The “L” Word
Loyalty: How do you measure it, and why is it important to your bottom line?

Jonathan Gilbertson  Director Client Services
You will find little argument among most business professionals that building a loyal customer base is essential to long-term business success. What you will find, however, is debate and even confusion about how to measure customer loyalty (compared to customer satisfaction), and how that measurement correlates to company growth and profitability.

In this paper, we will look at why loyalty is important and examine how companies are attempting to gather customer feedback. We will review why traditional customer surveys may fail, and examine how asking a single question could be part of the solution.

Why is customer loyalty important?

Let’s start by looking at the difference between customer satisfaction and customer loyalty. In his book, Customer Satisfaction is Worthless; Customer Loyalty is Priceless, Jeffrey Gitomer helps his readers distinguish between satisfaction and loyalty: (p. 252)

*Satisfied* customers will shop anywhere – satisfaction is not any indication that the customer will repeat a purchase. As a consumer, you have often been satisfied, yet never returned to that place of business.

A more complicated reason is that business is just now discovering that satisfaction is no longer the measure of customer success – loyalty is.

*What is a loyal customer? One who will create positive word-of-mouth advertising about you, refer other people to do business with you, and fight before they switch from you to a competitor.*

Drilling down further, studies have shown that *loyal* customers:

- Are less likely to be lured away by competitors who offer lower prices or promotional gimmicks
- Are more likely to accept the occasional instance of poor quality or service, provided it is truly occasional and is addressed quickly and to their satisfaction
- Are likely to account for a smaller percentage of complaints and support calls
- Are more likely to repurchase and adopt new products or services offered under the same brand
- Are more likely to offer constructive input to improve your products or services

Most importantly for this discussion, loyal customers are more likely to place their own reputation on the line and recommend your product or service to their friends and colleagues. Prospective consumers place a much higher value on product and service recommendations based on personal experience than they do on flashy advertising campaigns. This is especially true if they know or know of the person making the recommendation. Understanding this, many companies like Amazon.com and eBay have implemented customer-driven ranking systems to assist other consumers with their purchasing decisions.
The Amazon.com customer review process allows customers to comment and rate products found on the site. Customers are also able to leave video reviews.

With increased competition and globalization, it is increasingly difficult for companies to compete on cost alone. New products are brought to market and within weeks they are duplicated and perhaps improved upon by competitors, many times at a lower cost. There is increased urgency for companies to focus on building brand equity and strong customer loyalty.

**Poking holes in traditional customer satisfaction surveys**

Traditionally, business success and value is determined by looking at a company’s financial statements. This information is augmented by feedback gathered through various customer surveys meant to measure the level of satisfaction a customer has for the products or services offered by the company. The process of trying to arrive at a standard measurement of loyalty using traditional satisfaction surveys alone is full of challenges.

Loir Arussy, of Strativity Group, also questions the purpose of customer surveys. (Customer Surveys – What’s the purpose?) In his article he points out that most companies conduct surveys to seek affirmation or approval for their products or services. Questions are asked in such a way to provide very little strategic value other than to affirm their beliefs. The best surveys, according to some companies, are ones that tell them how great their products and services are. If the results are in contrast to their expectations, great effort is spent refuting the survey results.

Compared to a company’s survey expectations, customers are expecting their feedback to drive change and action. They look at this as their opportunity to share their thoughts with the company in hopes that any concerns they have will be addressed. Even though the truth may hurt, the most valuable survey is one where the customer shares their concerns and is asking you to correct them so they can continue to do business with you instead of simply walking away without ever telling you why they left.
In his book, *The Ultimate Question*, Fred Reichheld lists ten reasons satisfaction surveys fail. (Page 77-93)

<table>
<thead>
<tr>
<th>Reason</th>
<th>Description</th>
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<tbody>
<tr>
<td>Too many surveys, too many questions</td>
<td>How often is too often? Customer feedback is important but expecting customers to fill out lengthy surveys after every interaction is not advisable. Survey length continues to grow, reducing response rates and creating prejudicial results.</td>
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<tr>
<td>The wrong customers respond</td>
<td>It should not be assumed that a survey sent to all your customers is going to yield an accurate sampling. Suppose only customers who have complaints respond and business decisions are made solely on their feedback. Careful planning needs to be taken before and after the survey is completed to insure results represent a random sampling of one’s entire customer base.</td>
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<td>Employees don’t know how to take corrective action</td>
<td>Without a clear focus or business objective associated with satisfaction surveys, employees are often left to guess at what changes need to be made or which should have a higher priority. This is assuming of course that the survey results actually make it back to the frontline employee which often is not the case.</td>
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<td>Too many surveys are marketing campaigns in disguise</td>
<td>It’s an easy trap to fall into…one marketing question leads to another and soon you have a survey that is 40 questions long; mostly trying to learn about what new products or services you should pursue. While useful, these surveys have different purposes and often different audiences and should be conducted separately.</td>
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<tr>
<td>Survey scores don’t link to economics</td>
<td>Bain research has shown little connection between customer satisfaction scores and behaviors that drive profitability and growth. Analysis shows as many as 60 to 80 percent of customer defectors rated themselves as being satisfied.</td>
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<td>Plain-vanilla solutions can’t meet companies’ unique needs</td>
<td>One size does not fit all. Companies often utilize cookie cutter surveys designed by marketing companies and sold as quick Customer Survey solutions. Few companies take the added effort to conduct research and develop a customized survey strategy specific to their needs.</td>
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<tr>
<td>There are no generally accepted standards</td>
<td>Without a standardized survey strategy, many departments within companies are left on their own to gather and interpret customer feedback. This information is often inconsistent and therefore cannot be relied upon to identify trends or changes needed across the entire company.</td>
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<td>Surveys confuse transactions with relationships</td>
<td>Customer satisfaction surveys are often mistakenly interchanged with transactional surveys. The two should be kept separate. Additionally, not every transaction warrants the need for a survey.</td>
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<tr>
<td>Satisfaction surveys dissatisfy customers</td>
<td>If a customer is going to take time to complete your survey, they expect their response will be acknowledged and ideally action be taken to address any concerns they have. When it is not, the survey only makes the situation worse.</td>
</tr>
<tr>
<td>Gaming and manipulation wreck their credibility</td>
<td>The manipulation of survey results by sales and marketing teams often diminishes their usefulness.</td>
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Net Promoter Score®

Faced with the shortcomings of standard satisfaction surveys, Fred Reichheld, founder of the Loyalty practice at Bain & Company (in conjunction with Satmetrix), conducted a research project in 2003 with the goal of establishing a standard measurement for customer loyalty.

The starting point was to identify a loyalty question that linked to real behaviors (i.e. purchases and referrals). They collected survey data from customers in six different industries: financial services, cable and telephony, e-commerce, auto insurance, internet service providers and computer hardware. They asked respondents about satisfaction and loyalty to specific companies and their purchasing, referral histories associated with them. Follow-up surveys were sent to approximately 4,000 participants within a 6 to 12 month period to validate self reported loyalty and actual behavior.

The results indicated that one simple question, one’s “likelihood to recommend a particular company to a friend or relative” correlated to actual customer behavior 80% of the time. This group was also shown to be more likely to repurchase from the same company. (Satmetrix, The Power Behind a Single Number, p. 3)

Respondents were further categorized into three segments as shown below:

<table>
<thead>
<tr>
<th>Detractors</th>
<th>Passives</th>
<th>Promoters</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – Not at all Likely</td>
<td>1 – Neutral</td>
<td>2 – Extremely Likely</td>
</tr>
<tr>
<td>3 – Low Likelihood</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>6 – Very Low Likelihood</td>
<td>7 – Low</td>
<td>8 – Neutral</td>
</tr>
<tr>
<td>9 – Low to Medium Likelihood</td>
<td>10 – Medium</td>
<td>11 – High</td>
</tr>
</tbody>
</table>

1. **Promoters** – Customers who responded with a rating of 9 or 10 were highly likely to recommend a company. They reported the highest repurchase rates and accounted for more than 80 percent of all referrals.

2. **Passives** – Customers who responded with a rating of 7 to 8 were much less likely to provide referrals than promoters, often by 50 percent or more. They typically were not motivated to buy because of loyalty but may not defect until offered a better deal.

3. **Detractors** – Customers who responded with a rating of 0 to 6 were classified as detractors. They accounted for 80 percent of negative word-of-mouth comments.

**Formula**

Net promoter scores are tabulated by subtracting the percent of detractors from the percent of promoters.

\[ \% \text{ Promoters} - \% \text{ Detractors} = \text{Net Promoter Score}\]

To complete the research and confirm the connection between responses to the “Recommend” question and company growth, Satmetrix continued with studies where the “Ultimate Question”, “Would you recommend our product or service to a friend or colleague?” was asked and results tracked against company growth. The results showed a definite relationship between the two and Reichheld concluded that the percentage of promoters or net promoters was a viable metric to use when measuring customer loyalty. Reichheld found that companies who are NPS leaders in their industries outgrow their competitors by 2.5 times.

A 2005 study at the London School of Economics also concluded that NPS is a statistically significant predictor of annual sales growth. In their study of 1,256 consumers, they found a 7-point increase in NPS correlated to a 1% increase in growth.
Tracking your NPS

In the last several years, Net Promoter Scores (NPS) have become an increasingly important business metric for many companies. This is because:

- The method of collecting feedback and calculating ones score is easier than traditional customer feedback processes
- Because it is a single number, it is easily understood by employees
- The NPS is easy to compare to other organizations and is rapidly becoming accepted as a key metric for larger companies in measuring their performance
- There is strong evidence that a higher NPS is directly related to future business growth

Adoption of the Net Promoter Score continues to grow. Global companies like Intuit, Enterprise Rental Car, GE and Sony and many others have all adopted NPS.

Below are a couple examples of NPS reports. Because NPS is easy to calculate, it’s easily set up in Excel or similar spreadsheet program. Graphs can also be used to create a visual representation of your NPS.

<table>
<thead>
<tr>
<th></th>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
<th>Apr</th>
<th>May</th>
<th>Jun</th>
<th>Jul</th>
<th>Aug</th>
<th>Sep</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Promoters</strong></td>
<td>10%</td>
<td>20%</td>
<td>0%</td>
<td>30%</td>
<td>20%</td>
<td>30%</td>
<td>40%</td>
<td>40%</td>
<td>50%</td>
<td>60%</td>
<td>60%</td>
<td>70%</td>
</tr>
<tr>
<td><strong>Passives</strong></td>
<td>50%</td>
<td>40%</td>
<td>50%</td>
<td>50%</td>
<td>60%</td>
<td>30%</td>
<td>50%</td>
<td>50%</td>
<td>20%</td>
<td>30%</td>
<td>40%</td>
<td>30%</td>
</tr>
<tr>
<td><strong>Detractors</strong></td>
<td>40%</td>
<td>40%</td>
<td>50%</td>
<td>20%</td>
<td>20%</td>
<td>40%</td>
<td>10%</td>
<td>10%</td>
<td>30%</td>
<td>10%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Net Promoter Score</strong></td>
<td>-30</td>
<td>-20</td>
<td>-50</td>
<td>10</td>
<td>0</td>
<td>-10</td>
<td>30</td>
<td>30</td>
<td>20</td>
<td>50</td>
<td>60</td>
<td>70</td>
</tr>
</tbody>
</table>

While NPS can be used as a standalone metric as Reichheld suggests, I believe it should be used as part of an overall customer feedback strategy and serve as an indicator of where and when additional attention is necessary. In this way, you still have all the benefits of a single metric and are able to compare your score within your industry. In addition, the added data from a few additional questions is going to be very helpful in determining a course of action.
Regardless of whether you are conducting a traditional survey, Net Promoter Score, or a combination of the two, here are some simple guidelines you should follow:

1. Gain the support of upper management
   a. Provide rationale, context – the business case for doing this

2. Set clear, quantifiable goals for your survey
   a. Define follow-up paths
   b. Communicate to internal teams about the survey
   c. Plan how the results will be communicated and used to facilitate change

3. Write a survey that contains only the information necessary to accomplish your goals
   a. Be sure to distinguish between transactional and relational surveys, and do not combine them if at all possible
   b. Conduct separate marketing surveys

4. Do everything possible to encourage customers to respond
   a. Send a pre survey message letting them know a survey is coming soon. Let them know when they should expect it, a brief summary of what the data will be used for and let them know you will follow up with them and share survey results
   b. If the survey has not been completed as your deadline approaches, a reminder email is a friendly way of asking them to reconsider taking time to complete it

5. Review initial data keeping in mind that in many cases, dissatisfied customers may be more likely to provide their feedback

6. Review data internally and develop message to internal team as well as to your customers
   a. If the survey is not anonymous, personalize your message to each customer to acknowledge their specific feedback

7. Implement action plan as defined in step one

8. Measure progress.

Next Steps

Not sure where to start or how to get started with a survey program? Contact Sundog today. As a marketing and technology company, our experts have been on both sides of the table and have helped manage survey programs to drive business results and happy clients.
References


Shaw Colin, The DNA of Customer Experience (2007), (PP. 120-126), Palgrave Macmillan, New York, NY

Gitomer Jeffrey, Customer Satisfaction is Worthless; Customer Loyalty is Priceless (1998), (P 252), Bard Press, Austin, TX
