

Partnering: Practical Problems and Conceptual Limits to Relationship Marketing

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Key words

Client Loyalty, Client Satisfaction, Partnering, Relationship Marketing, Repeat Business, Switching Cost

Abstract

Partnering has become an important way in which contractors sell and clients procure construction services. Partnering has been approached tactically, such as project partnering, and as a strategy to increase repeat business. This paper conceptualises the economics of partnering. It analyses from the perspective of the contractor the theoretical role of marketing in the management of the economic context. It also examines the aggregate effect upon the sector derived from the theoretical application. The analysis finds there are few incentives for clients to maintain partnering arrangements and agreements in the long term unless partnering is underpinned by a strategic management approach – relationship marketing for the contractor plus a corresponding investment and loyalty from the client. Implementation of relationship marketing requires a transformation of the structure of contractors.

The primary obstacle to sustaining partnering arrangements in the long run is switching costs. Switching costs are a theoretical component of transaction analysis and thus the traditional marketing mix approach. The primary theoretical question concerns increasing the switching costs of transaction analysis through relationship marketing. The practical issue concerns what strategies and actions contractors can adopt to sustain partnering.

In the sector, the adoption of relationship marketing for partnering will lead to increasing differentiation of construction services and hence greater diversity among contractors. Theoretically there will be a consequential increase of concentration and hence a reduction of competition.

Introduction

Partnering has become an extremely popular tool in recent years. Partnering has become a means to increase the levels of client satisfaction and secure a more stable workload than work available on the open market. A mutual benefit emerges for client and

contractor. Yet the primary focus of partnering has been on the *principles* and *exemplars*, from which “best practice” can be derived¹. This is because much of the drive towards partnering has come from clients². As a result, attention to the underlying concepts and theory has been neglected to a considerable degree. This lack of attention is entirely acceptable providing there is both confidence in and real reasons for assuming that partnering will work in the medium and long term. This paper looks at the underlying concepts, particularly *relationship marketing*, of which partnering is a tool. The analysis addresses whether partnering is sustainable. The analysis concludes that there is scope for partnering as practised, although there will be an increasing number of problems experienced in practice. These problems will arise from the way in which partnering is conducted.

The paper goes on to argue that partnering is not sustainable without the theoretical underpinning being applied in practice. Therefore, there are theoretical means to overcome these practical problems. Overall, it is argued that relationship marketing in general and partnering in particular are desperately needed by the industry to create a sector that is not only more economically sustainable, but is also a more vibrant, dynamic, innovative and enjoyable one to work in for the next century. This can only come about from substantial restructuring.

In order to explore this it is first necessary to locate current perceptions of partnering. There are two elements: the generic types of partnering in practice and the perspective from which the industry approaches partnering.

In practice, partnering is divided into three main types:

- ❑ *Strategic partnering*: long term alliances that continue across a series of project opportunities
- ❑ *Project partnering*: objective driven, tactical and short term in approach
- ❑ *Framework agreements*: a hybrid, which packages a series of projects having a known life span.

The main emphasis to date has been upon project partnering.

In conceptual terms, partnering has mainly been viewed from a procurement perspective. This is a consequence of partnering being driven by the client. Coupled with the emphasis upon project partnering, the focus has primarily been upon tactical project objectives. The greatest potential benefits for the contractor arise from strategic partnering. The significant outcome of the current focus is that the benefits largely accrue to the client. The prime benefits are:

- ❑ Continuing cost reductions
- ❑ Tailored service provision
- ❑ Client satisfaction
- ❑ Repeat business
- ❑ Improved turnover and profitability³.

It can be put this way: the first three benefits accrue to the client. Only two directly affect the “bottom line” of the contractor. Repeat business is the most significant contractor benefit because it holds the key to realising increased profit both in terms of the mass of profit accumulated and the margins achieved. In other words, current practice indicates that the theoretical benefits of partnering are not entirely mutual. The client is the main beneficiary. The answer is to increasingly move towards strategic partnering. The procurement issue is one to be addressed by clients. They will need to increasingly address it as the economies and levels of client satisfaction diminish if the lessons learnt and the benefits of a close working relationship on one project – the learning curve – cannot be carried across projects.

It is therefore necessary to look at the current procurement perspective and then relate this to a marketing perspective, particularly relationship marketing.

Procurement

The concept of partnering has been viewed as a procurement issue⁴. Bennett and Jayes⁵ produced some of the seminal work in the UK. They stated:

“The UK construction industry needs partnering in order to achieve tough targets set for it in the Latham Report.” (p. 2)

Therefore the focus is upon meeting client procurement objectives. However, it is not a simple procurement issue. Bennett and Jayes see the three key objectives of partnering as achieving *mutual objectives*, *problem resolution* and *continuous improvement*. They have broken *mutual objectives* down into a “management by objectives” type of approach, which is couched in terms of procurement:

“Partnering is widely found to help customers get their project teams to focus on their needs and objectives.” (p. 13)

The procurement theme continues through quality, cost efficiencies, speed and other largely project related issues. The contractor is required to act in a responsive way via the project team to the client. Such “best practice” in reality can end up as the contractor “bending over backwards” to meet the terms laid down by the client. This is the foundation of how partnering is being practised, the only benefit to the contractor being securing the sale. This may lead to an increase in market share. It will only lead to higher profitability where the premium margin outstrips the costs of meeting the increased demands of the client. In practice, this will seldom be realised where the contractor is competing on a project-by-project basis for partnering contracts.

How can this procurement behaviour partnering be understood? Campbell⁶ provides a matrix of buyer and seller relationships. The matrix locates procurement in its various forms. Campbell identifies three main strategies for buying and selling:

- *Competitive*
- *Co-operative*
- *Command.*

The *competitive strategy* is the classical market approach. If the client and contractor behave in a competitive way, then both are acting independently of each other resulting in a perfect market. This is the traditional position that has dominated contracting.

The *command strategy* can be adopted where either the supplier or the client has a dominant position in the market. They can employ leverage from their position to drive the terms of procurement in decisive ways. In contracting this oligopolistic or monopolistic position seldom arises. However, the economic cycles, coupled with the fragmentation of the industry, intensifies competition so that the client is in a commanding position.

The *co-operative strategy* is the one in which mutual advantage can be achieved. Relationship marketing, and its tool partnering, is to be seen as part of this. These three strategies exist on both sides of the exchange process – buying and selling. This locates procurement in relation to marketing.

Classification of Buyer-Seller Relationships

Client Purchasing Strategies

Competitive	Independent <i>Perfect Market</i>		Independent <i>Seller's Market</i>
Co-operative		Interdependent <i>Domesticated Market</i>	Dependent <i>Captive Market</i>
Command	Independent <i>Buyer's Market</i>	Dependent <i>Sub-contract Market</i>	
	Competitive	Co-operative	Command

Contractor Marketing Strategies

Source: Smyth, 1999 forthcoming, adapted from Campbell⁷

Partnering is about moving away from open competition. It is about moving towards a more *co-operative strategy*. However, this does not mean that the co-operation is balanced or equal. Partnering always requires a *co-operative strategy* on behalf of the contractor. The procurement emphasis means that the client is maintaining a commanding position.

The contractor may find they are subject to the client being dominant for several reasons:

1. Adoption of a project bias to procurement
2. Having an imbalance between the number of contracts and size of contracts in relation to the number of contractors being partnered
3. Having intensive tender competition among partners for contracts
4. Changing the ground rules of partnering
5. Low levels of investment in the partnering relationship
6. Being disloyal to contractors.

Under such circumstances the contractor becomes *dependent* upon the client, acting in essence as a *subcontractor*. It is understandable why many contractors may end up paying “lip service” to partnering as a means simply to secure work, and then, failing to carry through their promises or deliver the improvements. For mutual objectives to be achieved in a balanced way a *co-operative strategy* is required on both sides. Co-operation integrates marketing and procurement through partnering. Under these circumstances *interdependence* emerges between the parties, the contractor operating in a domesticated market. In other words, the clients receive a service which contains many of the benefits of an in house service. This comes without the costs of an in house service – full management responsibility and some of the risks of a complacent service – depending upon how agreements are structured.

The client may perceive that they are investing in the partnering relationship and therefore the onus is now on the contractor to likewise. It is true that any type of partnering involves investment on behalf of the client. Assuming that the client is making that investment, the investment and commitment on the contractor side is a marketing question. It is therefore necessary to look at relationship marketing and how partnering fits into it as one tool of the concept.

Relationship Marketing

Partnering is one tool of *relationship marketing*. Relationship marketing is a concept for developing long term and sustained contact with clients or customers so that their needs can be targeted and satisfied in return for client loyalty. The benefit for the supplier is repeat business or high levels of orders in referral markets. Developed by the Nordic School, the aim was to develop marketing concepts appropriate in business-to-business markets and especially in the service sector.

Relationship marketing can achieve this as it embodies strategies that inform not only the sales process, but also the entire contract delivery and management structure for a company⁸. Partnering is one means of building relationships. It is an important one in construction because of many of the features of contracting, including lumpy workload, extremes in the economic cycle, ownership and geographical fragmentation. Partnering provides continuity where the aforementioned features are divisive.

Therefore the theoretical return on investing in partnering for the contractor embraces greater work continuity, increased market share and improved profitability. The contractor needs to be assured of some combination of the above at a sufficient level to justify the investment in delivering the client benefits over the long run. If the benefits are not mutual, then the service will be developed to the limits of the potential benefit at best or below that level in order to squeeze out some marginal improvement to the balance sheet. To put this another way, if the client does not adopt a co-operative strategy nor will the contractor in the long run. There is a need for one party to take the lead, the other being expected to follow in good faith. To date the clients have driven this. Contractors have been cautious at best. At worst, contractors have failed to change

their attitudes and restructure their organisations to deliver partnering in a strategic way. Clients in turn need to demonstrate their long term commitment too. In such a way a mutual and balanced co-operative approach will emerge.

It has been conceptually demonstrated that partnering can be viewed from a marketing perspective as well as a procurement perspective. There are benefits for client and contractor from integrating the two perspectives, especially for partnering that spans over more than one project. The client receives continuous improvement, and repeat business is secured by the contractor. It has been asserted that the most appropriate marketing approach is relationship marketing. Indeed, one further conceptual step has been taken, which is that partnering is a tool of relationship marketing. This assertion has been made on the basis that relationship marketing has a focus on close customer and supplier relationships, which are developed over the long term. Repeat business is a key supplier objective with the ultimate aim of translating that into higher turnover and profitability.

In order to achieve these ends there is a requirement for the client to be satisfied. It also implies that client satisfaction gives rise to repeat business. The purpose of the next stage of analysis is to demonstrate that there are strong economic forces, which militate against a co-operative strategy.

Economic Forces

The marketing theory of relationship marketing has to confront the economic forces as experienced in any industrial or commercial sector into which it is introduced. These economic forces are particularly strong in construction sector in the way they impact upon marketing practice. This will be shown to be the case because of the structure of and recent historical experiences in the sector.

Working within the structural constraints and harnessing the economic forces requires the application of relationship marketing management strategies. The analysis will show the principles for applying such strategies. In so doing, the assertion that partnering needs to be underpinned by relationship marketing will be reinforced. It will further be shown that the lack of an automatic link between client satisfaction and repeat business can be overcome using relationship marketing. In doing this, relationship marketing becomes more than an advantageous support for partnering, it becomes a necessity. Without relationship marketing principles being applied, partnering cannot stand in the long term.

The economic forces at play are *transaction costs* (Williamson, 1981; 1985).

Transaction costs are the costs associated with the exchange process. When favourable supply and demand factors meet in the marketplace under neo-classical economic theory an exchange takes place. That exchange is not “free”. It carries its own costs for both parties. In construction the exchange process is particularly complicated. From pre-qualification, tendering, post tender negotiations, through stage payments, until the final account is settled are a whole host of administrative costs for the contractor and client which are incurred as overheads. Prior to the tender or contract negotiations there are costs for selecting a contractor, which starts with pre-qualification under traditional contracting. These are the transaction costs incurred by the client.

Strategic partnering reduces some of these costs for the client. The early stages of contractor selection have already been undertaken. The result may have been the selection of one partner or a small panel of contractors may have been selected to undertake all projects over a period of time. However, these savings are not very high in relation to the transaction costs of negotiating a contract or the tender procedures among the panel of partners for selection. Partnering does not therefore reduce many of the front-end transaction costs for the client.

Therefore the client cost of *switching* from one contractor to another may be very low, even where partnering arrangements are in place. These are called the *switching costs*. This comparison of client transaction costs between choosing one contractor and another may lead to considering switching contractors. The question a client may be addressing is; “Why should this organisation consider or appoint the same contractor?” Under traditional tendering procedure it would defeat the purpose of open or selective tendering to give any preference to a previous contractor other than consider them again at pre-qualification stage, if a reasonable level of satisfaction had been experienced on a past project. The previous contractor would then proceed on an equal basis of competition with the other pre-qualifying contractors. Campbell’s buyer-seller matrix (1995) has helped to point out how partnering is aimed at reducing competition. Partnering embodies co-operation. However, at the early stages of a contract there may be little or no financial incentive for the client to remain loyal to the partnering process, although there may be a legal obligation to remain loyal to the partnering arrangement. If the client is still operating a *command strategy*, as is frequently the case, the risks for the contractor of the client switching contractors is higher than where both parties are acting according to a *co-operative strategy*.

A *command strategy* ensures that the client remains *independent*. The initial investment on behalf of the contractor is low. The commitment and loyalty may be correspondingly low too. While there may be benefits that accrue to clients during each project, these are achieved by the contractor responding to client demands. It has been shown to be an unequal yoking between the parties and thus the investment made by the client in the relationship is negligible or substantially less than the investment on the contractor side. Therefore the *transaction costs* incurred by the client are low, indeed they will not be significantly higher than those costs on a traditional contract. The client retains their competitive procurement approach, the *switching costs* are low and thus there is high risk that a client will switch contractors. On the other hand *transaction costs* for the contractor are high, particularly from the pre-qualification stage onwards. It is understandable that a contractor may sense this in practice and thus keep their up front sales costs low, only paying “lip service” to the notion of partnering either at a strategic or project level.

A *co-operative strategy* requires more investment in the relationship. An informal agreement works because the parties have overcome the steep learning curve and continuous improvement is expected. When the initial transaction costs are high, the downstream benefits in terms of time, cost, quality and risks are theoretically increased.

After the initial high transaction costs, subsequent transaction costs are lower at the front-end of each project. A formal agreement has the added legal transaction costs. In both cases the *switching costs* are high for the client. Should the client decide to switch contractor, the benefits derived from the agreement cease and in the case of breaking a formal agreement there may be additional legal costs incurred. Because of the long-term nature of contracting and of the co-operative arrangement, the switching costs are low at the outset and grow as the partnering arrangements mature. In other words, the *interdependency* takes time to be established. A short-term view leads to a high risk that the partnering arrangement will fail because the client may decide to switch contractors. Thus contractors, perceiving the risks, will keep their costs low and make minimum investment in the relationship. A relationship marketing approach, however, demands higher levels of investment during the sales process.

Therefore economic factors exist which theoretically exert a powerful force on the exchange process. Specifically, the cost of switching from one contractor to another are marginal between traditional contracting and strategic or project partnering where a *command strategy* is adopted on the client side. The financial incentives to maintain a partnering agreement of the command type are negligible. A *co-operative strategy* offers greater opportunity, providing the contractor invests in the relationship.

In summary, risks are high at the early stages of an agreement, for the switching costs take some time to increase to a significant level. It takes time for the benefits of a client-contractor relationship to work through to yield high switching costs. There are few economic incentives for a client to remain loyal to a contractor, even where the client may have been very satisfied with prior services. Whilst this may be the general theoretical position, it is necessary to see how this may be specifically manifested in the sector as a whole for partnering agreements.

Switching Costs and Low Loyalty Levels

The client has to be given good reasons to loyal. The construction industry is currently structured in the market place so that the client incurs low switching costs. Theoretically this should not be the case. Switching costs should be inherently high. The schedule below highlights what could be expected to lead to high or low switching costs according to marketing and economic theory:

1. High Switching Costs
 - ❑ Differentiated product
 - ❑ Differentiated service
 - ❑ Complexity of transaction
 - ❑ Complex procurement route
 - ❑ Complex delivery channel
 - ❑ Frequent purchase
 - ❑ Direct contact
 - ❑ Co-operation

2. Low Switching Costs
 - ❑ Standard product
 - ❑ Standard service
 - ❑ Simplicity of transaction
 - ❑ Simple procurement route
 - ❑ Simple delivery channel
 - ❑ Infrequent purchase
 - ❑ Indirect contact
 - ❑ Independence.

Why has the theoretical expectation of high switching costs not been realised in practice?
There are several causes:

1. Design, hence product differentiation, conducted by others
2. Fragmented industry inducing intensive competition
3. Intensive competition inducing competition around price
4. Contractors encouraging price based competition
5. Lack of service differentiation
6. Lack of added value
7. Adversarial relations and contracts
8. Absence of conditions of trust
9. Absence of a marketing culture where staff are all part-time marketers or part-time sellers

Jackson⁹ states in the *Havard Business Review* that where switching costs are low, transaction marketing is appropriate. Relationship marketing, she says, is inappropriate. Partnering is a tool of relationship marketing. Therefore, the risk is that partnering will fail in the medium to long term should the appropriate strategy and measures not be in place. This applies not only to strategic partnering, but also to project partnering. In the case of project partnering, contractors who pay “lip service” to project partnering will not continue to deliver the client satisfaction and those that incur additional costs trying to do so in a price sensitive environment will cease to pursue project partnering. This will particularly be the case where and when workloads increase or in a slump when cost cutting comes to the fore.

This begins to pose questions as to what supporting *management* measures are needed in order to address these issues¹⁰. Where are the areas to which management can look to increase switching costs? Some of the options are listed below:

- ❑ *Compatibility* in terms of cultural and market orientation
- ❑ Service differentiation
- ❑ Gearing up to *deliver* what can be or has been promised
- ❑ Able to *discharge* the delivery of the building with competitive advantage
- ❑ Able to realise a *premium profit* from more effective operations and management responsiveness
- ❑ *Clear oversight* from senior management of each partner

- ❑ *Regular client contact from senior management* between projects at a corresponding management levels and at the level of those responsible for projects
- ❑ *Increase of client contact from senior management* when client expectations are highest, frequently in the latter stages of a project
- ❑ Continuity of contract and site personnel *at the expense of opportunistic tendering.*

How these aspects are implemented is a matter of competitive advantage. The level of investment must be ahead of the competition in the market, which itself is embodied in *differentiation* above. These aspects must be considered as pointers. For a deeper insight into relationship marketing in construction, there are other key sources becoming available¹¹.

To recap, *partnering* will not in practice overcome the power of low switching costs. A more comprehensive strategy is needed. As partnering is a tool of relationship marketing is it this theoretical approach that offers a practical means to create the opportunity for long term sustainable change in the construction sector.

At this point, assume implementation of relationship marketing is successful at a company level and is carried over a significant number of leading contractors in the marketplace. Then, the primary question that emerges is: Will the adoption of a relationship marketing approach change the structural environment and overcome the economic processes which give rise to low switching costs?

The Impact of Increases in Switching Costs within the Sector upon Market Structure

Adopting relationship marketing for partnering will change the operations and management of a number of companies. This will begin to differentiate the services of leading contractors in the sector. Competition is therefore being reduced:

- ❑ Between the partnering (co-operative) market and traditional (competitive) market
- ❑ Between contractors offering more highly differentiated services *within* the partnering market.

Contractors who are successful in sustaining partnering market share will experience improved turnover and profitability. This will provide further opportunities to expand or take-over other companies. This will lead to:

1. Ownership being concentrated in fewer hands
2. Higher switching costs and thus a reduction of competition on price, especially within the partnering market.

Therefore the knock on effect of structural changes within companies can begin to change the structure of the entire market. This will not be to the detriment of clients. The reverse will prevail. Clients will benefit from:

- ❑ Continuous cost reductions from partnering
- ❑ Construction services which are more closely tailored to individual client needs
- ❑ Potentially a more responsive and dynamic sector should some of the stability and financial rewards become channelled into innovation and service improvements.

This is a win-win situation. It would normally be expected that improved market leverage amongst contractors would have the economic impact of reducing client satisfaction. The reverse is the case in this situation because the overall climate of price domination has seriously weakened contractors at a time when the market is more demanding. Contractors have become increasingly anorexic¹². Relationship marketing in general and partnering specifically are measures that intervene in the market that are not primarily economically driven, yet begin to directly affect the economics of the market and hence overcome the economic forces at work. It is a process of market management.

Conclusion

The above analysis demonstrates that there are good reasons why clients may seek to switch contractors. Partnering in itself, especially if conducted from a predominantly procurement perspective, will not overcome these switching costs. Remedies are required to increase interdependency between client and contractor. These remedies provide incentives to remain loyal. In other words, partnering offers a means to overcome low switching costs, providing relationship marketing practices are strategically and tactically implemented. Such measures raise the economic barriers in the market by increasing switching costs. This requires investment by both client and contractor, one party leading the way, and the other being required to follow behind swiftly. The starting point is to complement the current procurement with a marketing approach to partnering. It is from this that the management systems should flow. This investment begins to change the approach and structure of contracting organisations. This is absolutely necessary for partnering to survive because otherwise the low transaction costs of switching contractors will overpower the partnering approach.

A further and important conclusion is that structural change in the contracting organisation may invoke structural change in the market. In other words permanent barriers to switching could begin to be erected. This will occur as:

1. Sufficient contractors successfully follow the partnering route
2. Contractors differentiate their services
3. Competition is reduced through fewer contractors operating in the market.

The paper has conceptualised the theoretical underpinnings to partnering. The antidote to a procurement bias is the complimentary marketing approach. The economics of repeat business can be improved through partnering where the negative impact of low switching costs has been addressed. A co-operative strategy, resulting in greater interdependence between contractor and client is induced by investment on both sides. This helps to manage the market to mutual benefit for both parties.

Furthermore, the widespread implementation of such measures has an economic impact across the whole sector, inducing a win-win situation. The relationship marketing helps to overcome the low price, low value approach and induce a healthier sector economically that is more able to pursue continuous improvement for clients through service differentiation and added service value.

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¹ For example, see *see 7 pillars*

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