Originally appeared in World Oil® DECEMBER 2019 issue, pg 48. Used with permission.

MANAGEMENT ISSUES

Busting the engineering trap: A better way for oil field service companies to retool their strategies

For OFS firms to prosper, two distinguished business professors suggest using a science-based approach to strategy, selecting the areas with the biggest impact on sales growth through customer value.

VIKAS MITTAL, Rice University and SHRIHARI SRIDHAR, Texas A&M University

Editor's note: The comments and opinions in this article are strictly those of the authors.

CEOs and boards of many oil field service companies—Baker Hughes, Halliburton, National Oilwell Varco (NOV), NexTier (C&J Energy Services and Keane Group combined) Schlumberger and Weatherford—are developing a "strategy playbook," of relentless reduction in fixed costs through headcount reduction, coupled with a focus on technology as a differentiator.

In NOV's Oct. 29 earnings call, CEO and President Clay Williams emphasized "cost-savings initiatives" and "proprietary opportunities to develop and sell digital enhancements" to equipment owners. In an Oct. 21 earnings call, Halliburton Chairman, CEO and President Jeff Miller stated that his company expected to "capture approximately $300 million in annualized cost-savings over the next few quarters" and introduce new technologies, improve margins, and lower the overall service delivery cost. NexTier reiterated its commitment to reducing its workforce, optimizing spend across key areas, and right-sizing the business.

On the one hand, a fear of persistently low crude prices had kept CEOs on their heels, preventing them from making much-needed investments—infrastructure, technology and human capital—that can fuel long-term growth. On the other hand, they hope to gain pricing power through technology-enhanced products. As an example, NexTier is "investing in innovation to deliver further improvements in efficiency and sustainability," while Halliburton is "deploying technology that lowers our cost and accrues value" to the company. Almost irrationally, the CEOs assume that technology-infused products and services not only lower their costs but also improve pricing power. The holy grail of margin expansion seems within reach!

In Halliburton's Oct. 21 earnings call, Miller summed up this exuberant view: "To maximize production per every capital expenditure dollar they spend, operators will require technologies that can improve both efficiencies and well productivity.…While customers are mostly focused on price today, early studies confirm our technologies work, they are hard to replicate, and will be more valuable to Halliburton over time."

Such an approach to strategy seems detached from reality. Despite senior leadership's claim of differentiated offerings, OFS companies—over the last few years—have continued to compete on price with dwindling margins.

The C-CUBES Customer Value Index (C-CVI) reveals a ground reality that differs from the hopes and fears of the companies' leadership. The C-CVI is based on over 8,000 customer evaluations of 110-plus major energy companies, including OFS companies.

A score of 100 on the C-CVI indicates that a company is delivering the highest level of customer value, and a score of zero indicates the lowest customer value. Oil field services are delivering the highest customer value on providing the *lowest* price (78), compared to providing a *competitive* price (75).

The leadership of OFS companies is caught in an engineering trap—believing that customers only value technology and product superiority. The energy sector C-CVI shows that 60% of customer value comes from non-technological factors, such as ongoing service and support, sales process, project management, and communication. Yet, boards and CEOs of OFS companies have doubled down on cost-cutting and efficiency measures while overspending on technology. They have laid off employees and eroded their enterprises' abilities to provide project management, ongoing service and support, and superior sales process—the real drivers of customer value. They have lost the human touch, disappointing customers, employees and shareholders.

For OFS companies to improve prosperity while supplying plays like the Eagle Ford shale, they need to retool their strategies. Image: ConocoPhillips.

A better way forward would start by reevaluating the strategic premise of the leadership team. That premise would not be based on technology and product superiority. Instead, using a science-based approach to strategy, it would select the few-but-relevant strategic areas with the biggest impact on sales growth through customer value. To do this, CEOs will need to shed their technology fetish and go back to basics—understand that most drivers of customer value build a strategy that motivates employees to deliver on those drivers. This would help increase margins by simultaneously growing revenue and reducing costs. WO

VIKAS MITTAL is the J. Hugh Liedtke Professor of Marketing at Rice University's Jones Graduate School of Business.

SHRIHARI SRIDHAR is the Joe Foster '56 Chair in Business Leadership and Professor of Marketing at Texas A&M University's Mays Business School.