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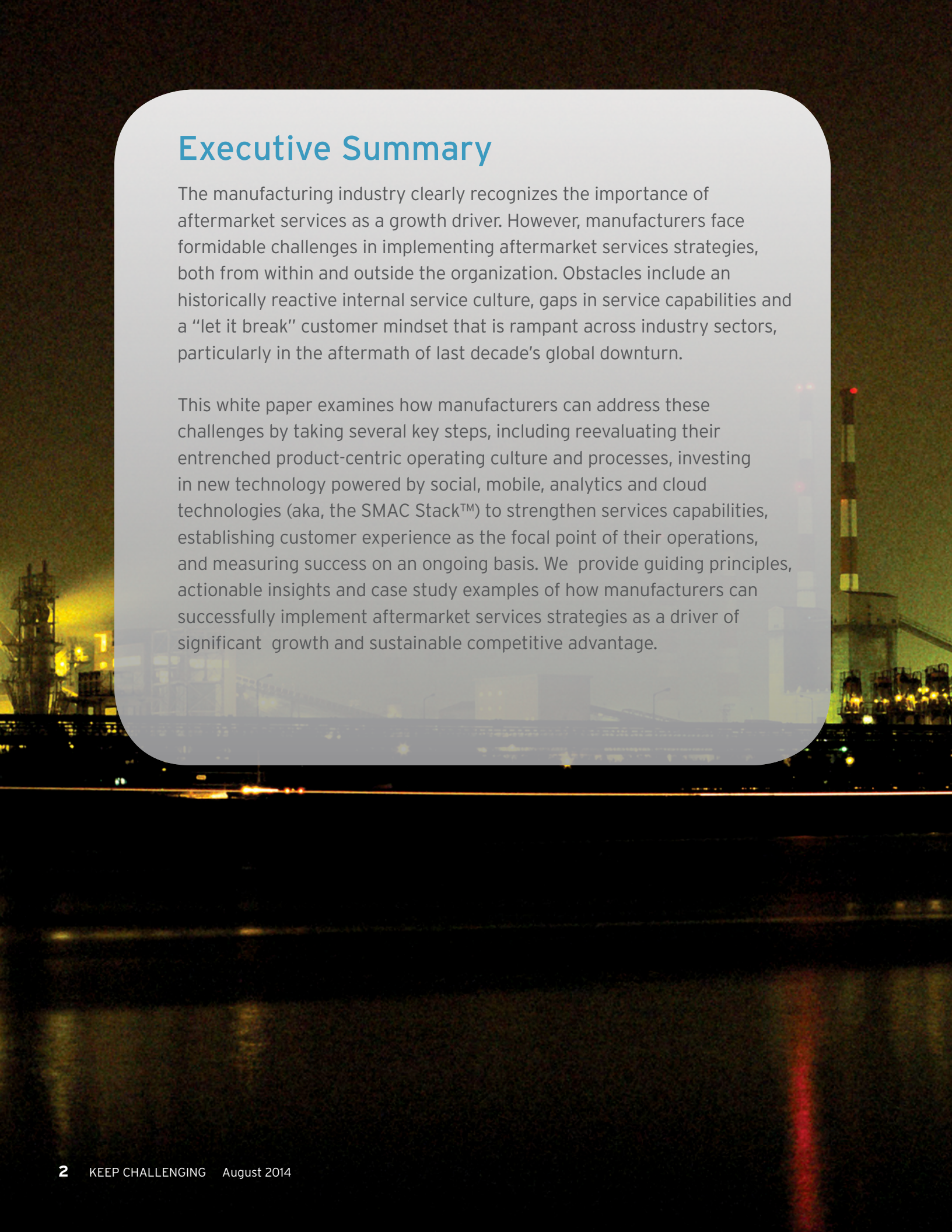
Enabling Aftermarket Services as a Growth Driver for Manufacturers

By embracing SMAC technologies and focusing on service excellence, manufacturers can overcome structural and cultural challenges and reap a panoply of rich rewards, including happier customers, more cross-selling and upselling opportunities and the chance to create lasting competitive advantage.

KEEP CHALLENGING™



Executive Summary

The manufacturing industry clearly recognizes the importance of aftermarket services as a growth driver. However, manufacturers face formidable challenges in implementing aftermarket services strategies, both from within and outside the organization. Obstacles include an historically reactive internal service culture, gaps in service capabilities and a "let it break" customer mindset that is rampant across industry sectors, particularly in the aftermath of last decade's global downturn.

This white paper examines how manufacturers can address these challenges by taking several key steps, including reevaluating their entrenched product-centric operating culture and processes, investing in new technology powered by social, mobile, analytics and cloud technologies (aka, the SMAC Stack™) to strengthen services capabilities, establishing customer experience as the focal point of their operations, and measuring success on an ongoing basis. We provide guiding principles, actionable insights and case study examples of how manufacturers can successfully implement aftermarket services strategies as a driver of significant growth and sustainable competitive advantage.

A Challenging Environment for Manufacturers

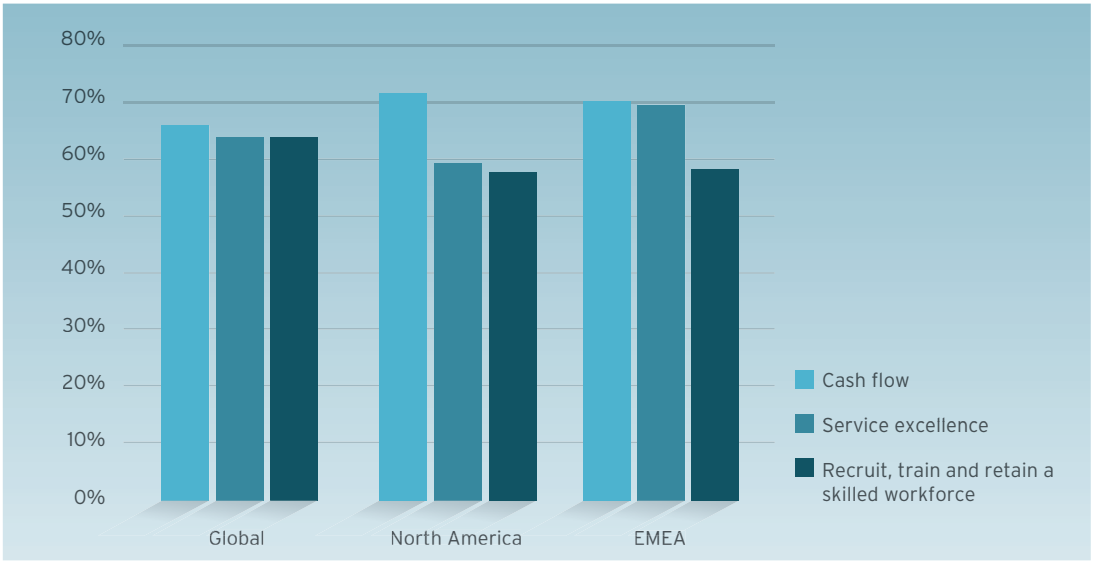
Manufacturers have operated in a highly challenging economic environment for the better part of the last decade and more so since the global downturn of 2008-2009.[1] According to a 2013 IDC Manufacturing Insights survey, just 12% of capital equipment manufacturers expect a substantial increase in equipment sales revenue over the next three years. A further 30% expect some increase, with 30% predicting flat revenues and 27% forecasting a decrease. In Europe, the Middle East and Africa (EMEA), just 15% of respondents expect a substantial increase in equipment sales volume over the next three years, compared with 9% in North America.[2]

Given the industry's engrained pessimism, equipment manufacturers worldwide have increasingly looked beyond traditional product portfolios to improve their top lines and profitability. They have focused on aftermarket services to counter both the cyclical demand for equipment and the volatility resulting from a persistently tough macroeconomic environment. Industry analysts predict that service optimization will be core to future profitable revenue growth; to enable new service strategies, leading manufacturers must make necessary investments.[3]

Obstacles to Establishing Strong Aftermarket Services Capabilities

In 2013, service excellence emerged as one of the top business concerns among manufacturers worldwide[4] (see Figure 1). While the importance of aftermarket services is now widely recognized in the industry, we have observed that equipment manufacturers continue to face significant ongoing challenges when transitioning to the aftermarket services space (see Figure 2, next page).

Top Business Concerns of Manufacturers Worldwide



Source: IDC Manufacturing Insights, 2013
Figure 1

Aftermarket Services Challenges

Figure 2

Identity Crisis

For a traditional product manufacturing company, moving from product-centricity to aftermarket services is easier said than done. When manufacturers discover that the product-focused strategies that have served them well and are responsible for their strong market positions are no longer sufficient to sustain their competitive advantage, they become unsure of their identity. The idea of moving away from a successful approach to a new, untested strategy — and the critical questions around repositioning as a service provider — are causing a troubling case of cognitive dissonance.

Entrenched Product-Centric Culture

Identity issues are exacerbated by an entrenched culture that revolves around products. A lack of clear vision and support for services from top leadership further compounds this problem. Resistance from product managers and internal competition for resources between products and services often emerge. The organization can even fall victim to its successful products if it refuses to look beyond them. It is, therefore, critical to overcome internal cultural issues and focus on improving service capabilities.

Reactive Service Mindset

Cultural problems are not limited to the leadership and product manager levels; they extend to the service organization, as well. Cast in the mold of the traditional service model, field service personnel tend to be highly resistant to change, putting them at odds with attempts to adopt new service strategies that revolve around proactive services and new technology platforms geared toward strengthening service capabilities and enhancing the customer experience. Figure 3 (next page) depicts a reactive service model.

Reactive Service Model

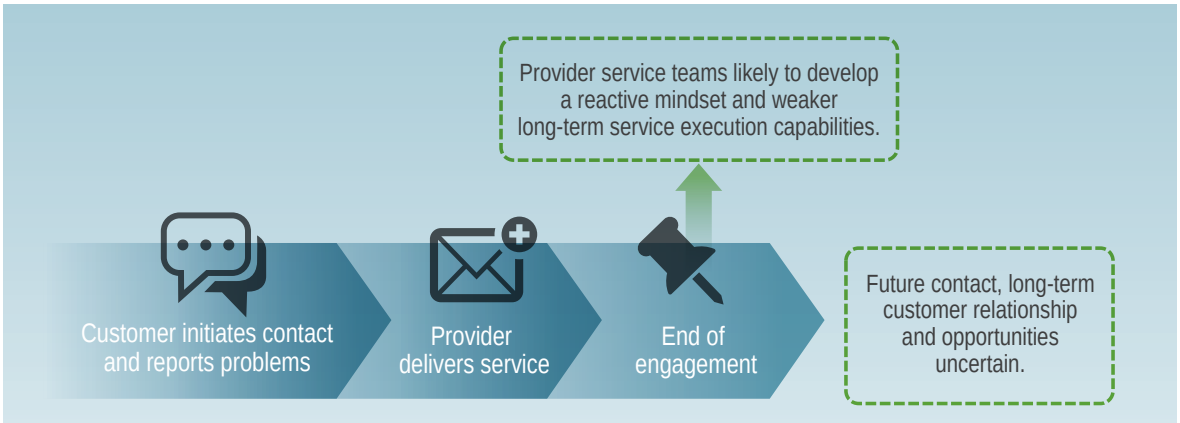


Figure 3

Understanding Customer Needs and Your Service Capabilities

The challenges for manufacturers are not limited to identity or cultural issues. Typically, customers of industrial manufacturers are not proactive in their service investments, adopting instead a "let it break" mentality. Changing this type of attitude is a significant challenge that requires long-term commitment, with gradual results. Moreover, manufacturers must understand their own ability to more effectively meet customer needs, a significant challenge that cannot be underestimated.

Developing Service Capability

It takes considerable time, resources and business acumen to develop strong service organizations. Manufacturers must make tough calls on service strategy, focus areas, personnel, training, customer experience and required technology investments, while continuing to administer to the health of their traditional product portfolio.

Nature and Scale of Service Investments

Developing service capabilities requires considerable focus, as well as allocation of limited resources. On the one hand, manufacturers can significantly impact the bottom line if they make an investment in assets such as qualified service delivery teams, service offerings and new technology infrastructure. However, they also need to balance their desire to capitalize on the potential of aftermarket services with the risk of over-investing in services or depriving resources to critical areas such as product innovation. This balance is not an easy one to strike, as immediate returns on investment have to be weighed against long-term goals.

Overcoming Challenges: How to Implement Aftermarket Services Strategies

The challenges outlined and the strategies required to counter them are complex and demand difficult cultural and operational changes. To overcome these challenges, manufacturers must focus on developing an internal culture that fosters customer-centric services. This new focus needs to be complemented by a technology infrastructure that enables service delivery and promotes a change in the service culture and its underlying processes in the long term.

Quick Take

Struggling with Aftermarket Services Challenges

A prominent equipment manufacturer with a highly diverse customer base is a classic example of a company struggling with an identity crisis. This company has enjoyed tremendous success due to its products, and it has continued to maintain a product-centric approach.

Despite its presence in close to 100 countries, this global manufacturer did not shift its focus sufficiently to aftermarket services, nor did it capitalize on its enormous installed equipment base when market conditions were favorable. In recent years, it has struggled to maintain revenues due to sluggish demand for its traditional products and the lingering effects of the global recession.

As a result of these market conditions, the company has been forced to enact significant austerity measures, including workforce reductions. In 2012, this manufacturer earned only about 6% of its total revenue of over $15 billion from maintenance or service of its installed base of equipment and related components — significantly lower than some of the leading equipment manufacturers, which average over 20%. This situation highlights the challenges faced by manufacturers in shaping their identity and determining the optimal product-service mix. More importantly, it presents a critical opportunity for this company to capitalize on aftermarket services to diversify its portfolio and mitigate the impact of declining product revenues, an approach that is likely to serve it well in the future.

Guiding Principles for Implementation of Aftermarket Services Strategies

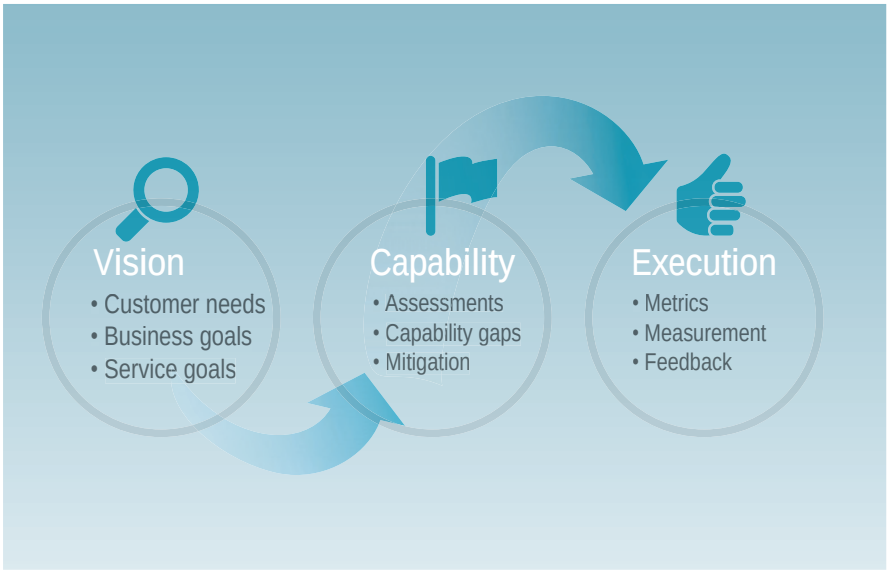


Figure 4

The proven guiding principles illustrated in Figure 4 should serve as the foundation for any aftermarket services strategies.

Vision: Organizational Goals and Customer Focus

There is no one-size-fits-all prescription for the extent to which an organization adopts service strategies, if it chooses to adopt them at all. Manufacturers must understand and lay out their long-term vision and goals for aftermarket services. Manufacturers that decide to make aftermarket services central to their operating model must confront a critical challenge of a traditional product-centric mindset, namely, a reactive service culture and the transition toward a proactive approach.

A reactive service culture results in transactional relationships with customers, depriving organizations of key opportunities to nurture long-term relationships and build service capabilities during the course of these relationships. On the other hand, a proactive approach, as represented in Figure 5 (next page), facilitates long-term relationships, enabling manufacturers to adjust to changing customer needs, and requires the ability to sustain such relationships.

For example, one of our clients, a leading industrial equipment manufacturer, is moving beyond a focus on operator-level customer personnel and maintenance issues and is making a proactive effort to engage the C-suite and directors, as well. It is pursuing an advisory role and educating customers about various service offerings and the impact of services on capital and expense planning, lifecycle costs for asset operation, operator productivity and intangibles such as safety, sustainability and environmental quality.

Figure 6 (page 10) provides a comparison of the performance indicators for both models and highlights the results achieved by one of our clients that made a concerted effort to change its reactive service culture to a proactive one.

A Proactive Service Model

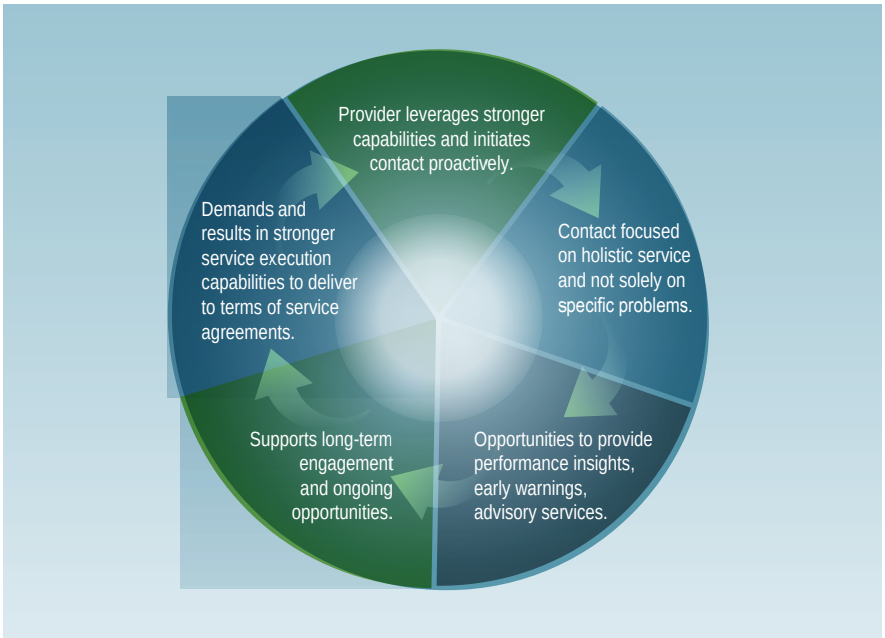


Figure 5

Further, manufacturers must establish goals for aftermarket services that are informed by their customers' expectations, which tend to be unique to each organization. This will also promote long-term internal organizational changes and foster an environment conducive to a proactive, customer-centric service model.

One of our clients, a leading HVAC equipment manufacturer, presents an illuminating example. This manufacturer has historically provided a valuable contract-bound service by sending highly critical alarms by e-mail to customers regarding their installed equipment. The alerts include the equipment name, equipment location, information regarding the root cause of the alarm and other details, wrapped in a string of characters that could be very difficult to interpret.

Working with us, this client created a customer service and branding strategy around this seemingly mundane transactional activity. Together, we:

- Revamped the delivery format, extending delivery to new channels, including smartphones and tablets with no change to the delivered content.
- Added one-touch service request capabilities that allow customers to request service calls, schedule service appointments and interact with service representatives instantly.
- Provided estimates of the time and cost of potential service visits based on the classification of the problem, which went a long way toward improving transparency and building the service brand.

These changes resulted in an overwhelmingly positive response from both customers and internal field service personnel, who were highly satisfied with the system's visual experience and ease of use. The average adoption rate increased from under 10% to over 70%, trending higher each month. These new customer touchpoints present new cross-sell and upsell opportunities, such as new equipment sales, parts sales and premium contracted service sales.

Continuous Self-Assessment of Service Capabilities and Mitigation

Services capabilities are not only difficult to establish; they are even more challenging to sustain over the long run. We believe the key is to cultivate a strong service development lifecycle similar to the one shown in Figure 7 (next page) and then progress toward service maturity. Manufacturers' competence in continuously assessing their capabilities, understanding customer needs, conducting a gap analysis and deploying mitigation strategies, such as investments in new technologies, is critical to progressing on the service maturity path and sustaining competitive advantage.

To assess capabilities and identify gaps, we recommend that manufacturers seek answers to the following key questions:

- How do we sell services today?
- What are our existing service capabilities?
- How do customers rate our existing services?
- What are our service goals?
- Do we have the technology infrastructure to support the desired service capabilities?
- How is our service organization adapting to these new technologies?
- What existing free services can be delivered for a price by adding additional value?
- How much are our customers willing to pay for such services?

Performance Attributes for Reactive and Proactive Service Models

Service Attributes	Reactive Service	Proactive Service
Contact initiation	By customer	By service provider
Predictive capability	Low	High
Problem identification	By customer	By service provider
Problem magnitude	Likely high	Likely prevented or low
Resolution time	Likely lengthy	Likely quick
Cost of resolution to service provider	Likely high	Likely low
Cost of resolution to customer	Likely high	Likely low
Continued customer engagement	Unlikely	Highly likely
Competition from other service providers	High, no service contract	Low during contracted period
Direct revenue forecast for service provider	Short-term, variable	Long-term, minimum assured
Pull-through revenue opportunities	Unlikely	Highly likely
Impact on provider's service capabilities	Negative	Positive
Impact on overall brand	Negative	Positive

Figure 6

- What do our customers want beyond our existing services?
- How much are customers willing to pay for these new services?
- What investments are required to build the capabilities to deliver new services?
- What non-service-related best practices can we leverage?
- How can we customize services and provide additional value at a premium?
- What is the experience that we want to deliver that complements our current brands?
- What is the impact on our existing operations?

Leveraging New Technology to Mitigate Capability Gaps

Cultural change is a long-term achievement that can be accelerated by the adoption of new technology, which also serves to mitigate capability gaps. It is not a coincidence that aftermarket services are gaining prominence in the age of advanced information technology. A recent phenomenon is the increasing emphasis on predictive capabilities using components of the SMAC Stack and the multiplier effect they provide when applied holistically.

Manufacturers are leveraging these technologies to sift through vast troves of mobile and social data stored on the cloud to identify value propositions for their customers, address specific customer needs and enhance the customer experience.

For example, we worked with a leading HVAC equipment manufacturer to redefine its service delivery mechanisms and the customer experience provided by its field service personnel. The manufacturer developed a remote service management

Service Development Lifecycle

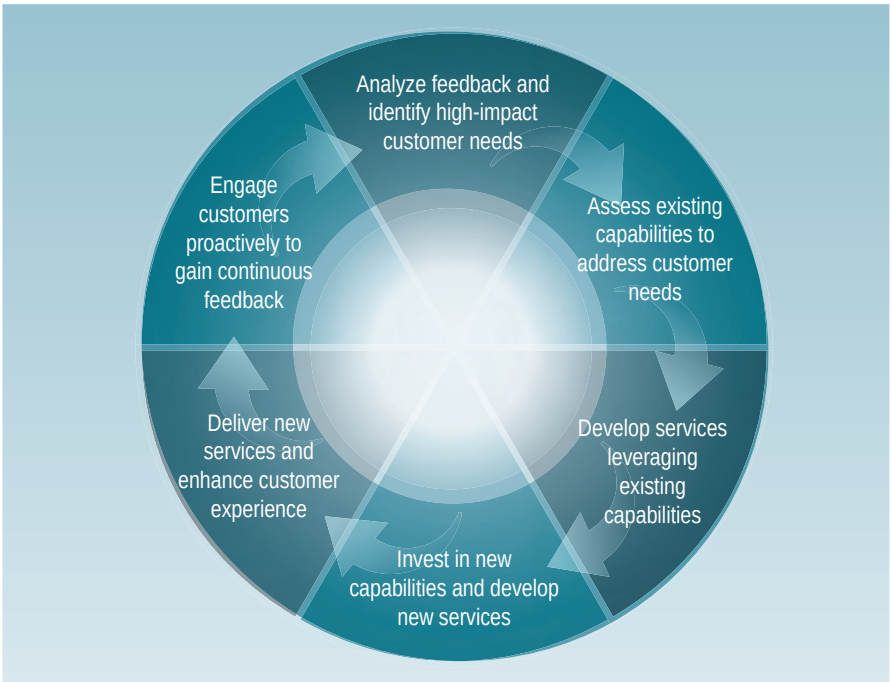


Figure 7

system that uses data analytics to generate alerts based on raw data collected from customer equipment. When the company utilized a holistic SMAC solution, it achieved benefits on many fronts simultaneously. The manufacturer is able to:

- Collect high volumes of real-time equipment performance data and store it on the cloud without capacity constraints.
- Detect early warnings of potential problems through predictive analytics, schedule technician visits for customers, identify potential causes for the problems based on the diagnostics codes detected remotely, and furnish an estimate of potential repair costs.
- Proactively send alerts to customers' mobile devices, advising them about ideal equipment use, and seek feedback at the push of a button provided in advisory messages.

As a result of this work, our client can now resolve over 55% of reported service problems remotely, thus reducing the cost of service visits by over 30%.

As a result of this work, our client can now resolve over 55% of reported service problems remotely, thus reducing the cost of service visits by over 30%. Early diagnosis has helped improve equipment life by 30% and reduce the number of problems reported by an additional 20% compared with a standalone data analytics solution.

Quick Take

Self-Assessment and Applying a Proactive Service Approach

One of our clients, a global industrial manufacturer, recently revisited its services strategy and organizational structure as a result of better understanding its customer base, reassessing its service capabilities and taking a proactive approach toward services. Over the past decade, it spent considerable resources on developing and delivering centrally envisioned services that complement its product portfolio. As a result, the manufacturer was able to achieve significant results, with over 30% of total revenues originating from aftermarket services.

However, in order to achieve continued growth by being more responsive to local needs, the manufacturer recently dissolved its global service organization and replaced it with four separate regional service organizations. The company discovered over the past two years that although its product portfolio is the same around the world, the dynamics that define the service market and the capabilities required to be successful vary drastically between regions. Customer attitudes toward aftermarket services, their willingness to pay, pricing differences and the capabilities of the local service teams are among the major contributors to the overall customer experience.

Our client also realized that despite ongoing success, it was important to adopt a proactive approach and ensure capabilities that are sustainable in the long term. We are helping this company redefine its service offerings, sales and service practices, and customer outreach through a customizable platform and regionalization initiatives. These initiatives include locally prevalent units of measure, local language support, customized reporting capabilities, emphasis on metrics that are relevant to local conditions, region-specific performance metrics and training. Such a localized approach is more effective than a one-size-fits-all, standardized global services organization.

Combined, these improvements resulted in a dramatic increase in customer satisfaction ratings, from an average of less than 2 to over 6 on a scale of 1 to 7 (with 7 being the highest). This illustrates the power and multiplier effect of the integrated SMAC Stack compared with the benefits that would have materialized from individual SMAC elements. (For more insights on this topic, see parts one and two of our white paper series on mobility in field services management.)

Adopting the SaaS Model to Deliver Services

Manufacturers are also leveraging technology by adopting the software as a service (SaaS) model to custom-build and/or deploy out-of-the-box software platforms that are capable of delivering services that did not previously exist in their service portfolios. For example, a leading building automation system and equipment manufacturing client recently ventured into energy management services by leveraging a combination of smart meters and customer energy consumption data. The manufacturer's customers were using third-party services to obtain these metrics.

We advised this company to invest in integrating a third-party energy benchmarking platform with its service portfolio, which consisted of equipment performance assessments, quarterly and on-demand performance insights, and sustainability advisory services to create new energy service offerings that make use of the benchmarking data. This was an innovative shift for our client from its core competency. As a result, the company can now sell services that provide insights about future trends in energy consumption, potential costs and comparisons with established industry benchmarks.

Execution: Establish Success Criteria, Measure Success and Incorporate Feedback

When implementing aftermarket services strategies, manufacturers should establish well-defined success criteria, measure success systematically and create mechanisms to incorporate the lessons learned. We recommend that companies develop internal assessment tools and metrics that will enable them to track the impact of the strategies implemented and take corrective actions promptly. Figure 8 (next page) depicts a scorecard that we developed for one of our clients to assess the maturity path of service teams across its service locations in North America.

The resulting corrective actions from such assessments served as inputs to the operational goals for the following period. They also provided visibility to top leadership regarding the performance of each service location, based on criteria such as vision, organizational structure, investments, technology adoption rates, incentive structure and so on. This has helped the service teams set realistic goals and show progress on the maturity path during each successive period. It has also helped improve mutual accountability between the leadership and service teams as they track leadership support and team performance.

Assessing Real-World Results

The journey to implement a successful aftermarket strategy places enormous demands on organizations to define clear goals, develop capabilities that run counter to traditional operating practices, and engage in a perpetual cycle of self-evaluation and gap mitigation. However, the benefits that manufacturers can realize are compelling, to say the least (see Figure 9, page 15).

Our clients have realized some of the benefits depicted in Figure 9 by diversifying into aftermarket services. One client – a global diversified manufacturer of industrial

Performance Attributes for Reactive and Proactive Service Models

Competencies/ Maturity Path Scorecard	Initiating	Progressing	Growing	Sustaining	Leading	Prior Rating	Current Rating	Gaps Identified	Corrective Actions
Vision and goals		✓							
Clear internal brand			✓						
Leadership commitment		✓							
Investment		✓							
Organizational structure			✓						
Defined roles and responsibilities		✓							
Adoption rate of new technology platform			✓						
Domain expertise				✓					
Revenue ($)		✓							
Pull-through revenue ($)			✓						
Percent growth over last period		✓							
Opportunities pipeline ($)					✓				
Opportunities conversion rate (%)			✓						
Number of new contracts signed			✓						
Contract renewal rate		✓							
Incentive structure				✓					
Training				✓					
Consolidated customer rating			✓						
Consolidated internal team rating				✓					
Consolidated leadership rating			✓						

Figure 8

Benefits of Aftermarket Services

Figure 9

products, including power tools, pumps, fluid handling systems and compressed air systems — invested in areas such as training and new services development, and partnered with us to develop a SMAC-enabled technology platform that leverages data analytics, cloud and mobility.

This platform allows our client's service teams to compare equipment performance over time and compare it with the performance of other assets operating in similar conditions and recommend changes to operator behavior. Because it is a cloud-based system, the platform also helps the company track the performance of higher numbers of equipment and handle larger data volumes.

Through the platform, the company can now provide business insights derived from analytics to its customers using Web and mobile dashboards. The platform also empowers its sales teams to convey the strong value proposition of its service offerings, such as deep insights into equipment performance, proactive service capabilities, reduced maintenance and service costs due to remote service features, and robust services capabilities that result in high responsiveness and an enhanced customer experience.

The quality of the manufacturer's business insights, enriched user experience, speed to market and scalability, powered by SMAC technologies, has enhanced the company's interactions and relationships with customers, which has benefited the product business, as well. The company is able to cross-sell or upsell alternative products, as well as upsell premium service contracts by leveraging the credibility of its existing services and the strength of its established relationships.

Typically, service contracts result in two to three times pull-through revenue. With new capabilities enabled by the service platform, our client anticipates up to 10 times pull-through revenue from service contracts and related equipment sales. In terms of revenues, it has reported over 30% of its $14 billion in annual revenues from the aftermarket.

The company can now collaborate with customers on service attributes such as delivery schedules, customer-preferred metrics and asset performance reports. These co-created services and their delivery structure serve as inputs to our client's larger service organization and are extended to its other customers, as well. Our

client's customers are recognizing the value of buying a product that is backed by an equally valuable service platform and the long-term benefit it will yield.

In addition to the new service platform, we also helped our client develop analytics to measure the adoption and effectiveness of the service platform within its internal services organization and use these tools to roll out new initiatives for training. Such initiatives are gradually improving organizational service capabilities and — coupled with enhanced customer relationships — transforming the business.

From operating as a reactive service provider, where services played a supporting role to product sales, our client is now a proactive service provider that uses its new SMAC-enabled capabilities to convey its strong services value proposition to customers. It is strengthening its brand by enhancing aftermarket customer experience with effective services and generating revenues independent of its product offerings. Moreover, it is now mature enough to perform self-evaluations that lead to corrective actions that advance its progress on the services maturity path. These capabilities are difficult for a competitor to replicate in a short period of time, thus delivering a sustainable competitive advantage.

Looking Ahead

Although manufacturers face formidable challenges when attempting to implement aftermarket service strategies, they must challenge the status quo with an eye on the future. This involves disruptive change, starting with the service culture and operating model, through building a new technology infrastructure around the SMAC Stack. In addition, they must establish competence and, eventually, outperformance in the aftermarket.

Achieving both objectives will help manufacturers serve the end-to-end needs of their customers, thereby facilitating a sustainable competitive advantage for the foreseeable future. Although this is by no means easy, it is possible, as the case studies in this white paper illustrate.

Footnotes

1. Bettina Wassener, "Manufacturing Reports Show Depth of Global Downturn," *The New York Times*, Jan. 2, 2009, http://www.nytimes.com/2009/01/03/business/worldbusiness/03yuan.html?_r=0.
2. "Aftermarket to Dominate Revenues for Equipment Manufacturers," Monitor Daily, Aug. 28, 2013, http://www.monitordaily.com/aftermarket-dominate-revenues-equipment-manufacturers/.
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4. "Aftermarket to Dominate Revenues for Equipment Manufacturers," Monitor Daily, Aug. 28, 2013, http://www.monitordaily.com/aftermarket-dominate-revenues-equipment-manufacturers/.

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About Cognizant

Cognizant (NASDAQ: CTSH) is a leading provider of information technology, consulting, and business process outsourcing services, dedicated to helping the world's leading companies build stronger businesses. Headquartered in Teaneck, New Jersey (U.S.), Cognizant combines a passion for client satisfaction, technology innovation, deep industry and business process expertise, and a global, collaborative workforce that embodies the future of work. With over 75 development and delivery centers worldwide and approximately 178,600 employees as of March 31, 2014, Cognizant is a member of the NASDAQ-100, the S&P 500, the Forbes Global 2000, and the Fortune 500 and is ranked among the top performing and fastest growing companies in the world. Visit us online at www.cognizant.com or follow us on Twitter: Cognizant.

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