Service Research/1

Why Is Management Always The Last To Know?

By Chuck Chakrapani

From Products to Service

As we move towards the post-industrial society, management focus has been shifting from goods to services. Until a few years ago, a company's main focus was on the quality of the product they offered. Not any longer. Now most products are of acceptable quality. Swiss watches or IBM computers do not inspire the same awe as they once did. The focus now is more on how you sell what you sell rather than on what you sell.

This is particularly true of institutions whose 'products' are services. Financial institutions, utility companies, travel services etc., fall into this category.

Two Sources of Information

Service organizations largely depend on two sources when they want to find out whether they measure up to customer expectations: 1) Customers approaching the organization (consumer complaints and comments) and 2) the organization approaching customers (research). How much can an organization depend on customer comments and complaints to understand whether it is meeting customer expectations? To what extent can it rely on its own research to know whether customers are properly serviced?

Two Basic Information Sources

Customers to Organization
Customer complaints/comments

Organization to Customers
Marketing Research

While universal answers to these questions are obviously misleading, one may safely state that both approaches are flawed in many instances. We will first discuss why voluntary customer communication to management can be a misleading measure. Then we will see why traditional marketing research can also mislead and what can be done to obtain usable information.

Financial Services Industry

While all service-oriented organizations share similar problems, I will confine my examples mostly to the financial services industry. Financial services are particularly interesting because the benefits (except perhaps interest rates) offered by them, such as 'service', 'convenience' etc., are largely intangible in nature. The intangible nature of the benefits is what sets service research apart from product research.

Management and Customers

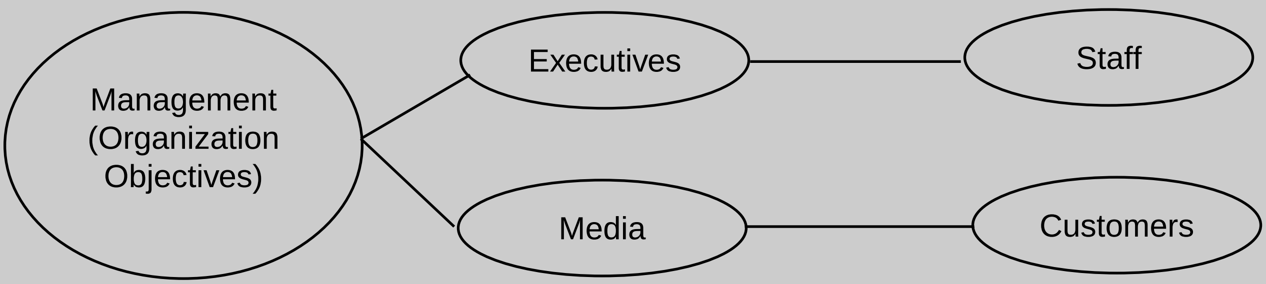
The management at many service oriented organizations, such as financial institutions, are genuinely concerned about service quality. However, in many organizations that I have observed first-hand in the past few years, there were no effective implementation strategies. Many organizations that are concerned with service appear to go through the following steps:

1. Decide at the top level that service quality should be improved;

2. Give pep talks to people in the organization; supply them with slogans such as 'Service Excellence' which they can proudly display on their desks; and

3. Mount a large scale campaign in the media to announce the institution's commitment to excellence in service.

A Model of Communication Frequently Used By Organizations



The chart below illustrates this communication model. Apparently, this model seems to achieve the dual objectives of communicating with the employees and with customers.

However, this model does not include several aspects which would guarantee that management will realize their objectives. Here are some of the key steps that are missing.

(1) Employee feedback and commitment: Did the employees really understand what changes are expected in their behaviour to achieve the objectives? Are they as committed to the objective as management is?

(2) Employee training: Do the employees have the required skills? Is there a continuous mechanism of quality control? For example, over 90% of the customers of banks and trust companies make over 90% of their transactions through tellers. Yet most banks and trust companies simply do not have any formal training program for this most critical service link between the institution and the customer. When a customer receives bad service, the institution's motto and advertising campaign make the customer acutely aware of what he or she is not getting from the institution!

(3) Management backing: Will management back the employees when there is no immediate pay-off? For example, to what extent will the management encourage or even tolerate employees who spend time with customers who are not particularly profitable to the organization? Does the management monitor performance constantly and retrain employees in areas where it is needed?

In other words, what is missing in the most common communication model is the strengthening and monitoring of the vital link that is supposed to achieve the objective: employee commitment, training and management commitment that goes beyond lip service.

What Customer Complaints Don't Tell you

A few years ago, there was widespread discontent about bank service charges. Yet one witnessed the amazing spectacle of different bank spokespersons appearing on TV to state that their customers were quite happy. They received hardly any complaints and everything had been stirred up by the media.

Yet at about the same time, my own research showed that there was not only a widespread discontent but that it as growing.

Assuming that these spokespersons meant what they said, why were they not aware of such an obvious phenomenon?

A Theory of Propagation of Discontent

There is research evidence that shows why customer complaints (especially a lack of them) is a poor indicator of customer dissatisfaction.

Most of the figures quoted below come from research carried out by a Washington-based non-profit research organization called Technical Assistance Research Program or TARP. They conducted a study on complaint handling in the U.S. The accuracy of the actual figures is not very critical. Even if the figures are rough approximations, they form the basis of a paradigm that shows why management has to be careful in using the number of complaints they receive as an indication of customer satisfaction.

Stage 1
Customer Management

- Let us assume that a bank has 1,000,000 customers.
- 10% of them (a fairly large proportion) are dissatisfied. This could potentially generate 100,000 complaints.
- However, in most cases only 4% of those (or 4,000 customers) will actually complain. This reduces the complaint rate to just .04% or just 4 complaining customers for every 1,000.
- Most of these complaints never reach even junior management. Only 1 in 2,000 will take their complaints to the second level. If we assume that the first level of complaints is received by non-management or 'non-recording' employees of the organization, the magnitude of the problem becomes evident.

For instance, a dissatisfied bank customer may complain to the teller. Normally complaints are not recorded at this level. As a result, only 50 complaints or 1 complaint for every 2,000 dissatisfied customers will reach the management.

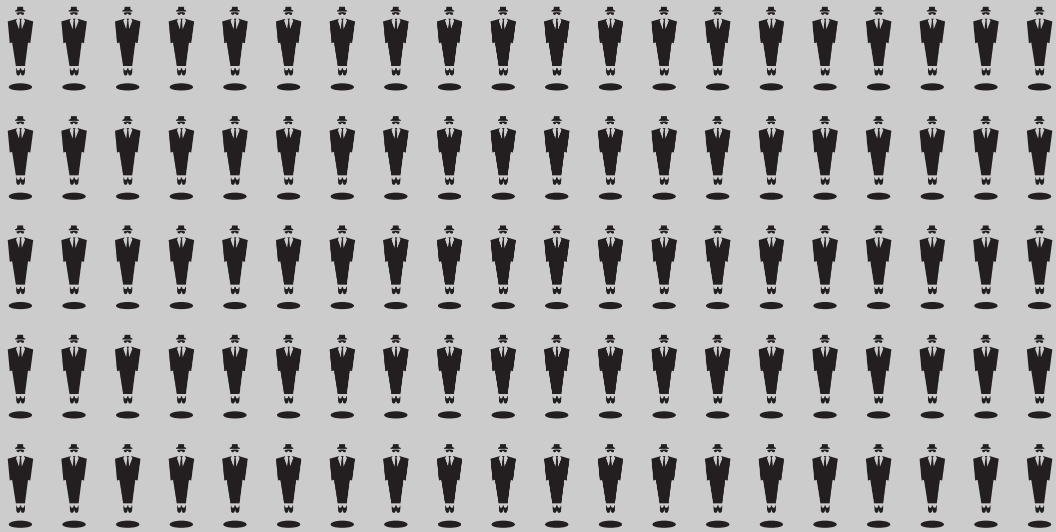
While 10% of the customers are dissatisfied, management is exposed to a complaint level of just .005% of the customers, a trivial proportion by any standard.

Stage 2
Customer to Others

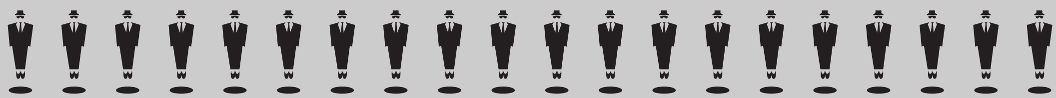
While customers may be reticent about talking to management, they are not so reticent when it comes to others about their institution.

- When a customer has a service problem, he/she will tell 9 or 10 people (13% of the unhappy customers will tell up to 20 other people about the incident.) In our example, 100,000 dissatisfied customers will talk about their dissatisfaction to 900,000 - 1,000,000 others.

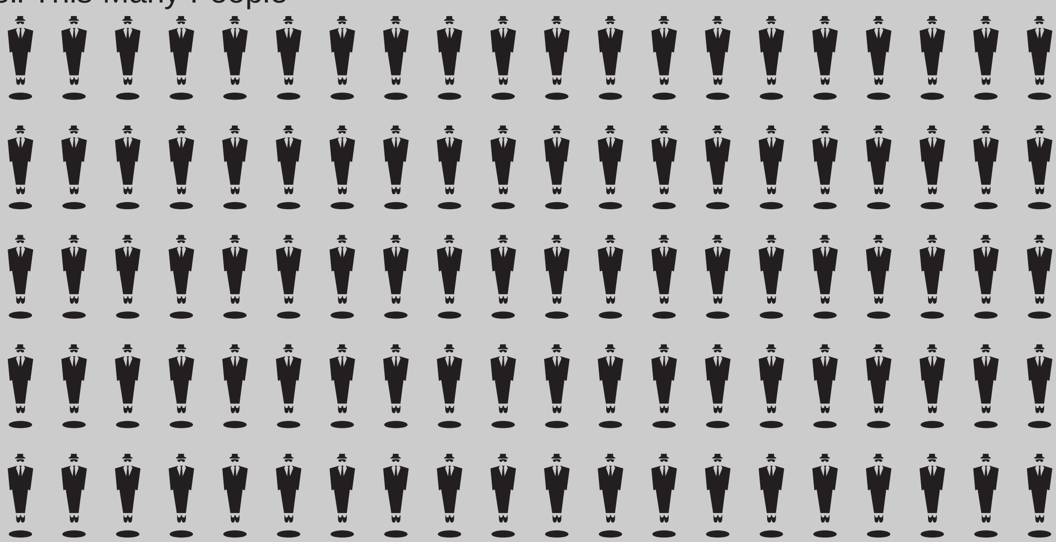
If your customer Base is 1,000,000 people



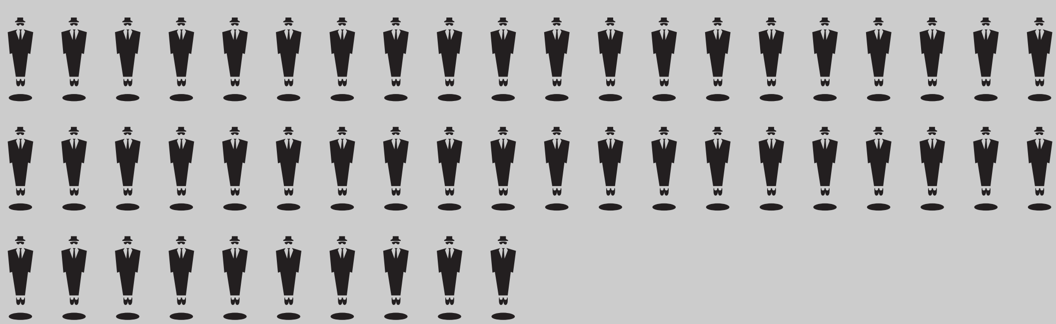
And if 10% of your customers are dissatisfied,
you lose 1,600,000 potential customers as shown below:
Your Dissatisfied Customers



They Tell This Many People



They Do Not Act as Your PR Person For This Many People



The analysis above assumes that they are dissatisfied with a transaction that costs less than $100. If the cost of the transaction is $100 or more, then 10% of the dissatisfied customers result in a loss of 2,500,00 potential customers as shown below:

Dissatisfied customers	100,000
They tell this many people	1,600,000
They do not act as your PR person for this many people	800,00
For a total loss of this many potential customers	2,500,000

Although you have lost 2.5 million potential customers
You would have received only 4,000 complaints at any level.
The number of recorded complaints could be as low as 50!

Reaching 2.5 million customers is likely to be far more expensive than keeping your current customer happy. A happy customer will act as your PR person - each will tell 5 to 8 potential customers.

Now a population that is as large as the example financial institution's customer base (one million people) knows about the poor service!

In fact, it gets worse if the transaction size is $100 or more. In this case, 100,000 dissatisfied customers will tell 1,600,000 people - much larger than the company's current customer base.

The Hundredth Monkey Syndrome
The hundredth monkey syndrome states that if enough people ('critical mass') know about a certain thing, then it becomes common knowledge. (This principle was first identified by Lyall Watson who observed that when a certain number of monkeys learnt a new behaviour, that behaviour was exhibited by monkeys that live in unrelated colonies as well.)

The fact that very few complaints are recorded is no guarantee that customers are happy. The actual level of discontent could be high, and large numbers of people who are not even customers can be aware of it.

Why Customers Don't Complain
Obviously, customers are not reticent. When they are dissatisfied they tell many people. They simply exclude the company management from the list of people to whom they complain. This sounds rather illogical. After all, if anyone could solve the problems the management can. Yet customers avoid contacting the management. Why?

TARP identified several reasons:

- Customers may not know whom to complain to. The bank teller? The person behind the desk? The bank manager (they probably need an appointment and they might need to come back some other time)? Someone at the head office?
- Customers are used to having their complaints handled poorly. Often they are told it is the 'bank policy' (bank policy can sometimes supersede logic and the basic understanding that the customer is the basis of the business). Or customers are reminded that they are being unreasonable, because nobody else seems to complain.
- Customers may feel patronized or ignored when they make a generalized complaint. For instance, customers may complain about poor service which is the cumulative result of many minor things that are not done right. Unless the person receiving the complaint is sensitive and caring (not a common experience) many customers perceive the exercise as completely futile.

Consequently they find walking out (forever) an easier and a more pleasant alternative. Besides, they often feel that it is the job of management, (not their job) to run the organization efficiently.

Satisfied Customers: Do They Compensate?
If a dissatisfied customer tells 10 other people about their dissatisfaction, one might assume that when a customer is satisfied he/she would tell others about it. The assumption is correct - except that satisfied customers tell only half as many people: on average, five other people. In other words, a company needs two new satisfied customers for every dissatisfied customer just to retain its current status.

The Cost of Poor Service
As a matter of fact, keeping current customers happy is much more cost effective than trying to reach new customers to replace them. As the chart above shows, every 100 dissatisfied customers could cost 1,600 to 2,500 potential customers. On the other hand, every satisfied customer works as an unpaid and credible salesperson for your organization. Every 100 satisfied customer tells 500 to 800 potential customers.

Getting the Right Information
By now it should be obvious that dissatisfied customers are extremely expensive to a service organization and special efforts should be made to keep customers happy and satisfied.

It is also obvious that few dissatisfied customers complain and only a fraction of the complaints are even recorded.

The paradigm discussed so far explains how there could be a large gap between the perceptions of management and those of customers.

One possibility is to let everyone in the organization keep detailed records of every complaint. In practice, however, this is not likely to work. In many cases, recorded complaints can turn out to be self-incriminating. In some cases, the customer may state his or her complaint in such an amiable way that it may not be perceived to be a complaint at all by the recipient.

The Role of Research
Can research close the gap? The answer to this is a qualified yes. Those of us who have tried traditional research procedures know that such research procedures do not really provide useful information. These approaches do not really show what customers expect, what ‘quality’ means to them and why and how they are frustrated.

Many institutions that make changes on the basis of traditional research wonder why customers do not flock to them, and why even their current customers continue to be dissatisfied. Briefly, the main problem is that most traditional market research procedures were developed for testing products. These procedures are not necessarily adequate for testing services.

We will see why traditional research procedures are inadequate and what alternatives may be available to researchers in this area in the next article.