Combating the Churn Phenomenon

The adoption of key retention policies will help operators identify and acquire the most valuable customer segments in the competitive mobile battleground.

Richard Siber

Churn — the persistent defection of customers — is an occupational hazard of any sales-driven business. But for wireless telecoms operators it has become a crisis which threatens profitability and shareholder value across the entire industry. Operators seem powerless to stem the tide; however, research suggests that not only are they actually causing the phenomenon, they have it in their power to reverse it.

Churn rates are increasing: research shows churn rates increasing by between four to seven percentage points a year in all the major markets; in the US, annualised churn reached 29 per cent in 1996. The effect on shareholder value is dramatic: research suggests that a typical operator could add US$ 150 million to its company valuation by reducing churn by just one percentage point. A reduction of five percentage points could increase shareholder value by between 15 to 20 per cent.

Churn is so damaging because the cost of acquiring customers is inordinately high: the industry average is between US$ 300-400. At this rate, an operator can wait three years to receive a payback on an average customer. At churn rates of more than 30 per cent, the return on investment is likely to be zero: yet evidence from the US suggests that churn rates will reach at least 40 per cent before they peak.

While wireless operators have become involved in the relentless pursuit of growth, they have created the fickle and unstable environment that now threatens them. The challenge now is to shift the emphasis to retention: the analysis of one company suggests that retention had a minimum of three and a maximum of six times more impact on bottom line figures than growth.

Clearly, action is required. But churn is not susceptible to an easy solution. It is a complex phenomenon, and tackling it demands a multi-faceted approach. Churn is not simply a matter of customer loyalty. An Andersen Consulting study for a European carrier facing a 25 per cent churn rate found that only five per cent of its customers were actually defecting to rivals. Double that number — 10 per cent of the customer base — were being recycled onto different tariffs or networks run by the same operator. The driving force behind this proved to be the channel reward structure, which encouraged customers to chop and change — at the operator's expense.

TYPES OF CHURN

There are essentially four types of churn:

• customer migration, or rotation, as previously outlined can be extremely costly. This may involve moving from an analogue to a digital network, or a switch in tariffs. In markets such as the UK, where handsets are heavily subsidised or even free, it may be the logical way for customers to upgrade their equipment. Discounts which disproportionately favour new customers may also be a factor;

• carrier-initiated churn occurs where the carrier disconnects the customer, for example for bad debt. This may be an indication that over enthusiastic growth is attracting marginal or inappropriate customers;

• subscription cancellation occurs when the customer simply ends the contract. This may be caused by 'price shock' when the customer receives the first full bill, shorn of incentives, discounts or introductory freetime;

• lastly, competitor churn is, surprisingly, not a significant cause of customer loss.

Latest research figures have confirmed an old rule of thumb: 80 per cent of the revenue comes from 20 per cent of the customers. Operators must therefore learn more about their customers, and identify the most valuable segments of the market. Targeting those areas for acquisition, followed by customer-loyalty schemes to ensure retention, must become a priority. Above all, growth at any price must be abandoned — some customers simply are not worth it.

To turn the tide of churn, operators must recognise it for the complex phenomenon it is, and adopt a similarly sophisticated range of techniques to combat it. These will vary from operator to operator, and from market to market. For example, in the UK the main source of churn lies in the distribution channel, where the availability of virtually free handsets, and dealer incentives that reward the quality rather than the quantity of customers, have turned the mobile phone into a commodity — virtually a fashion accessory. In the US however, the problem is subtly different. The lack of any real incentives for customer loyalty has created an entirely fickle customer base, always on the prowl for 'the best deal'. Even within one operator, churn is unlikely to stem from a single cause. It must, therefore, be attacked on a num-

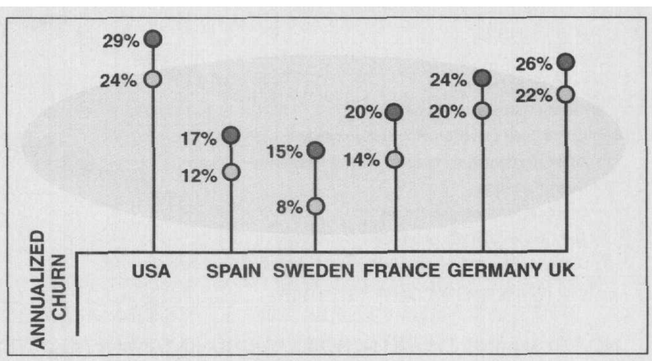

Fig. 1 Churn rates for major cellular markets

Beating Churn — A European Perspective

A European operator realised that protecting its existing customer base against new competitors was now a priority. But it found it lacked basic information on the causes and the costs of churn. Targeting churn became the number one strategic priority; a cross functional team drawing together such disciplines as marketing, customer service, distribution and productive development joined Andersen consultants to investigate the churn crisis. The results were startling: a quarter of the customer base was churning, but of these, 40 per cent were coming back as re-acquired customers. This was soon seen to be the greatest source of revenue loss. The culprit was the channel reward structure. Now the company has a structured range of anti-churn measures based on clear cost-benefit analysis. These include both reactive measures to win back customers as well as more proactive strategies designed to prevent churn before it occurs.

ber of fronts simultaneously, with highly tailored and adaptive strategies. Another case study outlines how one US operator adopted a multifaceted approach to achieve industry-beating churn rates at a time when it faced its greatest competitive threat.

A WINNING STRATEGY

There are a number of different strategies to combat churn. Some are purely reactive, attempting to win back customers once they have identified themselves as actual or potential defectors. These can range from simple discount incentives to highly sophisticated 'win-back' teams, trained customer care specialists backed by state-of-the-art information, and sales teams. More proactive measures can involve after-sales service schemes, modification of distribution and marketing channels, or improvements to processes such as billing and credit control.

Getting the mix right depends on the exact nature of the problem. So step one is: understanding churn. Why are customers leaving, and where did they go (to a competitor, out of the market all together — or back to the same operator in a different guise)? What were they worth, and where (i.e. through which distribution channel) did they come from? These seem like simple questions, but in many cases operators do not have the answers. This may be because in the drive for growth, the data is not being captured, or the distribution channel means the data is in the possession of third parties. Often, operators are unable to link the customer information they themselves hold on different databases, such as sales, billing and service.

Once the causes of churn have been identified, a number of strategies will present themselves — too many in fact. Despite the wireless telecoms industry's current lack of sophistication in dealing with this problem, other industries have lit the way. The financial services industry, for example, has developed acquisition processes which segment their customer base and target the most profitable segments. Airlines have a powerful array of customer loyalty and reward programmes at their disposal.

The next step, therefore, is to develop a programme which incorporates those strategies which will offer the best returns. Again, the key is to obtain and deploy customer information. Data warehousing and data mining techniques are sure to become key weapons in the battle against churn, supplemented by reporting mechanisms and predictive tools which reflect the complex mixture of channel types and relationships in this industry.

Implementation of the strategy is probably the most complex stage. This will involve a major shift of emphasis within the organisation, and with it the unlearning of a whole range of behaviours which are almost standard industry practice. The key shift is that from acquisition to retention. This may involve the dismantling of entire distribution structures which are found to either attract the wrong customers, or to reward the wrong behaviour. At the same time, different approaches to existing customers must be developed. Reward structures may have to be altered, so that good customer service comes to hold a higher value than razor sharp sales technique. Information systems may need to be upgraded or integrated; the long term result may be a thorough overhaul of processes and cultures throughout the organisation. Above all, the approach must be adaptive. Just as there is no one single solution to the problem, it is unlikely that any given mixture of approaches will remain valid for long in such a rapidly changing market.

The investigation of churn has led to two conclusions: the tide can be turned, and a reduction of as much as five percentage points in the rate of churn is eminently achievable. No other area of activity has the potential to create such dramatic increases in shareholder value. This is by no means easy money. Attacking the root causes of churn may involve a reorientation of the entire business, but not only are the rewards substantial — failure to act may prove fatal. □

Beating Churn — An American Perspective

An American operator was forced to evaluate its churn rates by an influx of new operators using the PCS system. It quickly realised that a 'one-size fits all' approach would not address its churn problem, and opened fire on a number of different fronts. Improved credit screening procedures identified 'at risk' customers, and by requiring them to pay an initial deposit, minimised the risk. At the same time, a more lenient approach was taken to disconnecting existing customers. Not only are churn rates constantly analysed, they are related to other information the operator holds on customers. This allows the operator to identify potential defectors and target them with defensive measures before they decide to leave. Customer service staff are now fully empowered to deal with customer complaints. Armed with on-line access to customer history files, they can resolve difficulties with priority customers. This sophisticated, multi-level approach has produced outstanding results. Churn rates — which average 29 per cent in the US market — are now down to 15 per cent, among the lowest in the industry.

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This article is based on research carried out by Andersen Consulting and published in the report, Battling Churn to Increase Shareholder Value: Wireless Challenges for the Future

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