

The role of knowledge management in customer retention – how smart companies use it to create value

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Abstract. The relationship between Knowledge Management and Customer Resource Management is discussed with a focus around the knowledge utilization in the area of customer satisfaction and retention. The theoretical background from literature research is enriched by numerous examples from daily operations as well as strategic policy implications in diverse multinationals. The article discusses two non-traditional but still widely used customer satisfaction survey techniques, the Net Promoter Score and the Advocacy Index. The advocacy impact on corporation's growth, the knowledge base as well as key advocacy tools are presented to demonstrate value creation opportunities that origin in the utilisation process of knowledge from the customers in particular.

1. Introduction

Companies in today highly competitive global market collect a lot of data. Big share of them is related to their customers. Raw data from various sources need to be however converted into the meaningful conclusions and consequently followed up by actions in order to make a proper use of them. The understandings of product or service advocates on customer's side play a significant role in helping companies drive sales. There are various tools how to track the voice of customer and capitalize on it. In spite of the fact the Net Promoter Score (NPS) as the customer satisfaction survey method has been debated by scientists it is still being widely used in corporate practice around the globe. As a result of successful customer related knowledge management diverse opportunities identified in the voice of customer can be captured and monetized.

Demanding customers continuously increase their expectations. Next to the competitive price, value for money and quality, the top service is gaining increasing importance, both in goods as well as service industry. The latest research in customer satisfaction shows that the average customer with a problem tells nine other people. It is generally recognized that satisfied customers share about their positive service experience with five other people. Only 4% of the dissatisfied will however complain. On the other hand, with the newest communication technologies readily available a dissatisfied customer via the 'world of mouth' in a single online post does not only influence another individual's (non purchase) behavior, but can have a far reaching consequence for the company across the globe, in real time.

Understanding customers and tracking their satisfaction has become critical to success. This holds true also from the financial point of view as the customer retention rate is closely linked with company's profitability. It is estimated that it is five to eight times more expensive to win new customers than to retain the existing ones. Measuring customer satisfaction is still relatively new to many companies. Many of them keep focusing mostly on the balance sheets and income statements. Increasing competition on the crowded markets with little space left for product differentiation indicates however that companies must change their focus. There are two pieces of old wisdom that are very relevant and still hold true here even in the 21st high tech century:

1. Customer is the king.
2. You can't improve what you don't measure.

2. Customer related data

Companies collect diverse information concerning customers. Desirably the knowledge deployment should be internally cross functional, supported by various flows within organization's departments as well as business units. According to researchers knowledge can be basically divided into 3 categories:

- from the customer – knowledge residing in the customers,
- about the customer – customer's preferences and characteristics
- for the customer.

The research carried out by Gibbert et al. (2002) concluded that majority of companies consider themselves as market-driven and customer-oriented. Only few however actually manage well the knowledge residing in their customers, they rather focus around the knowledge about them. The findings of this research indicate that corporations utilizing knowledge **from their customers** are more able to sense and also utilize market opportunities before their competitors; they are able to create value more rapidly.

Several recent cases indicate that the cutting edge companies shift customer's position from being the passive recipient of goods and services to the knowledge partner actually. The sale statement 'if only did we knew what we know' has been converted into the claim 'if only we knew what our customers know'. The multidisciplinary research of Gibbert's team carried out during 6 years illustrated the interlink of KM with the area of CRM, evolving it into a next level, so called Customer Knowledge Management (CKM). According to the authors in the CKM customers are actually 'freed' from various loyalty schemes or reward programs, the knowledge residing in them gains momentum. Gibbert perceives traditional KM more about efficiency gains, a strive to reduce 'the wheel reinventing', while the CRM is for them more about innovation and growth. Customers then as partners are considered to be the co-creators of value for organizations.

3. Knowledge from the customer

Let's have a look at how a successful multinational online retailer has built on customers' interaction. Amazon.com started selling books in 1994. The company built a platform of readers enthusiasts. Up to date customers are motivated to share their knowledge, the keen ones willingly post their reviews (intrinsic motivation). Next to books the updated information on movies, music, games and many other goods is daily populated and shared online. Amazon enables customers to access their own purchase history; the orders of others are visible too. Similar customers' views are shared, suggestions, tips and tricks added. Customized non-intimidated suggestions based on the past interaction preferences stimulate next possible purchase and help to drive sales further. In addition, the knowledge about customers' preferences can be shared with authors, providing them with hints for new books, as well as supplying the market potential information to them.

From the theory point of view, the KM and CRM are focusing more on the knowledge about customers while the management of customer knowledge is focused more on knowledge directly from the customer. Internet companies in their online interactions actually gain competitive advantage. It is quite a costly exercise to build a CKM tool, but it does not mean that the brick-and-mortar companies do not use it, on the contrary, opposite is true. For example, international furniture retailer IKEA positions customers in a role of a co-creator. Customers are not just the passive recipients but a part of the process allowing for creativity. Giving those new competences and benefits stimulate mutual value-creating ideas and co-production. NIKE, for example, similarly changes the passive recipient into an active contributor in their NIKEiD studios. The customers, either online or in the selected NIKEiD shops can design, customize and make own shoes, cloth or accessories for males, ladies or kids.

When it comes to an online active interaction, in IT or game industry for example, a specific customer group, the testers are heavily involved. Thousands of devoted game or software beta-versions testers possess vast expert knowledge. These like-minded users are not only utilizing the 'free' product, they willingly exchange professional user's thoughts, regularly share posts as well as regularly report back to the company. Not only they provide the product related feedback, they also receive one back, the company regularly shares information with them, via the product news groups or chat rooms. This seems to be having a positive impact on users' loyalty and partially even also on the sense of ownership.

Another interesting example of company utilizing customers' knowledge sharing among their clients are Weight Watchers. Those eager to lose weight meet in regular (carefully managed) sessions. Experience and knowledge sharing during those sessions in the group has a positive effect on endurance stimulation as well as slimming motivation.

4. Customer satisfaction in the subscription model

Recently the literature dealing with contractual customers' relationship uses a term customer churn. Looking at the etymology the English word churn refers to "agitate or produce violent action". The churn is sometimes also referred to as the retention rate. In principle retention rate quantifies the number of retained, so considered satisfied customers. The retention rate is often applied in business relating to the contractual customer base, referring to those who retained when their contract expires. Subscription based service model is widely used for example by mobile phones providers or TV operators.

According to the Accenture's global study on Customer Retention (2010), the most service sensitive clients are in retail. Due to the poor customer service 40% of them switched to another provider. Emerging markets compared with the mature markets showed significantly more sensitive to the poor customer service. Next to the retail, banks and telecom providers (internet, phone, TV and satellite) suffered from lowest customer loyalty when it came to low quality customer service. On average their almost every 5th customer in case unhappy signed up with competition within a year.

There are several companies that have quantified and shared these implications in figures in terms of savings, sales and profitability. Based on Accenture's Study on Profitability Growth (2010) the customer loyalty represented 38% of margin, 40% of revenue growth and it stood for 38% of shareholder value. According to the Bain & Co a

1% increase in customer loyalty is equivalent to a 10% cost reduction. Marketing Metrics published outcomes related to sales quantifying the probability of sale to a new prospect being 5-20% contrasting it with the probability of sale to existing customers, reaching 60-70% [9].

5. The Net Promoter Score

Customer's satisfaction in order to be understood, correctly interpreted and the follow-up actions implemented it needs to be measured first. Corporations from various industries, including global players like DELL, EON, GE, Philips Apple or American Express currently benchmark customer satisfaction via the NPS (Net Promoter Score). The NPS is a management tool that was developed by Reichheld in the cooperation with the consulting companies Bain & Company and Satmetrix. It was introduced in 2003 in the Harvard Business Review article "One number you need to grow". The NPS has got criticized but still it is being used as an alternative to the traditional research in the area of customer satisfaction. In recent years it gained popularity mostly due to its simplicity and the claim it correlates to the profitable growth and business success.

In the NPS surveys customers are asked to respond to a single question: "How likely would you recommend our company/product/service" to your friend or a colleague. Their response is quantified on the scale 0-10. Zero stands for not at all, ten meaning extremely likely. There are 3 groups of customers accordingly: promoters, passives and detractors. The first group, **Promoters** (rating 10 and 9) are loyal enthusiasts who keep buying. They actually keep fueling growth by referring others. The second group, **Passives** (rate 8 and 7) constitute those who are not enthusiastic, so being vulnerable to the competition offerings. The third group, so called **Detractors** (rate 6 and lower, represents the unhappy ones. They are the ones who actually impede growth through their negative word-of-mouth. The NPS score is calculated by deducing the detractors from the promoters. In order to correctly interpret results the benchmarking of performance is necessary. It can take place within the same industry, product group or service. When the NPS was developed Satmetrix concluded that the companies with higher ratio Promoters to Detractors grew more rapidly compared to the competition. It seems the companies with NPS 50-80 grow most efficiently. On average companies reach the NPS of 5 to 10, meaning the Promoters number barely exceeded the number of Detractors. Many firms and even whole industries have a negative NPS, so having many more Detractors than Promoters. The low scores indicate no profitable sustainable growth. The NPS is currently developed for 175 companies across 19 industries. Relevant for global corporations, an NPS study by Tempkin group on 5000 consumers [7] concluded there are differences in results based on the age, income and ethnicity too. The authors claim there is a proven link between the NPR and future purchases. When customers were asked what would make them to recommend the company, the promoters suggested the lower price; the detractors were more likely to select customer service.

From the scientific perspective in academic circles there have been some criticism voiced around the NPS. Indeed the model is quite simple; the opponents claim there is also insufficient base for its outcome. Customer satisfaction is more complex than just numbers or percentages; the reasoning behind the consequences as well as correlation is relevant and seems to be missing in this model. There could be also a gap between what customers claim they would do (to recommend the product) and their actual action is. The model does not take this into

consideration. In addition a recommendation of one customer not necessarily needs to be equal to the value of another's one. In addition the NPS targets only the customers, while the non-customers can have also a significant message to deliver, detractors do not share the most positive publicity around when not satisfied. In addition for example a score of +40% can mean both 70% Promoters and 30% Detractors, while the same score will be reached if there are 40% Promoters and 0% Detractors, both cases end up providing the same result.

The NPS is however being implemented as a strategic tool across many organizations. The rationale behind the NPS promotion is based on the fact that the high loyalty is a significant driver of sustainable business growth. Loyal customers do stay longer (Life time value), they buy more (Cross-and-up sale). In addition they get the new customers (Word-of-mouth). The tool is practically cost efficient and simple, correlating with business success. The companies like Dell, Harley Davidson, Amazon and Zappos for example reach the NPS ratings of 50% up to 80%, suggesting even in those fast growth engines there is room for improvement. Cross industry samples are presented in Table 1.

Sector	Brand	NPS®
Home/Contents Insurance	USAA	80
Hotels	Marriott	62
Internet Service	Brighthouse Networks	29
Laptop Computers	Apple	76
Life Insurance	State Farm	44
Online Entertainment	Netflix Online	50
Online Shopping	Amazon.com	69
Smartphones	Apple iPhone	70
Software & Apps	TurboTax	54
Tablet Computers	Apple iPad	65
Travel Websites	TripAdvisor	36

Tab. 1 Selected NPS scores, Source: Satmetrix (2013)

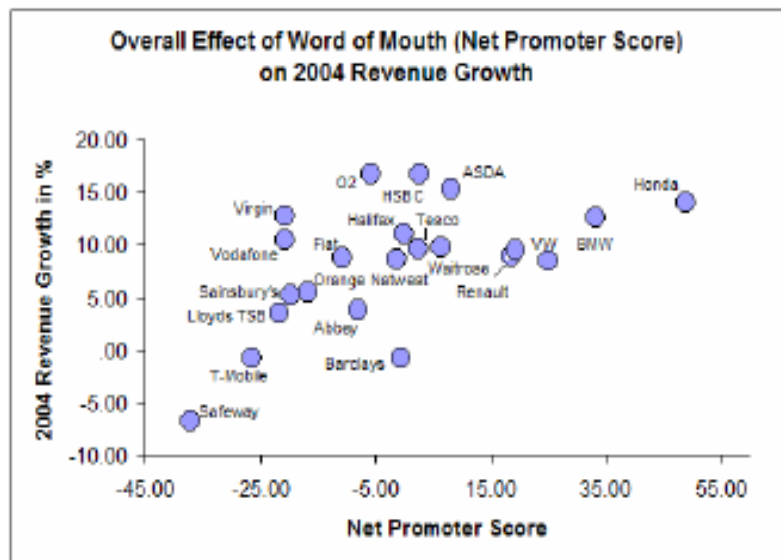
6. Advocacy Index

Based on the fact customer satisfaction interviews often take place over the phone next to the NPS a so called Advocacy Index was developed as a specific survey technique. Marsden et al. (2005) from the London School of Economics questioned a random sample of 1256 adult consumers in UK. The respondents were asked 3 questions. First was how likely they were to recommend their current mobile phone provider, supermarket, car maker (if they

owned one) and the bank to their friend or a colleague. Secondly they were asked if they indeed made such recommendation in the past year, and on the contrary, if they did spread any negative comments. As a control question, a third one was added, how satisfied the respondents were with those brands they owned.

The research actually showed that the two metrics, the NPS and the Advocacy Index, were statistically significant in the business growth predictions. The word of mouth was measured by the NPS score (Pearson's coefficients of correlation of $r=.484$, significance of $p<.01$) and the negative word of mouth ($r=.524$, $p<.01$). Companies like HSBS, Asda, Honda and O2 grew faster enjoying the higher level of word-of-mouth-advocacy. Those with low net promoter scores, like Safeway, T-Mobile or Fiat, underperformed in terms of growth.

Marsden's team extended the NPS to a predictor of sales, the predictor of share performance (likelihood for investors recommending to invest in a certain company), as well as predictor of productivity (likelihood that employees would recommend working for a company). The authors referred to the financial value of the word of mouth as 'the economics of the buzz'. Their research quantified for example that a reduction of 2% in the negative word of mouth boosted sales by 1%. For the average in studied corporations a 1% increase in the word of mouth advocacy drove £8.82m additional sale [4].



Tab. 2 Customer Advocacy Drives Business Growth, Source: Marsden (2005)

7. Customer Advocacy Tools

The overall conclusions of key findings of more than 20 books on advocacy suggested by Marsden imply that the businesses that grow are the ones that build customer advocacy. In the literature 8 distinct tools have been identified that have demonstrated to be effective. All of them point to the large corporations and proved to have significant measurable outcomes. The power of these measures can be demonstrated in several below mentioned cases.

Referral programs, or reward programs for a referral: in the US the ‘Friends and Family’ referral scheme for the MCI phone operator provided in less than 2 years 10 million new subscribers. The Dove soap producer Unilever with their “Share-a-Secret” referral program gained 10% market share increase. The scheme involved existing Dove users to order a free gift soap pack with vouchers for a friend, while the ‘referee’ got rewarded with a free pack. From the psychological point of view it was a powerful message, both the ‘referee’ and the referred one were rewarded. This gave the ‘referee’ an excuse, ordering soap for a friend was actually not just doing it for self-interest.

The so called **Tryvertsing** is a relatively new marketing term (from ‘try’, ‘advert’ and ‘marketing’). Company provides free samples of a new product or service – not to anyone, but the selected basis of users. The idea behind is to remove the price barrier of the trial and via the exclusivity and scarcity of the ‘privilege’ to grow advocates who showcase the product to others. For example the beta testing of some software versions when the yet-to-be-launched product via the sneak preview turns the lead customers into advocates. In FMCG industry for example, a small bottles of perfume samples to the selected limited ‘group of friends’ the teen trend setters shortly before the product launch made can have a huge impact. The new BCBG’s girl perfume with ‘special samples’ distributed some days shortly before the launch increased the advocacy significant. The perfume in the week of its launch became the bestseller. The ‘tryvertsing is also often being used in fashion brands, during the campaign invitations are sent to participate in exclusive trials, new products are showcased to others.

As a sample of advocacy by the **empowered involvement**, the Procter and Gamble in US used their online tool in the Crest toothpaste project. The company let their consumers vote on flavor selection for the toothpaste’s new range. Web polls over the SMS for example create empowered involvement that is scalable, fast and cost effective solution to stimulate growth by advocacy. The American Idol/Big Brother audience participation empowered voters to bring competing participants off the show creating ‘I did that’ or a so called the Hawthorn Effect. This effect was identified by Harward’s researchers already in 1930s, market research participants were turned into advocates by having a say in how the product, initiative or a service is rolled out. The Tremor, an online US-wide empowerment panel working with well established brands like Sony, AOL and Toyota estimated that the sales generated by the empowered initiatives could bring additional 10-30% revenue [2].

Being exposed to TV ads all of us witness for example the **Brand ambassador programs**. They are widely used by companies like L’Oreal, Siemens, or Unilever. Highly valued satisfied customers selected as brand ambassadors represent valuable advocates with a powerful impact on others. Under the **Causal Campaigns** for example by sponsoring a good cause customers are mobilized and volunteer sales force is created. In US the American Express pledged to donate a penny to the restoration of the Statue of Liberty for each of the transaction their customers would make. As a consequence the use of Amex card increased by 28%, the number of new users rose by 17%.

Systematic tracking of (also and specifically negative) advocacy for example in forums, review sites or blogs can help companies also in innovation or product enhancement. Apple, in the initial buzz around its iPod music player spotted negative user experience of its battery. It was actually too costly and difficult to replace it. Unhappy users shared a video clip “iPod’s Dirty Secret’ that got viral and got viewed 1.4 million times. Listening to the

negative buzz and taking immediate action, removing product weakness by innovation, helped Apple to prevent major PR catastrophe.

8. Conclusion

As demonstrated in multiple industries the traditional sales claim “if only we knew what we know” has been turning into the claim “if we only knew what our customers know.” Companies across the globe can create additional opportunities by active listening to the voice of their customers. Monitoring advocacy levels support them in identifying the short comes as well as business opportunities. The knowledge gained however needs to be turned into relevant actions. The conclusions may have impact on the strategic programs as well as daily operations. Understanding customers, their wants and needs, aims as well as dreams can contribute to the mutual value creation and improved performance. The customer knowledge management shall therefore be a continuous process, customers perceived as valuable knowledge partners. All provided evidence suggests that the CKM utilizing KM and CRM principles can actually be perceived as one of very powerful tools in company’s differentiation on the global market.

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