

ABSTRACT

Loyalty Myth #43:

Loyal Customers Are Less Expensive to Service than Non-Loyal Customers

*In this excerpt from their book **Loyalty Myths**, the authors argue that loyal customers are more demanding and therefore cost companies more money to serve.*

The fallacy that loyal customers are less expensive to service than non-loyal customers has its origins in the manufacturing environment. At its foundation are two seminal findings that dramatically influenced the strategy and tactics of manufacturers around the world.

The first is commonly referred to as the experience curve (also called the learning curve), originally by the Boston Consulting Group. The figure to the right depicts this curve. In essence, the theory behind the experience curve states that the costs of complex products and services will decline approximately 20 to 30 percent with each doubling of accumulated experience. Experience curve strategies have been integrated into the strategies of companies since the 1960s.

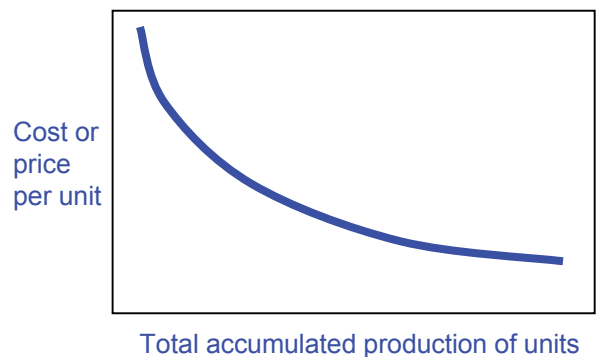
The second source of this myth rests in the quality movement of the 1980s and 1990s. Manufacturers found that improving quality produced greater cost savings than the costs of improving operations. In essence, improving quality created operating efficiencies that lowered manufacturing costs.

Both the experience curve and the operating efficiencies of quality have consistently proven true in the manufacturing environment. As a result, it would appear intuitive that they should likewise hold true in the service environment. It is important to remember that the customer retention and customer loyalty movement – initially at least – revolved around services, which is why Frederick F. Reichheld and W. Earl Sasser, Jr.'s (1990) ground breaking Harvard Business Review article was entitled “Zero Defections: Quality Comes to Services.” Reichheld argues that customer loyalty translates into cost savings for companies, stating that “your operating costs to serve them [loyal customers] decline” over time. The reason: “As the company gains experience with its customers, it can serve them more efficiently.” Given the results that manufacturers experienced through learning efficiencies and quality improvement, Reichheld’s assertions not only sound plausible, but probable.

Loyalty Myth No. 43: Debunked!

But the separation between appearing probable and occurring is all too often a chasm. In renown studies conducted by Werner J. Reinartz and V. Kumar, none of the companies tracked showed that loyal customers are consistently less expensive to manage than short-term customers. The only correlation that they could find was in the high-tech service sector, and here loyal customers were more expensive to serve.

The Experience Curve



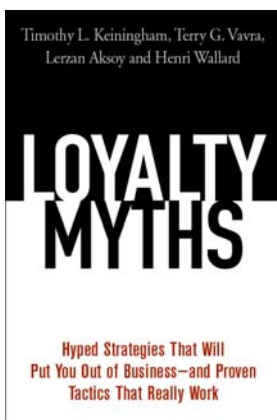
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While a company may know more about their loyal customers, loyal customers know the firm better as well. As a result, they may be more demanding of the company through better knowledge of the inner workings of the system. This allows them to seek recourse for what they believe to be inadequate treatment, and they are more likely to get perks from the relationship, which cost money to administer and fulfill.

We end with a statement made by a senior officer of a large airline when he was presenting to officers of the firm. In particular, he was discussing the complaints of flight attendants regarding the airline's high-mileage frequent-flier customers. He noted that the crew complained of these passengers being difficult and demanding. His reply, "yes, but they're ours."

In *Loyalty Myths*, business strategists and renowned authors Keiningham, Vavra, Aksoy, and Wallard reveal the ugly truth about customer loyalty: almost everything we have been told about it is wrong. Following the conventional wisdom that has been propagated about customer loyalty has, at best, led to misallocated resources; at worst, it is a recipe for financial disaster.

The pursuit of customer loyalty can be a highly profitable strategy, but not by following the myths that have developed. Our current knowledge of customer loyalty has advanced to the point of being able to identify the flaws in the conventional positions – the myths. More importantly, we can now establish and prove "loyalty truths" that we've associated with profitable customer loyalty strategies.



Praise for *Loyalty Myths*

by Keiningham, Vavra, Aksoy, and Wallard

"Nothing But the Truth: Does it cost five times as much to get new customers as to keep old ones? If you believe so, read *Loyalty Myths* by Timothy L. Keiningham, Terry G. Vavra, Lerzan Aksoy and Henri Wallard. These market researchers thoroughly dismantle that and many other customer-loyalty shibboleths, and offer better ideas."

Mark Hendricks
Entrepreneur magazine