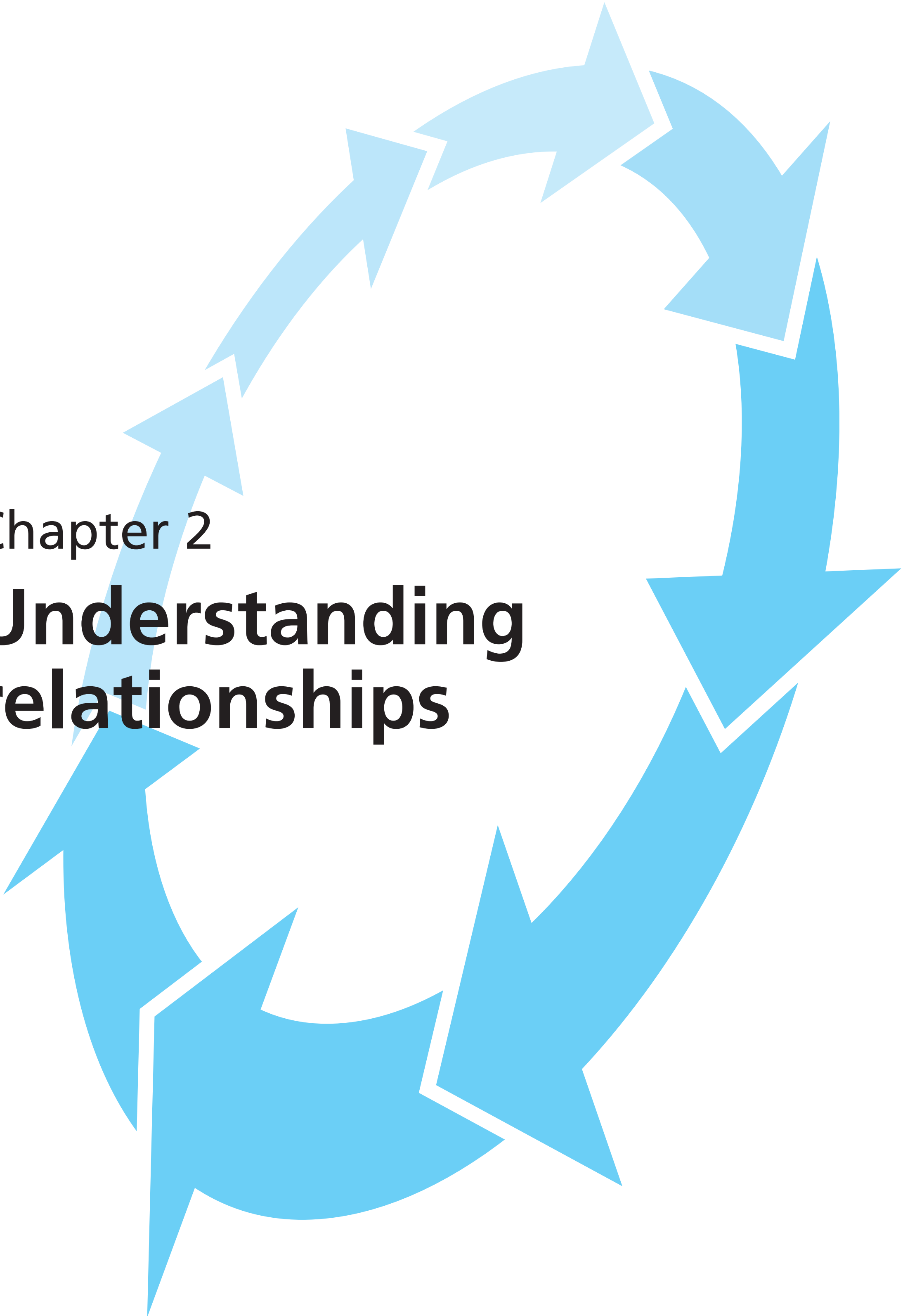


Chapter 2

Understanding relationships

Chapter objectives

By the end of this chapter, you will understand:

1. **how to recognize a relationship**
2. **attributes of successful relationships**
3. **the importance of trust and commitment within a relationship**
4. **why companies and customers are sometimes motivated to establish and maintain relationships with each other, and sometimes not**
5. **the meaning and importance of customer lifetime value**
6. **the five different schools of thought that contribute to our understanding of relationships and relationship management.**

What is a relationship?

The 'R' of CRM stands for 'relationship'. But what do we really mean by the expression 'relationship?' Certainly, most of us would understand what it means to be in a personal relationship, but what is a relationship between a customer and supplier?

At the very least a relationship involves interaction over time. If there is only a one-off transaction, like buying a vacuum cleaner from a specialist outlet, most of us wouldn't call this a relationship. Thinking in terms of a dyadic relationship, that is a relationship between two parties, if we take this interaction over time as a critical feature, we can define the term 'relationship' as follows:

> A relationship is composed of a series of interactive episodes between dyadic parties over time.

Let's be clear about what is meant by 'interactive episode'. Episodes are time bound (they have a beginning and an end) and are nameable. Within a sales representative–customer relationship it is often possible to identify a number of discrete episodes, such as making a purchase, enquiring about a product, making a sales call, negotiating terms, dealing with a complaint, resolving an invoicing dispute and playing a round of golf.

Each episode in turn is composed of a series of interactions. Interaction consists of action and response to that action. Within each episode, each participant will act towards, and interact with, the other. The content of each episode is a range of communicative behaviours including speech, deeds (actions) and body language.

Some authorities think that it is insufficient, even naïve, to define a relationship as interaction over time. Jim Barnes, for example, suggests that there needs to be some emotional content to the interaction.[1] This implies some type of affective connection, attachment or bond.

Similarly, a relationship has been said to exist only when the parties move from a state of independence to dependence or interdependence.[2] When a customer buys an occasional latte from a coffee shop, this is a transaction not a relationship. If the customer returns repeatedly because she likes the store's atmosphere, the way the coffee is prepared or has taken a shine to the barista, this looks more like a relationship. And while, in this instance, there is dependence (of the customer on the coffee shop) there is no interdependence.

This suggests the parties within the dyad may have very different ideas about whether they are in a relationship. For example, in a professional procurement context for a multinational organization, corporate buying staff may think they are being tough and transactional. Their suppliers may feel that they have built a relationship.

We can conclude from this that a relationship is a social construct. That is to say, a relationship exists if people believe that a relationship exists and they act accordingly. It is also apparent that relationships can be unilateral or reciprocal; either one or both of the parties may believe they are in a relationship.

Change within relationships

Relationships change over time. Parties become closer or more distant; interactions become more or less frequent. Because they evolve, they can vary considerably, both in the number and variety of episodes, and the interactions that take place within those episodes. Dwyer has identified five general phases through which customer–supplier relationships can evolve.[3]

1. awareness
2. exploration
3. expansion
4. commitment
5. dissolution.

Awareness is when each party comes to the attention of the other as a possible exchange partner. Exploration is the period of investigation and testing during which the parties explore each others' capabilities and performance. Some trial purchasing takes place. If the trial is unsuccessful the relationship can be terminated with few costs. The exploration phase is thought to comprise five subprocesses: attraction, communication and bargaining, development and exercise of power, development of norms, and development of expectations. Expansion is the phase in which there is increasing interdependence. More transactions take place and trust begins to develop. The commitment phase is characterized by increased adaptation and mutually understood roles and goals. Purchasing processes that have become automated are a sure sign of commitment.

Not all relationships reach the commitment phase. Many are terminated before that stage. There may be a breach of trust that forces a partner to reconsider the relationship. Perhaps the requirements of

the customer change and the supplier is no longer needed. Relationship termination can be bilateral or unilateral. Bilateral termination is when both parties agree to end the relationship. They will probably want to retrieve whatever assets they invested in the relationship. Unilateral termination is when one of the parties moves to end the relationship. Customers may exit relationships for many reasons, such as repeated service failures or changed product requirements. Suppliers may choose to exit relationships because of their failure to contribute to sales volume or profit goals. One option to resolve the problem and continue the relationship may be to reduce cost-to-serve.

This model of relationship development highlights two attributes of highly developed relationships: trust and commitment. These attributes have been the subject of a considerable amount of research.[4]

Trust

Trust is focused. That is, although there may be a generalized sense of confidence and security, these feelings are directed. One party may trust the other party's:

- **benevolence**: a belief that one party acts in the interests of the other
- **honesty**: a belief that the other party's word is reliable or credible
- **competence**: a belief that the other party has the necessary expertise to perform as required.

The development of trust is an investment in relationship building which has a long-term payoff. Trust emerges as parties share experiences, and interpret and assess each other's motives. As they learn more about each other, risk and doubt are reduced. For these reasons, trust has been described as the glue that holds a relationship together across time and experience.[5]

When mutual trust exists between partners, both are motivated to make investments in the relationship. These investments, which serve as exit barriers, may be either tangible (e.g. property) or intangible (e.g. knowledge). Such investments may or may not be retrievable when the relationship dissolves.

If trust is absent, conflict and uncertainty rise, while cooperation falls. Lack of trust clearly provides a shaky foundation for a successful customer-supplier relationship.

It has been suggested that as relationships evolve over time so does the character of trust:[6]

- **calculus-based trust**: this is present in the early stages of a relationship and is quite calculative. It is as if one party says: 'I trust you because of what I am gaining or expect to gain from the relationship'. The outcomes of creating and maintaining the new relationship are weighed against those of dissolving it.
- **knowledge-based trust**: this relies on the individual parties' interactive history and knowledge of each other, allowing each to make accurate predictions about how the other will act.

- **identification-based trust**: this happens when mutual understanding is so deep that each can act as substitute for the other in interpersonal interaction. This is found in the later stages of relationship development.

Commitment

Commitment is an essential ingredient for successful, long-term, relationships. Morgan and Hunt define relationship commitment as follows:

> Commitment is shown by 'an exchange partner believing that an ongoing relationship with another is so important as to warrant maximum effort to maintain it; that is, the committed party believes the relationship is worth working on to ensure that it endures indefinitely'. [7]

Commitment arises from trust, shared values, and the belief that partners will be difficult to replace. Commitment motivates partners to cooperate in order to preserve relationship investments. Commitment means partners eschew short-term alternatives in favour of more stable, long-term benefits associated with current partners. Where customers have choice, they make commitments only to trustworthy partners, because commitment entails vulnerability, leaving them open to opportunism. For example, a corporate customer committed to future purchasing of raw materials from a particular supplier may experience the downside of opportunistic behaviour if the supplier raises prices.

Evidence of commitment is found in the investments that one party makes in the other. One party makes investments in the promising relationship and if the other responds, the relationship evolves and the partners become increasingly committed to doing business with each other. Investments can include time, money and the sidelining of current or alternative relationships. A partner's commitment to a relationship is directly represented in the size of the investment in the relationship, since this represents termination costs. Highly committed relationships have very high termination costs, since some of these relationship investments may be irretrievable. In addition, there may be significant costs incurred in switching to an alternative supplier, such as search costs, learning costs and psychic costs.

Relationship quality

This discussion of trust and commitment suggests that some relationships can be thought to be of better quality than others. Research into relationship quality generally cites trust and commitment as core attributes of a high quality relationship.[8] However, a number of other attributes have also been identified, including relationship satisfaction, mutual goals and cooperative norms.

Relationship satisfaction is not the same as commitment. Commitment to a supplier comes as investments are made in the relationship, and investments are only made if the committed party is satisfied with

their transactional history. In other words, investments are made in relationships which are satisfactory.[9] Mutual goals are present when the parties share objectives that can only be achieved through joint action and relationship continuity. Cooperative norms are seen when relational parties work together constructively and interdependently to resolve problems.

Given that CRM implementations are often designed to build closer, more value-laden relationships with customers, it makes sense for managers to be aware of the quality of the relationships they have with customers.

Why companies want relationships with customers

The fundamental reason for companies wanting to build relationships with customers is economic. Companies generate better results when they manage their customer base in order to identify, acquire, satisfy and retain profitable customers. These are key objectives of many CRM strategies.

Improving customer retention rates has the effect of increasing the size of the customer base. Figure 2.1 compares two companies. Company A has a churn rate (customer defection rate) of 5 per cent per annum; company B's churn rate is 10 per cent. Put another way, their respective customer retention rates are 95 and 90 per cent. Starting from the same position and acquiring an identical number of new customers each year, company A's customer base is 19 per cent larger than company B's after four years: 1268 customers compared with 1066 customers.

Churn rates vary considerably. The energy utilities used to enjoy very low churn levels because of their monopoly positions. However, after

Year	Company A (5% churn)			Company B (10% churn)		
	Existing customers	New customers	Total customer base	Existing customers	New customers	Total customer base
2001	1000	100	1100	1000	100	1100
2002	1045	100	1145	990	100	1090
2003	1088	100	1188	981	100	1081
2004	1129	100	1229	973	100	1073
2005	1168	100	1268	966	100	1066

Figure 2.1 The effect of customer retention on customer numbers

industry deregulation in the UK, about 25 per cent of utility customers changed suppliers within the first 24 months. The industry had been expecting 5–10 per cent churn, and were surprised at the actual levels. Most switchers were looking for better prices and to achieve a dual-fuel (gas and electricity) discount.

Case 2.1

Consequences of customer churn at Sprint Nextel

Sprint Nextel, the third largest wireless telecommunications firm in the USA, is downsizing its workforce by 4000 jobs and closing 125 stores in the first half of 2008. The moves are part of cost-saving measures prompted by anticipated decreases in the firm's subscriber base, revenues and profitability in the fourth quarter of 2007. The firm expects to save $700 to $800 million annually by cutting the jobs.

Sprint Nextel lost 190 000 subscribers and 683 000 'post-paid' customers during the fourth quarter of 2007. The subscriber losses are being attributed to a slowdown in the growth of wireless subscriptions in the USA, and continuing customer defection to larger rivals AT&T Mobile and Verizon Wireless since Sprint bought Nextel Communications for $36 billion in 2005. The firm is also struggling with service quality problems.

On this news, shares of Sprint Nextel fell to their lowest price since October 2002.

Source: http://www.allheadlinenews.com[10]

There is little merit in growing the customer base aimlessly. The goal must be to retain existing customers and recruit new customers that have future profit potential or are important for other strategic purposes.[11] Not all customers are of equal importance. Some customers may not be worth recruiting or retaining at all, for example those who have a high cost-to-serve, are debtors, late payers or promiscuous in the sense that they switch frequently between suppliers.

Other things being equal, a larger customer base does deliver better business performance. Similarly, as customer retention rates rise (or defection rates fall), so does the average tenure of a customer, as shown in Figure 2.2. Tenure is the term used to describe the length of time a customer remains a customer. The impacts of small improvements in customer retention are hugely magnified at higher levels of retention. For example, improving the customer retention rate from 75 to 80 per cent grows average customer tenure from 10 to 12.5 years. Managing tenure by reducing defection rates can be critical. For example, it can take 13 years for utility customers to break even by recovering the costs of their initial recruitment.

Managing customer retention and tenure intelligently generates two key benefits for companies; reduced marketing costs and better customer insight.

Customer retention rate (%)	Average customer tenure
50	2 years
67	3 years
75	4 years
80	5 years
90	10 years
92	12.5 years
95	20 years
96	25 years
97	33.3 years
98	50 years
99	100 years

Figure 2.2
Retention rate and average customer tenure

Reduced marketing costs

Improving customer retention reduces a company's marketing costs. Fewer dollars need to be spent replacing churned customers.[12] For example, it has been estimated that it costs an advertising agency at least 20 times as much to recruit a new client than it does to retain an existing client. Major agencies can spend up to $4 million on research, strategic analysis and creative work in pitching for one major client, with up to four creative teams working on different executions. An agency might incur these costs several times over as it pitches to several prospective clients to replace a lost client.[13] In addition to reducing the costs of customer acquisition, cost-to-serve existing customers also tends to fall over time. Ultimately, as in some business-to-business markets, the relationship may become fully automated. Some supply-chain relationships, for example, employ electronic data interchange (EDI) that fully automates the ordering, inventory and invoicing processes. EDI is a relationship investment that acts as an exit barrier.

Better customer insight

As customer tenure lengthens, suppliers are able to develop a better understanding of customer requirements and expectations. Customers also come to understand what a supplier can do for them. Consequently, suppliers become better placed to identify and satisfy customer requirements profitably, selling more product and service to the retained customer. Over time, as relationships deepen, trust and commitment between the parties is likely to grow. Under these circumstances, revenue and profit streams from customers become more secure. One study, for example, shows that the average online clothing customer spends 67 per cent more, and grocery customers spend 23 per cent more, in months 31–36 of a relationship than they spend in months 0–6.[14] In sum, both the cost and revenue sides of the profit equation are impacted by customer retention.

Some companies employ a model that has been variously known as a value ladder[15] or value staircase[16] to help them understand where customers are positioned in terms of their tenure with the company. Customers typically buy from a portfolio of more or less equivalent offers or suppliers. For example, large and medium-sized businesses often do business with more than one bank, and consumers may select a soft drink from a small portfolio of branded carbonated beverages. When customers climb the ladder, their value to your company grows. Your share of their portfolio expands. Put another way, your share of customer spending, or customer wallet, grows. In Table 2.1 we present a seven-stage customer journey from suspect status to advocate status.

Table 2.1 The customer journey

Stage	Description
Suspect	Does the potential customer fit your target market profile?
Prospect	The customer fits the target market profile and is being approached for the first time.
First-time customer	The customer makes a first purchase.
Repeat customer	The customer makes additional purchases. Your offer plays a minor role in the customer's portfolio.
Majority customer	The customer selects your company as supplier of choice. You occupy a significant place in the customer's portfolio.
Loyal customer	The customer is resistant to switching suppliers and has a strong positive attitude to your company or offer.
Advocate	The customer generates additional referral dollars through positive word-of-mouth.

As in the Dwyer model cited earlier, not every customer progresses uniformly along the path from 'never-a-customer' to 'always-a-customer'. Some will have a long maturity phase (i.e. loyal customer); others will have a shorter life, perhaps never shifting from first-time customer to repeat customer; others still might never convert from prospect to first-timer. CRM software allows companies to trace where customers are on this pathway and to allocate resources intelligently to advance suitable customers along the value trajectory.

Costs and revenues vary from stage to stage of the journey. In the early stages, a company may invest significant sums in converting a prospect into a first-time customer. The investment in initiating a relationship may not be recovered for some time. For example, Reichheld and Sasser have shown that it takes a credit-card company approaching two years to recover the costs of customer acquisition.[17] Another study shows that the average online clothing customer takes four purchases (12 months) to recover the costs of their acquisition, whereas grocery customers take 18 months to break even.[18] In later years, the transactions within the relationship may become highly routinized and very low cost to complete, because each party knows and trusts the other.

Lifetime value

This leads to the core CRM idea that a customer should not be viewed as a set of independent transactions, but as a lifetime income stream. In the automobile industry, for example, it is estimated that a General Motors retail customer is worth $276 000 over a lifetime of purchasing cars (11 or more vehicles), parts and service. Fleet operators are worth considerably more.[19] When a GM customer switches to Ford, the revenue streams from that customer may be lost for ever. This makes customer retention a strategically important goal for GM.

Case 2.2

Customer lifetime value (CLV) in the banking industry

One in five banking executives does not measure CLV. Couple this with the 22 per cent who do not measure portfolio or wallet share, and it is easy to see why cross-selling is such a challenge for financial service providers. Unless a banker knows which of a customer's financial needs are being met, it is exceedingly difficult to suggest additional services. A robust business intelligence system can provide a financial services firm with a 360 degree view of the customer. Transactions can be consolidated with demographic and psychographic data, revenue and profit measures, as well as with historical customer service incidents and queries. With this total picture, the provider can see the customer from multiple perspectives and craft programmes that will satisfy a broader range of client requirements. Part of this multifaceted view of the customer is the ability to aggregate multiple customers into a household perspective. The benefits of this consolidated view are clear and strong. Multiple financial service needs can be seen in total, investment opportunities can be tied to life events for cohabiting family members and marketing costs can be driven down by providing a single, comprehensive marketing message.

Source: IBM[20]

Lifetime value (LTV), which is also known as customer lifetime value (CLV), is a measure of a customer's, or customer segment's, profit-generation for a company. LTV can be defined as follows:

> Lifetime value is the present day value of all net margins earned from a relationship with a customer, customer segment or cohort.

LTV can be estimated at the level of the individual customer, customer segment or cohort. A cohort of customers is a group that has some characteristic or set of characteristics in common. These might be customers recruited in a single year or recruited though a single campaign or channel. This type of analysis is useful, for example, to find out whether certain channels are more effective or more efficient at recruiting high value customers. A European motoring organization knows that it costs an average of $105 to recruit a new member. However, recruitment costs vary across channels. The organization's member-get-member (MGM) referral scheme costs $66, the organization's direct response TV campaign costs $300, and door drops cost $210 per newly acquired member. The

MGM scheme is most cost-effective at customer acquisition, but if these customers churn at a high rate and cost significantly more to serve, they may in fact be less valuable than customers generated at higher initial cost. In fact, customers acquired through the MGM referral scheme remain members longer, buy more and also generate word-of-mouth referrals.

To compute LTV, all historic net margins are compounded up to today's value and all future net margins are discounted back to today's value. Estimates of LTV potential look only to the future and ignore the past.

The focus on net margins rather than gross margins is because a customer that appears to be valuable on the basis of the gross margins generated might seem less profitable once cost-to-serve the customer is taken into account. Companies that do not have the processes in place to allocate costs to customers cannot use net margin data. They must work either with gross margin or sales revenue data.

For most companies, an important strategic objective is to identify and attract those customers or segments that have the highest LTV potential. They are unconcerned with the past. What matters is the future.

Research by Reichheld and Sasser indicates why it is important to look forward to compute LTV.[21] Their data suggest that profit margins tend to accelerate over time, as shown in Figure 2.3. This has four causes.

1. **Revenues grow** over time as customers buy more. In the credit-card example in Figure 2.3, users tend to grow their balances over time as they become more relaxed about using their card for an increasing range of purchases. Also, a satisfied customer may look to buy additional categories of product from a preferred supplier. An insurance company that has a loyal car insurance customer is likely to experience some success cross-selling other personal lines, for example home, property and travel insurance.

Profit (loss) per customer over time ($)

Service	Year 0	1	2	3	4	5
Credit card	(51)	30	42	44	49	55
Industrial laundry		144	166	192	222	256
Industrial distribution		45	99	121	144	168
Auto servicing		25	35	70	88	88

Figure 2.3 Profit from customers over time

2. **Cost-to-serve is lower** for existing customers, because both supplier and customer understand each other. For example, customers do not make demands on the company that it cannot satisfy. Similarly companies do not communicate offers that have little or no value to customers.

3. **Referrals are generated** by existing, satisfied customers through their unpaid advocacy. Lexus UK, for example, believes that every delighted customer generates £600 000 of referral business. Word-of-mouth is recognized as powerfully persuasive because it is regarded as being independent and unpaid.
4. **Higher prices are paid** by existing customers than those paid by new customers. This is partly because they are not offered the discounts that are often employed to win new customers, and partly because they are less sensitive to price offers from other potential suppliers because they are satisfied with their experience.

Computing LTV

The computation of LTV potential is, in principle, very straightforward. Several pieces of information are required. For an existing customer, you need to know:

1. what is the probability that the customer will buy products and services from the company in the future, period-by-period?
2. what will the gross margins on those purchases be, period-by-period?
3. what will the cost of serving the customer be, period-by-period?

For new customers an additional piece of information is needed:

4. what is the cost of acquiring the customer?

Finally, to bring future margins back to today's value, another question needs to be answered for both existing and new customers:

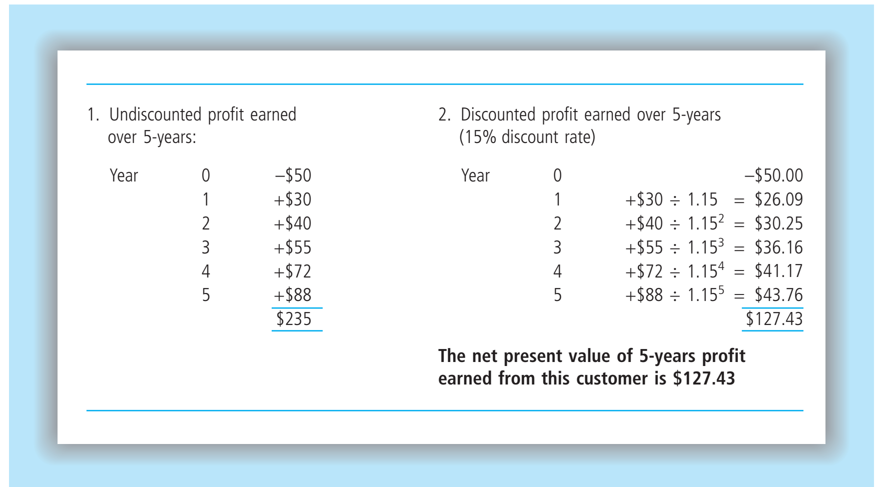
5. what discount rate should be applied to future net margins?

Some commentators suggest that LTV estimates should not be based only on future purchasing, but also on word-of-mouth (WOM) influence. The logic is that a satisfied and retained customer not only buys, but also influences others to buy. Lee and colleagues show that incorporation of WOM effects increases LTV estimates significantly.[22]

Figure 2.4 demonstrates the impact that discount rate has on customer value. Without discounting future profits, the customer appears to have an LTV of $235. However, once a 15 per cent discount rate is applied, the customer's LTV in today's dollar is only $127.43. A common practice is to use the weighted average cost of capital (WACC) as the discount factor. WACC takes into account the costs of the two sources of capital: debt and equity. Each usually has a different cost, and therefore the average cost of capital for a business will reflect the degree to which the business is funded by the two sources.

Computation of a meaningful LTV estimate requires companies to be able to forecast customer buying behaviour, product and service costs and prices, the costs of capital (for determining the discount rate) and the costs of acquiring and retaining customers. This is very demanding, especially at the level of the individual customer, but it is a challenge that analytical CRM implementations often address.

A number of companies have developed models that produce approximate LTV estimates. US Bancorp, for example, calculates a



1. Undiscounted profit earned over 5-years:

Year		
	0	−$50
	1	+$30
	2	+$40
	3	+$55
	4	+$72
	5	+$88
		$235

2. Discounted profit earned over 5-years (15% discount rate)

Year			
	0		−$50.00
	1	$+\$30 \div 1.15$	= $26.09
	2	$+\$40 \div 1.15^2$	= $30.25
	3	$+\$55 \div 1.15^3$	= $36.16
	4	$+\$72 \div 1.15^4$	= $41.17
	5	$+\$88 \div 1.15^5$	= $43.76
			$127.43

The net present value of 5-years profit earned from this customer is $127.43

Figure 2.4
Impact of discount rate on lifetime value

customer profitability metric called customer relationship value (CRV) in which they use historical product ownership to generate 'propensity to buy' indices. Overhead costs are not factored into the computation. Within their customer base, they have been able to identify four CRV segments, each having different value, cost, attrition and risk profiles:

- top tier, 11% of customers
- threshold, next 22%
- fence sitters, next 39%
- value destroyers, bottom 28%.

Each of these segments is treated to different value propositions and customer management programmes: product offers, lending decisions, fee waivers, channel options and retention efforts. For situations where the cost of generating accurate LTV data is thought not to be prohibitive, Berger and Nasr have developed a number of mathematical models that can be used in LTV estimation.[23]

Case 2.3

High lifetime value (LTV) customers at Barclays Bank

Barclays is a leading UK-based bank with global operations. As part of the bank's CRM strategy, it undertook customer portfolio analysis to identify which retail segments were most strategically significant. The analysis found that customers within the 25–35 year age group, who were professionally employed, who had a mortgage and/or credit-card product were most strategically significant. These were the bank's most profitable customers.

The bank also found that this segment represented the highest potential lifetime value (LTV) for the bank, 12 per cent greater than any other segment. LTV is derived from the bank's estimates of future income from fees, interest and other charges over their lifetime as a customer.

Figure 2.5 shows how to compute LTV for a cohort of customers. In year 0, the company spent $10 million in marketing campaigns to generate new customers. The result was 100 000 new customers added to the customer base at an acquisition cost of $100 per customer.

Year	$ Profit per customer	$ net present value at 15% discount	Customer retention rate (%)	No. of customers	$ Total annual profit
0	−100			100 000	−10 000 000
1	50	43.48	60	60 000	2 608 800
2	70	52.93	70	42 000	2 223 062
3	100	65.75	75	31 500	2 071 125
4	140	80.00	80	25 200	2 016 000
5	190	94.53	85	21 420	2 024 776
6	250	108.23	90	19 278	2 086 364
7	320	120.30	92	17 736	2 133 654
8	400	130.72	94	16 672	2 179 346
9	450	127.84	95	15 838	2 024 744
10	500	123.15	96	15 204	1 872 372

Figure 2.5 Computing cohort value

In year 1 the company lost 40 per cent of these new customers, but the remaining 60 per cent each generated $50 contribution to profit. If this is discounted at 15 per cent, in year 0's currency each retained customer's profit contribution is $43.48. In year 2, the retention rate rises from 60 to 70 per cent, and each of the remaining customers contributes $70 ($52.93 at discounted rate) to profit. You can see from the right hand column in Figure 2.5 that it takes nearly five years to recover the investment of acquiring this cohort. The data demonstrate two well-established phenomena. First, profit per customer rises over time, for reasons set out earlier in this chapter. Secondly, customer retention rate rises over time. It is feasible to use data such as these to manage a business for improved profitability. Several strategies are available:

1. Improve customer retention rate in the early years of the relationship. This will produce a larger number of customers to generate higher profits in the later years.
2. Increase the profit earned per customer by:
   a. reducing cost-to-serve
   b. cross-selling or up-selling additional products and services.
3. Become better at customer acquisition by:
   a. using more cost effective recruitment channels
   b. better qualification of prospects. Customers who defect early on perhaps should not have been recruited in the first place.

Don't leave this discussion of LTV by believing that if you improve customer retention business performance will automatically improve. It depends entirely on which customers are retained and how you manage those relationships.

Why companies do NOT want relationships with customers

Despite the financial benefits that can accrue from a relationship, companies sometimes resist entering into relationships with customers. In the business-to-business (B2B) context there are a number of reasons for this resistance.

Loss of control: a mature relationship involves give and take on both sides of the dyad. In bilateral relationships, suppliers may have to give up unilateral control over their own business's resources. For example, a supplier of engineering services might not want to provide free pre-sales consultancy for a new project with an established client because of the high costs involved. However, the relationship partner might have clear expectations of what activities should be performed and what resources deployed by both themselves and the other party.

Exit costs: not all relationships survive. It is not necessarily easy or cost-effective to exit a relationship. Sometimes, investments that are made in a relationship are not returned when a relationship breaks down. Relationship investments vary from the insignificant (e.g. co-branding of promotional literature) to highly significant (e.g. setting up a new production line to service a particular customer's requirements). A company might justifiably be concerned about the security of a relationship-based investment in new manufacturing operations.

Resource commitment: relationships require the commitment of resources such as people, time and money. Companies have to decide whether it is better to allocate resources to customer management or some other area of the business, such as operations or research and development. Once resources are committed, they can become sunk costs. Sunk costs are unrecoverable past expenditures. These would not normally be taken into account when deciding whether to continue in a relationship, because they cannot be recovered whether the relationship endures or not. However, it is a common instinct to consider them.

Opportunity costs: if resources are committed to one customer, they cannot be allocated to another. Relationships carry with them high opportunity costs. If you commit resources to customer A, you may have to give up the possibility of a relationship with customer B, even if that does seem to be a better proposition. An engineering consultancy that commits consultants to pre-sales activities with a current client

might incur the opportunity cost of losing more lucrative work generating new business opportunities from other prospective clients.

Why customers want relationships with suppliers

B2B context

There are a number of circumstances when a B2B customer might want a long-term relationship with a supplier:

Product complexity: if the product or its applications are complex, for example, networking infrastructure.
Product strategic significance: if the product is strategically important or mission-critical, for example, supply of essential raw materials for a continuous process manufacturer.
Service requirements: if there are down-stream service requirements, for example, for machine tools.
Financial risk: if financial risk is high, for example, in buying large items of capital equipment.
Reciprocity: a financial audit practice may want a close relationship with a management consultancy, so that each party benefits from referrals by the other.

B2C context

In a business-to-consumer (B2C) context, relationships may be valued when the customer experiences benefits over and above those directly derived from acquiring, consuming or using the product or service. For example:

Recognition: customers may feel more valued when recognized and addressed by name, for example at a retail bank branch, or as a frequent flyer.
Personalization: products or services can be customized. For example, over time, a hairdresser may come to understand a customer's particular preferences or expectations.
Power: relationships with suppliers can be empowering. For example, some of the usual power asymmetry in relationships between banks and their customers may be reversed when customers feel that they have personal relationships with particular bank officers or branches.
Risk reduction: risk takes many forms – performance, physical, financial, social and psychological. High levels of perceived risk are uncomfortable for many customers. A relationship can reduce or even, perhaps, eliminate perceived risk. For example, a customer may develop a relationship with a service station to reduce the perceived performance and physical risk attached to having a car serviced. The

relationship provides the assurance that the job has been skilfully performed and that the car is safe to drive.

Status: customers may feel that their status is enhanced by a relationship with a supplier, such as an elite health club or a company offering a platinum credit-card.

Affiliation: people's social needs can be met through commercially based, or non-commercially based, relationships. Many people are customers (members) of professional or community associations, for example.

Customer segments can vary in their desire to have relationships with suppliers. For example, large corporations have their own treasury departments and often get little value from a bank relationship; small private account holders have no need for the additional services that a relationship provides; small and medium-sized business and high net worth individuals may have most to gain from a closer relationship with a bank.

A number of B2C organizations deliver incremental benefits by building closer relationships with their customers. Casa Buitoni, for example, offers customers the opportunity to learn more about Italian cuisine through an online customer club. The Harley Owners Group (HOG) offers a raft of benefits to Harley Davidson owners, including club outings and preferential insurance rates. Nestlé's mother and baby club offers advice and information to new mothers.

Why customers do NOT want relationships with suppliers

While companies generally want long-term relationships with customers for the economic reasons described above, it is far less clear that customers universally want relationships with their suppliers. B2B customers cite a number of concerns.[24]

Fear of dependency: this is driven by a number of worries. Customers may be concerned that the supplier might act opportunistically, once they are in a preferred position, perhaps introducing price rises. They may also fear the reduction in their flexibility to choose alternative suppliers. There may also be concerns over a loss of personal authority and control.

Lack of perceived value in the relationship: customers may not believe that they will enjoy substantial savings in transaction costs, or that the relationship will help them create a superior competitive position, generate additional revenue or that there will be any social benefits. In other words, there is no perceived value above and beyond that obtained from the product or service.

Lack of confidence in the supplier: customers may choose not to enter a relationship because they feel the potential partner is unreliable,

too small, strategically insignificant, has a poor reputation or is insufficiently innovative.

Customer lacks relational orientation: not all company cultures are equally inclined towards relationship building. Some are much more transactional. For example, some retailers make it a policy to buy a high proportion of their merchandise through special offers. The preference for transactional rather than relational business operations may be reflected in a company's buying processes and reward systems.

Rapid technological changes: in an industry with rapidly changing technology, commitment to one supplier might mean that the customer misses out on new developments available through other suppliers.

In the B2C context, consumers buy hundreds of different convenience, shopping and speciality products and services. Whereas consumers might want a relationship with their financial service advisor or their physician, they can often find no good reason for developing closer relationships with the manufacturer of their household detergent, snack foods or toothpaste. However, for consumer products and services that are personally important, customers can become more involved and become more emotionally engaged.

Customer satisfaction, loyalty and business performance

An important rationale for CRM is that it improves business performance by enhancing customer satisfaction and driving up customer loyalty, as shown in Figure 2.6. There is a compelling logic to the model, which has been dubbed the 'satisfaction–profit chain'.[25] Satisfaction increases because customer insight allows companies to understand their customers better,

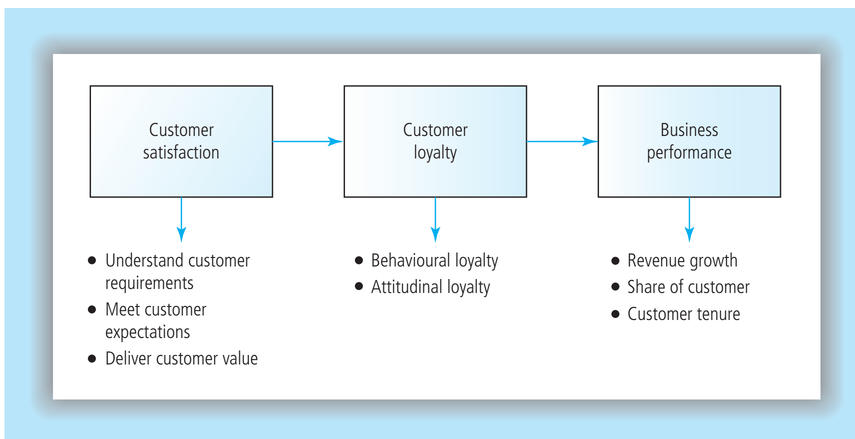


Figure 2.6
The satisfaction–profit chain

and create improved customer value propositions and better customer experiences. As customer satisfaction rises, so does customer intention to repurchase.[26] This in turn influences actual purchasing behaviour, which has an impact on business performance.

We'll examine the variables and linkages between them. First we'll define the major variables of customer satisfaction, customer loyalty and business performance.

Customer satisfaction

Customer satisfaction has been the subject of considerable research, and has been defined and measured in many ways.[27] We define customer satisfaction as follows:

> Customer satisfaction is the customer's fulfilment response to a customer experience, or some part thereof.

Customer satisfaction is a pleasurable fulfilment response. Dissatisfaction is an unpleasurable fulfilment response. The 'experience, or some part thereof' component of the definition suggests that the satisfaction evaluation can be directed at any or all elements of the customer's experience. This can include product, service, process and any other components of the customer experience.

The most common way of quantifying satisfaction is to compare the customer's perception of an experience, or some part of it, with their expectations. This is known as the expectations–disconfirmation model of customer satisfaction. This model suggests that if customers perceive their expectations to be met, they are satisfied. If their expectations are underperformed, this is negative disconfirmation and they will be dissatisfied. Positive disconfirmation occurs when perception exceeds expectation. The customer might be pleasantly surprised or even delighted. This model assumes that customers have expectations, and that they are able to judge performance. A customer satisfaction paradox has been identified by expectations–disconfirmation researchers. At times customers' expectations may be met but the customer is still not satisfied. This happens when the customer's expectations are low. 'I expected the plane to be late. It was. I'm unhappy!'

Many companies research customer requirements and expectations to find out what is important for customers, and then measure customers' perceptions of their performance compared to the performance of competitors.

Customer loyalty

Customer loyalty has also been the subject of considerable research. There are two major approaches to defining and measuring loyalty, one based on behaviour, the other on attitude.

Behavioural loyalty is measured by reference to customer purchasing behaviour. Loyalty is expressed in continued patronage and buying. There are two behavioural aspects to loyalty. First, is the customer still active? Secondly, have we maintained our share of customer spending?

In portfolio purchasing environments, where customers buy products and services from a number of more-or-less equal suppliers, the share of customer spending question is more important.

Many direct marketing companies use RFM measures of behavioural loyalty. The most loyal are those who have high scores on the three behavioural variables: recency of purchases (R), frequency of purchases (F) and monetary value of purchases (M). The variables are measured as follows:

R = time elapsed since last purchase
F = number of purchases in a given time period
M = monetary value of purchases in a given time period.

Attitudinal loyalty is measured by reference to components of attitude such as beliefs, feelings and purchasing intention. Those customers who have a stronger preference for, involvement in, or commitment to a supplier are the more loyal in attitudinal terms.

Recently, researchers have combined both views into comprehensive models of customer loyalty. The best known is Dick and Basu's model, as shown in Figure 2.7.[28] These authors identify four forms of loyalty, according to relative attitudinal strength and repeat purchase behaviour. 'Loyals' are those who have high levels of repeat buying and a strong relative attitude. 'Spurious loyals' have high levels of repeat purchase but weak relative attitude. Their repeat purchasing can be explained by inertia, high switching costs or indifference. Latent loyalty exists when a strong relative attitude is not accompanied by repeat buying. This might be evidence of weakness in the company's distribution strategy, the product or service not being available when and where customers want.

From a practical point of view, the behavioural definition of loyalty is attractive because sales and profits derive from actions not attitudes.

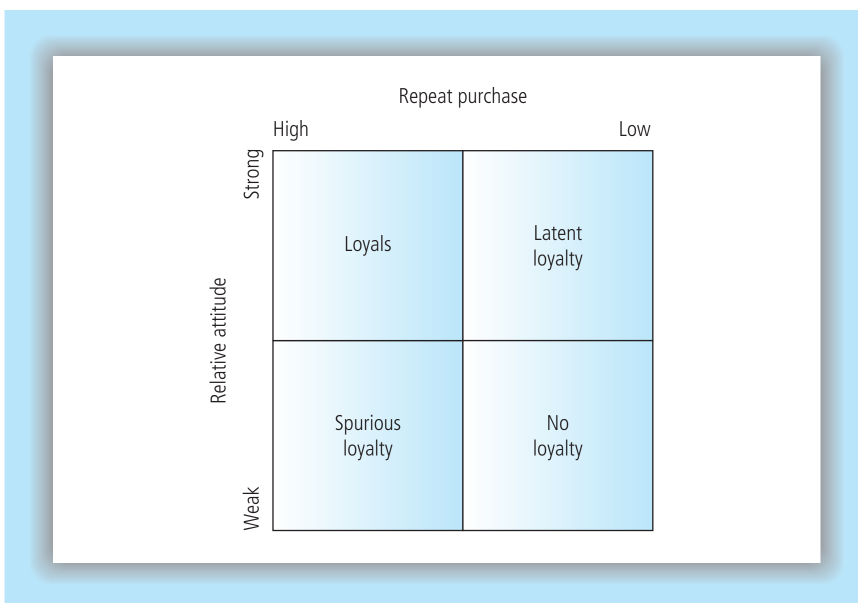


Figure 2.7
Two-dimensional model of customer loyalty

However, taking the trouble to understand the causes of weak or negative attitudes in customers can help companies identify barriers to purchase. It is equally true that knowledge of strong or positive attitudes can help companies understand the causes of competitor-resistant commitment. However, it is not clear from the Dick and Basu model whether attitude precedes behaviour or behaviour precedes attitude. Researchers generally accept that causation is circular rather unidirectional. In other words, attitudes influence behaviour, and behaviour influences attitude.

Business performance

Business performance can be measured in many ways. The recent trend has been away from simple short-term financial measures such as quarterly profit or earnings per share. Leading companies are moving towards a more rounded set of performance indicators, such as represented by the balanced scorecard.[29]

The balanced scorecard employs four sets of linked key performance indicators (KPI): financial, customer, process and learning and growth. The implied connection between these indicators is that people (learning and growth) do things (process) for customers (customer) that have effects on business performance (financial).

Customer-related KPIs that can be used to evaluate business performance following a CRM implementation include: customer satisfaction levels, customer retention rates, customer acquisition costs, number of new customers acquired, average customer tenure, customer loyalty (behavioural or attitudinal), sales per customer, revenue growth, market share and share of customer (wallet).

The balanced scorecard is highly adaptable to CRM contexts. Companies need to ask the following questions. What customer outcomes drive our financial performance? What process outcomes drive our customer performance? What learning and growth outcomes drive our process performance? The satisfaction–profit chain suggests that the customer outcomes of satisfaction and loyalty are important drivers of business performance.

Share of customer (share of wallet or SOW) is a popular measure of CRM performance. If your company makes a strategic CRM decision to serve a particular market or customer segment, it will be keen to measure and grow its share of the chosen customers' spending. As indicated in Figure 2.8, share of customer focuses on winning a greater share of targeted customers' or segments' spending, rather than market share.

Researching the satisfaction–profit chain

We'll now look at some of the research into the links between customer satisfaction, loyalty and business performance. Analysis has been done

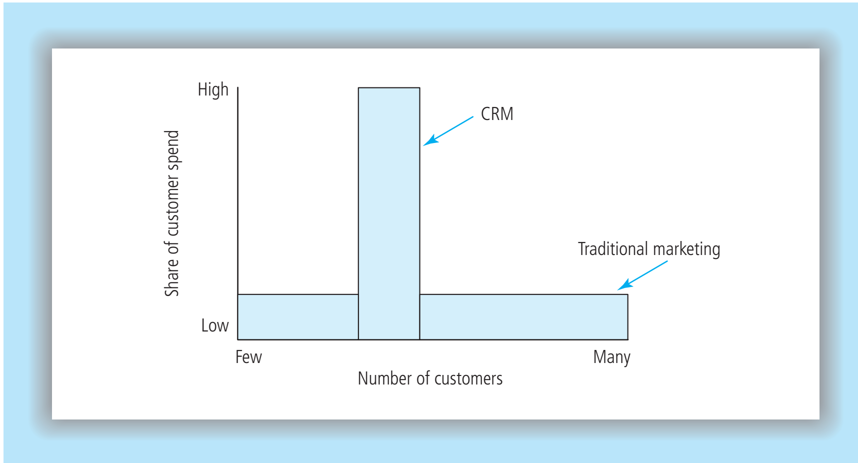


Figure 2.8
Share of market versus share of customer

on international data, national data, industry data, corporate data and individual customer data.

The American Customer Satisfaction Index (ACSI) was established in 1994. It has tracked the relationships between customer satisfaction and a number of antecedents and consequences, including customer loyalty as measured by customers' probability of buying at different price points. The ASCI model appears in Figure 2.9. Data are collected in telephone interviews with approximately 250 current customers of the larger companies in a number of industries.[30] Results from the multi-industry study show that there is a strong correlation between customer satisfaction scores and corporate earnings in the next quarter. According to the ACSI organization, 'the reason is that a satisfied customer is more profitable than a dissatisfied one. If satisfaction declines, customers become more reluctant to buy unless prices are cut. If satisfaction improves the opposite is true'. [31] An independent study, using data from the ACSI, has also found that customer satisfaction had a considerable effect on business performance, although there was variation across sectors.[32]

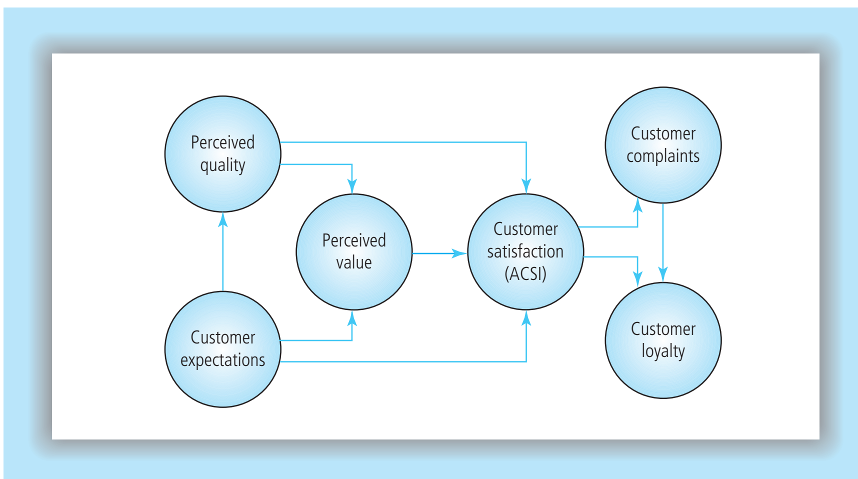


Figure 2.9
The American Customer Satisfaction Index (ACSI) model[33]

The European Customer Satisfaction Index, using a somewhat different model, analyses data from 11 European countries and also reports a strong relationship between customers' value perceptions, satisfaction levels and loyalty.[34]

At the national level, customer data from the Swedish Customer Satisfaction Barometer (SCSB) have been correlated with corporate profit performance since 1989. A lagged relationship has been identified, indicating that current customer satisfaction levels impact on tomorrow's profit performance.[35] The SCSB database matches customer-based measures with traditional financial measures of business performance, such as productivity and return on investment (ROI). The SCSB is one of several such national indices.

A number of studies in different industries and companies – telecommunications, banking, airline and automobile distribution – support the relationship between customer satisfaction, loyalty and business performance.

- **Telecommunications**: one study of the telecoms industry found that a 10 per cent lift in a customer satisfaction index predicted a 2 per cent increase in customer retention (a behavioural measure of loyalty) and a 3 per cent increase in revenues. The authors concluded that customer satisfaction was a lead indicator of customer retention, revenue and revenue growth.[36]
- **Banking**: another study found that customer satisfaction in retail banking correlated highly with branch profitability. Highly satisfied customers had balances 20 per cent higher than satisfied customers, and, as satisfaction levels went up over time, so did account balances. The reverse was also true, as satisfaction levels fell, so did account balances.[37]
- **Airlines**: a study in the airline industry examined the link between customer dissatisfaction, operating income, operating revenue and operating expense. The study identified the drivers of dissatisfaction as high load factors (i.e. seat occupancy), mishandled baggage and poor punctuality. The study concluded that as dissatisfaction rose, operating revenue (an indicator of customer behaviour) and operating profit both fell, and operating expense rose.[38]
- **Car distribution**: a study of Volvo car owners examined the links between customer satisfaction with three attributes – car purchase, workshop service and the vehicle itself – and dealer business performance. The results indicated that a one scale-point increase in overall customer satisfaction was associated with a 4 per cent increase in dealer profitability at next car purchase.[39]
- **Multi-industry**: using 400 sets of matched corporate-level data obtained from two databases – the ACSI (see above, which provided customer satisfaction scores) and Standard and Poors' Compustat (which provided business profitability data) – Yeung and colleagues found a linear relationship between customer satisfaction scores and business profitability. They rise and fall together in the same time period.[40]

Research into the satisfaction–profit chain has also been performed at the level of the individual customer. Using data collected from both customers and exporters in the Norwegian fishing industry, Helgesen finds support for both steps in the satisfaction–profit chain.[41] Satisfaction is positively associated with behavioural loyalty, which in turn is positively associated with customer profitability. However, he notes that 'the satisfaction level has to pass a certain threshold if it is to have any influence on customer loyalty', and that as satisfaction increases it has a diminishing effect on loyalty. The same effects are observed in the relationship between loyalty and customer profitability. Furthermore, only 10 per cent of the variance in each independent variable was accounted for by the dependent variable.

According to one review, there is 'growing evidence that the links in the satisfaction–profit chain are solid'.[42] However, the relationships can be both asymmetrical and non-linear. The asymmetric nature of the relationships is found by comparing the impact of an increase in one variable with an equivalent decrease. For example, a one-scale point shift up in customer satisfaction (say from three to four on a five-point scale) may not have a comparable impact on customer retention rates as a one-scale point downward shift (say from three to two on the same five-point scale). Secondly, links can be nonlinear. Nonlinearity is sometimes reflected in diminishing returns, at other times in increasing returns. For example, increasing returns may be obtained in repeat purchase levels as customers progress up the customer satisfaction scale, as shown in Figure 2.10. Diminishing returns may set in if customer expectations are already largely met. Investments in increasing customer satisfaction at already high levels of performance do not have the same impact as investments at lower levels of performance.

Figure 2.10 Non-linear relationship between customer satisfaction and repeat purchase

Relationship management theories

There are five main schools of thought that offer different perspectives on relationships between customers and suppliers. Although some schools are quite similar, they generally describe relationships in different terms and have different implications for relationship management. The major schools of thought are the Industrial Marketing and Purchasing (IMP) school, the Nordic school, the Anglo-Australian school, the North American school, and the Asian (*guanxi*) school. Each is briefly reviewed in the following sections. Concepts and themes from these schools have been incorporated into the preceding discussion.

The Industrial Marketing and Purchasing school

The Industrial Marketing and Purchasing school (IMP) has a dedicated focus on B2B relationships. The IMP school first emerged in the late 1970s when a number of European researchers began investigating B2B relationships with the simple goal of describing them accurately. Some of the major contributors to the IMP school are Malcolm Cunningham, David Ford, Lars-Erik Gadde, Håkan Håkansson, Ivan Snehota, Peter Naudé and Peter Turnbull.[43]

The IMP school argues that B2B transactions occur within the context of broader, long-term relationships, which are, in turn, situated within a broader network of relationships. Any single B2B relationship between supplier and customer is composed of activity links, actor bonds and resource ties. IMP researchers were among the first to challenge the view that transaction costs determined which supplier would be chosen by a customer. IMP researchers identified the important impact of relationship history on supplier selection. The characteristics of B2B relationships, from an IMP perspective, are as follows:

- Buyers and sellers are both active participants in transactions, pursuing solutions to their problems rather than simply reacting to the other party's influence.
- Relationships between buyers and sellers are frequently long-term, are close in nature, and involve a complex pattern of interaction between and within each company.
- Buyer–seller links often become institutionalized into a set of roles that each party expects the other to perform, with expectations that adaptations will be made on an ongoing basis.
- Interactions occur within the context of the relationship's history and the broader set of relationships each firm has with other firms – the firm's network of relationships. We examine the role of network members in the achievement of CRM goals in Chapter 10.
- Firms choose whom they interact with and how. The relationships that firms participate in can be many and diverse, carried out for different purposes, with different partners, and have different levels

of importance. These relationships are conducted within a context of a much broader network of relationships.

- Relationships are composed of actor bonds, activity links and resources ties, as now described.

Actor bonds

Actor bonds are defined as follows:

> Actor bonds are interpersonal contacts between actors in partner firms that result in trust, commitment and adaptation between actors.[44]

Actor bonds are a product of interpersonal communication and the subsequent development of trust. Adaptation of relationships over time is heavily influenced by social bonding.

Activity links

Activity links can be defined as follows:

> Activity links are the commercial, technical, financial, administrative and other connections that are formed between companies in interaction.

Activities might centre on buying and selling, technical cooperation or inter-firm projects of many kinds. Activities such as inter-partner knowledge exchange, the creation of inter-partner IT systems, the creation of integrated manufacturing systems such as just-in-time (JIT) and efficient consumer response (ECR), the development of jointly implemented total quality management (TQM) processes, are investments that demonstrate commitment.

IMP researchers have focused on two major streams of activity-related research: the structure and cost effectiveness of activity links, and the behavioural characteristics that enable relationships to survive. The reduction of transaction costs is an important motivation for customers forming links with suppliers. Dyer argues that search costs, contracting costs, monitoring costs and enforcement costs (the four major types of transaction cost) can all be reduced through closer B2B relationships.[45]

Resource ties

Resources are defined as follows:

> Resources are the human, financial, legal, physical, managerial, intellectual and other strengths or weaknesses of an organization.[46]

Resource ties are formed when these resources are deployed in the performance of the activities that link supplier and customer. Resources that are deployed in one B2B relationship may strengthen and deepen that relationship. However, there may be an opportunity cost. Once resources (for example, people or money) are committed to one relationship they might not be available for another relationship.

The Nordic school

The Nordic school emphasizes the role of service in supplier–customer relationships. The main proponents of the Nordic school are Christian Grönroos and Evert Gümmesson.[47]

The Nordic school emerged from research into services marketing that began in the late 1970s, particularly in Scandinavia. The key idea advocated by the Nordic school is that service is a significant component of transactions between suppliers and their customers. Their work became influential in the development of the field of relationship marketing, which presents a challenge to the transactional view of marketing that has been dominant for so long. The Nordic school's approach has application in both B2B and B2C environments. Grönroos has defined relationship marketing as follows:

> Relationship marketing is the process of identifying and establishing, maintaining, enhancing, and, when necessary, terminating relationships with customers and other stakeholders, at a profit, so that the objectives of all parties involved are met, where this is done by a mutual giving and fulfilment of promises.[48]

Gümmesson goes further, redefining marketing as follows:

> Marketing can be defined as 'interactions, relationships, and networks'. [49]

The Nordic school identifies three major characteristics of commercial relationships – interaction, dialogue and value – known collectively as the 'Triplet of Relationship Marketing'.[50]

Interaction

The Nordic school suggests that inter-firm exchanges occur in a broader context of ongoing interactions. This is a significant departure from traditional notions of marketing where interfirm exchanges are conceptualized as discrete, unrelated events, almost as if there is no history. From the Nordic school's perspective, interactions are service-dominant. As customers and suppliers interact, each performs services for the other. Customers supply information; suppliers supply solutions.

Dialogue

Suppliers and customers are in dialogue with each other. Indeed, communication between partners is essential to the functioning of the relationship. Traditional marketing thinking has imagined communication to be one way, from company to customer, but the Nordic school emphasizes the fact that communication is bilateral.

Value

The concepts of 'value', 'value creation' and 'value creation systems' have become more important to managers over the past twenty years. The Nordic school stresses the mutual nature of value. To generate value from

customers, companies need to generate customer-perceived value, that is, create and deliver something that is perceived to be of value to customers. Value creation therefore requires contributions from both buyer and seller. From the Nordic school's perspective, service performance is a key contributor to customer-perceived value.

The Anglo–Australian school

The Anglo–Australian school takes the view that companies not only form relationships with customers, but also with a wide range of other stakeholders including employees, shareholders, suppliers, buyers and governments. The main proponents of this school are Martin Christopher, Adrian Payne, Helen Peck and David Ballantyne.[51]

Stakeholder relationships vary in intensity according to the level of relationship investment, commitment and longevity. Unlike the IMP school which takes a descriptive approach, the Anglo–Australian school takes a more prescriptive approach. Their work sets out to help managers to improve relationships with stakeholder groups.

The major conceptual contribution of this school is their Six-Markets Model which has been revised several times (see Figure 2.11). The model suggests that firms must satisfy six major stakeholder 'markets': internal markets (employees), supplier/alliance markets (including major suppliers, joint venture partners and the like), recruitment markets (labour markets), referral markets (word-of-mouth advocates and cross-referral networks) influence markets (these include governments, regulators, shareholders and the business press) and customer markets (both intermediaries and end-users).

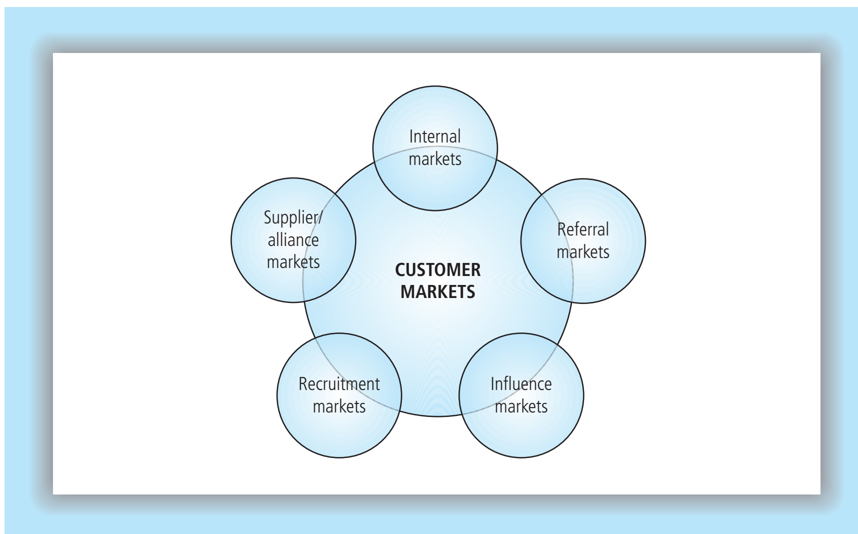


Figure 2.11
The six-markets model[52]

The school's researchers have focused on a number of topics: customer retention, customer loyalty, customer satisfaction, customer relationship economics and value creation. One of their major findings is that

customer satisfaction and customer retention are drivers of shareholder value.[53]

The North American school

The North American school receives less emphasis as a separate school of relationship management than other schools. Significant contributors to this school are Jeffery Dyer, Sandy Jap, Shelby Hunt, Robert Dwyer, Jan Heide, Robert Morgan, and Jagdish Sheth. A major theme flowing through this school's work is the connection between successful inter-firm relationships and excellent business performance. The school acknowledges that relationships reduce transaction costs,[54] and that trust and commitment are two very important attributes of successful relationships. Indeed, one of the more important theoretical contributions to come from the North American school is Morgan and Hunt's 'Commitment-Trust Theory of Relationship Marketing'. This was the first time that trust was explicitly linked to commitment in the context of customer–supplier relationships. According to the theory, trust is underpinned by shared values, communication, non-opportunistic behaviour, low functional conflict and cooperation. Commitment, on the other hand, is associated not only with high relationship termination costs, but also with high relationship benefits.[55]

The North American school tends to view relationships as tools that a well-run company can manipulate for competitive advantage. They also focus on dyadic relationships rather than networks, most commonly buyer–supplier dyads or strategic alliance/joint venture partnerships.

The Asian (Guanxi) school

Guanxi is, essentially, a philosophy for conducting business and other interpersonal relationships in the Chinese, and broader Asian, context. Therefore, its effects have a significant impact on how Asian societies and economies work.

The notion of Guanxi has been known to western economists since at least 1978. This was the time when the Chinese market began to open up to the west.[56] The foundations of Guanxi are Buddhist and Confucian teachings regarding the conduct of interpersonal interactions. Guanxi refers to the informal social bonds and reciprocal obligations between various actors that result from some common social context, for example families, friendships and clan memberships. These are special types of relationships which impose reciprocal obligations to obtain resources through continual cooperation and exchange of favours.[57]

Guanxi has become a necessary aspect of Chinese and, indeed, Asian business due to the lack of codified, enforceable contracts such as those found in western markets. Guanxi determines who can conduct business with whom and under what circumstances. Business is conducted within networks, and rules based on status are invoked. Network members can only extend invitations to others to become part of their network if the invitee is a peer or a subordinate.

Summary

In this chapter you have learned that there are differing beliefs about what counts as a relationship. Although interactions over time are an essential feature of relationships, some believe that a relationship needs to have some emotional content. Although the character of a relationship can change over time, successful relationships are based on a foundation of trust and commitment. The primary motivation for companies trying to develop long-term relationships with customers is the profit motive. There is strong evidence that long-term relationships with customers yield commercial benefits as companies strive to enhance customer lifetime value. The satisfaction–profit chain suggests that customers who are satisfied are more likely to become loyal, and high levels of customer loyalty are associated with excellent business performance. However, companies are advised to focus their customer acquisition and retention efforts on those who have profit-potential or are otherwise strategically significant. Although companies generally want to develop long-term relationships with customers, there are good reasons why customers don't always share the same enthusiasm. Finally, the chapter closes with a discussion of several schools of management or marketing theory that shed light on customer relationship management. These are the IMP, Nordic, Anglo–Australian, North American and Asian (Guanxi) schools of thought.

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