Chapter 2: Service value chain

The Purpose of this chapter is twofold. First an introduction to services will be presented. This is done in order to provide valuable background information regarding how we deal with services throughout the thesis. Second, Service Profit Chain is use in this thesis as a structural tool when analyzing the relationship between internal operations (employee) and external operation (customer satisfaction) in services, the model will be introduced and discussed. Having identified the critical issues of the Service Profit Chain a modified version will be proposed thereafter.
2.1 **Introducing Services**

First introduction of services. Second, service characteristics will be outlined, and distinctions between various goods and services will be introduced. Finally, a service-good continuum will be presented which assigns different industries on a continuum between pure goods and pure services. This continuum will be utilized in Part III of this thesis. Companies that primarily earn revenue through providing quality services. Service industry companies are involved in banking & financial products, retail, transport, food service, distribution, as well as other service-dominated businesses. Also called tertiary sector of industry.

2.1.1 **Characteristics of services**

The characteristics which show services elements are:

- Perish ability
- Ownership
- Inseparability
- Heterogeneity
- Intangibility

Goods-Services Continuum.

![Goods-Services Continuum](image)

*Figure 1: Goods-Services Continuum*
The continuum of five characteristics, e.g., a fast food counter service is high on intangibility, highly standardized, and generally performed near to customer. On other hand, financial services are less tangible, highly variety, to understand the characteristics of service and their applications in tour operator. Better understanding of these elements would enable to design, operate and sell these services effectively.

2.1.1.1 **Intangibility**

a) Service cannot be touched  
b) Standardization is not possible  
c) No ownership transfers  
d) Service cannot be patented  
e) Service cannot be store  

When in tour operator customer buy tour package that time customer can develop an imaginary picture about what going to see at destination. In case of tour operator there is no such fixed method to calculate that what would be the level of satisfaction that a tourist will get in return.

2.1.1.2 **Inseparability**

A service is provided by a service firm who possesses a skill (chef or an escort) by using technology to handle a tangible product (dry cleaning) to use of hotel, train.

2.1.1.3 **Heterogeneity**

In service firm employees play an important role. The employee plays an important element which is involved in providing services to a benchmark level. A chef (restaurant) who cooks authentic cuisines in great manner with full attention, but every time same chef might behave differently.
2.1.1.4 **Perish ability**

Services cannot be stored they are perishable. An unoccupied air seat or a vacant hotel room is irreparable loss because all these are perishable services. This fluctuating demand pattern (up and down) evaluate the Perish ability characteristics of services.

2.1.1.5 **Ownership**

In case of a service customer only pay for service which it want to use but never own it. Customers booked an air ticket from Bombay to Dubai; customer paid only for the use of service till destination but can’t own it. Thus, services have to be treated as on time quality service.
2.1.2 The Service-Good Continuum

Having identified the main characteristics of service, a further distinction between services and physical goods will be conducted. This is done by presenting different definitions of services which stress the difference between services and goods, and finally by demonstrating the service-good continuum.

Service-Goods Continuum

When moving from the "quality good" towards "quality service" the purchase of tangible good, decreases, and intangible (service) increases. Personnel’s training is shown at the important point of the business services that “ideal” of a service convert into on time quality service.
2.2 Service Profit Chain

Having introduced services, it is now of interest to relate services to customer satisfaction. To illustrate the relation between internal operations (employee) and (external) customer satisfaction in services is proposed in the Service Profit Chain.

This model function the overall framework to evaluate the relation between quality service delivery and customer satisfaction in services, so appropriate to introduce the Service Profit Chain.

The convergence of work being carried out on customer satisfaction, associated with the cycle of failure in front-line human resources management led to the creation of a broader framework with day-to-day management relevance. A close relationship between the defection of customers and dissatisfaction of employees in service companies.

The Service Profit Chain concern between employee satisfaction and productivity which give customer satisfaction. It is not solely the various elements of the chain that are of interest, it is also the links in the chain that focus should be placed on.
Service Profit Chain is influenced primarily by the previous components in the chain. Customer Loyalty is directly resulting of customer satisfaction. A strong influence on employee satisfaction results primarily on quality services and policy that enable employees to deliver service to customers.

But specific components of chain are importance attention should be paid to the links between the services. It emphasize that the Service Profit Chain is circular. Direct influences to each link from the previous one but, indirectly all links are interrelated and therefore interdependent.

Even so, the main focus is on relation between internal operations, customer satisfaction, and loyalty. The importance of customer loyalty is that companies should be aware of the disadvantages concerning defection of customers on the preferable aspects of loyal customers.

The importance of customer loyalty has affected leading service firms currently to quantify customer satisfaction. However, today's customers are strongly value orientated, and research programs have shown that it is extremely important to distinguish between very satisfied and satisfied customers as they have different repurchasing behavior.

2.3 Service value chain

One of the greatest advantages of Service Profit Chain is the fact it covers horizontal spectra entirely. It puts attention both on elements backwards and forwards, e.g. it encompasses both elements concerned with employees, employee satisfaction, and productivity which lead to profit (customer satisfaction)

According to the model, the latter has a positive influence on the value of services provided to external customers. At the same time; this interrelation can be criticized for being too exclusive and too narrow. In order to fit the model to the specific problem formulation of this thesis we have chosen to substitute the first link of the chain. The value of services provided to customers depends on internal operations. One important but not sole issue thereby is employee
satisfaction. Internal operations take place among employees both in front-line and back-office positions and are characterized by employee interactions.

A decision one employee makes has in general an impact on other employees, and vice versa; which makes inter-organizational behavior complex. Looking for example at consumers, price is not the only buying parameter; such as staff performance does not depend solely on one parameter as suggested in this model (SPC).

A modification of the model seems therefore necessary. The purpose of the modification is simply to adjust the Service Profit Chain in a way which serves our analysis best, thus it can be used as our overall structural model.

Service value chain

In order to take the complex structure of organizations into account, it is suggested to label the first link of the Service value chain as internal service. Internal service is concerned with organizational behavior with focus on employees.
It includes, for example decision making processes, intra-organizational communication, and employee motivation. The purpose of terming it internal services is to create a starting point for a Service value chain which in not too narrow. This will be of help when analyzing the interrelation of internal operations and provided external value.

In comparison with the original chain, the final link has been modified as well. The direct influence of customer loyalty to growth of revenue and profitability is still considered; but, it is less emphasized.

It is argued that profit is caused by loyal customers. This is true, but, revenue growth and profitability have many different determinants such as for example, prices of services, costs, and repurchase frequency.

As researcher can see the most critical issues of SPC are relations between internal operations and customer satisfaction, which return to customer loyalty which is considered to be one of the possible outcomes of customer loyalty. In order not to neglect the final link, profit is included in the Service value chain.

It ranks, however, below customer loyalty. Therewith, profitability remains an element of the chain which influences other links, as for example internal service; but, it becomes subsequent to customer loyalty. As such, customer loyalty gains importance in the Service value chain.

The main elements of the original Service Profit Chain continue. However, also the circular character of the chain remains. This means that the interrelation between the different links is still emphasized. In order to know the link between internal operations and customer satisfaction & loyalty, the various links of the Service value chain will be further discussed in the following Part II.