Services Marketing: Integrating People, Technology, Strategy
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Lecture 31 - Managing Relationships and Building Loyalty - Part 2

Welcome to services marketing. And now we will talk about module 31st.

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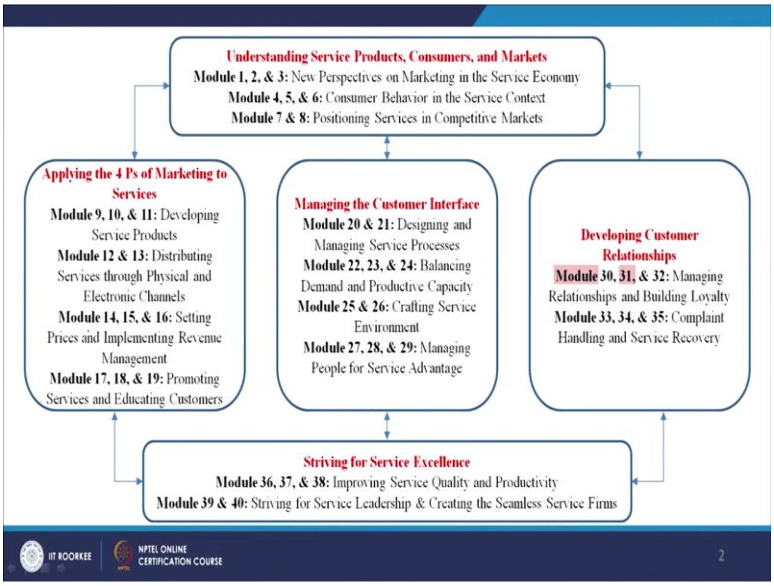

So as you know that this is a module that covers managing relationships and building loyalty. So we this this section is comprises of three module, module 30, 31, 32. And we have talked about module 30, and now we will start with module 31, and we are still talking about managing relationships and building loyalty. Now let us see, what are the topics that will be covered in this module.

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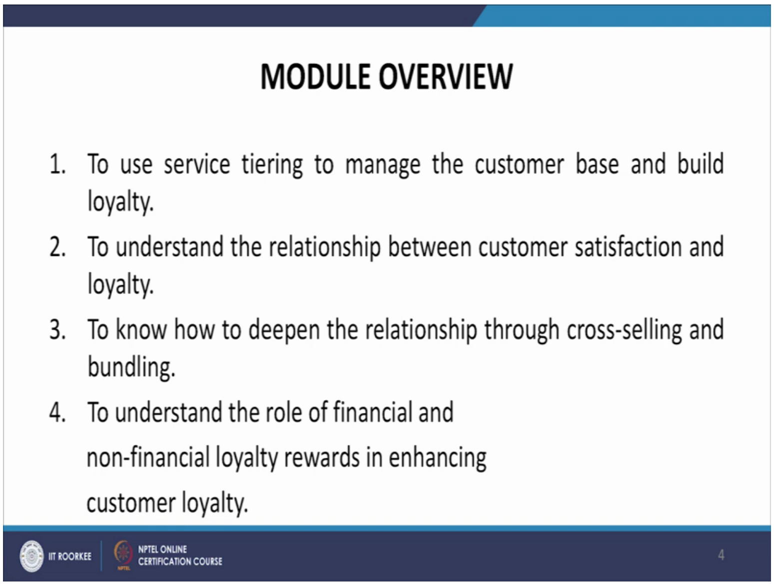

The first is, we will try to understand how to use service tiering to manage the customer base and build customer loyalty. Then, we will understand the relationship between customer satisfaction and loyalty. And then, we will try to understand to know how to deepen the relationship between cross-selling and bundling. And then, to understand the role of financial and non-financial loyalty rewards in enhancing customer loyalty.

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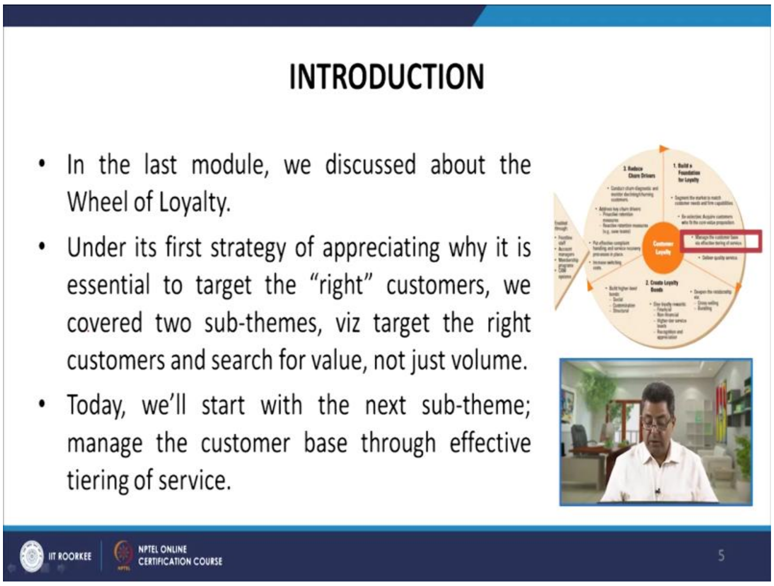

So, now to introduce, in the last module we have discussed about the Wheel of Loyalty. So, this is the Wheel of Loyalty that you can see at the right hand side. We have talked about that in the last module. So, it is about building customer loyalty, so that is the first is to build a foundation for loyalty. Then, moving on to create loyalty bonds. And the third is to reduce churn drivers. So, we are talking about this thing.

Under its first strategy of appreciating why it is essential to target the right customers, we covered two sub-themes, that is targeting the right customers and search for value, and not just volumes. Today, we will start with the next sub-theme, managing the customer base through effective tiering of service. Managing the customer base through effective tiering the service. So I will explain these concepts in a moment.

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So, this Wheel of Loyalty is for building a foundation for customer loyalty, and we are talking about managing the customer base through effective tiering of services. So, marketers should adopt a strategic approach to retaining, upgrading, and even ending relationships with the customers. So, it is not about retaining and upgrading relationships but also about ending relationships with the customers.

Customer retention involves developing long-term, cost-effective links with customers for the mutual benefit of both parties, but these efforts need not necessarily target all the customers of a firm with the same level of intensity, because this intensity will be different for different level of customers, different targets of the customers. Customer profitability and return on sales can be increased by focusing a firm’s resources on top-tier customers, those customers who are giving in more profits.

So if more resources are dedicated to those customers who are giving more profits, then it will create loyal customers. Furthermore, different customer tiers often have quite different service expectations and needs. Therefore, it is critical for service firms to understand the need of the customers and within different profitability tiers and adjust their service levels accordingly. So, first is that they understand what are the needs of the customers and how profitable they are. And then accordingly, they should adjust their service levels.

Now, service tiers can be developed around the level of profit contribution of different group of customers and their needs. So, service tiers can be developed around, first is the level of profit contribution or different groups of customers and their needs, which includes sensitivity to variables such as price, comfort, and speed. And then to identify personal profiles such as the demographics.

So, first we will understand, first what the company needs to do is, to find out the levels of profit contribution of different customers, and how their needs are different, depending upon the sensitivities to variables such as the price, comfort, and speed. And then, so, that is the first thing, and then you would identify and develop their profiles. For example demographics or geographics and so on so forth. So, Zeithaml and Rust, Lemon illustrate this principle through a four-level pyramid. That, we will see, this is the four level pyramid.

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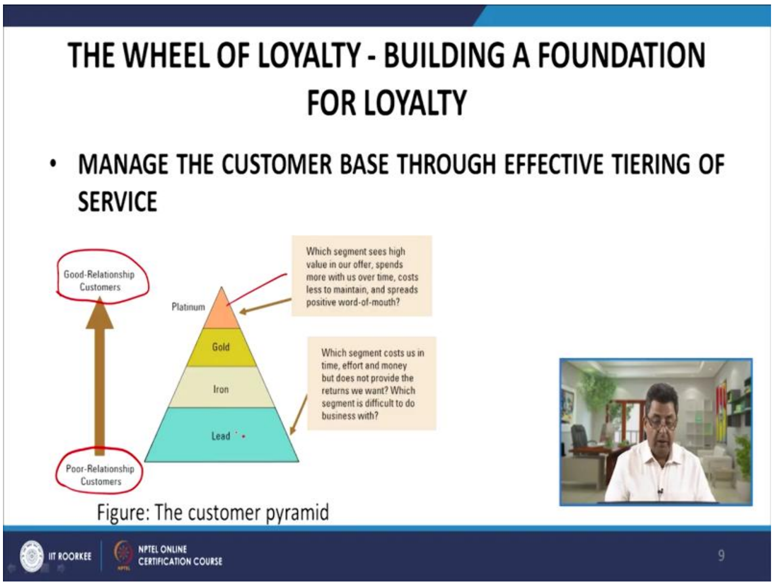

And we are still talking about managing customer base through effective tiering of service. So, now you see that this pyramid, this is a customer pyramid. It has four levels at the top and which is the smallest one is platinum, followed by gold, iron and lead. So, let us look at, so these are, at the base of this pyramid are poor relationship customers and at the top are good relationship customers. So, this platinum, which segment sees high value in our offer, spends more with us over time, costs less to maintain, and spreads positive word-of-mouth.

So, obviously they come in the first and the best tier that is the platinum tier. And at the bottom that is the lead customers, which segments cost us time, effort and money but does not provide the return we want, which segment is difficult to do business with, so that is at the bottom of this pyramid. So, obviously what companies want is that this should be platinum; this lower level lead should turn platinum. So that the companies can have huge number of platinum customers. But it does not so happen.

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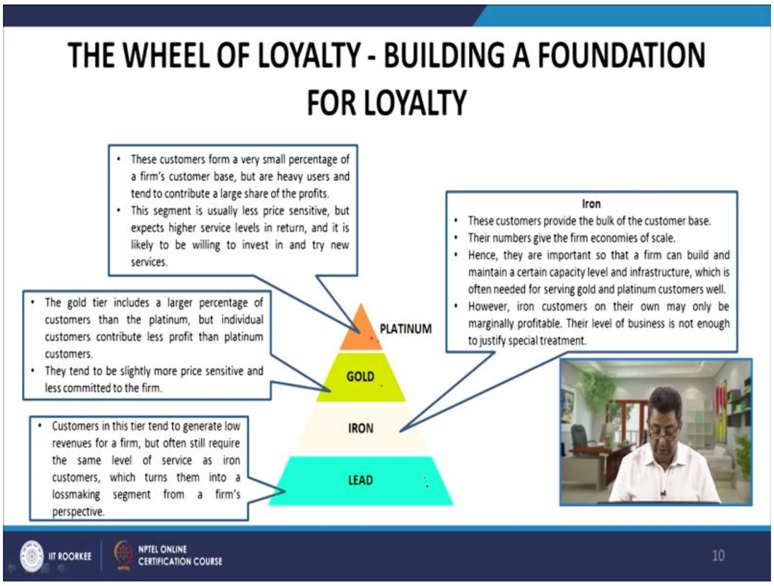

Now, also keep in mind that platinum customers, they may come from the lowest level, the lead customers. So, now again look at this platinum. These customers form a very small percentage of a firm's customer base, but are heavy users and tend to contribute a large share of profits. So, although they are (lower) smallest in number, or the least in numbers but they contribute most to the profits. This segment is usually less price sensitive, but expects higher service level in return, and it is likely to be willing to invest in and try new services.

So, this is what the companies want, this type of customers, the platinum type. Now, let us look at what are the gold types of customers. This gold tier includes a larger percentage of customers than the platinum. So, the number of customers here are more as compared to in platinum. But individual customers contribute less profit than platinum customers. They tend to be slightly more price sensitive and less committed to the firm.

So, the number of customers in gold are more as compared to platinum but their profitability per head is less. They are also more price sensitive and they are also less committed to the firm as compared to the platinum. This iron customers, these customers provide the bulk of the customer base. Their number gives the firm economies of scale. Hence, they are important so that a firm can build and maintain a certain capacity level and infrastructure, which is often needed for serving gold and platinum customers well.

However, iron customers on their own, may only be marginally profitable. Their level of business is not enough to justify special treatment given to them. Let us look at these lead customers, customers in this tier tend to generate low revenues for a firm, but often still require the same level of service as iron customers, which turns them into a loss making segment from a firm's perspective.

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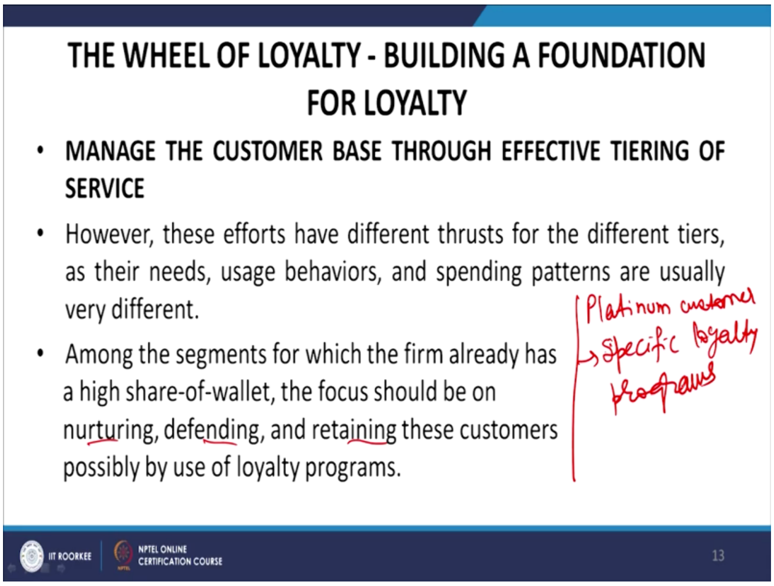

Now, the precise characteristics of customer tiers vary from one type of business to another and even from one firm to another firm. Customers' tiers are typically based on profitably and their service needs. So, rather than providing the same level of service to all customers, each segment receive a service level that is customized based on its requirement and value to the firm.

For example, the platinum tier is provided some exclusive benefits that are not available to the other segments because obviously they have, they contribute more to the profit of the firm. The benefit feature for platinum and gold customers should be designed to encourage them to remain loyal, because these customers are the ones competitors would like to steal the most. So, now you see that it is the battle between all competitors to catch and to retain those platinum customers.

Marketing efforts can be used to encourage an increased volume of purchases, upgrading the type of service used, or cross-selling additional services to any of the four tiers. However, these efforts have different thrust for the different tiers, as their needs, usage behaviours, and spending patterns are usually very different.

Among the segments for which the firm already has a high share-of-wallet, the focus should be on nurturing, defending, and retaining these customers possibly by the use of loyalty programs. So, now for this platinum customers, you know that they are the best and they give lots of profits etcetera, etcetera. So, there is a need to nurture and to defend and retain these customers. How? By way of developing specific loyalty programs. Otherwise if they are not tied in with this loyalty programs, it is easier for the competitors to catch hold of them.

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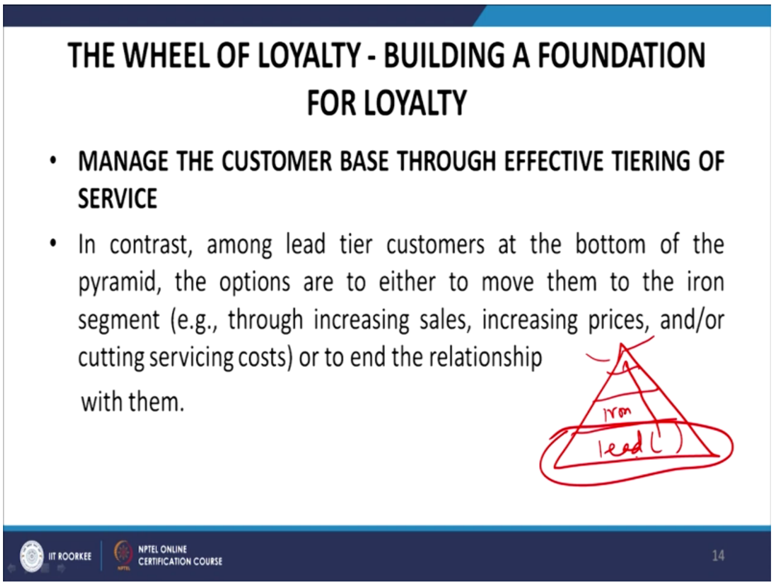

So, in contrast, many lead tier customers at the bottom of the pyramid, the option are to either to move them to the iron segment through increasing sales, increasing prices, and, or cutting servicing cost or to end the relationship with them. So, now keep in mind that when we are talking of this pyramid, obviously this triangle or pyramid will have a huge base and a smaller narrower top.

So, this lead customers they may be unprofitable etcetera, etcetera, but the key is to identify some of these customers who can then move up this ladder. Obviously, people from somewhere else will not come here, they will move from bottom to the top. So, the key for the company's success is to identify which customers have the potential to be taken up, where the company can make more profits and take the customers to the iron or gold or platinum level.

If a customer does not have any kind of that potential, then it is beneficial for the company to end relationship with those customers. But keep in mind that company should not be ending relationships with all customers in this lead segment, because from here these customers will move up the ladder.

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Migration can be achieved through a combination of strategies, so this migration is necessary, migration from the lowest level to the top level. How? By including things like up-selling, cross-selling and setting base fee and price increases. For example, imposing a minimum fee that is waived, when a certain level of revenue is generated, may encourage customers to use several suppliers to consolidate their buying with a single firm instead.

So, now when the customers are told that they will get some more benefits if they buy more. So instead, so the customers instead of buying from several different sellers they will consolidate their buying, they will buy only from one seller so that they are able to achieve that kind of target. Another way to move customers from the lead tier to the iron tier is to encourage them to use low-cost service delivery channels.

So, instead of coming to the branch which is the costlier affair, they can use the internet. For instance, lead tier customers may be charged a fee for face-to-face interactions, but the fee is waived when such customers use electronic channels. For example, in the cellular telephone industry, low-use mobile users can be encouraged to use prepaid packages that do not require the firm to send out bills and collect payment, which also eliminates the risk of bad debts on such accounts.

Divesting or terminating customers come as a logical consequence of the realization that not all existing customer relationships are worth keeping. So, there are, in this lead segment there are some customers who can be moved up, and there are some customers who have to be moved out. So, some relationship may no longer be profitable for the firm because they cost more to maintain than the contribution they generate.

So, the cost of retaining those customers is more than the profits that they generate. So, obviously they become loss making for the company. Why is some customers no longer fit the firm's strategy? Either because that strategy has changed, or because the customer's behaviour and needs have changed. So, some customers in that segment may no longer be be good, because the company's strategy has changed, or because their behaviour and needs have changed.

Therefore, in these two cases the company should end the relationship with these kind of customers. Then, there will be another category that will move from lead to iron. And then there will be some customers, some potential customers, new customers who are first in this lead segment. LEAD. And then obviously they are either moved out or moved up and then new customers come and the cycle continues.

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So, each firm needs to examine its customer portfolio regularly and consider ending unsuccessful relationships. Of course, legal and ethical considerations will determine how to take such an action. So, you just cannot end relationship one fine morning. But, so there can be legal and ethical considerations, but but then these customers should be read flagged that they are no longer profitable and the company has to end relationship with them.

For example, a bank may introduce a minimum monthly fee for accounts with a low balance, but for social responsibility consideration, waive this fee for customers on social security. So, those who are getting, those who are not earning money, getting government subsidies, government funds, for them this kind of minimum fees can be waived off.

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Now, let us look at how customer satisfaction and service quality are prerequisites for loyalty. Customer satisfaction and service quality. So the foundation for building true loyalty lies in customer satisfaction. So loyalty will come from satisfaction. Highly satisfied or even delighted customers are more likely to consolidate their buying with one (seller) one supplier, (provide) spread positive word-of-mouth, and become loyal apostles of the firm.

So, these this highly satisfied or delighted customers, they will obviously buy from one supplier instead of buying from several different suppliers. They will spread the positive word-of-mouth and they become positive apostles of the firm. In contrast, dissatisfaction drives customers away and is a key factor in switching behaviour. So, the dissatisfaction has the opposite effect, the customers may switch.

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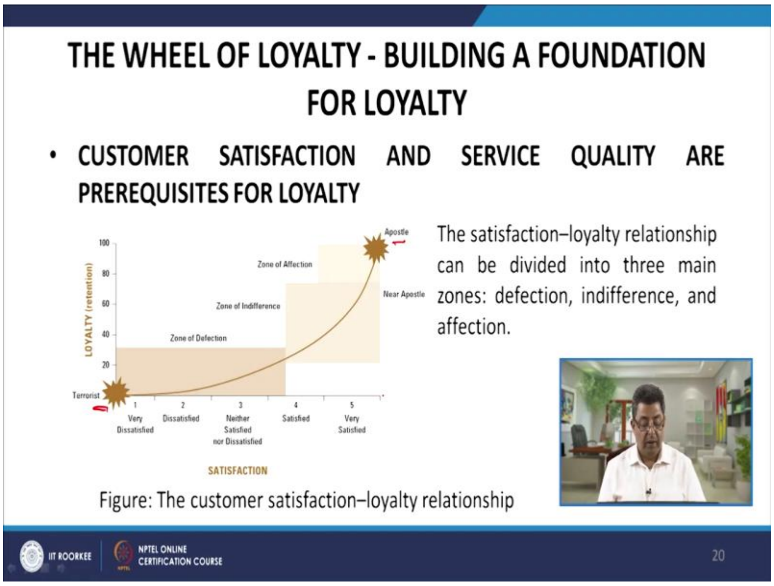

Now, just look at this customer satisfaction and service quality and loyalty relationship. This figure shows, on the x axis you have satisfaction and on the y axis you have loyalty. So, loyalty is also a prerequisite for retaining the customers. So, now you see that this curve moves from left to right. The biggest is this zone of tolerance.

And then comes the zone of indifference and this zone of affection. So, here at the top are apostles and here these are the terrorist. So, it moves from very dissatisfied, dissatisfied, neither satisfied nor dissatisfied and very satisfied and loyalty moves from 0 to 100. So, when the customers are very satisfied and they are 100 percent loyal, then they are termed as apostle.

So, this satisfaction-loyalty relationships can be divided into three main zone, defection, indifference and affection. So, in defection the people will defect in this zone of defection, the people will defect. In this zone of indifference, they are indifferent and in zone of affection, the customers they love the company.

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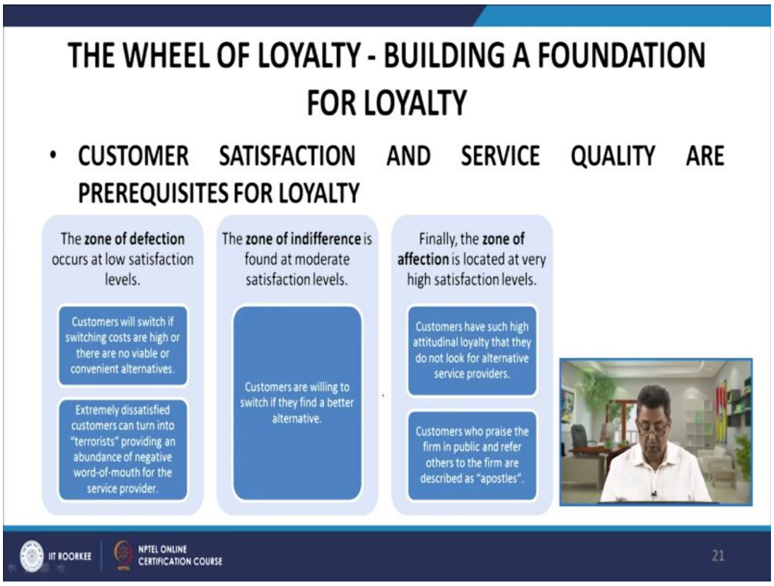

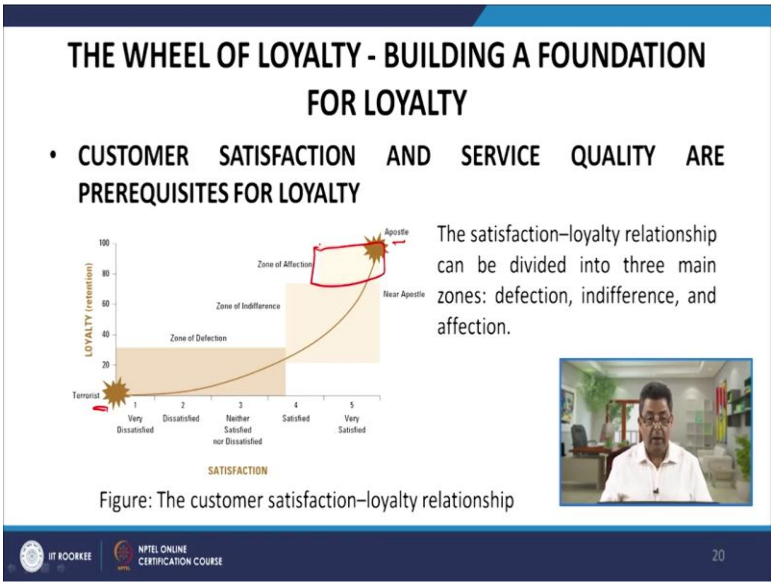

So, this zone of tolerance occurs at low satisfaction levels. So customer will switch, if switching cost are high or there are no viables or convenient alternatives. Extremely dissatisfied customers can turn into terrorist providing an abundance of negative word-of-mouth for the service provider. This then, the second is the zone of indifference. It is found as moderate satisfaction level. So, at this moderate satisfaction level, there comes the zone of indifference. Customers are willing to switch if they find a better alternatives.

And finally, the zone of affection is located at very high satisfaction levels. Customers have such high attitudinal loyalty that they do not look for alternative service providers and customers who praise the firm in public and refers others to the firm are described as apostle. So, this is the area where the customers do not shift and they spread positive word-of-mouth. So this is what every company, every service company wants to achieve. But you see that this is the smallest area.

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True loyalty is often defined as combining both behavioural and attitudinal loyalty. We are talking of both this behavioural and attitudinal loyalty. So, both of them combined makes a person truly loyal. It is also referred to as share-of-wallet and the share-of-heart. So, behavioural is share-of-wallet and attitudinal is share-of-heart.

Behavioural loyalty, behaviour such as buying again, a high share-of-wallet, providing positive word-of-mouth. And attitudinal loyalty is a true liking and emotional attachment of the firm, service and brand.

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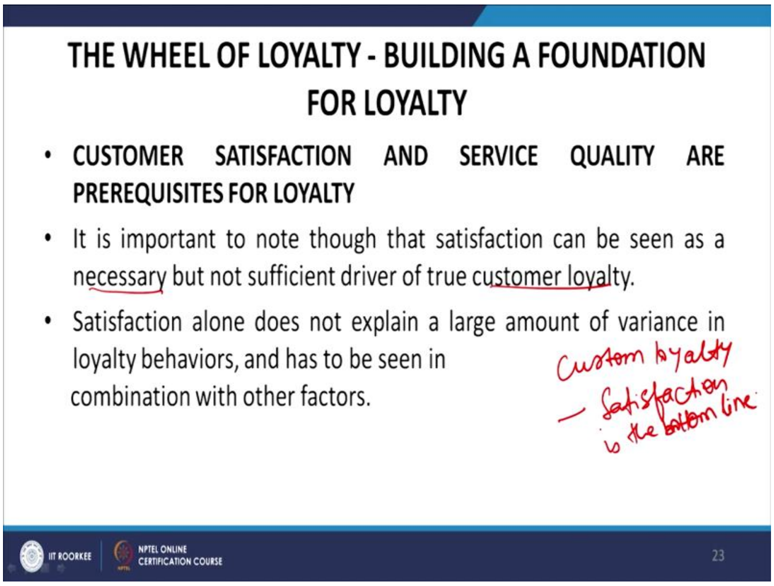

It is important to note though that satisfaction can be seen as a necessary but not sufficient driver of true customer loyalty. It is necessary but not sufficient condition. So this customer loyalty, this satisfaction is necessary condition, but it is not all. So, satisfied, some of the satisfied customers may become loyal, while some may not.

Satisfaction alone does not explain a large amount of variance in loyalty behaviour, and has to be seen in combination with other factors. So, what are these factors? The factors that are to be considered along with satisfaction include, first switching costs and customer knowledge. Knowledgeable customers feel more confident in switching and have lower risk perceptions.

So, in addition to satisfaction, this is the first thing that is needed. The second thing is, how the firm compares to competitors. For example, if a firm is seen as offering the best value proposition compared to that of the next best alternative provider, switching makes little sense and customers keep buying. And the third is the loyalty bonds. So, in addition to satisfaction, presence of these three things are necessary for customer loyalty.

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So, firms can bond more closely with their customers using a variety of strategies, including first, deepening the relationship through cross-selling and bundling. Second is creating loyalty rewards and the third is building high-level bonds such as social, customization, and structural bonds. So, now the firm has to bond with the customers, and how?

So there are number of strategies to bond with the customer. So, the first is to deepen this relationship by cross-selling and bundling, so that the customers they are buying more and more from this company. Second is, because they are buying more and more from the company, then you start creating giving them loyalty rewards, for example loyalty points that we have.

And the third is to build higher-level bonds such as social, customization and structural bond with the customers. So, that will lead to loyal customers. But all these things, all these three strategies without a satisfied customer will not give you anything. So, the satisfied customer is a prerequisite for converting them, for making him a loyal customer.

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Now, how to deepen the relationship? To build closer ties with its customers, firm can deepen the relationships through bundling and or sometimes cross-selling of services. For example, banks like to sell as many financial products to an account or household as possible. So, you have a bank account and then the bank want to sell a number of financial products to you.

So, once a family has a saving, or credit card, or a current account, a safe deposit, a car loan, a mortgage and so on with the same bank, the relationship is so deep that switching becomes a major exercise and is unlikely, unless customers are extremely dissatisfied with the bank. So, now once the customer has so much exposure to, that it has the credit card and debit card, and car loans and lockers etcetera, so, now it becomes very difficult for the customers to shift all these things to some other bank.

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In addition to raising switching costs, there is often value for the customers when buying all particular services from a single provider. One-stop shopping typically is more convenient than buying individual services from different provider. If you have all these things from different banks, so now you see how difficult it will be for you to manage all these things, because for one thing you go to one bank, for another thing you go to another bank and so on so forth. So, it is beneficial for the customer also to have all these things at one place.

So, obviously one-stop shopping typically is more convenient than buying individual services from different providers. When having many services with the same firm, the customer may achieve a higher service tier and receive better services, and sometimes service bundles do come with price discounts. So, when you have so many things from the same bank, so the bank will give you some price discounts also.

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Another thing is to encourage loyalty through financial and non-financial rewards. Few customers buy only from one supplier. This is especially true in situations where service delivery involves separate transactions, such as a car rental instead of being continuous in nature, as with insurance coverage.

So, when we are buying insurance, we continue to buy from the same company. But, when you are taking a car on rent, so that can be from different companies. In many instances, consumers are loyal to several brands sometimes described as polygamous loyalty but avoid others. So, they are not buying from everyone, but they are definitely buying from more than one brand.

In such instances, the marketing goal is to strengthen the customer preference for one brand over others, and to gain a greater share of the customer spending in that service category. So, now in that case when a customer is loyal to more than one brand, then the marketing goal is to make him loyal to one brand and then make him to spend more and more with that one particular brand.

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Once acquired, it tends to be reward-based bonds often offered through a loyalty program, that entice customers to spend more money and increase a firm's share-of-wallet. Incentives that offer rewards based on the frequency of purchase, value of purchase, or a combination of both, represent a basic level of customer bonding.

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THE WHEEL OF LOYALTY - STRATEGIES FOR DEVELOPING LOYALTY BONDS WITH CUSTOMERS

- **ENCOURAGE LOYALTY THROUGH FINANCIAL REWARDS**
- It is important for firms to be selective in choosing loyalty program partners.
- Even well-designed reward programs by themselves are not enough to keep a firm's most desirable customers.
  - Sometimes, what the customer wants is just for the firm to deliver the basic service well, meet their needs, and solve their problems quickly and easily, and they will be loyal.

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- **ENCOURAGE LOYALTY THROUGH FINANCIAL REWARDS**
- Finally, customers can even get frustrated especially with financial rewards–based programs, so rather than creating loyalty and goodwill, they breed dissatisfaction.

This can happen when

1 Customers feel they are excluded from a reward program because of low balances or volume of business

2 If the rewards are seen as having little or no value

3 If they cannot redeem their loyalty points because of black-out dates during high demand periods

4 If redemption processes are too troublesome and time-consuming

THE WHEEL OF LOYALTY - STRATEGIES FOR DEVELOPING LOYALTY BONDS WITH CUSTOMERS

- **ENCOURAGE LOYALTY THROUGH FINANCIAL REWARDS**
- Also, some customers already have so many loyalty cards in their wallet that they are simply not interested in adding to that pile, especially if customers see them as only of marginable value.

How to encourage loyalty through financial as well as non-financial rewards. So, these rewards can be financial and non-financial in nature. Financial rewards are customer incentives that have a financial value also called hard benefits. And, these includes discounts on purchases, loyalty program rewards such as frequent flier miles and the cash-back programs provided by some credit card issuers.

Let us look at how to encourage loyalty through financial rewards. It is important for firms to be selective in choosing loyalty program partners. Even well-designed loyalty programs by themselves are not enough to keep a firm's most desirable customers. Sometimes, what the customer want is just for the firm to deliver the basic service well, meet their needs, and solve their problems quickly and easily, and they will remain loyal.

So, this is what the basic thing that the customer want, to remain loyal. Finally, customers can even get frustrated especially with financial rewards-based programs, so rather than creating loyalty and goodwill, they breed dissatisfaction. So, this can happen when customers feel they are excluded from a reward program because of low balances or volume of business, or if the rewards are seen as having little or no value.

The third, if they cannot redeem their loyalty points because of black-out dates during high demand periods. And obviously, then the fourth one, if redemption processes are too troublesome and time-consuming. Also, some customers already have so many loyalty cards in their wallet that they are simply not interested in adding to that pile, especially if customers see them as only of marginable value. So, the customer already has so many loyalty cards, so adding just one more card, the customer may not be interested in doing that.

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So, then how to go about encouraging loyalty through non-financial rewards, also called as soft benefits? Provide benefits that cannot be translated directly into monetary terms. For example, include giving priority to loyalty program members on reservation waitlists and virtual queues in call centers. Some airlines provide benefits such as higher baggage allowances, priority upgrading, access to airport lounges, and the like, to its frequent flyers even when they are only flying in economy class.

These non-financial rewards especially if linked to higher-tier service levels, are typically more powerful than financial ones, as the former can create tremendous value for the customers. In many cases, this non-financial rewards are much more beneficial for the customers as compared to the financial rewards. So, unlike the financial rewards, non-financial rewards directly relate to the firm's core service and improve the customer experience and value perception.

In the hotel context for example, redeeming loyalty points for free gift does nothing to enhance the customer experience. However, getting high priority for reservation, early check-ins, late check-outs, upgrades, and receiving special attention and appreciation will. So make your stay more pleasant, leave you with the fuzzy warm feeling that this firms appreciate your business, and make you want to come back again and again.

Small businesses often do not run formal loyalty programs but can still employ effective bonds with the customers. For example, they can use informal loyalty rewards that may take the form of one, periodically giving regular customer a small treat as a way of thanking them. The second is reserving their favourite table in the restaurant context. And the third is paying them special attention, and the like.

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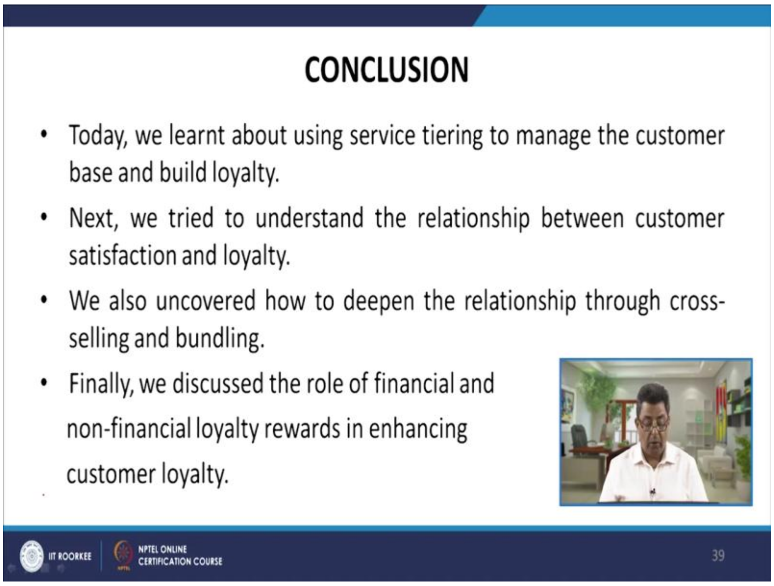

So, to conclude this module, today we have learnt about using service tiering to manage the customer base and build loyalty. Then, we have tried to understand the relationship between customer satisfaction and customer loyalty. We have also uncovered how to deepen the relationship through cross-selling and bundling and up-selling. Finally, we have discussed the role of financial and non-financial loyalty rewards in enhancing the customer loyalty.

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And these are the three books from which the material for this module was used. Thank you.