Customer Retention:

Keeping Your Best Customers for the Long Term

It's easier and less costly to sell to existing customers than to new customers. The more customers you keep through active retention efforts, and the longer you keep them, the more profitable your company will be.

Introduction: The Economics of Customer Retention

Keeping customers drives profitability. Whether we're talking about consumers or business-to-business customers, existing customers cost less to reach, cost less to sell, are less vulnerable to attacks from the competition, and buy more over the long term. The economics of customer retention is obvious according to Frederick Reichheld of Bain & Company, and author of *The Loyalty Effect*: customer spending tends to accelerate over time; longer-term customers are more efficient users of the products and services they buy and have lower operational costs; long-term satisfied customers provide more referrals; and longer-term customers are less price-sensitive than newer customers. The end result is that the overall value of a customer increases the longer that customer remains a customer. Bain & Company's research in a variety of industries suggests that a mere 5% increase in a company's customer retention rates will increase the average lifetime profits per customer.

Making the effort to track loyalty is the first step toward profitability. In a recent study, Deloitte Research found that manufacturing companies who tracked customer retention, set loyalty goals, and made efforts to exceed their loyalty goals, were 60% more profitable than those manufacturers who made no efforts to track customer loyalty. In addition, the study found that these loyalty-conscious manufacturers were also more likely to exceed their goals for growth and shareholder value.

Similar economics exist from the perspective of business-to-business sales. In a comprehensive survey of selling costs, *Sales & Marketing Magazine* reported that the number of sales calls required to sell a product to a new account was more than twice the number required to sell the same product to an existing account. Overall, the study found that it costs 133% more to sell new accounts than existing ones.

The Customer Retention Challenge

In an era when technology changes are accelerating, low price competition abounds, sales channels are shifting daily, and loyal customers are in short supply, the company that invests in a customer retention strategy and makes a commitment to customer loyalty gains an important competitive edge. The key is to understand where that commitment and investment can be best applied and what tools and programs can make them work.

Empirical evidence suggests that success in retaining customers often boils down to doing the basics right, such as:

- Building a customer database that identifies and characterizes loyal customers

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and collects their individual attributes and needs.

- Using this information to segment customers and prospects based on high, medium and low value.
- Building trust to get customers to give permission to receive ongoing marketing and special offers (permission-based marketing).
- Matching the right type of frequency/ loyalty marketing program to your customers' needs/values. For example, loyalty programs should include elements that focus on recognizing and retaining high value customers, growing medium value customers, and either growing or disengaging low value customers.
- Making sure that employees deliver the promises made by marketing and sales departments.

Customer Knowledge: The Basis of Any Long-Term Relationship

Many consumer incentive and promotion programs can increase sales, but when the goal is customer retention, it is best to start by learning more about your customer base. Specifically, you will want to identify the specific customers that you want to retain, understand what types of services they value, and determine what incentive motivational programs will work best with those customers.

How do you begin the process of listening to and learning about customers? Thomas O. Jones and W. Earl Sasser Jr., in an article in the *Harvard Business Review,* offer the following suggestions for customer research:

- **Customer satisfaction indices (CSI).** "Surveying customers about their level of satisfaction and plotting the results can help managers understand just how satisfied or dissatisfied customers feel about both their dealings with the company in general and with various elements of the company's product or service in particular," the authors say. Quantitative indices are also useful for comparing results from different time periods, locations, and business units.
- **Feedback.** Customer comments, complaints, and questions on product and service quality provide the critical information needed to anticipate areas of potential dissatisfaction. However, be prepared to respond. The quickest way to disengage any customer is to ask for input and then ignore it. Used correctly, however, customer input can be used to develop a customer retention strategy. "A company cannot implement a recovery strategy—a plan for making amends when something has gone wrong—if it does not know who has had a problem," the authors say.
- **Market research.** Many companies invest heavily in market research, but they often overlook two "critical listening points," say Jones and Sasser. "Customers should be interviewed both at the time of arrival (when they become customers) and at the time of departure (when they defect) about the reasons for their behavior." The authors found that simply contacting departing customers and "listening to them earnestly" was enough to recapture 35% of one company's departing customers.

Trusting Relationships with Customers Engender Loyalty

In an ideal world, loyal, long-term customer relationships will evolve toward partnerships.

Michael LeBoeuf, author of *How to Win Customers & Keep Them for Life*, argues that "It's not enough to reward your customers with good service. You have to make them aware of the good deal that they're getting for doing business with you—and keep reminding them of that in many subtle, different ways." For instance:

- Develop a customer profile that will give you a clear picture of the kind of customers you want to win and keep. "The more you can precisely define which customers you're trying to serve, the easier it is to perceive your business through their eyes," LeBoeuf says.
- Look at your business from your customers' perspective. Evaluate everything about your company that the customer sees or comes into contact with—from business communications to telephone greetings to sales and service contacts.
- Use problems as opportunities to demonstrate what great service your company gives. "Smart companies go the extra mile for the customer and show them just how dedicated they are to making sure that they feel good about doing business with them," says LeBoeuf.
- Develop a unique relationship with your customers and treat each one as someone special. The more customization you can build into customer relationships the better.
- Keep in touch with customers and keep them informed. "By staying in touch with customers after the sale or between sales," says LeBoeuf, "you can remind them of the fine service you give, make them aware of new products and services, and offer information to help them get more for their money."

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■ Remember that a large part of good service is show-biz. So don't be shy about infusing your customer retention program with some style and pizzazz.
■ Retain your own employees. Research shows that companies that have high employee retention rates have high customer retention rates.

Promoting Loyalty and Retention through Frequency Marketing

Frequency marketing is a term generally applied to any program designed to generate brand or customer loyalty which results in a long-lasting relationship with customers. Specifically, it encourages and rewards the ongoing purchase of products and services.

The concept gained popular attention in the 1930s with supermarket trading stamps. Overuse and tight grocery margins caused those early frequency marketing programs to lose their luster after a few years, but they have now returned with a vengeance. Often online, most offer more extensive and sophisticated reward possibilities, and this time the goal is more than loyalty: the goal is to get permission from consumers to market to them over time, and to make them feel appreciated for loyalty. The cost of the incentives pales against the value of target marketing to a willing customer.

By giving consumers an incentive to allow their purchases to be tracked, frequency marketing programs enable marketers to target promotions in a way never before possible—based specifically on consumer requests and business needs. They can help increase store traffic (online or on-premise), influence the size of purchases, stimulate faster purchase cycles, and/or add value, etc. They can prompt consumers to load up on product to thwart a competitive launch or encourage referrals. Best of all, because they target a specific, defined audience, you can precisely measure the results.

The growth of Internet-based marketing has given a whole new life to loyalty marketing. It's a medium that allows organizations to build extensive, permission-based databases, segment customers by pertinent characteristics, and communicate frequently to receptive customers with customized messages at costs far below traditional advertising.

A marketer can send an e-mail to one million consumers who have opted in to receive it for far less than the comparable cost of print, radio, and television advertisers, with the further benefit that consumers have given permission and the results can be precisely tracked.

When to Use Loyalty Marketing

Some businesses have characteristics better suited than other businesses for loyalty/frequency marketing programs, according to Jill Griffin, author of *Customer Loyalty: How to Earn It, How to Keep It*. Her book includes the following questions to help determine whether a frequency marketing program makes sense for your company:

■ Does your product or service have a frequent and regular repeat purchase cycle? Successful programs target customers who have an ongoing need.
■ Do your customers perceive little differentiation between your product or service and your competitors'? If customers perceive your product as replaceable and if they can be persuaded to buy from a competitor, then a frequency marketing program may help.
■ Will your customers perceive the rewards as valuable? Your customers must consider your frequent buyer benefits to be valuable and worth the effort.
■ Will you communicate with these customers on an ongoing basis in order to build a long-term relationship? You'll need a monthly statement by which you report to your customer and provide useful information and special offers.
■ Can you afford the program? The rewards, tracking, regular communication, and customer inquiries connected with the program will require significant time and monetary resources.

And, most importantly, what do you intend to do with the data you receive? Do you have a comprehensive relationship-building strategy and a means to measure it?

A Loyalty Marketing Success Checklist

Not every product or service is suitable for loyalty marketing. You have to evaluate your product or service from all sides to determine how it stacks up, in terms of economics, not only to the

Types of Frequency Marketing Programs

Because of their long experience with frequency marketing programs, incentive companies have developed a number of different variations—both traditional and online—suitable for a variety of different needs and goals. For instance:

■ Continuity premium programs are long-term customer loyalty programs that reward consumers with brand-logo merchandise or with premiums that can be associated with the product.

■ Free or pay-to-join club programs are formal membership programs geared to generate significant incremental purchases of sponsored products.

■ Collect-and-win games are designed to operate over a short period of time to generate four or five repeat visits or product purchases. Participants generally qualify for prizes at various levels.

■ Escalating rebate offers are designed to stimulate multiple purchases of a variety of brands. The more products purchased, the greater the rebate.

■ Credit-card or ATM automatic-entry sweepstakes: Every time you use a credit card to make a purchase or use your ATM card, you're automatically entered into a sweepstakes.

■ External group programs entail joint participation by two or more sponsoring companies. The program rewards consumer loyalty by offering points, such as air miles, based on purchases of a wide variety of products or services.

■ Time-release programs provide the required coupons upfront, but encourage purchases over an extended period of time by staggering the valid dates of the price offers.

Don't forget to communicate.
Whatever your choice of program, don't forget that communication is one of the keys to a successful customer retention program, and communication is a two-way street. You are advertising and marketing to external customers, who in turn communicate with the internal employees they encounter on a day-to-day basis. The feedback customers give to employees about your program may be one of the most overlooked areas of business intelligence in helping organizations better understand what they can do to please customers and promote retention over the long-term.

competition, but also to the most discriminating consumer. Here are some things to keep in mind:

■ Will it pay? Does your product-service profit margin support a loyalty strategy with sufficient funds to reward customers? If not, there will be no way to motivate consumers to opt-in.

■ Does it have buy-in from Sales, Financial, IT and Marketing Executive Management? Because loyalty programs may take months or years to generate a positive ROI it is important to get a long-term commitment from all key stakeholders.

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■ Think ahead. Loyalty marketing is a long-term strategy that should align with your strategic business goals. Don't think of your loyalty or retention program as a promotion. Promotions are short-term events. Loyalty programs use some of the same tools and rewards, but the focus is on enhancing satisfaction and promoting repeat business.

■ Target the right audience. Loyalty and retention programs are aimed at keeping the customers you already have. Remember, it can cost significantly more to gain a new customer than to keep an existing one, but not all customers are profitable. Make sure that your efforts are spent on customers you want to keep.

■ Consider the database issues. You need an efficient method of tracking customer purchases and measuring loyalty over time, a capability now provided by both proprietary and open source software. No program can exist without a proper technology infrastructure.

■ Use the program to build meaningful relationships. In addition to rewarding customers with discounts or free merchandise, a loyalty program should provide useful information and special offers that help make good customers even better customers.

■ Communicate one-to-one. One key to relationship-building and customer retention is to communicate genuinely, not generically, whether it's by mail, phone, the Internet, or face to face. Aim for dialogue. A loyalty program should be as close to one-to-one communication as possible, not simply a targeted direct mail with a general message.

■ Link external marketing promises with internal management. Do your employees understand your brand and the promises made to customers? Do employees know precisely what steps they can take to meet or exceed customer expectations? Make sure internal employees buy in to the promises being made to customers. Numerous studies have found that employee attitudes and their willingness and ability to develop relationships with customers have a significant impact on customer retention and future sales.

Budgeting and Measurement

A loyalty marketing campaign can cost anywhere from a few thousand dollars to millions of dollars, depending on the size of the audience. Because of the wide variety of options and the many ways in which a company can target its top customers, many components go into determining the cost and return on investment:

■ **Technology**—does it already exist or do you need a new solution?

■ **Concept design**—do you have inhouse capability to create, implement, and measure an effective program?

■ **Marketing**—how will you let customers know that the program exists?

■ **Tracking**—how will you make sure that loyalty is properly tracked, promoted, and rewarded?

■ **Awards**—what will you offer to keep customers engaged?

■ **Customer service**—are you making sure that whatever rewards you offer to consumers come with superb customer service so that your reward doesn't end up disappointing a key customer?

■ **Communications**—how and what will you communicate over time to build the relationship?

■ **Measurement**—how will you measure the return-on-investment? Can you track repeat customers and compare it with nonparticipants or with historical data? Can you track response rates of target customers to special offers against response rates of the general population?

What to Look for in a Supplier

Different types of companies can assist with various aspects of a loyalty program, including technology, awards, communications and promotion, tracking and administration, customer service, etc. Full-service performance improvement companies can provide a complete solution, while various types of technology, marketing, and fulfillment companies can provide unbundled services without strategic support.

If your organization takes its customer loyalty programs seriously and recognizes the significant returns of this marketing strategy, you will greatly benefit by using a performance marketing agency that specializes in designing and measuring loyalty solutions.

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This White Paper was put together under the auspices and with the input of the Performance Improvement Council, a unit of the Incentive Marketing Association.

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