

# **The Loyalty Connection: Secrets To Customer Retention And Increased Profits**

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## Executive Summary

Customer churn rates are higher than ever, and businesses haven't figured out how to stop the bleeding. New CRMGuru research points to the cause: Although businesses say they are devoted to loyalty, their management systems and budgets don't back that up.

Loyalty experts agree it is more cost effective to retain customers than to acquire them, but, based on numerous interviews and two surveys, CRMGuru found that few companies have strong programs in place. And those that do may be focusing on the wrong things. From a recent CRMGuru survey, we learned that even though more than 70 percent of customers say poor service caused them to take their business elsewhere, business managers believe price to be a prime factor for defection.

In a landscape of similar products and global competition, cutting down on defection—or churn—and building loyalty can be a significant way to grow your business. For example, churn rates for mobile telecommunications companies in Great Britain average between 25 percent and 35 percent, according to Customer Value Management expert Graham Hill. At the low end is Virgin Mobile, with about 14 percent of its customers leaving annually. At the high end is T-Mobile, with a 34.8 percent churn rate. Hill says the cost to replace these departing customers is €122 million or about \$162.3 million.

Most business leaders believe in loyalty. The CRMGuru survey found that nearly 80 percent felt that loyalty was either “extremely important” or “very important” to top management. Unfortunately, they may be investing their money in the wrong areas. CRMGuru survey respondents prioritized investments in new customer acquisition (40 percent) much higher than customer retention (22 percent).

In this white paper, I will review why customer loyalty is so crucial to business success. But more importantly, I will discuss four steps to improve loyalty and retention which, if focused on appropriate customers, will improve profitability.

1. Understand drivers of loyalty and defection, from the customers' point of view.
2. Develop a loyalty strategy focused on the “right” customers.
3. Systematically deliver what your customers value, and fix it quickly when you don't.
4. Implement measurement and reward systems to encourage customer-centric behavior.

Following these steps will make your organization more customer-centric—what Customer Relationship Management (CRM) should be about. And it will enable your business to grow faster and earn more money. And that's the business benefit that CRM should deliver.

The relationship between customer loyalty and profitable growth has been proven by industry leaders. Read on and learn how to lead *your* industry.

## The Value of Loyalty Leadership

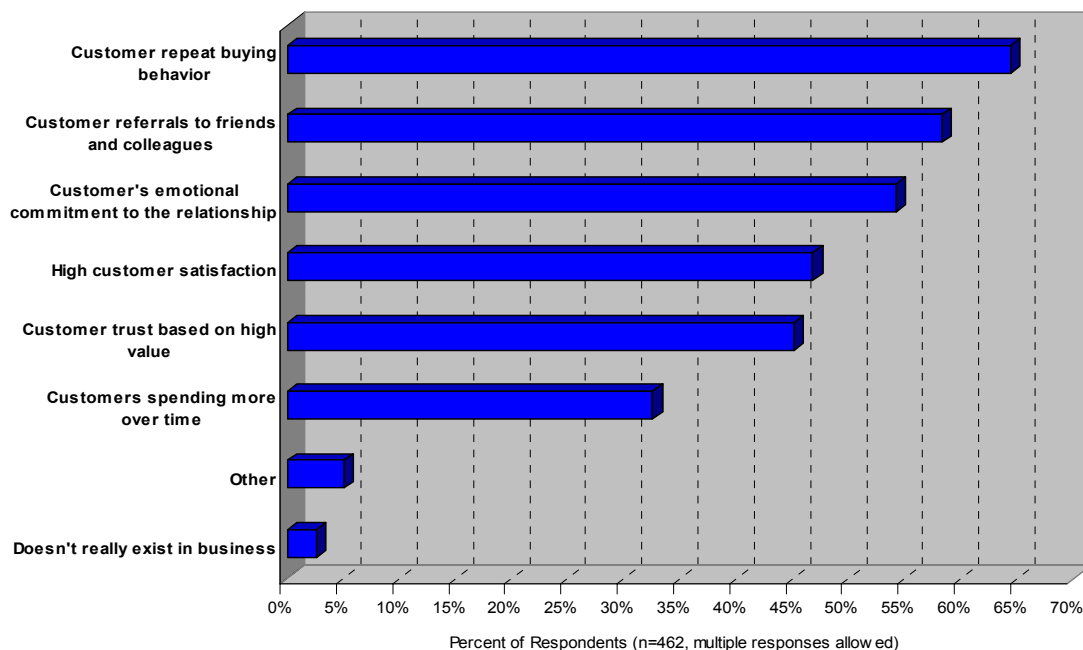
Loyalty experts generally agree that loyal customers stick around longer and buy more frequently. This *behavior* is driven by the customers' *attitude* that they really want to continue to do business with the company. As a result, loyalty leaders enjoy a substantial advantage in revenue growth and profitability.

### What Is Loyalty?

In some cases, customers continue to do business because they have no other alternatives or exit barriers are too high. It's important not to confuse these "trapped" customers, as defined by loyalty research firm Walker Information, with "truly loyal" customers, who have a positive attitude about the business relationship and will give recommendations to friends and colleagues. Think "free marketing."

Business leaders do seem to grasp the concept. In a December 2004 CRMGuru survey, 64 percent defined loyalty as repeat buying behavior; 58 percent as a customer who makes referrals to friends and colleagues and 54 percent as a customer's emotional commitment to the relationship. Only 32 percent of the respondents defined loyalty as a customer spending more over time.

What Is Customer Loyalty?



### The Gift That Keeps on Giving

The "loyalty effect," as described by loyalty guru Frederick Reichheld, is a powerful profit generator because loyal customers tend to spend more, refer others and cost less to serve. Reichheld, author of *The Loyalty Effect* and *Loyalty Rules*, found that loyalty leaders grow, on average, more than twice as fast as the industry average across a wide variety of industries. In a recent study, Walker Information found that IT industry leaders outperform "laggards." A survey of more than 4,000 people in September 2004 found that IT vendors with high customer loyalty generated an average operating margin of 12 percent, while laggards experienced a *negative* 11 percent margin.

According to Jeff Marr, the firm's vice president and senior consultant on the study, Walker Information developed an index that combined the customer's actual experience with the customer's intent to stay

with a particular company. Walker Information looked at the degree to which the suppliers met the customers' expectations; whether the customer planned on continuing the relationship; and how large a share of "wallet" the customer was willing to give the company. The resulting index allowed Walker to classify the "true loyalty" of a customer, which had a strong correlation with the companies' financial performance.

Over the past decade, the American Customer Satisfaction Index (ACSI), an organization supported in part by the University of Michigan Business School, has emerged as a valuable source of consumer insight. The ACSI model links customer expectations, perceived quality and perceived value to an overall score, which, in turn, is linked to consequences such as customer complaints and loyalty. ACSI leaders—those in the top 50 percent in ACSI rankings—have been able to build market value more rapidly over the past decade. A case in point is Southwest Airlines, which has made more profit and created more market (stock) value over the past decade than the rest of the airline industry combined.

Finally, Reichheld's research and that of loyalty consultants Jill Griffin and Michael Lowenstein has demonstrated that keeping existing customers costs substantially less to a company than acquiring new ones. In *Customer Winback: How To Recapture Lost Customers—And Keep Them Loyal.*, Griffin and Lowenstein cite a 2002 Marketing Metrics study, which found that the average company has a 60 percent to 70 percent probability of a success sale to active customers; a 20 percent to 40 percent probability of a sale to lost customers; and only a 5 percent to 20 percent probability of a sale to prospects.

### Making the Business Case

These examples show that becoming a loyalty leader doesn't happen overnight. How, then, are investments justified in this area? In CRMGuru's December 2004 survey, loyalty leaders—those whose executives rated their loyalty programs as "excellent"—justified loyalty programs with expected improvements in profitability, revenue growth and customer base expansion. It might be surprising to learn that improving products and services was also popular, selected by 39 percent of leaders.

#### Top 5 Methods Leaders Use To Justify Customer Loyalty Programs

Justification Approach	"Leaders" Pct. Selecting	All Others Pct. Selecting	Comments
1. Increasing total profitability	54%	45%	Leaders are more focused on profit, not just revenue growth.
2. Increasing profitability per customer/segment	46%	33%	Leaders dig deeper into segments to optimize profitability.
3. Increasing total company revenues	46%	43%	At same marketing cost, a company with lower attrition rate grows faster.
4. Increasing total numbers of customers	39%	35%	Loyal customers refer others—and reduce marketing costs.
5. Improving products and services	39%	37%	Loyal customers give more feedback!

Source: CRMGuru Survey, December 2004, 462 Respondents

## Drivers of Loyalty and Defection

In customer loyalty, there's no substitute for good research and planning. No matter the size or type of your business, you must start by understanding why customers stay and why they leave. Taking this customer-centric view will enlighten your management on why customers behave the way they do so that you can create a profit-generating loyalty strategy.

It is, of course, possible to acquire and retain unprofitable customers. Some companies make this mistake by constantly acquiring new customers with price promotions and then wondering why these same customers flit to the next deal offered by a competitor. The resulting high-churn, low-margin customer base is unlikely to ever be profitable. Keeping the *right* customers is crucial to effective CRM.

### Analyze This

Larger companies, generally with thousands to millions of customers, should take this approach further and apply analytical tools and statistical techniques to uncover the true “drivers” of customer loyalty—the factors that have a strong correlation with loyal attitudes and behavior.

In the IT industry, for example, Walker Information found that loyal customers were primarily driven by:

- Attitudes—about brand, quality and customer focus
- Brand Images—as an industry leader, trustworthy company and innovative supplier
- Customer Experiences—with product quality, purchase process, technical support and consulting

The Walker study also found that “price contributes to how customers view the value of what they buy,” but “price by itself doesn't contribute a great deal to customer loyalty.”

### It's the Service

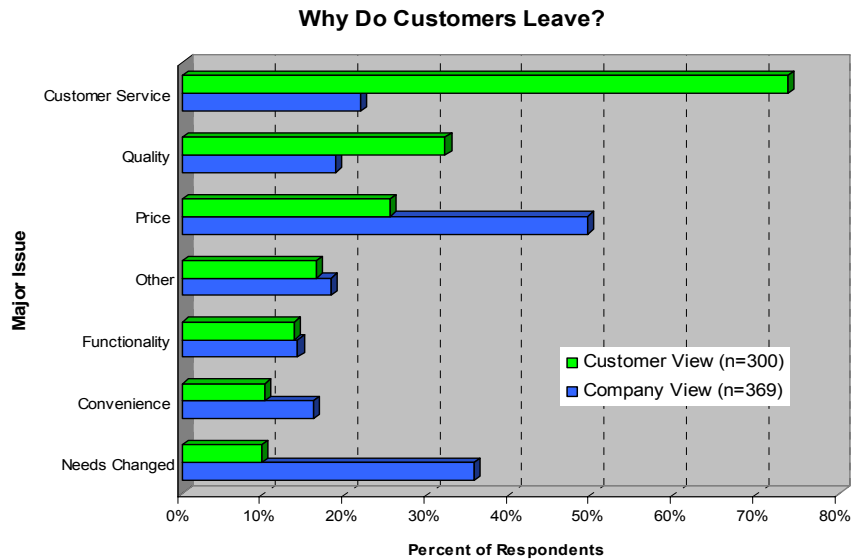
Monopolies aside, the odds are that today's customers can acquire similar products at similar prices, from an array of local and global suppliers. Loyalty experts say that emotion plays a much higher role than quality and price in the decision to defect. And poor customer service is the most likely culprit in creating negative feelings that will motivate a customer to bolt.

“Most people leave a company because they feel they're not treated well,” according to Arthur Hughes, author of *The Customer Loyalty Solution*. “They feel that, for some reason, they have been ignored or not treated properly. Management usually thinks the reason for leaving is price, and of course, that's true in some cases. But it's usually because they feel that they've been neglected or somehow abused,” Hughes said. “They write a letter, and no one answers the letter. They send an email, and no one answers the email. They telephone the company, and they're put on hold for two hours.”

A CRMGuru survey in November 2004 bears that out. Of the respondents who said they had stopped using a product or service, 74 percent blamed customer service as a major factor in their decision. The second-most frequently cited problem—poor quality—was selected by 32 percent of respondents, and 25 percent said they defected because of price issues. The functionality of the product/service was selected as a major factor by only 14 percent of respondents.

## Mind the Perception Gap

Unfortunately, CRMGuru research also revealed that business managers may be deluding themselves about why customers defect. As you can see from the following chart, managers are out of sync with customers: Price was viewed as the primary reason customers leave, selected by 49 percent of respondents, followed by “needs changed” at 36 percent and “customer service” at 22 percent.



While every business is different, this study suggests that executives should check their assumptions and invest in research to understand the real reasons that customers leave or stay. It’s human nature to find blame elsewhere. “If only our company had better pricing, the customer wouldn’t have left.” Or, “It’s not our fault the customer’s needs changed.” Or, “Too bad our product wasn’t competitive.” Dig deeper for the real reasons.

## Survey Customers and Use Analytics

Discovering the problem can be tricky, and here’s where surveys can help. But you can’t always survey customers, and even if you do, it may be too late.

A company that sold prepaid cellular phones had an attrition rate of 12 percent per month, which meant it was churning its entire customer base in the course of a year. Executives couldn’t figure out what to do. A survey was out of the question, because the only contact information they had for the customers was their phone numbers. They didn’t want to telephone the customers for fear that the call—which would be on the customers’ dime—would only irritate them.

So they turned to marketing analytics—a type of modeling—which found a correlation between the sales channel and the defectors. Those who bought their phones at mass marketers hadn’t been shown how to replace their phone cards when they expired. So when the phones stopped working, they stopped using the phones. Armed with that knowledge, the company began working through its mass-market channel to educate those customers and make it easier for them to purchase replacement cards. The company saw a 65 percent drop in the attrition rate.

That’s a dramatic example, according to marketing analytics consultant Naras Eechambadi, CEO and founder of Quaero, in Charlotte, North Carolina, of how a business can founder until its leaders have the

full story of why customers choose to continue using a product or service—and why they leave for the competition. Marketing analytics can give you an accurate picture of your customer base. The technology typically allows you to plug in numbers and parse out the past, present and future value of your customers. The investment is generally cost-effective for medium to large businesses.

### Start Small

Companies of all sizes can implement a loyalty program. Small business CRM guru Jay Curry of Jay Curry Associates advocates conducting customer interviews with top customers to get feedback on the relationship. Interviews can be conducted in person, for high-value customers; via telephone or web for medium-size customers; or direct mail, for small customers likely to remain so.

Regardless of the method, these interviews and surveys can provide useful information on the following subjects, says Curry:

- Satisfaction levels
- Products/services they don't know about
- Competitors on site
- Future spending plans in your category
- How you can get more of that spend
- Internal politics

Managers can then make decisions about changes in product/service offerings, pricing or post-sales customer service. Issues that surface can be addressed before the customer reaches the boiling point. What this approach may lack in statistical rigor, it makes up for in a more personal approach that can generate a positive frame of mind with the customer. Just asking for feedback is, itself, a loyalty-generating process, provided that the company is committed to act on what it has learned.

### The Last Straw

In 83 percent of the cases, respondents of the CRMGuru survey on defection said there was a “triggering event” that caused them to sever the business relationship. Write-in responses indicated the role that emotion played. In one case, a survey respondent said the company lost out to the competition when it held an event intended to *reward* loyal customers. The event was poorly planned, and the attendees were not taken care of. In another case, the respondent said, “Everyone in the store ignored me, never acknowledged me. Finally, when I approached a sales representative, my question was responded to flippantly, as if I were stupid for even asking.”

Alan Piesse, a marketing consultant who specializes in customer retention in telecommunications, had a contract with a landline telephone company trying to stem its tide of unhappy customers. The lack of customer retention, Piesse said, was caused by poor ongoing customer management. “Of those customers defecting, 43 percent quoted poor customer management as the reason.” In particular, Piesse said, the company exploited high contract prices after the end of a contract while the market rate dropped. It wasn't so much the high rate as it was the inequity that irritated the customers. “As soon as the customers found they were paying ‘over the odds,’ they immediately switched to another supplier; 30 percent of this business's revenue was disappearing each year because they didn't treat customers ‘fairly.’”

### Predicting Churn

It's not easy for a business to predict churn. “Only a small percentage of customers will complain,” writes Griffin in *Customer Loyalty*. “A typical business hears from only four percent of its dissatisfied



customers. The remaining 96 percent go away, and on average, 91 percent never go back.” Yet, you can track customers’ actions. After four years of research on the best practices of about 200 companies for Customer Loyalty, Griffin was able to put together the following list of six indicators that a customer was ready to walk out the door for good:

- Customer approval of your proposals comes slower.
- Access to upper-level management decreases.
- The flow of customer data slows down.
- Plans for future work become progressively shorter-term.
- One or more of your products or services are discontinued.
- The volume of business the customer is doing with you is reduced.

Some indicators, such as customer approval of proposals and access to upper-level management, are related more to the business-to-business market than the business-to-consumer market. However, even consumer businesses can note if the level of business is reduced. Certain industries, where companies keep activity logs—such as telecommunications, pay television and Internet service—are in a good position to note when activity drops off and take action before a defection occurs.

In an interview with CRMGuru, Lowenstein cited the case of a German book club that spent a year comparing its efforts to re-establish a relationship with past customers and its efforts to woo new prospects. The company looked at the returning customers’ “spend,” profitability, use of customer service and amount of returns vs. that of new customers. It found \$10 in revenue and profit for the former customers compared to \$1 for the best of the prospects it was able to convert: a 10-to-1 difference in cost. “The reality is there are limited numbers of good customers out there for any company,” Lowenstein said.

If you understand loyalty and haven’t “operationalized” it, you’ve got a lot of company. Relatively few businesses practice any type of retention program and even fewer, win-back, according to Griffin and Lowenstein. Leaders at the average company don’t “recognize the huge potential that’s sitting in their lost customer base,” Griffin said. “Either they don’t recognize it, or it’s a political hot potato and nobody wants to go there.”

### **The More Things Change...**

CRMGuru’s research confirmed the findings of other studies that identified customer service as the top issue in loyalty. In *Excelling in the 1990s: CEO Perspectives*, R.P. Cooley found that 68 percent of the reasons customers defected were related to service problems, often just a feeling of being treated with indifference.

Customers have many options in today’s market. If the way your business interacts with your customers is a problem, it may be all the incentive they need to look elsewhere. Why give them an excuse?

## How To Retain or Win Back Customers

In CRMGuru's survey of customers who had defected, 83 percent of the respondents said an event "triggered" their decision to go to the competition. Often, the customers had been with a company for a long time when they stopped doing business.

Even so, the "last straw" from the customer's perspective isn't always obvious to the business. In numerous cases, CRMGuru survey respondents cited a failure of customer service representatives to treat them politely or a transaction handled in error that led to their ceasing business. But it's not clear from the customers' descriptions that the defection was even noticed by the business. In fact, 91 percent never heard anything from the business about their departures, and only 26 percent reported that the business tried to save the relationship before they left for good.

Loyalty experts say that retaining the right customers or winning back defecting customers can be accomplished by following these steps:

- Identify potential defectors.
- Communicate with customers.
- Listen to front-line people.
- Treat valuable customers well.
- Be fair, even when you don't have to.
- Use exit barriers, carefully.
- Win the right customers back.

### Identify Potential Defectors

If you have records, use them to take a quick pulse of your customer base, suggests Hughes, who works in database marketing. Credit card companies, for example, can simply monitor the level of customer activity. If it's dropping off, there's a good chance the customer will give up the card when renewal comes around. Similarly, with a cell phone, you can gauge how much the customer is using your service. You also should note how old—and obsolete—the phone is.

Just as emotion plays a key role in customers' decision to stop patronizing a business, emotion can be used to keep customers from leaving, loyalty experts say. "Even the very basic act of re-communicating with these people, without any kind of formal program, gets you tremendous returns," Lowenstein says. "In other words, people do want to be engaged, not only on a functional or rational level, but they want to know that you care, and they want to hear from you."

### Communicate With Customers

Hughes says he has found that communication, by phone, email, direct mail or, if need be, in person, can keep a customer on the verge of defection from leaving. The human touch goes a long way. When he consulted for BMW, Hughes implemented a regular series of contacts throughout the year, beginning with a welcome kit and including a magazine. With a car buyer, you can concentrate your efforts on the end of the lease period, typically three years, and promote the new features that will be available.

According to Hughes, Travelers Insurance, one of the largest providers of personal insurance in the United States, found that if agents telephoned customers every year to review their policies, the customers were less likely to cancel those policies. "The fact that someone called them up and talked about it is going to encourage them to stay." Hughes said it was easy to prove the effect of that simple

communication just by monitoring those customers who weren't called. Travelers, Hughes said, also trades on emotion to keep customers from even contemplating defecting, by sending cards at birthdays and other holidays.

**Listen to Front-Line Staff**

David Rance, managing director of U.K.-based Round, which develops tools to help businesses improve their customer-centricity and lower operating costs, advocates talking to your customer service people. "Customer service is the organizational drip-tray into which fall all the inconsistencies, contradictions, errors, omissions and downright stupid things that companies do to their customers." Service people are the first ones to hear what bothers customers.

He cites as an example the approach introduced to Amazon.com by Bill Price, its first vice president of global customer service. Every customer contact was coded, and the codes flagged the most were investigated to identify the root cause of the call. The cost for servicing those calls was then charged back to that department. "You can be sure that the offending department worked closely with customer service to eliminate those calls as quickly as possible," Rance said.

**Treat Valuable Customers Well**

Lowenstein recommends surveying customers to find out what they like about your company and to find out how they feel about your product vs. that of the competition. If the survey shows that the customer is merely moving from transaction to transaction, the customer's level of commitment is low and the odds of defection are high.

When you're determining how to retain customers, you also want to determine *which* customers to focus on: Which ones are the most valuable for your business and would be the most costly to lose?

Hughes suggests using a risk/revenue matrix to determine which customers businesses should care about most. You first must perform two steps: 1) Determine the lifetime value of your customers and divide them into high, medium and low lifetime value segments, then 2) Determine the likelihood that they will leave you and divide the customers into three defection classes.

**Risk/Revenue Matrix**

**Probability of Leaving Soon**

	High	Medium	Low	
Life-Time Value	High	priority A	priority B	priority C
	Medium	priority B	priority B	priority C
	Low	priority C	priority C	priority C

Source: Arthur Middleton Hughes, *The Customer Loyalty Solution*

Assuming all your segments are about the same size, you should have 44 percent of yours customers in priorities A and B. "The only ones you should care about are the four most important boxes, which I call priorities A and B," Hughes said. Regardless of lifetime value, those who are most likely to stay with you

are considered priority C customers. Those with the highest lifetime value and the highest probability of defecting are your priority A customers.

“Priority C, which is the low lifetime value—or very loyal ones that are never going to leave you—those, you don’t need to spend a lot of money on,” Hughes says. Once you’ve identified those customers you most want to retain, you can do something as simple as making sure those customers are bumped to the head of the line in your contact center—or have a dedicated phone number to call.

### **Be Fair, Even When You Don’t Have To**

Piesse believes that equity plays a tremendous role in building customer loyalty. In the mobile telecom industry, he found customer churn in a particular segment to be caused largely by customers who were courted with aggressively priced deals. “These customers defected either because they were ‘promiscuous’ and sought the best new deal each year, or the package they were sold was inappropriate,” Piesse said. “Customers who stayed were those who were on the right tariff and believed they were. Once we took the step of offering to put customers onto the best available tariff, retention among high-value customers increased dramatically.

“The big surprise was that most customers did not change their tariff but stayed on their old one, and still their retention rate soared,” he said. “So when we treated customers fairly, we got a large increase in retention with ultimately very little cost and a big increase in margin.”

“The conventional wisdom today in progressive companies is that a customer complaint represents an opportunity to set things right,” writes Jim Barnes in *Secrets of Customer Relationship Management*. “Unless customers are encouraged to complain, management is often unaware that there are difficulties in the relationship. “Complaints that are resolved quickly and to the customer’s satisfaction often result in higher levels of customer loyalty,” Barnes says.

### **Use Exit Barriers, Carefully**

One way to give your business a chance to respond is to make it difficult for your customers to leave. In *Customer Winback*, Griffin and Lowenstein recommend erecting a simple barrier to departure, such as a requirement that a customer turn in a formal notice before ending the relationship, so you have an opportunity to find out what’s wrong and fix it *before the customer leaves*.

At the same time, Griffin and Lowenstein write, you must empower your customer service representatives to take care of the problem quickly and efficiently. They must be skillful enough to allow the customer, who is most likely angry, to blow off steam: “Don’t interrupt. Don’t argue. Just listen for a while,” advise Griffin and Lowenstein. “Such statements as, ‘I’m sorry you’ve had problems; please tell me the circumstances, so I can help you,’ will encourage the customer to explain and, in doing so, cool off a bit.”

### **Win the Right Customers Back**

Despite your best efforts, some customers will still leave. How can you get them back? Experts advise a commonsense approach: 1) Figure out which customers you want back; 2) Find out why they left; 3) Fix the problem; and 4) Invite them to return.

“Relationships that we want to restore are those that have been strong and close but for some reason have begun to disintegrate,” Barnes writes. “They may be with customers who are valuable not only because of what they buy but because of the referrals they make or who boost staff morale because of their positive interactions and feedback or who enhance the image of the business because of their activities and role in

the community.” Those customers you don’t want back are those who cost more to serve than they bring into the business, according to Barnes.

Griffin and Lowenstein advocate looking at Second Lifetime Value: a formula to determine your customer’s worth the second time around. First, multiply the number of orders per year by the dollar amount of the average order. That gives you your base revenue. Then add the cross-sell dollar amount (15 percent of the base revenue) and informational revenue (10 percent of the base revenue). Cross-sell opportunities are other products you think the customer may purchase. Informational revenue is something you know about the customer—such as the fact that the firm is planning to open up a new store that could mean more purchases. Subtract from that amount the total costs, including direct, winback and retention costs, to arrive at the gross profit. Repeat for the second and third projected years.

<b>Calculating Second Lifetime Value</b>	
	Base revenue (number of orders/year x dollar amount of average order)
<i>plus</i>	Cross-sell dollar amount (15% of base revenue)
<i>plus</i>	Informational revenue (10% of base revenue)
<i>minus</i>	Total costs (direct, winback and retention costs)
<i>equals</i>	Gross profit

In *Customer Winback*, Griffin and Lowenstein cite four different reasons why a customer’s “second life cycle” can be different—and better for the business—than his or her first life cycle:

- The defected customer is already familiar with the services offered.
- The service provider has more data about the likes and dislikes of the customer than it has about new customers and, therefore, can offer a more targeted service.
- The business can offer personal recognition that can lead to a sales performance better than that generated by the “typical, anonymously recruited first-time customer.”
- The length of the “prospect phase” and the “new customer phase” may well be shorter in the second life cycle than the first one.

An obvious tactic is one that can be easily overlooked: Fix the problem that led to the defection. Lowenstein cites a personal example of having been a customer of Netflix, the online DVD rental service. With Netflix, when you’re done with a DVD, you send it back, and the company sends you another DVD on your list. However, Lowenstein and his wife found themselves waiting a long time for subsequent DVDs, because Netflix did not have enough distribution centers to make its system work. They ultimately decided the turnaround wasn’t worth it and stopped using the service. The company sent out an announcement that it had increased the number of service centers and distribution centers and had shortened the turnaround time. “In other words,” said Lowenstein, “They addressed the key issue.”

## Implementation Considerations

As you build your loyalty program, CRM technology and “points” programs can help—if they affect loyalty drivers. And regardless how elegant your strategy, or sophisticated your loyalty program, without the support of the employees and managers in your organization, nothing much will happen.

### What About CRM Systems?

CRM has been a buzzword for the past decade. Does CRM information technology help build loyalty?

It depends. If your view is that CRM is just a more sophisticated method of direct marketing or merely a tool to track selling activities or primarily an efficient way to provide customer service, then you might achieve an excellent ROI on your CRM technology investment. Nothing wrong with that.

But if your objective is to improve genuine customer loyalty, remember that the value the customer *perceives* is all important. CRM systems can have an impact on customer loyalty by helping you:

1. **Improve service delivery with a single view of the customer.** CRM systems that give you an integrated view of each customer across all channels and touch-points enable your organization to provide the flawless service that customers demand today. And remember, poor customer service is the leading cause of defection.
2. **Optimize marketing with customer analysis.** Instead of “spray and pray” campaigns, use CRM analytical tools to dig deep into customer data to uncover purchase patterns and buying indicators. Then you’re prepared to make offers that are welcomed. Valued, even.
3. **Identify potential defectors and be proactive.** Analysis is critical, but the real secret is acting before it’s too late. CRM systems, especially when tied to other operational systems, enable you to proactively contact “at risk” customers and resolve their issues before they leave for good. Chances are you won’t get a second chance.
4. **Tie customer-centric behavior to employee rewards.** If you know the factors that drive customer loyalty, then you can use CRM systems to track employee behavior. But don’t stop there. Real change will only occur when employees and management are rewarded for doing the right things.

### The Point About “Points” Programs

One traditional method of retention that some loyalty experts do not tout highly is traditional rewards programs, such as frequent-flier programs and others in which a customer earns points toward an airplane trip or other reward. “The effectiveness of loyalty programs was limited largely to companies selling commoditized products and services—like airline travel, lodging and video rentals—with a high ratio of repeat purchase and one other key characteristic: a product that can be given away for free without incremental cost,” writes Howard Schneider and Richard Metzner in *What’s the Latest in Loyalty Programs? No Program at All*.

Schneider and Metzner, who both spent years in the airline industry before founding the loyalty consulting firm Metzner Schneider Associates, Inc., say even airlines can’t sustain the old frequent-flier model easily, anymore. Delivering printed mail and cards can be costly. Even JetBlue, which relies on the Internet to save marketing costs, must “carry millions of dollars worth of accrued miles or points on their books as a liability.”

Yet the United Kingdom’s retail giant Tesco has reaped enormous rewards from its Clubcard program. Using the customer behavior insight it gleaned from Clubcard data, Tesco has been able to tune its

marketing and service to optimize loyalty and profit. The results speak for themselves: In the past decade Tesco has zoomed past large established grocery retailers to become the largest in the U.K.

### **Getting Your Whole Company on Board**

Customer loyalty programs must be built on a solid understanding of customer drivers, rationalized with the company business strategy and supported with measurement systems.

But there's still one thing missing. People must be encouraged to do the right things, so linking measurements to rewards is critical.

In CRMGuru's loyalty survey (December 2004), we found more than 70 percent of respondents self-classified as leaders (doing an "excellent" job with loyalty programs) said their company gives both tangible and intangible rewards. For all other respondents, only 46 percent gave rewards of any kind. The primary metric driving an incentive was customer satisfaction score, followed by retention rate, customer value perception and loyalty score.

Are rewards just "show me the money"? Not necessarily. At Enterprise Rent-A-Car, an industry loyalty leader, according to Reichheld, only managers in the top 50 percent of branch offices, measured by customer satisfaction scores, are eligible for promotion. That's a powerful incentive for upwardly mobile managers to be part of a high-performance team that serves customers well.

At Amica Life Insurance, the rewards are cultural. The company has built a loyal customer base by hiring and retaining employees that love providing great service. Employees stick around for years, sometimes decades, and customers do, too. For the past five years, J.D. Power and Associates has ranked Amica "Highest in Overall Customer Satisfaction Among National Auto Insurers."

If you're serious about customer loyalty, you'll find a way to measure it and reward the people who make it happen, day in and day out.

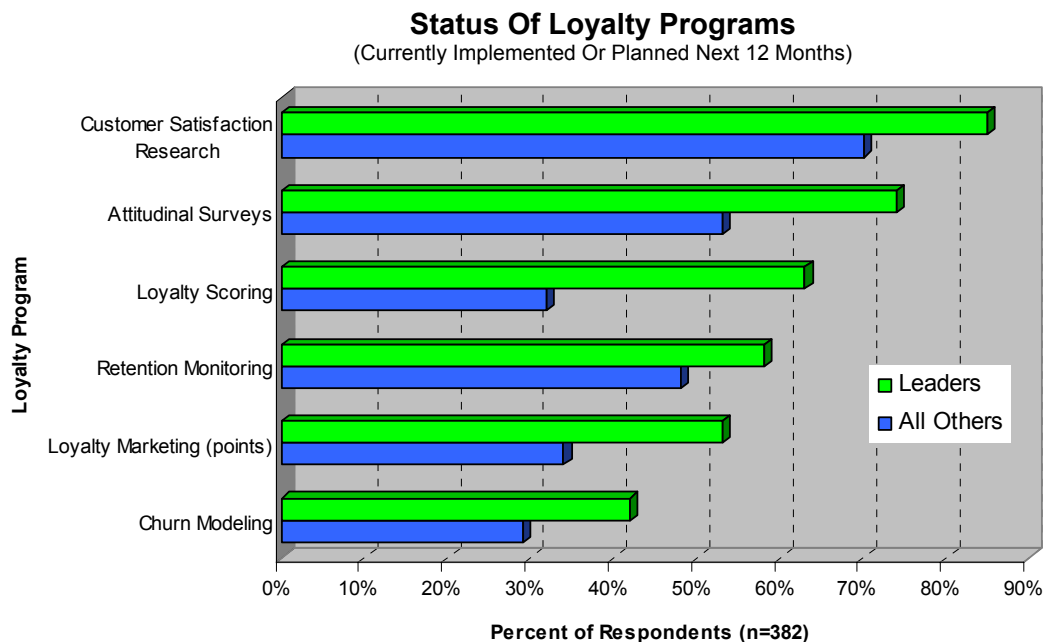
## Recommendations

The good news is that managers claim to place a high importance on loyalty. The bad news is the reality is a far cry from those claims. Despite nearly 80 percent of the CRMGuru.com survey respondents saying that management found loyalty to be “extremely” or “very” important, only 45 percent of those same respondents rated their businesses’ efforts at managing customer loyalty as “good” or “excellent.”

That’s plenty of room for improvement—and an opportunity to gain competitive advantage. Seize it!

Those that rated their efforts “excellent” are more likely to have formal loyalty programs implemented or planned (see chart below). These leaders are also more likely to:

- Put senior executives (CXOs) in charge, with dedicated staff to help
- Invest more marketing money in retention programs, not just acquisition
- Measure loyalty frequently, and reward the organization for results



Follow the example set by these leaders. Take the advice of loyalty gurus. But above all, do something! All the knowledge in the world won’t prevent customers from defecting or help you win them back, if you don’t try.



## About the Author



Bob Thompson is CEO of CustomerThink Corporation, an independent customer relationship management (CRM) research and publishing firm, and founder of CRMGuru.com, the world's largest CRM industry portal.

Mr. Thompson specializes in CRM strategic planning and research. Since 1998, Mr. Thompson has researched the leading industry trends, including how CRM concepts can be applied to extended enterprise value networks. In January 2000 Mr. Thompson launched CRMGuru.com, which has become the world's largest CRM industry portal with 200,000 members. He is frequently published and quoted in industry publications such as *BusinessWeek*, *InformationWeek*, and *Computerworld* and speaks at conferences and seminars worldwide.

Throughout his career, Mr. Thompson has advised companies on the strategic use of information technology to solve business problems and to gain a competitive advantage. Before starting his consulting and research firm in 1998, Mr. Thompson had 15 years of experience in the IT industry, including positions as Business Unit Executive and IT Strategy Consultant at IBM.

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## About the Sponsor



RightNow Technologies delivers highly effective on-demand CRM solutions to companies seeking to improve the quality of their customer relationships, enhance productivity and reduce costs.

Today, more than 1,200 companies use RightNow Technologies to improve customer loyalty and drive profits throughout the organization. Offered through a multi-tenant, hosted on-demand model, RightNow solutions reduce the cost and risk associated with deploying traditional enterprise customer relationship management

Founded in 1997, RightNow is headquartered in Bozeman, Montana, with offices in Europe and Asia.

For further information, visit [www.rightnow.com](http://www.rightnow.com) or send an email to [info@rightnow.com](mailto:info@rightnow.com).