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# The Challenges of Successful Servitization

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# We know manufacturers are servitizing...



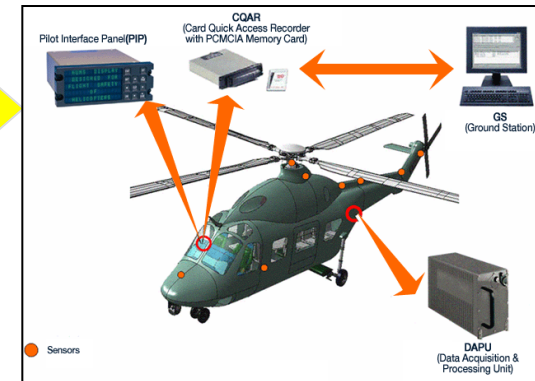
## John Deere iGuide system (2007)

Uses GPS technology to automatically shift the steering pattern of the tractor to compensate for implement drift

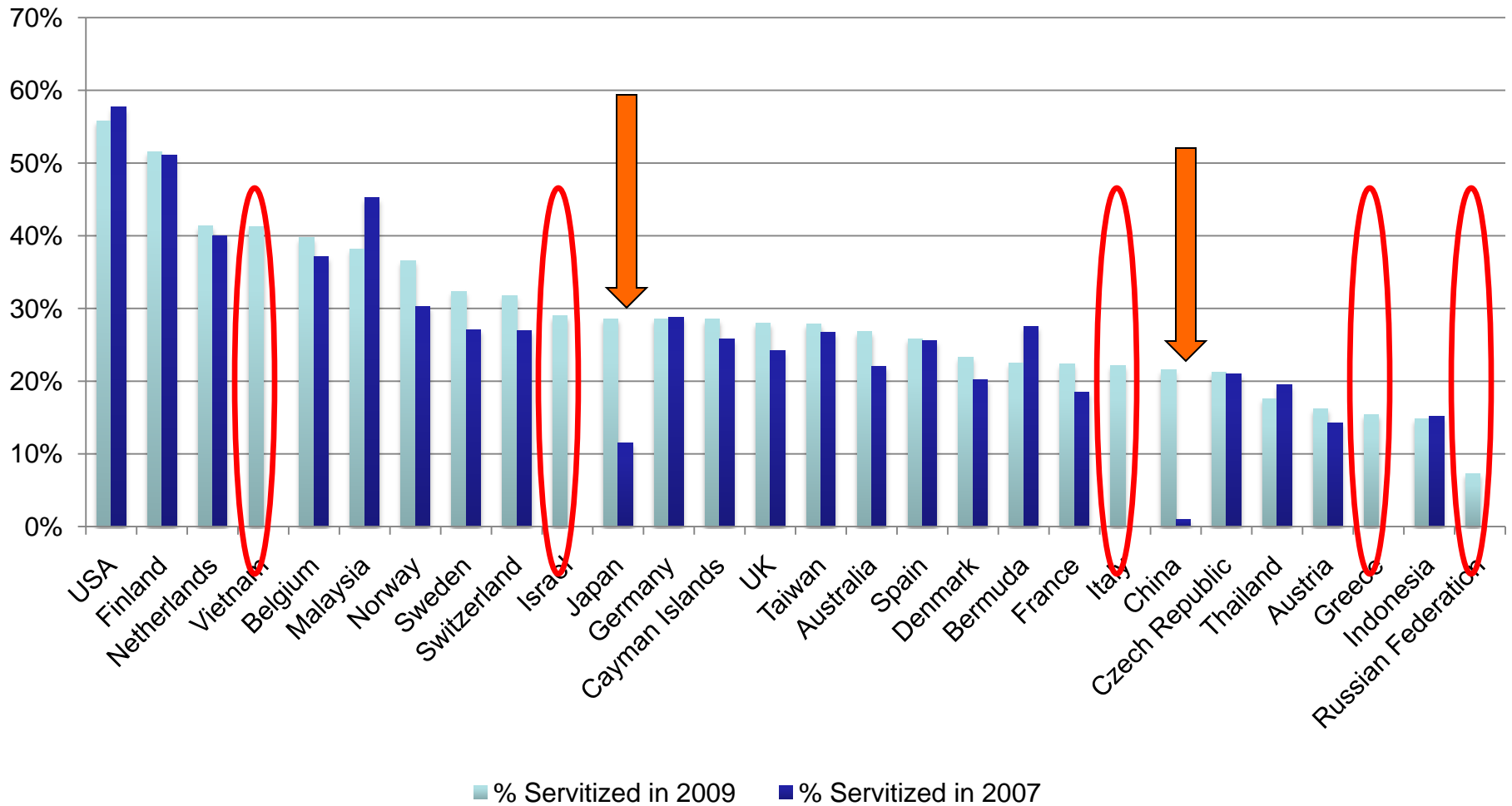


## Health and Usage Monitoring Systems

Use sensors on equipment to detect repair and overhaul requirements



# And that servitization is a global phenomenon...



# Firms are servitizing for different reasons...

<b>Economic rationale</b>	<ol style="list-style-type: none"><li>1. Manufacturing firms in developed economies cannot compete on the basis of cost (technological developments are enabling them to add innovative services)...</li><li>2. The installed base argument (e.g. for every new car sold there are already 13 in operation, 15 to 1 for civil aircraft and 22 to 1 for trains)...</li><li>3. Stability of revenues – services vs. products...</li></ol>
<b>Strategic rationale</b>	<ol style="list-style-type: none"><li>1. Lock in customers (sell the original equipment at cost, make money on spares &amp; suppliers - razor, printers)...</li><li>2. Lock out competitors...</li><li>3. Increase the level of differentiation (e.g. equipment provider offers to take customer's risk and give predictable maintenance costs)...</li><li>4. Customers demand it (e.g. contracting for capability)...</li></ol>
<b>Environmental rationale</b>	<ol style="list-style-type: none"><li>1. Environmental rationale (change notions of ownership and resource use – e.g. Mobility cars)...</li></ol>

# And offering a range of services...

Service Offered?	% of Firms Offering Service in 2009	% of Firms Offering Service in 2007
Design and Development Services	23.21%	21.92%
Systems and Solutions	15.92%	15.70%
Maintenance and Support Services	12.33%	11.94%
Retail and Distribution Services	12.14%	12.18%
Installation and Implementation Services	5.35%	5.10%
Property and Real Estate	4.89%	3.83%
Financial Services	3.80%	3.89%
Consulting Services	3.37%	2.69%
Leasing Services	2.06%	1.07%
Outsourcing and Operating Services	1.46%	1.68%
Procurement Services	1.18%	1.15%
Transportation and Trucking Services	0.19%	0.20%

# What we know about servitization so far...

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1. Widespread efforts to servitize...

58% of US firms with manufacturing SIC codes offer services.

2. Although the extent of servitization differs markedly by country...

Less than 2% of Chinese manufacturing firms had servitized by 2007 (Neely, 2009).

3. While services are thought to deliver higher margins, there is mixed evidence on the impact of servitization...

(Gebauer et al, 2005; Neely, 2009; Visnjic and Van Looy, 2009).

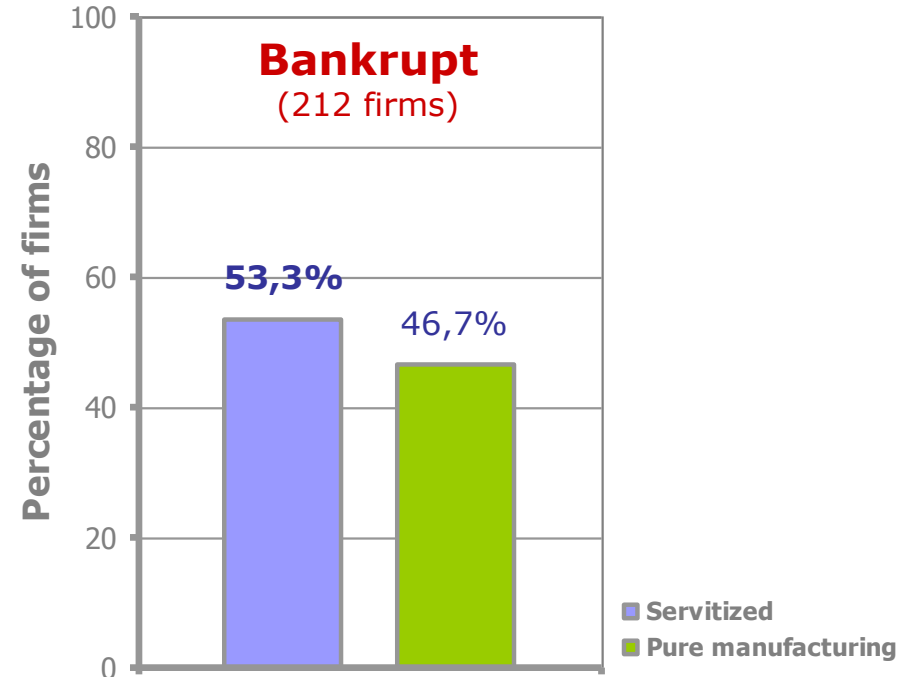
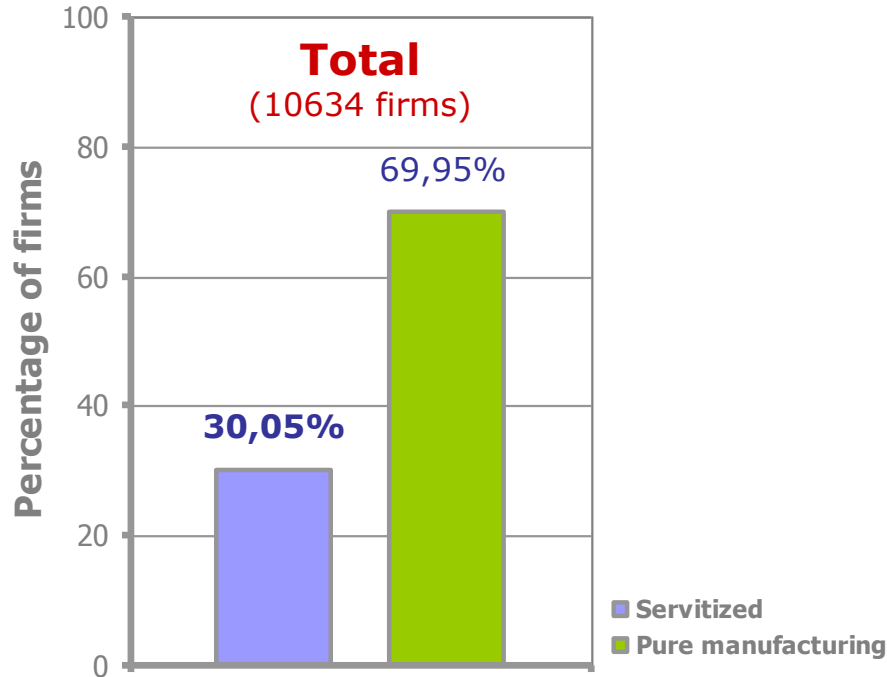
4. With increasing evidence that the relationship is non-linear...

(Fang et al, 2008; Suarez et al, 2008).

5. And that servitizing can be high risk...

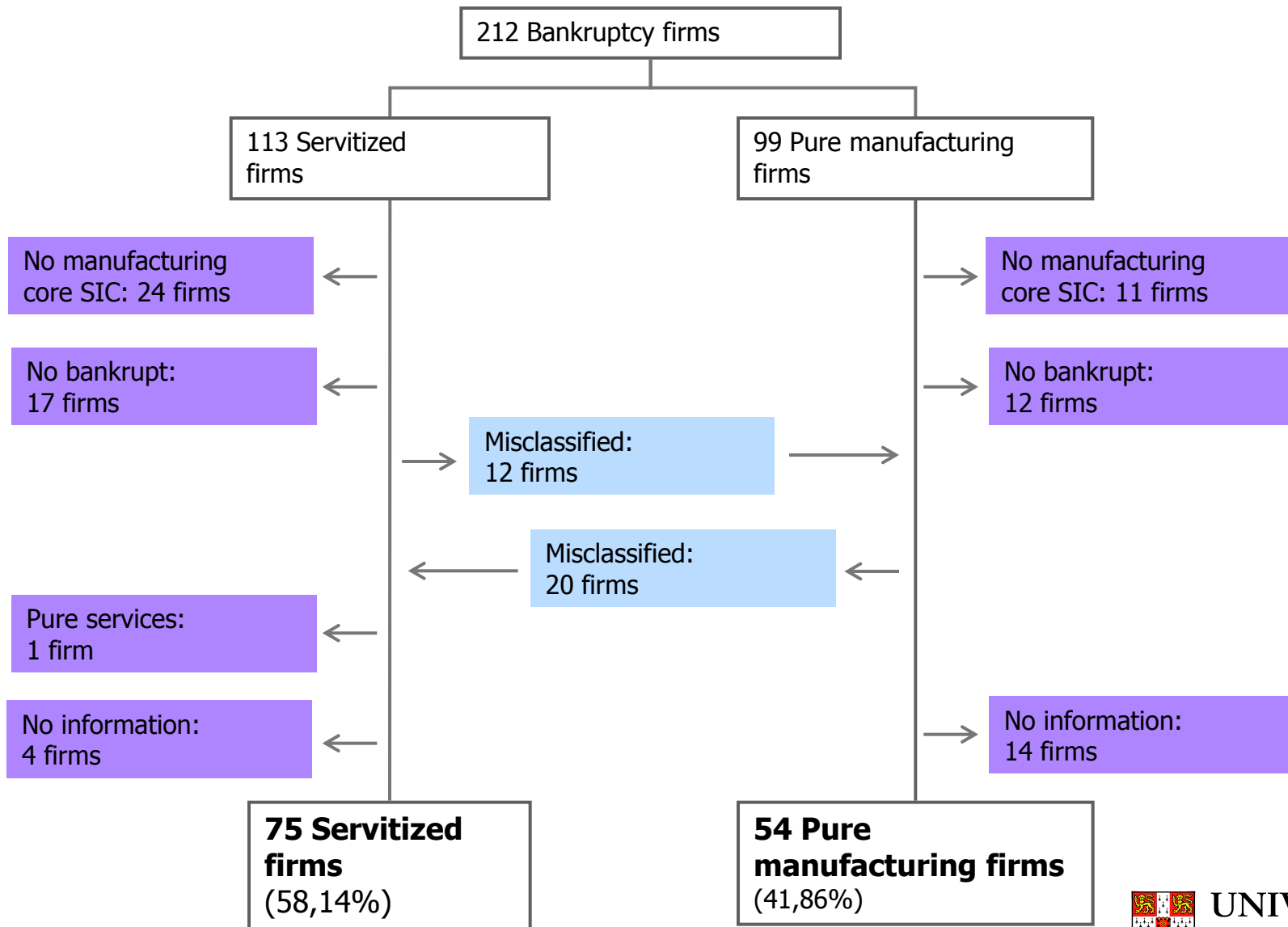
Firms that servitize appear more likely to suffer bankruptcy (Neely, 2009).

# But the transition to services is not straightforward!

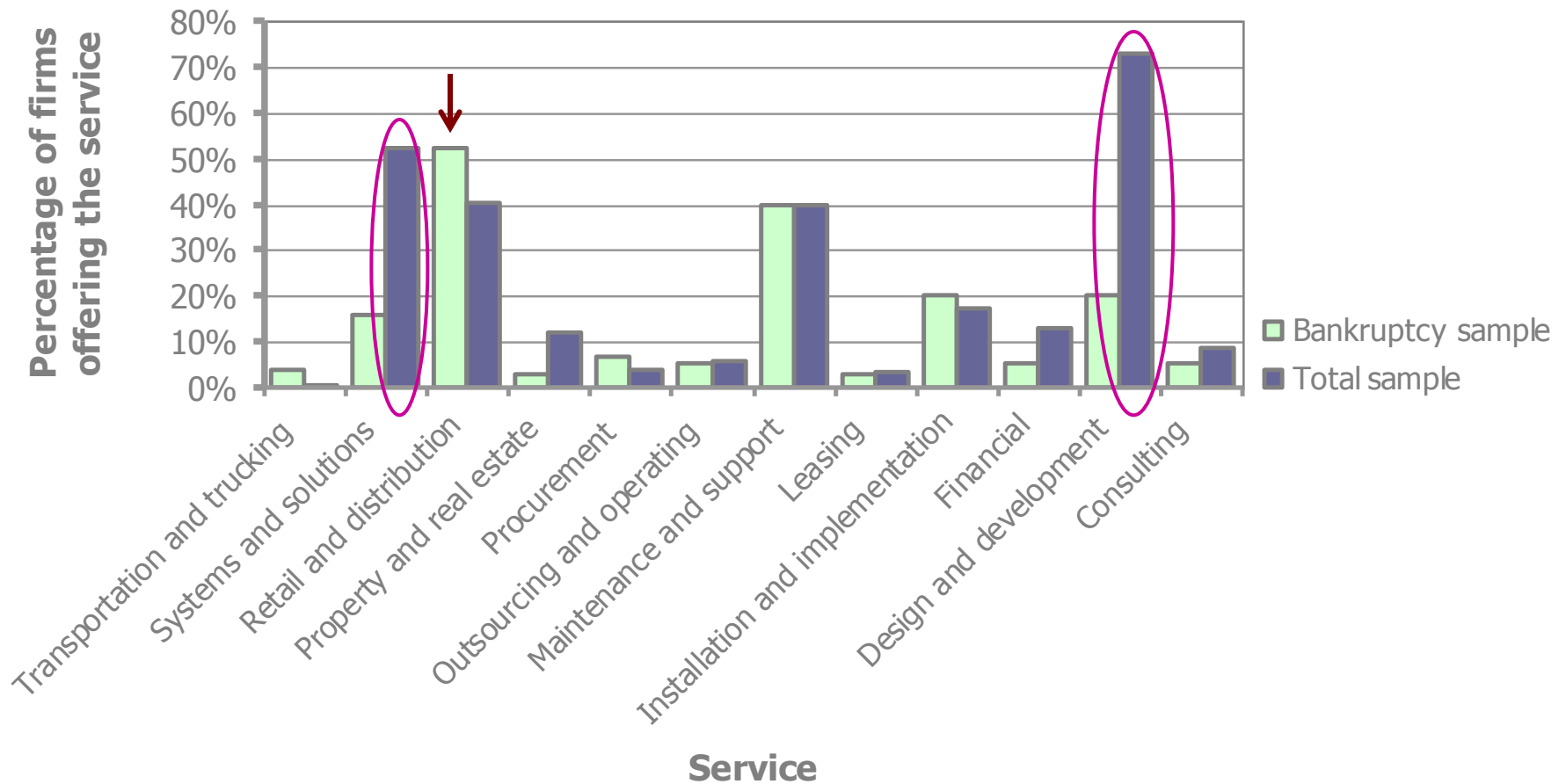


While the shift to services is clear the transition to services is not straightforward – the latest research suggests that servitized manufacturers achieve lower profit margins and are more likely to go bankrupt than pure manufacturers (in the short-term).

# Data used in this study...



# Are some services higher risk?



A greater proportion of firms declaring bankruptcy offered retail and distribution services than might be expected while a smaller proportion offered systems and solutions and design and development services

# How do the risks vary by sector?

Core SIC code	Description	Main service offering	Implications	Risks
22 33	Textile mill products Primary metal industries	Distribution	Expansion because of the acquisition of distribution facilities and assets  Service revenues exclusively related to the sale of new product units	Excessive operating losses and restructuring charges when production decreases and firms need to downsize
35 37	Industrial and commercial machinery and equipment Transportation equipment	Maintenance services and spare parts provision	Capital and organisational investments to set-up the service business  Service revenues proportional to the dimension of the installed base of products	Installed base of products to service not sufficiently large to ensure good revenues and repay the service investment
36	Electronic and other electrical equipment and components, except computer equipment	Design, engineering, technical support services, system integration	Complex and technologically advanced products	Inability to recoup high R&D expenses

# The challenges of servitizing...

## Shifting mindsets

- Of marketing – from transactional to relational
- Of sales – from selling multi-million dollar products to selling service contracts and capability
- Of customers – from wanting to own the product to being happy with the service

## Timescale

- Managing and delivering multi-year partnerships
- Managing and controlling long term risk and exposure
- Modelling and understanding the cost and profitability implication of long-term partnerships

## Business model and customer offer

- Understanding what value means to customers and consumers (not producers and suppliers)
- Developing the capability to design and deliver services rather than products
- Developing a service culture
- Embedding all of the above into a service organisation

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