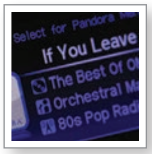
5 Creating Long-Term Loyalty Relationships

Although their enhanced capabilities can help companies earn strong customer loyalty, increased consumer capabilities pose challenges. Regardless, marketers must connect with customers—informing, engaging, and maybe even energizing them in the process. Customer-centered companies are adept at building customer relationships, not just products; they are skilled in market engineering, not just product engineering. Technology plays an increasing role for many companies and industries, offering new ways to satisfy customer needs and build loyalty. The music industry is a dramatic example.[1]



Perhaps no industry has been more thoroughly transformed than the music industry. Technological advances have changed the way consumers purchase, listen to, and share music, and music-streaming services are in a virtual arms race for their loyalty. Internet radio company Pandora has staked a claim to be the market leader with its innovative automated music discovery and recommendation service, the Music Genome Project, which has helped attract more than 200 million registered users. Based on a listener's musical selection, Pandora recommends other musical selections of a similar well-defined genre. Listener feedback to those recommendations and more than 400 different musical attributes judged by professional music lovers who pass a rigorous test are combined and analyzed to suggest future songs. Pandora launched its smart-phone app in 2008, making its service available truly "anywhere, anytime" and enriching the opportunity to provide feedback and buy music that makes it highly involving to listeners. Advertisers are able to target Pandora's audiences by key demographics and traits such as gender, birth year, zip code location, type of music, and time of day. Pandora faces steep competition, however, from Spotify, iHeartRadio, and Slacker, each of which has unique features that may drive customer preference and loyalty.

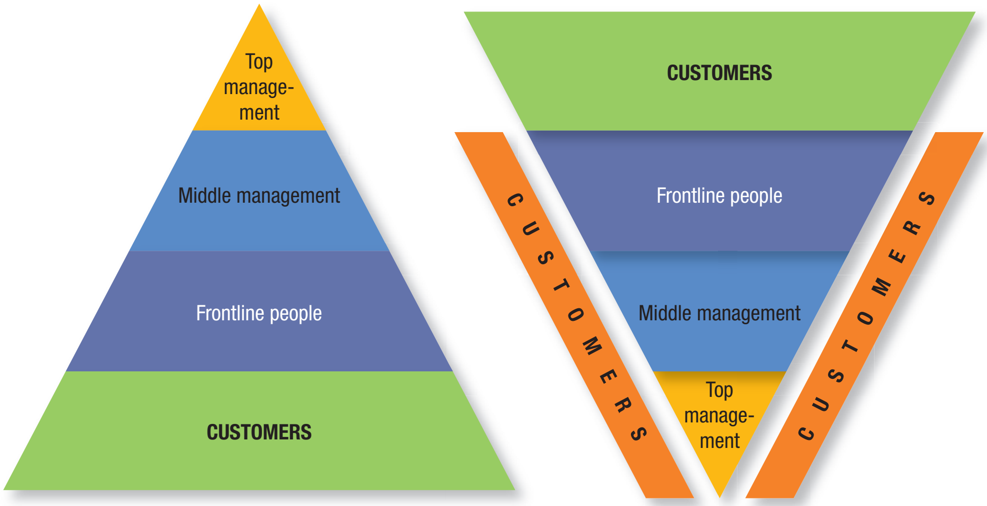
Successful marketers are those who carefully cultivate customer satisfaction and loyalty. In this chapter, we spell out the different ways they can go about winning customers and beating competitors.

Building Customer Value, Satisfaction, and Loyalty

Managers who believe the customer is the company's only true "profit center" consider the traditional organization chart in Figure 5.1(a)—a pyramid with the president at the top, management in the middle, and frontline people and customers at the bottom—obsolete.[2]

| Fig. 5.1 |

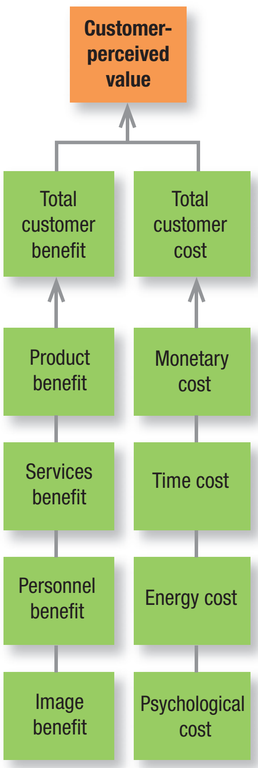
Traditional Organization versus Modern Customer-Oriented Company Organization



Successful marketing companies invert the chart to look like Figure 5.1(b). At the top are customers; next in importance are frontline people who meet, serve, and satisfy them; under them are the middle managers, whose job is to support the frontline people so they can serve customers well; and at the base is top management, whose job is to hire and support good middle managers. We have added customers along the sides of Figure 5.1(b) to indicate that managers at every level must be personally engaged in knowing, meeting, and serving customers.

Some companies have been founded on the customer-on-top business model, and customer advocacy has been their strategy—and competitive advantage—all along. With the rise of digital technologies, increasingly informed consumers expect companies to do more than connect with them, more than satisfy them, and even more than delight them. They expect companies to *listen* and *respond* to them.

When Office Depot added customer reviews to its Web site, revenue and sales conversion increased significantly. The company also incorporated review-related terms in its paid search advertising campaign. As a result of these efforts, Web site revenue and the number of new buyers visiting the site both increased by more than 150 percent.[3]



| Fig. 5.2 |

Determinants of Customer-Perceived Value

CUSTOMER-PERCEIVED VALUE

Consumers are better educated and better informed than ever, and they have the tools to verify companies' claims and seek out superior alternatives. Even the best-run companies have to be careful not to take customers for granted, as Dell found out.[4]

DELL Dell rode to success by offering low-priced computers, logistical efficiency, and after-sales service. The firm's maniacal focus on low costs has been a key ingredient in its success. When it shifted its customer-service call centers to India and the Philippines to cut costs, however, understaffing frequently led to 30-minute waits for customers. Almost half the calls required at least one transfer. To discourage customer calls, Dell even removed its toll-free service number from its Web site. With customer satisfaction slipping, while competitors matched its product quality and prices *and* offered better service, Dell's market share and stock price both declined sharply. Dell ended up hiring more North American call center employees. "The team was managing cost instead of managing service and quality," Michael Dell confesses.

How do customers ultimately make choices? They tend to be value maximizers, within the bounds of search costs and limited knowledge, mobility, and income. Customers choose—for whatever reason—the offer they believe will deliver the highest value and act on it (Figure 5.2). Whether the offer lives up to

Source: Bloomberg via Getty Images

When Dell cut costs too much on its customer service, customer satisfaction dropped and the company's stock price sank.

expectation affects customer satisfaction and the probability that the customer will purchase the product again. In one survey asking U.S. consumers "Does [Brand X] give good value for what you pay?" the top ten–scoring brands were: Subway, Cheerios, Amazon, History Channel, Ford, Discovery Channel, Lowe's, Olive Garden, YouTube, and Google.[5]

DEFINING VALUE **Customer-perceived value (CPV)** is the difference between the prospective customer's evaluation of all the benefits and costs of an offering and the perceived alternatives. **Total customer benefit** is the perceived monetary value of the bundle of economic, functional, and psychological benefits customers expect from a given market offering because of the product, service, people, and image. **Total customer cost** is the perceived bundle of costs customers expect to incur in evaluating, obtaining, using, and disposing of the given market offering, including monetary, time, energy, and psychological costs.

Customer-perceived value is thus based on the difference between benefits the customer gets and costs he or she assumes for different choices. The marketer can increase the value of the offering by raising economic, functional, or emotional benefits and/or reducing one or more costs. The customer choosing between two value offerings, V1 and V2, will favor V1 if the ratio V1:V2 is larger than one, favor V2 if the ratio is smaller than one, and be indifferent if the ratio equals one.

APPLYING VALUE CONCEPTS Suppose the buyer for a large construction company wants to buy a tractor for residential construction from either Caterpillar or Komatsu. He wants the tractor to deliver certain levels of reliability, durability, performance, and resale value. The competing salespeople carefully describe their respective offers. The buyer decides Caterpillar has greater product benefits based on his perceptions of those attributes. He also perceives differences in the accompanying services—delivery, training, and maintenance—and decides Caterpillar provides better service as well as more knowledgeable and responsive staff. Finally, he places higher value on Caterpillar's corporate image and reputation. He adds up all the economic, functional, and psychological benefits from these four sources—product, services, people, and image—and perceives Caterpillar as delivering greater customer benefits.

Does he buy the Caterpillar tractor? Not necessarily. He also examines his total cost of transacting with Caterpillar versus Komatsu, a cost that consists of more than money. As Adam Smith observed more than two centuries ago in *The Wealth of Nations*, "The real price of anything is the toil and trouble of acquiring it." Total customer cost therefore also includes the buyer's time, energy, and psychological costs expended in product acquisition, usage, maintenance, ownership, and disposal. The buyer evaluates these elements together with the monetary cost to form a total customer cost. Then he considers whether Caterpillar's total customer cost is too high compared to total customer benefits. If it is, he might choose Komatsu. The buyer will choose whichever source delivers the highest perceived value.

Now let's use this decision-making theory to help Caterpillar succeed in selling to this buyer. Caterpillar can improve its offer in three ways. First, it can increase total customer benefit by improving economic, functional, and psychological benefits of its product, services, people, and/or image. Second, it can reduce the buyer's nonmonetary costs by reducing the time, energy, and psychological investment. Third, it can reduce its product's monetary cost to the buyer.

Suppose Caterpillar concludes the buyer sees its offer as worth $20,000. Further, suppose Caterpillar's cost of producing the tractor is $14,000. This means Caterpillar's offer generates $6,000 over its cost, so the firm needs to charge between $14,000 and $20,000. If it charges less than $14,000, it won't cover its costs; if it charges more, it will price itself out of the market.

Caterpillar's market success can be attributed in part to its focus on maximizing total customer value.

Source: James Mattil/Shutterstock

Caterpillar's price will determine how much value it delivers to the buyer and how much flows to Caterpillar. If it charges $19,000, it is creating $1,000 of customer-perceived value and keeping $5,000 for itself. The lower Caterpillar sets its price, the higher the customer's perceived value and, therefore, the higher the customer's incentive to purchase. To win the sale, the firm must offer more customer-perceived value than Komatsu does.[6] Caterpillar is well aware of the importance of taking a broad view of customer value.[7]

CATERPILLAR Caterpillar has become a leading firm by maximizing total customer value in the construction equipment industry, despite challenges from a number of able competitors such as John Deere, Case, Komatsu, Volvo, and Hitachi and emerging ones such as LiuGong Machinery in China. First, Caterpillar produces high-performance equipment known for reliability and durability—key purchase considerations in heavy industrial equipment. The firm also makes it easy for customers to find the right product by providing a full line of construction equipment and a wide range of financial terms. Caterpillar maintains the largest number of independent construction-equipment dealers in the industry. These dealers all carry a complete line of Caterpillar products and are typically better trained and perform more reliably than competitors' dealers. Caterpillar has also built a worldwide parts and service system second to none in the industry. Customers recognize all the value Caterpillar creates in its offerings, allowing the firm to command a premium price 10 percent to 20 percent higher than competitors'. Caterpillar also makes strategic acquisitions to acquire new customers, such as picking up mining equipment maker Bucyrus International for $8.6 billion in 2010. Despite a recession that brought hard times to its industry and battered many of its competitors' finances, Caterpillar was one of the best-performing stocks among the 30 companies in the Dow Jones Industrial Average coming out of the recession.

Very often, managers conduct a **customer value analysis** to reveal the company's strengths and weaknesses relative to those of various competitors. The steps in this analysis are:

1. ***Identify the major attributes and benefits that customers value.*** Customers are asked what attributes, benefits, and performance levels they look for in choosing a product and vendors. Attributes and benefits should be defined broadly to encompass all the inputs to customers' decisions.[8]
2. ***Assess the quantitative importance of the different attributes and benefits.*** Customers are asked to rate the importance of different attributes and benefits. If their ratings diverge too much, the marketer should cluster them into different segments.
3. ***Assess the company's and competitors' performances on the different customer values against their rated importance.*** Customers describe where they see the company's and competitors' performances on each attribute and benefit.
4. ***Examine how customers in a specific segment rate the company's performance against a specific major competitor on an individual attribute or benefit basis.*** If the company's offer exceeds the competitor's offer on all important attributes and benefits, the company can charge a higher price (thereby earning higher profits), or it can charge the same price and gain more market share.
5. ***Monitor customer values over time.*** The company must periodically redo its studies of customer values and competitors' standings as the economy, technology, and product features change.

CHOICE PROCESSES AND IMPLICATIONS Some marketers might argue the process we have described is too rational. Suppose the customer chooses the Komatsu tractor. How can we explain this choice? Here are three possibilities.

1. ***The buyer might be under orders to buy at the lowest price.*** The Caterpillar salesperson's task is then to convince the buyer's manager that buying on price alone will result in lower long-term profits and customer value for the buyer's company.
2. ***The buyer will retire before the company realizes the Komatsu tractor is more expensive to operate.*** The buyer will look good in the short run; he is maximizing personal benefit. The Caterpillar salesperson's task is to convince other people in the customer company that Caterpillar delivers greater customer value.
3. ***The buyer enjoys a long-term friendship with the Komatsu salesperson.*** In this case, Caterpillar's salesperson needs to show the buyer that the Komatsu tractor will draw complaints from the tractor operators when they discover its high fuel cost and need for frequent repairs.

The point is clear: Buyers operate under various constraints and occasionally make choices that give more weight to their personal benefit than to the company's benefit.

Customer-perceived value is a useful framework that applies to many situations and yields rich insights. It suggests that the seller must assess the total customer benefit and total customer cost associated with each competitor's offer in order to know how its own offer rates in the buyer's mind. It also implies that the seller at a disadvantage has two alternatives: increase total customer benefit or decrease total customer cost. The former calls for strengthening or augmenting the economical, functional, and psychological benefits of the offering's product, services, personnel, and image. The latter calls for reducing the buyer's costs by reducing the price or cost of ownership and maintenance, simplifying the ordering and delivery process, or absorbing some buyer risk by offering a warranty.

DELIVERING HIGH CUSTOMER VALUE Consumers have varying degrees of loyalty to specific brands, stores, and companies. **Loyalty** has been defined as "a deeply held commitment to rebuy or repatronize a preferred product or service in the future despite situational influences and marketing efforts having the potential to cause switching behavior."[9] Table 5.1 lists brands with the highest customer loyalty, according to one 2012 survey.

The **value proposition** consists of the whole cluster of benefits the company promises to deliver; it is more than the core positioning of the offering. For example, Volvo's core positioning has been "safety," but the buyer is promised more than just a safe car; other benefits include good performance, design, and safety for the environment. The value proposition is thus a promise about the experience customers can expect from the company's market offering and their relationship with the supplier. Whether the promise is kept depends on the company's ability to manage its value delivery system. The **value delivery system** includes all the experiences the customer will have on the way to obtaining and using the offering. At the heart of a good value delivery system is a set of core business processes that help deliver distinctive consumer value.[10]

TOTAL CUSTOMER SATISFACTION

In general, **satisfaction** is a person's feelings of pleasure or disappointment that result from comparing a product or service's perceived performance (or outcome) to expectations.[11] If the performance or experience falls short of expectations, the customer is dissatisfied. If it matches expectations, the customer is satisfied. If it exceeds expectations, the customer is highly satisfied or delighted.[12]

Customer assessments of product or service performance depend on many factors, including the type of loyalty relationship the customer has with the brand.[13] Consumers often form more favorable perceptions of a product with a brand they already feel positive about. Research has also shown an asymmetric effect of product performance and expectations on satisfaction: The negative effect on customer satisfaction of failing to meet expectations is disproportionally stronger than the positive effect of exceeding expectations.[14]

Although the customer-centered firm seeks to create high customer satisfaction, that is not its ultimate goal. Increasing customer satisfaction by lowering price or increasing services may result in lower profits. The company might be able to increase its profitability by means other than increased satisfaction (for example, by improving manufacturing processes or investing more in R&D).

The company also has many stakeholders, including employees, dealers, suppliers, and stockholders. Spending more to increase customer satisfaction might divert funds from increasing the satisfaction of other "partners." Ultimately, the company must try to deliver a high level of customer satisfaction subject to also delivering acceptable levels to other stakeholders, given its total resources.

TABLE 5.1 Top 30 Brands in Customer Loyalty

Brand	Category	Rankings	
		2012	2011
Apple	Tablet	1	N/A
Amazon	Tablet	2	N/A
Apple	Smart phone	3	2
Amazon	Online retail	4	1
Apple	Computer	5	5
Samsung	Tablet	6	N/A
Call of Duty	Major league gaming	7	N/A
Samsung	Cellphone	8	4
Halo	Major league gaming	9	N/A
Twitter	Social networks	10	20
Kindle	E-reader	11	8
Mary Kay	Cosmetics	12	10
Grey Goose	Vodka	13	15
Google	Search engine	14	16
YouTube	Social networks	15	N/A
Facebook	Social networks	16	3
Dunkin' Donuts	Coffee	17	12
Zappos	Online retailer	18	6
Patron	Tequila	19	9
Crest Whitestrips	Tooth whitener	20	10
Walmart	Discount retailer	21	13
Maybelline	Cosmetics	22	14
Clinique	Cosmetics, luxury	23	34
Ketel One	Vodka	24	17
Hyundai	Automotive	25	7
Samsung	Smart phone	26	56
LG	Cellphone	27	19
Mary Kay	Facial moisturizer	28	28
Avis	Car rental	29	23
LinkedIn	Social networks	30	24

Source: "2012 Brand Keys Customer Loyalty Leaders List," www.brandkeys.com.

How do buyers form their expectations? Expectations result from past buying experience, friends' and associates' advice, public information and discourse, and marketers' and competitors' information and promises. If a company raises expectations too high, the buyer is likely to be disappointed. If it sets expectations too low, it won't attract enough buyers (although it will satisfy those who do buy).[15]

Some of today's most successful companies are raising expectations and delivering performances to match. Korean automaker Kia found success in the United States by launching low-cost, high-quality cars with enough reliability to offer 10-year, 100,000-mile warranties.

MONITORING SATISFACTION

Many companies are systematically measuring how well they treat customers, identifying the factors shaping satisfaction, and changing operations and marketing as a result.[16]

Wise firms measure customer satisfaction regularly because it is one key to customer retention.[17] A highly satisfied customer generally stays loyal longer, buys more as the company introduces new and upgraded products, talks favorably to others about the company and its products, pays less attention to competing brands and is less sensitive to price, offers product or service ideas to the company, and costs less to serve than new customers because transactions can become routine.[18]

The link between customer satisfaction and customer loyalty is not proportional, however. Suppose customer satisfaction is rated on a scale from 1 to 5. At a very low level of satisfaction (level 1), customers are likely to abandon the company and even bad-mouth it. At levels 2 to 4, customers are fairly satisfied but still find it easy to switch when a better offer comes along. At level 5, the customer is very likely to repurchase and even spread good word of mouth about the company. High satisfaction or delight creates an emotional bond with the brand or company, not just a rational preference. Xerox's senior management found its "completely satisfied" customers were six times more likely to repurchase Xerox products over the following 18 months than even its "very satisfied" customers.[19]

The company needs to recognize, however, that customers define good performance differently. Good delivery could mean early delivery, on-time delivery, or order completeness, and two customers can report being "highly satisfied" for different reasons. One may be easily satisfied most of the time, and the other might be hard to please but was pleased on this occasion.[20] It is also important to know how satisfied customers are with competitors in order to assess "share of wallet" or how much of the customer's spending the company's brand enjoys: The more highly the consumer ranks the company's brand in terms of satisfaction and loyalty, the more the customer is likely to spend on the brand.[21]

MEASUREMENT TECHNIQUES *Periodic surveys* can track customers' overall satisfaction directly and ask additional questions to measure repurchase intention, likelihood or willingness to recommend the company and brand to others, and specific attribute or benefit perceptions likely to be related to customer satisfaction.

The University of Michigan's Claes Fornell has developed the American Customer Satisfaction Index (ACSI) to measure consumers' perceived satisfaction with different firms, industries, economic sectors, and national economies.[22] Research has shown a strong and consistent association between customer satisfaction, as measured by ACSI, and firm financial performance in terms of ROI, sales, long-term firm value (Tobin's Q), and other metrics.[23] Table 5.2 displays some of the 2014 ACSI leaders. "Marketing Insight: Net Promoter and Customer Satisfaction" describes why some companies believe just one well-designed question is all that is necessary to assess customer satisfaction.[24]

Companies need to monitor their competitors' performance too. They can monitor their *customer loss rate* and contact those who have stopped buying or who have switched to another supplier to find out why. Finally, as described in Chapter 3, companies can hire *mystery shoppers* to pose as potential buyers and report on strong and weak points experienced in buying the company's and competitors' products. Managers themselves can enter company and competitor sales situations where they are unknown and experience firsthand the treatment they receive, or they can phone their own company with questions and complaints to see how employees handle the calls.

INFLUENCE OF CUSTOMER SATISFACTION For customer-centered companies, customer satisfaction is both a goal and a marketing tool. Companies need to be especially concerned with their customer satisfaction level today because the Internet allows consumers to quickly spread both good and bad word of mouth to the rest of the world. Some customers set up their own Web sites to air grievances and galvanize protest, targeting high-profile brands such as United Airlines, Home Depot, and Mercedes-Benz.[25]

Companies that do achieve high customer satisfaction ratings make sure their target market knows it. Once they achieved number-one status in their category on J. D. Power's customer satisfaction ratings, Hyundai, American Express, Medicine Shoppe (a chain pharmacy), and Alaska Airways, among others, communicated that fact.

TABLE 5.2 2014 ACSI Scores by Industry

Industry	Firm	Score
Airlines	Jet Blue	79
Apparel	Levi-Strauss, V.F.	82
Automobiles & Light Vehicles	Mercedes-Benz	84
Banks	JPMorgan Chase	76
Breweries	Anheuser-Busch InBev	81
Cellular Telephones	Samsung	81
Department & Discount Stores	Nordstrom	83
Fixed Line Telephone Service	Verizon	73
Food Manufacturing	H. J. Heinz, Quaker & General Mills	87
Health Insurance	Blue Cross and Blue Shield	74
Hotels	Marriott	81
Internet Brokerage	Charles Schwab	84
Internet News & Information	FOXNews.com & USATODAY.com	76
Internet Portals & Search Engines	Google	83
Internet Retail	Amazon	88
Internet Travel	Orbitz	77
Life Insurance	New York Life	80
Personal Care & Cleaning Products	Clorox, Colgate-Palmolive & Unilever	85
Personal Computers	Apple	84
Soft Drinks	Dr Pepper Snapple	86
Supermarkets	Publix	86
Wireless Telephone Service	Verizon Wireless	75

Source: ACSI LLC, www.theacsi.org.

PRODUCT AND SERVICE QUALITY

Satisfaction will also depend on product and service quality. What exactly is quality? Various experts have defined it as “fitness for use,” “conformance to requirements,” and “freedom from variation.” We will use the American Society for Quality’s definition: **Quality** is the totality of features and characteristics of a product or service that bear on its ability to satisfy stated or implied needs.[26] This is clearly a customer-centered definition. We can say the seller has delivered quality whenever its product or service meets or exceeds the customers’ expectations.

A company that satisfies most of its customers’ needs most of the time is called a high-quality company, but we need to distinguish between *conformance* quality and *performance* quality (or grade). A Lexus provides higher performance quality than a Hyundai: The Lexus rides more smoothly, accelerates faster, and runs marketing insight

Net Promoter and Customer Satisfaction

Many companies make measuring customer satisfaction a top priority, but how should they go about doing it? Bain's Frederick Reichheld suggests only one customer question really matters: "How likely is it that you would recommend this product or service to a friend or colleague?"

Reichheld was inspired in part by the experiences of Enterprise Rent-A-Car. When the company cut its customer satisfaction survey in 1998 from 18 questions to two—one about the quality of the rental experience and the other about the likelihood customers would rent from the company again—it found those who gave the highest ratings to their rental experience were three times as likely to rent again than those who gave the second-highest rating. The firm also found that diagnostic information managers collected from dissatisfied customers helped it fine-tune its operations.

In a typical Net Promoter survey that follows Reichheld's thinking, customers are given a 1-to-10 scale on which to rate their likelihood of recommending the company. Marketers then subtract *Detractors* (those who gave a 0 to 6) from *Promoters* (those who gave a 9 or 10) to arrive at the Net Promoter Score (NPS). Customers who rate the brand with a 7 or 8 are deemed *Passively Satisfied* and are not included. A typical set of NPS scores falls in the 10 percent to 30 percent range, but world-class companies can score over 50 percent. Some firms with top NPS scores in 2014 included USAA (82 percent), Amazon (64 percent), Southwest (62 percent), Wegmans (61 percent), Apple (72 percent), and Costco (82 percent).

Reichheld has picked up many believers through the years. American Express, Dell, and Microsoft, among others, have all adopted the NPS metric. GE has tied 20 percent of its managers' bonuses to its NPS scores. When the European unit of GE Healthcare scored low, follow-up research revealed that response times to customers were a major problem. After it overhauled its call center and put more specialists in the field, GE Healthcare's Net Promoter scores jumped 10 to 15 points. Philips has focused on engaging Promoters as well as addressing the concerns of Detractors, developing a Reference Promoter program to get customers willing to recommend the brand to actually do so through taped testimonials.

Reichheld says he developed NPS in response to overly complicated—and thus ineffective—customer surveys. So it's not surprising that client firms praise its simplicity and strong relationship to financial performance. When Intuit applied Net Promoter to its TurboTax product, feedback revealed dissatisfaction with the software's rebate procedure. After Intuit dropped the proof-of-purchase requirement, sales jumped 6 percent.

Net Promoter is not without critics. A common criticism is that many different patterns of responses may lead to the same NPS. For example, NPS equals 20 percent when Promoters equal 20 percent, Passives equal 80 percent, and Detractors equal 0 percent, as well as when Promoters equal 60 percent, Passives equal 0 percent, and Detractors equal 40 percent, but the managerial implications of the two patterns of responses are very different. Another common criticism is that it is not a useful predictor of future sales or growth because it ignores important cost and revenue considerations.

Others question its actual research support. One comprehensive academic study of 21 firms and more than 15,000 consumers in Norway failed to find NPS superior to any other metrics such as the ACSI measure. Some have criticized both NPS and ACSI measures for not fully accounting for ex-customers or those who were never customers. Peoples' opinions about any of the single items or indices measuring customer satisfaction depend in part on how they value the trade-off between simplicity and complexity.

Sources: Fred Reichheld, *Ultimate Question: For Driving Good Profits and True Growth* (Cambridge, MA: Harvard Business School Press, 2006); Fred Reichheld, "The One Number You Need to Grow," *Harvard Business Review*, December 2003; Neil A. Morgan and Lopo Leotte Rego, "The Value of Different Customer Satisfaction and Loyalty Metrics in Predicting Business Performance," *Marketing Science* 25 (September–October 2006), pp. 426–39; Timothy L. Keiningham, Lerzan Aksoy, Bruce Cooil, and Tor W. Andreassen, "Linking Customer Loyalty to Growth," *MIT Sloan Management Review* (Summer 2008), pp. 51–57; Suhail Khan, "How Philips Uses Net Promoter Scores to Understand Customers," *HBR Blog Network*, May 10, 2011; Robert East, Jenni Romaniuk, and Wendy Lomax, "The NPS and ACSI: A Critique and an Alternative Metric," *International Journal of Market Research* 53, no. 3 (2011), pp. 327–45; Randy Hanson, "Life after NPS," *Marketing Research* (Summer 2011), pp. 8–11; Jenny van Doorn, Peter S. H. Leeflang, and Marleen Tijs, "Satisfaction as a Predictor of Future Performance: A Replication," *International Journal of Research in Marketing* 30 (September 2013), pp. 314–18; www.satmetrix.com.

problem-free longer. Yet both a Lexus and a Hyundai deliver the same conformance quality if all the units deliver their promised quality.

IMPACT OF QUALITY Product and service quality, customer satisfaction, and company profitability are intimately connected. Higher levels of quality result in higher levels of customer satisfaction, which support higher prices and (often) lower costs. Studies have shown a high correlation between relative product quality and company profitability.[27] The drive to produce goods that are superior in world markets has led some countries to recognize or award prizes to companies that exemplify the best quality practices, such as the Deming Prize in Japan, the Malcolm Baldrige National Quality Award in the United States, and the European Quality Award.

Companies that have lowered costs to cut corners have paid the price when the quality of the customer experience suffers. British Airways also encountered turbulence when it became overly focused on cost cutting.[28]

Enterprise Rent-A-Car found its customer satisfaction surveys were more effective with just two questions.

Source: UIG via Getty Images

BRITISH AIRWAYS Since 2012, British Airways has won no less than 35 major awards for its quality of service. Most recently, the airline won Best Airline, Best Short Haul Carrier, and Best Frequent Flyer Program at the Business Traveler Awards. In 2014, British Airways also scooped the Times Travel Award for Best Airline, the Condé Nast Traveller Award for Short Haul Airline of the Year, several Daily Telegraph awards, and the renowned Chinese Travel Industry Award for Best European Airline and the Superbrands Award for Consumer Superbrand.

For many global brands, such as British Airways, quality service is at the center of all their activities, but recognition of their efforts tends to come periodically since they are perceived as leaders in one year and ignored the next.

British Airways celebrated its 90th anniversary in 2009, as part of the International Airlines Group; it now has 40,000 employees including 15,000 cabin crew members, 3,600 pilots, and 5,500 engineers.

All this is in sharp contrast with the problems British Airways suffered between 1996 and 2009 when sharp budget cuts led to job losses, low employee morale, and strikes. Punctuality, customer service, and baggage handling all suffered during this time.

Total quality is everyone's job, just as marketing is everyone's job. Nevertheless, marketing plays an especially important role in helping companies identify and deliver high-quality goods and services to target customers. How do marketers help?

- They correctly identify customers' needs and requirements.
- They communicate customer expectations properly to product designers.
- They make sure customers' orders are filled correctly and on time.
- They check that customers have received proper instructions, training, and technical assistance in the use of the product.
- They stay in touch with customers after the sale to ensure they are, and remain, satisfied.
- They gather customer ideas for product and service improvements and convey them to the appropriate departments.

When marketers do all this, they make substantial contributions to total quality management and customer satisfaction as well as to customer and company profitability.

Maximizing Customer Lifetime Value

Ultimately, marketing is the art of attracting and keeping profitable customers. Yet every company loses money on some of its customers. The well-known 80–20 rule states that 80 percent or more of the company's profits come from the top 20 percent of its customers. Some cases may be more extreme—the most profitable 20 percent of customers (on a per capita basis) may contribute as much as 150 to 300 percent of profitability. The least profitable 10 to 20 percent, on the other hand, can actually reduce profits between 50 and 200 percent per account,

| Fig. 5.3 |

Customer-Product Profitability Analysis

with the middle 60 to 70 percent breaking even.[29] The implication is that a company could improve its profits by "firing" its worst customers.

Companies need to concern themselves with Return on Customer (ROC) and how efficiently they create value from the customers and prospects available.[30] It's not always the company's largest customers who demand considerable service and deep discounts or who yield the most profit. The smallest customers pay full price and receive minimal service, but the costs of transacting with them can reduce their profitability. Midsize customers who receive good service and pay nearly full price are often the most profitable.

CUSTOMER PROFITABILITY

A **profitable customer** is a person, household, or company that over time yields a revenue stream exceeding by an acceptable amount the company's cost stream for attracting, selling, and serving that customer. Note the emphasis is on the *lifetime* stream of revenue and cost, not the profit from a particular transaction.[31] Marketers can assess customer profitability individually, by market segment, or by channel.

Many companies measure customer satisfaction, but few measure individual customer profitability.[32] Banks claim this is a difficult task because each customer uses different banking services and the transactions are logged in different departments. However, the number of unprofitable customers in their customer database has appalled banks that have succeeded in linking customer transactions. Some report losing money on more than 45 percent of their retail customers.

CUSTOMER PROFITABILITY ANALYSIS A useful type of profitability analysis is shown in Figure 5.3.[33] Customers are arrayed along the columns and products along the rows. Each cell contains a symbol representing the profitability of selling that product to that customer. Customer 1 is very profitable; he buys two profit-making products (P1 and P2). Customer 2 yields mixed profitability; she buys one profitable product (P1) and one unprofitable product (P3). Customer 3 is a losing customer because he buys one profitable product (P1) and two unprofitable products (P3 and P4).

What can the company do about customers 2 and 3? (1) It can raise the price of its less profitable products or eliminate them, or (2) it can try to sell customers 2 and 3 its profit-making products. Unprofitable customers who defect should not concern the company. In fact, the company should encourage them to switch to competitors.

Customer profitability analysis (CPA) is best conducted with the tools of an accounting technique called **activity-based costing (ABC).** ABC accounting tries to identify the real costs associated with serving each customer—the costs of products and services based on the resources they consume. The company estimates all revenue coming from the customer, less all costs.

With ABC, the costs in a business-to-business setting should include the cost not only of making and distributing the products and services but also of taking phone calls from the customer, traveling to visit the customer, paying for entertainment and gifts—all the company's resources that go into serving that customer. ABC also allocates indirect costs like clerical costs, office expenses, supplies, and so on, to the activities that use them, rather than in some proportion to direct costs. Both variable and overhead costs are tagged back to each customer.

Companies that fail to measure their costs correctly are also not measuring their profit correctly and are likely to misallocate their marketing effort. The key to effectively employing ABC is to define and judge "activities" properly. One time-based solution calculates the cost of one minute of overhead and then decides how much of this cost each activity uses.[34]

MEASURING CUSTOMER LIFETIME VALUE

The case for maximizing long-term customer profitability is captured in the concept of customer lifetime value.[35] **Customer lifetime value (CLV)** describes the net present value of the stream of future profits expected over the customer's lifetime purchases. The company must subtract from its expected revenues the expected costs of attracting, selling, and servicing the account of that customer, applying the appropriate discount rate (say, between 10 and 20 percent, depending on cost of capital and risk attitudes). Lifetime value calculations for a product or service can add up to tens of thousands of dollars or even run to six figures.[36]

Many methods exist to measure CLV.[37] "Marketing Memo: Calculating Customer Lifetime Value" illustrates one. CLV calculations provide a formal quantitative framework for planning customer investment and help marketers adopt a long-term perspective. One challenge, however, is to arrive at reliable cost and revenue estimates. Marketers who use CLV concepts must also take into account the short-term, brand-building marketing activities that help increase customer loyalty. One firm that has excelled in taking a short-run and long-run view of customer loyalty is Harrah's.[38]

HARRAH'S Harrah's Entertainment, led by one-time academic Gary Loveman, has gone in a different direction from the big players in the Las Vegas gaming industry whose business models are based on building bigger and more opulent casinos. Back in 1997, Harrah's launched a pioneering loyalty program that pulled all customer data into a centralized warehouse and then ran sophisticated analyses to better understand the value of the investments the casino made in its customers. Harrah's has more than 40 million active members in its Total Rewards loyalty program, a system it has fine-tuned to achieve near-real-time analysis: As customers interact with slot machines, check into casinos, or buy meals, they receive reward offers—food vouchers or gambling credits, for example—based on predictive analyses from its database. Harrah's spends $100 million a year on information technology. The company has now identified hundreds of highly specific customer segments, and by targeting offers to each of them, it can almost double its share of customers' gaming budgets and generate $6.4 billion annually (80 percent of its gaming revenue). Research has shown that contrary to conventional wisdom, the most profitable customers are not the jet-setting high rollers, but older slot machine players. Harrah's also learned to dramatically cut back on its traditional ad spending, largely replacing it with direct mail and e-mail—a good customer may receive as many as 150 pieces in a year. Harrah's also rewards staff and bases compensation in part on customer service scores. To better fine-tune its Web sites and online ads, Harrah's monitors customer reviews and comments on TripAdvisor.com as well as social media sites such as Twitter and Facebook. After the company made changes to reflect customer interest in hotel amenities and the iconic views of the Las Vegas strip from its Paris Las Vegas hotel and casino, online bookings increased by double digits. Data from the Total Rewards program even influenced Harrah's decision to buy Caesars Entertainment, when company research revealed that most of Harrah's customers who visited Las Vegas without staying at a Harrah's-owned hotel were going to Caesars Palace. Harrah's latest loyalty innovation is a mobile marketing program that sends time-based and location-based offers to customers' mobile devices in real time.

ATTRACTING AND RETAINING CUSTOMERS

Companies seeking to expand profits and sales must invest time and resources searching for new customers. To generate leads, they advertise in media that will reach new prospects, send direct mail and e-mails to possible new prospects, send their salespeople to participate in trade shows where they might find new leads, purchase names from list brokers, and so on.

Different acquisition methods yield customers with varying CLVs. One study showed that customers acquired through the offer of a 35 percent discount had about one-half the long-term value of customers acquired without any discount.[39] Many of these customers were more interested in the offer than in the product itself.

Similarly, many local restaurants, car wash services, beauty salons, and dry cleaners have launched "daily deal" campaigns from Groupon and LivingSocial to attract new customers. Unfortunately, these campaigns have sometimes turned out to be unprofitable in the long run because coupon users were not easily converted into loyal customers.[40]

Source: AFP/Getty Images

Harrah's uses sophisticated customer analytics to guide its marketing activities, including filling rooms in its Paris Las Vegas hotel and casino.

marketing memo

Calculating Customer Lifetime Value

Researchers and practitioners have used many different approaches for modeling and estimating CLV. Columbia's Don Lehmann and Harvard's Sunil Gupta recommend the following formula to estimate the CLV for a not-yet-acquired customer:

$$CLV = \sum_{t=0}^{T} \frac{(p_t - c_t)\, r_t}{(1+i)^t} - AC$$

where p_t = price paid by a consumer at time t,
c_t = direct cost of servicing the customer at time t,
i = discount rate or cost of capital for the firm,
r_t = probability of customer repeat buying or being "alive" at time t,
AC = acquisition cost, and
T = time horizon for estimating CLV.

A key decision is what time horizon to use for estimating CLV. Typically, three to five years is reasonable. With this information and estimates of other variables, we can calculate CLV using spreadsheet analysis.

Gupta and Lehmann illustrate their approach by calculating the CLV of 100 customers over a 10-year period (see Table 5.3). In this example, the firm acquires 100 customers with an acquisition cost per customer of $40. Therefore, in year 0, it spends $4,000. Some of these customers defect each year. The present value of the profits from this cohort of customers over 10 years is $13,286.52. The net CLV (after deducting acquisition costs) is $9,286.52, or $92.87 per customer.

Using an infinite time horizon avoids having to select an arbitrary time horizon for calculating CLV. In the case of an infinite time horizon, if margins (price minus cost) and retention rates stay constant over time, the future CLV of an existing customer simplifies to the following:

$$CLV = \sum_{t=1}^{\infty} \frac{mr^t}{(1+i)^t} = m\frac{r}{(1+i-r)}$$

In other words, CLV simply becomes margin (m) times a *margin multiple* $[r/(1+i-r)]$.

Table 5.4 shows the margin multiple for various combinations of r and i and a simple way to estimate CLV of a customer. When retention rate is 80 percent and discount rate is 12 percent, the margin multiple is about two and a half. Therefore, the future CLV of an existing customer in this scenario is simply his or her annual margin multiplied by 2.5.

Sources: Sunil Gupta and Donald R. Lehmann, "Models of Customer Value," Berend Wierenga, ed., *Handbook of Marketing Decision Models* (Berlin, Germany: Springer Science and Business Media, 2007); Sunil Gupta and Donald R. Lehmann, "Customers as Assets," *Journal of Interactive Marketing* 17, no. 1 (Winter 2006), pp. 9–24; Sunil Gupta and Donald R. Lehmann, *Managing Customers as Investments* (Upper Saddle River, NJ: Wharton School Publishing, 2005); Peter Fader, Bruce Hardie, and Ka Lee, "RFM and CLV: Using Iso-Value Curves for Customer Base Analysis," *Journal of Marketing Research* 42, no. 4 (November 2005), pp. 415–30; Sunil Gupta, Donald R. Lehmann, and Jennifer Ames Stuart, "Valuing Customers," *Journal of Marketing Research* 41, no. 1 (February 2004), pp. 7–18.

TABLE 5.3 A Hypothetical Example to Illustrate CLV Calculations

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Number of Customers	100	90	80	72	60	48	34	23	12	6	2
Revenue per Customer		100	110	120	125	130	135	140	142	143	145
Variable Cost per Customer		70	72	75	76	78	79	80	81	82	83
Margin per Customer		30	38	45	49	52	56	60	61	61	62
Acquisition Cost per Customer	40										
Total Cost or Profit	–4,000	2,700	3,040	3,240	2,940	2,496	1,904	1,380	732	366	124
Present Value	–4,000	2,454.55	2,512.40	2,434.26	2,008.06	1,549.82	1,074.76	708.16	341.48	155.22	47.81

TABLE 5.4 Margin Multiple

	Discount Rate			
Retention Rate	**10%**	**12%**	**14%**	**16%**
60%	1.20	1.5	1.11	1.07
70%	1.75	1.67	1.59	1.52
80%	2.67	2.50	2.35	2.22
90%	4.50	4.09	3.75	3.46

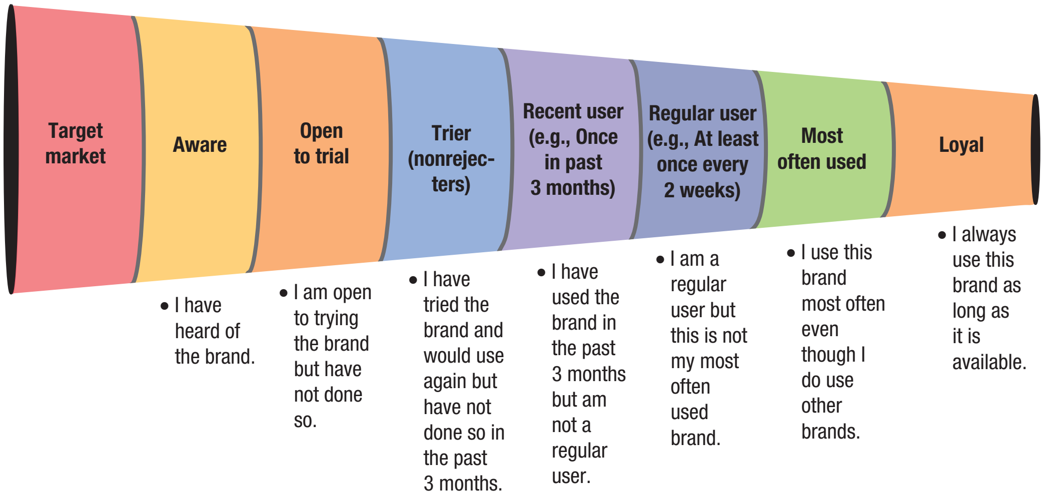
Promotional campaigns that reinforce the value of the brand, even if targeted to the already loyal, may be more likely to attract higher-value new customers. Two-thirds of the considerable growth spurred by UK mobile communication leader O2's loyalty strategy was attributed to recruitment of new customers; the remainder came from reduced defection.[41]

REDUCING DEFECTION It is not enough to attract new customers; the company must also keep them and increase their business.[42] Too many companies suffer from high **customer churn** or defection. Adding customers here is like adding water to a leaking bucket.

Cellular carriers and cable TV operators are plagued by "spinners," customers who switch carriers at least three times a year looking for the best deal. Many carriers lose 25 percent of their subscribers each year, at an estimated cost of $2 billion to $4 billion. Defecting customers cite unmet needs and expectations, poor product/service quality and high complexity, and billing errors.[43]

To reduce the defection rate, the company must:

1. *Define and measure its retention rate.* For a magazine, subscription renewal rate is a good measure of retention. For a college, it could be first- to second-year retention rate or class graduation rate.
2. *Distinguish the causes of customer attrition and identify those that can be managed better.* Not much can be done about customers who leave the region or go out of business, but poor service, shoddy products, and high prices can all be addressed.[44]
3. *Compare the lost customer's lifetime value to the costs of reducing the defection rate.* As long as the cost to discourage defection is lower than the lost profit, spend the money to try to retain the customer.



| Fig. 5.4 |

The Marketing Funnel

RETENTION DYNAMICS Figure 5.4 shows the main steps in attracting and retaining customers, imagined in terms of a funnel, and some sample questions to measure customer progress through the funnel. The **marketing funnel** identifies the percentage of the potential target market at each stage in the decision process, from merely aware to highly loyal. Consumers must move through each stage before becoming loyal customers. Some marketers extend the funnel to include loyal customers who are brand advocates or even partners with the firm.

By calculating *conversion rates*—the percentage of customers at one stage who move to the next—the funnel allows marketers to identify any bottleneck stage or barrier to building a loyal customer franchise. If the percentage of recent users is significantly lower than triers, for instance, something might be wrong with the product or service that prevents repeat buying.

The funnel also emphasizes how important it is not just to attract new customers but to retain and cultivate existing ones. Satisfied customers are the company's *customer relationship capital.* If the company were sold, the acquiring company would pay not only for the plant and equipment and brand name but also for the delivered *customer base,* the number and value of customers who will do business with the new firm. Consider these data about customer retention:[45]

- Acquiring new customers can cost five times more than satisfying and retaining current ones. It requires a great deal of effort to induce satisfied customers to switch from their current suppliers.
- The average company loses 10 percent of its customers each year.
- A 5 percent reduction in the customer defection rate can increase profits by 25 percent to 85 percent, depending on the industry.
- Profit rate tends to increase over the life of the retained customer due to increased purchases, referrals, price premiums, and reduced operating costs to service.

Source: Courtesy of Whole Foods Market. "Whole Foods Market" is a registered trademark of Whole Foods Market IP, L.P.

Whole Foods builds customer loyalty through its skillful procurement and merchandising of natural and organic foods.

MANAGING THE CUSTOMER BASE Customer profitability analysis and the marketing funnel help marketers decide how to manage groups of customers that vary in loyalty, profitability, risk, and other factors.[46] A key driver of shareholder value is the aggregate value of the customer base. Winning companies improve that value by excelling at strategies like the following:

- ***Reducing the rate of customer defection.*** Selecting and training employees to be knowledgeable and friendly increases the likelihood that customers' shopping questions will be answered satisfactorily. Whole Foods, the world's largest retailer of natural and organic foods, woos customers with a commitment to market the best foods and a team concept for employees.
- ***Increasing the longevity of the customer relationship.*** The more engaged with the company, the more likely a customer is to stick around. Nearly 65 percent of new Honda purchases replace an older Honda. Drivers cited Honda's reputation for creating safe vehicles with high resale value. Seeking consumer advice can be an effective way to engage consumers with a brand and company.[47]
- ***Enhancing the growth potential of each customer through "share of wallet," cross-selling, and up-selling.***[48] Sales from existing customers can be increased with new offerings and opportunities. Harley-Davidson sells more than motorcycles and accessories like gloves, leather jackets, helmets, and sunglasses. Its dealerships sell more than 3,000 items of clothing—some even have fitting rooms. Licensed goods sold by others range from predictable items (shot glasses, cue balls, and Zippo cigarette lighters) to the more surprising (cologne, dolls, and cell phones). Cross-selling isn't profitable if the targeted customer requires a lot of services for each product, generates a lot of product returns, cherry-picks promotions, or limits total spending across all products.[49]
- ***Making low-profit customers more profitable or terminating them.*** To avoid trying to terminate them, marketers can instead encourage unprofitable customers to buy more or in larger quantities, forgo certain features or services, or pay higher amounts or fees.[50] Banks, phone companies, and travel agencies all now charge for once-free services to ensure minimum revenue levels from these customers. Firms can also discourage those with questionable profitability prospects. Progressive Insurance screens customers and diverts the potentially unprofitable to competitors.[51] However, "free" customers who pay little or nothing and are subsidized by paying customers—as in print and online media, employment and dating services, and shopping malls—may still create useful direct and indirect network effects, an important function.[52]
- ***Focusing disproportionate effort on high-profit customers.*** The most profitable customers can be treated in a special way. Thoughtful gestures such as birthday greetings, small gifts, or invitations to special sports or arts events can send them a strong positive signal.

BUILDING LOYALTY

Companies that want to form strong, tight connections to customers should heed some specific considerations (see Figure 5.5). One set of researchers sees retention-building activities as adding financial benefits, social benefits, or structural ties.[53] Next we describe three marketing activities that improve loyalty and retention.

INTERACT CLOSELY WITH CUSTOMERS Connecting customers, clients, patients, and others directly with company employees is highly motivating and informative. End users can offer tangible proof of the positive impact of the company's products and services, express appreciation for employee contributions, and elicit empathy. A brief visit from a student who had received a scholarship motivated university fundraisers to increase their weekly productivity by 400 percent; a patient's photograph inspired radiologists to improve the accuracy of their diagnostic findings by 46 percent.[54]

| Fig. 5.5 |

Forming Strong Customer Bonds

- Create superior products, services, and experiences for the target market.
- Get cross-departmental participation in planning and managing the customer satisfaction and retention process.
- Integrate the "Voice of the Customer" to capture their stated and unstated needs or requirements in all business decisions.
- Organize and make accessible a database of information on individual customer needs, preferences, contacts, purchase frequency, and satisfaction.
- Make it easy for customers to reach appropriate company staff and express their needs, perceptions, and complaints.
- Assess the potential of frequency programs and club marketing programs.
- Run award programs recognizing outstanding employees.

Listening to customers is crucial to customer relationship management. Some companies have created an ongoing mechanism that keeps their marketers permanently plugged in to frontline customer feedback.

- Deere & Company, which makes John Deere tractors and has a superb record of customer loyalty—nearly 98 percent annual retention in some product areas—has used retired employees to interview defectors and customers.[55]
- Chicken of the Sea has 80,000 members in its Mermaid Club, a core-customer group that receives special offers, health tips and articles, new product updates, and an informative e-newsletter. In return, club members provide valuable feedback on what the company is doing and thinking of doing. Their input has helped design the brand's Web site, develop messages for TV advertising, and craft the look and text on the packaging.[56]
- Build-A-Bear Workshop uses a "Cub Advisory Board" as a feedback and decision-input body. The board is made up of twenty 5- to 16-year-olds who review new-product ideas and give a "paws up or down." Many products in the stores are customer ideas.[57]

But listening is only part of the story. It is also important to be a customer advocate and, as much as possible, take the customers' side and understand their point of view.[58]

DEVELOP LOYALTY PROGRAMS **Frequency programs (FPs)** are designed to reward customers who buy frequently and in substantial amounts. They can help build long-term loyalty with high CLV customers, creating cross-selling opportunities in the process. Pioneered by the airlines, hotels, and credit card companies, FPs now exist in many other industries. Most supermarket and drug store chains offer price club cards that grant discounts on certain items.

Typically, the first company to introduce an FP in an industry gains the most benefit, especially if competitors are slow to respond. After competitors react, FPs can become a financial burden to all the offering companies, but some companies are more efficient and creative in managing them. Some FPs generate rewards in a way that locks customers in and creates significant switching costs. FPs can also produce a psychological boost and a feeling of being special and elite that customers value.[59]

Club membership programs attract and keep those customers responsible for the largest portion of business. Clubs can be open to everyone who purchases a product or service or limited to an affinity group or those willing to pay a small fee. Although open clubs are good for building a database or snagging customers from competitors, limited membership is a more powerful long-term loyalty builder. Fees and membership conditions prevent those with only a fleeting interest in a company's products from joining.

Apple encourages owners of its computers to form local Apple user groups. There are hundreds of groups, ranging in size from fewer than 30 members to more than 1,000. The groups provide Apple owners with opportunities to learn more about their computers, share ideas, and get product discounts. They sponsor special activities and events and perform community service. A visit to Apple's Web site will help a customer find a nearby user group.[60]

CREATE INSTITUTIONAL TIES The company may supply business customers with special equipment or computer links that help them manage orders, payroll, and inventory. Customers are less inclined to switch to another supplier when it means high capital costs, high search costs, or the loss of loyal-customer discounts. McKesson Corporation, a leading pharmaceutical wholesaler, invested millions of dollars in EDI (Electronic Data Interchange) capabilities to help its independent-pharmacy customers manage inventory, order-entry processes, and shelf space. Another example is Milliken & Company, which provides proprietary software programs, marketing research, sales training, and sales leads to loyal customers.

BRAND COMMUNITIES

Thanks to the Internet, companies are interested in collaborating with consumers to create value through communities built around brands. A **brand community** is a specialized community of consumers and employees whose identification and activities focus around the brand.[61] Three characteristics identify brand communities:[62]

1. A "consciousness of kind," or a sense of felt connection to the brand, company, product, or other community members;
2. Shared rituals, stories, and traditions that help convey the meaning of the community; and
3. A shared moral responsibility or duty to both the community as a whole and individual community members.

TYPES OF BRAND COMMUNITIES Brand communities come in many different forms.[63] Some arise organically from brand users, such as the Atlanta MGB riders club and the Porsche Rennlist online discussion

Harley-Davidson has built an active brand community through its Harley Owner's Group which boasts more than one million members.

Source: Nicholas J Reid/Getty Images

group. Others are company-sponsored and facilitated, such as Club Green Kids (official kids' fan club of the Boston Celtics) and the Harley Owners Group (H.O.G.).[64]

HARLEY-DAVIDSON Founded in 1903 in Milwaukee, Wisconsin, Harley-Davidson has twice narrowly escaped bankruptcy but is today one of the most recognized motor vehicle brands in the world. In dire financial straits in the 1980s, Harley licensed its name to such ill-advised ventures as cigarettes and wine coolers. Although consumers loved the brand, sales were depressed by product-quality problems, so Harley began its return to greatness by improving manufacturing processes. It also developed a strong brand community in the form of an inclusive owners' club, called the Harley Owners Group (H.O.G.), which sponsors bike rallies, charity rides, and other motorcycle events and now numbers more than 1 million members in some 1,400 chapters. H.O.G. benefits include a magazine called *Hog Tales*, a touring handbook, emergency road service, a specially designed insurance program, theft reward service, discount hotel rates, and a Fly & Ride program enabling members to rent Harleys on vacation. The company also maintains an extensive Web site devoted to H.O.G. with information about club chapters and events and a special members-only section. Harley is active with social media too and boasts more than 3.3 million Facebook fans. One fan inspired a digital video and Twitter campaign dubbed E Pluribus Unum—"Out of Many, One"—where Harley riders from all walks of life show their diversity and their pride in their bikes.

Companies large and small can build brand communities. When New York's Signature Theatre Company built a new 70,000-square-foot facility for its shows, it made sure there was a central hub where casts, crew, playwrights, and audiences for all productions could mingle and interact.[65]

Online, marketers can tap into social media such as Facebook, Twitter, and blogs or create their own online community. Members can recommend products, share reviews, create lists of recommendations and favorites, or socialize together online.

Online forums can be especially helpful in a business-to-business setting for professional development and feedback opportunities. The Kodak Grow Your Biz blog is a place for members to learn and share insights about how Kodak products, services, and technologies can improve important company or industry business performance.[66] The Pitney Bowes User Forum is a place for members to discuss issues related to Pitney Bowes equipment and to mailing and marketing in general. Members often answer each other's business questions, though Pitney Bowes customer service representatives are available for any particularly difficult support questions.[67]

MAXIMIZING THE BENEFITS OF BRAND COMMUNITIES A strong brand community results in a more loyal, committed customer base. One study showed that a multichannel retailer of books, CDs, and DVDs enjoyed long-term incremental revenue of 19 percent from customers—what the authors called "social dollars"—after customers joined an online brand community. The more "connected" a member of the community was, the greater the likelihood he or she would spend more.[68]

A brand community can be a constant source of inspiration and feedback for product improvements or innovations. The activities and advocacy of members of a brand community can also substitute to some degree for activities the firm would otherwise have to engage in, creating greater marketing effectiveness and efficiency as a result.[69]

To better understand how brand communities work, one comprehensive study examined communities around brands as diverse as StriVectin cosmeceutical, BMW Mini auto, Jones soda, Tom Petty & the Heartbreakers rock and roll band, and Garmin GPS devices. Using multiple research methods such as "netnographic" research with online forums, participant and naturalistic observation of community activities, and in-depth interviews with community members, the researchers found 12 value creation practices taking place. They divided them into four categories—social networking, community engagement, impression management, and brand use—summarized in Table 5.5.

Building a positive, productive brand community requires careful thought and implementation.[70] One set of researchers offers these recommendations for making online brand communities more effective:[71]

1. *Enhance the timeliness of information exchanged.* Set appointed times for topic discussion; give rewards for timely, helpful responses; increase access points to the community.
2. *Enhance the relevance of information posted.* Keep the focus on topic; divide the forum into categories; encourage users to preselect interests.
3. *Extend the conversation.* Make it easier for users to express themselves; don't set limits on length of responses; allow user evaluation of the relevance of posts.
4. *Increase the frequency of information exchanged.* Launch contests; use familiar social networking tools; create special opportunities for visitors; acknowledge helpful members.

TABLE 5.5 Value Creation Practices

SOCIAL NETWORKING	
Welcoming	Greeting new members, beckoning them into the fold, and assisting in their brand learning and community socialization.
Empathizing	Lending emotional and/or physical support to other members, including support for brand-related trials (product failure, customizing) and/or for nonbrand-related life issues (illness, death, job).
Governing	Articulating the behavioral expectations within the brand community.
IMPRESSION MANAGEMENT	
Evangelizing	Sharing the brand "good news," inspiring others to use, and preaching from the mountaintop.
Justifying	Deploying rationales generally for devoting time and effort to the brand and collectively to outsiders and marginal members in the boundary.
COMMUNITY ENGAGEMENT	
Staking	Recognizing variance within the brand community membership and marking intragroup distinction and similarity.
Milestoning	Noting seminal events in brand ownership and consumption.
Badging	Translating milestones into symbols and artifacts.
Documenting	Detailing the brand relationship journey in a narrative way, often anchored by and peppered with milestones.
BRAND USE	
Grooming	Cleaning, caring for, and maintaining the brand or systematizing optimal use patterns.
Customizing	Modifying the brand to suit group-level or individual needs. This includes all efforts to change the factory specs of the product to enhance performance.
Commoditizing	Distancing/approaching the marketplace in positive or negative ways. May be directed at other members (you should sell/should not sell that) or may be directed at the firm through explicit link or through presumed monitoring of the site (you should fix this/do this/change this).

Source: Adapted from Hope Jensen Schau, Albert M. Muniz, and Eric J. Arnould, "How Brand Community Practices Create Value," *Journal of Marketing* 73 (September 2009), pp. 30–51.

WIN-BACKS

Regardless of how hard companies may try, some customers inevitably become inactive or drop out. The challenge is to reactivate them through win-back strategies.[72] It's often easier to reattract ex-customers (because the company knows their names and histories) than to find new ones. Exit interviews and lost-customer surveys can uncover sources of dissatisfaction and help win back only those with strong profit potential.[73]

Cultivating Customer Relationships

Companies are using information about customers to enact precision marketing designed to build strong long-term relationships.[74] Information is easy to differentiate, customize, personalize, and dispatch over networks at incredible speed. But that capability cuts both ways. For instance, customers now comparison-shop quickly and easily through sites such as Bizrate.com, Shopping.com, and PriceGrabber.com, and Epinions.com and Yelp.com let them share information about their product and service experiences with others. Company empowerment has been matched by customer empowerment, and companies have to adjust to shifts in the nature and strength of their customer relationships.

CUSTOMER RELATIONSHIP MANAGEMENT

Customer relationship management (CRM) is the process of carefully managing detailed information about individual customers and all customer "touch points" to maximize loyalty.[75] CRM is important because a major driver of company profitability is the aggregate value of the company's customer base. A related concept, **customer value management (CVM),** describes the company's optimization of the value of its customer base. CVM focuses on the analysis of individual data on prospects and customers to develop marketing strategies to acquire and retain customers and drive customer behavior.[76]

A *customer touch point* is any occasion when a customer encounters the brand and product—from actual experience to personal or mass communications to casual observation. For a hotel, the touch points include reservations, check-in and checkout, frequent-stay programs, room service, business services, exercise facilities, laundry service, restaurants, and bars. The Four Seasons relies on personal touches, such as a staff that always addresses guests by name, high-powered employees who understand the needs of sophisticated business travelers, and at least one best-in-region facility, such as a premier restaurant or spa.[77]

CRM enables companies to provide excellent real-time customer service through the effective use of individual account information. Based on what they know about each valued customer, they can customize market offerings, services, programs, messages, and media. Companies' increased ability to track and market to individual customers is not without its controversies, as "Marketing Insight: The Behavioral Targeting Controversy" highlights.

PERSONALIZING MARKETING Widespread Internet usage allows marketers to abandon the mass-market practices that built brand powerhouses in the 1950s, 1960s, and 1970s for new approaches that are a throwback to marketing practices from a century ago, when merchants literally knew their customers by name. *Personalizing marketing* is about making sure the brand and its marketing are as personally relevant as possible to as many customers as possible—a challenge, given that no two customers are identical.

Companies are using e-mail, Web sites, call centers, databases, and database software to foster continuous contact between company and customer. Although technology can help with customer relationship management, firms have to be careful not to roll out too many automated-response phone systems or social-networking tools as ways to satisfy customer service requests. Many customers still prefer to talk to a live representative to receive more personal service—an ongoing priority in marketing.[78]

Companies are recognizing the role of the personal component in CRM and its influence once customers make actual contact with the company. Employees can create strong bonds with customers by individualizing and personalizing relationships. Consider the lengths to which British Airways is going to satisfy valued customers.[79]

marketing insight

The Behavioral Targeting Controversy

The emergence of *behavioral targeting* is allowing companies to track the online behavior of target customers and find the best match between ads and prospects. Tracking an individual's Internet usage behavior relies on cookies—randomly assigned numbers, codes, and data that are stored on the user's computer hard drive and reveal which sites have been visited, the amount of time spent there, which products or pages were viewed, and which search terms were entered.

The *Wall Street Journal* reviewed 1,000 top Web sites and found that 75 percent included code from social networks such as Facebook's "like" and Twitter's "tweet" buttons. The existence of the code could match people's identities with their Web-browsing activities, tracking a user's arrival on a page even if the Facebook or Twitter button was never clicked. Another *Wall Street Journal* study showed that roughly a quarter of the times a user logged into one of 70 popular Web sites, the user's real name and e-mail address or other personal details, such as username, were passed on to third-party companies.

A new customer signing up with Microsoft for a free Hotmail e-mail account, for example, is required to give the company his or her name, age, gender, and zip code. Microsoft can then combine those facts with information such as observed online behavior and characteristics of the area in which the customer lives to help advertisers better understand whether, when, and how to contact that customer. Although Microsoft maintains it carefully preserves consumer privacy—it claims it won't purchase an individual's income history—it can still provide advertising clients with behavioral targeting information.

For example, Microsoft can help a DiningIn franchisee zero in on working moms ages 30 to 40 in a given neighborhood with ads designed to reach them before 10 AM when they're most likely to be planning their evening meal. Or if a person clicks on three Web sites related to auto insurance and then visits an unrelated site for sports or entertainment, auto insurance ads may show up on that site. Microsoft claims behavioral targeting can increase the likelihood a visitor clicks an ad by as much as 76 percent.

Proponents of behavioral targeting maintain that it also brings consumers more relevant ads. Because the ads are more effective as a result, more ad revenue is available to support free online content. Supporters also maintain that many consumers would be less concerned if they knew exactly how tracking worked. They argue that practices conform with the online ad industry's self-regulation norms, ensuring anonymity by not giving firms access to "personal identifiable information" (PII).

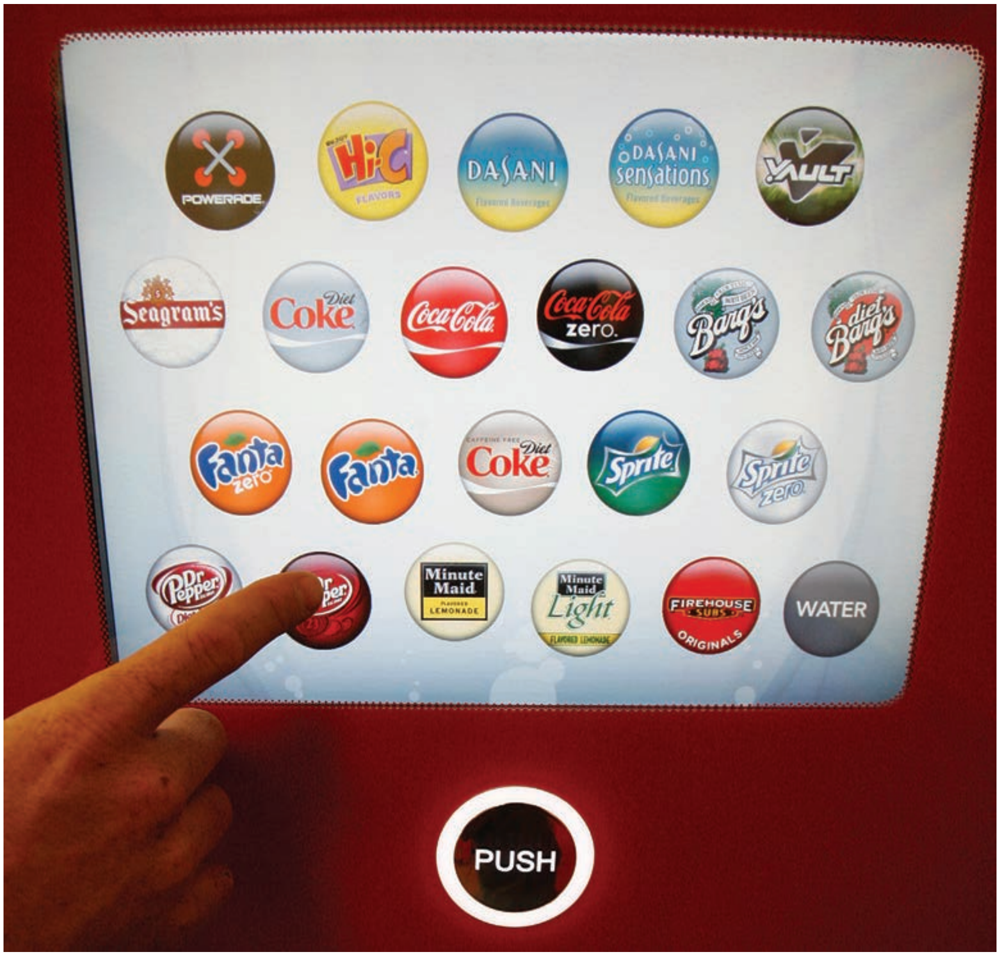
Identity information is removed, protected, or separated from browsing history in different ways. For example, a Web site can use a formula to turn its users' e-mail addresses into jumbled strings of numbers and letters, as can an advertiser. Both can send their jumbled lists to a third company that looks for matches so the Web site can show an ad targeted to a specific person without any real e-mail addresses changing hands.

Nevertheless, as Chapter 3 pointed out, consumers have significant misgivings about advertisers tracking them online. A single Web page can contain computer code from dozens of different ad companies or tracking firms. Government regulators wonder whether industry self-regulation will be sufficient or whether legislation is needed.

Sources: Elisabeth Sullivan, "Behave," *Marketing News*, September 15, 2008, pp. 12–15; Stephanie Clifford, "Two-Thirds of Americans Object to Online Tracking," *New York Times*, September 30, 2009; Jessica Mintz, "Microsoft Adds Behavioral Targeting," *Associated Press*, December 28, 2006; Laurie Birkett, "The Cookie That Won't Crumble," *Forbes*, January 18, 2010, p. 32; Alden M. Hayashi, "How *Not* to Market on the Web," *MIT Sloan Management Review* (Winter 2010), pp. 14–15; Deborah L. Golemon and Laurie A. Babin, "How Marketers Are Dealing With the Controversy Surrounding Behavioral Targeting," *International Journal of Business, Marketing and Decision Sciences* 4 (Spring 2011), pp. 127-141; Jennifer Valentino-Devries and Jeremy Singer-Vine, "They Know What You're Shopping For," *Wall Street Journal*, December 7, 2012.

BRITISH AIRWAYS British Airways took personalization to a higher level in the summer of 2012 with its new "Know Me" program. One goal was to centralize information about frequent fliers from every one of BA's service channels—Web site, call center, e-mail, on board planes, and inside airports—into a single database. For any one passenger booked on a flight, BA would know his or her current seating location, previous flights and meal choices, prior complaint history, and so on. BA also distributed 2,000 iPads among crew members and ground staff to allow them to access the database as well as receive personal recognition messages about passengers on any one flight. The goal was to have 4,500 daily messages, or approximately seven message updates per flight. To facilitate VIP passenger identification, British Airways also used stored photos of fliers downloaded from Google Image searches. One company representative described the program as aiming to "recreate the feeling of recognition you get in a favorite restaurant when you're welcomed there, but in our case it will be delivered by thousands of staff to millions of customers." Although some observers raised privacy concerns—even calling it "creepy"—British Airways noted that the passenger information was already available or viewed as helpful by its most valuable fliers.

As part of a broad trend towards personalization, Coca-Cola has introduced Freestyle dispensing machines that allow users to customize their soft drink choices.



Source: Scott Keeler/ZUMAPRESS/Newscom

While British Airways is personalizing its service experiences, BMW is figuring out ways to personalize its products. While 15 percent of U.S. drivers custom-ordered their cars in 2010, BMW's goal was to make that number 40 percent of its buyers by 2015. The company offers 500 side-mirror combinations, 1,300 front bumper combinations, and 9,000 center-console combinations and provides new buyers a video link to watch their car being "born" while waiting for delivery. Its detailed manufacturing and procurement system takes the slack out the production process, reduces inventory carrying costs, and avoids rebates on slow-moving sellers. Customers tend to load up with options—generating more profitability for BMW and its dealers—but are also more loyal.[80]

Even Coca-Cola is getting in on the action. The Coca-Cola Freestyle dispensing machine can dispense 125 sparkling and still brands that consumers can mix via a touchscreen, creating a beverage to suit their particular taste.[81]

To adapt to customers' increased desire for personalization, marketers have embraced concepts such as permission marketing. *Permission marketing*, the practice of marketing to consumers only after gaining their expressed permission, is based on the premise that marketers can no longer use "interruption marketing" via mass media campaigns. According to Seth Godin, a pioneer in the new technique, marketers develop stronger consumer relationships by respecting consumers' wishes and sending messages only when they express a willingness to become more engaged with the brand.[82] Godin believes permission marketing works because it is "anticipated, personal, and relevant."

Permission marketing, like other personalization approaches, presumes consumers know what they want, though they often have undefined, ambiguous, or conflicting preferences. "Participatory marketing" may be a more appropriate concept than permission marketing because marketers and consumers need to work together to find out how the firm can best satisfy consumers.

CUSTOMER EMPOWERMENT Marketers are helping consumers become evangelists for brands by providing them resources and opportunities to demonstrate their passion. Doritos held a contest to let consumers name its next flavor. Converse asked amateur filmmakers to submit 30-second short films that demonstrated how the iconic sneaker brand inspired them. The best of the 1,800 submissions were showcased in the Converse Gallery

Web site, and the best of the best became TV commercials. Sales of shoes via the Web site doubled in the month after the gallery's launch.[83]

As much as new technologies help customers assist or become involved in a brand's marketing, they also help them avoid marketing at the same time. For example, ad blocking is the most popular software extension for leading browsers, and the overall rate of ad blocking by users averages about 10 percent.[84]

Although much has been made of the newly empowered consumer—in charge, setting the direction of the brand, and playing a much bigger role in how it is marketed—it's still true that only *some consumers* want to get involved with *some of the brands* they use and, even then, only *some of the time*. Consumers have lives, jobs, families, hobbies, goals, and commitments, and many things matter more to them than the brands they purchase and consume. Understanding how to best market a brand given such diversity in customer interests is crucially important.[85]

When will consumers choose to engage with a brand? Many factors can come into play, but follow-up analysis of the IBM 2010 CEO Study revealed the following about customer pragmatism: "…most do not engage with companies via social media simply to feel connected.… To successfully exploit the potential of social media, companies need to design experiences that deliver tangible value in return for customers' time, attention, endorsement and data." According to these IBM analysts, that "tangible value" includes discounts, coupons, and information to facilitate purchase. They also note that many businesses overlook social media's most potent capabilities for capturing customer insights, monitoring the brand, conducting research, and soliciting new-product ideas.[86]

CUSTOMER REVIEWS AND RECOMMENDATIONS Although the strongest influence on consumer choice remains "recommended by relative/friend," an increasingly important decision factor is "recommendations from consumers." With increasing mistrust of some companies and their advertising, online customer ratings and reviews are playing a growing role in the customer buying process.[87]

A Forrester research study, for example, found that close to 50 percent of consumers won't book a hotel that does not have online reviews. Not surprisingly, more hotels are launching their own program to post reviews (Starwood places independent, authenticated reviews on individual hotel sites) or are using travel review sites (Wyndham streams its five most recent reviews from TripAdvisor on its site, leading to a 30 percent increase in bookings).[88] TripAdvisor has quickly grown to be a valuable online resource for travelers.[89]

TRIPADVISOR After being frustrated by the lack of detailed, reliable, and up-to-date information available to help him decide where to go on a Mexican holiday, Stephen Kaufer founded TripAdvisor in 2001. The pioneer in online consumer travel reviews, the company grew quickly and is now the world's largest travel Web site, with more than 170 million user reviews and opinions as of 2014. It allows users to collect and share information and make bookings for a wide variety of hotels, vacation rentals, airlines, restaurants, and other travel-related locations or businesses through its hotel and air booking partners. Users can post reviews, photos, and opinions and participate in discussions on a variety of different topics. To improve the quality and accuracy of its content, TripAdvisor uses both manual review and advanced computer algorithms, including a verification and fraud detection system that considers the IP and e-mail address of reviewers (as well as other review attributes) and monitors suspicious patterns of postings as well as inappropriate language. About 30 hotels have been blacklisted from the site for suspicious reviews. TripAdvisor has more than 280 million unique visitors monthly, and hundreds of millions of people each month view its content on 500 other sites, including Best Western International, Expedia, and Thomas Cook. In recent years, TripAdvisor has innovated to improve the personalization and social nature of its services; in fact, it was one of Facebook's initial launch partners for its "Instant Personalization" project, which allows users to personalize their TripAdvisor experience by allowing them to see TripAdvisor content posted by their Facebook friends, subject to their privacy elections. Local Picks is a Facebook app that allows users to localize TripAdvisor restaurant reviews and auto-share user reviews on Facebook Timeline. The Friends of Friends function allows TripAdvisor users to sort reviews by a user's Facebook friend status. Its acquisitions of social and mobile connectivity travel sites Wanderfly and EveryTrail have further strengthened TripAdvisor's capabilities in that area.

When online pet food retailer PETCO started using consumer product ratings and reviews in e-mails and banner ads, it found its click-through rate increased considerably as a result.[90] Brick-and-mortar retailers such as Best Buy, Staples, and Cabela's are also recognizing the power of consumer reviews and have begun to display them in their stores.[91]

Despite consumer acceptance of such reviews, however, their quality and integrity can be in question.[92] In one famous example, over a period of seven years, the cofounder and CEO of Whole Foods Market posted more than 1,100 entries on Yahoo! Finance's online bulletin board under a pseudonym, praising his company and criticizing competitors.

Some companies offer computer-recognition technology to monitor for fraud. Bazaarvoice helps companies such as Walmart and Best Buy manage and monitor online reviews using a process called device fingerprinting. The company caught one firm posting hundreds of positive reviews of one of its products and negative reviews of its competitor's.[93]

Online reviews and blogging sites such as Gawker have struggled to police comments.[94] To avoid attracting anonymous or biased reviews, Angie's List allows only paid and registered subscribers to access its Web site, which compiles about 40,000 reviews of service companies and health care professionals from its 1.5 million North American subscribers each month. Users rate providers on price, quality, responsiveness, punctuality, and professionalism using a report card–style A-to-F scale.[95]

Other sites offer summaries of professional third-party reviews. Metacritic aggregates music, game, TV, and movie reviews from leading critics—often from more than 100 publications—averaged into a single 1-to-100 score. Review sites are important in the video game industry because of the influence they wield and the product's high selling price—often $50 to $60. Some game companies tie bonuses for their developers to game scores on the more popular sites. If a major new release doesn't make the 85-plus cutoff, the publisher's stock price may even drop.[96]

Bloggers who review products or services are influential because they may have thousands of followers; blogs are often among the top links returned in online searches for certain brands or categories. A company's PR department may track popular blogs via online services such as Google Alerts and Technorati. Firms also court the favor of key bloggers via free samples and advance information. Most bloggers disclose this special treatment.

For smaller brands with limited media budgets, online word of mouth is critical. To generate prelaunch buzz for one of its new hot cereals, organic food maker Amy's Kitchen shipped out samples before its release to several of the 50 or so vegan, gluten-free, or vegetarian food bloggers the company tracks. When favorable reviews appeared on these blogs, the company was besieged by e-mails asking where to buy the cereal.[97]

As it turns out, sometimes even negative reviews can be surprisingly helpful. For one thing, although they can hurt a well-known brand, they can create awareness about an unknown or overlooked one. They can also provide valued information.

A Forrester study of 10,000 consumers of Amazon.com's electronics and home and garden products found that 50 percent found negative reviews helpful. Most purchased the products regardless of negative comments because they felt these merely reflected personal tastes and opinions different from their own. When consumers can better learn the advantages and disadvantages of products through negative reviews, fewer product returns may result, saving retailers and producers money.[98]

Online retailers often add their own recommendations to consumer selections or purchases: "If you like that black handbag, you'll love this red top." One source estimated that recommendation systems contribute 10 percent to 30 percent of an online retailer's sales. Specialized software tools help facilitate customer "discovery" or unplanned purchases.

At the same time, online companies need to make sure their attempts to create relationships with customers don't backfire, as when customers are bombarded by computer-generated recommendations that consistently miss the mark. Buy a few baby gifts on Amazon.com, and your personalized recommendations suddenly don't look so personal! E-tailers need to recognize the limitations of online personalization while searching for technology and processes that really work.

CUSTOMER COMPLAINTS Some companies think they're getting a sense of customer satisfaction by tallying complaints, but studies show that while customers are dissatisfied with their purchases about 25 percent of the time, only about 5 percent complain. The other 95 percent either feel complaining is not worth the effort or don't know how or to whom to complain. They just stop buying.[99]

Of the customers who register a complaint, 54 percent to 70 percent will do business with the organization again if their complaint is resolved. The figure goes up to a staggering 95 percent if the customer feels the complaint was resolved *quickly*. Customers whose complaints are satisfactorily resolved tell an average of five people about the good treatment they received.[100] The average dissatisfied customer, however, gripes to 11 people. If each of these tells still other people, the number exposed to bad word of mouth may grow exponentially.

No matter how perfectly designed and implemented a marketing program is, mistakes will happen. The best thing a company can do is make it easy for customers to complain. Suggestion forms, toll-free numbers, Web sites, and e-mail addresses allow for quick, two-way communication. The 3M Company claims that more than two-thirds of its product-improvement ideas come from listening to customer complaints.

Given that many customers may choose not to complain, companies should proactively monitor social media and other places where customer complaints and feedback may be aired. Jet Blue's 27-member customer service team is charged with monitoring the airline's Twitter account and Facebook page, among other responsibilities. When a customer's complaint about a fee for bringing a folded bike on board began to circulate online, Jet Blue quickly responded and decided it was not a service it should charge for.[101]

Given the potential downside of having an unhappy customer, it's critical that marketers deal with negative experiences properly.[102] Although challenging, the following practices can help to recover customer goodwill:[103]

1. Set up a seven-day, 24-hour toll-free hotline (by phone, fax, or e-mail) to receive and act on complaints—make it easy for the customer.
2. Contact the complaining customer as quickly as possible. The slower the company is to respond, the more dissatisfaction may grow and lead to negative word of mouth.
3. Accept responsibility for the customer's disappointment; don't blame the customer.
4. Use customer service people who are friendly and empathic.
5. Resolve the complaint swiftly and to the customer's satisfaction. Some complaining customers are not looking for compensation so much as a sign that the company cares.

Not all complaints, however, reflect actual deficiencies or problems with a company's product or service.[104] Big companies especially are targets for opportunistic customers who attempt to capitalize on even minor transgressions or generous compensation policies. Some firms fight back and even take an aggressive stance if they feel a criticism or complaint is unjustified.

When Taco Bell began to attract negative buzz online after rumors and a consumer lawsuit alleged that its taco mixture consisted of more filler than meat, it leaped into action with full-page newspaper ads headlined, "Thank you for suing us." There and in Facebook postings and a YouTube video, the company pointed out that its taco mixture was 88 percent beef, with ingredients such as water, oats, spices, and cocoa powder added only for flavor, texture, and moisture. To help spread the word, Taco Bell marketers bought the key words "taco," "bell," and "lawsuit" so that its official responses appeared as the first link on Yahoo!, Google, and Bing searches.[105]

Many senior executives worry about their firms using social media and the potential negative effects of cranky customers communicating online. Marketers, however, contend that the positives outweigh the negatives and steps can be taken to minimize the likelihood of such damage.

One strategy for companies active in corporate social responsibility is to actively shape their public image during quiet times and then leverage that goodwill in paid or other media during difficult times. Nike was once a target of Internet-savvy critics who skillfully used search engine optimization to populate unflattering portraits of the company. Now, searches for Nike yield links to sites that describe its many environmental and community initiatives (such as shoe recycling).[106]

Source: ASSOCIATED PRESS

Taco Bell aggressively defends the quality of its products via social media.

Summary

1. Customers are value maximizers. They form an expectation of value and act on it. Buyers will buy from the firm that they perceive to offer the highest customer-delivered value, defined as the difference between total customer benefits and total customer cost.
2. A buyer's satisfaction is a function of the product's perceived performance and the buyer's expectations. Recognizing that high satisfaction leads to high customer loyalty, companies must ensure that they meet and exceed customer expectations.
3. Losing profitable customers can dramatically affect a firm's profits. The cost of attracting a new customer is estimated to be five times the cost of keeping a current customer happy. The key to retaining customers is relationship marketing.
4. Quality is the totality of features and characteristics of a product or service that bear on its ability to satisfy stated or implied needs. Marketers play a key role in achieving high levels of total quality so that firms remain solvent and profitable.
5. Marketing managers must calculate customer lifetime values of their customer base to understand their profit implications. They must also determine ways to increase the value of the customer base.
6. Companies are also becoming skilled in customer relationship management (CRM), which focuses on developing programs to attract and retain the right customers and meeting the individual needs of those valued customers.

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Applications

Marketing Debate

Online versus Offline Privacy

As more firms practice relationship marketing and develop customer databases, privacy issues are emerging as an important topic. Consumers and public interest groups are scrutinizing—and sometimes criticizing—the privacy policies of firms and raising concerns about potential theft of online credit card information or other potentially sensitive or confidential financial information. Others maintain online privacy fears are unfounded and that security issues are as much a concern offline. They argue that the opportunity to steal information exists virtually everywhere and that it's up to consumers to protect their interests.

Take a position: **Privacy is a bigger issue online than offline *versus* Privacy is no different online than offline.**

Marketing Discussion

Using CLV

✪ Consider customer lifetime value (CLV). Choose a business and show how you would go about developing a quantitative formulation that captures the concept. How would that business change if it fully embraced the customer equity concept and maximized CLV?

Marketing Excellence

>> Audi

The year 1899 marked the establishment of August Horch & Cie, the first car manufacturing company founded by August Horch. As a pioneer in automotive engineering, Horch had previously worked with Carl Benz, inventor of modern automobiles with combustion engines. Horch left his company in 1909 because of differences with its co-management and supervisory board. He immediately set up a second car venture which he named "Audi"—the Latin translation of his German family name, Horch ("hark" or "listen" in English). From the very beginning, Audi established a tradition of sports victories. Thanks to Audi's accomplishments in the Austrian Alpine Runs between 1911 and 1914, August Horch succeeded in making the brand internationally well-known within just a few years.

In 1932, the company's famous four-ring emblem was created when Audi merged with the previously independent companies Horch, Dampf-Kraft-Wagen, and Wanderer to form Auto Union. For many years, the name Audi was not in use. A new merger in 1969, between Auto Union and NSU Motorenwerke AG, established Audi NSU Auto Union AG. The company was renamed Audi in 1985 by Volkswagen, the holding company of Audi since the mid-1960s.

A new advertising slogan was created for the company in 1971 and has been used as the company's mission statement ever since. "Vorsprung durch Technik," which roughly translated means "progress through technology," remains the main catchphrase for Audi. In the 1970s and 1980s, the company was effectively putting this to practice with innovations like the quattro four-wheel drive, aluminum car bodies, direct-injection engines, and the first hybrid vehicles.

Despite these achievements, Audi had problems and needed to reposition itself in an increasingly competitive environment. Customers in the United States complained about a mysterious acceleration in their cars, and the image of Audi was not sophisticated enough for a manufacturer of premium and luxury cars. So in a bold move, the company's management decided on an extreme repositioning strategy. Audi was to be the most progressive of all premium car manufacturers. Sportiness was picked as the second differentiating factor. With a famous commercial, the brand transformation was put into practice in 1986. An Audi 100 quattro, a four-wheel drive, drove up a snow-covered ski jump, apparently all by itself. The commercial won a Gold Lion (Lion' d'Or) at the international advertising festival in Cannes, and in 1997 was voted best German advertising of all times by a professional jury.

Audi also heavily invests in motor sports. Numerous races and world championships have been won with its cars. Besides its motor sports activities, Audi sponsors major teams like Germany's number one soccer club FC Bayern Muenchen. Since 2002, Audi and the Bavarians have been strategic partners. Audi is also the sponsoring partner for other leading European soccer clubs like FC Barcelona and Chelsea FC. In India, Audi became famous overnight in 1985. India won the world championship in cricket, the sport the country is most passionate about, and Ravi Shastri of the Indian team was awarded an Audi 100 for his winning performance—an event that is fondly remembered in the country even today.

The success of Audi's marketing over the past two decades becomes clear if you compare the company's sales figures to the turnover of their major competitive brands, BMW and Mercedes-Benz. In 2000, Audi sold approximately 653,000 cars, BMW 822,000, and Mercedes-Benz 1.053 million. Based on sales figures from 2013, BMW is leading the market with a narrow margin of 1.66 million cars as compared to Audi's 1.58 million and Mercedes-Benz's 1.46 million cars. In China, the most important automotive market in the world with 15.9 million cars sold (USA: 15.6 million) in 2013, Audi leads the market among the German competitors with 492,000 cars sold as compared to BMW's 360,000 and Mercedes-Benz's 228,000. Overall, 84 percent of Audi's sales are realized outside of Germany today.

What else has Audi done over the past years besides a bold move in repositioning, and the creation of a convincing advertising and sponsorship concept? Audi offers a variety of innovative products that meet the customer's increasing demand for SUVs and luxury cars on the one hand, and alternative driving systems and compact cars on the other. Audi's SUVs are branded in its "Q" series. The company is rounding up its product range with a new Q7 in 2015, a Q1 in 2016, and a Q8 in 2017. With other Audi products like the Audi A3 e-tron, customers can combine the advantages of hybrids with traditional-drive systems. The company's image of being a superior sports car manufacturer is being enhanced with models like the R8, a car based on Audi's race car prototype for the Le Mans 24-hours race. Its compact and middle-class cars A1, A3, and A4 mark the other side of the product portfolio. They also profit from the company's innovativeness through light-weight construction and plug-in hybrid technology. According to a 2014 consumer survey, Audi is considered to be Germany's most innovative car manufacturer.

To further involve its customers emotionally, while at the same time acknowledging the increasing importance of the Internet as a communication and distribution channel, Audi has introduced digital showrooms. In these "Audi Cities," consumers can experience the virtual world of Audi in 3D. London, Beijing, and Berlin were the starting places for the concept. Moscow and other locations will follow. An innovative idea for car-sharing has recently been presented by Audi's Chief of Sales and Marketing, Luca de Meo. Stockholm serves as a test market for a concept where up to five persons share a car for one or two years. Through an app, participants can make advance reservations and locate their car.

Despite its global success, there are challenges remaining for Audi. The average selling price of an Audi is still lower than an average BMW or Mercedes-Benz. New entrants in the growing market for environmentally sustainable cars like Tesla as well as its German key competitors will test Audi's innovativeness even further.

Questions

1. In your opinion, how important is it to invest in customer loyalty for cars, a product most people buy only every couple of years?
2. Try to estimate the lifetime value of an Audi customer.
3. What measures should Audi take to build long-term loyalty relationships?

Sources: Frank Janssen, Heiner Müller-Elsner, "Mutiger Steilpass", *Stern*, March 7, 2005; Debasish Roy, "Audi hands over Q5 to Yuvraj Singh; with some low-scale marketing moves," *The Economic Times*, April 17, 2011; Sergio Zyman, *The End of Advertising as We Know it*, (Hoboken, New Jersey: Wiley, 2003); "Facebook bleibt für uns in erster Linie eine Dialog- und Kommunikationsplattform," *Absatzwirtschaft*, December 2, 2013; "Audi will noch größere SUVs bauen," *Automobil Produktion*, October 17, 2014; Rebecca Eisert, "Carsharing: Audi testet in Stockholm," *Wirtschaftswoche*, October 13, 2014; "Audi Case Study: Post-milennium success," MarketLine, December, 2011; Audi, www.audi.com; BMW, www.bmwgroup.com; Daimler, www.daimler.de; Statista, http://de.statista.com; Volkswagen, www.volkswagenag.com.

Marketing Excellence

>> Harley-Davidson

Harley-Davidson, a U.S. brand synonymous with beautiful motorbikes, inspires many to own its customized bike with iconic engine. Today the brand is sought after not only in the United States but globally too. What explains its wide global acceptance, and the strong sense of brand loyalty among Harley-Davidson motorbike owners?

Harley-Davidson dealers, ranging from the CEO to the sales staff, maintain personalized relationships with customers through face-to-face and social media contact. Knowing customers as individuals and conducting ongoing research to keep up with the changing expectations and experiences helps Harley-Davidson to define its customers' needs better.

Current customers have told Harley-Davidson's management to keep the identity, look, and sound of the motorcycles because they are unique. Globally, customers accept the U.S. brand image as it stands. When customers' views are heard and accepted by management, customers develop greater brand loyalty, creating an extraordinary customer experience that is unique and valuable. Buying a Harley allows owners to express their individualism and freedom, connect with friends, and share a sense of comradeship through the activities of H.O.G., the company-sponsored Harley Owners Group and riding club. Owners of new Harley-Davidson motorbikes enjoy free H.O.G. membership in the first year. If renewed, members can enjoy various discounts and benefits.

Examples of events and activities that are sponsored by independent dealerships, such as Harley-Davidson of Singapore, can range from short rides and major destination rides, to local charity events. H.O.G. members are also invited to events, such as new model launches, and riders' appreciation nights. Dealers in each country support H.O.G. members and foster positive bonding relationships among members and other dealers.

In Singapore, for instance, a community of friends rides Harley-Davidson motorcycles with a passion. "We ride 'em, and we have lots of fun! And we've been doing it since 1996 in Singapore." "To Ride and Have Fun" is a motto that all H.O.G. chapters around the world follow. Riders associate riding with other owners as a time of bonding that conveys the image of freedom and adventure.

Membership in H.O.G. has increased. Now not only men but women, children, and families are a part of H.O.G.'s many and varied group outings and activities. Harley-Davidson has developed a strong brand image and consumers appreciate it even more by experiencing it firsthand. The desire to be associated with the Harley-Davidson brand is strong because it is linked to an aspirational lifestyle.

There are more than 2,000 H.O.G. members in Malaysia alone, with around 500 active riders. The Southeast Asia Harley Owners Group (SEA HOG) organizes rallies and rides as well as charity events. In late 2013, a two-day event followed by a five-day riding tour attracted 800 owners to celebrate the 110th anniversary of the brand.

Some H.O.G. members around the world ride in rallies every Sunday, rain or shine, displaying a strong sense of loyalty to the Harley-Davidson brand. In Hong Kong, H.O.G. members include professionals, like doctors, lawyers, accountants, pilots, engineers, movie stars, and business executives. Their participation shows the strong brand loyalty among Harley-Davidson owners and the strong desire to be engaged in H.O.G. members' activities.

Proactive in people development, Harley-Davidson shares company values, philosophy, and brand experience with its staff and provides effective communication to its independent dealers. Professional training by members of the Harley-Davidson University in the U.S. encourages consistent service at every dealership. Thus, Harley-Davidson's employees around the world can be confident about providing the genuine Harley-Davidson experience. Satisfied employees deliver outstanding services that generates sustainable customer and brand loyalty, positive word of mouth, and ultimately higher company sales.

To remain competitive, Milwaukee-based Harley-Davidson has started to enlarge its customer base and successfully connect with new, younger riders by way of social media applications, such as Facebook and Twitter. Engaging relationships have been established with young adults who form a large part of its global followership. Important feedback that Harley-Davidson's strong brand name remains appealing to the younger audience is encouraging.

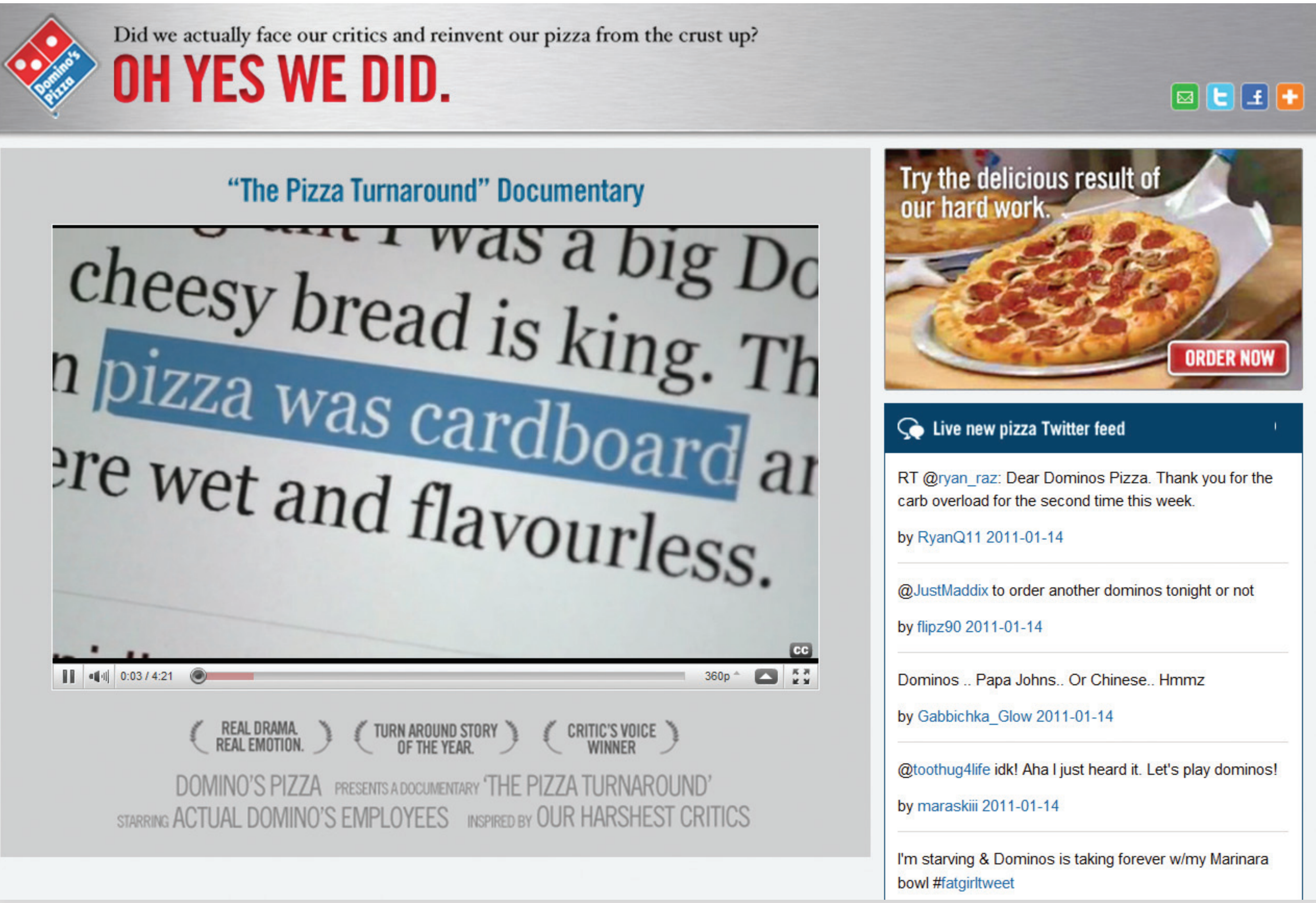
Harley-Davidson also makes in-person connections with potential riders at music festivals by using dynamometers to create an interactive experience called Jump Start, which allows novice or non-riders an opportunity to feel what it's like to ride a Harley-Davidson.

In 2008, it became the leading manufacturer of motorcycles to sell to customers younger than 34 years without changing the products too drastically or lowering its prices. Harley-Davidson merely modified some design elements for its Dark Custom series of motorcycles, which consists largely of existing Harley-Davidson motorcycles but with flat black paint, much less chrome, and toned-down styling. It portrayed its heritage message of freedom, uniqueness, individual expression, and shared experience as recognized by older customers.

Questions

1. What has Harley-Davidson done with its H.O.G. program to create an extraordinary customer experience that is unique and valuable to its members? Has the motorcycle manufacturer been successful?
2. To enlarge its customer base, what would you recommend Harley-Davidson do to cultivate long-term relationships with a younger audience, aged between 18–34?

Sources: Jill Z. McBride, "DMA2010–How Harley-Davidson Builds Champion Customers One Rider at a Time," www.colloquy.com; Shaun Smith, "Customer Experience Management Plus: Harley-Davidson," *CustomerThink*, March 4, 2008; Harley-Davidson Hong Kong; Harley-Davidson Kuala Lumpur; Harley-Davidson Singapore; H.O.G. Singapore, www.hogsingapore.com/events.php; Eric Decker, "Harley reaches out to the next generation," *Biz Times*, July 23, 2010.



Based on detailed customer insights, Domino's improved its products and how they were marketed.

Source: Domino's Pizza, LLC

In This Chapter, We Will Address the Following **Questions**

1. How do consumer characteristics influence buying behavior? (p. 179)
2. What major psychological processes influence consumer responses to the marketing program? (p. 187)
3. How do consumers make purchasing decisions? (p. 194)
4. In what ways do consumers stray from a deliberative, rational decision process? (p. 202)

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