Customer loyalty and customer value - 4
Transactions: the building blocks of loyalty

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Correlates of customer loyalty
What is the basis of customer loyalty? How can we create customers who are loyal? In the previous article we noted some demographic and psychological correlates of loyalty. For instance, relatively older and less educated customers tend to be loyal; innovators and risk-takers tend to be less loyal. However, we need to note that:

Demographic and psychographic variables just influence - but do not decide - customer loyalty; and

There are variables that we can influence to create customer loyalty.

Transactions, quality and loyalty
The variables we can influence are transactional in nature. Transactions can be seen as the basic units of business. A customer uses an organization through a series of transactions such as calling the organization to get some information, bringing the product in for service, returning a product for a refund or buying an additional product or service from the organization. Transactions involve personal experience with the organization. This personal experience in turn leads to judgements with regard to quality. Higher quality perceptions lead to loyalty (see Exhibit 1).

Changes over time
How do these three attributes behave over time?

Obviously the transactions that a customer has with an organization will vary from time to time. As a result, a customer's experience with the organization can potentially change from year to year.

This is not true for a vast majority of customers who have minimal and predictable contact with the organization. But we already saw why such customers are not necessarily profitable for the organization. Profitable customers tend to be heavy users and are the customers we are primarily concerned with. Heavy users tend to have varied transactions and hence varied experiences with the organization.

This leads to potentially different perceptions of quality over a period of time. Since perceptions of quality affect loyalty, the heavy user's loyalty is more volatile than that of the light user.

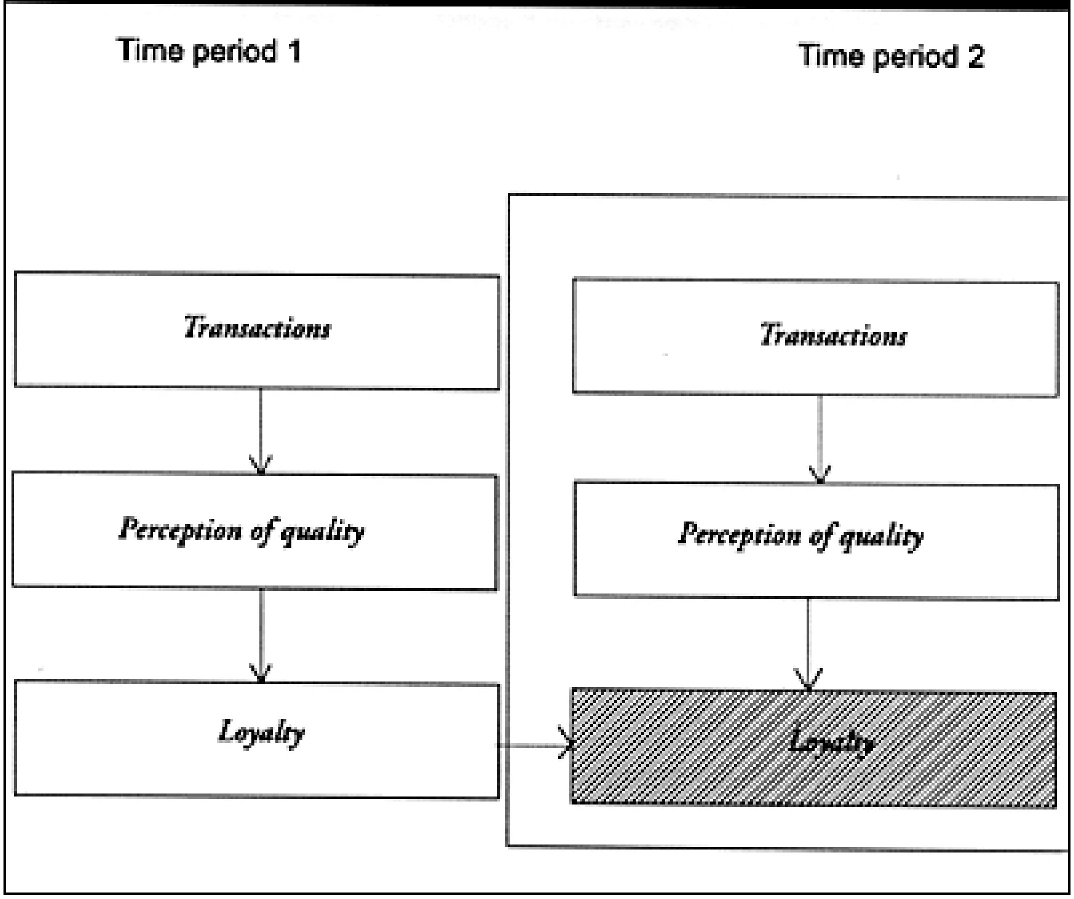
Studies by Terry Gleason (Customer Loyalty: A challenge for the 90's. A presentation to the Measurements Research Sym?posium 1995) and others indicate that perceptions of quality directly influence loyalty.

However, the effect is not symmetrical: Perceived high quality may induce customer loyalty, but perceived poor quality induces customer disloyalty even more. Customers - especially the profitable ones - tend to punish the firm severely for lack of quality. They also reward the firm with loyalty for delivering high quality performance, but they do so with less intensity.

How do transactions, perceptions of quality and loyalty change over time? For heavy users, at least, transactions change from year to year. They are not necessarily correlated over a period of time. Since perceptions of quality are related to transactional experiences, they do not stay stable over a period of time.

What about loyalty? Loyalty is affected by perceptions of quality and therefore we would expect it to change from time to time as well. However, loyalty seems to be more stable than quality or transactional experience, although loyalty is influenced by both factors. Loyalty is not only a function of perceived quality, it is also a function of past loyalty. It is not clear why this is so. Some possible hypotheses could include inertia (continuing the same past behaviour patterns), cognitive dissonance (exhibiting consistency in behaviour) and the tendency to temper current judgements of quality with past experiences.

Exhibit 2
Past loyalty affects current loyalty



As customers experience different transactions from year to year, they tend to modify their perceptions of quality and their decision to be loyal. In addition to current transactional experience and the resultant perception of quality, past loyalty also affects current loyalty.

Pitfalls of transactional measurements

Since transactions form the basic building block of loyalty, measurement should start at this level. However, many measurement systems fail at this stage. The main reason for this is the assumption of an existence of correspondence between what needs to be measured and what is measured. As a result whenever there is an improvement in what is measured, it is assumed that there is an improvement in what is delivered. Unfortunately, in many cases, this assumption is incorrect.

Here are a few actual examples where measurements showed transactional improvements with actual deterioration in quality:

- ·A telephone company attempted to measure transactional efficiency using the number of minutes a customer was on hold. The waiting time showed measurable improvement. The firm failed to notice that the service representatives ignored many calls during busy periods, thereby decreasing the waiting periods for those whose calls were picked up. The frustration of customers who abandoned the calls was not reflected in this transactional measure of wait time.
- A financial institution, which asked representatives to keep a record of customer queries/complaints along with comments as to whether the problems were successfully dealt with, found an increase in the number of 'successful dealings'. Many representatives 'successfully dealt' with customers by simply transferring them to another person in the organization.

Measuring transactional efficiency is not always straightforward. A good transactional measure should have a high degree of correlation with the transaction rather than with the measure that purports to capture the transaction.

Measuring relationship

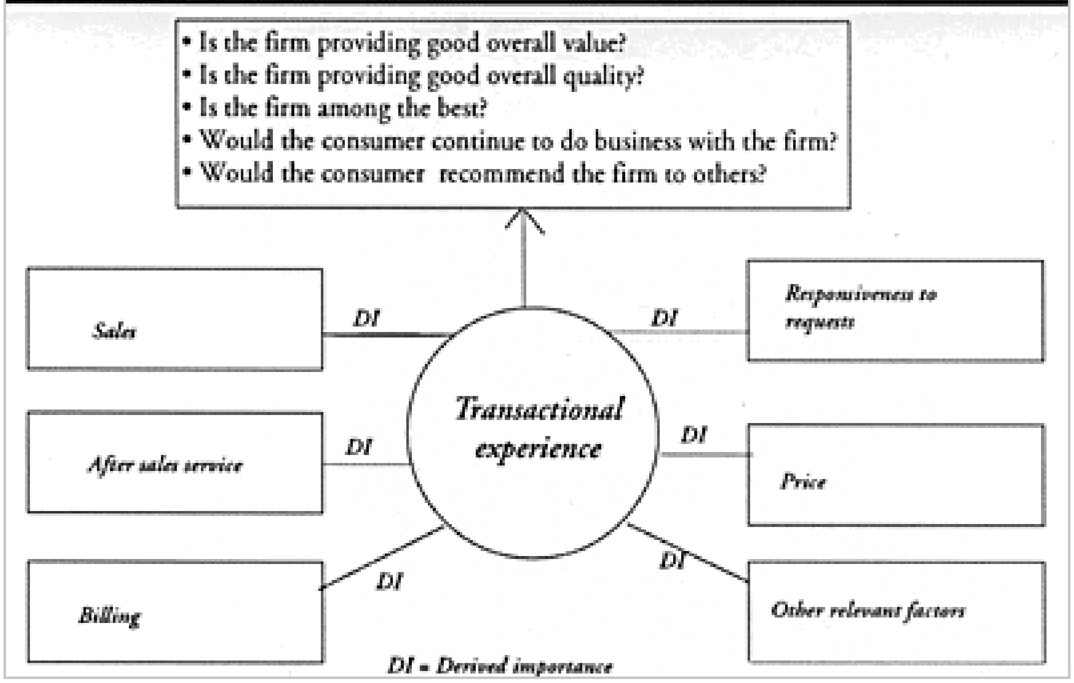
In the previous article we noted that loyalty is not an attribute of the customer but refers to the relationship with the customer. Consequently, we need to measure the relationship between the company and the client.

What constitutes a relationship between a firm and a customer? Broadly speaking, every transaction between the two is a way relationship. However, what is critical is the firm's performance with respect to customer priorities. It is this match that creates a relationship and the perception of quality. Some of the critical aspects are:

- Is the firm providing good overall value?
- Is the firm providing good overall quality?
- Is the firm among the best?
- Would the consumer continue to do business with the firm?
- Would the consumer recommend the firm to others?

The above judgements are based on the transactional experience of customers with the firm. Such transactional experiences are predicated and can arise in a number of areas such as an experience with the sales representatives, experience with the service personnel, price and accuracy of transactions filtered through demographic and usage attributes.

Exhibit 3
Aspects of loyalty



Derived importance
To arrive at the contribution of each of these variables to the critical aspects of relationship, we can derive the importance of each one of these attributes through (1) survey research to obtain customer reactions and (2) by using statistical techniques to estimate the derived importance. The higher a customer rates a firm on the above attributes, the more likely it is that he or she will stay loyal to the firm. We need to understand what influences customer judgements. As a result, it becomes important for us to understand how customers' experiences influence their overall judgments as exemplified in the critical areas mentioned above. Essentially our analyses attempt to clarify the impact of different attribute ratings on overall measures.

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