CUSTOMER RELATIONSHIP MANAGEMENT

CONCEPTS AND TECHNOLOGIES

Chapter 2  Understanding relationships
Defining ‘relationship’

- A relationship is composed of a series of interactive episodes between parties over time.
- Episodes are time bound (they have a beginning and an end) and are nameable.
- Episodes are composed of a series of interactions. Interaction consists of action, and response to that action.
- Is a relationship more than interaction-over-time?
  - What about emotional content? Do relationships have some type of affective connection, attachment or bond?
1. Awareness
2. Exploration
3. Expansion
4. Commitment
5. Dissolution
Major relationship attributes

- Trust
- Commitment
Types of trust

A party in a relationship may trust the other’s..

- **Benevolence.** A belief that one party acts in the interests of the other.
- **Honesty.** A belief that the other party’s word is reliable or credible.
- **Competence.** A belief that the other party has the necessary expertise to perform as required.
How trust emerges

- Trust emerges as parties share experiences, and interpret and assess each other’s motives.
- As they learn more about each other, risk and doubt are reduced.
- For these reasons, trust has been described as the glue that holds a relationship together across time and different episodes.
Commitment defined

- Commitment is shown by ‘an exchange partner believing that an ongoing relationship with another is so important as to warrant maximum effort to maintain it; that is, the committed party believes the relationship is worth working on to ensure that it endures indefinitely’.
Characteristics of commitment

- Commitment arises from trust, shared values, and the belief that partners will be difficult to replace.
- Commitment motivates partners to cooperate in order to preserve relationship investments.
- Commitment means partners forgo short-term alternatives in favour of more stable, long-term benefits associated with current partners.
- Commitment entails vulnerability, leaving partners open to opportunism.
Evidence of commitment

- Evidence of commitment is found in the investments that one party makes in the other.
- One party makes investments in the promising relationship and if the other responds, the relationship evolves and the partners become increasingly committed to doing business with each other.
- Investments can include time, money and the sidelining of current or alternative relationships.
- A partner’s commitment to a relationship is directly represented in the size of the investment in the relationship, since these represent termination costs.
Attributes of high-quality relationships

- Core attributes
  - Trust
  - Commitment

- Additional attributes
  - Relationship satisfaction
  - Mutual goals
  - Cooperative norms
Companies want relationships with customers

Why?

- because companies that manage their customer base in order to identify, satisfy and retain profitable customers enjoy better business results
- reduced customer churn creates
  - A larger customer base
  - Longer average customer tenure
  - Reduced marketing costs to replace defected customers
  - Better understanding of customer requirements
  - More cross-selling opportunities
THE ADVANTAGES FOR THE LOYAL CUSTOMER

LOYAL CUSTOMER

COSTS
- Lower management costs
- Lower promotion costs

RETURNS
- Costant and increasing incomes
- Cross-selling
- Premium price

OTHER
- Positive word of mouth
- Innovative and customized offered mix
- Stimulated staff
UNITARY PROFIT PER CUSTOMER (in $)

Credit cards
Car insurance
Distribution
Concessionaire service

1st year  2nd year  3rd year  4th year
## Impact of churn on customer numbers

<table>
<thead>
<tr>
<th>Year</th>
<th>Company A (5% churn)</th>
<th></th>
<th>Company B (10% churn)</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Existing customers</td>
<td>New customers</td>
<td>Total customer base</td>
<td>Existing customers</td>
</tr>
<tr>
<td>1</td>
<td>1,000</td>
<td>100</td>
<td>1,100</td>
<td>1,000</td>
</tr>
<tr>
<td>2</td>
<td>1,045</td>
<td>100</td>
<td>1,145</td>
<td>990</td>
</tr>
<tr>
<td>3</td>
<td>1,088</td>
<td>100</td>
<td>1,188</td>
<td>981</td>
</tr>
<tr>
<td>4</td>
<td>1,129</td>
<td>100</td>
<td>1,229</td>
<td>973</td>
</tr>
<tr>
<td>5</td>
<td>1,168</td>
<td>100</td>
<td>1,268</td>
<td>966</td>
</tr>
</tbody>
</table>
Connecting customer retention to customer tenure

<table>
<thead>
<tr>
<th>Customer retention rate (%)</th>
<th>Average customer tenure</th>
</tr>
</thead>
<tbody>
<tr>
<td>50</td>
<td>2 years</td>
</tr>
<tr>
<td>67</td>
<td>3 years</td>
</tr>
<tr>
<td>75</td>
<td>4 years</td>
</tr>
<tr>
<td>80</td>
<td>5 years</td>
</tr>
<tr>
<td>90</td>
<td>10 years</td>
</tr>
<tr>
<td>92</td>
<td>12.5 years</td>
</tr>
<tr>
<td>95</td>
<td>20 years</td>
</tr>
<tr>
<td>96</td>
<td>25 years</td>
</tr>
<tr>
<td>97</td>
<td>33.3 years</td>
</tr>
<tr>
<td>98</td>
<td>50 years</td>
</tr>
<tr>
<td>99</td>
<td>100 years</td>
</tr>
</tbody>
</table>
Organizational benefits from managing customer retention

- **Reduced marketing costs**
  - Fewer dollars need to be spent replacing churned customers

- **Better customer insight**
  - Suppliers are able to develop a better understanding of customer requirements and expectations. Customers also come to understand what a supplier can do for them.
  - Consequently, suppliers become better placed to identify and satisfy customer requirements profitably, selling more product and service to the retained customer.
  - Over time, as relationships deepen, trust and commitment between the parties is likely to grow, and revenue and profit streams from customers become more secure.
## The customer journey

<table>
<thead>
<tr>
<th>Role</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suspect</td>
<td>Does the potential customer fit your target market profile?</td>
</tr>
<tr>
<td>Prospect</td>
<td>The customer fits the target market profile and is being approached for the first time.</td>
</tr>
<tr>
<td>First-time customer</td>
<td>The customer makes a first purchase.</td>
</tr>
<tr>
<td>Repeat customer</td>
<td>The customer makes additional purchases. Your offer plays a minor role in the customer’s portfolio.</td>
</tr>
<tr>
<td>Majority customer</td>
<td>The customer selects your company as supplier of choice. You occupy a significant place in the customer’s portfolio.</td>
</tr>
<tr>
<td>Loyal customer</td>
<td>The customer is resistant to switching suppliers, and has a strong positive attitude to your company or offer.</td>
</tr>
<tr>
<td>Advocate</td>
<td>The customer generates additional referral dollars through positive word-of-mouth.</td>
</tr>
</tbody>
</table>
Customer lifetime value (CLV) defined

- CLV is the present-day value of all net margins earned from a relationship with a customer, customer segment or cohort.
  - To compute CLV, all historic net margins are compounded up to today’s value and all future net margins are discounted back to today’s value.
  - Estimates of CLV potential look to the future only, and ignore the past.
  - A customer that appears to be valuable on the basis of the gross margins generated will most likely be less profitable once cost-to-serve the customer is taken into account.
Four causes of profit margin growth over time

1. **Revenues grow** over time, as customers buy more.
2. **Cost-to-serve is lower** for existing customers, because both supplier and customer understand the other.
3. **Higher prices are paid** by existing customers than new customers.
4. **Value-generating referrals** are made by existing, satisfied customers through their unpaid advocacy.
### Table 2.4 Profit from customers over time

<table>
<thead>
<tr>
<th>Service</th>
<th>Year 0</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit card</td>
<td>(51)</td>
<td>30</td>
<td>42</td>
<td>44</td>
<td>49</td>
<td>55</td>
</tr>
<tr>
<td>Industrial laundry</td>
<td>144</td>
<td>166</td>
<td>192</td>
<td>222</td>
<td>256</td>
<td></td>
</tr>
<tr>
<td>Industrial distribution</td>
<td>45</td>
<td>99</td>
<td>121</td>
<td>144</td>
<td>168</td>
<td></td>
</tr>
<tr>
<td>Auto servicing</td>
<td>25</td>
<td>35</td>
<td>70</td>
<td>88</td>
<td>88</td>
<td></td>
</tr>
</tbody>
</table>
Customers are potential income streams

- A core CRM idea is that a customer should not be viewed as a set of independent transactions but as a lifetime income stream.
Customer lifetime value

- The total present-day value of a customer is the sum of
  - all past net margins compounded to today’s value, and
  - all future net margins discounted to today’s value

- The potential value of a customer is
  - all future net margins discounted to today’s value
What you need to compute CLV

- insight into future buying behaviour
  - probabilities of buying products 1-n over the next x time periods
- margins earned from those products
- periodic costs of customer management

Plus, for new customers
- costs of customer acquisition

And finally
- Discount rate
When do B2B companies not want relationships?

- When they fear **loss of control**. Relationships are bilateral arrangements, which involve giving up unilateral control over resources.
- When **exit costs** are high. Not all relationships survive. It is not necessarily easy or cost-effective to exit a relationship.
- **Resource commitment**. Relationships require the commitment of scarce resources such as people, time and money.
- When **opportunity costs** are high. If resources are committed to one customer relationship, they cannot be used for another.
Business customers want relationships when …

1. the product or its applications are complex, for example, networking infrastructure
2. the product is strategically important or mission-critical, for example, core raw materials supply for a manufacturer
3. there are downstream service requirements, for example, for machine tools
4. financial risk is high, for example, in buying large pieces of capital equipment
5. reciprocity is expected. A financial audit practice may want a close relationship with a management consultancy, so that each party may benefit from referrals by the other.
When do customers want relationships with suppliers?

In the B2C context, customers may value relationships for several reasons:

- **Recognition.** Customers may feel more valued when recognized and addressed by name.
- **Personalization.** Products or services can be customized.
- **Power.** Relationships with suppliers can be empowering.
- **Risk reduction.** A relationship can reduce, or even, perhaps, eliminate perceived risk.
- **Status.** Customers may feel that their status is enhanced by a relationship with a supplier.
- **Affiliation.** People’s social needs can be met through commercially based, or non-commercially based, relationships.
Why B2B customers do NOT want relationships with suppliers

- Fear of dependency
- Lack of perceived value in the relationship
- Lack of confidence in the supplier
- Customer lacks relational orientation
- Rapid technological changes
The satisfaction–profit chain

- Customer satisfaction
  - Understand customer requirements
  - Meet customer expectations
  - Delivery customer value

- Customer loyalty
  - Behavioural loyalty
  - Attitudinal loyalty

- Business performance
  - Revenue growth
  - Share of customer
  - Customer tenure
Customer satisfaction defined

- Customer satisfaction is the customer’s fulfilment response to a customer experience, or some part thereof.
Two dimensions of customer loyalty

- **Behavioural loyalty**
  - Is the customer active?
  - What is our share of customer spend?
  - RFM variables
    - Recency
    - Frequency
    - Monetary value

- **Attitudinal loyalty**
  - Beliefs
  - Commitment
  - Preference
  - Intention to buy
RFM measures behavioural loyalty

- $R =$ time elapsed since last purchase
- $F =$ number of purchases in a given time period
- $M =$ monetary value of purchases in a given time period
Loyalty squares (Dick and Basu)

Repeat purchase

<table>
<thead>
<tr>
<th></th>
<th>high</th>
<th>low</th>
</tr>
</thead>
<tbody>
<tr>
<td>strong</td>
<td>true loyalty</td>
<td>latent loyalty</td>
</tr>
<tr>
<td>weak</td>
<td>spurious loyalty</td>
<td>no loyalty</td>
</tr>
</tbody>
</table>
Share of market vs. share of customer spend

- **High**
  - CRM

- **Low**
  - Traditional marketing

**Number of customers**
- Few
- Many
Researching the satisfaction–profit chain

- International data
- National data
- Industry data
- Corporate data
- Individual customer data
The American Customer Satisfaction Index (ACSI) model
Returns from investments in customer satisfaction
FOCUS: Managing Service Quality and Customer Satisfaction
CS measurement methods

We have two different approaches in CS evaluation:

DIRECT  Customer is engaged

INDIRECT  We use KPI or other techniques
Some implications about CS

- CS is different among segments
- CS can change during the time
- CS can change in the space
- CS in service is different from product
- CS is post-experience
CS drivers of an hotel service

OVERALL CS HOTEL

CHECK IN
  ROOM
  BREAKFAST
  RISTO
  CHECK OUT

CHECK OUT

BED
FURNITURE
BATHROOM
ROOM SERVICES

CLEANING
  TOWELS
  COURTESY KIT
  ......
Customer Satisfaction in Hotel

![Bar Chart]

- **Check in**: 11
- **Room**: 7
- **Ristorante**: 8
- **Breakfast**: 9
- **Check out**: 8
- **Satisfaction media**

The bar chart illustrates customer satisfaction levels across various aspects of the hotel experience.
Importance of secondary service and their impact on Overall Satisfaction

<table>
<thead>
<tr>
<th>Service</th>
<th>Importance (0= Low.)</th>
<th>Satisfaction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Check in</td>
<td>0.17</td>
<td>11</td>
</tr>
<tr>
<td>Room</td>
<td>0.30</td>
<td>8</td>
</tr>
<tr>
<td>Breakfast</td>
<td>0.24</td>
<td>8</td>
</tr>
<tr>
<td>Restaurant</td>
<td>0.01</td>
<td>7</td>
</tr>
<tr>
<td>Check out</td>
<td>0.12</td>
<td>9</td>
</tr>
</tbody>
</table>
Customer Satisfaction Matrix

- **Improvement Area**
- **Competition Area**
- **Monitoring Area**
- **Illusion Area**

<table>
<thead>
<tr>
<th>Importance of Secondary Service</th>
<th>Level of Satisfaction</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>High Satisfaction</td>
</tr>
<tr>
<td>Low</td>
<td>High Satisfaction</td>
</tr>
<tr>
<td>Low</td>
<td>Unsatisfied</td>
</tr>
<tr>
<td>High</td>
<td>Unsatisfied</td>
</tr>
</tbody>
</table>
In base alla Sua esperienza quale cliente di alberghi, La preghiamo di pensare al tipo di impresa alberghiera che fornisce una qualità eccellente. Pensate al tipo di im presa alberghiera con la quale sarebbe lieto di intrattenere rapporti d’affari. E’ gentilmente pregato di indicare in quale grado tale im presa presenterrebbe le caratteristiche descritte in seguito. Se ritiene che una caratteristica non sia affatto essenziale cerchi il numero 1; se ritiene che una caratteristica sia assolutamente essenziale cerchi il numero 7.

<table>
<thead>
<tr>
<th>In completo s'accordo</th>
<th>Assolutamente d'accordo</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Le imprese alberghiere eccellenti avranno attrezzature dall'aspetto moderno.</strong></td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td><strong>Le strutture fisiche di imprese alberghiere eccellenti sono attraenti a vedersi.</strong></td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td><strong>I dipendenti di imprese alberghiere eccellenti hanno sempre un aspetto curato e in ordine.</strong></td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td><strong>Nelle imprese alberghiere eccellenti i materiali associati al servizio (come pieghevoli o libretti) sono attraenti a vedersi.</strong></td>
<td>1 2 3 4 5 6 7</td>
</tr>
<tr>
<td><strong>Quando le imprese alberghiere eccellenti promettono di fare qualcosa entro un certo tempo, la fanno realmente.</strong></td>
<td>1 2 3 4 5 6 7</td>
</tr>
</tbody>
</table>

L’insieme di proposizione che segue si riferisce alle Sue sensazioni sull’albergo X X X. Per ciascuna proposizione La preghiamo di indicare quanto l’albergo X X X possieda la caratteristica descritta. Anche in questo caso se ritiene che la caratteristica non sia affatto presente in X X X cerchi il numero 1; se è assolutamente d’accordo che l’albergo X X X la possieda, cerchi il numero 7. Può cerchare i numeri intermedi per far vedere quanto specifica sia la Sua posizione in un senso o nell’altro.

<table>
<thead>
<tr>
<th>In completo s’accordo</th>
<th>Assolutamente d’accordo</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>L’albergo X X X ha attrezzature dall’aspetto moderno.</strong></td>
<td>1 23 4 5 6 7</td>
</tr>
<tr>
<td><strong>Le strutture fisiche dell’albergo X X X sono attraenti a vedersi.</strong></td>
<td>1 23 4 5 6 7</td>
</tr>
<tr>
<td><strong>I dipendenti dell’albergo X X X si presentano sempre con un aspetto curato e in ordine.</strong></td>
<td>1 23 4 5 6 7</td>
</tr>
<tr>
<td><strong>Nell’albergo X X X i materiali associati al servizio (come pieghevoli o libretti) sono attraenti a vedersi.</strong></td>
<td>1 23 4 5 6 7</td>
</tr>
<tr>
<td><strong>Quando l’albergo X X X promette di fare qualcosa entro certo tempo, la fa realmente.</strong></td>
<td>1 23 4 5 6 7</td>
</tr>
</tbody>
</table>

(continua)
Example (2)

Gentile Cliente, La preghiamo di aprire una X nella casella da più si avvicina al suo giudizio. Servi sono dei servizi non qualificati, per favore lasciare le case in bianco e passa alla domanda successiva. E' sufficiente un questionario per stanza.

**SODDISFAZIONE GENERALE**

Q1. Nel complesso, è rimasto soddisfatto della permanenza all'Hotel XXX?

   - Molto soddisfatto
   - Soddisfatto
   - Nei dubbi
   - Insoddisfato
   - Molto insoddisfato

   Perché?

**RECEPTION**

Q2. Qual è la Sua opinione complessiva sui servizi della reception?

   - Molto positiva
   - Positiva
   - Nei dubbi
   - Negativa
   - Molto negativa

   Perché?

Q3. E' rimasto soddisfatto dei seguenti aspetti relativi alla reception:

   - Efficienza del servizio prenotazioni
   - Accoglienza del check-in
   - Soluzione a richieste specifiche
   - Cortesia e disponibilità del personale addetto

   Perché?

Q4. Ha ricevuto informazioni sui servizi dell'albergo?

   - Sì
   - No

**STANZA**

Q5. Qual è la Sua opinione complessiva sulla stanza in cui ha permanito?

   - Molto positiva
   - Positiva
   - Nei dubbi
   - Negativa
   - Molto negativa

   Perché?

Q6. E' rimasto soddisfatto dei seguenti aspetti relativi alla stanza:

   - Comfort del letto
   - Acustica della camera
   - Arredamento e atmosfera
   - Pulizia della stanza
   - Servizio del personale al piano
   - Pulizia del bagno
   - Areezione del bagno
   - Servizio consuntiva presente nel bagno
   - Periodicità dell'(spazio della biancheria
   - Servizio lavanderia

**COLAZIONE**

Q7. Qual è la Sua opinione complessiva sulla colazione offerta dall'Hotel XXX?

   - Molto positiva
   - Positiva
   - Nei dubbi
   - Negativa
   - Molto negativa

   Perché?

Q8. E' rimasto soddisfatto dei seguenti aspetti relativi alla colazione:

   - Qualità e varietà del cibo
   - Presentazione del cibo e della bevanda
   - Accessibilità e freschezza del buffet
   - Pulizia
   - Efficienza e cortesia del personale di sala

   Perché?
REGRESSION ANALYSIS

HIGH IMPACT

LOW IMPACT
Soft Measures of Service Quality

Key customer-centric SQ measures include:
♥ Total market surveys, annual surveys, transactional surveys
♥ Service feedback cards
♥ Mystery shopping
♥ Analysis of unsolicited feedback—complaints and compliments, focus group discussions, and service reviews

Ongoing surveys of account holders to determine satisfaction in terms of broader relationship issues
Customer advisory panels offer feedback/advice on performance
Employee surveys and panels to determine:
♥ Perceptions of the quality of service delivered to customers on specific dimensions
♥ Barriers to better service
♥ Suggestions for improvement