Customer Relationship Management

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Introduction

Customer Relationship Management (CRM) is developing into a major element of corporate strategy for many organisations. CRM, also known by other terms such as relationship marketing and customer management, is concerned with the creation, development and enhancement of individualised customer relationships with carefully targeted customers and customer groups resulting in maximizing their total customer life-time value.

Industry leaders are now addressing how to transform their approach to customer management. Narrow functionally-based traditional marketing is being replaced by a new form of cross functional marketing - CRM. The traditional approach to marketing has been increasingly questioned in recent years. This approach emphasised management of the key marketing mix elements such as product, price, promotion and place within the functional context of the marketing department.

The new CRM approach, whilst recognising these key elements still need to be addressed, reflects the need to create an integrated cross-functional focus on marketing - one which emphasises keeping as well as winning customers. Thus the focus is shifting from customer acquisition to customer retention and ensuring the appropriate amounts of time, money and managerial resources are directed at both of these key tasks. The new CRM paradigm reflects a change from traditional marketing to what is now being described as "customer management".

The adoption of CRM is being fuelled by a recognition that long-term relationships with customers are one of the most important assets of an organisation and that information-enabled systems must be developed that will give them 'customer ownership'. Successful customer ownership will create competitive advantage and result in improved customer retention and profitability for the company.

In many companies there is still confusion as to what CRM is all about. To some it is about a loyalty scheme, to some it is about a help desk. To others it is about a relational data base for key account management and for others it is about mass profiling the customer base without undertaking detailed segmentation. Relatively few organisations have implemented an integrated approach, which addresses all the key strategic elements of CRM. Only a small number of businesses have a clear idea what should be done with information technology in order to successfully implement CRM.

This paper addresses: why traditional marketing is longer enough; the role of information technology in CRM including understanding the economics of customer acquisition and retention; developing appropriate metrics; and CRM implementation issues.

Traditional marketing is no longer enough

The amount an organisation spends on marketing is not necessarily related to its marketing effectiveness. Some organisations undertake relatively little marketing activity and as a result have a fragmented customer base, poor market positioning and low levels of marketing effectiveness.

Other organisations have been successful with relatively little expenditure on marketing. For companies such as Virgin Atlantic, The Body Shop and First Direct, public relations and word-of-mouth marketing have been very important to them, so that despite fairly low levels of advertising spend they are highly effective in their marketing.

Many organisations, despite heavy investment in marketing departments and marketing activities, have achieved poor results from their marketing effects; quite a number of financial services companies fall into this category. We call this "marketing trappings" marketing.

Relatively few organisations have adopted relationship marketing and CRM approaches to effectively harness the tools of marketing to deliver real increased customer value and, with the help of technology, developing appropriate long-term relationships with customers.

To achieve success, businesses need to have the appropiate measurement systems and marketing metrics in place to ensure their are effective in terms of their use of customer-focused resources. Over the past two decades businesses have developed sophisticated approaches to measurement in other functional activities within their business - in Operations, Finance, IT and Human Resources. However, the Marketing function may be the last bastion of inadequate and inappropriate metrics. Lord Leaverhume is reputed to have said, " Half the money I spend on advertising is wasted - the trouble is I never know which half it is." This approach to marketing is not acceptable. Organisations would not tolerate an HR manager who recruited two people due to lack of knowledge of which one would work out; or an operations director who built two plants because he was not sure which one would operate effectively!

Traditional marketing activities which emphasise customer acquisition are no longer sufficient. CRM recognises that marketing starts after the sale is over, not when the sale is completed.

In future marketing will need to create much stronger metrics so that strategies can be evaluated rigorously.

The role of information technology in CRM

In considering how CRM should be implemented, information technology has a pivotal role to play in enabling companies to maximize profitability through more precise targeting of market segments and the micro segments within them. We are now in a new era of technology-enabled marketing which involves leveraging relationships through the use of technology. Powerful new technological approaches involving the use of data bases, data marts, data warehouses, data mining and one-to-one marketing are now assisting organisations to increase customer value and their own profitability.

Technology can greatly assist in managing the data required to understand customers so that appropriate CRM strategies can be adopted. In addition, the use of IT can enable the necessary data to be collected to determine the economics of customer acquisition, retention and life-time value.

Research shows that a 5% points increase in customer retention yields a profit, in net present value terms, of between 20% and 125%. Although many managers are now familiar with these findings, our research shows that few managers know the profit impact of retention in their own business. Some managers may know the the their customer retention rate but they struggle to understand how changes in this impact their profitability. Few companies segment their customer base by life-time value. A result, they may not adopt appropriate retention and acquistion strategies.

Given the dramatic effect that improved customer retention can have on business profitability, organisations need an approach that leads to greater customer loyalty, enhanced retention and profitability. To improve customer retention; three steps are needed: measurement of customer retention, identification of root causes of defection and related key service issues; and the development of corrective action to improve retention.

Measurement of existing customer retention rates is the first critical step in the task of improving loyalty. This involves measuring retention rates and profitability analysis by segment. We have developed a detailed methodology, the Retentiongram Model, which enables informed choices to made about the relative marketing emphasis to be placed on strategies for different customer segments. The model allows managers to determine the impact on profitability of various factors related to customer retention and acquistion. These include changes in: the cost of acquisition, the number of new customers acquired, the profitability of retained customers, and the retention rate.

Regardless of the approach taken to modelling the economics of acquisition and retention, life-time value will need to be identified by market segment and needs to address how to improve it. Clearly improving retention can have a huge impact on life-time profitability. The business will also need to consider how they will get the greatest benefit from their acquisition activities. To facilitate improved acquisition, retention and life-time value, companies need to utilise the appropriate technology tools to assist this process.

In the business-to-business context an example of this would be sales force automation - creating an information empowered sales force which increases the sophistication of customer management. This can dramatically improve sales force productivity and significantly enhance the bonds with the customer.

In business-consumer organisations who are dealing with a large number of customers, a critical issue will be increasing the quality of customer contact through tools such as sophisticated call centers and electronics commerce .

Organisations will need to determine the appropriate customer management strategy and then develop the appropriate information technology platform to suit their requirements, now and in the future. This may involve a creative blending of a range of information technology infrastructures starting with databases and then progressively moving towards data marts, enterprise data warehouse and integrated CRM solutions using electronic commerce. It may also involve using approaches such as data-mining, event-driven marketing and channel optimisation. The ultimate objective of this will be to identify opportunities for

increased profitability through enhanced customer acquisition, improved customer retention and targeted cross-selling.

Developing appropriate metrics

Central to achieving success will be the development of new metrics to measure performance in CRM across the business. It is increasingly being recognised that there are linkages between employees satisfaction, employee retention, customer satisfaction, customer retention, sales and profitability. A number of academics and consultants have developed models based on these linkages. The best known is the "service profit chain", a research methodology developed by faculty at the Harvard Business School. This methodology describes the linkages between employee attitude, customer retention and loyalty and profitability.

One of the most outstanding exemplas of use of the service profit chain approach is Sears, Roebuck and Company, the leading US department Store. Sears, one of the great turnaround successes of the 1990s, has undergone a radical transformation in the last 5 years. Much of its success is due to rigorous measurement systems which track employee attitudes and their impact on customer satisfaction and profitability. Critically, management alignment has been created around the metrics and there is widespread understanding throughout Sears as to how this model works. (For a description of their approach, see the box below).

Sears, Roebuck and Company: Developing "best-in-class" metrics

In 1992, the company reported massive losses of $3.9 billion on sales of $52.3 billion. Arthur Martinez was appointed to head the merchandise group and he undertook a streamlining of the business - he closed 113 stores and terminated the 101 year old Sears catalog, which was a household institution within the US. He also set about changing the service strategy, focusing on women who were the most important buying decision makers. As a result in 1993 the company reported a net income of $752 million - a dramatic reversal of fortunes for a mature company such as Sears.

Martinez set up five task forces (customers, employees, financial performance, innovation and values) to define world class status in each specific area, identify obstacles and define metrics for measuring progress. The task forces spent months listening to customers and employees, observing best practice in other organisations and establishing measures against objectives. Gradually it became apparent that what was needed was a model to show direct causation from employee attitudes, through customer satisfaction to profits. The company needed to know how management action, such as investment in sales force training, would directly translate into improved customer satisfaction, retention and higher revenues. What was needed was an operationalisation of the employee-customer profit model.

Sears defined a set of measures based on its objectives. These were broken down into three objectives which focused on making Sears - "a compelling place to work, to shop at and to invest in. Relationships between changes in key metrics were identified using causal pathway modeling.

The results were impressive - direct links were identified between employee measures, customer measures and revenues so total profit indicators for the company could be established. Employee attitude towards the job and company were found to be critical to employee loyalty and behaviour towards customers,

whilst customer impression directly affected customer retention and the likelihood of recommendations. After further refinement, the model is now used as a predictor of revenue growth: 5 unit increase in employee attitude drives 1.3 unit increase in customer impression, 0.5 increase in revenue growth and a quantifiable increase in store profitability.

To successfully implement the service profit chain model it was necessary for Sears to change the behaviour of leadership to take responsibility for the company"s culture and understand how this impacted on revenues. In addition, employee rewards needed to be aligned to the model for financial and non-financial measures. A further change has been the streamlining of IT - from 18 separate databases to a single, integrated system. The results have been impressive - employee satisfaction at Sears has risen by 4% and customer satisfaction by almost 4%. More than $200 million additional revenues have been achieved through this value creation process.

CRM implementation issues

This paper has argued that whilst Customer Relationship Marketing is being increasingly viewed as a major element of corporate strategy, there is confusion about what it means in practice. Further, many organisations are adopting CRM practices on a fragmented basis through a range of activities such as direct mail, help desks, call centres and loyalty cards. These activities are often not properly integrated.

Where CRM is well understood as a concept, many board-level managers are still unclear as to how a particular CRM approach should be cost-effectively implemented and what technology options should be adopted.

The starting point for introducing or further developing CRM must be determined from a strategic review of the organisation"s current position. Companies need to address four broad issues: what is our core business and how will this evolve in the future; what form of CRM is appropriate for our business now and in the future; what IT infrastructure do we have and what do we need to support the future organisation needs; and what vendors and partners do we need to choose?

An organisation should first examine its core business and consider how will it evolve in the future. It then needs to consider the form of CRM that is appropriate for their business now and in the future and what organisation resources does it have to support the business now and in the future.

Having identified the present and future focus of CRM, the organisation then needs to address the appropriate information architecture to enable their CRM strategy to be implemented. Stated simply the task is how can we exploit technology for improved CRM.

As organisations increase their sophistication they will need to creativity integrate these technologies. "Planned evolution" is a good way of summarising the technology approach to building the backbone to support the relevant CRM strategy that has been mapped out for the business.

An essential element of achieving successful implementation is to ensure that their strategy is underpinned by viable and appropriate technology architecture. This involves the selection of vendors and partners based on issues of customisation capability and other appropriate commercial factors including both technological and commercial criteria.

The new millennium, Customer Relationship Management will have advanced considerably and we will have reached much more sophisticated level of one-to-one marketing and data mining. There is now an enormous opportunity for organisations to improve their "customer ownership" by building a co-ordinated and integrated set of activities which address all the key strategic elements of CRM. Ultimately, however, organisations" success in CRM will involve creating an appropriate strategic vision for the future, making the appropriate choice of applications, creatively using appropriate analytical techniques to exploit the data, and choosing the right vendor for supply of the technology solution.