather than functional teams help OESOs to further streamline themselves. Jefferson Pilot, when introducing lean thinking, broke down functional barriers and organised teams around a set of linked activities for processing insurance applications<sup>4</sup>.

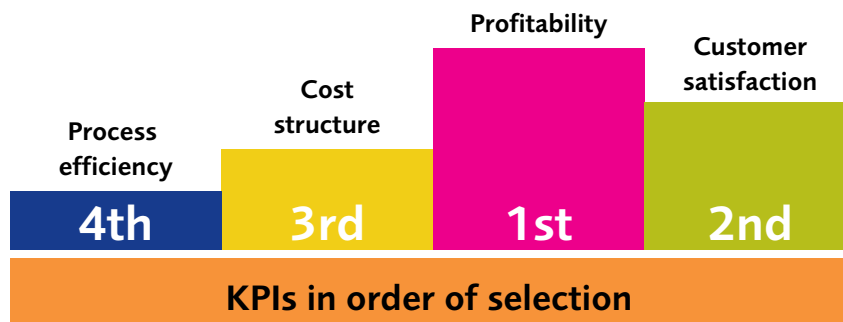
To increase agility, Knighton Optical, a US optician, has trained a multi-skilled workforce. Sales assistants are also trained to work in the lab to produce spectacles. This ensures the company can keep its promise of supplying new customers with spectacles in a short time when demand spikes<sup>7</sup>.

## 6. People and culture

As we have suggested earlier, culture in OESOs is all about reducing costs and improving operational performance. Senior

### Figure 2.

The top four key performance indicators (KPIs) used by operationally excellent service companies



managers have a key role through leading by example. In Dell, senior executives attend meetings with junior supervisors to discuss cost savings of the order of \$20K<sup>9</sup>. In BUPA Insurance, a healthcare provider, performance improvement is so important that all people have a line of sight to the chief executive's key performance indicators.

In building teams, our research demonstrates that OESOs largely prefer to recruit 'doers' rather than 'thinkers'. However in some quarters such as an investment bank we spoke with, the rise in outsourcing processes to 'doer' third-parties has led to an increase in recruitment of 'thinkers'.

OESOs empower their staff to solve problems and improve operations. At easyJet, staff in their call centres are incentivised to cross sell and close as quickly and efficiently as possible so they can move on to the next revenue generating call. This is in stark contrast to a Disney call centre where operators are encouraged to build the right relationship with the customer who might be about to book a holiday of a lifetime.

The six clusters discussed above cover the majority of the 35 OESO characteristics we identified in the course of our research. They have led us to believe that this truly is a sustainable strategy for organisations – both in the service and manufacturing sectors. However, not everyone seems to agree.

### Was Michael Porter wrong?

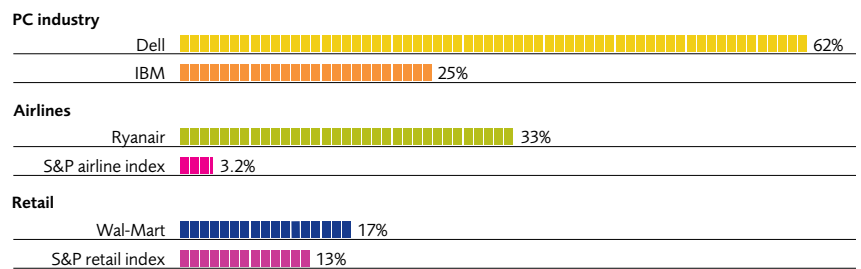
There is a conflict with our proposition for operational excellence and Michael Porter's argument that operational excellence (effectiveness) is not a sustainable strategy<sup>9</sup>. We believe there is evidence that challenges Michael Porter: operational excellence *is* a sustainable strategy. \*\*\*

Porter argued that operational excellence is not a sustainable strategy because it can be imitated. Therefore any competitive advantage is short-lived and, ultimately, limited. We support Porter for relatively simple service operations such as courier delivery (as opposed to couriers' complete supply chain solutions), and car rental operations.

However, we would argue that over the past decade, companies such as Dell, Ryanair and Wal-Mart have sustained significant competitive advantage through a strategy centred on operational excellence (Figures 3 and 4)<sup>10</sup>.

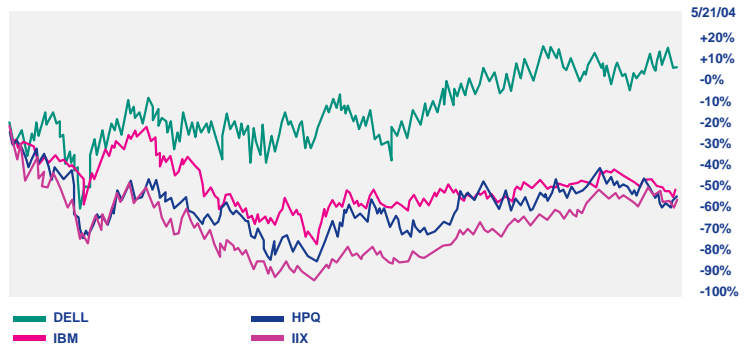
**Figure 3.**

Compound annual growth rates of Dell, Ryanair and Wal-Mart versus their peer groups 1993-2003



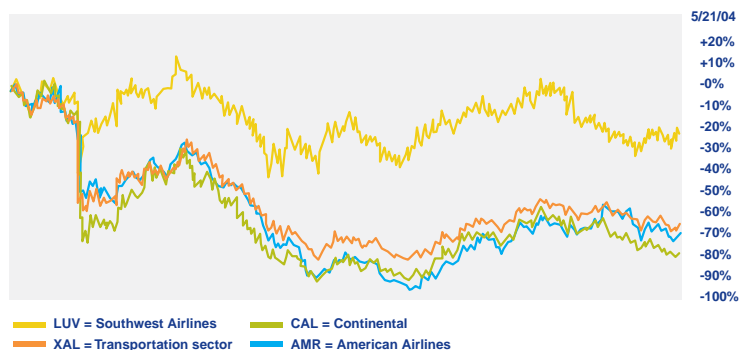
**Figure 4a.**

Dell share price vs. rivals 2002-04



**Figure 4b.**

Southwest Airlines share price vs. rivals 2002-04



We argue that there are four possible reasons for this:

Firstly, gains in operational effectiveness may not be as easy to imitate as the information technology sellers and quality management consultants would have us believe. This is because operational excellence is not just about the tangibles of technology and process re-engineering but is also about the intangibles of people and culture. Much credit is given to Michael Dell's management principles for the sustained success at Dell. These are 'be direct, no excuses, leave the ego at the door, no easy targets, no victory laps, worry about saving money not saving face'<sup>8</sup>. Furthermore, those firms who strive for operational excellence in our research suggest that people and culture are critical to the sustainability of this strategic approach, even though few perform well here.

Secondly, continual improvements in technology and management approaches constantly push the limits of operational effectiveness gains. Leaders in operational excellence develop and adopt these improvements to sustain their competitive advantage: one example is Tesco. Supermarkets in the UK have been fighting for a bigger share of the public's grocery spend for decades and one firm has consistently outperformed the others. Tesco's approach to supply chain management through effective supplier integration, information sharing and superb cash management, together with their common sense management approach, has provided them with a solid operationally excellent foundation on which to build for the future.

Thirdly, there appears to be a link between an organisation's ability to sustain its operationally excellent strategy and its position on the volume/variety matrix shown in **Figure 5**.

Organisations that sustain operational excellence are most likely to reside in the high volume, high variety segment of the matrix. Here the complexity arising from high variety makes it more difficult for competitors to replicate their success. Although operational excellence is also an appropriate strategy to follow in the high volume, low variety segment, this will be harder to sustain in the long term as it is somewhat easier to duplicate.

Finally, many service organisations fail to focus relentlessly on a single value discipline. Our research highlighted many companies where executives talk about giving customers what they want and exceeding their expectations (service excellence) while reducing costs (operational excellence). It takes an exceptional company to achieve both. Singapore Airlines is one example. They offer exceptional personalised services but are also highly cost effective<sup>11</sup>. In most cases these contrasting messages cause confusion, departments don't pull together and the strategy is not executed well. Mediocre performance results.

### The choice is yours

We think operational excellence makes sense for service organisations struggling to respond to the spiralling demands of consumers and business customers alike. Shareholder pressures for cost effectiveness and profitability lend additional support to this approach. There is strong evidence that companies that achieve

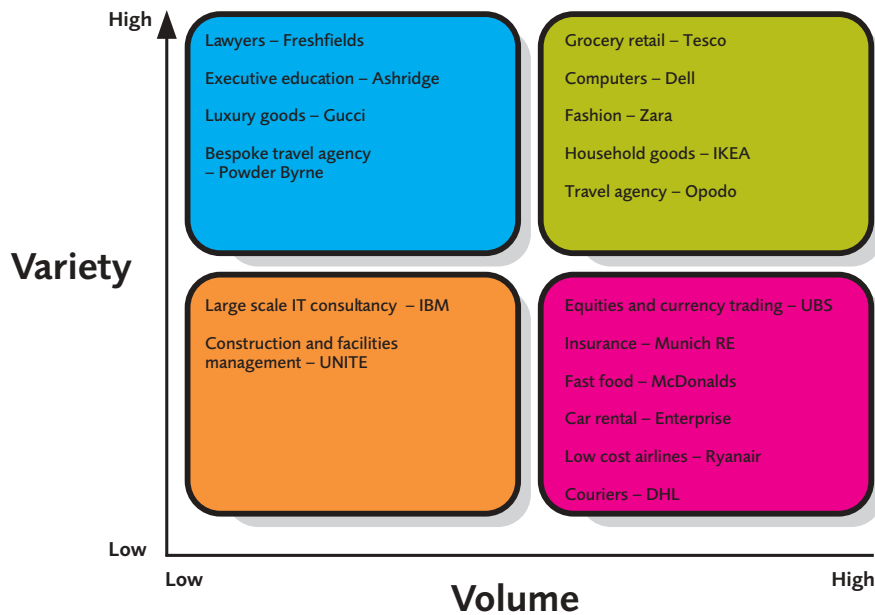
operational excellence are building market share, growing revenues and delivering impressive profits.

Our research has indicated that many service businesses from all sectors are considering operational excellence. For others it may offer an overlooked opportunity to jump off the service excellence bandwagon.

However, operational excellence is not at all easy to achieve. It requires relentless focus and full commitment across the company to the best practice areas we have highlighted in this article. Many companies fall into the trap of trying to deliver both operational and service excellence. It is important that you focus on one or the other. Service excellence or operational excellence: it's your choice!

**Figure 5.**

The positioning of various service sectors and companies on the traditional operations management Volume/Variety matrix



'Lean thinking' is an organisational philosophy which focuses on the elimination of waste in all aspects of one's operations. It was popularised in Womack, Jones and Roos' classic text – *The Machine that Changed the World*. Toyota epitomise lean thinking in the way their operations are run.

\*\*Six Sigma – based on the principle of statistical process control – that if one can maintain a process within six standard deviations of the norm, then one's failure rates will move towards zero (ie zero defects. Six sigma actually signifies a failure rate of 3.4 per million). Originated in Motorola and popularised by GE in the USA.

\*\*\* Reflecting on the provocative nature of our challenge, we believe Porter's concept of operational effectiveness is a useful starting point. He builds on this by citing the specific activities of Southwest Airlines and IKEA – providing support to Treacy and Wiersema's value discipline approach. Our research takes this one step further, providing detail on 35 specific characteristics, which, if actively pursued, will provide sustainable competitive advantage.

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## Look further

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