WORTH BEYOND REVENUE: THE FULL VALUE OF A LOYAL CUSTOMER

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ABSTRACT

The influence of loyal customers on a company can reach far beyond their proximate impact. We view this impact as analogous to the ripple caused by a pebble tossed into a still pond. In this paper we introduce the *loyalty ripple effect* and describe it as the influence, both direct and indirect, customers have on a firm by encouraging new customer patronage or by other actions that create value for the organization. That is, in addition to their revenue stream, we suggest loyal customers may engage in several behaviors that add value to the firm. In the paper we describe some of these behaviors, provide illustrative examples, discuss managerial issues, and make suggestions for future research on this topic.

INTRODUCTION

The cultivation of customer loyalty is an important, if not the most important, challenge facing most firms. Indeed, businesses are concerned about not only attracting and satisfying customers, but in developing long-term relationships with them. Such organizations expend considerable effort cultivating these relationships with customers (Reichheld and Sasser 1990). In practice, what these firms are striving for is the development of relationships with *loyal customers*.

Firms have increased their efforts to retain customers for various reasons, but most often the reasons relate to the customer's direct value to the company. Loyal customers can lead to increased revenues for the firm (Reichheld 1993, 1996; Schlesinger and Heskett 1991), provide predictable sales and profit streams (Aaker 1992), and are more likely to purchase additional goods and services (Clark and Payne 1994; Reichheld 1996). Yet, to more accurately assess the *full* value of a loyal customer, we believe firms must look beyond the influence of these direct measures. That is, firms should look beyond direct revenue streams and include the value of *all* the benefits associated with possessing a loyal customer (Zeithaml and Bitner 1996).

SERVICE LOYALTY

Before understanding the full value of a loyal customer to a firm, we explore the concept of service loyalty. *Service loyalty* may be defined as "the degree to which a customer exhibits repeat purchasing behavior from a service provider, possesses a positive attitudinal disposition toward the provider, and considers using only this provider when a need for this service arises" (Gremler and Brown 1996, p. 173). Although loyalty is an important issue for all businesses, it is particularly salient for service firms for three reasons: loyalty is greater or more prevalent among services consumers than among goods consumers (Zeithaml 1981); services provide more opportunities for person-to-person interactions which, in turn, often provide opportunities for loyalty to develop

(Parasuraman, Zeithaml, and Berry 1985; Surprenant and Solomon 1987); and perceived risk is often greater when purchasing services than goods (Murray 1991), providing an atmosphere more likely to lead to customer loyalty since loyalty is often used as a risk reducing device (Zeithaml 1981).

THE FULL VALUE OF A CUSTOMER

Reichheld (1996) has extensively investigated the value of loyal customers to service businesses over the past decade. He has generally focused his research on the *direct* impact of loyal customers on the firm. In particular, the major focus of his and others' studies is on the direct revenue stream resulting from retaining a customer and keeping him/her satisfied (e.g., Reichheld 1993, 1996; Schlesinger and Heskett 1991). Although several have calculated the lifetime value of a customer (e.g., Peters 1987; Sewell and Brown 1990; Zeithaml and Bitner 1996), such calculations generally do *not* extend beyond his/her own consumption behavior. Thus, indirect contributors to the customer's value, such as influencing other new customers to buy from the firm, are usually not included in the calculations. That is, a conservative approach is usually taken when assessing the *full* value of a loyal customer.

Zeithaml and Bitner (1996) suggest customers can contribute to their own satisfaction by their participation in the service delivery process. We contend the contribution loyal customers make to a service business can go well beyond creating value for themselves and beyond their direct financial impact on the firm's revenues. Some of the ways customers can create value for the firm include positive word-of-mouth communication, voluntary customer citizenship behaviors, co-production assistance, social relationships, and mentoring of other customers (see Figure 1 below). We explore each of these briefly in the following paragraphs.

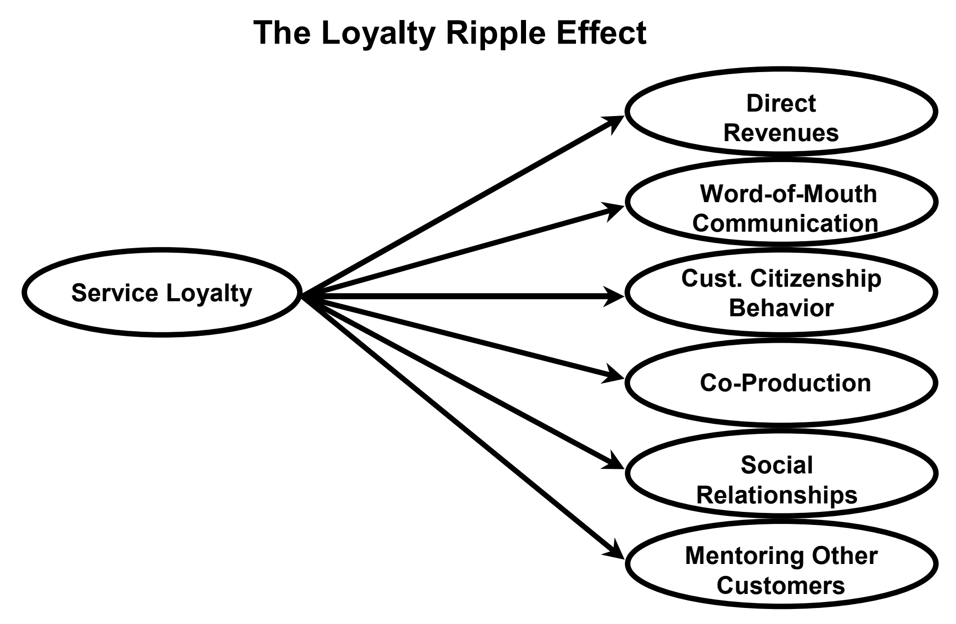

Figure 1

Word-of-mouth Communication. This communication about services is arguably the most significant way that customers can create value for a firm. Loyal customers often *talk a great deal* about a company and may "drum up a lot of business" over the years (Reichheld and Sasser 1990). Customers who provide recommendations have been described in many ways, such as *true customers* (Berry and Parasuraman 1991), *apostles* (Heskett et al. 1994), *champions* (Wilson 1991), and *advocates* (Christopher, Payne, and Ballantyne 1991; Cross and Smith 1995). Perhaps the most illustrative term is used by Peters (1987), who describes loyal customers as *appreciating assets*--and the more they tell others the more valuable they are to the company.

Customer Citizenship Behavior. Loyal customers may engage in positive, voluntary behavior that creates added value to the firm. Such behavior has been labeled *customer citizenship behavior* (Gruen 1995), *customer organizational commitment* (Kelley, Donnelly, and Skinner 1990), *customer voluntary performance* (Bettencourt 1997), and *customer discretionary behavior* (Zabava Ford 1995). Gruen (1995) contends customer citizenship behavior can be exhibited in a variety of forms including altruism, courtesy, sportsmanship, civic virtue, and conscientiousness. As examples of such behavior Gruen includes participation in company sponsored research, display of relationship affiliation (through T-shirts, hats, bumper stickers, etc.), making suggestions for improving processes, and proactive communication of anticipated problems (e.g., making a cancellation even when it is not required). Bettencourt (1997) suggests customers who pick up trash, bus tables, or report burnt out light bulbs and messy changing rooms to an employee are exhibiting behaviors that add value to the firm. As these scholars suggest, such voluntary behaviors help to keep the organization running smoothly (Gruen 1995).

Co-production. Loyal customers may, because of their experience with and knowledge of the provider, contribute to the *co-production* of the service (Bowen 1986; Lengnick-Hall 1996) by assisting in service delivery. Customers who regularly visit a provider often acquire the knowledge, skills, and dispositions that will enable them to perform as effective "partial employees" while in the service creation process (Mills and Morris 1986). Similarly, committed customers tend to be more involved with a service organization and the service delivery process and, as a result, more effective partial employees for the organization (Kelley, Donnelly, and Skinner 1990). As co-producers of the service, customers may even contribute to their own satisfaction by their participation in the service delivery process (Zeithaml and Bitner 1996). Customers who are good at co-producing the service can obviously add value to a service provider.

Social relationships. For some services, loyal customers may provide social benefits to *other customers* in the form of friendships (Goodwin 1994; Goodwin and Gremler 1996; Grove and Fisk 1997), as encouragers for others (Zeithaml and Bitner 1996), in the forming of a special community (Arnould and Price 1993), or in developing a "strong fellowship" with fellow customers (Goodwin 1994). Such relationships, while hard to quantify, can add value to a customer's service experience and thus indirectly add value to the firm. In some instances, loyal customers may also provide social benefits to *employees* (Goodwin, Macintosh, and Mayo 1994; Price, Arnould, and Hausman 1996). For example, Goodwin, Macintosh, and Mayo (1994) found employees frequently formed a "strong social friendship" with their customers. Similarly, in a study of hairdressers, Price, Arnould, and Hausman (1996) found that providers often consider clients to be friends who talk about their children, life, and other issues of importance to them. Although such friendships can not be easily measured, there is little doubt that they are another way that loyal customers can add value to the organization.

Mentoring of Other Customers. Finally, loyal customers may serve as mentors to other less experienced customers (Zeithaml and Bitner 1996). Because of their experience with the provider, loyal customers can help other customers understand the explicitly or implicitly stated rules of conduct (Grove and Fisk 1997). By sharing their expertise with uninformed customers, loyal customers can make the service delivery process easier for all parties involved--employees, customers, and even other customers involved in the service experience. Indeed, when loyal customers mentor others, they take over some of the functions of the service provider (e.g., provide their own entertainment, demonstrate how to use equipment). These customers may be even more effective than paid employees--they are readily available, and the absence of a profit motive can lend credibility to their advice (Adelman, Ahuvia, and Goodwin 1994).

THE LOYALTY RIPPLE EFFECT

As the discussion above illustrates, the influence of loyal customers can reach far beyond their proximate impact on the company. We view this impact as analogous to the ripple caused by a pebble tossed into a still pond--the effect the small stone can have on the surface of the pond goes well beyond the original water displacement--and introduce the *loyalty ripple effect* to illustrate the far reaching influence a loyal customer can have on other customers and on an organization. Unfortunately, in many instances such influence is not easily measured. However, we offer a numerical illustration of the loyalty ripple effect stimulated by word-of-mouth communications.

Consider Samantha--a loyal customer of Mallory's Hair Salon. Samantha is 38, married with two young children, and spends about $75 every three months on haircuts for her family. Thus, on average, Samantha spends about $300/year at Mallory's. Assuming her family will have similar service needs for another 15 years and that they continue to live in their current neighborhood, Samantha's direct contribution to Mallory's as a loyal customer is $4,500 ($300/year × 15 years). Although this figure provides some indication of how valuable Samantha is to the organization, her *full* value to Mallory's is actually much greater. Let us imagine Samantha is pleased with the services provided by Mallory's and recommends the salon to five people over the next 15 years--one recommendation every three years. Even if only two of those five people subsequently visit Mallory's and become loyal customers, the loyalty ripple effect of Samantha's patronage becomes evident. Assuming these two new customers will have needs similar to Samantha's, her value to Mallory's can actually be $13,500 ($4,500 + 2 × $4,500).

Beyond this direct revenue, Samantha and the two new customers may offer indirect value to Mallory's that is not as easily quantified. For example, as they become loyal customers they may be more inclined to engage in small helpful tasks such as picking up a glass bottle left in the parking lot or pointing out a water spout in a rest room that does not shut off completely. They may help co-produce the service by providing detailed descriptions of precisely the hair cut desired and bringing in a picture of that specific hair style. In addition, these customers may contribute to the satisfaction of other customers and Mallory's employees by offering advice and encouragement and by sharing stories of past positive experiences with Mallory's.

MANAGERIAL IMPLICATIONS

Management can benefit from insight on how to facilitate the generation of loyalty ripples. In the following paragraphs we discuss implications for firms in regards to word-of-mouth communication; probably the most salient ripple generated by their loyal customers.

The power of the loyalty ripple effect. Firms can benefit in at least four ways from having customers provide recommendations to others. First, as argued throughout the paper, the customer base may be increased as a result of new customers generated by positive recommendations. Second, the firm not only gains new customers from such recommendations, it gains new customers who are more likely to become *loyal* customers. Indeed, Reichheld (1993) contends receivers of a personal recommendation are more likely to become loyal customers than those who buy because of an advertisement and others have argued that such receivers are favorably "predisposed" to the provider before purchase (Arndt 1968; Gremler 1994). Third, customers recommending a provider subsequently become more loyal to the organization (Gremler and Brown 1994) which, in turn, can lead to increased customer retention and thus increased revenues. And fourth, firms who have customers generating ripples may be able to decrease advertising and promotion costs (Rust, Zahorik, and Keiningham 1995). For these reasons, we believe service managers should place a high priority on encouraging recommendations by its customers.

Ripple generators...an extended sales force. Marketing managers of service organizations might consider loyal customers as a kind of extended or part-time sales force. One way to develop this extended sales force is to increase the expertise of loyal customers. Since loyal customers tend to have much experience with the service offering they may naturally, over time, develop knowledge about the service provider. However, anything the organization can do to proactively increase customers' knowledge of and confidence in the service provider will better equip them to "work" as an extended sales force. For example, providers should willingly supply interested customers with information about the service, thereby making them better informed and potentially more likely to give word-of-mouth recommendations (Murray 1991). "Bring-a-friend" programs encouraging customers to bring guests "gratis" to the service provider may help motivate them to tell others. Service managers might consider "tangiblizing" the service offering by providing visible or explanatory cues in order to give customers something to talk about or assist them in initiating discussions about the service provider (Murray 1991). That is, managers might provide customers with brochures they can hand out to help introduce the service provider to potential new customers and help to explain the service offering. In effect, each of these examples suggest ways loyal customers can be better prepared for potential opportunities to "spread the gospel" (Dichter 1966) about the service provider.

To encourage ripple-like behavior from its loyal customers, firms might consider establishing some type of customer membership. Bettencourt (1997) argues that when customers see themselves as *members* of a firm, they are more likely to act as partners in service delivery. Bhattacharya, Rao, and Glynn (1995) suggest managers build an *identification bond* with customers in order to get them to engage in pro-firm types of behaviors. Thus, the more an organization can formally get customers to commit to and identify with the firm, the more likely these customers are to engage in behaviors that create value for the organization.

Rewarding ripple generators. Marketing managers might consider rewarding a loyal customer who repeatedly recommends the organization to others by (1) giving personal recognition to the customer (e.g., a restaurant owner coming over and greeting the customer by name in front of his/her dinner party), (2) providing price discounts not available to other customers, (3) dispensing other types of rewards, such as service upgrades, express check-ins, or extended/additional services (e.g., if you get someone else to sign up for our frequent flier program, we'll credit your account for 1000 miles), or (4) directly compensating (i.e., paying) those customers whose recommendations result in new customers for firm. Although some of these suggestions may push an organization beyond its comfort zone, many businesses fail to even acknowledge their gratitude for such recommendations. At a minimum, a thank-you should be provided to every customer whose recommendation leads to a new customer. Flowers, candy, or even discounts on future service can also be provided as a way to say thanks to those loyal patrons who have acted as an advocate on the firm's behalf. One chiropractic clinic actually posts in its lobby the names of those who have referred others to the clinic, thus giving public recognition to these customers. Expressing gratitude for recommendations further encourages such behavior and reaffirms the customer's commitment to the organization.

The power of rapport. Some customers may not find the suggestions just made to be a motivating force to refer others to the firm. However, customers may be motivated to be contributors to the firm when they have developed interpersonal relationships with its employees. Indeed, for many services, an important component of the service offering is the interpersonal interaction between employees and customers (Czepiel and Gilmore 1987; Surprenant and Solomon 1987). Gremler and Brown (1996) refer to relationships between customers and employees as *interpersonal bonds* and argue that the degree to which the customer perceives such a bond exists depends upon the extent to which the customer feels that a rapport has been established in the relationship. Reingen and Kernan (1986) suggest customers who are members of a service marketer's social network are more likely to make referrals. In situations where rapport has developed between the customer and the service provider, a desire to help out a "friend"” by giving referrals may be more of a motivating force than a "reward." In contexts where rapport building leads to referrals, management should train and reward employees for positive interpersonal behaviors with customers (Bettencourt and Brown 1997).

Encouraging employees to generate ripples. Through interpersonal bonding with customers, employees can help build ripples. Such behavior, however, needs to be an integral expectation of the firm's culture and stimulated through employee recruitment and training (Bettencourt and Brown 1997). Southwest Airlines, for example, carefully addresses rapport building and interpersonal skills of prospective employees before hiring them. Once hired, this behavior is encouraged and reinforced through training and performance evaluations. Similarly, the overt asking for referrals by employees is a skill that can also be enhanced through training. As employees become more experienced and believe in the firm's offerings, they can be shown how to comfortably ask for referrals from customer. This overt asking can, of course, be further encouraged when the employee and customer are rewarded for generating successful referrals.

The service context may make a difference. The magnitude of the ripple generated from tossing a stone into a pond may depend, in part, on the characteristics of the pond itself. Similarly, the magnitude of the ripple created by a loyal customer may be influenced, in part, by the context. Consider word-of-mouth communication. In some contexts, the word-of-mouth ripple has little effect--almost like dropping a small stone in the ocean. For example, several types of services, such as long distance telephone services, fast-food restaurants, and plumbing services, may not be affected much by the ripple effect. In other contexts, however, the ripple has large effect--like tossing a very large stone in a still pond. In particular, some services--such as financial planners, insurance agencies, and fine dining restaurants--depend heavily upon such ripples for their livelihood. In fact, many professional services--particularly legal, accounting, medical, and architectural services--have traditionally done very little promotional activity and depend almost exclusively upon new clients being generated through the loyalty ripple effect. The key point here is that the impact of personal recommendations may be more influential in certain contexts.

FUTURE RESEARCH

Although the loyalty ripple effect may be hard to quantify, we believe its potential importance makes it worthy of future research. We conclude the paper by posing several research questions to encourage further investigation of the loyalty ripple effect.

What other types of ripple effects can be generated by loyal customers? Much of the discussion has been on the ripple effect generated by word-of-mouth recommendations. However, as we argued earlier, there are several other ways that a loyal customer can add value to the organization. For example, Bettencourt (1997) contends that, in addition to being a promoter of the firm, a customer can contribute value to the firm as both a human resource and an organizational consultant. Because of their experience with a particular provider, loyal customers may help co-produce the service (Bowen 1986) by assisting in service delivery. And, these customers are "uniquely qualified" to serve as consultants to service providers (Lengnick-Hall 1996) because of the intimate knowledge they have of the service delivery process. For some services, loyal customers may serve as mentors and encouragers to other customers (Zeithaml and Bitner 1996), as well as provide social benefits to both customers (Goodwin and Gremler 1996) and employees (Price, Arnould, and Hausman 1996). This list of customer behaviors we have identified that add value to the firm is certainly not exhaustive, and other types of loyalty ripples should be identified and researched.

How should ripple effects be measured? As the ways in which a customer can contribute to the overall value of a firm are identified, the next logical question becomes one of measurement. That is, what is the best way to measure such effects? For example, in terms of word-of-mouth communication, Rust, Zahorik, and Keiningham (1995) report that, at an aggregate level, some data are available to indirectly measure the impact of word-of-mouth communication. Much more work is needed, however, to measure the loyalty ripple effect at the individual consumer level--not only for word-of-mouth communication, but for other types of ripples.

What is the full value of a loyal customer? We have pointed out several ways that customers can add value to an organization. However, identifying the ways customer can add value is relatively easy in comparison to quantifying what they actually mean to the organization. For example, how can you quantify the value of a customer who picks up a glass bottle laying in a parking lot and throws it in the trash? Or, what is the encouragement that one physical therapy patient provides to another that is trying to overcome knee surgery actually worth? Assuming that future research is able to identify and measure ripple effects, the primary question managers are sure to ask is--so what?

What is a loyal customer really worth? And, similarly, what impact does the loyalty ripple effect have on the bottom line?

Is there a ripple effect coefficient? Reichheld (1996) contends that a *loyalty coefficient* exists, meaning that some customers are much more prone to be loyal than others. We believe a similar situation may exist in regards to the loyalty ripple--that is a *ripple effect coefficient*. This can be illustrated by thinking about word-of-mouth communication. Some customers prefer not to talk about service providers. Some have a more powerful influence because of their social status, stage of their life, or the number of social organizations to which they belong. Some have a much larger social network of contacts, friends, and associates. The idea of a ripple effect coefficient raises some additional questions needing to be researched.

Under what conditions are ripples stimulated? An assumption made throughout the paper is that loyal customers will indeed be ripple generators. However, this may not always be the case. For example, it would be useful to identify under what conditions loyal customers actually provide word-of-mouth recommendations about a service provider. In particular, why don't all loyal customers provide recommendations? Why do some customers who are very satisfied with and repeatedly use a provider fail to make *any* recommendations? In what situations is customer citizenship behavior more likely to occur? Under what conditions might customers serve as mentors to others? A better understanding of the conditions that help to facilitate the loyalty ripple effect can provide marketing managers with insight as to how to best stimulate such behavior.

SUMMARY

Loyal customers are more than just purchasers. They can also act like a large stone tossed into a small, still pond and generate ripples benefitting the firm, its employees, and other customers. This paper examines the loyalty ripple effect as a means of recognizing that the full value of a loyal customer includes repeat purchases, referring new customers to the firm, co-producing the service, offering social support or benefits to other customers and employees, and mentoring other inexperienced customers. Firms understanding and encouraging the ripple effect are more likely to realize--and benefit from--the full value of customer loyalty.

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QUIS 6

Pursuing Service Excellence: Practices and Insights

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