BLIND SPOT

Illuminating the Hidden Value of Business

by

Steve Diller, Nathan Shedroff, and Sean Sauber

Foreword by Douglas Rushkoff

TWO WAVES

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CHAPTER

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A World of Hidden Value

On July 14, 2014, an Engadget editor named Ryan Block and his wife called to cancel their Comcast cable and Internet service. During an 18-minute phone call (only 8 of which were recorded), a Comcast customer service representative badgered them with questions and refused to do the simple task they asked. The entire conversation consisted of exchanges like the following:

> Block: "I'd like to disconnect."
>
> Service rep: "Help me understand why you don't want faster Internet."
>
> Block: "Help me understand why you just can't disconnect us."
>
> Service rep: "Because my job is to have a conversation with you…about keeping your service."

This went on until the bemused Block wondered aloud, "Am I being punked?"

For those of you outside of North America, Comcast is a cable TV and Internet company that frequently tops the lists of the worst companies on the continent. Its most obvious problem is the terrible relationships it has with its customers. Many people simply hate dealing with the company.

Part of the blame falls on the industry: almost all cable and Internet companies in the United States fare poorly in customer surveys. Still, part of the blame has to fall on the company itself. Comcast offers an array of conflicting and confusing promotions. The deals routinely end 12 months after they begin, triggering huge increases in prices that surprise customers. Then, if you try to disconnect, the company makes you cancel over the phone, where you'll find a customer service rep trained to do nearly anything to keep you as a customer. And after you cancel their services, the company often doesn't stop billing your account until you physically return equipment to the nearest store, which may not be nearby.

Worse still, customer service reps often act like Block's did. He may as well have been a robot—he had a script, and he stuck to it. His compensation was likely based on how many customers he could prevent from discontinuing service. In an ordinary interaction, people respond to one another. If a person seems upset, you don't start telling jokes. If they're happy, you're happy for them. You build relationships using empathy, not by stubbornly saying the same thing over and over, regardless of what the other person says.

Over time, emotional experiences add up. If you have one interaction after another that leaves you feeling worse, it will result in a bad relationship. When that happens, you talk about the company in the same way that you talk about a person you can't stand: obtuse, frustrating, and annoying. You can actually come to hate a business. And when you get a chance to get rid of its services, you dump it, just as you might dump a friend or romantic partner. (The same is true in the positive, too: you might love and admire a company based on the kinds of interactions you have with them.)

That said, you might ask why Comcast is still in business. Because it's lucky. It has a virtual monopoly in some regions and competes with only one or two rivals in the rest of the regions. Its competitors all engage in the same unpleasant practices, so consumers have to pick their poison. But most companies have no such luxury. If Comcast were a neighborhood restaurant, it wouldn't last more than a few months. Within days of opening, anyone who went there would tell everyone else to stay away.

In fact, most small businesses understand that their customers have a series of experiences that turn into a *relationship*. They know that developing positive relationships is critical to their success. They have to learn their customers' names, understand their preferences, and know what their customers want before they say so. Their business has to be positive, upbeat, and sensitive. Being good at what they do simply isn't enough. They have to know how to give and take in a two-way conversation. They have to care.

Blind Spots and Opportunities

You'll find that this is just one of many blind spots that businesses have. In Comcast's case, short-term profit is much more important than long-term relationships, and holding customers prisoner is the only acceptable corporate strategy. Comcast prefers to incentivize management and front-line employee alike to make it nearly impossible for customers to leave (although, ultimately, it's no more difficult than a call to their credit card company to cancel the account) than to give its customers a reason to *want* to be customers for the long term.

This is just one way in which traditional business thinking has blinded its practitioners to reality. Relationships are the source of long-term value, not merely because it's easier to keep an existing customer than to acquire a new one, but because satisfied customers help a business acquire new ones.

It's really no different than personal relationships. While the healthy relationships you forge with friends and family are built more on emotional and meaningful value, the same is still true of relationships built on financial and functional value. For some strange reason, businesspeople have been told that only the short-term, financial value is worth building, but any wise businessperson knows this isn't the case. Still, traditional business literature is rife with this contradiction.

Broadly speaking, everyone has at least some blind spots. This reference indicates an area of the retina (the inside back of your eyeballs), which has no light-sensitive rods and cones because it's where all of the other optic nerves flow out of the eye and into the brain. This creates a small disc in your field of view that has no actual information, although your brains are facile in filling in the missing signals with assumed data that makes it seem like you're getting a complete, seamless picture of our surroundings. You don't really notice that you're not really seeing some of the data around you.

Likewise, organizations often have blind spots that they don't notice because their managements "fill in" what's missing with alternative perspectives, or they ignore missing data because they can't make sense of it themselves. Unfortunately, this process is often filled in with dogma and not experience. Unlike what our brains are capable of doing, these blind spots cause companies to miss important cues, obscure lucrative opportunities, and assume they have the complete picture when they're leaving dollars on the table, because they never see what they don't look for.

The blind spot we're most interested in here has to do with what contributes to companies' total value, namely, the building of relationships with customers Without seeing relationships for what they are—a mutual appreciation built on sequences of pleasing customer experiences over time—organizations miss what is often the single most important opportunity to build their total value (see Chapter 2, "Defining a Business Relationship," for more information).

Relationships and Opportunities

What defines a relationship with a company instead of another person? Put simply, it's a connection with a company that someone values. You can use a product to do a task, but for many of the things you own and use, you don't value them beyond their functions. A relationship is different. It grows out of the customer's interactions with your company. It can be quite strong and even have human dimensions, and it's an opportunity for a company to create a long-term customer.

Such a definition may seem strange or overstated, but research has shown that people see and react to brands and businesses much as they do to other people. In the 1990s, for example, Stanford researchers Cliff Nass and Byron Reeves found that users of devices such as computers and microwave ovens often treated these objects as if they were human. In other words, they used a shorthand with these objects that granted them a kind of "virtual personhood."[1] Everyone knows that a microwave isn't a person, nor a computer, but it's much easier to treat it as if it were—and to expect the same treatment, in kind. This grants the device (or company) the permission to have and express emotions, personalities, and even agency—but only as long as it acts like like a decent human being. The moment the company crosses the social boundaries

1. Nass and Reeves' tests showed that even really smart graduate students at one of the best universities in the world performed this shorthand. It's not something that only naïve or inexperienced people do. They showed that complex interactions resulting in trust, persuasion, and allegiance could all be created through very simple tasks with computers. In just one example, they found that a computer that flattered itself in very simple language, after performing a routine web search, garnered distrust and disgust, just as if a person had flattered itself. However, if a second computer flattered the first (the one performing the search), the operator thought more highly of both (the one that had been praised and the one doing the praising). This exactly mimics Western human behavior. Nearly any complex social relationship can be modeled between people and devices, and fascinatingly, they still hold true.

of acceptable behavior (like ignoring your pleas to cancel your service), the same power that builds brand value allows it to be destroyed—even faster. That colleague you trust at work, that you treat with respect? Once you find him to be a purposeful impediment to your own tasks, he's no longer an ally but an adversary—or even an enemy. This is the nature of human relationships, and it's the same with how you expect devices, services, and organizations to behave. The value you grant them (or revoke) is entirely built on the relationships you build.

In a ground-breaking study in 1998, Susan Fournier (a noted management scholar and researcher on brand value) argued that brands and customers do forge meaningful relationships. The reason is fairly simple. We're human, and as humans, it's what we do. We grow up learning how to forge relationships with other people. When we interact with products or companies, we default to what comes naturally.

Of course, products and companies aren't people. It may not make sense to love Disney, or you may be disappointed that the creator of a mobile device espouses a cause you dislike, but it happens. You might get angry and frustrated at a vending machine. You possibly love shoes or one of your home appliances. You may feel like you're greeting an old friend returning from a trip abroad when you crack open your favorite soda. It's how humans make sense of the complex world around them. It's just how we are.

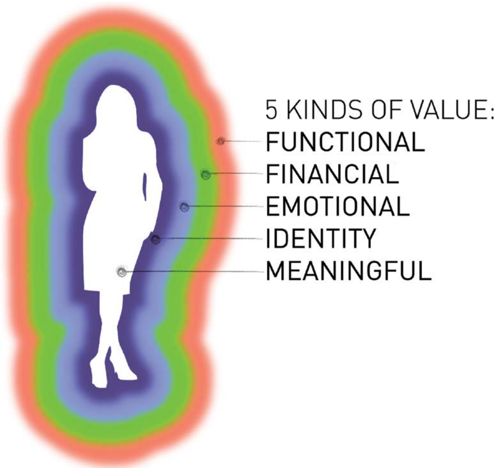
Unfortunately, most companies don't understand this tactic and don't invest in relationships, at least not in a continuous, strategic way. It's easy to understand why. Relationships are fuzzy, not easily measured, and they mean different things to different people. Marketers talk about them, but few businesses treat them as strategic assets. Walk into a boardroom, and you can get a long way talking about income statements, P&L, CapEx, and ROI. Talk about relationships, and few people want to listen, especially if the business isn't doing well. When challenged, there's not yet any way to point to the value of relationships in an organization's financials because the value is spread throughout *all* of the statements. It doesn't feel real, but it's encapsulated everywhere a company does business. Relationships don't seem real or concrete enough to act upon. They're seen as a byproduct of other activities, something that happens on their own as long as you take care of other things.

For most businesses, relationships are a major factor in building what's known as *premium value*. Premium value indicates how much more a customer would pay for one product or service over an equivalent replacement. A relationship-conscious company like Disney can charge much more per visit to its parks than Six Flags. Coke sells for more than generic soda. And Apple can charge much more than its rivals for products that do much the same thing.

You might think we're merely talking about one product being better than another. That's not the entire story, though, as good relationships start with products that work. But functionality is table stakes these days, and premium brands don't stress functional attributes. Almost any company can build products that do what they're supposed to do, or it can offer unique features that don't really matter. However, most companies have to compete on price, and relatively few understand how to create the kinds of experiences that build a durable relationship that customers value and that transcend price.

Five Types of Premium Value

Functional value is usually easy to quantify. Anytime a company stresses a particular feature of its offering (or how many there are), or the performance of the product or service as a whole, it is communicating about functional value. This is the first consideration customers usually make, and it's a great differentiator—unless some other company offers a slightly better feature or just one more. Functional value is usually easy to communicate, but it almost never engenders loyalty because it's the shallowest kind of value that can be provided to someone.



Financial value is the second kind, and it's a little more involved, creating a slightly deeper connection between a customer and a company (though not by much). When the number of choices is narrowed by various options, consumers turn to issues of money: how much are buyers really willing to spend for certain function or performance? Everyone has a different answer, which is why there are so many options for cars, computers, types of hand soap, and everything in between—at all price levels.

Because they're easy to measure quantitatively, both functional and financial values are pretty easy to see and understand. Either a product or service has the function a consumer wants or not. Either it's within a set budget or not. Most see the process of deciding what to buy or use as rational. These types of value, because they're quantifiable and, in a sense, visible—since they operate at a material level—are the least significant for consumers and provide the least sustainable source of differentiation for companies. They're about as basic as value gets, so buyers refer to them as, well…basic.

The other three forms of value are entirely different, however. This makes them complicated and difficult to work with. Ironically, these forms of value are just where the greatest opportunities to differentiate in the market reside. They're also the most important source of stock valuation. Havas Media, for instance, has determined that companies that consistently offer these types of value are, on average, valued significantly higher by the markets. Because of this, and because they offer so much greater benefits to customers, which leads to sustainable competitive advantage, these are thought of as the source of premium value.

The third kind of value is *emotional value*. Everyone acknowledges that emotions exist, yet some in business are still unable to see their impact on customer decisions. A "just-the-facts-ma'am" approach doesn't allow room for emotions to enter the equation. Yet, emotions are not only deeper in the relationships between customers and companies (and between individuals, too), but they're also very much a type of value that gets exchanged, even if they feel invisible. It's also easy to explain: consumers are willing to pay more for those experiences that provide them with the emotions they seek. That's all there is to it, but it flies in the face of traditionalists who insist that "people won't pay more for things than they have to."

Of course, every good salesperson knows that they're selling on the basis of emotions more than on price or performance. It's why consumers end up with a choice that's often over their budget or doesn't meet all of the functional needs they've specified. What drives decisions, in these cases, is that the choice makes the buyer feel greater, younger, happier, thinner, more accomplished, sexier—something. That's incredibly powerful and starts to explain the discrepancy between the book value of a company (the simple tally of its assets and liabilities) and its brand value (which is usually many times higher). This isn't a nefarious thing, by the way. We're usually after satisfaction more than features or price, in the first place.

Contrary to being irrational, emotions often aren't. You may not have realized you had a deep need to feel younger, more active, more successful, but if you respond positively to offerings that make you feel those things, that's a pretty rational response. The difference is that the decision drivers, at this stage, are no longer so easy to spot, can't be easily defined, and can't be easily measured quantitatively. Because they're not measured, often management is blind to them. The result is huge missed opportunities that are never even seen.

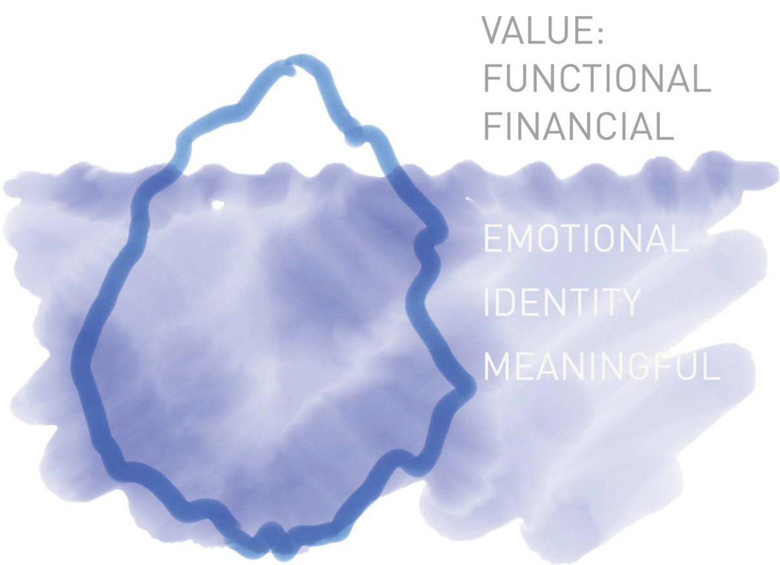
The fourth type of value is *identity value*, and this governs decisions in terms of what consumers feel fits who they are. Some people are Nike folks; others Adidas; still others identify with Puma or New Balance or Lululemon. Some come from cultural backgrounds that instruct them to only purchase brands that will advance their cultural communities or causes.

Even those who eschew brands react on this level. It may not be healthy to align a personal identity with brands—or construct self-images and identities from brands—but consumers do. They gravitate to things that complement who they feel they are and align with personal values. Like all premium types of value, this decision driver often acts unconsciously and, because humans don't change their sense of self often, it's even more powerful and stable than emotional value. For example, if you're a conservative, a liberal, an agnostic, a Canadian, a Yankee's fan, or a fanboy of anything (in short, anything you put after "I am a..."), this particular type of value lives in this space.

Whereas many business people recognize that identity value exists, they often manage it in a haphazard way because they can't easily quantitatively measure its importance, as they can with price and performance. Frequently, they hand off its management to the marketing and advertising folks, who are given at least a bit of a pass on justifying what they do on quantitative grounds. The attitude seems to be, "Well, we can't really measure this, but we know it matters, so let's just let the brand people do their thing and hope it pays off." The blind spot here is even more significant, and the lack of rigor in addressing it can be deeply disconcerting for anyone who has to answer for investment choices.

Finally, there's *meaningful value*, which transcends the other types of premium value in significance to customers. It is the deepest, most stable value that gets exchanged between people. In the past, it was mostly exchanged between individuals or between people and institutions like churches or government. Now, however, corporations and organizations of all types play this role in daily life. At this level, it's not so much about who you are but about how you see the world around you. This is governed by 15 core meanings (see Chapter 7, "Discovering," for an explanation of core meanings).

People's core meanings drive decisions about who they're friends with, what jobs they'll take, what they buy, and what they read, watch, and play. Whether you see the world as a scary, terrible, dangerous, wondrous, friendly, or hilarious place, that belief lives at this level and when you can surround yourself with people and things that reinforce this view, you're more satisfied and, as a consumer, willing to pay a lot more. Prius owners and survivalists, alike, are driven by different core meanings at this level.



Premium Value Is Real Value

While it's more difficult to measure and it's not a traditional business approach, premium value is very real and definitely valuable. If they make no place for it, business people are actively blinding themselves to the highest value there is in the market.

Not everyone pays more for premium value in everything they buy. Most have certain categories in which these types of value mean more to them—and some they couldn't care less about—for example, Porsche and Cartier, Hilton and Nike, Apple and Whole Foods.

These, of course, are generalizations. But some people care deeply about the food they eat; others just consider it food. Some give great care to the clothes, accessories, hair and makeup they put on; others eschew these for more generic choices. The point is that your customers engage on premium levels for many, but not all, things, and it's your job to understand which.

All of the above examples are evidence that premium value exists. It's often difficult to tease the five values apart, in the wild, since all five are active at all times (potentially). And all are part of what makes a relationship engaging, attractive, and valuable. No company that wowed investors with huge valuations on an IPO or sale did so on the basis of functional and financial value alone. In fact, for most companies, the more premium value you generate, the bigger the share it has of your overall value. If you're innovating to drive growth and value in a company, the best kind to focus on is premium value. And, you can't get there focusing only on features and price.

There are rare opportunities to "see" this value distinctly when a company goes public or is acquired by, or merges with, another. At these moments, the balance and income statements of a company are distinctly different before and after the sale. For example, when Instagram was purchased by Facebook in April 2012, the "books" said that

Instagram (then only 13 people) was worth around $86 million. This represented their total assets (including a $50 million investment the week prior to purchase).

The company was "valued" at $500 million before the sale, but this wasn't a real number, just a guess, based on past valuations of similar companies. According to the book, if the company had to shut down and sell everything off, it was only worth that $86 million.

But Facebook bought Instagram for $1.1 billion! That's a huge difference! Why did Facebook pay almost 13 times that $86 million figure? Where did that value exist in the company's financial statements? It was even double the amount that Instagram's investors guessed the company was worth.

We contend that the extra $1 billion that Instagram received in the sale *was* the result of the premium value it had built. Before the sale, this extra billion dollars didn't appear to exist and wasn't tracked, nor was it trackable. The day after the sale was final, however, that extra $1 billion was very real and had to be put into the balance sheet somewhere—and there's a special catch-all cell just for these things. It's called "goodwill" and it's a place to shove the extra money companies make when they're purchased or offer their IPO.

How could $1 billion go missing? Or how could it not be visible one day, but very visible the next? The majority of the business world will say that there are plenty of reasons why Facebook (and others) pay so much for companies like Instagram: it's a calculation of the value of future business, or how much it's worth to keep these companies out of their competitors' hands. But that doesn't answer why the numbers are often so high or how they're calculated.

To us, this is the value of the relationships that Instagram had created. (We also know from statements that Facebook had made that it was interested in Instagram's users and didn't want Google, Apple, or someone else to get them.) It certainly wasn't Instagram's code. Google could have likely put a team of engineers on the project and in a few months created a very similar set of features that were also free to users. That would have cost them much less for the "same" thing (if all you were looking at were the features).

This isn't just the case for software and other technology companies. When Pixar was acquired by Disney in 2006, it was "worth" just under $2 billion, according to the company books, but "earned" an extra $2.3 billion in goodwill (an extra 100%). Nextel was "worth" $5.3 billion when it was purchased in 2004, but "earned" an extra $30 billion in goodwill (that's almost 680%!). Every healthy company, in every category, has premium value, but no one knows just how much until events like these. It's hidden from view by traditional business measures and blind to those who practice it.

It's fair to say that premium value is the largest component of relationship value (which comprises all five types of value). There's no traditional way to measure relationship value (or its premium component), but it would be foolish to claim it didn't exist.

And yet, the first two kinds of value, functional and financial, because they're relatively easy to measure, get most of the serious attention in business. Sometimes, as in the nonprofit world, or even in some places in government, they're not as stressed, but they're very visible. The other forms of value, the premium types, are also there, but blind spots cause companies to ignore them in a business setting, hand them off to people not accountable for the bottom line, or treat them as mercurial or random.

Because they've been difficult to define, articulate, and measure, some companies, such as ad agencies, have a tendency to lump the types of premium value together and call them *emotional*, because they're all equally invisible—unlike basic value, they take place on the inside, in people's states of mind. Branding firms do the same thing, but lump it all under *brand* (and, unfortunately, never differentiate the components). Regardless, they're distinct and need to be approached differently if you hope to innovate in order to grow premium value.

There is also a lack of effective tools for measuring and understanding premium value's impact on relationships. It's not enough to know it's there. Most business owners don't know how to visualize and understand this value, let alone relationships—and, less still, how to innovate to improve them. For them, these types of relationship values are equally significant blind spots. Most leaders know intuitively that these relationships are important and valuable, but they fail to prioritize or act on them when making either strategic or tactical decisions. Relationships don't show up on the income statement or on the balance sheet after the fact (in owner's equity). They don't make an appearance in strategic discussions, even though their long-term effect on both should be obvious. In fact, neither revenue nor profit is sustainable without the foundation that relationships provide.

At this point, we can't fully solve the "naming, defining, measuring" problem of premium value entirely, although Nathan and Steve gave it a shot in the book *Making Meaning: How Successful Businesses Deliver Meaningful Customer Experiences* (New Riders, 2006). Although there has been some progress in developing metrics, these forms of value have a certain intangibility (they exist only the mind, after all!) that will probably always make them tougher to work with quantitatively than the other, more basic forms of value. However, whereas relationships can't be easily measured, they can, in fact, be worked with to provide superior value for customers, to build superior returns for investors, and to build enduring relationships between businesses and customers that benefit both hugely.

A New Approach

This book offers a solution for building and managing relationships like these, one that's been deployed successfully in a wide range of contexts. It involves tools and processes that help you accomplish a number of tasks:

- Understanding and visualizing your relationships with customers
- Identifying the best opportunities for innovation (and total value)
- Creating better relationships

With these new tools and processes, you'll be able to see when and where your customers are having the experiences that create great relationships—and the value that comes with them (and when they're not). You'll learn how those customers feel when they first encounter your products or services. You'll understand how they feel when they buy them or if they regret buying them at all. You'll understand their reactions to your customer service and ongoing attempts to stay in contact with them. You'll also have a complete picture of where you interact with people, what happens when you do, and why it matters.

Knowing all this is not merely important in theory. It also provides a strategic foundation for innovating to improve relationships and increasing value for your company. You can turn from being passive and reactive to proactive and helpful. You'll be able to prioritize opportunities for improvement. You'll know where to innovate and what to expect from your efforts. And you'll be able to evaluate your innovation program over time. In other words, you'll understand and know how to influence your relationships, moving them from your blind spot into plain view.

You'll also begin to see the impact that your entire organization has on these relationships. They don't live in product development, customer service, or in the store. They live everywhere, because they're reinforced (or decreased) by nearly every action the company takes. This new view of relationships will give you a way to strategically tie together the disparate pieces of your organization and focus them on the impact they can have on building long-term value. Too often, one part of the organization is countering the gains of another part *because* there's no way to tie them together. Our tools help illuminate these at a strategic level and show how everyone within the organization can contribute to successful relationships (and more value).

At the beginning of this chapter, Comcast was painted in a fairly negative light; however, this company is trying to become more conscious of building lasting relationships. For example, it is creating online tools that enable people to do more for themselves—and thus avoid its harried service reps. This may seem to be an admission of failure, but it's actually a promising sign. The company is innovating to improve an experience that it knows isn't great. This is our goal, as well: to describe relationships so that you can innovate to make them better.

This book is divided into two halves. The first half, (Chapters 1–4), describes what relationships are and how they are built. It also introduces a tool called a *waveline diagram*. It provides a visual representation of relationships, since a picture is worth a thousand words and many more dollars. The second half (Chapters 5–12) looks at an innovation process called *becoming by doing*. It is a holistic program that touches not only on how to create things that your customers want, but also how to manage relationships inside and outside your company.

Welcome to the new world of relationships. Hopefully, this book will take them out of your blind spot and enable you to understand the value that relationships create for your company. As brand loyalty has fallen and customers have become both more fickle and more savvy, it's time to start focusing on their real needs and consciously build a relationship with them.

EYE OPENERS

In this chapter, we've introduced a new definition of value in business (and design) and how it requires us to take a new approach to designing and developing much improved customer relationships. To recap what we've said:

- There are five kinds of value that get exchanged between people, and these are always potentials in any relationship: functional, financial, emotional, identity, and meaningful.
- The types of value that are easily measured quantitatively (functional and financial) are well understood and attended to in business because they are much easier to assess and plan for.
- The three types of value that are more elusive in nature (emotional, identity, and meaningful) are more difficult to measure and plan for, which is why they aren't typically a part of product development or customer relationship planning. This leads to missed opportunities to provide higher levels of value to customers.
- These more premium types of value often have a much bigger financial impact than the more basic types of value.
- Value can't be exchanged without a relationship of some kind, making the design of customer relationships central to the realization of any business value be they basic or premium.
- Relationships don't occur outside of some kind of experience, making the design of the customer experience, over time, central to long-term business value, as well.
- We need new, improved business tools to help develop better relationships and more premium value from these understandings, but it's already clear that traditional tools are inadequate in keeping businesses focused on premium value.