

Managing Services
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Lecture – 41
Loyalty – Relationship

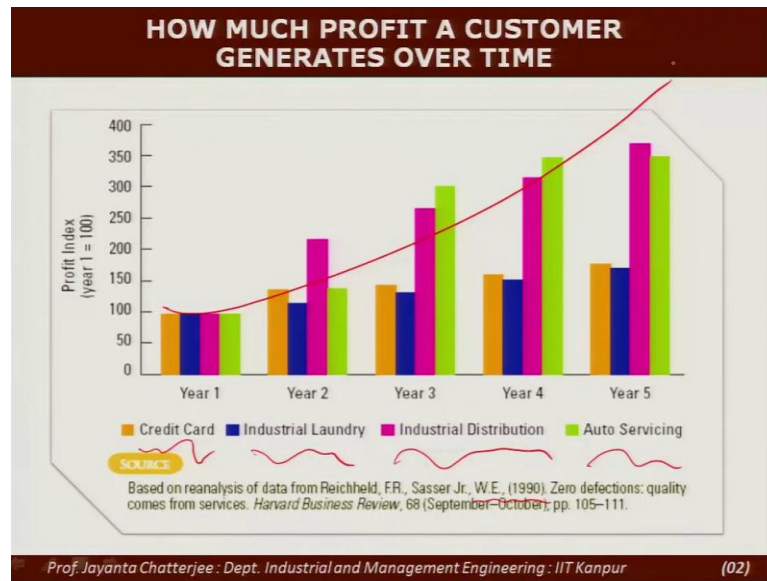
Hello, so our concluding topics for the 7th week will be from service recovery, service complaint and service recovery which we discussed in the last session.

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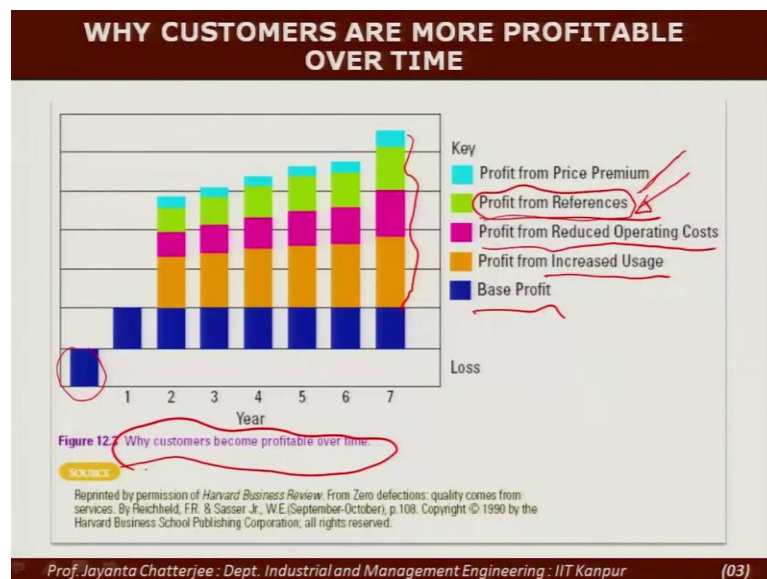
How do we reach our ultimate aim that we have been talking about during this week, the customer advocacy through the path way of Customer Loyalty. As we discuss this pyramid that first of all you must have service quality and service quality will not automatically lead to customer satisfaction, you have to have a manage process to reach customer satisfaction. And in that, one part of that is the service recovery strategy and if you have customer satisfaction, good service recovery strategy, then you are able to overlay the processes for customer delight and that is the path way ultimately to reach customer advocacy and we are going to discuss today many issues relating to this journey.

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Let us look at this a very interesting research paper that we know right from 1990 and this was published in Harvard business review and this research very clearly shows that for services like credit card, industrial laundry, industrial distribution, auto servicing, how year upon year the life time value of the customer increases almost exponentially. So, it is just not incremental benefit that you get from long term relationship with the customer, but you get multiple multi tear benefits.

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For example, as you can see here in this diagram, this is also reprinted from that same research paper that this is year one, where actually you just have, if you have done everything well then some small surplus. Now, as it goes on then it is not that only you

get every year this base profit with the base profit. But, then you have this pile of benefits, pile of benefits are profit from increased usage, a satisfied customer with the mobile service, a satisfied customer with a credit card service tend to use the service more and therefore, you have some incremental revenue.

Then; obviously, as the customer becomes known to you and the customer knows you and each party develops more confidence in each other, then due to this additional revenues coming in, you are doubly benefited. Because, your operating cost also come down and we are not also discussing that you no longer have a customer acquisition cost that is already given that we have discussed before. But, now you also start getting profit from references, the customer becomes your advocate, so there are referral revenue sources.

So, the customer recommends your credit card service to others and the customer knows what kind of credit check system that you have, what kind of people will qualify and therefore, the right kind of references and you can actually further reinforce it. Many credit card companies do that if your reference ultimately is issued a credit card, then you are given some points, reward points and so on. So, you can therefore, make these references beneficial to the service organization as well as the service customer.

And then of course, a service customer who is bounded with you will tend to will more amendable to higher level of service. So, a gold credit card customer may agree to go to the platinum level here with some persuasion with some reward points and also can therefore, continue to bring you additional revenue. So, profit from price premium, profit from reference, profit from reduced operating cost, profit from increased usage, these are all that piles up on top of the based profit year after year.

So, that is why customers always become more and more profitable over time and that is why today in all most all businesses, because as we discussed right in the beginning of this week in the hyper competitive world of service business today, the cost of acquiring a new customer is going higher and higher. Therefore, the more emphasis you do to retention rather than to acquisition, you will be better of operationally as well as financially.

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WHY IS CUSTOMER LOYALTY IMPORTANT TO A FIRM'S PROFITABILITY?

- Customers become more profitable the longer they remain with a firm:
 - Increased purchases and/or account balances
 - Customers/families purchase in greater quantities as they grow
 - Reduced operating costs
 - Fewer demands from suppliers and operating mistakes as customer becomes experienced
 - Referrals to other customers
 - Positive word-of-mouth saves firm from investing money in sales and advertising
 - Price premiums
 - Long-term customers willing to pay regular price
 - Willing to pay higher price during peak periods

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Customers become profitable as we discussed due to reduced operating cost, increase purchases, referrals to other customers, price premiums and so on. This same points are discussed in more detail in this slide and the following slide.

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ASSESSING THE VALUE OF A LOYAL CUSTOMER

- Repeat and loyal customers : Not always : Cardiac Patient
 - Costs
 - Not all types of services incur heavy promotional expenditures to attract a new customer
 - Walk-in traffic more important at times
 - Revenue
 - Large customers may expect price discounts in return for loyalty
 - Revenues don't necessarily increase with time for all types of customers

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Now, of course, it is not that every where you want this repeat customer, like if a, your healthcare facility and you have successfully dealt with a cardiac patient, you are not really looking for a repeat business from that. Because, that is not neither ethical not desirable not practical and some types of repeat customers are long term relationships and may be quite costly and therefore, in such cases the walk in traffic will also be quite

important, this is true again in certain health care cases, this is true in some very high value exclusive services.

And that is because if you in certain high values services, a long term customer will expect some price discount. And therefore, it may be business wise may be not the right approach, but I would say that this particular, these are exceptions and we can ignore this exceptions in today's hyper competitive service businesses and focus more on this diagram that longer the customer stays with you, the longer is the relationship, better are your opportunities and most importantly that is the path way to develop the relationship towards customer advocacy.

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ASSESSING THE VALUE OF A LOYAL CUSTOMER

- Profit impact of a customer varies according to stage of service in product life cycle
 - e.g., referrals and negative word-of-mouth have a higher impact in early stages
- Tasks:
 - determine costs and revenues for customers from different market segments at different points in their customer lifecycles
 - predict future profitability

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So, the value of a customer can be the profit impact of a customer can vary depending on the product life cycle and in the early stage for example, a repeat customer is far more valuable than in the saturation stage, where you know they are may be in some cases not so profitable to serve some low value customers and so on, we will discussed that just now. At this stage I would like to point out thus the relationship is far more important for younger companies, for startups than for much older companies. So, guard with hoxie the relationships that you develop at the early stage of the product life cycles, service life cycle.

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**MEASURING CUSTOMER EQUITY:
LIFETIME VALUE OF EACH CUSTOMER**

- **Acquisition revenues less costs**
 - Revenues (application fee + initial purchase)
 - Costs (marketing + credit check + account set up)
- **Projected annual revenues and costs**
 - Revenues (annual fee + sales + service fees + value of referrals)
 - Costs (account management + cost of sales + write-offs)

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Measuring the customer equity or what we call life time value of each customer, we it is a basically acquisition revenue less costs. So, revenues are in a if we take for example, credit card or mobile service, then revenues are your application fee plus initial purchase and plus requiring revenues coming and costs will be marketing and the credit check, setting up the account and so on. So, revenues will be annual fee, sales, service fees, value of referrals and cost will be account management, cost of sales and write offs. So; obviously, this line minus this line if that keeps growing, then you are on the right track of developing relationship.

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**MEASURING CUSTOMER EQUITY:
LIFETIME VALUE OF EACH CUSTOMER**

- **Value of referrals**
 - Percentage of customers influenced by other customers
 - Other marketing activities that drew the firm to an individual's attention
- **Net Present Value**
 - Sum anticipated annual values (future profits)
 - Suitably discounted each year into the future

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The value of referrals can be actually a big multiplier depending on how you handle it and actually this referral system can be a ripple and therefore, one person can refer five persons and those five persons can bring in five each. And that will in fact, many of the network marketing companies use this method, the pyramid marketing is not a good approach it is illegal in many countries, but creating a network of customers as your co marketer can be a very powerful force multiplier.

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GAP BETWEEN POTENTIAL AND ACTUAL VALUE

- **What is current purchasing behavior of customers in each target segment?**
- **What would be impact on sales and profits if they:**
 - buy all services offered by the firm,
 - use these to the exclusion of any purchases from competitors,
 - pay full price?
- **How long, on average, do customers remain with firm?**
- **What impact would it have if they remained customers for life?**

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The gap between potential and actual value, to know that we have to basically find out that what is the current purchasing behavior of the customer in each target segment. How long an average to customers remain with the company? What impact would it have if they remained customers for life?

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WHY ARE CUSTOMERS LOYAL?
(SERVICE INSIGHTS 12.1)

- Customers stay loyal when we create value for them
- Value can be created for customers through:
 - **Confidence benefits**
 - Confidence in correct performance
 - Ability to trust the provider
 - Lower anxiety when purchasing
 - Knowing what to expect and receive
 - **Social benefits**
 - Mutual recognition and friendship
 - **Special treatment**
 - Better price
 - Discounts not available to most customers
 - Extra services
 - Higher priority when there is a wait

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And then you have to analyze this with data and then that is how you will actually determine the customer life time value and the importance of CLV in your kind of services business. So, if you are in the business of credit card, if you are in business of mobile telephony, if you are in the business of relationship banking for high network individual, in all these cases long term relationships are crucial and the life time value of the customer are normally much higher than transactional value.

In the text book that we are using for this course there are some interesting insides at chapter number 12, which is the chapter relating to managing relationship and building loyalty. So, you will see that the, we have given some small cases from where you can see that when we create value, we can create this value to different mechanism through social benefit, where you know there is a mutual recognition.

So, if the customer is greeted by name, if the customer is treated with a smile and saying the usual professor Chatterjee then; obviously, that service establishment delights mean. Because, they remember me, recognize me and those are the kind of social benefits of course, you can develop this much further you can develop. Now a day's many service organizations do it routinely that greet you on your birthday send you a card on your anniversary may be sometimes they will if you are high value customer, they will send you some gift or some flowers on social occasions.

These are benefits for the customer give some psychological feeling of goodness of feeling good and of course, it has a much bigger impact in on the service business,

because it often creates impulse purchases it often creates... So, if you get a greeting card on your birthday from a restaurant which you are frequent it is likely that evening party you will hold at that restaurant and they may even some times if you have done it once or twice then a you will not be surprise when that restaurant calls you a day before your birthday and say shall we are organize the party like last time and so on and so forth.

So, you can create these opportunities for conversation, the conversation and communication and a continuing loop of this conversation and communication is the way relationship is kept alive and kept interesting. And these are very important this may appear to be innocuous, but these small actions can give you this big result in developing loyalty and relationship.

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TRANSACTIONAL MARKETING

- **Transactional Marketing**
 - One transaction or a series of transactions does not necessarily constitute a relationship
 - Requires mutual recognition and knowledge between the parties

Handwritten annotations: 'Transactional' and 'Relational' are circled in red, with an arrow pointing from 'Transactional' to 'Relational'.

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So, basically today we want to any service marketing, you want to claim this ((Refer Time: 14:00)) way at the lowest level we have transactional marketing, which is one time, one transaction or just some series of transaction in near vicinity it is then recall relational, where as suppose to transactional, where the service provider may have no knowledge about the service customer in relationship. Obviously, you have develop the knowledge about the customer.

So, this is a more knowledge based relationship and which is only possible if your organization has the learning capability of about your customer to gather data, to interpret that data, to format the data and make it available at the right time to the front line personnel who are giving the service. And then of course, from rash relational we

want to go to advocacy or customer as your co marketer and this is the desired state and this is the stairway.

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RELATIONSHIP MARKETING

- Marketing that creates **extended relationships** with customers
- Database Marketing:
 - Includes market transaction and information exchange
 - Technology is used to
 1. Identify and build database of current and potential customers
 2. Deliver differentiated messages based on customers' characteristics
 3. Track each relationship to monitor cost of acquiring that customer and lifetime value of resulting purchases

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So, from no recognition to mutual recognition and knowledge between the parties and going forward to the extended relationship, this is what we want to achieve to do this fortunately today, there are number of good technical tools that are available. First tool that is very important, very simple data base marketing, even a simple spread sheet or a very minimal database can actually create a excellent opportunities for creating repeat sales, for creating up sales and cross sales opportunities.

So, it allows you to therefore, understand the customers as individuals or understand the customer as a particular class or define the segment much more clearly in terms of demographics, psycho graphics and behavior almost important by the behavioral patterns. So, that you are able to contact the customer at the right time when you can create a sales revenue opportunity.

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RELATIONSHIP MARKETING

- **Interaction Marketing:**
 - Face-to-face interaction between customers and supplier's representatives
 - Value is added by people and social processes
 - Increasing use of technologies make maintaining relationships with customers a challenge
 - e.g., self service technology, interactive website, call centers
- **Network Marketing:**
 - Common in B2B context
 - Companies commit resources to develop positions in a network

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And then besides the face to face interaction which is; obviously, the most the costliest you can use therefore, technology the information and communication technology to keep the interaction going in B2B marketing or high value marketing, we also pickup something called network marketing, where actually we have not only the directly from the service organization. But, you also have number of distributors and service representatives and other people in the network who will sustain each other's effort.

So, hardware manufacturers, software manufacturers, network equipment manufacturers they often indirectly keep this interactions going and give each other leads. So, that the sales, so if somebody a data center customer a first contacts a contractor who will give a turnkey supply of the data center will automatically lead to contacts with work station suppliers or server suppliers or other networking equipment suppliers or the specialized air conditioning supplier and so on.

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RELATIONSHIPS WITH CUSTOMERS		
Type of Relationship Between the Service Organization and its Customers		
Nature of Service Delivery	Membership Relationship	No Formal Relationship
Continuous	<ul style="list-style-type: none">DTH TVInsurance PolicyCollege enrollment	<ul style="list-style-type: none">Radio StationPoliceLighthouse
Discrete Transactions	<ul style="list-style-type: none">Theater subscriptionWarranty repair	<ul style="list-style-type: none">Movie TheatrePublic Transport

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So, today many of these businesses are performed as networks and therefore, network marketing is based on a relationship among the network partners. And so now, we will look a different types of relationship with customers and at this moment before I conclude I will only list these... So, there is a nature of service delivery can be continuous and can be decreed transaction. So, there can be within this there can be a relationship based and there is no formal relationship based therefore; obviously, we are actually interested in this block.

There are certain services where creating relationship is not that easy. Because, if you are having a radio broadcast or a television telecast, then it is difficult to create formal relationship. But, these days as you see with the power of telephone and the with the high penetration of phone across India many radio programs have call in opportunities. So, as your favorite songs are getting played, you can call in you can chat with the jockey, radio jockey and you can actually create a recognition and some sort of relationship.

In movie theater also normally you know people just go there by a ticket and see the movie. But, now more and more theaters are actually trying to create a subscription based a membership relation. So, the idea therefore, is that more and more businesses are trying to move in this direction, where you have better a continuous relationship at least if there is no continuous relationship, each transaction is based on mutual knowledge that is what we are trying to achieve. We will see details of these processes in the next session.

Thank you.