Think Your Customers Are Loyal? Think Again

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It is critical to understand the multitude of variations of customer loyalty if a company is to win customers, increase market share and achieve high performance.

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You've gone to great lengths to identify and nurture the most valuable segments of your customer base. You've closely monitored them through surveys and focus groups, and you know they consistently indicate they are "highly satisfied" with your company and its products. But … are they loyal?

If you're like most companies, you don't really know – at least, not for sure. And that's a problem.

The loyal customer is perhaps the most elusive subject in all of management science. And a recent Accenture customer loyalty study suggests that the psychology at the heart of customer buying patterns and preferences is far more complex than previously thought. Different variations of customer loyalty must be understood if a company is to win the long-term battle for customers and market share.

Loyalty and High Performance

Understanding, nurturing and ultimately serving these different forms of loyalty is essential to a company's "market focus and position" – one of the three building blocks of high performance identified by ongoing Accenture research (see "The Right Place, the Right Time," *Outlook*, October 2005).

Through their market focus and position, high performers achieve a kind of strategic decision-making capability that enables them to compete in the best markets and maximize growth opportunities, without reaching or scaling beyond their capability to do so. Companies with an overly simplistic view of loyalty and of their customers are likely to have a misguided market focus and position, taking them down errant and expensive paths that can leave them poorly equipped to compete.

What makes customer loyalty such a vexing matter? Some loyalty challenges are inherent in the current market. Customers, for example, are harder to reach and impress than they used to be. Many traditional marketing channels have been weakened as consumers pursue various "market of one" activities: iPods, video games, movies on demand and personal video recorders that allow commercial skipping. In the hypercompetitive Internet age, customers also have more pricing information and more buying options than ever before.

But a number of misconceptions about loyalty have also led companies to make misguided investments in customer management programs.

The notion that loyalty is all about improving customer "satisfaction" is perhaps the most common mistake. The frustrating truth is that what customers say about being satisfied turns out to be a poor indicator of loyalty. In fact, a consistent finding from customer research is that 60 to 80 percent of lost customers across all industry segments reported on surveys just prior to defecting that they were "very satisfied" or "satisfied."

Another misstep is thinking that because a company has a loyalty program in place, it is doing all it can to improve customer loyalty. Loyalty programs are one part of an overall loyalty strategy, but they lack the nuance that gives companies the ability to target the most profitable segments. Our research has found that loyalty cannot be sustained by incentives alone. In Accenture's loyalty survey, for example, only 20 percent of consumers said they had switched providers in the past year because of the absence of loyalty perks and rewards. And just 22 percent said they have stayed with a provider because of frequent-buyer rewards.

Senior management has also diluted efforts to encourage customer loyalty through the attitude that "it's marketing's job." Marketing has a vital role to play, to be sure. But developing customer loyalty is a team sport. Human resources, product development and pricing, operations, and sales and service must all be pulling in the same direction to generate the kind of loyalty that produces high performance.

The True Drivers

To attract and retain the most loyal and profitable customers, a company must first understand the true drivers of loyalty: the customer attitudes that, in turn, drive the different types of behaviors that must be understood and nurtured.

Accenture has developed a loyalty model – based on our own research and client experience as well as on leading academic studies – to enable better analysis of different kinds of loyalty drivers. At the heart of the model is a better delineation of the different types of loyalty customers exhibit. These types can be understood as spectrums of attitude and behavior along three dimensions.

Involvement With the Product or Service Category

How interested are customers in the category's products and services? Are they active and engaged participants in loyalty programs? Are they "heavy" users of the category and enthusiastic about the category in general?

Commitment to the Brand

How passionate are customers about the brands they buy? Do they identify themselves with a brand and develop deep ties to it? Do they care about the fate of the brand? Are they willing to pay a premium for the brand? Are they advocates for the brand with people within their family and social network? Much as educators have discovered that teaching a subject helps a person understand the content more deeply, leading companies have discovered that the very process of advocating a brand to others creates deeper loyalty to that brand.

Likelihood to Re-evaluate

How prone are customers within a particular product or service category to re-evaluate their current buying choices? What are the most important shopping triggers? What barriers exist or might be erected against switching brands? For example, do changes in personal circumstances, such as income level or moving to a new home, trigger a re-evaluation of alternatives?

By analyzing the behavior and attitude indicators of this three-part model, different loyalty segments emerge, each with its own distinct loyalty drivers. Companies that recognize these nascent segments can improve their market focus and position by identifying previously unseen markets within markets. They can then design marketing, sales and service strategies to deliver a unique customer experience within each subsegment.

Applying the Loyalty Model

The following examples demonstrate how this loyalty model can help companies compete on customer loyalty.

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Variety Seekers

With the equivalent of 238 billion bottles sold annually worldwide, beer is a $413 billion global business. The marketing efforts of many of the largest brewers have, for the most part, been aimed at retaining brand loyalists by appealing to their competitive nature, asking them to identify with a brand much as they would with their favorite sports team. Using our three-part loyalty model, this means beer companies have been targeting customers with high category involvement (that is, they like beer), high brand involvement (that is, they are loyal Heineken or Kirin or Miller drinkers, for example) and a low likelihood to re-evaluate.

Yet a marketing approach targeted primarily at brand loyalists ignores a significant subsegment of the "high category involvement" customer base: drinkers of microbrewed, or "craft" beers. These customers are after not only quality but also variety. They are loyal, not in the sense that they can be counted on to order their favorite brand of beer again and again, but in their commitment to a diversity of experience. Such buyers constitute a growing market. In the United States, for example, craft-beer output rose 9 percent in 2005, even as production for domestic large brewers fell by 2 percent.

To respond to the unique characteristics of this market, some craft brewers have begun providing "seasonal" varieties of their beers. The Samuel Adams brand, for example – owned by U.S.-based Boston Beer Company – offers Octoberfest, Summer Ale, White Ale and Winter Lager to meet its customers' seasonal taste changes. This gives the company a better chance of holding on to the microbrew customers within its overall Samuel Adams suite of brands, even though these buyers technically would still be categorized as having a high tendency to re-evaluate their beer-buying habits. By meeting a customer's need for variety within the overall brand, companies can build greater long-term loyalty in a segment that might otherwise have seemed to defy loyalty.

Habitual Buyers

Consider another category of buyers whose loyalty patterns can fool companies: habitual buyers. If your company sells soft drinks or snack foods, for instance, you can easily take for granted the steady business from your retail outlets. But as one soft drink maker found out several years ago in a spat with Sainsbury's Supermarkets, the third-largest grocery retailer in the United Kingdom, nothing is a sure thing. Sainsbury's pulled the brand from its shelves and substituted its own private-label brand. Within months, the private-label brand was one of the best-selling soft drinks in the United Kingdom. What happened? Shoppers were more loyal to the store than to the soft drink brand.

In the context of our loyalty model, the brand commitment for these customers appeared high, but for a substantial segment of the market it was, in fact, quite low. Because re-evaluation was also quite low, it was only when customers were forced to rethink their purchase that the true nature of this segment's loyalty became apparent. So if loyalty comes more from purchase habit than brand preference, what becomes crucial is the third dimension of the loyalty model: that is, what the company must do to reduce the likelihood of re-evaluating.

One method used by market leaders to lower the risk of re-evaluation is to embed themselves inside the supply chain of buyers through approaches like vendor-managed inventory and continuous replenishment. These suppliers restock store shelves (for example, snack foods in grocery aisles) and companies' production inventories (say, cooking oil) on a continual basis, relieving the buyer of the need to constantly reorder to maintain supply. Becoming a quiet but essential player in the supply chain not only adds value for buyers in terms of ease of management, it also avoids the risk of buyers rethinking their supplier choices every time they fill out a purchase order.

Electronics giant Panasonic has recently instituted this type of strategy in its cooperative relationship with such retailers as Best Buy. Using a vendor-managed inventory model, Panasonic has taken on responsibility for the inventory of its products in the retailers' supply chains. Everyone wins with this model. The retailers eliminate or reduce the costs of owning the inventory but then share their higher margins with Panasonic. For its part, Panasonic gets an even greater benefit: an end-to-end view of its retailers' supply chains in real time, enabling Panasonic to better manage its business activities, including production timing.

Loyalty Engineering

Creating the right loyalty capabilities in a company, and then effectively managing customer loyalty, demands what might be called an "engineering" perspective. That is, it requires a data-driven approach that enables a company to analyze and understand the different configurations of loyalty drivers among its customers, and that supports long-term initiatives to shift and evolve the market focus and position of the company based on those customer configurations. The Accenture Customer Loyalty Management Framework, for example, combines detailed steps involving insight, strategy, execution and measurement, as well as essential enablers such as leadership, technology and organizational design.

Some practical steps for creating differentiated customer loyalty-building capabilities:

Understand Loyalty in the Context of Your Business Model

Most organizations continue to place more emphasis on customer acquisition than on customer loyalty. That can be an expensive mistake. A rigorous analysis of the comparative costs of acquiring new customers and retaining existing ones can be eye-opening. For example, one telecommunications service provider recently conducted an analysis of different customer churn models, mapping various churn percentages to the number of customer acquisitions that would be required to offset the losses. The company found that more effective customer loyalty programs were more important than customer acquisition programs.

Only by challenging long-held beliefs with hard facts and figures rooted in the company's business model and financial targets will change be effective. It is absolutely imperative that the full costs and benefits of a revitalized loyalty strategy are explored across all aspects of the organization to ensure that initiatives gain senior-level endorsement as part of the company's overall growth plan.

Develop a Detailed Mapping of Loyalty Drivers

Understand the different types of loyalty that exist within your current customer base and across the wider market, and how each type influences the risk of defection and the possibility of achieving even greater loyalty than you currently have. Leverage loyalty-driver insights to plan distinctive customer experiences that create and sustain each type of loyalty.

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Plan a Comprehensive Response, Integrated Across All Relevant Dimensions of Your Company

Use an integrated approach to generating customer loyalty that involves a coordinated series of initiatives across the following five dimensions.

- **Insight** – Use sophisticated data mining tools, behavior analyses and external research to understand different segments of the customer base over time.
- **Strategy** – Align loyalty drivers to the customer experience, and ensure that the brand values are consistent with the needs of targeted customer segments. Define loyalty metrics and who owns them.
- **Execution** – Implement customer treatments across channels, organizational boundaries and technologies. Make sure that a rewards-based loyalty program delivers clear business benefits and that it is flexible over time. Appoint a clear owner of the entire "customer experience."
- **Measurement** – Track loyalty measures at each customer touch point. Proactively address the causes of excessive customer churn. Make sure that loyalty programs have a clear purpose within the loyalty strategy and that the return on investment for such programs can be measured.
- **Enablers** – Build technology capabilities that enable data mining and cross-organization integration. Align leadership, culture and values toward a customer-centric approach. Implement governance and journey management capabilities to ensure that silo-based turf warfare does not derail the necessary change.

Test New Loyalty-Building Programs Before Scaling Them Across the Company

A common practice among loyalty leaders is to pilot loyalty-building initiatives to prove their value and gain broader organizational buy-in before making sizable investments in long-term programs. The key is to start with a high-impact first phase and then scale quickly.

ExxonMobil Corporation, for example, used a pilot approach to test the potential of its Speedpass system, which is based on a small key-tag device that customers pass in front of a reader at the gas pump to expedite their purchases.

With more than 7 million users, Speedpass has created a loyal subsegment within the company's customer base, and is helping to drive additional revenues. ExxonMobil continues to improve the Speedpass system by pilot-testing related programs.

A Comprehensive Approach

Loyalty is the result of multiple factors involving brand, customer characteristics, category involvement, cultural issues and a myriad of other considerations. Companies that continue to base their market focus and position on a monolithic and overly simplistic view of customer loyalty may be investing in the wrong things for the wrong reasons. Even well-intentioned loyalty programs can hamper competitive effectiveness if they are not based on the right customer loyalty drivers.

The advantage of the approach to building customer loyalty recommended here is that it integrates strategy, analytics and measurement to quickly put into practice the strategic changes that can have the greatest impact on business performance. By using this approach, companies can shape and deliver optimal customer experiences based on the unique loyalty characteristics of a complex customer base.

This approach can help companies better understand what their customers are thinking and what motivates their purchasing decision – and, thus, can help companies keep those profitable customers. It's a far better method than basing strategic decisions on how customers have acted in the past, which is often not the best predictor of future behavior. In the end, companies may find that the loyal customers they seek have been there all along, hiding in plain sight, simply waiting to be identified, understood and marketed to in the right ways. ■

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THE CUSTOMER EXPERIENCE

When marketers use the phrase "customer experience," it is not merely a matter of semantics. One of the most important developments in management science in recent years has been the insight that we are in an "experience economy." Customers are not buying just a product or service from a company, they are buying the total experience around its consideration, purchase, use and service.

Companies that master this experience – that can understand it and deliver it better than their competitors – have an edge in the marketplace. Research backs up this point. The Accenture High Performance Marketing study, for example, revealed that a positive customer experience accounts for 33 percent of a company's ability to achieve strong customer loyalty (see "Marketing Mastery Matters," *Outlook,* May 2006).

THE IMPORTANCE OF LOYALTY

Cultivating loyal customers is essential to achieving high performance for several reasons. Reliable studies continue to point to the fact that it is far more expensive to attract customers than to retain them. Loyal customers also buy more. In a recent Accenture survey, 81 percent of consumers said they will continue buying from companies to which they are loyal, and about half said they would buy more or respond to specials from such a company. In short, customer loyalty provides pricing power in the marketplace and better protection from competitive threats. Loyalty provides a platform for stronger, deeper relationships with customers; it can also increase market share and revenue, and lower the overall cost of customer acquisition.

The bad news is that when customer loyalty is measured, the numbers are pretty dismal. The annual customer defection rate has grown from 16.9 percent in 2003 to 19.1 percent in 2005. One study found that, on average, U.S. corporations lose half of their customers every five years. A recent Accenture survey of U.K. and U.S. consumers – customers across a range of service providers – found that 60 percent of them had switched loyalties in the past year, and 64 percent said they are likely or very likely to stop doing business with a company they currently patronize.

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