Customer "Stickiness"...Or...Customer "Loyalty"... Is It Profitable?

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Research performed by a noted organization (HBR, Reinartz & Kumar) indicates that long-term customer loyalty (customer "stickiness") does not necessarily produce high profits from that group.

We have this built-in notion that a loyal customer over the years provides for higher than average profit contributions. Subordinated in this belief are certain claims or truisms. Here are those "truisms":

Long-term loyal customers cost less to serve. Those who support this theory argue that loyal customers have lower overall costs since the up-front costs of acquiring them are amortized over a large number of dealings. That argument presupposes that these loyal customers have been profitable in those historical transactions. A more plausible argument for this "loyalty link" is lower maintenance costs could be built on the fact there should be less hand-holding over the years.

These long-term loyal customers pay higher prices versus other customers. If loyalty does not necessarily lower costs, then perhaps it generates more revenue. There are those who might debate that their loyal customers realize the cost of switching to another supplier is too high, therefore, the loyal customer is willing to accept higher prices.

Reality says that long-term customers in fact pay lower prices than do newer customers . . . between five percent and seven percent lower. In general, then, it seems that a loyal customer is actually more price sensitive than an occasional one. There is evidence of a strong resentment against companies that attempt to leverage price increases and profit from loyalty.

Loyal customers market the company. Some feel that the more frequent customers are also the strongest advocates for your company. There is a belief that loyal customers (by word-of-mouth) help bring in new customers. Evidence says that the link between customer longevity and the propensity to market by word-of-mouth was not that strong.

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Choosing a LOYALTY Strategy

When choosing a loyalty strategy we segment four types of customers into high and low profit contributors and then into short-term and long-term customers. Each has a particular strategy for handling successfully:

- **Humming Birds:** Are quick to change, never staying in one place very long. These are short-term high profit customers. Challenge is to cease investing soon eough.
- **Great Friends:** Long-term good fit; highest profit potential; investment is encouraged
- **Alien:** This customer has little company fit and low profitability; no investment is recommended.
- **Crustacean:** limited company fit; low profit potential; these customers many times become long-term loyal customers and tend to slow the organization in the process.

The conclusion from these inputs basically says... No company should ever take for granted the idea that managing customers for loyalty is the same as managing them for profits. Loyalty is nice to have because it provides some since of security as a solid continuum base but it should never be assumed to provide extraordinary profits. **CW**

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