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Chapter 9: Customer Service in Logistics Planning

Objectives

- Understand why customer service is important in logistics & logistics planning.
- Examine the elements of customer service.
- Appreciate the strategic advantage of customer service.
- Examine the cost of service and profitability matrix.

1. Introduction – Importance of Customer Service in Logistics

In a mechanized warehouse, approximately 65 percent of personnel are employed in some facet of order picking. The two basic methods of order picking are individual and area selection, also known as batch selection.

Using individual selection, one employee completes a customer's total order. This system is not widely used. Its primary application occurs when a large number of small orders are selected for repack or consolidated shipment, such as e-commerce fulfillment.

Under the more commonly used area selection system each employee is assigned responsibility for a specific portion of the warehouse. To complete a customer's order, several different selectors are required. Because each employee has a thorough knowledge of a specific selection area, less time is required to locate items.

Systems described above are constantly improved to shorten delivery time in effort to support customers' needs. Good customer service is the lifeblood of any business.

Customer service is an organization's ability to supply their customers' wants and needs.

Excellent customer service is the ability of an organization to constantly and consistently exceed the customer's expectations

Improving customer service involves making a commitment to learning what our customers' needs and wants are, and developing action plans that implement customer friendly processes.

2. Elements of Customer Service

Customer service is not confined to just the face-to-face communication with customer.

It encompass a broader aspects and include the infrastructure elements such as buildings, IT systems, warehouse, transports as well as the soft elements such as employee, culture, software tools, policies, procedures, and etc, all blended into one

that operates in unity to satisfy customer and are considered as having value to the customer.

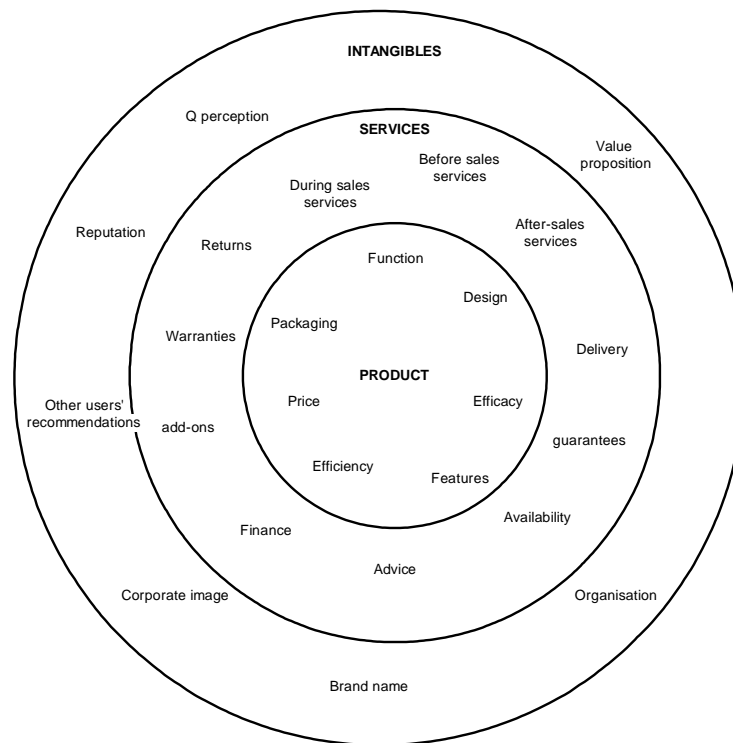


Figure 9-1: Product Construct
(after McDonald, 2002)

As illustrated in Figure 9-1, customers are not just buying a product. They buy the peripheral services such as delivery time, delivery reliability, order fulfillment and so forth. In essence, they acquire the physical product and the customer service element.

Customer perception of value is often 'experienced' rather than in the detail analysis of the tangibles.

Having all the right elements of the system to dish out logistic and customer services is just one aspect of piecing together the complexity to better fulfill customer needs.

However things do go wrong and when that happens, the real differentiator of who has the better customer service in Logistic will depend on the service recovery experience.

When customers have certain expectations and they are disappointed, then they can form very negative impressions.

Service recovery is not just about fixing the problem that has happened. It involves doing more and surprising the customer, leaving him/her with a positive impression rather than a negative one.

3. Competitive Advantage

Competitive advantage is a position that a firm occupies in its competitive landscape. A competitive advantage, sustainable or not, exists when a company makes profits, that is, their earnings exceed their costs (including cost of capital).

That means that normal competitive pressures are not able to drive down the firm's earnings to the point where they cover all costs and just provide minimum sufficient additional return to keep capital invested.

As shown in Figure 9-3, customers are seeking benefits when they buy a product and/or service. They will compare prices with the seller's competitors, termed cost differentials. They will also seek the value they can derive from the company they have chosen. If the perceived value is greater than the price differential, then customers may choose the one that they perceived will have the greatest benefit.

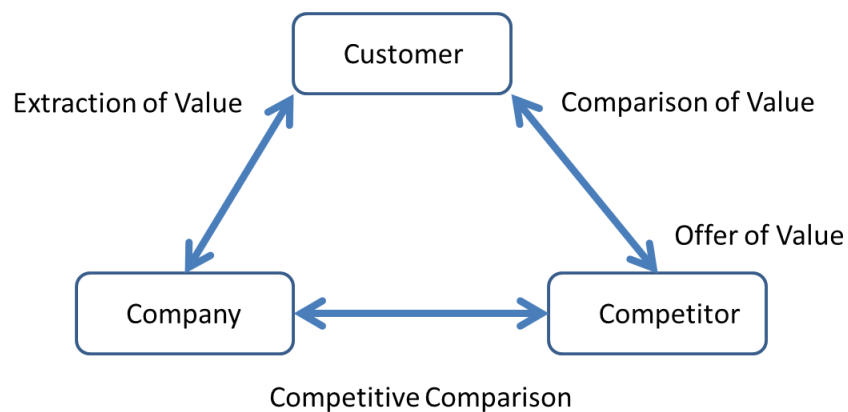


Figure 9-2: Customer Competitive Profile

4. Competitive Advantage in Logistics

A company can choose to operate in one of the 4 quadrants of the Value Advantage and Cost Advantage matrix as shown in Figure 9-4.

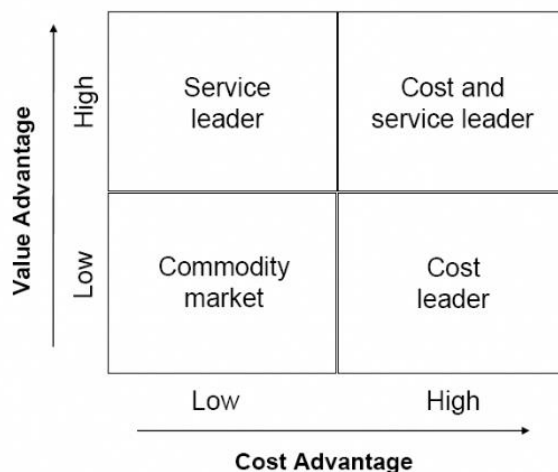


Figure 9-3: Value versus Cost Advantage Matrix (after Christopher, 2011)

The quadrants are explained in the Table 9-1 below.

Quadrant	Characteristic
Commodity Market	Both Value advantage and Cost advantage are minimal and profit margins are thin. Customers do not perceive value and will not pay.
Service Leader	Companies that operate in this quadrant are able to deliver on products and services that are highly valued by the customer even though the cost advantage is minimal.
Cost Leader	Companies that operate in this quadrant are able to provide the lowest cost relatively to the competition. Customer that uses the products and services of these companies look for cost as the only key value.
Cost & Service Leader	Companies that operate in this quadrant are able to provide great value at the lowest cost.

Table 9-1: Value versus Cost Advantage Quadrants

5. Customer Service as a Value differentiator

With the given financial means, anyone can start up a logistic business by acquiring the hard assets to get it started. Duplicating the assets of another successful logistic company is not difficult. However, duplicating on the value advantage becomes an uphill task.

Value advantage such as tailored services; reliability and responsiveness are gotten only from years of experience to gain the advantage. The learning curve for new start up is always steep and it will take a while before they can become serious challenger.

The value proposition that customer seek will not remain static. It will change as the customers strive to move towards extracting more value from its vendors. Companies that are able to renew and provide new value proposition to the customer at the lowest cost will be clear winners.

As depicted in Figure 9-3, competitive advantage is sought after when customers perceived the value of the product of a particular firm outweighs that of its competitors.

Offering superior customer service can be a competitive advantage to many firms. Customers must perceive a firm's customer service level as superior in order to be able to leverage on it.

6. Customer Value Chain in Logistics

Customer service is an important part of the logistic equation for creating the value differentiation or advantage.

Because each customer preference and perception of value will be different, it is critical that a company is able to accurately link the customer value to its supply chain and logistic strategy.

Figure 9-4 shows the steps in identifying what matters to customers and then implement these into actions in the supply chains.

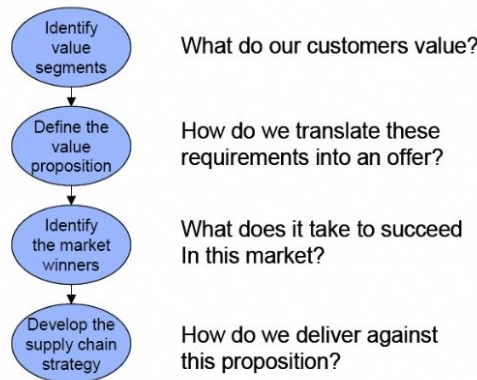


Figure 9-3: Customer Need (after Christopher, 2011)

7. Cost of Customer Service and Pareto 80/20 rule

Deploying customer service in different forms and flexibility will enable a company to tailor different value proposition to their customers.

However, the cost of deploying too many variations of customer service programs and service levels across to different customers will have a great impact on the profitability of the company.

The more elaborate the customer service programs, the higher the cost.

Figure 9-4 shows the exponential relationship between the cost of service and the service level.

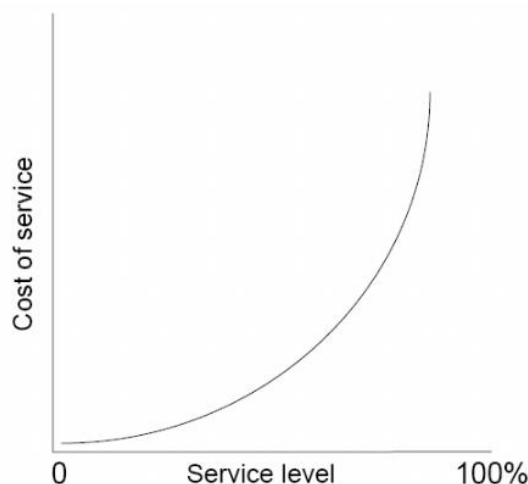


Figure 9-4: Cost of Service

Customer Service Level and programs need to be perceived as a value advantage by customer before it can be deployed.

Based on the Pareto principle, only 20% of the customer's base contributes 80% of the revenue or profit.

Hence it makes business sense to focus on these 20% of the customer and develop custom-made service programs that will keep these customers highly satisfied.

This is demonstrated in Figure 9-5.

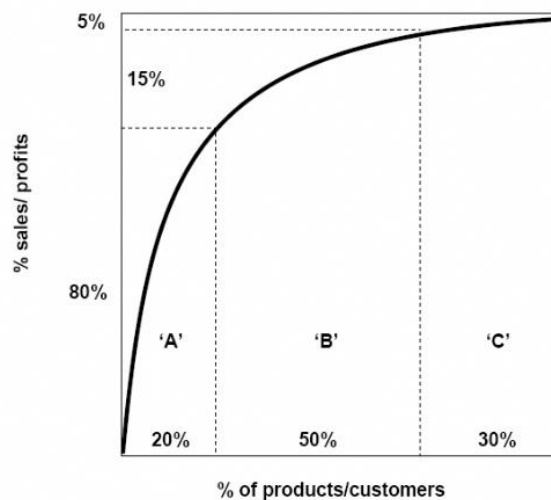


Figure 9-5: Pareto Principle

Customer's requirements and expectation are different and their willingness to pay additional premium for superior customer service level may also vary.

Companies trying to retain their major customers ought to be looking at coming up with different Customer Service Level program (eg Service Level A, B or C). Such differentiation is important because the major customers expect more.

Based on many research studies that have been conducted, the cost of acquiring a new customer is higher compared to the cost of customer retention.

8. Differentiated Customer Service

Not all services or products should be provided the same level of customer service. This is a fundamental principle for logistics planning.

Different customer service requirements, different product characteristics, and different sales levels among the multiple items that the typical firm distributes suggest that multiple distribution strategies should be provided within the product line.

Managers have made use of this principle when they broadly classify their products

into a limited number of groups such as high, medium, and low sales volume and then apply a different stocking level to each. To a lesser extent, the principle is also applied to inventory location.

When a firm stocks all products at all warehouse locations, it may do so to simplify administration, but this strategy denies the inherent differences between products and their costs, and it leads to higher-than-necessary distribution costs.

Of the sales volume remaining, the products should be differentiated by location. That is, the fast-moving items should be placed in the field warehouses with the most forward locations in the distribution channel. Medium-volume items should be placed in fewer regional locations.

The slow-moving items should be located only at centralized stocking points such as plants. As a result, each stocking point may contain a different product mix.

9. Conclusion

Customers assume that customer service involves an interaction with another human being, whether that person helps them find something, choose something or buy something.

For businesses, then, a more useful definition is that customer service is a business's ability to satisfy its customers.

Companies can have all the elements of customer service in place, from wait-staff through return policies, but if customers are not satisfied with the way their transaction was handled or its results, they won't be back.

And that's the core of good customer service – bringing old customers back (and attracting new ones through the “good news” that current customers are spreading about your business).

Customer service is therefore an important element in logistics itself and also in logistics planning. Before anything else, customer service must be built into the planning. It must be a deliberate effort and should not be an after-thought.

Reference

1. Christopher, M. (2011) Logistics & Supply Chain Management, 4th Edition, Pearson, Great Britain.
2. McDonald, M. (2002) Marketing Plans, 5th edition, Oxford, Butterworth-Heimann.