Customer satisfaction: Do you know the score?

Now, more than ever, companies across industries are realizing the importance of "putting the customer first;" paying attention to customer satisfaction translates to enhanced shareholder value. Surprisingly – although corporations have spent millions on ad campaigns, IT solutions, new customer service programs and organizational changes – customer satisfaction levels, across almost every industry, continue to erode. Can the downward trend be reversed? Is it really worth the effort?

By Melody Badgett, Whitney Connor and Jennifer McKinley

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Customer satisfaction—the score matters

In today's marketplace, customer dissatisfaction is a pervasive problem–unfortunately it is not a new one. Between the first quarter of 1995 and the third quarter of 2001,[1] the American Customer Satisfaction Index (ACSI) cross-industry average dropped 2.6 percent, with several sectors falling 3 to 5 times that amount.[2]

Even within sectors that have faired better than average, individual industries and major players have experienced declines. For example, although Retail customer satisfaction ratings remained relatively flat between the fourth quarter of 1994 and the fourth quarter of 2001, one major player experienced an 8 percent decline during that same period.[3]

The sad state of customer satisfaction assumes additional significance when one examines the downstream effects. When customers are not happy, they stop spending. In fact, when adjusted for the one-quarter lag, consumer spending trends correspond closely with customer satisfaction (see Figure 1).

Consumer spending and customer satisfaction

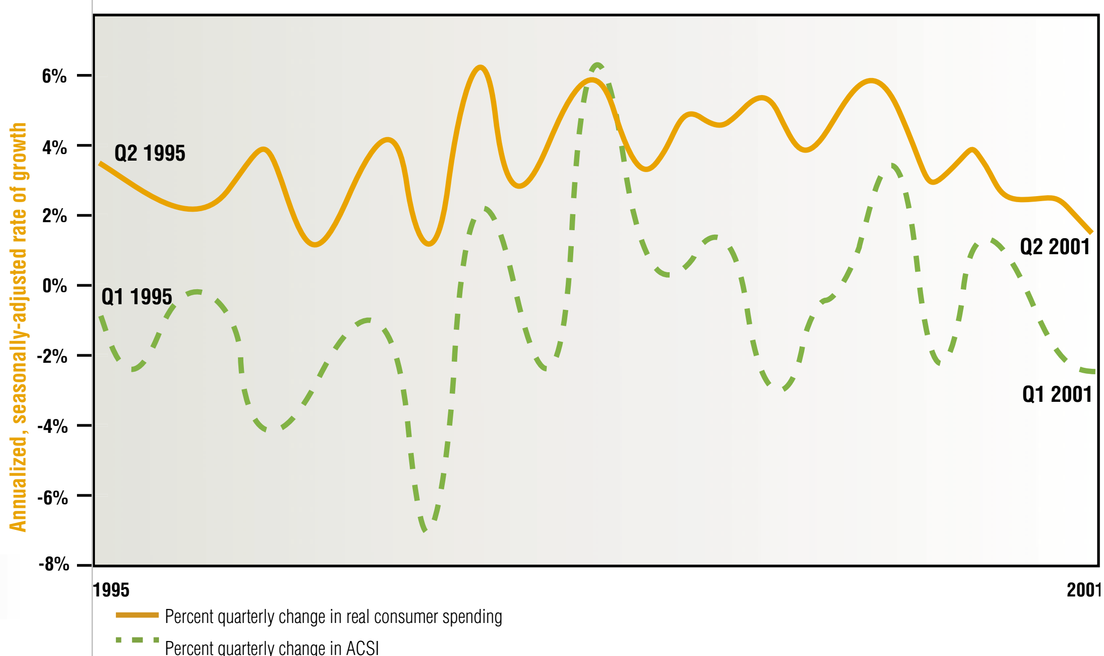


Figure 1. When customers are unhappy, they stop spending.

Note: One quarter lag beween customer satisfaction decline and consumer spending decline.

Source: Professor Claes Fornell. Director, National Quality Research Center, University of Michigan Business School. Consumer Spending Depends on Customer Satisfaction. *August 20, 2001.*

The average customer with an unresolved complaint will tell nine to ten people.[4]

Dissatisfaction has a clear impact on shareholder value. Simply stated, if customers stop spending, corporate profitability suffers. Unhappy customers shy away from the companies that have disappointed them. Making matters worse, those frustrated customers may share their unfavorable opinions, driving away potential new customers.

Unfortunately, the impact doesn't stop with lost revenue; costs go up too. Businesses are forced to spend more on customer acquisition, trying to replace losses in their customer base. Plus, companies must absorb the expenses associated with resolving customer complaints. With profits eroding on several fronts, the association seems obvious: *customer satisfaction can significantly impact shareholder value*. When the ACSI is compared to S&P earnings growth over the past six years (see Figure 2), the assumed association becomes even stronger.

Impact of customer dissatisfaction on shareholder value

Figure 2. If customers stop spending, corporate profitability suffers.

Note: One quarter lag beween customer satisfaction decline and consumer spending decline.

Source: Professor Claes Fornell, Director, National Quality Research Center, University of Michigan Business School. Customer Satisfaction and Corporate Earnings. *May 21, 2001.*

Blame game

So, what is going wrong? Why are corporations today failing to please so many customers? It seems there are plenty of excuses to go around:

The economy

Corporate budgets are tighter. Companies are spending less on customer care programs, customer service training and new customer-related technology, which can lead to poor customer service in the short term and declining customer loyalty over the long term. With less disposable income, customers have become more price-sensitive and more discriminating about where they will spend their limited dollars.

Although the slowing economy makes customer retention and acquisition more difficult, keeping good customers is more important than ever. According to recent interviews with senior executives, priorities and areas of focus have shifted as revenue growth has slowed. Companies are making tactical adjustments in response to ongoing economic pressure. Businesses are spending more time "hand holding" current customers and offering scaled-down products priced to fit constrained customer budgets. In good times—but even more so in bad times—retaining customers is much more cost-effective than acquiring new ones. Unfortunately, customer dissatisfaction can halt both.

Technology

With all that has been spent on understanding customers better, we should be exceeding expectations at every turn. Has technology failed us?

Information technology advances over the last decade provide benefits to both businesses and consumers. Companies can segment customers across a variety of dimensions and learn more about them as they shop, purchase and communicate directly with the business in realtime. Consumers enjoy more targeted services and communication, up-to-the-minute status information, "anytime, anywhere" access and a wealth of data at their fingertips for price and product comparisons.

But, there are some downsides:

- Convenience provided by technology is great… but, with so many new channels for serving customers, customers themselves can get lost in the shuffle.
- Personalization can be beneficial… but, with access to increasing information about the customer, companies can target to such an extent that they cater to the elite (most profitable customers) at the expense of the masses (rest of the customer base, often up to 80 percent of all customers).
- Information enriches the customer experience… but it also elevates customer expectations.

Customers themselves

Frustrated, many executives are beginning to believe that customers are impossible to please; their expectations are simply too high. Businesses sense a growing culture of entitlement where customers expect privileges and perks in return for their loyalty—and their information.

Customers, on the other hand, have the opposing view. They believe their demands are reasonable, usually centered around trust and respect, and do not find themselves difficult to satisfy. Indeed, some customers' expectations may be so low at this point that it would take very little for them to have a pleasant interaction with a company.

There are winners… and there are losers

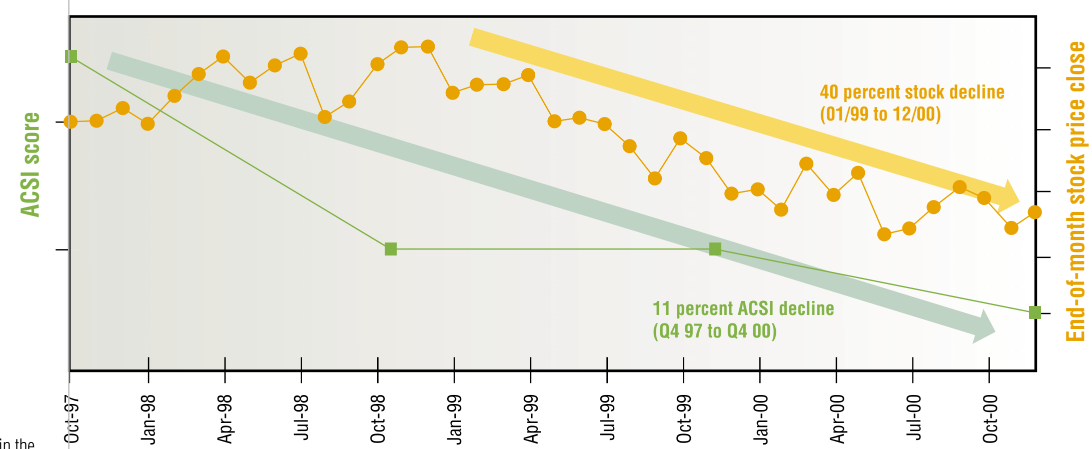
While the challenges may seem insurmountable, companies can – and are – bucking the downward trend. Sector by sector, industry by industry, winners are distancing themselves from the rest of the field. At the IBM Institute for Business Value, analysts took a closer look at some of the winners – and losers – to learn more about which activities are making a difference and how these companies' customer satisfaction results relate to shareholder value.

Banks

Some retail banks are making customers happy by offering personalized, responsive products and services. Winners are investing in new technologies, like wireless access, that provide customers with increased flexibility and implementing software that distributes and manages customer information so that banks can respond faster and more comprehensively. They are also investing in their front-line employees, rewarding tellers for delivering high quality service and empowering them to make key decisions on their own.

On the flip side, some banks frustrate their best customers by providing uniform service to everyone. Recent rounds of consolidation in the banking industry have been particularly damaging: firms have delivered inconsistent and confusing information related to a merger's impact on accounts and service contracts and customers have had difficulty putting their confidence in an institution that they fear may soon disappear.

Loser: A top 20 U.S. retail bank



ACSI - Reported annually in the fourth quarter (Q4 97 - Q4 00), score graphed on first month of the quarter

Stock price - Closing price on last day of each month (10/97 - 12/00)

Figure 3. This bank lost two customers for every new customer acquired.

- Allowed a rocky merger to distract employees and affect customers
- Implemented a new application that, unfortunately, made it difficult for customer service representatives (CSRs) to deliver acceptable service
- Failed to provide enough information for CSRs to sound confident and knowledgeable
- Structured teller incentives to reward acquisition, not retention.

Winner: A top 20 U.S. retail bank

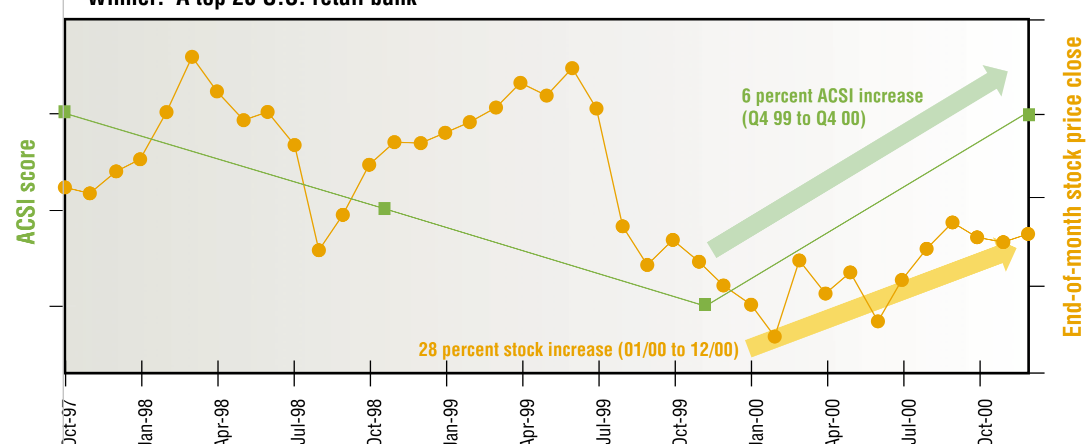


Figure 4. This bank's stock price increased over 25 percent in 2000.

- Initiated a formal customer satisfaction measurement program
- Established a multi-million dollar alliance partnership to develop offerings specifically targeted at small- and medium-size businesses
- Revised policies to empower tellers to be more customer-friendly, enabling on-the-spot problem resolution
- Implemented workflow automation to improve response time.

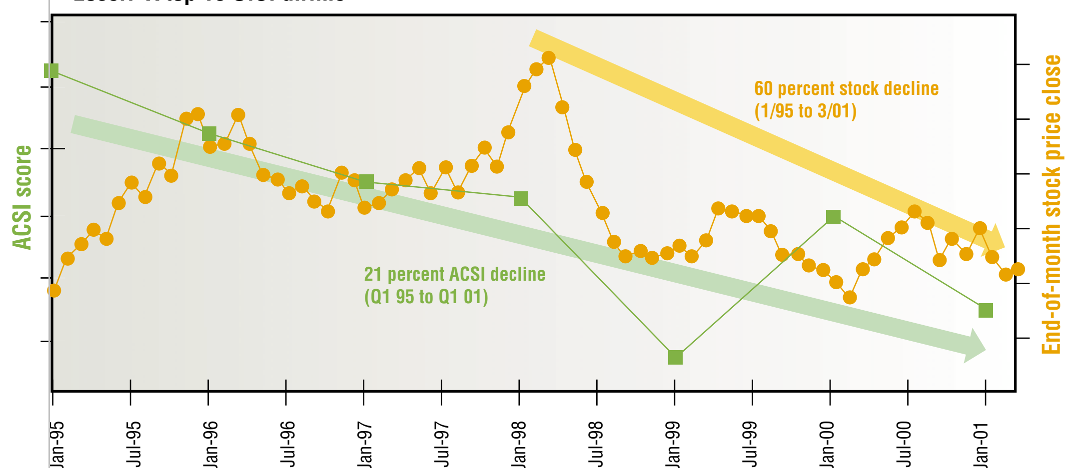
Source: American Customer Satisfaction Index (ACSI), IBM Institute for Business Value analysis

Airlines

Despite a logistically complex industry backdrop, winning airlines have made customers happy by delivering on promises and demonstrating attentiveness to customer care. Winners focused on improving the aspects of service that matter most to their customers: on-time arrivals, fewer denied boardings, appropriately handled baggage and general responsiveness to complaints.

In contrast, the losers turned frequent flyers into frustrated flyers with deteriorating service levels. As an industry, the on-time arrival percentage dropped from a poor 76 percent in 1999 to an even lower 73 percent in 2000 while the mishandled baggage average rose from 5.1 to 5.3 bags per 1000 customers during the same time period.[5] Some airlines have aggravated customers even further by eliminating perks, like in-flight snacks and special meals for children, overlooking discourteous flight attendants and ignoring issues with check-in processes.

Loser: A top 10 U.S. airline



ACSI - Reported annually in the first quarter (Q1 95 - Q1 01), score graphed on first month of the quarter

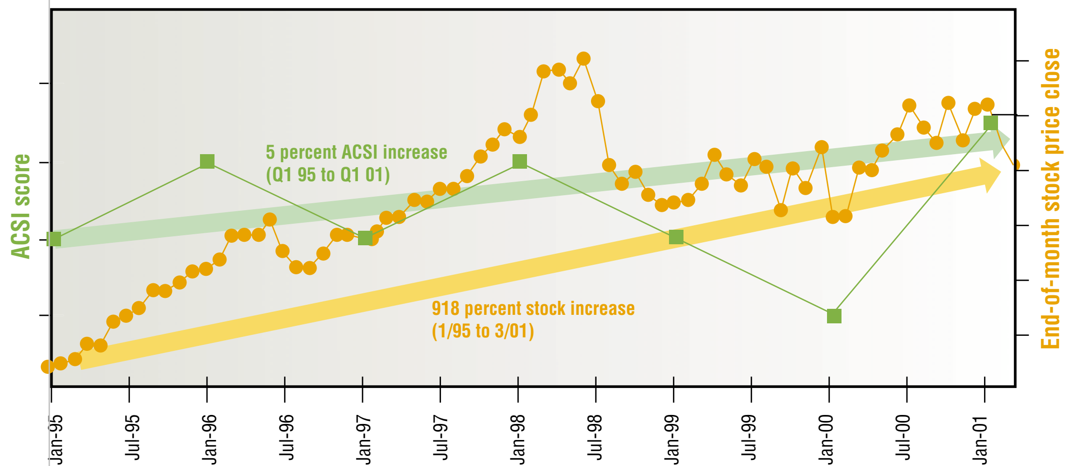
Stock price - Closing price on last day of each month (1/95 - 3/01)

Figure 5. This airline's stock price declined over 50 percent in three years, commensurate with a 5 percent decline in quality ratings.

- Failed to deliver on the basics: declining on-time arrival record coupled with an upward trend in mishandled baggage
- Limited customer choice by dominating gates in several major markets
- Gained notoriety one year as the carrier with the highest frequency of customer complaints and worst on-time performance.

Source: American Customer Satisfaction Index (ACSI), IBM Institute for Business Value analysis

Winner: A top 10 U.S. airline



ACSI - Reported annually in the first quarter (Q1 95 - Q1 01), score graphed on first month of the quarter

Stock price - Closing price on last day of each month (1/95 - 3/01)

Figure 6. This airline's stock price increased over 900 percent between 1995 and 2001.

- Increased focus on customer service enterprise-wide, led by the CEO
- Initiated employee contests to encourage "perfect attendance" (saved millions by reducing absenteeism)
- Rewards employees when company achieves specific, high-priority goals such as industry-leading on-time arrival performance
- Offers best customers a different class of baggage handling
- Ranked number 1 for on-time arrivals, with nearly 80 percent on-time flights.

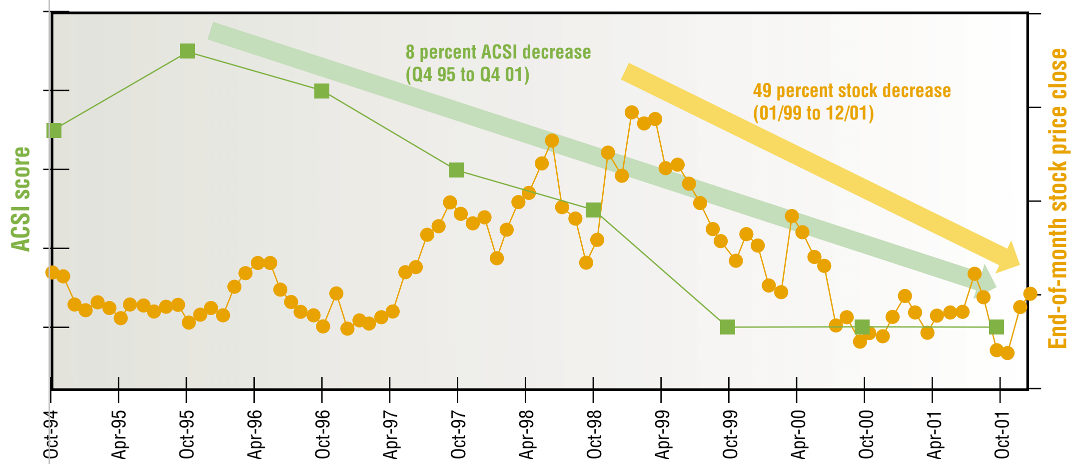
Retailers

Customers feel special when retailers provide personalized services – appropriate product recommendations, well-targeted promotional mailings and customer service representatives that know "their" customers' shopping habits and preferences. As expected, winning retailers give customers a choice of when, where and how to interact with the company and provide consistent levels of service across all of these channels. To accomplish this objective, leading retailers typically arm customer service representatives with an up-to-date customer profile that encompasses all types of interaction.

On the other end of the spectrum, losing retailers have difficulty maintaining adequate numbers of employees, resulting in long lines at the counter and on the phone. They offer primarily mass-produced products, with few options for customized products or services. Some retailers are driving customers away by continually raising prices.

Source: American Customer Satisfaction Index (ACSI), IBM Institute for Business Value analysis

Loser: A large, well-established U.S. retailer



ACSI - Reported annually in the fourth quarter (Q4 94 - Q4 01), score graphed on first month of the quarter

Stock price - Closing price on first day of each month (10/94 - 12/01)

Figure 7. This retailer's stock price declined over 45 percent in two years.

- Set extremely high expectations around customer service, offering personalized VIP service, a generous return policy and free alterations, but then failed to meet these expectations
- When service levels declined, experienced significant customer satisfaction backlash because expectations were so high.

Winner: A large, well-established U.S. retailer

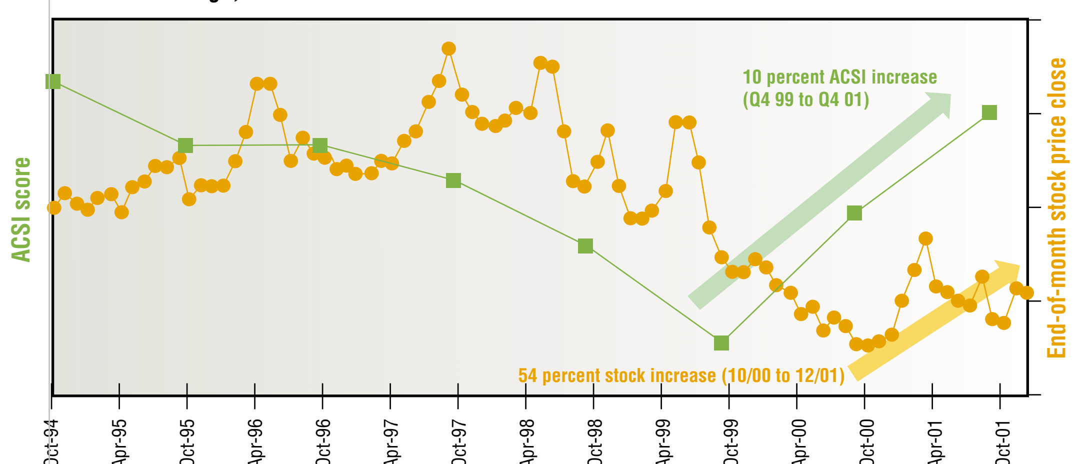


Figure 8. This retailer's stock price increased over 50 percent in one year, with a 10 percent improvement in ACSI rating.

- Experienced significant decline in customer satisfaction from 1995 to 1999, but recently turned numbers around by focusing on customer service improvement
- Split some stores into two in order to create a more pleasant shopping experience and offer a better assortment of products
- Reconfigured product mix to better meet customer demands.

Source: American Customer Satisfaction Index (ACSI), IBM Institute for Business Value analysis

Play to win

With customer satisfaction, winning depends on designing an appropriate strategy, executing it well and making mid-game adjustments as necessary. Practically speaking, your results depend on how well your business performs in the following areas:

Knowing your customers

Businesses should understand what customers value—and how valuable each customer is to them. By getting to know customers better as they progress through their lifecycle, from prospect to new customer to loyal customer, businesses can learn what products and services to offer. Segmentation abilities improve: general demographic groupings mature into needs-based segmentation, which eventually grows into specific segments based on purchase and preference patterns.

Another important segmentation dimension is a financial one: knowing the profitability of serving specific customers within each segment. Once customers are classified by profitability, businesses can:

- Identify characteristics of their most profitable customers
- Target similar candidates in lower profitability rungs
- Decide how to serve each level economically (see Figure 9).

However, *no* customer should be served poorly; every customer—regardless of economic worth to the business—has the ability to positively or negatively impact a company's reputation. The key is providing respectable service for each tier, at a cost that is commensurate with the revenue potential. With a limited budget, it's critical to plan out an optimal distribution of customer-retention dollars, in order to produce the largest return possible. Focusing on share-of-wallet and expanding relationships with existing customers is a more cost-effective way to influence profitability than paying the high costs associated with acquisition.

Economics of customer value

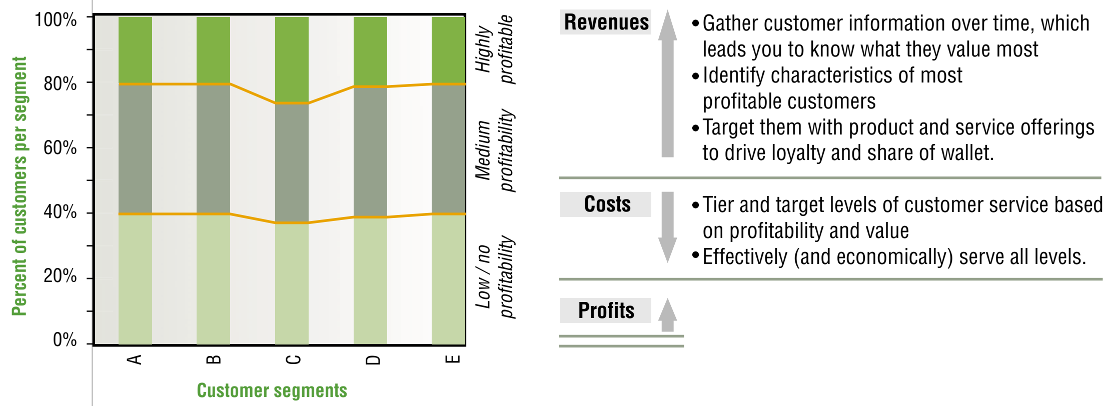


Figure 9. Understanding customer segment profitability helps to drive customer strategy.

Source: IBM Institute for Business Value.

Businesses today may rely on only 20 percent of their customers for 80 percent of their profit. Given the volatility of the marketplace, this can be a precarious position. But if firms can migrate medium-profitability customers up to profit levels of those in the high-profitability tier, they can ultimately reduce risk and increase overall revenues.

Many companies today are focusing on top-tier customers. However, medium profitability customers may well be the tier of greatest opportunity. Because the bulk of a company's customers usually fall into the medium profitability tier, the sheer size of the opportunity is attractive. More importantly, if one assumes a ceiling on attainable share-of-wallet per customer, high-profitability customers—who are probably big spenders with the company already—are likely to be approaching their spending limit with the company, making it difficult to expand the relationship. By increasing wallet-share of the medium-profitability customer instead, companies can broaden the customer base over which high profitability is spread, increase total profitability and, at the same time, reduce risk (see Figure 10).

Customer migration strategy

Purchase profile	Negative	Positive
High	**Medium profitability: Maintain** Maintain those who are high spenders but do not exhibit high value potential beyond their current state. *Keep them satisfied, but don't go above and beyond to try to serve them since value potential is already maximized.*	**Highly Profitable: Expand** Expand those that are already repeat customers and are good candidates for advanced products and services and increased share of wallet. *Ensure that they receive top-quality, standard services and offer targeted new services based on customer profile data.*
Low	**Low or no profitability: Phase out** Phase out those who are neither big spenders nor have a high degree of potential spending based on demographic and traits that would require too much time and money to change their ways. *Don't spend extra cost or effort to retain segments in this category, and in some circumstances, actively phase them out.*	**Medium profitability: Migrate** Migrate those exhibiting high value potential (that is, show characteristics similar to highly profitable customers) but currently spend a minimal amount of money with the company. *Maintain top-quality, standard services, begin to build a relationship with these segments and slowly offer targeted new services based on customer profile data.*

Attractive demographics and traits

Figure 10. Satisfying your customers and knowing your customers go hand-in-hand; know what they want, frame expectations based on what they value, and deliver accordingly.

Source: IBM Institute for Business Value.

Making sure your customers know you

Companies can significantly influence customer satisfaction by clearly framing expectations and actively delivering what is promised. When it comes to expectations, businesses frequently fall into a few traps. Sometimes, companies do not set specific expectations with their customers – and then they seem surprised when they don't meet the expectations that the customers invented on their own. Once their customer strategy is set, businesses need to communicate a clear value proposition: Tell customers exactly what to expect, and then do what is said.

A second common trap is particularly alluring to businesses that are extremely focused on pleasing the customer. These companies have a keen understanding of what customers want and attempt to be "all things to all people." But, because their focus is fragmented across so many dimensions – from convenience to consistent products and prices to customer experience – these companies fail to excel in any one area. To increase the odds of surpassing customer expectations, a business should not focus on "what customers want" but rather "what customers *value most*," concentrating the majority of their efforts on being great at the top one or two customer value drivers that matter most.

The terms *customer satisfaction* and *customer service* are often used interchangeably, but customer satisfaction is broader than just good customer service; it includes many other factors such as the type of experience offered, product quality, accessibility and price. When it comes to satisfying customers, winning companies realize it's best not to try to be "all things to all people." They focus on one or two key attributes in order to deliver what their customers value (see Figure 11).

Primary and secondary attributes of brokerage houses	Charles Schwab	Quick & Reilly	Merrill Lynch
Primary focus	**Multiple access options** • Serves investors of all levels and empowers them to make their own decisions • Melds technology and people to provide an integrated "high tech" and "high touch" service with either "do it yourself" or full-service options • Pioneered and lead the move to online investing • Customers can access their accounts through one of over 400 branches or join over 4 million others with online accounts.	**Discounted prices** • Offers access to personal financial consultants whose goals are wealth building for customers, not generating commissions • Offers attractive products and pricing • Offers easy to understand and detailed pricing information on the Web.	**High-touch and quality service** • Provides access to experienced and knowledgeable financial advisors • Provides access to highly qualified money managers • Offers combined services for investing and banking activities • Offers comprehensive online investing services.
Secondary focus	**Fair and competitive pricing** • Highlights its fair pricing • Doesn't always offer the lowest prices, but strives to offer competitive commissions and rates.	**Choice of 24/7 access options** • Offers "do it yourself" Internet trading, integrated banking and brokerage online through Fleet HomeLink, phone or wireless access • Serves customers through 100 Investor Centers and a 24-hour customer service center • Features 24/7 access that offers choice and accessibility regardless of where, when, and how customers choose to work with them.	**Takes care of its customers** • Strong brand and reputation creates ambiance of excellence and quality • Offers "hand holding" in addition to advice so investors feel cared for and important • Offers an online learning channel where investors can learn the basics of financial planning and investing • All customers are treated with respect and as valuable customers.

Figure 11. **Companies that offer similar products and services differentiate themselves by the service attributes they choose to emphasize.**

Source: www.charlesschwab.com; www.quickandreilly.com; www.ml.com; IBM Institute for Business Value analysis.

Lastly, companies must sidestep the temptation to set unrealistic expectations. Before making promises to customers, businesses should be certain that they have the wherewithal to deliver. Saying one thing and doing another is a sure way to disappoint customers.

Know how well you are performing… all the time

Sensing and responding to customer satisfaction issues requires companies to look beyond historical, surface-level indicators (see Figure 12). They are not specific enough to help you pinpoint problems… or opportunities. Businesses should watch for indications of how customers are reacting to the company's efforts (ROI per customer) as well as which factors may be influencing customer satisfaction (employee retention).

Indicators historically watched	New customer-centric indicators to watch
Market share	• Share of most valuable customers • Conversion rate and cost (from interested consumer to customer) • Customer lifetime value (customer retention) • Quality elasticity of demand.
Number of customers	• Share of wallet • ROI per customer or customer segment • Fluctuations in profitability • Customer reaction rates to marketing/promotional offers • Number of repeat visits, frequency of repeat visits, and repurchase probability • Periodic, primary research • Customer comments.
Number of employees	• Employee retention and satisfaction • Turnaround time associated with the resolution of complaints/inquiries.

Figure 12. A broader perspective can offer better insight into customer satisfaction drivers.

Source: IBM Institute for Business Value.

31 percent of customers with major problems never complain, and 97 percent of consumers that encounter minor problems do not bother to complain.[6]

Up to 70 percent of complainers will return to your business if their complaint is resolved. Up to 95 percent return if the problem is resolved quickly.[7]

Knowing where to improve

Direct customer feedback – both good and bad – can be your best source of emerging market trends and new product ideas. Successful businesses create ways to continuously "listen and learn." Although it seems paradoxical, businesses benefit when customers complain. A vocal dissident is rarely the only customer who is unhappy.

Unfortunately, most consumers never bother to tell the business when they have been disappointed. (They do manage to tell several other consumers, however.)

Most importantly, by speaking up, customers give companies the opportunity to correct the situation. Taking swift action can potentially save a valuable customer relationship and stem negative word-of-mouth.

By consistently recording and closely evaluating customer complaints, inquiries, feedback and purchasing activity, businesses can identify unmet needs and potential problems. Companies can use the resulting insights to refine their customer strategy and improve operational execution. Given the pace of today's marketplace, an annual or even quarterly checkpoint on customer satisfaction is inadequate; companies should measure and make adjustments continually.

Customer service principles

Do	Don't
• Segment and tailor offerings • Set realistic expectations • Focus on retention and profitability • Establish methods to prevent mistakes • Respond expeditiously to complaints • Demonstrate value with values • Learn how to migrate customers toward more-profitable relationships • Compensate customers for your mistakes, according to value	• Settle for simplistic segmentation • Set false expectations • Misrepresent value provided • Serve half-heartedly • Assume customer is to blame • Treat less-profitable customers as "third-class" citizens • Respond slowly or reluctantly to customer concerns • Offer a poor "resolution" to a problem

Figure 13. What to do and and what not to do.

Source: IBM Institute for Business Value.

Improving your game

Customer satisfaction is inexorably linked to shareholder value. It is a truism: pleasing customers keeps them happy… and buying. With today's constrained budgets and constant earnings pressure, businesses simply cannot afford to lose valued customers.

To discuss how we can help your organization improve customer satisfaction, please contact us at *bva@us.ibm.com*. To browse other resources for business executives, we invite you to visit our Web site at

ibm.com/services/strategy

About the authors

Melody Badgett is a Senior Consultant and Whitney Connor is a Consultant in the Customer Dynamics Group at the IBM Institute for Business Value. They produce research for the Institute's member program, the IBM Business Value Alliance. You can contact Melody at *mbadgett@us.ibm.com* or Whitney at *connorw@us.ibm.com*.

Jennifer McKinley heads the Customer Dynamics Group and leads the member programs within the IBM Institute for Business Value. She can be contacted at *jmmckin@us.ibm.com*.

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Contributors

Hathaway Bowen, Associate Consultant, IBM Institute for Business Value.

References

[1] Because Q4 2001 was impacted by the September 11th tragedy, which led to a temporary increase in consumer tolerance, Q4 2001 data was not included. Thus, this report only includes ACSI National Average Scores from Q1 1995 to Q3 2001.

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IBM Global Services
Route 100
Somers, NY 10589
U.S.A.

Produced in the United States of America
06-02

G510-1675-00