

# Chapter 2

## Goods, Products and Services

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### 2.1 Introduction

Defining terminology is a useful starting point when reading or writing on the subject of service to prevent any confusion or assumptions that we all understand the terms to mean the same thing. So, what do we mean by goods, products and services? This is a book about service, but what *is* a ‘service’ and how is it different to ‘goods’ or ‘products’? Whilst most people intuitively know the difference between a product and service, actually defining this difference with clarity and accuracy of text is not straight forward. The terms ‘goods’ and ‘products’ appear to be used interchangeably in much of the literature, but even here we can find debate about meaning (Araujo and Spring 2006; Callon 1991, 2002). However, for the sake of brevity we will here accept that they both refer to the same thing and focus on attempts to differentiate goods and services. This quest is far from straightforward. Since the early eighteenth century academics and scholars from different domains have attempted to define these terms explicitly (Say 1803; Levitt 1981; Hill 1999; Gadrey 2000). In this chapter we will attempt to illustrate their findings in order to provide some background to the debate.

### 2.2 Goods

In the eighteenth century Adam Smith (1776) stated that goods have exchangeable value and so a characteristic of a good is that its ownership rights can be established and exchanged. Goods can be considered as embodying specialised

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knowledge in a way that is highly advantageous for promoting the division of labour (Smith 1776; Demsetz 1993). Nassau Senior (1863) described goods as material things, meaning that goods are tangible and have physical dimensions. These concepts were still accepted over 100 years later when The System of National Accounts (SNA) (1993) defined goods as physical objects for which a demand exists, over which ownership rights can be established and whose ownership can be transferred from one institutional unit to another by engaging in transactions on markets. Hill (1999) summed up the major characteristics of goods as an entity that exists independently of its owner and preserves its identity through time; his definition supporting that of the SNA. Following these definitions we can outline a set of attributes for goods:

- Physical objects for which a demand exists
- Their physical attributes are preserved over time
- Ownership rights can be established
- They exist independently of their owner
- They are exchangeable
- Unit ownership rights can be exchanged between institutions
- They can be traded on markets
- They embody specialised knowledge in a way that is highly advantageous for promoting the division of labour

These attributes are broadly accepted by academics and reflect 200 years of ongoing debate.

## 2.3 Services

Although we have found a long standing agreement over the definition of products/goods and their characteristics, the definition of services has never reached consensus. Consequently it is hard to obtain full acceptance about the distinction between goods and services. Here we will present some of the different perspectives on service from the literature.

## 2.4 Intangible, Heterogeneous, Inseparable & Perishable (IHIP) Characteristics

As marketers began to recognise and emphasise the importance of services (Fisk et al. 1993) they consequently called for services to form a separate part of a companies' marketing strategy (Lovelock 1983). A major contribution to the services debate was a classification consisting of four features:

- Intangible
- Heterogeneous

- Inseparable
- Perishable

These features of what makes a service, referred to as ‘IHIP’ characteristics, have formed the basis of a consensus in most of the marketing literature. But what do they mean in this context and do they provide a strong differentiator? Each characteristic is discussed below.

### ***2.4.1 Intangible***

Intangible things are not physical objects and only exist in connection to other things. Examples include a brand's image, or goodwill. Harker (1995) humorously, though usefully described services as ‘something that you cannot drop on your foot’, which vividly illustrates the intangible characteristics of services. Although the habit of describing services as intangible goods comes from the economics literature (Hill 1999; Miller 2000), this view is common in management and marketing sectors (Chase and Aquilano 1992; Bowen and Ford 2002).

However intangibility may have failings as a differentiator between service and product. What is music, a book or a film? A product or a service? Hill (1999) identified this group of intangible products in the form of entities that are recorded and stored on media such as paper, film, tape or disk. Intangible products include the stories generated by authors, music created by composers or software games designed by software engineers. Although these have no physical dimensions of their own, Hill (1999) argues that in their saleable form these intangible products have the salient economic characteristics of goods and little in common with services. Therefore he suggests this type of intangible product should be recognised and marketed as a type of good rather than a service. The intangible nature of service is a useful characteristic to employ, but an ambiguity remains.

### ***2.4.2 Heterogeneous***

A common service varies according to the context, nature and requirements of each customer. It may be varied according to different quality standards associated with different costs; services can be varied across regions or cultural background; services can also be fluctuated by different characteristics of providers. Therefore heterogeneity, referring to the multifaceted different experience that may be had from a single type of service is considered as a factor to distinguish goods from services.

However, numerous exceptions can be invoked to counter this distinction. For example, some tangible goods can be heterogeneous. For example in the automotive sector, the Mercedes E Class car is offered with  $10^{24}$  variations and the claim on the production line is there has never been two the same (Schaffer and Schleich 2008). In contrast, services can be standardised. McDonald's produces food under highly

automated and controlled conditions (Levitt 1972) and customers receive the same taste and quality of a certain type of burger all around the world – a homogeneous offering. Yet most would consider a car to be a product and fast food a service.

### **2.4.3 Inseparable**

Services may be said to be inextricably linked with customers in terms of production and consumption and so it is said that service is inseparable. For instance, a service provider may not provide their services until the customer engaged. In contrast, a manufacturing company can still manufacture and deliver goods through channels of distribution without knowing the end customers. However, this characteristic is also open to challenge and interpretation. Automated services such as an ATM allow customers access to a predefined set of services, such as to check bank account balances and withdraw money, without the pre-knowledge or assistance of banking staff. It could be argued that here the production and consumption must be separated in order for the service to be mechanised.

### **2.4.4 Perishable**

Using technical criteria to define services, Smith (1776) states a service will ‘perish in the very instant of its performance, and seldom leave any trace or value behind them for which an equal quantity of services could afterwards be procured’. Here Smith shows one of the important features of services, which is perishability. It may be said that services are not a stock of fixed assets and it is not possible to store services in inventories (Hill 1999; Gadrey 2000). For example, when operating an airline a seat on a plane may be offered for a Sunday night flight. If that seat is not sold, it cannot be stored and sold in the future – it has perished. Likewise, if a traveller buys the seat and flies to their destination, once the contract ends, the client is no longer entitled to stay in the seat or to acquire any further services from the airline. Hence, the services provided perish in the very instant of the contract termination and may be described as leaving no trace or value behind them.

Jean Gadrey (2000) argued that services were not necessarily perishable, using the example of the servant to illustrate his point. If it is the servant’s task to clean and tidy the premises, then the output of their efforts does not vanish when the work is done. In fact, the visual result is used to evaluate the quality of the work. Therefore perishability is not a definite feature for all service sectors, but certainly may be a useful characteristic to recognise in many service domains (Fisk et al. 1993; Hill 1999; Zeithaml et al. 2006; Araujo and Spring 2006).

Whilst IHIP characteristics are useful to the discussion on services, the characteristics of a service offering they propose cannot be used to distinguish all goods and services because we can find exceptions in each case.

## 2.5 Experience

The notion of service as experience is provided by Pine and Gilmore (1998), who suggest: ‘Experiences occur whenever a company intentionally uses services as the stage and goods as props to engage an individual’. For instance, when a ticket for a rock concert is bought the buyer is provided a particular seat and is entertained by musicians. It may be argued that they did not wish to buy a ticket or a seat but in fact their purchase relates to their desire for a memorable and unique experience. Tangible goods and intangible services are brought together to create a memorable experience for customers at a point in time. Following Pine and Gilmore (1998) we can suggest that the value of experience is a significant intangible characteristic of a service.

## 2.6 Quality

Customer service and service quality are key issues facing many service operations managers. For a tangible product, customers can visualise its physical attributes before purchase (Zeithaml 1981). For example, even though they perform a similar ‘transport’ function one can easily justify why a Rolls Royce is more costly than the basic Tata Nano motor car from their aesthetic characteristics (Bowen and Ford 2002). However, it is relatively more difficult to compare the banking service provided by two similar UK based high street banks such as HSBC plc and NatWest plc objectively. We may, for example, be heavily influenced by our own or our friends experience. Chase and Dasu (2001) conclude that ultimately a customer’s perception will be a determining factor on the effectiveness of a service organisation. Therefore managers of service operations would usefully have a methodology to evaluate customer satisfaction and loyalty subjectively (Heskett et al. 1994; Bowen and Shoemaker 1998; Paulin et al. 2000). Lundberg noted that more often than not, the quality and value for a particular service can depend wholly on the customer’s judgement at that particular instance (Lundberg 1991). For example, two people sat together can easily have different views on a music concert and even the same person can have different opinions of the service experience if asked at different times (Bowen and Ford 2002). One commonly cited method that has been developed to assess the subjective quality of a service is named SERVQUAL which is based on the gaps between expectation and the perception of the service delivered (Parasuraman et al. 1988). SERVQUAL enables service and retailing companies to evaluate consumer perceptions of service quality and helps to identify areas requiring managerial action (Parasuraman et al. 1988). The approach divides the notion of a service into five factors that address a customer’s perception of quality. The factors are:

- Tangibles – physical facilities, equipment, staff appearance, etc.
- Reliability – ability to perform service dependably and accurately
- Responsiveness – willingness to help and respond to customer need
- Assurance – ability of staff to inspire confidence and trust
- Empathy – the extent to which caring individualised service is given

Quality is measured for each factor by the gap between the expectation and the perceived service delivered. Using this method it is possible to gauge how well a service offered meets the expectation of a customer. Using this model suggests that manipulation of individual customer expectation through marketing or brand management can alter perception and hence the quality of the service.

## 2.7 Tradability

The producer of a certain product is its first owner, but the ownership can be transferred in terms of money or goods exchange during trading. According to Rathmell (1966), compared to goods, a service is an act rather than a thing. When a service is purchased the buyer pays out his money without establishing an ownership right because there is no actual asset to establish ownership of. In contrast, when a good is purchased the buyer acquires an asset where he can establish his ownership right. As such goods and services may be defined with reference to their tradability. The SNA (1993) definition mentioned earlier defined services as outputs produced to order and which cannot be traded separately from their production; ownership rights cannot be established over services and by the time their production is completed they must have been provided to the consumers. From this definition, two ways to distinguish goods and services are tradability and ownership rights, with goods often seeming more tradable than services. This is because goods such as clothes and electronics have a physical presence and therefore may prove relatively easier to distribute globally, providing sufficient funds and resources. In the days of Adam Smith it would have appeared near impossible to produce services in one country and subsequently export them to another country. However, as a result of the rapid development of technology, such as the internet and telecommunication channels, services can now be provided in a way similar to goods. It is not unusual, for example, to set up a telephone call centre in India and to provide services back to the UK (Araujo and Spring 2006). Companies adopting this approach may take advantage of the cheaper labour of one country whilst gaining the higher price of providing that service in another. Due to this, Hill (1999) concluded that services can be, and are, exported, but only by resident producers providing the services directly to non-resident consumers.

## 2.8 A Change of Condition

Hill (1977) defined service as a change in the condition of a unit or a person, or of goods belonging to some economic unit, which is brought about as a result of the activity of some other economic unit, with the prior agreement of the former person or economic unit. Hill emphasises that the institutional structure of production is essential for the definition of services. Gadrey (2000) then built the service triangle

involving producer-user interaction. The concept of the triangular relationship is illustrated by Gadrey's garage example. Someone (A) owns a car (B) and the owner (A) requests a garage (C) to repair the car. Ownership rights are not exchanged, but value is created for both the owner in terms of having the car fixed and the garage in terms of financial reward. Gadrey (2000) points out services always involve a triangular relationship between A, B and C. This main contribution clarifies the nature of services and places producer-user interaction at the centre of attempts to distinguish between goods and services.

## 2.9 Goods and Services, or Is It All Service?

From the analysis so far, it is found that there is no perfect definition for separating goods from services, though scholars have been trying for a very long time. In their attempts to identify the differences between goods and services the similarities between them are often neglected. Firstly, both goods and services can be tradable which means both entities must at least have one provider and one customer. The customer often pays an agreed fee to the provider in order to acquire the ownership of a certain good or gain services for a certain period of time. In addition, there is always a reason and motivation behind the act of providing certain goods and services. It could be the provider who wants to make profit or improve their reputation. Secondly, the characteristics of goods and services often overlap each other. It is believed that there are actually very few pure goods and pure services. Instead they may form a spectrum from pure goods on one side to pure services at the other, with tangibility as the differentiator, joint entities in between having variations of joint characteristics (Shostack 1977, 2001). Commodity items which are traded globally based solely on price may be thought of as a pure form of tangible good e.g. wheat, gold, crude oil. A purely intangible service may be teaching as each person in the class will gain something different from the experience. John Rathmell (1966) took a sculpture as an example of a pure good as 'no act is performed' – though as a sculpture has aesthetic value, which could be seen as intangible, this may be questioned. He also suggested that the benefit or utility arising from legal counsel represented a pure service. With these forming the extreme, most goods, whether consumer or industrial, require supporting services in order to be useful; most services require supporting goods in order to be useful. Hence they will sit at a point along this spectrum. It may be more appropriate to take a goods-services continuum view point rather than defining goods and services explicitly.

Vargo and Lusch (2004, 2006, 2008) develop this line of thinking further and contend that all products and services only realise their value through their use. All products and services exist to provide 'service' to a customer, hence *everything is a service*. They have developed this into a concept they describe as 'Service Dominant Logic' or SD-logic. SD-logic focuses upon the concept of value creation rather than 'production' and places value creation as an interactive process where the firm and their customer must be considered within their relational context.

Firms work in value creation networks, in dialogue with their partners co-creating value. They state that ‘innovation is not defined by what firms produce as output but how firms can better serve’. They make a clear distinction between competing with offerings called *services*, which reflects a product/service distinction and *competing through service* to provide value and positive experience for all parties.

We can see the rise of ‘service’ within industry as manufacturing firms provide more complex product service combinations so that they do not need to compete on the basis of cost along (Neely 2010). Servitization is the term becoming more commonly used to describe this process, where companies increase revenue by offering service options in addition to their products, such as guaranteeing availability or providing service for the products life (Vandermerwe and Rada 1988; Oliva and Kallenberg 2003). This integration of products and services has been labelled a ‘product and service system’ [PSS]. PSS are described as offering ‘value in use’ (Baines et al. 2007), which means their value is only realised through their utility – which takes us back towards the concept of service as experience (Pine and Gilmore 1998).

## 2.10 What Are Products/Goods and Services?

Despite many years of research clear definitions of product and service has eluded researchers. Figure 2.1 shows the timeline for some of the debate in the literature, covering more than 200 years.

From this work the ambiguity of any single definition of service and how any perspective taken may influence process or value should be recognised. What we have seen is that the thinking has shifted from a pure service or pure product focus to a combination or product-service system (PSS). This recognises the offering of a combination of product and service for which greater revenue may be generated. Taking a pragmatic view, we should *work with the customer* to understand how goods and services best *create a service value proposition*, meet market requirements and generating sustainable profit *for the firm and the customer*.

## Exercises

- Identify three different services that you have used and are familiar with.
  - Why are the three cases you chose services and not products?
  - How is the service delivered?
  - What contribution do you as a client have to make to access value from the service?
    - E.g. fill in forms, make decisions etc.
  - Could you improve on the design of one of these services to deliver a better experience for the client and greater profit for the provider?

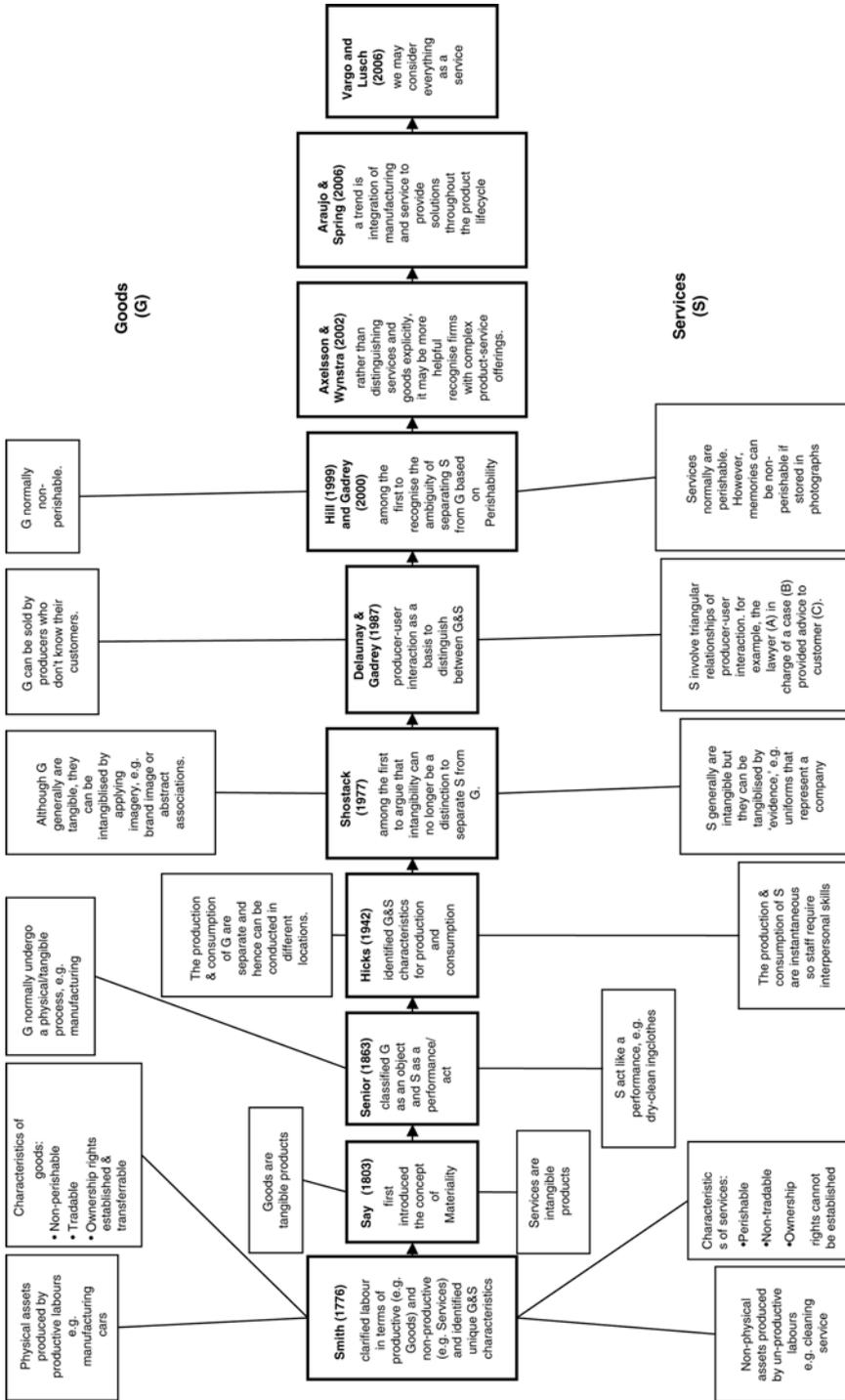


Fig. 2.1 Defining goods and service: over 230 years and counting

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<http://www.springer.com/978-1-4419-8320-6>

Service Design and Delivery

Macintyre, M.; Parry, G.; Angelis, J. (Eds.)

2011, XXII, 170 p., Hardcover

ISBN: 978-1-4419-8320-6