Thoughts on Evaluation of SME Strategic Relationships

Andrew Boyd & John A. Boyd

Abstract

Inherent in the development of Strategic Relationships must be a methodology of evaluation. To date, the implicit assumption is that strategic relationships between SME's and larger firms are mutually beneficial – unfortunately, this is not always the case. This paper focuses on a dichotomy and classification of possible relationships and evaluation methodologies from a conceptual perspective.

The dichotomy is somewhat simplistic as all relationships are initially classified as Mercantile or Symbiotic. Mercantile relationships are those with a clear vendor/buyer relationship. Classic accounting principles can be used to evaluate these relationships and from the vendor perspective, the transaction must be profitable or the relationship terminated. From a buyer perspective the relationship must be satisfying. Evaluation of satisfaction can be accomplished by use of a new heuristic on the five fundamental principles of customer satisfaction.

Symbiotic relationships are far more difficult to classify and evaluate. With symbiotic relationships, benefits are not always equal or even mutual. However, relationships will not last if they are based on a win-lose situation or lose-lose situation for the parties. Symbiotic relationships include joint development, working with market leaders, management of influencers, loose affiliations, vendor certifications and other network relationships.

Since there is no clear-cut buyer or seller, it is difficult to evaluate symbiotic relationships from the profitability perspective or by using the customer satisfaction heuristic. Often, alliances are formed without thought to a customer-focused end goal (like better service or better quality). More often, they are formed around general business goals such as greater profits or "image" without regard to clearly defined products or customers. Essentially, the strategic relationship

should exist for the long-term benefit of customers while generating profits for the businesses involved.

In the past, Symbiotic relationships developed on a personal basis or through industry affiliations. More recently, relationships have been developed for the purpose of knowledge sharing, access to customers and access to capital. Several evaluation techniques that appear promising in evaluating future benefits and gains are the reiterative "Balanced Scorecard" paradigm, as well as objective-based models such as OEI, GQIM and OGSM.

Background

Conferences, books and papers have been devoted to the concept of developing strategic relationships and networking. The presumption is that SME's can benefit from affiliations with larger firms, but this may not always be the case.

For instance, AT&T recently notified customers that worldnet.att.net service was being canceled including email service unless they agreed to new and onerous terms. Many had chosen WorldNet as their ISP and email account because they thought the AT&T name would carry more prestige than Yahoo or Hotmail. Now AT&T has withdrawn the WorldNet service and former users must pay to continue using their email addresses and source a new ISP to access their email account.

For years, small business folklore in the plastics industry had warned against affiliating with a certain large retail business that had the reputation of nurturing small firms to be sole suppliers, then threatening them with loss of business unless they sold out to the company at a low price. However, this phenomenon is not only a prevalent in small businesses; problems in developing and maintaining long-term relationships are common in the largest of companies. Recently, Ford and Firestone dissolved their 75-year relationship in a very acrimonious divorce with allegations by Ford of defective tires and counter-allegations of defective automobile design by Firestone.

The doctor's relationship with the HMO provides an excellent example of an instance when a symbiotic relationship may not be mutually beneficial (Boyd & Baldasare, 1997). HMO guidelines mandate certain treatments and indications that doctors must follow when administering care. However, it is likely that a doctor may not be able to provide the highest possible quality care due to these restrictions. These regulations leave the doctor's hands tied and can have a significant impact on the patient's perception of their care and resulting overall satisfaction.

Because of the potential destructive nature of business relationships, SME's must have the tools to evaluate their relationships with other businesses – particularly their most important ones. This paper discusses two very different types of business relationships, Mercantile and Symbiotic, and presents methods to evaluate these relationships.

Introduction

In evaluating business relationships, it is useful to classify those relationships as Mercantile or Symbiotic. Mercantile relationships are the traditional vendor-customer situations. Deming has stressed the need for businesses to develop close and enduring relationships with vendors in developing his TQM process. Strong relationships are also crucial in JIT management techniques. When close mercantile relationships exist, those vendors who have adopted Activity Based Costing (ABC) and Activity Based Management (ABM) have the ability to evaluate each customer and even individual transactions for profitability.

The evaluation of customer satisfaction has been somewhat more elusive to define and evaluate and the Five Pillars of Customer Satisfaction was developed to fill this void. Customer Satisfaction in Mercantile relationships will be discussed in the next section.

Symbiotic relationships are conceptually more difficult to define or even describe. They include joint development, working with market leaders, joining the coattails of influencers, loose affiliations, vendor certification and other network relationships. We choose to describe these relationships as Symbiotic because benefit from the relationship is not always equal for both parties, and sometimes there is not even mutual benefit.

A colleague, Dr. Roderick Moorehead, suggested marriage as the best example of the variability of benefit from a symbiotic relationship. Not all marriages provide mutual or equal benefit to both parties. Because of the lack of evaluation criteria, some dissolve prematurely because of the capricious whim of one partner while others marriages endure long past the point of mutual benefit. Despite the mixed record of success, most parents tout the positive benefits of marriage and recommend it for their children.

Conferences such as this one are predicated on the assumption that there is universal gain from networking and developing partnerships and those relationships will be win-win if both parties work hard enough. History proves that this assumption is simply not true and a methodology of evaluating non-Mercantile, Symbiotic relationships must be developed. While this paper presents the "balanced scorecard" paradigm and other techniques as potential tools for reiterative evaluation of Symbiotic relationships, more work is needed in this area.

Customer Satisfaction in Merchantile Exchanges

Literature Review of Customer Satisfaction

According to Henkoff (1994), companies pay lip service to customer satisfaction and quality but rarely measure either. Chief Executive Officers (CEO's) still evaluate their companies on the basis of profits and stock performance. Stewart (1995) points out that neglecting customer satisfaction has a direct impact on profitability. The highest-ranking companies out performed those companies that ranked lowest in the American Consumer Satisfaction index in the stock market.

Satisfaction is important because the cost of acquiring new customers is five times the cost to sustain an old one (Stewart, 1995). Moreover, Fierman (1995) reports that dissatisfied customers are likely to tell 20 friends while satisfied ones will only recommend to eight.

A customer's decision to defect is often the result of many small negative encounters with a company (Stewart, 1997). One national survey found that familiarity breeds contempt and the less face-to-face contact an organization has with their customers, the happier the customers are (Smith, 1996). An explanation of this phenomenon may be related to Parieto's rule where 80% of sales volume is generated by 20% of customers. Hence, random failures in quality or customer service are most likely to occur with the best customers.

Losing business based on customer dissatisfaction is not inevitable. Legare (1996) reports that 15% switch because a competitor is cheaper and 15% switch because a competitor offers better value. However, the vast majority switched because of preventable reasons. Twenty percent left because they did not get enough attention and another 50% left because the attention they did receive was poor.

Small businesses are also aware of the need for customer satisfaction. "More than half of those surveyed cited customer satisfaction as the most important measure of business success, nearly twice as many as the 28% who mentioned profitability" (Advancement of Education, 1997. p.10). Unfortunately for businesses large, and small, the measurement of customer satisfaction is a difficult process.

Measurement difficulties involve what to measure, how to measure it and who to measure. In most cases, there is value in measuring both current and former customers to determine why some remained loyal and others left. The "how to" of customer satisfaction surveys is somewhat more difficult as the scale for satisfiers and dissatisfiers may be vastly different (Boyd & Baldasare, 1997). For instance, waiting time in a doctor's office can be a dissatisfier, but not necessarily a satisfier. A long wait will generally leave patients with a lasting negative impression, whereas a short wait will not have a proportional positive impact (or any impact at all) on satisfaction scores. Hence, waiting time is a dissatisfier, but not a satisfier. In this case, the physician would do well to try to minimize waiting time, but not put undo pressure on the office to see patients too quickly (as positive performance will have little impact in overall satisfaction). The impact of both satisfiers and dissatisfiers must be considered when designing evaluation programs.

Choosing what to measure is equally challenging. Stewart (1997) argues very pragmatically that happy customers should exhibit one of three measurable characteristics as dependent variables: loyalty (retention rates), increased business (market share) or price tolerance. Increases in these characteristics could be expected to contribute to increased profitability in the long run. Various studies have focused on the different components that might contribute to increased customer satisfaction. A summary of these factors or potential independent variables is shown in Table 1.

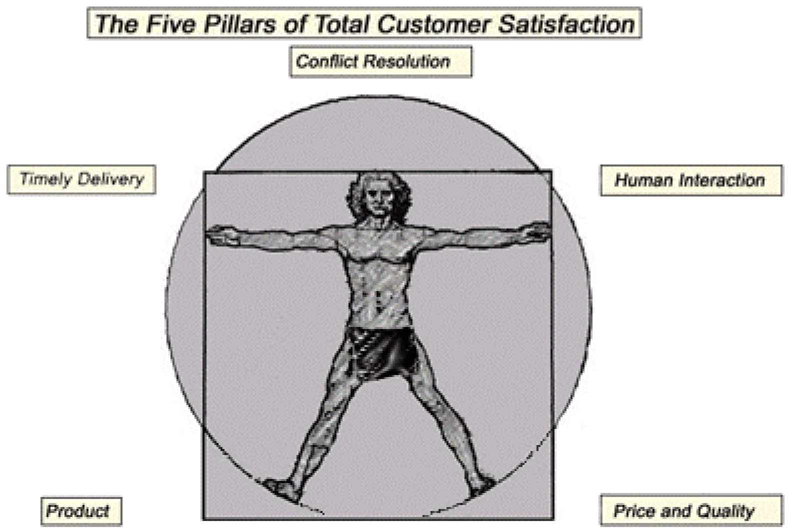
TABLE 1: A COMPARISON OF COMPONENTS THAT MAY CONTRIBUTE TO INCREASED SATISFACTION

Stewart, 1997	**Fredrick & Salter, 1995**	**Legare, 1996**	**Ellis & Curtis, 1995**
1. Price	1. Price	1. Price	1. Responsiveness/ Conflict Resolution
2. Quality	2. Product Quality	2. Better Value	2. Technology
3. Customer Service	3. Service Quality	3. Attentive Staff	3. Quality & Reliability
4. Response to Complaints	4. Innovation	4. Quality of Attention	4. Timeliness
5. Staff Behavior	5. Company Image		

There is one caveat that should be addressed relative to price. As an independent variable the price of an item relative to its intrinsic value to the consumer is one factor contributing to overall satisfaction. However, most “very satisfied” customers are willing to pay a little more for the service and quality they desire. Thus, a tolerance to price increases is also a dependent variable in measuring customer satisfaction.

The investigators represented in Table 1 do not appear to have selected the independent variables based on a unified model for customer satisfaction. J. Boyd & A. Boyd (2001) developed a heuristic for consumer satisfaction that was broad enough to include the variables of the prior investigators clustered within five underlying categories (FIGURE 1). The work was originally presented as The Five Pillars of Customer Satisfaction (J. Boyd & A. Boyd, 2001) and subsequently the Five Maxims of Customer Satisfaction (Boyd, A. 2001, 2002). Briefly, the fundamental independent variables identified by the authors are shown below.

FIGURE 1: THE FIVE PILLARS OF SATISFACTION



The Five Pillars of Customer Satisfaction:

1. ***Deliver the product that the customer wants to fill their need. Include the degree of innovation, technology, design and features the customer is looking for.***

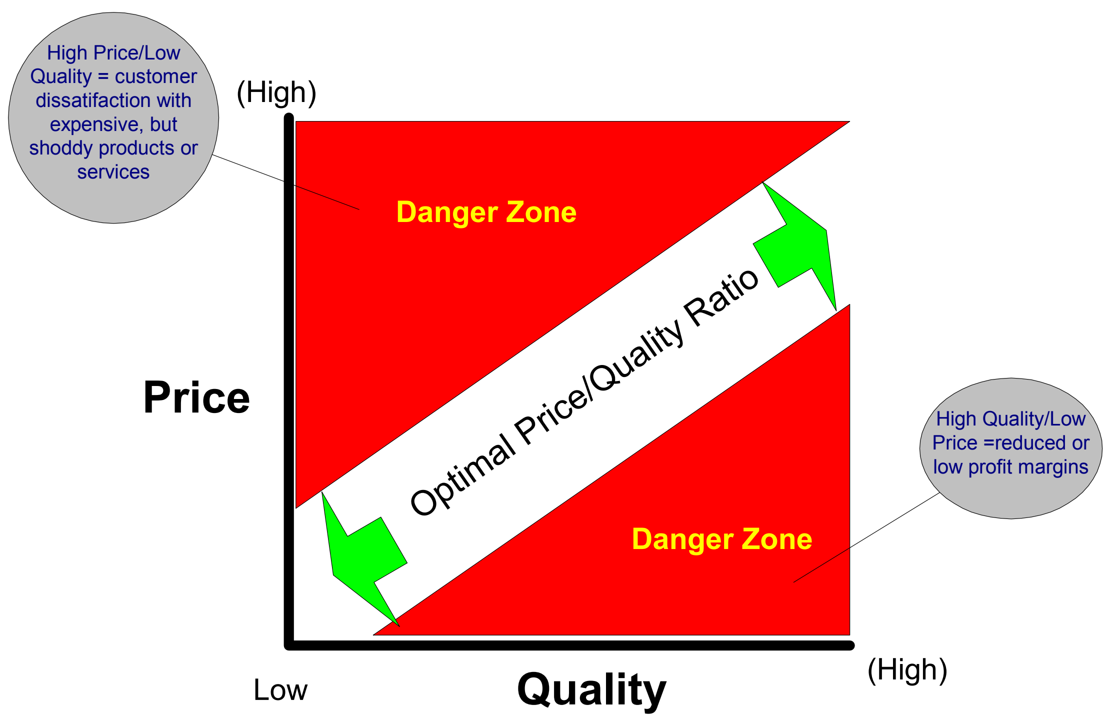
2. ***Deliver a quality level consistent with the price. These two items cannot be logically separated. Most consumers expect a 69-cent burger to be different from a $6.90 burger or a $120,000 car to differ from a $12,000 car. Every product and service has an optimal price/quality ratio (FIGURE 2). If a low-quality product is priced too high, customers will become dissatisfied when the purchase fails to meet their quality expectations. On the other hand, low-priced/high quality products will erode margins and firm's profit expectations will not be met.***

3. ***Deliver the product in the time frame the customer needs, wants or desires. This is complex. Sometimes the expressed desire conflicts with reality.***

4. ***Deliver the degree of human interaction a customer desires. Some people want no banal interaction at all and on some solemn occasions most people will avoid humor.***

5. ***Have in place a system of conflict resolution that is fair to both the business owner and the consumer. Paying false claims increases the cost of doing business and this will be passed on to all the other consumers. Ignoring just claims will result in a loss of business.***

FIGURE 2: THE PRICE/QUALITY TRADEOFF



While the heuristic is broad enough to include the variables selected by prior investigators, it is narrow enough to provide guidance in the development of consumer satisfaction programs. By using the Five Pillars of Customer Satisfaction and Activity Based Costing and Management, companies can evaluate profitability of various customers and the cost of improving customer satisfaction. However, attempts to use this model in evaluating Synergistic relationships are totally futile.

In many cases it is difficult to determine the exact product and sometimes even the expected outcomes of a relationship with another firm. This, of course, makes it impossible to evaluate concepts of price and quality. It is also difficult to measure long-term economic benefits from strategic relationships, yet there is a cost associated with initiating, developing and nurturing any relationship. It is within this context that a new search was initiated on methods for evaluating non-Mercantile or Synergistic relationships.

Evaluation of Symbiotic Relationships

Literature Review of Evaluation Techniques

Organizational evaluation techniques such as Kaplan and Norton's balanced scorecard (BSC) provide an interesting starting point when seeking to evaluate the firm's non-financial successes. Instead of focusing on a historical financial perspective, BSC presents three additional operational considerations for measurement: customer satisfaction, internal processes and organizational learning (Harvard Business Review, February 1992). Kaplan & Norton analogize that the BSC provides managers an "airplane cockpit"-like view of the organization and that it provides answers to four basic questions (1992, p. 126):

- How do our customers see us (customer perspective)?
- What must we excel at (internal perspective)?
- Can we continue to improve and create value (innovation and learning perspective)?
- How do we look to shareholders (financial perspective)?

All of these questions are crucial for SME managers to consider when evaluating symbiotic relationships.

To begin using the BSC method Kaplan and Norton suggest that the organization must determine goals and measures for each area of concern including financial, internal processes and innovation and learning and customer satisfaction. Like The Five Pillars, Kaplan and Norton put forward that customers tend to be concerned with timing, quality, service, performance and cost (Harvard Business Review, 1992, p. 128). The principle difference in evaluating consumers is that Kaplan and Norton do not suggest quality and price as a matched pair, nor do they recognize the need for conflict resolution as part of a customer satisfaction program.

In later work, Kaplan and Norton outline how the BSC can be used as a strategic management system (Harvard Business Review, February 1996). This process involves four steps:

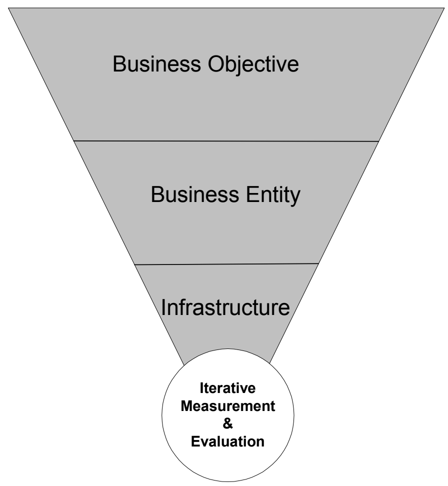
- Translating the vision
- Communicating and linking [strategy to unit and organizational goals]
- Business planning
- Feedback and learning [through testing and gathering feedback]

Clearly, BSC provides an interesting starting point in beginning to provide a framework for the evaluation of symbiotic relationships, particularly with the focus on customer satisfaction measures as criteria for success. However traditionally, BSC is an internal evaluation method, meaning that it only focuses on one of the entities involved with the partnership. To be truly effective in measuring strategic relationships, all participating entities must be evaluated.

When used in conjunction with the objective, entity, infrastructure (OEI) framework (A. Boyd, 2002), traditional BSC is extended outside the boundaries of the SME. The OEI framework (FIGURE 3) presents both practitioners and researchers an evaluation method whereby, like BSC, high-level organizational objectives are linked to specific measures of success. However it goes one-step further by linking the measures with the underlying organizational information architecture.

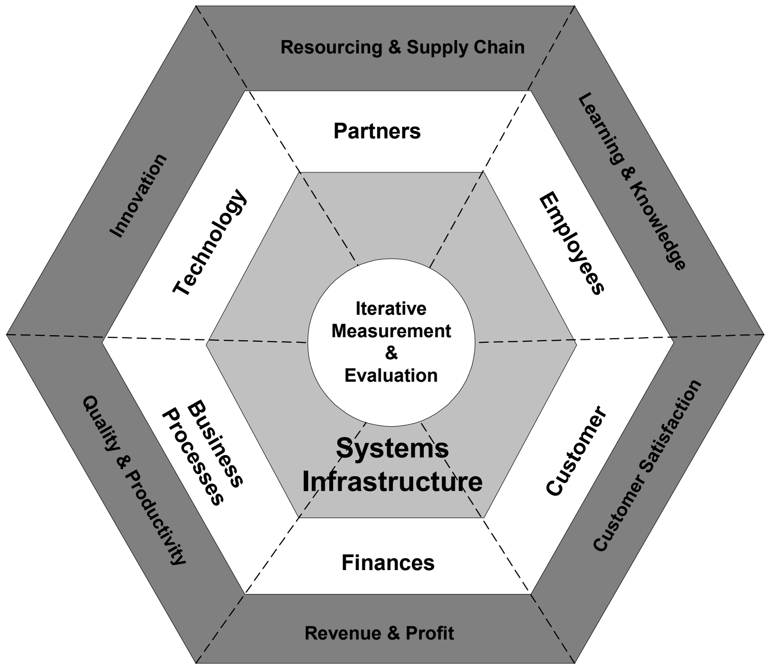
The OEI framework starts with the firm's business objectives. For customer satisfaction, the five pillars provide an excellent starting point for managers when developing their organization's objectives. Next, managers must determine each business entity that will need to be influenced or affected to achieve the business objective. Entities can generally be considered the nouns of OEI. That is, entities are the "person, place or thing" that will be directly impacted when achieving objectives. Lastly, entities are mapped to the information architecture and a gap analysis is conducted to determine what information exists and what will need to be developed to support the evaluation program.

FIGURE 3: THE OBJECTIVE, ENTITY, INFRASTRUCTURE EVALUATION MODEL



Once the OEI exercise is completed for each of the business goals, a new paradigm emerges that encompasses all of the BSC considerations such as Customer, Finances, Business Processes and Innovation and Learning, as well as non-BSC factors such as partners, employees and technology (FIGURE 4). This figure is illustrative in nature, as each firm's OEI framework model will differ depending on the stated objectives and influenced entities of the organization. Using this paradigm, the goals of the symbiotic relationship are put into the context of larger organizational considerations.

FIGURE 4: THE OEI FRAMEWORK FOR THE SME

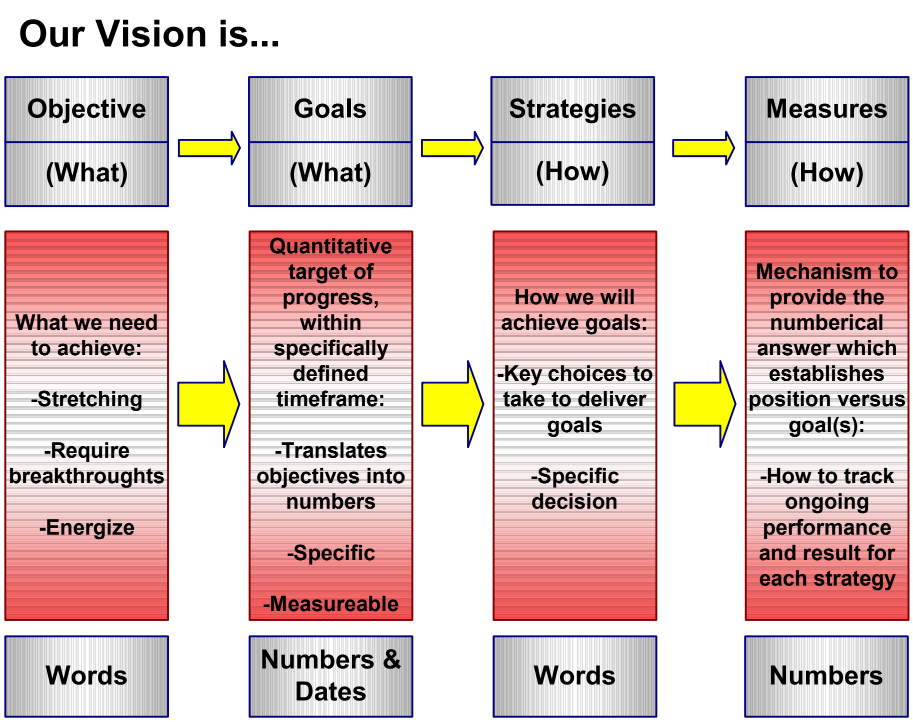


Another powerful evaluation method includes Park, et al's goals, questions, indicators and measures (GQIM) methodology. Developed by researchers at the Software Engineering Institute, GQIM method provides a powerful way for software evaluators to ensure that the software measurement achieves pre-determined business objectives. This method starts by asking, what is it that I want to know?" not by asking, "what measures should I use?" The GQIM process has 10 steps (Park et al, p. 23, 1996):

1. Identify business requirements
2. Identify what you want to know or learn
3. Identify sub-goals
4. Identify entities and attributes related to sub-goals
5. Formalise measurement goals
6. Identify quantifiable questions and the related indicators that will be used to help achieve measurement goals
7. Identify data elements that will collected to construct indicators
8. Define the measures to be used, and make these definitions operational
9. Identify the actions that you will take to implement the measures
10. Prepare a plan for implementing the measures

Lastly, the objective, goal, strategy, measures (OGSM) method (FIGURE 5) also provides an interesting starting point for researchers and academics when evaluating symbiotic relationships. Although research indicates that this method was developed by Proctor & Gamble (Kingham and Tucker) and is commonly used by many consultancies, the verifiable origins of OGSM are unclear. OGSM starts with business objectives that are linked to the overall organizational vision, and then links goals to those objectives. Objectives are what the firm wants to accomplish, whereas goals are achievable targets that address those objectives. Strategies outline how the firm will accomplish goals, and measures determine the effectiveness of strategies. Once the exercise is completed, the firm (or department) has an articulated its high-level objectives and has produced a documented and measurable strategic plan.

FIGURE 5: THE OGSM MODEL



Sources: Tucker and Kingham

A common theme in all the evaluation techniques is the starting with business objectives and building an evaluation program around that core. Undoubtedly, without a clear and demonstrable objective, any business relationship is likely to fail to meet expectations. Each of the discussed methods has advantages and disadvantages (TABLE 2) in how it guides the organization in translating high-level objectives into operational reality. However, none of the methods are perfect for the evaluation of symbiotic relationships. Clearly, much work needs to be done to fully understand and appreciate the contributions of each method.

TABLE 2: COMPARISON OF EVALUATION METHODS

	Strengths	**Weaknesses**
Balanced Scorecard	Well documented, deployed in major corporations and supported by consultancies.	Still heavily focused on financial measures. Limited in scope (predetermines evaluation areas).
GQIM	Well-documented approach for both quantitative and qualitative approached.	Documentation written in the context of software measurement and evaluation. Limited use in wider context.
OGSM	Very flexible and easily grasped at all levels of the organisation.	Minimal documentation, no rigorous method.
OEI	Ties high-level business objectives to the organisation's information architecture. Flexible in handling customised business objectives/situations.	Methodology untested in evaluating business relationships. Largely, to date, processes are undocumented.

CONCLUSION

For SME's, the evaluation of purely Mercantile relationships is fairly straightforward. The models for evaluating customer satisfaction and profitably readily exist and are adaptable to all

Mercantile exchanges. From the vendor perspective the account is either profitable or not; and from the customer's perspective, reasonable expectations are satisfied or not.

Although methods and measurement systems that could potentially be suitable to measure the effectiveness of symbiotic relationships abound, a clear advantage of one over another is not immediately evident. As seen in this paper, methods such as the balanced scorecard, OGSM, OEI and GQIM provide an interesting starting point, significant work needs to be done before the best one for SME's can be determined. The authors contend that the optimal solution will likely result from a cross-disciplinary and combination approach such as the BSC and the OEI frameworks cited in this paper.

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About the Authors:

Author: Andrew Boyd
Company or Institution: City University -Department of Information Science
Country: United Kingdom
Email: andrew@strategyst.net

Author: John A. Boyd
Company or Institution: Boyds VI Consulting
Country: St. Croix
Email: boydsvi@viaccess.net