Optimizing Value TO and FROM the Customer

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OPTIMIZING CUSTOMER INTERACTIONS™

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Introduction

What if it were possible for a large corporation to serve its customers with the same intimacy and attentiveness that is the norm for doing business with many small proprietorships? In dealing with small businesses managed by actively-involved owners, customers can often count on getting exactly what they want or something just as good or better, because the owners know each customer personally, remember his or her preferences, and anticipate his or her needs. Unfortunately, this capability is often lost by large corporate organizations that serve thousands of customers and invest in initiatives that focus on the profitability of business units and functions within the organization. Some organizations have tried to capture the customer-centric focus of many small proprietorships, but have been disappointed with the results as the returns in terms of customer loyalty and profitability have fallen short of expectations. These attempts have been unsuccessful, not because the investment in customer relationships was inappropriate, but rather because the investment was not appropriately balanced between value to the customer (VTC) and value from the customer (VFC).

This paper will describe how to appropriately balance the value provided to and derived from your customers. It will take you through the steps that will define and quantify the impact of each initiative on your customer relationships to help you evaluate the balance between the VTC and the VFC. First, a framework for evaluating VTC for each initiative will be presented and then you will be guided through the use of analytics for assessing VFC. With this information in hand, you will be shown how it can be aggregated into a score that will let you prioritize your initiatives to ensure appropriate allocation of capital to those most likely to increase customer loyalty and profitability for your business. And finally, you will be shown the results of firsthand experience in applying VTC/VFC analytics in a case study that demonstrates how this approach has resulted in significant results for a large corporation.

Guiding Principle: Balancing VTC and VFC

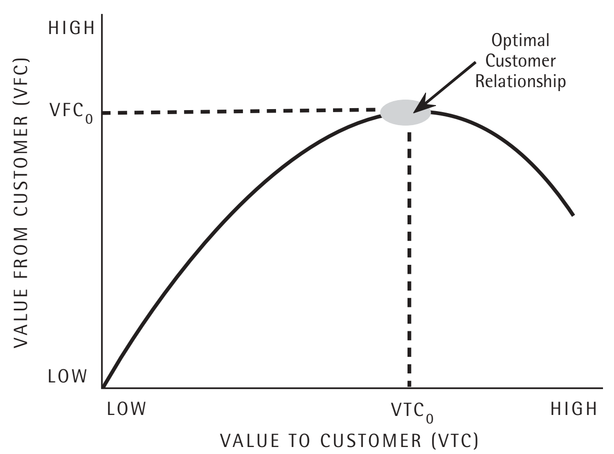
Investment in customer-centric initiatives is most successful when focused on enhancing customer relationships. An optimal customer relationship is achieved when there is an appropriate balance between VTC and VFC. To determine whether such a balance exists, both VTC and VFC must be quantified. In the cost-conscious environment existing in most organizations today, investment prioritization will favor those initiatives that can support a demonstrable impact that enhances efficiency. Yet, such cost-cutting efforts with a short-term impact on the bottom line may have negative impacts on the value to the customer and result in lower profitability in the long run due to customer defection. Consequently, the value to the customer must be assessed with the same rigor as the value from the customer.

Optimizing Customer Relationships

In an optimal customer relationship, the customer experiences a discernible benefit from an interaction with the organization that results in increased profitability for the company from this customer. When there is an imbalance between VTC and VFC, organizations risk losing customers and/or profitability. In relationships where both VTC and VFC are low, customers and long-term shareholder value are at risk. When VTC and VFC are low, a company typically invests in low ROI customer-centric initiatives with little positive impact on the customer. For example, a credit card company may invest in technology that allows a cardholder to punch in his card number before speaking to a Customer Service Representative (CSR) in an effort to route calls to a self-service channel. However, the credit card company fails to design the Interactive Voice Response (IVR) system in a way that is user friendly, resulting in the cardholder requesting to speak to a CSR who asks for the card number again because the CSR has no visibility of the card number that was originally entered into the system by the cardholder. As a result of an exclusive focus on efficiency gains, the credit card company not only increased the amount of time the cardholder was on the phone with the CSR, but also frustrated the cardholder due to the confusing IVR design and need to repeat the card number verbally to the CSR.

CRM GUIDING PRINCIPLE: BALANCING VALUE *TO* & *FROM* THE CUSTOMER

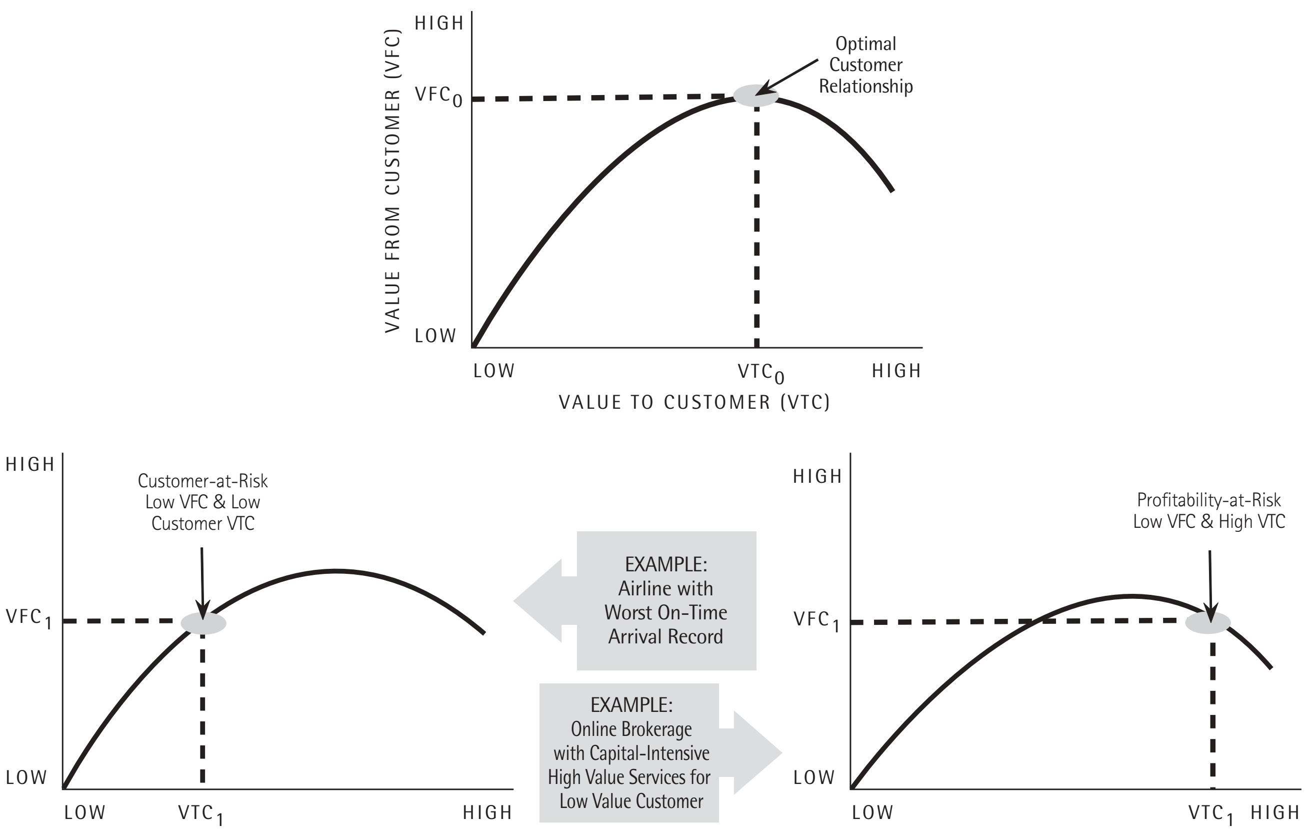
The ultimate goals of a Customer Relationship Strategy are to define and quantify optimal customer relationships, provide a roadmap for execution, and a method for tracking success.



On the other hand, if VTC is high and VFC is low, profitability is immediately at risk. In this instance, a company is usually following a herd mentality by providing various features in its offering that its competition is providing, with little understanding of the cost implications of the additional features. This was very much the case in the Internet era when online companies offered various features for free in order to keep up with the competition. As a result of this policy, many of these companies filed for bankruptcy. However, such a policy is not limited to Internet companies. Financial service and pharmaceutical companies, for example, frequently provide products and services at low or below cost with little understanding of whether such services provide sufficient incremental value to the customer to justify decreased margins in terms of value from the customer. Thus, profitability is also at risk when the customer and the organization do not perceive VTC in the same way. Less than optimal customer relationships result from imbalances between VTC and VFC. By appropriately quantifying VTC and VFC, companies can avoid these traps and make better decisions regarding customer-centric investments.

OPTIMIZING THE CUSTOMER RELATIONSHIP

Appropriately balancing the value derived from the customer and the value provided to the customer results in an Optimal Customer Relationship.



Focusing on VTC

A customer perceives that an organization is providing value in its products and services if it fulfills three simple objectives. These objectives center around the customer's need to be recognized, heard, and helped by the company.

- Recognize me

  Customers want an organization to recognize who they are and what their relationship with the company has been throughout their interactions with the company. In response to this objective, companies engage in analysis involving customer profiling and segmentation, customer lifetime value, revenue and margin contribution, and customer demographics and preferences.

- Hear me

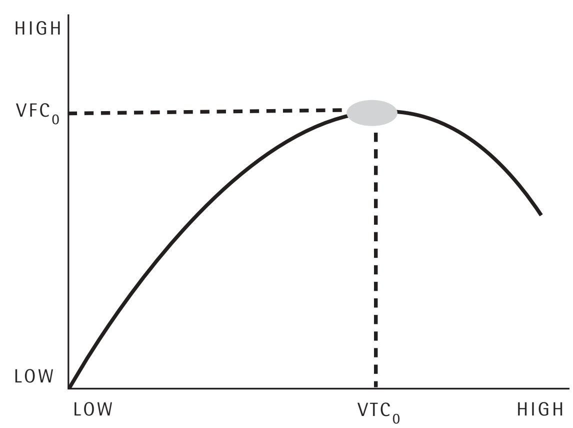
  Customers want companies to understand their likes and dislikes in interacting with the organizations, so that the companies can learn from past errors and take proactive steps in the future. This involves monitoring customers throughout the entire life cycle of interactions with the company from purchase to service.

- Help me

  Based upon recognizing and hearing the customer, companies should be able to help customers through refinements of their products or services. This focus might generate projects that address marketing, sales, or service issues, or provide unique and differentiated treatments.

  Once a company ascertains what is important to a customer, it must decide whether it is economically feasible to pursue such activities. A quantitative analysis of value from the customer will provide guidance in exploring this issue.

FOCUSING ON VALUE *TO* THE CUSTOMER (VTC)

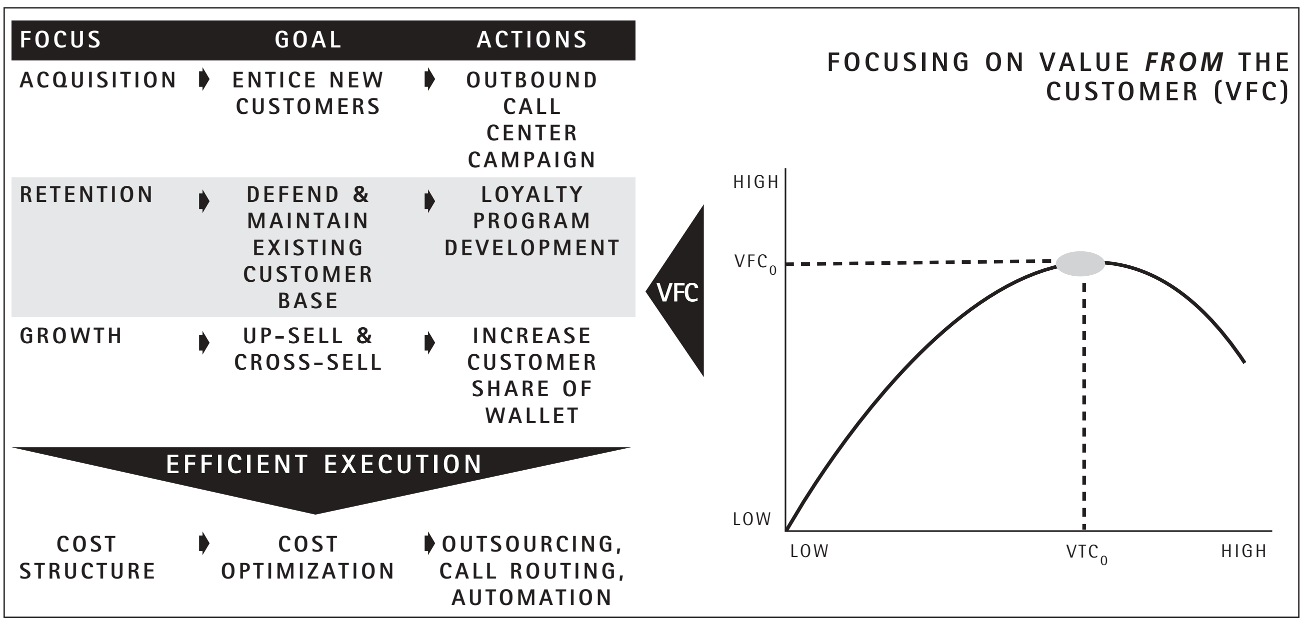


VTC

CUSTOMER REQUEST	COMPANY ACTION	FOCUS AREA
KNOW ME	ANALYZE	• CUSTOMER PROFILING/SEGMENTATION • CUSTOMER LIFETIME VALUE, REVENUE, MARGIN • CUSTOMER DEMOGRAPHICS & PREFERENCES
HEAR ME	MONITOR	• CUSTOMER SATISFIERS & FRUSTRATIONS • VOICE OF CUSTOMER RESEARCH
HELP ME	ACT	• ONE-TIME PROBLEM RESOLUTION • UNIQUE OFFERS • AFTER-SALES SERVICE, DIFFERENTIATED BY CUSTOMER VALUE • CLEAR BILLING • EFFICIENT PRODUCT RESEARCH, QUOTING, AND ORDER PROCESSING • ON-TIME DELIVERY

Focusing on VFC

Initiatives that focus on VFC are designed to meet the goals of either enhancing or protecting revenue or of avoiding or reducing costs. When the specific focus is on acquisition, an outbound marketing campaign may be sensible if the goal is to entice new customers. Development of a loyalty program is a worthwhile project when the focus is on retention and the goal is to defend and maintain an existing customer base. If growth is the focus, projects that promote cross-selling and up-selling are logical if the goal is to increase customer share of wallet. Projects that focus on cost structure with a goal of cost optimization might include outsourcing, call routing, and automation.

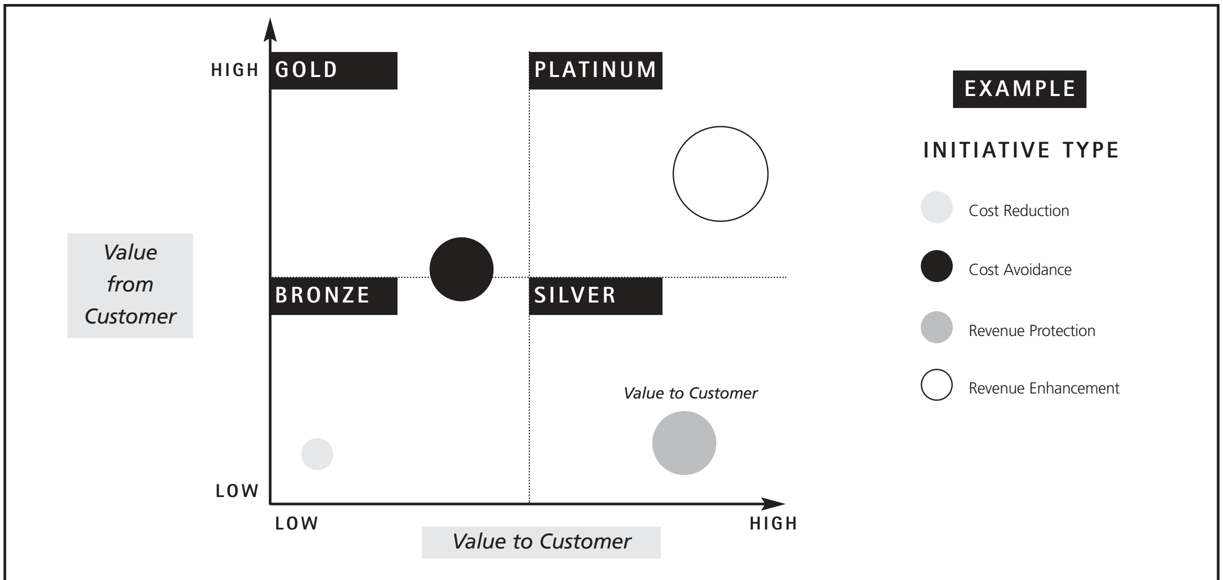


Prioritizing Projects Based Upon VTC/VFC Principles

Any initiative that is developed and/or evaluated based on VTC/VFC principles will have the potential to impact customer relationships in an optimal manner. The challenge comes in determining which of these projects should be given the highest investment priority. In a customer-centric and value-based prioritization process, all potential projects are passed through an analytic filter that will quantify both VTC and VFC. These analytics generate a VTC/VFC value matrix plotting VTC scores against VFC scores. The scores for each project will cross at a position in one of four quadrants of high-high, high-low, low-high, and low-low scores for VTC and VFC. The highest level is achieved when VTC and VFC are both high and the lowest level is achieved when both VTC and VFC are low. The prioritization of initiatives within this value matrix forms the basis for a customer-centric roadmap around optimal capability sequencing that also factors in people, process, technology, and execution timing risks.

CRM ROADMAP OUTCOME: INITIATIVE PRIORITIZATION

The optimal allocation of capital among the initiatives of the CRM Roadmap is based upon a prioritization that balances the value provided to and derived from the customer.

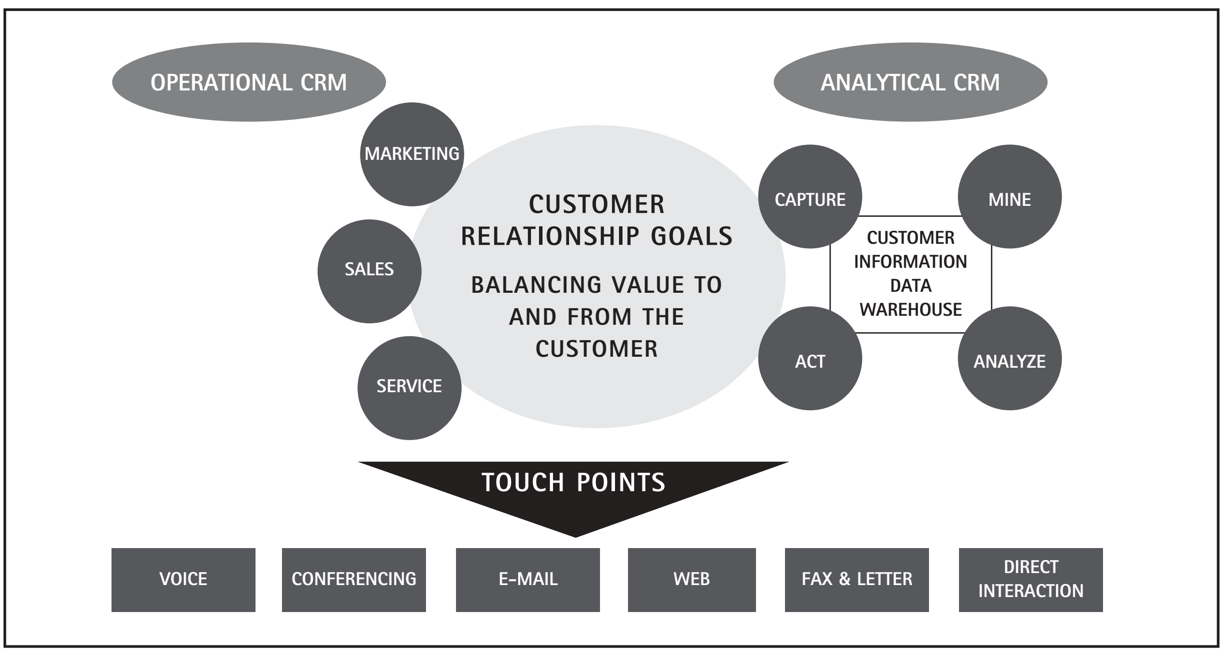


*Note: Size of circle represents magnitude of gap between the company's performance and the industry's best-in-class in meeting particular customers' needs.

Applying the VTC/VFC Principles Across Marketing, Sales, and Service

VTC/VFC analysis can be applied to initiatives generated in marketing, sales, and customer service for prioritization of projects across any touch point. In marketing, these principles can be applied to decide which program or campaign should be tackled first, whether it involves targeting prospects, data mining, campaign management, or lead distribution. For sales, forecasting and reporting may need to be prioritized against contact management, lead generation, task management, or pipeline management. Customer service may find that tracking and recording service issues should have a higher priority than call center applications or Web-based self-service.

APPLYING THE VTC/VFC PRINCIPLES ACROSS MARKETING, SALES & SERVICE



VTC and VFC Analytics

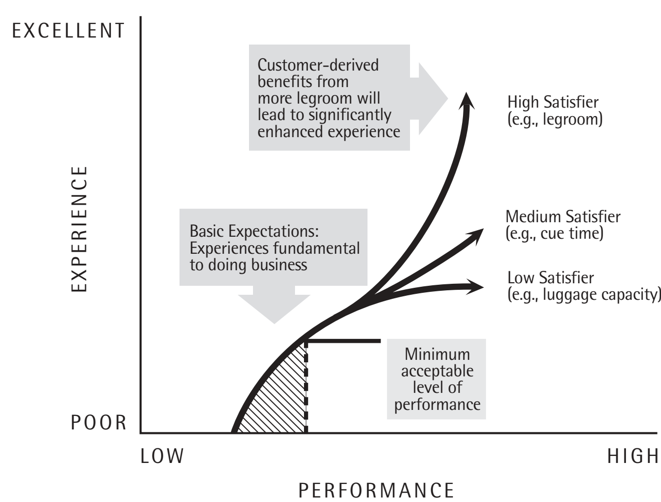
A successful prioritization process relies on analytics that quantify VTC and VFC to generate scores that can be aggregated into a scorecard that reflects the real value of each initiative in optimizing customer relationships.

“Value To” Customer Framework

To accurately measure “Value To” the customer, the experiential impact of an initiative across customer segments must be incorporated in the analysis. Experiential impacts include a customer’s perspective of the emotional, sensory, intellectual, and relational effects of the interaction with the company at a specific touch point. For example, the Westin Hotel chain’s retrofitting of its rooms with “Heavenly Beds” is an attempt to enhance customers’ sensory perceptions of the experience in its hotel rooms. An organization can gain an understanding of experiential impacts on customers by creating a customer experience hierarchy that allows the performance of the organization to be evaluated against the experience of the customer. In the customer experience hierarchy, the minimum acceptable level of performance and the customer’s basic expectations of performance can be identified for every experience. Whether the organization’s performance creates an experience that is highly satisfying, moderately satisfying, or unsatisfying to the customer will depend on whether the company’s performance exceeds the customer’s basic expectations of an experience at the identified touch point in a standard business transaction. Linking key customer segment characteristics and attributes to customer experience expectations leads to the development of experience expectations by identified customer segment. For example, an airline may offer increased luggage capacity in an attempt to enhance the customer experience. However, for a frequent business traveler, the most satisfying experience may come from having more legroom because comfort is a benefit derived from the experience that is more important than the convenience that extra luggage capacity offers that customer. Consequently, experience impacts must be examined by customer segment in order to determine whether the contemplated change in the customer experience matches the preferences and expectations of the targeted customer segment.

CUSTOMER EXPERIENCE HIERARCHY

Linking key segment characteristics and attributes to customer experience expectations leads to the development of value segment experience expectations.



Segment: Frequent Business Traveler

STAGES OF VTC ANALYSIS

The VTC methodology addresses the fundamental premise that each initiative will create or alter a customer experience at a particular touch point in the customer life cycle. The VTC analysis quantifies the premise by measurements that answer three critical questions for each initiative:

1. What is the magnitude of the initiative impact on the point experiences?

The first stage of VTC analysis identifies the touch point in the customer life cycle and defines the customer experience that is impacted by the initiative. This point experience may be directly or indirectly impacted or not impacted at all. A score of 2, 1, or 0 is then assigned to direct, indirect, or no impact, respectively. If the new initiative is an Interactive Voice Response (IVR) system, for example, designed for product support that reduces customer wait time on hold for a Customer Service Representative (CSR), the life cycle touch point is support and the point experience is directly impacted by a reduction in wait time, earning the initiative a score of 2.

2. What is the driver of the point experience?

At the second stage, the point experience is mapped to an experience driver and the driver is in turn mapped to one of the experience classes most applicable to the situation under consideration (e.g., quality, customer support, or features.) If the IVR project reduces customer wait time on hold, for example, it has an impact on queue time, which is a driver of the Customer Support experience class by facilitating access.

3. How important is the experiential impact across all customer segments?

The third stage of the analysis maps the affected experience class against the experience profiles of customer segments to assess its importance across all customer segments. This step determines whether the newly created experience represents a compelling, average, or basic experience for each customer segment. A compelling experience is one that will entice the customer to switch brands or services; an average experience is one that is commonly encountered in the situation under consideration; and a basic experience represents the minimal level of service that must be performed to maintain a relationship with a customer. A customer preference score of 3, 2, or 1 is assigned to the newly created experience if it represents a compelling, average, or basic experience, respectively. The direct impact of the IVR project on queue time that is a driver of access to Customer Support may be a compelling experience for one customer segment, an average experience for another, and a basic experience for a third.

An initial experience profile can be created for existing customer segments by soliciting information from key customer segments about their expectations at certain interactions with the company. For each customer segment, the preference for the experience class (e.g., quality, customer support, or new features) is defined by a customer preference score for each class. Consequently, the experience profile for each customer segment reflects a preference for an experience class or a mix of experience classes.

At this point, the information gathered from each stage of analysis is ready to be aggregated into a single score.

VALUE TO CUSTOMER SCORECARD

The VTC Scorecard takes the cumulative results from the three stages of analysis and aggregates them into a single VTC score. For each project, the score reflecting the magnitude of the impact on each of the customer experience classes is listed against the customer experience profile score for each customer segment. A project score is then calculated for each customer segment by multiplying the magnitude of the experience impact by the experience profile score for each customer segment. A project total is then obtained by adding the scores for each customer segment by experience class. The VTC score for a specific project is the sum of the customer segment totals. With the VTC side of the value equation quantified, the next step is to quantify the VFC side.

"Value From" Customer Analytics

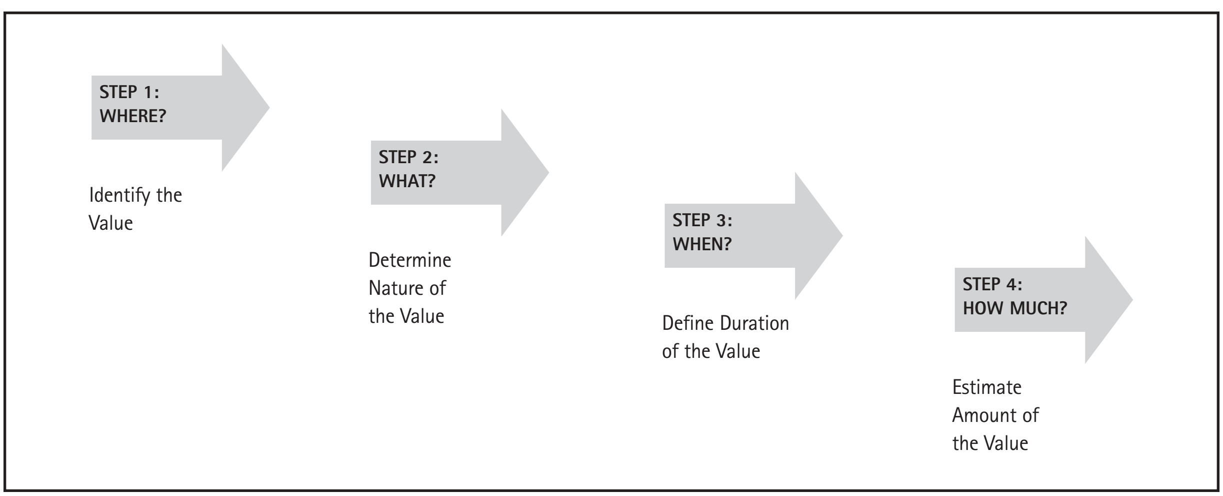
VFC analysis explores four basic valuation questions:

1. **Where?** The first step identifies the location of the value creating activity. The impact of costs and benefits are assessed at different levels of the company: enterprise, division, process, and individual.
2. **What?** This step determines the nature of the value or benefits. At this point, operating metrics are linked to financial metrics. The economic value that each initiative will provide to the organization is calculated from specific operating metrics directly impacting financial metrics.
3. **When?** At this step, the duration of the value is defined. Measurable milestones are established to map the progress of the project from initiation to completion. Progress should be easily identifiable at any time point over the project schedule by specific milestones that all parts of the organization can identify.
4. **How Much?** And finally, the costs of the value-producing activities are estimated from the identified operating metrics. The amount of value is estimated by incorporating customer metrics such as lifetime value and traditional financial metrics such as investment costs, benefit streams, net present value (NPV), and return on investment (ROI).

This analysis results in calculation of customer metrics such as lifetime value and traditional financial metrics such as NPV and ROI. The VFC score is a composite of ROI and NPV, as ROI will determine positioning relative to VFC on a VTC/VFC value matrix and NPV will reflect magnitude of impact.

VALUE FROM CUSTOMER ANALYSIS

In evaluating initiatives, four basic valuation questions should be explored.



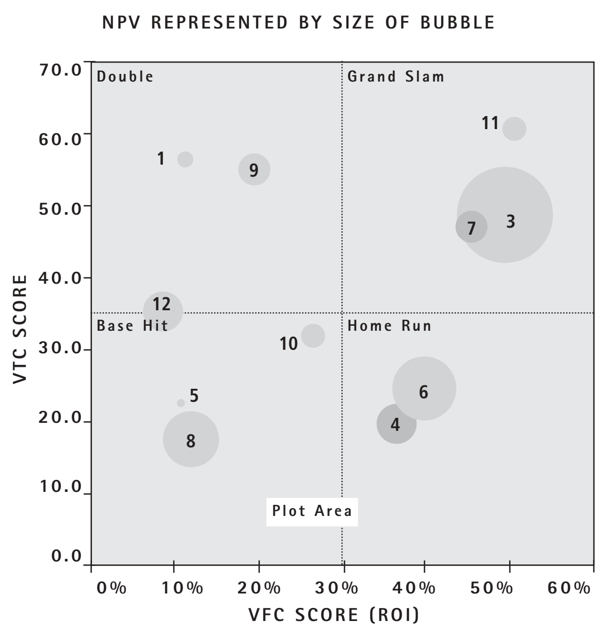
VTC/VFC Summary Scores

Using the VTC and VFC summary scores obtained from the respective analyses, all projects can be plotted on a VTC/VFC value matrix that graphically prioritizes each initiative. With the VTC score on the vertical axis, the ROI representing the VFC score on the horizontal axis, and the size of the bubble representing the NPV, the priority level for each can be visually derived.

VTC & VFC SCORES

	INITIATIVE	VTC SCORE	VFC SCORES	
			ROI	NPV
1	ONE CUSTOMER VIEW	55.1	11%	$ 55,234
2	ASSET/CONFIGURATION MGMT.	60.0	–5%	$ (2,398)
3	3RD PARTY MGMT. PROCESS DESIGN	45.5	49%	$1,213,451
4	SERVICE/WARRANTY SALES PROCESS	15.0	34%	$ 423,098
5	ADVANCED CALL ROUTING	23.0	12%	$ 12,765
6	DIFFERENTIATED SERVICE	22.7	39%	$ 753,897
7	SERVICE QUOTE & CONTRACT MGMT.	45.0	45%	$ 253,478
8	BILLING & INVOICE REDESIGN	15.8	13%	$ 652,015
9	WEB SITE ENHANCEMENTS	53.4	20%	$ 198,127
10	ENHANCED CUSTOMER ANALYTICS	31.0	25%	$ 128,361
11	SALES FORCE AUTOMATION	59.9	50%	$ 213,461
12	ORACLE MIGRATION	34.1	8%	$ 309,308

VTC & VFC GRAPHICAL PRIORITIZATION



Case Study

A leading provider of advanced wireless services for consumers and businesses operating one of the largest digital wireless networks in North America was in the process of designing, managing, and implementing a variety of initiatives within the context of its overall business transformation strategy. This strategy consisted of programs ranging from customer relationship management to the development of new products and offerings.

A sound approach to initiative prioritization was needed in order to optimize the allocation of capital to the various initiatives. The prioritization methodology was needed to enhance both the company's profitability and its relationships with its customers while maintaining strategic alignment with the overall objectives of the organization.

The wireless services provider utilized the VTC/VFC framework to prioritize initiatives and create a comprehensive roadmap encompassing all of the business transformation programs.

The company faced two key challenges in achieving its goal of developing a comprehensive prioritization framework and roadmap: 1) How to strategically prioritize long-term initiatives and 2) How to translate a list of strategically prioritized initiatives into operational tactics.

1. **How does the organization strategically prioritize long-term initiatives?** Three key areas were addressed in prioritizing long-term initiatives: Value From the Customer (VFC), Value To the Customer (VTC), and corporate and operational strategic alignment. First, the organization had to identify a portfolio of initiatives and account for both the VFC and the VTC generated by each initiative. This portfolio of initiatives was then assessed against both corporate and operational strategies to ensure alignment across strategic goals and objectives and operating tactics.
2. **How does the organization translate a list of strategically prioritized initiatives into sequenced tactics?** The organization needed a comprehensive consolidated roadmap encompassing each of the program's initiatives in order to translate the strategically prioritized initiatives into sequenced tactics. This process involved defining key capabilities across all initiatives and sequencing these capabilities based on VFC, VTC, and strategic goals while accounting for legacy dependencies, initiative interdependencies, timing, and risk.

The VTC/VFC framework enabled the wireless services provider to:

- Establish a common language and method for translating initiatives into a common set of capabilities with associated dependencies
- Build consensus among the various business units and functions within the organization based upon the objectively defined and calculated VTC and VFC factors
- Develop a flexible prioritization model that could be updated on a regular basis based upon changes in strategies, budgets, economic conditions, and customer preferences
- Delineate interrelationships among projects for optimal allocation of capital
- Perform scenario planning based upon profitability and customer impact
- Lay the foundation for tracking results and performing post-execution analysis

In leveraging the VTC/VFC framework, the company was able to narrow the number of initiatives under consideration and reallocate capital to the areas of the company that provided both the greatest return in terms of profitability and enhanced customer experience. As a result, the company reduced the total number of initiatives under consideration while increasing the overall economic return of the portfolio of projects.

Conclusion

The utilization of the VTC/VFC framework enhances a company's ability to make customer-centric investment decisions that improve both the bottom line and the customer experience. Given that this framework is based upon a quantitative approach for measuring value to and from the customer, it allows for consensus building by focusing discussion on the VTC/VFC metrics rather than individual agendas and goals.

It is possible to make your customer experiences as intimate and rewarding as those found in many sole proprietorships without compromising your company's profitability. Solid business investments require meeting customer needs. To understand and meet customer needs, companies need to gather direct input from the customer, organize the data, and estimate tangible impacts of contemplated actions. The challenge resides in leveraging the vast amount of accumulated customer data in order to quantify both the value to and from the customer to drive solid investments that both earn a return on investment and meet customer needs. Utilization of VTC and VFC analytics to generate and prioritize initiatives enhances the customer focus of the capital allocation process. The key is to balance the value provided to and derived from your customers.

About the Author

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Paul Marushka is a Vice President and Leader of eLoyalty's Marketing Solutions Service Line. He is responsible for the development, management, and promotion of eLoyalty's services focused on customer analytics, campaign management, direct marketing, lead management, and marketing resource management. He is the developer of the Customer Experience Analytics™ methodology for measuring, monitoring, and managing the customer experience in a tangible and quantifiable manner. He is a frequent speaker at conferences such as the Gartner CRM Summits, the Information Management Forum, the University of Chicago Graduate School of Business eBusiness Roundtables, and the author of several articles, including "Customer Experience Analytics," "A Value-Based Framework for Analytics," "The Evolving CRM Roadmap," "Valuing the CRM Life Cycle," and "Developing a Methodology for Measuring Customer Value." He has advised clients such as Audi Financial Services/Volkswagen Credit, Abbott Labs, AT&T Wireless, Avaya Communications, Cable & Wireless, Chase Manhattan, Franklin Templeton Investments, Federal Express, General Motors, McGraw-Hill, Motorola, R.R. Donnelley, Siemens, VWR Scientific, T. Rowe Price, Telekom Austria, Westpac, and Whirlpool in developing and assessing value-based, customer-centric strategies.

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About eLoyalty

eLoyalty is a leading management consulting, systems integration, and managed services company focused on optimizing customer interactions. With professionals in offices throughout North America and Europe, eLoyalty's broad range of enterprise Customer Relationship Management (CRM)-related services and solutions include creating customer strategies; defining technical architectures; selecting, implementing, and integrating best-of-breed CRM software applications; and providing ongoing support for multivendor systems. The combination of eLoyalty's methodologies and technical expertise enables eLoyalty to deliver the tangible economic benefits of customer loyalty for its Global 2000 clients. For more information about eLoyalty, visit www.eloyalty.com or call 877.2ELOYAL.