

When Customer Loyalty Is a Bad Thing

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The economic crisis has jolted companies into the need to redouble efforts to foster customer loyalty. Numerous articles now tout the increased importance of giving customers premium service [in troubled times](#) to [ensure customer retention](#). The underlying reasoning is simple — loyal customers help a company to weather the storm through their continued patronage.

Without question, there is some truth to this logic. No firm can survive for long without loyal customers. The problem, however, is that success through loyalty isn't nearly so simple. Like most "big" ideas, there are conditions where it is unarguably correct and less popular but equally true conditions where it is wrong.

Loyalty is a big idea. At its most basic level, it is a feeling of attachment that causes someone to be willing to continue a relationship. And while exclusive loyalty has been replaced in customers' hearts and minds with multiple loyalties for many if not most product categories, often greater than 50% of a company's customers would classify themselves as holding some level of loyalty to a particular company. Even if we narrow our classification of loyalty to customers who feel loyal and give the majority of their purchases in a category to the firm, typically we find this to represent one-third of a firm's customers.

The fly in the ointment is that typically only 20% of a firm's customers are actually profitable. And many — often most — of a company's profitable customers are not loyal.

This presents managers with a loyalty problem, although not one that they expect. If typically most loyal customers in a firm aren't profitable, how exactly does a customer loyalty strategy *ever* generate a positive return on investment? Instead asking whether you have enough loyal customers in your customer base, you need to ask yourself three more complex questions: 1) which loyal customers are good for the business, 2) how do we hang onto them, and 3) how do we get more customers like them.

In this down economy, customers in both B-to-B and B-to-C settings are naturally much more sensitive to economic issues. Furthermore, companies in B-to-B relationships are often more reliant on their vendor partners to help them shoulder this burden. There is nothing inherently wrong with this, and we as managers need to recognize that our job is to meet our customers' needs if we are to deserve their loyalty.

But the simple solution to improving customer loyalty in a down market is to offer price deals. In fact, firms that track their customer loyalty can be guaranteed that loyalty scores will increase with each substantial decrease in price all things being equal.

But [that's a bad loyalty strategy](#). No, this doesn't mean we should not find ways to be more efficient so that we can pass cost savings on to our customers. But price-driven loyalty is always the lowest form of loyalty. It means that we aren't offering differentiated value to our customers.

The place to begin any loyalty strategy is to determine which loyal customers are profitable and which are not. A closer examination of these two types of customers always reveals very different reasons for their loyalty. Unprofitable loyal customers tend to be loyal for one of two reasons: 1) they are driven by unprofitable pricing or exchange policies, or 2) they demand an excessive amount of service that they are not willing to pay fairly to receive.

Profitable loyal customers on the other hand are almost always driven by differentiating aspects of our product or service offering. The key to a successful loyalty strategy is to become crystal clear as to what these are, and to focus on tangibly improving these elements. It is also imperative that we actively let customers and prospective customers know that these are the things the company stands for and that the firm is committed to being best at. By doing this, our best customers will have the necessary information to clearly articulate why our organizations deserve their loyalty in good times and in bad.

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http://blogs.harvardbusiness.org/cs/2009/05/when_customer_loyalty_is_a_bad.html