theloyaltreatment 32

Base Your Customer Loyalty Performance Measures on Cause-and-Effect

Performance measurement models provide clear lines of sight, from employee actions to customer loyalty.

synovate Loyalty

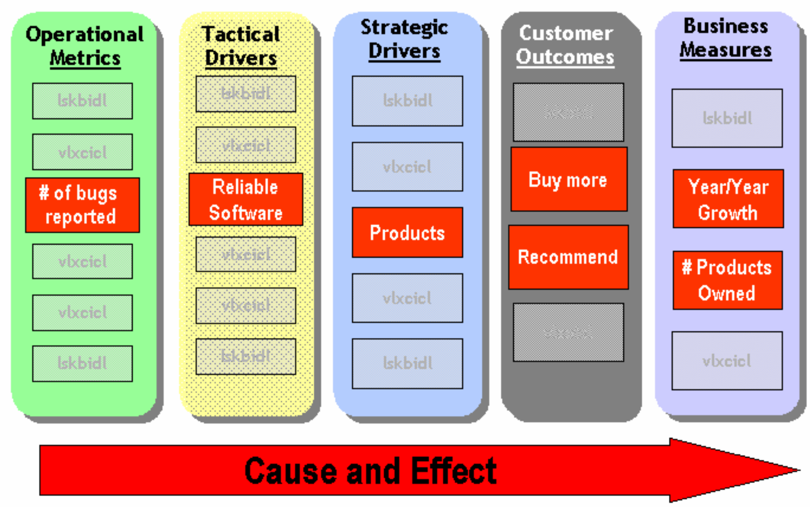
by Dr. Lawrence A. Crosby and Sheree L. Johnson

The business requirement to meet the needs and expectations of customers and other stakeholders is the primary impetus behind strategy. Financial results are the ultimate measures of strategic effectiveness, but not the drivers of business success. Consequently, there is a need to link day-to-day, relationship-affecting activities to financial results. Defining what drives a company's overall business success—from the activity and process level to increased customer loyalty and financial/ marketplace success—should be one of management's highest priorities.

Top management can be held accountable for developing a customer loyalty strategy that positively influences sales volume, market share, cash flow, profit, return on investment, dividends, and market value. For operating management, however, there's often a big disconnect from that strategy. This is because of the lack of alignment and proper measurement of the business processes/activities that drive customer loyalty, and ultimately financial results.

Corporate level measures are very important, but they aren't going to have much impact unless they are cascaded to frontline employees. The question is simple: Do you want 10% of your employees working toward the company's customer loyalty objectives, or 100%?

Causal relations among performance measures are key features of performance measurement models (PMM),



Shift in Measurement Systems

Before the 1980s, business success was evaluated purely by financial measures. Throughout the 1980s and 1990s, academics and practitioners highlighted the deficiencies of those key performance indicators (KPIs) in organizations. In particular, they recognized the emphasis on short-term results and the lack of long-term strategic focus.

As a result, they developed new measurement systems, which consisted of financial and non-financial measures (e.g., a customer loyalty index) and provided multidimensional perspectives of performance. These comprehensive "performance measurement models" (PMMs) describe links between business decisions and outcomes, and guide strategy development, communication, implementation, and feedback at multiple points along value chains. Because PMMs reflect inputs and both intermediate and final outputs, they generally include measures of operational, strategic, financial, and non-financial performance.

Academics and practitioners alike argue the benefits of using PMMs over mere lists of KPIs.

- Models, which explain the underlying economics of businesses, are essential for tying strategic insights to financial results.
- Operational measures, such as those observed prior to

financial outcomes, have improved "line of sight" to desired financial performance.
- Even simplified but credible models can be powerful communication and learning devices.
- Models can successfully become integral parts of management debate, dialogue, communication, and experimentation.
- Models provide bases for effective motivation and incentives, by showing how actions might affect outcomes.
- The identification and selection of appropriate systems of models enhances the implementation/acceptance of the business strategy, and employee understanding of the company's business.

Cause and Effect

A PMM exceeds the benefits of KPI lists alone—partly by providing reliable predictions of outcomes, which are based on cause-and-effect relations among the performance measures. These "causal relations" are key features of PMMs. Unfortunately, many companies that use PMM frameworks don't apply the rigor of testing such relations. Perhaps they should.

A study conducted a few years ago reported that only 23% of 157 surveyed organizations consistently built and tested causal models—but that this percentage, on average, achieved 2.95% higher return on assets and 5.14% higher return on equity.

Many companies find it difficult to cascade and execute customer loyalty strategies. People aren't accustomed to customer loyalty measures, and don't understand how they can influence them. Using a PMM for customer loyalty is an excellent communications tool; it tells the story of how managers and their organizations can succeed by managing intermediate activities.

A statistical correlation between tactical measures and new strategic measures (e.g., a customer loyalty index) instills great confidence in the latter, and creates a willingness to move ahead with the strategy and usage of those new measures.

The question of whether we can affect customer loyalty is answered by the statistical correlations, showing the linkages between internal operational metrics and strategic customer metrics. We need to show our employees that their actions and behaviors can influence customer loyalty.

Corporate level measures are very important, but they aren't going to have much impact unless they are cascaded to frontline employees.

For example, software programmers might be accustomed to tracking operational metrics such as number of program bugs fixed (see p. 1 Exhibit). They can better understand and experience their roles in a company's customer loyalty strategy if they see those same metrics correlated to tactical customer loyalty drivers (e.g., customers' perceptions of reliable software), strategic drivers (e.g., customers' perceptions of the company's products), customer outcomes (e.g., customers' likelihood to buy more and recommend), and business measures (e.g., year-over-year growth or the number of products customers own).

Causal relations among PMM measures are an important design criterion and feature of a successful customer loyalty strategy. Conversely, a PMM without valid causal relations is ineffective or counterproductive to communication and motivation.

Setting Your Compass

What you measure at the top is what you must measure at all levels; the same is true of customer loyalty. The specific metrics will change with every function and organizational level because managers performing different jobs need different information to make different decisions. As you go down the organizational chart, the focus is on operations or processes. Your customer loyalty strategy should be incorporated into operational measures by giving more weight to the ones that are strategically important, and by using a causal PMM to show a clear line of sight—from daily actions to customer loyalty behaviors and market/financial results. This communicates strategy to all employees, by translating it into operational terms.

Effective performance measurement is the compass. It guides management in a direction that will produce meaningful results at the process level—results that will directly tie to your company's customer loyalty goals. If the PMM doesn't clearly focus on customer loyalty, then it will enforce the wrong actions.

Managers must strive to direct all levels of their organizations to focus on the right priorities, those that build customer loyalty. The most successful companies know PMMs that encourage the right response and behavior require linking the customer loyalty strategy to day-to-day actions: clear linkage to cause-and-effect—up, down, and across the company.

About the Authors

Lawrence A. Crosby, Ph.D., is CEO of Synovate Loyalty. ***Sheree L. Johnson*** is Synovate Loyalty's Global Director of Strategic Marketing.

To learn more, visit
www.synovate.com/loyalty