

HOW PRE-PURCHASE ALTERNATIVE EVALUATION PROCESSES AND CUSTOMER BEHAVIOUR FACTORS DETERMINE THE SELECTION OF AN ELECTRICITY SUPPLIER IN A DEREGULATED ENVIRONMENT FOR A LARGE USER OF ELECTRICITY IN AUSTRALIA

*Judy Rex, Swinburne University of Technology, PO Box 218, Hawthorn, 3122, Australia,
judyrex@hotmail.com, (61 3) 9214 8055*

ABSTRACT

Factors such as deregulation and the changing demands of customers have meant that businesses have had to change the way they operate, and to seek new ways to differentiate themselves from their competition. This is particularly the case in an industry such as electricity where there is no product differentiation on the core product. Using the results from pilot in-depth interviews, this study highlights some of the pre-purchase alternative evaluation factors that business users expect from their electricity supplier, and gives an insight into the decision making process for a business that is a heavy user of electricity.

INTRODUCTION

This paper seeks to establish the factors that underlie the pre-purchase evaluation factors that face business customers when making the choice between different electricity supply companies. It does this by examining theoretical and conceptual frameworks in the field of customer behaviour, and reporting the findings from a preliminary qualitative study of some of the issues facing a large user of electricity in the deregulated environment in Australia.

The steps undertaken by a customer before they actually make the decision to purchase a product or service are called the pre-purchase alternative evaluation stage of the process by some consumer behaviour theorists. The pre-purchase alternative evaluation stage is the 'process by which a choice alternative is evaluated and selected to meet consumer's needs' [8] and this stage of the consumer decision process model will be the focus of this paper. Most of the customer behaviour studies examined by the author focussed on households and individuals, and fewer studies were found about customer behaviour and decision making in the business context. One industry that provides an example to allow an examination of the pre-purchase alternative evaluation processes in the business context is the privatised and deregulated electricity industry in Victoria, Australia. The electricity industry is an interesting case study as Victoria was the first state in Australia and one of the first states in the world to privatise and deregulate its electricity industry.

The first section of this paper will outline the theoretical and conceptual frameworks related to the pre-purchase evaluation processes. Sheth [14] suggests that the decision making process for businesses (particularly large businesses) is usually more formalised and generally involves a greater level of structure than do decisions for households and individuals, and these processes and differences will be discussed. In order to gain a practical insight into the customer decision making process from a business perspective, the second section of the paper will report on the findings from pilot in-depth interviews. These interviews were conducted with decision-makers from a large Australian business that manufactures and retails a wide variety of products throughout Australia. This large business was chosen as they are a large user of electricity and they have been through the process of choosing their electricity suppliers on two occasions in the deregulated environment.

CUSTOMER BEHAVIOUR AND THE BUYER DECISION PROCESS

In today's increasingly competitive environment, businesses need to realise that 'The key to success is giving the customer what will meet his underlying needs better than the competitors' [11]. Businesses need to 'evolve with their customers over time' [9] and to do this they need to have a good understanding of how their customers behave. Customer behaviour is defined as 'the mental and physical activities undertaken by households and business customers that result in decisions and actions to pay for, purchase, and use products and services' [14]. Sheth [14] says that the key premises that underlie the differences in the decision processes between businesses and households include differences in the specialisation of the roles of the decision-makers; the formalisation of the processes they go through; and who is accountable for the ultimate decision. Further, even within different

kinds of businesses such as large and small businesses, differences will exist in the decision making process with respect to their internal capabilities and the complexity of their requirements [14].

DEVELOPING CHOICE CRITERIA

Understanding how consumers develop choice criteria involves understanding what alternative suppliers there are and what each one offers. Therefore, we need to consider the information that is available, understand the decision-making processes, and identify the attributes that are important in the final decision. Initially, customers will limit their information search to the best-known brands, and as customers become more aware of what is available they will develop a greater incentive to search for more information. Heilman [9] says that for first time buyers, the pre-purchase stage includes information consolidation that leads to a preference for the brands that provide the greatest 'utility'. *'People buy goods for what the goods can do for them'* [10]. Once a business has realised the need to use a product or service they will develop choice criteria to enable them to compare the alternative businesses and what each one has to offer [14]. In the electricity industry, the supply companies need to differentiate themselves because the product that is being offered (electricity) is intangible and the different suppliers are all offering the same product (electricity). Many businesses have begun to use the concept of unbundling to develop new and unique offerings. Unbundling occurs when 'the individual components of a provider's products and services are separated and made available to the user - either on their own or as a part of a re-bundled package for an additional fee to those businesses that want to pay extra for them' [12]. Which components the customer decides to pay for will vary according to the perceived benefit (or 'utility') that these unbundled (or re-bundled) products and services will give them.

A business needs to determine the importance of price in the final decision, however 'having the lowest price is not as important as having the price fall in the range that consumers expect to pay for the product' [6, p. 41]. Customers 'do the best they can for themselves' and if they are presented with a choice of 'bundles' and a 'given income', the customer will choose the bundle that 'maximises his or her satisfaction' (or utility) [2]. By maximising satisfaction, supply companies will have the added benefit of increasing the loyalty of their customers. Heilman [9] posits that customers will become loyal to the brand or business that provides them with the greatest utility. Therefore, in order to create loyalty, electricity supply companies need to unbundle their offerings, which will assist in creating utility to their customers. As customers become more experienced and knowledgeable about a market, as well as demanding more information they will also require more product options and a higher level of service from their supplier [4]. As well as knowledge, the customer's level of involvement in the process and the risk they perceive to be associated with the decision would also affect the decision making process. The two levels of involvement are high involvement and low involvement [1]. Customers who have a high involvement with a decision 'are more likely to pay attention to their advertising, to evaluate brands carefully, and to become more brand loyal' [1]. For electricity, it could be expected that customer involvement would be higher among customers that are reliant on electricity for their daily operations and for customers where the cost of electricity is a major expense for the business. For these businesses, the decision-making process would be considered to be a 'complex decision making process' [1] as the customer's involvement in the process is high and customers 'actively search for information to evaluate and consider alternative brands by applying specific criteria'.

Understanding customers' aversion to choosing an electricity company that is considered 'risky', also raises the notion that in some cases customers will behave 'rationally' and in others they will behave 'irrationally'. Schiffman [13] says that to behave rationally (in the economic sense), a customer would have to be 'aware of all the available product alternatives, be capable of correctly ranking each alternative in terms of its benefits and disadvantages, and be able to identify the one best alternative'. It is expected that customers with a higher involvement in the decision making process would be more likely to behave 'rationally' than customers who are less involved in the decision making process [1].

RESEARCH APPROACH

To explore the theory raised in this paper, it was decided to conduct a qualitative study using in-depth interviews. After reviewing the literature, a semi-structured preliminary discussion outline was drawn up, and two pilot in-depth interviews were conducted with two decision makers who work for one large user of electricity to test this discussion outline. Large electricity users were chosen as these users have had their electricity supply deregulated for about five years and as such, they are experienced in the processes of choosing a supply company. The two respondents had much experience in the decision making process as a result of choosing their electricity supplier on two separate occasions (since the advent of deregulation). They were both part of the strategic sourcing team for their company. This business was selected for the pilot in-depth interviews, as it owns many different kinds of

businesses that are involved in the manufacturing and retailing of products throughout Australia. As expected, the interviews with two of the main decision-makers provided a valuable insight into the processes involved. It is clearly understood that these interviews are not representative of the total market, however, the complexity and details obtained from the interviews provided an interesting case study to give an insight into the theoretical issues raised in this paper, and to provide a basis for further research. A summary of these interviews is described below.

CONCLUSIONS

Many of the findings from the pilot in-depth interviews were consistent with the literature. For the business interviewed, the decision-making processes they used were formal, as was the on-going process of evaluation for the period of the contract [14]. This business required little information to assist in the decision making process as they had a good understanding of market, and what was more important was what the supply company could offer them, and getting this for a 'fair price'. When they started their information search the business initially limited their search to the best-known companies which were considered to be low-risk [9]. When they were making their choice of an electricity supplier for the second time, the process was different as they had become more knowledgeable about the processes involved and they realised that the risk associated with choosing a supplier that was unknown to them was low. The second time, their consideration set also included companies from Interstate, which supported the findings of Heilman [9] who said that 'the latter stage that extends to lesser-known brands'.

Because of their high level of involvement in the decision making process this business behaved 'rationally' when they were making their decisions for both the first and the second contracts. When it came to the business' product and service needs for the second contract, the experience and knowledge they had gained from their first purchase decision meant that they required more unbundled products and a higher level of service from their supplier. Upon signing both contracts the business knew exactly what they needed, with 'a fair price' being at the top of the list. However, it was interesting that when making the final decision there was some leeway in terms of the importance of price. The business determined that if there was a price difference of about 4% or less between any of the companies then the attributes would have a greater importance than price. This is in accordance with the premise of Blackwell [6] that 'having the lowest price is not as important as having the price fall in the range that consumers expect to pay for the product'.

While this research is in no way conclusive, it does provide interesting benchmarks against which in-depth interviews with other industries and user groups can be compared. The findings from subsequent in-depth interviews will be used to design a quantitative study to enable statistical comparisons to be made to add new insights into the pre-purchase decision making processes for electricity suppliers among a representative sample of deregulated electricity users in Victoria, and elsewhere in the world.

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