Lessons in
LOYALTY

In 50 Words Or Less
- Accelerating business growth depends on effectively measuring the three facets of customer loyalty related to retention, advocacy and purchasing behaviors.
- A new measurement approach and rating system can help organizations learn more about their customers and make better business decisions.

There's a **better way** to measure customer loyalty and **boost business growth**

by Bob E. Hayes

BUSINESS GROWTH DEPENDS on improving customer loyalty behavior. Companies with higher customer loyalty usually experience faster business growth than companies with lower customer loyalty, research has shown.

Different business growth models exist, but they all share one common premise: The primary factor responsible for driving business growth and company value is customer loyalty[1-2]—the degree to which customers experience positive feelings for, possess allegiance to and exhibit positive behaviors toward a company.

But just how can you accurately measure how loyal your customers are so you can make smart decisions related to growing your company's business?

A new measurement approach can help organizations identify and assess three customer loyalty components: retention, advocacy and purchasing, or RAPID. In turn, organizations can learn more about their customers and formulate better strategies to accelerate business growth.

While there are many different ways customers can show their loyalty to a company, product or brand, these three behaviors reflect general components of customer loyalty.[3, 4]

1. **Retention:** Customers remain with your company and do not defect to competitors. For example, customer retention or defection rate is an important loyalty metric in the wireless service industry, in which processes—such as the number of transfers and contract terminations—make customer defections straightforward and routine.

2. **Advocacy:** Customers advocate for your company, product or brand. Companies can grow when their customers promote and recommend you to their friends, who, in turn, become customers.
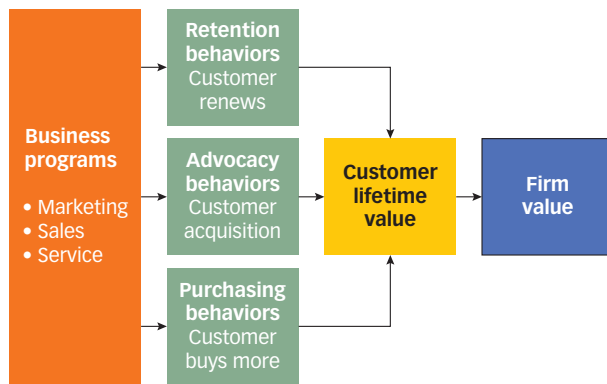
Customer loyalty behaviors affect business growth / FIGURE 1

Based on "Modeling Customer Lifetime Value," by Sunil Gupta, et al., *Journal of Service Research,* Vol. 9, No. 2, 2006, pp. 139-155.

Company profit and customer loyalty behaviors / FIGURE 2

Based on Frederick Reichheld's *The Loyalty Effect,* Harvard Business School Press, 1996.

3. **Purchasing:** Customers increase their purchasing behavior (for example, up-selling, increasing the amount of purchases or cross-selling) because they believe in your company.

Figures 1 and 2 show that customer loyalty can lead to financial growth, which depends on the company's ability to acquire and keep existing customers.

Customer surveys remain a popular way to assess customer loyalty because:
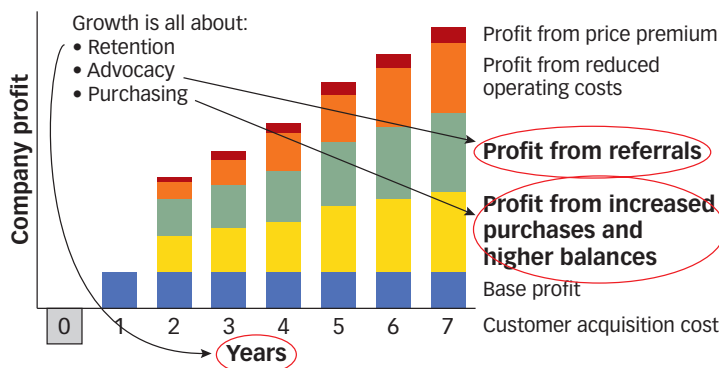
- Surveys allow companies to quickly and easily gauge levels of customer loyalty. Companies may not have easy access to objective customer loyalty data or may not even gather such data.

- Surveys allow companies to assess customer perceptions—such as customer experience—and help prioritize initiatives that will maximize customer loyalty.

- Survey results can be used to change organizational business processes. Surveys commonly include questions about customer loyalty and customer experience (for example, product, service and support). Used jointly, these questions can help identify (through driver analysis or segmentation analysis) reasons why customers are loyal or disloyal.

- Objective customer loyalty measures provide a backward look into customer loyalty levels (for example, defection rates and repurchase rates). Surveys, however, allow companies to examine customer loyalty in real time. Surveys include questions regarding expected levels of loyalty related behavior and provide opportunities for companies to look into the future regarding customer loyalty.

With any survey, the right questions need to be included. Practitioners and survey developers are faced with several options regarding the type of questions to use. For example, Net Promoter Score (NPS)[5, 6] developers claim the "recommend" question ("Do you recommend this product or service?") is the only loyalty question needed because it is the best predictor of business growth.

Other researchers[7-9] contend common loyalty questions related to overall satisfaction and continued purchasing are equally as effective in predicting business growth. In fact, there is evidence these loyalty questions measure the same underlying construct as the recommend question[10] and explains why these common loyalty questions predict business growth equally well.

While there has been improvement in the quality of managing customer loyalty survey data, the quality of the measurement and meaning of customer loyalty has not

kept pace. Specifically, customer feedback professionals have little scientifically driven guidance regarding what loyalty questions they need to use in customer surveys.

Do they employ the NPS approach? Do they use an "overall satisfaction" question? Do they use several loyalty questions? If multiple loyalty questions are used, do they aggregate the responses into a single score or metric?

Measuring customer loyalty via survey questions is not as simple as it might appear. Unlike objective measures of customer loyalty (such as defection rates and number of purchases made), customers' ratings of each loyalty question (typically, their likelihood to engage in particular behaviors) become the measure of customer loyalty. Even though we can calculate separate loyalty scores—one for each loyalty question—the distinction among the loyalty questions may not be warranted.

Because of the way customers interpret survey questions and the inherent error associated with measuring psychological constructs, ratings need to be critically evaluated to ensure you understand their meaning.[11] When using surveys to measure constructs, you must be mindful of how the customers interpret and respond to the questions.

Customer loyalty, when measured through surveys, is commonly assessed using standard questions, including the following 11 behaviors:

1. Likelihood to stop purchasing from the company (a reverse-coded item so higher scores reflect higher levels of customer loyalty).
2. Likelihood to switch to a different provider (a reverse-coded item).
3. Likelihood to stop purchasing (a reverse-coded item).
4. Overall satisfaction.
5. Likelihood to choose again for the first time. In other words, asking customers: "If you were selecting a vendor, a product or service for the first time, how likely would you choose the organization again?"
6. Likelihood to recommend.
7. Likelihood to continue purchasing same products or services.
8. Likelihood to purchase different products or services.
9. Likelihood to increase frequency of purchasing.
10. Likelihood to increase amount of purchases.
11. Likelihood to purchase more expensive offerings.

All but one of the items allow respondents to indicate their likelihood of behaving in different ways toward the company (for example, 0 = not at all likely to 10 = extremely likely). The satisfaction question is rated on a satisfaction scale (for example, 0 = extremely dissatisfied to 10 = extremely satisfied). For all questions, higher ratings reflect higher levels of customer loyalty.

Recently, I conducted a study of consumer perceptions in the wireless service industry using the 11 customer loyalty survey questions. About 1,000 general consumers in the United States ages 18 and older were asked about their wireless service provider. A factor analysis was conducted using the entire set of questions.

Factor analysis is a data-reduction technique that explains the statistical relationships among a given set of variables (the 11 items) using fewer unobserved variables (customer loyalty factors). In simpler terms, a factor analysis can reveal two things:

1. The number of factors (constructs) being measured by the set of questions.
2. Which questions are related to which factors.

For this survey, a factor analysis helped determine whether the original loyalty questions actually measured fewer constructs (factors). It is important to note that an exploratory factor analysis involves some form of judgment when determining the number of factors and which variables are related to the smaller set of factors.[12]

The elements in the factor pattern matrix are called factor loadings. They essentially reflect the correlation between each item and the factors. Higher factor loadings indicate a stronger relationship between the item and the underlying factor. Factor analysis of the 11 items showed these seemingly different loyalty items measured three general components of customer loyalty (see Table 1, p. 28).

The items that loaded on the first factor appear to have a strong emotional component, demonstrating a generally positive attitude toward the company. This positive attitude is defined by the extent to which customers advocate the company and would maintain their relationship. The items that loaded highly on the second factor reflect future purchasing intentions—for example, purchasing different offerings and increasing purchase frequency or amount.

For the third factor, items with high loadings reflect likely customer behaviors around defection. When customers withdraw from a company, they can do it in different ways, from ceasing to purchase to switching to a competitor.

Creating RAPID loyalty indexes

Factor analyses show the apparently disparate loyalty questions really measure three components of loyalty: retention, advocacy and purchasing loyalty. So, how can you derive actual measures of each of the three components of loyalty?

Measuring the three components of customer loyalty involves the process of aggregating the questions that load highly on the same factor. Loyalty indexes for each component are calculated by averaging the loyalty items within each scale. These loyalty indexes are:

- **Retention loyalty index (RLI).** Measures whether customers will remain as customers and is an average of: stop purchasing, switch to another company and purchase from a competitor.
- **Advocacy loyalty index (ALI).** Measures how customers feel positively toward and will advocate for your product, service or brand. It is an average of: satisfaction, choose, recommend and purchase the same.
- **Purchasing loyalty index (PLI).** Measures whether customers will increase their purchases and is an average of: purchase different, increase frequency, increase amount and buy more expensive offerings.

These three customer loyalty components add up to the RAPID loyalty measurement approach. The resulting scores for each index can range from zero (low loyalty) to 10 (high loyalty).

Not all 11 items must be used to create the RAPID loyalty indexes. For example, because the four items (overall satisfaction, choose again, recommend or continue buying) measure the same underlying construct (advocacy loyalty), these four items are essentially interchangeable. Consequently, ALI can be calculated using all four or even two ALI items. Because survey space is limited, companies can use two items to measure advocacy loyalty instead of four. Similarly, PLI can be calculated using all four or fewer PLI items.

Different forms of the RAPID loyalty measurement approach have been used across a few studies, and the measurement quality of the indexes is not greatly affected when fewer items are used. Table 2 contains the results of five studies that used different combinations of loyalty questions. Results show that each of the RAPID loyalty indexes had good measurement properties (low measurement error). Reliability estimates—for example, Cronbach's alpha—are at acceptable levels (0.80 or higher).[13]

Additionally, the average correlation among the RAPID indexes (correlations were ALI/PLI = 0.46, ALI/RLI = 0.41 and PLI/RLI = -0.11) was relatively lower than their reliabilities. This indicates these indexes each measure something unique about customer loyalty and provide different information about the quality of the customer relationship.

Figure 3 (p. 30) shows the means for the three RAPID loyalty indexes across the five studies. The results, consistent across all studies, reveal advocacy loyalty is significantly higher than purchasing loyalty and retention loyalty. It appears customers are more willing to be advocates (ALI) than they are to increase their purchasing (PLI) or even remain as a customer (RLI).

Predicting business growth

Each of the RAPID loyalty indexes has minimal measurement error for each of the indexes. While reliability of measurement is essential, you still must be concerned with the metrics' usefulness.

A good gauge for the quality of a metric includes how well the metric predicts important outcomes. Other researchers have found that loyalty questions, specifically those measuring advocacy loyalty (satisfaction, recommend and purchase same), do predict business growth.[14-17] The next phase of the study examined how well each of the new loyalty indexes predicted business growth.

A nationwide survey of 994 wireless provider customers (study one in Table 2) examined how well the three loyalty indexes predicted important business metrics commonly tracked by wireless providers.[18] Each RAPID loyalty index was correlated with the following business growth metrics:

- Actual churn (attrition) rate.
- Percentage of total of new customer growth.
- Average revenue-per-user growth.

The results showed that different RAPID loyalty indexes predicted different business metrics. Online Figure 1 at www.qualityprogress.com shows the loyalty indexes predicted different business metrics across several U.S.

Factor pattern matrix / TABLE 1

Loyalty survey questions	Factor 1 (advocacy)	Factor 2 (purchasing)	Factor 3 (retention)
Satisfaction	0.85	0.41	0.38
Choose again for first time	0.93	0.43	0.41
Recommend	0.94	0.45	0.38
Purchase same product/service	0.92	0.42	0.44
Purchase different product/service	0.47	0.82	-0.06
Purchase more frequently	0.35	0.89	-0.17
Increase purchase amount	0.49	0.86	-0.05
Purchase more expensive offerings	0.41	0.95	-0.14
Switch to another company*	0.21	-0.31	0.72
Purchase from competitor*	0.41	-0.06	0.88
Stop purchasing	0.47	0.02	0.85

Based on a principal factor analysis with varimax rotation. Bold numbers indicate primary loadings for a given question on a specific factor.

* Items were reverse coded (for example, 10 = 0; 0 = 10) so higher scores indicate higher levels of customer loyalty.

Reliabilities for each RAPID index across studies / TABLE 2

	Loyalty questions	Study 1: wireless providers	Study 2: PC manufacturers	Study 3: wireless providers	Study 4: insurance	Study 5: wireless providers
ALI Items	Satisfaction	×	×	×	×	×
	Choose again for first time	×	×	×	×	×
	Recommend	×	×	×	×	×
	Purchase same product/service	×	×	×	×	×
	Reliability of ALI	**0.95**	**0.94**	**0.96**	**0.88**	**0.92**
PLI Items	Purchase different products/services	×	×	×	×	×
	Purchase more frequently		×	×	×	
	Increase purchase amount	×	×	×		
	Purchase more expensive offerings			×		×
	Reliability of PLI	**0.82**	**0.87**	**0.93**	**0.77**	**0.77**
RLI Items	Switch to another company*	×		×		×
	Purchase from competitor*			×	×	×
	Stop purchasing			×	×	×
	Reliability of RLI	N/A	Not used	0.85	0.53	0.80

X indicates use of the loyalty question in the particular study. Sample sizes for each study: Study 1 (N = 994), Study 2 (N = 1,058), Study 3 (N = 1,077), Study 4 (N = 49) and Study 5 (N = 5,686). Sample and data collection were provided by GMI (www.gmi-mr.com) for Studies 1 and 2, MSI (www.msimsi.com) for Study 3 and Mob4Hire (www. mob4hire.com) for Study 5.

* Reverse coded so lower rates of these behaviors indicates higher levels of retention loyalty.

ALI = advocacy loyalty index
PLI = purchasing loyalty index
RLI = retention loyalty index
RAPID = retention, advocacy and purchasing loyalty indexes

wireless providers, such as Alltel, AT&T, Sprint/Nextel, T-Mobile and Verizon. As expected, churn was best predicted by the RLI, new customer growth was best predicted by the ALI, and average revenue per growth was best predicted by the PLI. Network operators with higher loyalty scores experienced faster business growth than network operators with lower loyalty scores.

Whether it is early in their relationship or later in the life cycle of their relationship with a company, customers can leave or stay, advocate or complain, and purchase more or less. At any time throughout the customer life cycle, companies can influence whether customers engage in these loyalty behaviors.

Figure 4 (p. 30) depicts the three general phases all customers experience in the customer life cycle:

- **The attraction phase**: The company's marketing programs bring in customers by advertising the perceived value of the product or service.
- **The acquisition phase:** The company's sales programs secure customers and set their product or service expectations.
- **The service phase:** The company relies on its processes to deliver exceptional service to ensure customers' expectations are met.

The customer continues through the next iteration of the life cycle with the introduction of new marketing campaigns to maintain and grow the relationship.

The loyalty indexes allow companies to manage customer relationships to increase the three types of customer loyalty. Life-cycle management is the process companies use to manage the customer relationship in each phase of the customer life cycle. Figure 5 (p. 30) shows how companies can target improvements in each of the stages to increase each type of customer loyalty.

Customer experience, personal values

Research has shown that advocacy loyalty is greatly affected by the customer experience—typically in the service phase. But retention and purchasing loyalty is less influenced by the customer experience in the service phase. Improving the customer experience will have a moderate impact on improving retention and purchasing loyalty but a substantial impact on improving advocacy loyalty.

Research also shows that customers' personal values have an impact on behavior and consumption patterns.[19, 20] Certain types of consumers (for example, status-oriented) might be more predisposed to engage in certain activities than other types of consumers. Companies can use their marketing and sales programs to target and acquire specific types of customers—those who will remain with them longer and be more willing to buy more from them.
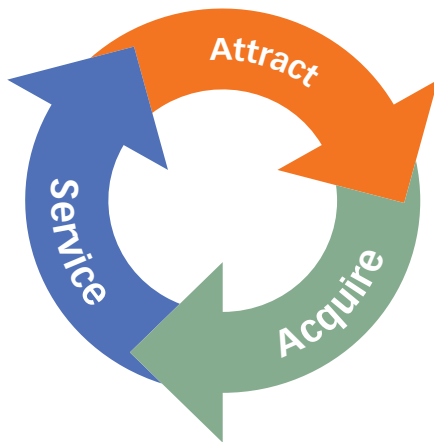
A few applications of the RAPID approach include identifying key drivers for different types of loyalty. Companies conventionally measure only advocacy loyalty by
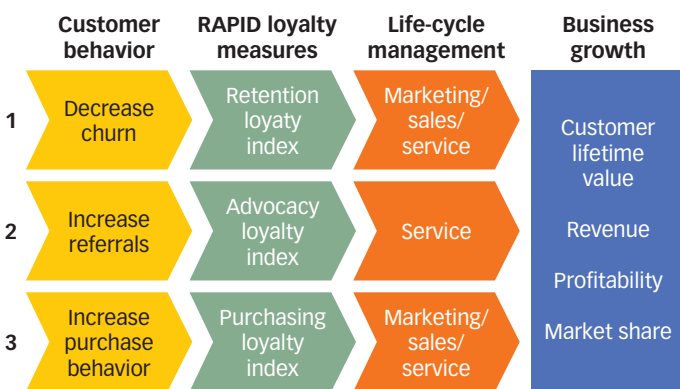
Mean loyalty ratings across five studies / FIGURE 3
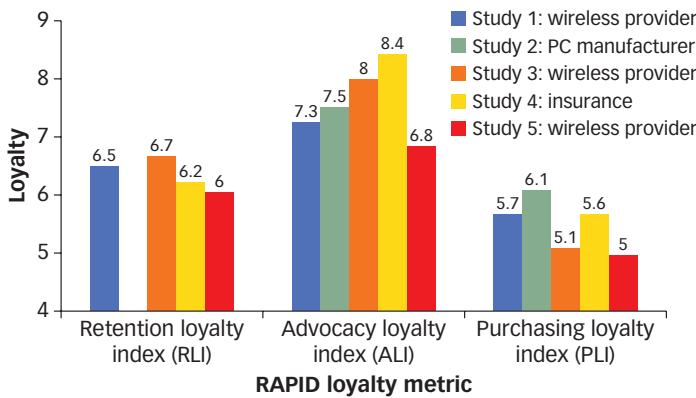
RAPID = retention, advocacy and purchasing loyalty indexes
RLI was not used in Study 2.

Customer life cycle / FIGURE 4

Ways to grow business / FIGURE 5

	Customer behavior	RAPID loyalty measures	Life-cycle management	Business growth
1	Decrease churn	Retention loyalty index	Marketing/ sales/ service	Customer lifetime value
2	Increase referrals	Advocacy loyalty index	Service	Revenue
3	Increase purchase behavior	Purchasing loyalty index	Marketing/ sales/ service	Profitability
				Market share

RAPID = retention, advocacy and purchasing loyalty indexes

using three standard loyalty questions: overall satisfaction, recommend and buy again. While some companies use each question as its own measure of loyalty, others, more appropriately, aggregate (typically averaged) responses across the three questions to derive an overall customer loyalty index.

This measure of advocacy loyalty is useful for growing business through new customers, but companies may be missing opportunities to grow their business through existing customers by increasing customer retention and purchasing behavior.

In a survey of PC customers, key loyalty drivers were different across different RAPID indexes.[21] Satisfaction with technical support was not a key driver of advocacy loyalty but was for purchasing loyalty. Advocacy loyalty appeared to be driven primarily by the product-related features—for example, product reliability. But purchasing loyalty appeared to be driven equally by product-related features and technical support. Decisions on growing the business were enhanced by understanding potential growth opportunities through new and existing customers.

Selecting loyalty questions for a customer survey should be driven by the company's specific needs. A business growth strategy focused on up-selling and cross-selling versus a strategy focused on new customer growth may require different loyalty questions. The former growth strategy requires the company to understand drivers of purchasing loyalty, while the latter requires the company to understand drivers of advocacy loyalty.

A company experiencing a great deal of customer churn can include retention loyalty questions in its customer survey to identify why customers are defecting. By specifically measuring retention loyalty, the company can identify the drivers of customer retention, consequently tailoring specific programs in their marketing, sales and service phases.

Customer segmentation helps tailor marketing message. Machaon Medical Evaluations provides independent medical evaluations and chart reviews for claims management professionals. Machaon wanted to understand how to drive business growth across two key customer segments.

Using the RAPID loyalty indexes, Machaon discovered one of its customer segments had a higher PLI score compared to the other segment. As a result, Machaon tailored its marketing message to each of these two customer groups to ensure it was maximizing purchasing loyalty to the customer segment that was likely to increase its purchasing behavior in the future.

Comparing companies. Mob4Hire, a market research community for mobile applications, wanted to assess customer loyalty toward wireless providers and rank these companies. Read the online sidebar "Comparing Wireless Providers" to see how Mob4Hire used the loyalty indexes to perform its analysis.

Despite many companies using NPS, researchers have disputed whether using this metric alone is adequate. Online Table 1 compares the RAPID loyalty approach and NPS. While the NPS may be easy to understand, its strength ends there. Single-item measures, such as the NPS, are inherently less reliable (have more measurement error) than multiple-item measures.

In addition, the difference-score approach used by the NPS results is ambiguous because the same result can occur under different circumstances (for example, $50 - 20 = 30$; $40 - 10 = 30$). Finally, the NPS measures only one component of customer loyalty (advocacy), focusing primarily on driving new customer growth at the potential risk of mismanaging customers.

Relying solely on the NPS, companies may miss opportunities for growth through existing customers. In contrast, the RAPID loyalty approach offers a clear, straightforward and reliable method to comprehensively measure all three distinct facets of customer loyalty.

Understand and advance

Companies can use these customer loyalty indexes in a variety of ways to help understand the customer relationship and grow their businesses. Customer feedback programs that measure these key loyalty dimensions will help a company improve all areas of the business, from marketing and sales to service. Improvements in each phase of the customer life cycle not only help businesses ensure they deliver exceptional products and services, but also ensures they are acquiring the right type of customer through their marketing and sales efforts.

The three components of customer loyalty behaviors are not unique to wireless service providers. We have found similar results using loyalty questions in samples from other industries (PCs and insurance). The common structure of customer loyalty across samples supports the value of business programs examining all components of how loyalty (retention, advocacy and purchasing) applies in any industry.[22, 23]

Rather than blindly using loyalty questions in customer surveys, practitioners are better served if they actively select the loyalty questions that fit their specific needs. Matching the loyalty measures to the company's needs improves growth opportunities.

Online Table 2 depicts the relationship between customer loyalty predictors and business growth outcomes. A company that finds itself losing customers to its competitors could use the RLI to improve customer retention. A company that

wants to increase purchasing behavior could use the PLI to target programs that result in higher purchase behavior. A company that finds its new customer growth rate stagnant could use the ALI to increase new customer growth.

To effectively manage business growth, companies need to intelligently select their customer loyalty measures. The RAPID loyalty indexes reflect one approach to understanding the three facets of customer loyalty. **QP**

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