



Focus: Customer

by Lior Arussy

Passionate & Profitable!

The Economics of Customer Relationships

Following the release of our 2003 Customer Experience Management Global Survey, and the results that were revealed last year, we felt compelled to identify the root cause of the inherent conflict between the nature of the customer and the nature of the company. Specifically, we wanted to learn, despite the forceful articulation expressed by academics, media and consultants worldwide, why companies refuse to make the necessary investment in their customer relationships? While we suspected that the answer was tied to an overall misunderstanding and distrust of the financial upside associated with successful customer strategies, what we found this year, was even more startling.

New to the 2004 study was a section for measuring the economics of relationships. In it, we asked some pretty basic questions, such as, “Do you know the cost of a customer complaint?”, “Do you know the average annual customer value?” and “Do you know what the cost of complaint resolution is?” Amazingly enough, the answer “I Don’t Know” was circled 89, 83 and 90 percent of the time, respectively.

As it turns out, the survey results validated our hunch. The great majority of executives lack basic customer information and do not understand the costs and revenues associated with customer relationships.

Knowing and understanding the questions as laid out above is core to understanding your business and key to managing successful customer relationships.

Ignorance to Actual Costs and Revenues Associated with Customer Relationships

As mentioned above, when asked about the economics associated with managing customer relationships, a large majority of executives did not have access to basic information. Despite focused attention from academia and the media directed towards the value of existing customers and the cost inherent in obtaining new ones, companies are ignorant to many of the economics associated with their customer relationships. In light of much of the cost-cutting going on at many companies, this lack of understanding is startling. Companies continue to pay a great deal of lip-service to their customers and customer strategies yet very few of them can demonstrate long-term success in forming strong, sustainable, and profitable relationships with customers. The Strativity Group study demonstrates that despite the pick up in the economy, companies have not improved their investment in their customer relationships.

Customer relationship financial drivers such as these must be monitored by every company. In the absence of such measurements, companies ultimately miss the full potential of their customer relationships by not taking advantage of the financial opportunities associated with each. Consequentially, they cannot justify proper investment for a long-term relationship which is exactly what is needed in order to properly address customer issues, in depth.

Another critical and representative driver of customer relationship economics is Portion of Budget (the percentage of business the customer gives your company vs. what is given to your competitors). For every company and industry, these are examples of industry specific, customer relationship numbers that can be measured and tracked. The results above clearly indicate that the great majority of executives

don't get it. The most important element of business – the customer – is left unmeasured, improperly managed and under-invested in. In spite of the current trend where businesses are transforming management into a science and are measuring every element of the operation, the lack of measurement on the customer management side of the business is contradictory, and shocking.

This lack of basic understanding and subsequent absence of customer performance metrics certainly helps to explain some of the other surprising results, as revealed in the study: 60% of the respondents claim they do not deserve the loyalty of their customers! Study respondents claim that the majority of companies do not provide the tools and authority to solve problems, do not invest in their people, or base compensation on quality of service. The absence of these investments can only be explained by their association with them as being unnecessary.

It appears that the great majority of executives have blindly taken the position that maintaining passionate and committed relationships is an added cost and not a profitable way of doing business.

This myth must be defused. It is an incorrect assumption stemming from a lack of basic information. It is a critical mistake that must be rectified as soon as possible.

Companies which fail to understand the costs and revenues associated with their customer relationships will continue to treat their customers as a cost item. Lacking the ability to see the future value of a customer or the current cost of a complaint will lead companies to “skim” over customers and not invest in them over the long term. Despite the large amount of ink dedicated to the topic of existing customer value or the cost of obtaining new customers, it appears that companies have been unable to internalize this knowledge. This is especially surprising considering the ongoing cost conscious approach taken by most companies over the last several years. One would think that with such a focus on the bottom line (or the last dollar), executives would have a better understanding of the economics of their customer relationships and would operate according to a more transparent economic model.

The imperative is clear: Companies need to measure and track the numbers associated with customer value and establish benchmarks by which they can profitably manage their customer strategies. In my new book, *Passionate & Profitable, Why Customer Strategies Fail and 10 Steps to do the Right* (John Wiley & Sons, February, 2005), I argue that applying passion to your products and strategies is a far better and more profitable way to do business.

In the book I detail ten strategic steps companies should take to become more passionate and ultimately, more profitable. In addition, I've included what I believe are the 10 fatal mistakes companies make in their existing customer relationship strategies.

Passionate relationships with customers can be extremely profitable and must be embraced by any company seeking to last beyond the quarterly results. Customers will pay a premium for passionate service. As detailed in the book, this premium comes in several forms including longevity of relationship, lower cost of marketing and sales, evangelization and recommendation by word of mouth or other means, as well as actual premium price. But to get the customer strategy right, companies must start taking their relationships seriously. They must understand the financial metrics associated with these relationships and start adapting their strategies accordingly.

Perhaps executives avoid trying to obtain this understanding and knowledge because they are afraid of what they might find...Who knows? But what we do know is that no stockholder will knowingly invest in a company ignorant of the key drivers behind revenue generation.

It is time to take grab the truth by the horns, no matter how bad it may be, and do something about it. Understanding the economics of relationships will set you free and for the first time will enable you to build profitable customer strategies on a solid foundation.

Lior Arussy is the President of Strativity Group and the author of several books including the new book *Passionate & Profitable: Why Customers Strategies fail and 10 Steps to Do Them Right!* (John Wiley & Sons, 2005) Available today at Amazon.com. To learn more about customer strategies sign up for Lior's newsletter at www.StrativityGroup.com/knowledge.