



Point of view

Why OEMs Must Shift Focus to **Outcome-Based Services?**

Harvard Business School Professor Theodore Levitt wisely observed:
“People don’t want to buy a quarter-inch drill. They want a quarter-inch hole!”

Professor Levitt’s statement reflects a paradigm shift underway across industries—from products to services to solutions. From aerospace to technology, industries are looking beyond their products and services and are focusing on the customer’s needs and wants (“the quarter-inch hole”).

While industrial customers are demanding outcomes rather than products, businesses must retrospect and build capabilities before they deliver. In this article, we explore the capabilities industrial businesses must build and the impact such a model will have on the value chain.

What is outcome-based service?

One of the conversations centers on outcome-based service, a business model based on providing outcomes of equipment as a service contract. Instead of traditional maintenance, repair, and overhaul activities on products sold, organizations are looking to provide a set of holistic outcomes that their customers desire of the products without necessarily owning the product.

This business model isn’t entirely new. Rolls Royce’s Total Care program (for the aircraft engine business) provides a power-by-the-hour business model whereby their customers are charged per engine flight hour. The value proposition targets key customer needs the aircraft is always ready and available to fly, the flight is efficient and optimized, and the asset is so managed that it creates value—instead of selling aircraft engines and repair, maintenance, and overhaul services. In sum, they have shifted from selling aircraft engines to selling uptime.

Other examples include Schneider Electric’s Secure Power as a Service and Honeywell’s outcome-based services (part of Connected Building).



Why industrial manufacturers need to look at delivering outcomes

Commoditization is a bane for any company. Be it products or services, once it becomes difficult for the customer to differentiate a product from that of its competitors, margins start to erode because the manufacturers then have to be the low-cost provider to maintain market share. On the other hand, a differentiated offering that adds value to the customer (and therefore, is sought by the customer), can help sustain margins. If there are no outcome-based offerings in the market, companies can look to creating a segment in the market with such an offering and be a dominant provider before competitors catch up. The outcome-based market maybe their “blue ocean” of sorts!

On the other hand, customers themselves may start mentioning outcomes in their sales conversations because a few players in the industry have started rolling out such offerings. The manufacturer, in this case, is simply catching up with market demand.

Either way, advances in technology (IoT, cloud, and data and analytics) have enabled companies to provide such offerings to their customers that deliver long-term business value by creating new revenue streams or bolstering existing revenue streams to improve top lines and margins.

Why buyers of industrial machinery may prefer outcomes over equipment

The case for outcome-based service can be appealing for end clients for several reasons. Primarily, a departure from the asset ownership model to a pay-as-you-go model (from CAPEX to OPEX) frees up capital that can now be utilized in core activities. This is one of the reasons why cloud storage and computing look so appealing—instead of owning and maintaining IT assets, organizations can now focus on their core competencies. More so if the end customers themselves sell services because the business models are now aligned.

Another appealing reason is the transfer of operational risk from the client to the vendor as the equipment life cycle ownership lies with the service provider. Take the case of Schneider’s Secure Power as a Service. Instead of life cycle management of complex power system equipment, consumers pay for consumption by the hour instead. And, since the equipment is monitored 24x7, there is an improvement in the resiliency of the equipment.

Pre- requisites for companies to embark on this journey

Organizations must get two things right if they want to embark on the outcome-based service journey:

- Predict how their products will behave in a customer environment.
- Optimize their customer services to the extent that the new business model creates value both for them and their end clients.

The first involves leveraging new technologies such as IoT, cloud, data, and analytics. Embedding sensors to collect data from installed equipment and setting up an analytics team to analyze the data with the help of AI and ML algorithms can provide insights that can be leveraged to create value for the client and OEM alike.

However, merely adding sensors to products will not help clear the first hurdle. Most organizations have a good idea of how their product performs within the four walls of their manufacturing units. But how equipment will perform in the customer environment depends on customer usage patterns—a data set rarely collected by manufacturers. Leveraging IoT technologies, this data set must be captured by the OEM. Further, using AI and ML technologies, tangible insights must be drawn that can predict breakdowns and failures before they occur.

The second involves fine-tuning the customer service offering to the point where delivering outcome becomes a logical next step. This entails transforming field service operations of the company. In most organizations, field service is considered to be a cost center. While it may be an efficient cost center, field service must first transform into a profit center before embarking on an outcome-based service journey. This change in focus from cost reduction to top line growth is easier said than done as it involves a substantial amount of change management.

As evident in Fig 1 (based on data from the TSIA Field Service Benchmark report), field service plays a key role in determining whether a business will be profitable in delivering outcome or not. As high as 88 % of all incidents or breakdowns need assistance from the manufacturer or service provider, with 45% requiring on-site support [1]. Businesses that have profitable field service operations will reap higher benefits

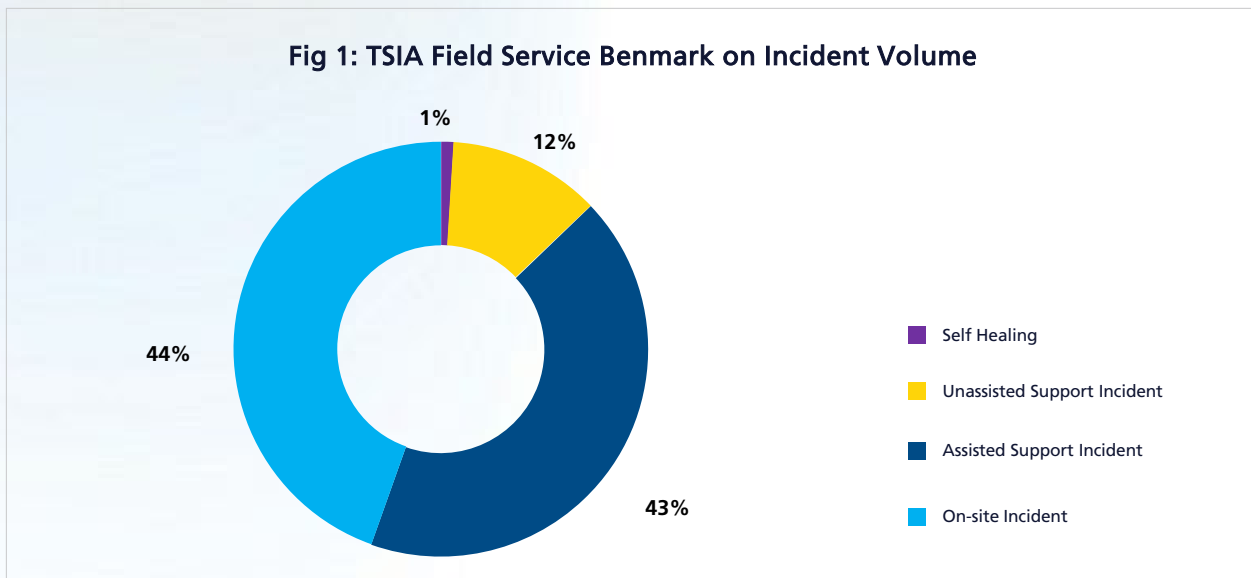


Fig 1: TSIA Field Service Benchmark on Incident Volume

Further, a digital transformation of field services involves alignment of metrics, people and processes, technology, and the service offering. The journey starts with defining the right set of metrics or KPIs to meet the strategic objectives, that too for each role (field technician, supervisor, dispatchers etc.). The transformation needs to be complemented by changes in people and processes—field technicians as the face of the brand and dispatchers as the nerve center of the customer service. From a technology enablement perspective, optimizations, simulations, forecasting, mobility, AR/ VR technologies, and connected products can be leveraged to improve technician performance and productivity. All these need to be aligned to the intended service offering.

The journey to outcome-based service—a value chain analysis

The path to outcome-based service isn't easy and involves collaboration among various functions such as corporate strategy, product and service development, sales, and the supply chain.

On the product and services front, many product features that are designed with the customer's ease of use in mind may need to be rethought because of the change in ownership. Simply put, the customer will not be handling the product; OEMs will. Therefore, customer-centric features may no longer be of paramount importance. This will, in turn, affect the manufacturing, supply chain, and channels partners.

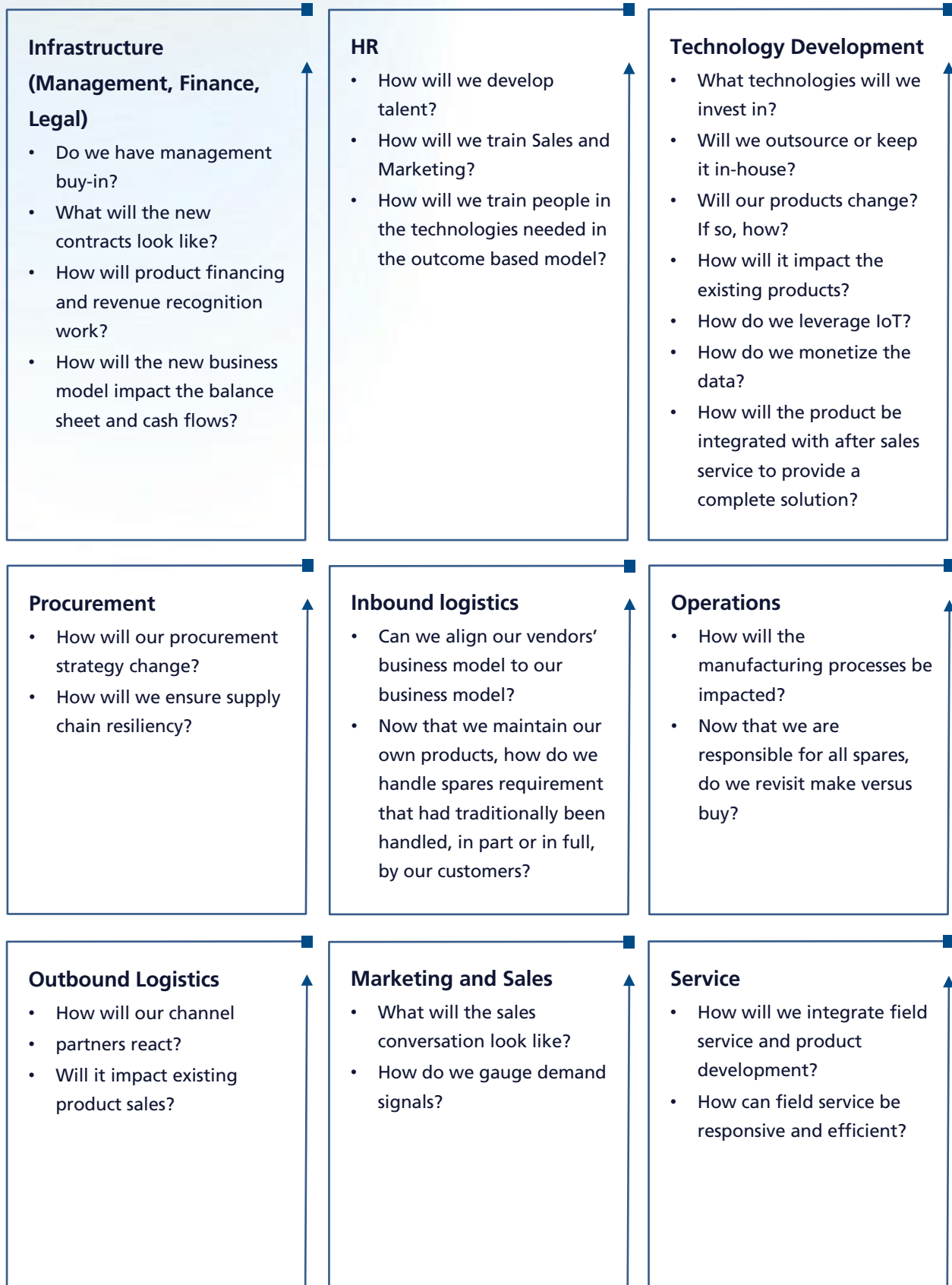


Fig 2. Value chain analysis

Nor will product strategy follow a linear path. It is unlikely that an organization will switch to outcome-based service in a big bang approach. Products will continue to be sold in parallel with outcomes which will necessitate a change in the sales strategy. Sales will have to straddle a fine line between selling products and outcomes under the new business model.

Much will depend on the C-suite buy-in. People involved from strategy to product development to sales will need to be sufficiently incentivized for the initiative. Change management will play a big role in bringing the organization along.

However, the most crucial piece of the puzzle is what the customer wants and needs. There is a need to understand where the product fits into the end consumer's value chain, the outcome the customer values, and the consumer experience preferred.

In most industries, demand signals have begun to come in from customers for an outcome-based approach. This approach involves close coordination with the end consumer to develop a mutually beneficial arrangement. The biggest hurdle would be to decide on the set of outcomes that customers want and those which OEMs can offer sustainably. It may not be as simple as dollars per engine flight hours. Even after a reasonable set of outcomes is determined, it is possible that customers may want to switch to a traditional approach down the road. Customer-centricity is key—customers must always have the option to switch between solutions of their choice. Finally, businesses need to understand that the end consumer may not always be on board with the new business model and may want to keep buying products and services instead.

All things considered, it is recommended to follow an Agile development process in creating the service offering. Once an MVP is developed, OEMs should focus on rolling out the pilot in a closed geography to gauge customer response. With customers onboarded, OEMs can work on fine-tuning the delivery model before they roll out to a larger audience.



About the Author



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