How to Measure Customer Loyalty
By Dan Richards
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Perhaps more than in any industry, advisors know the importance of customer loyalty and the role it plays in client retention and referral generation. But few advisors have ever tried to systematically measure the client loyalty in their practice.

Here’s a way to do that.

Recently, I attended a talk by Fred Reichheld, a long time partner with consulting firm Bain & Company (the same firm that Mitt Romney worked for after graduating from Harvard Business School).

Reichheld is one of the pioneers in the area of promoting customer satisfaction and loyalty as a core strategy to drive business growth. In 1996, he published The Loyalty Effect, one of the first attempts to rigorously quantify the financial payoff from satisfied customers.

In 2003, he published an article in the Harvard Business Review, titled “One number you need to grow.” He introduced a simple 12-word question and a resulting measure called the “net promoter score” that correlates with customer loyalty and can focus organizations on creating higher levels of customer satisfaction.

12 words to measure loyalty

The net promoter score (NPS) starts with one simple 12-word question that customers are asked to answer on a scale from zero to 10. That question:

How likely are you to recommend us to a friend or colleague?

Customers are then put into three categories:

- **Promoters** (score 9-10) are loyal enthusiasts who will keep buying and refer others, fueling growth.

- **Passives** (score 7-8) are satisfied but unenthusiastic customers who are vulnerable to competitive offerings.
• **Detractors** (score 0-6) are unhappy customers who can damage your brand and impede growth through negative word-of-mouth.

The NPS is the percentage of promoters less detractors – what’s left are your net promoters. So if you have 30% of clients scoring you a 9-10 (your promoters), 50% a 7-8 (your passives) and 20% a 0-6 (your detractors), your NPS is 10.

In the US, recordings of NPS north of 70% have been attained by USAA in banking, Costco and Apple. Other firms using the NPS metric to track satisfaction include Charles Schwab, Amazon, Intuit (maker of Quicken), General Electric and Procter and Gamble.

In a presentation at a conference, a senior executive of TD Bank explained how they used the NPS to shift from satisfaction-focus to loyalty-focus. With high satisfaction scores, it was hard to identify issues and motivate employees to improve. By moving to a net promoter-approach using willingness to recommend as the metric, they uncovered new issues and identified the best practices of top-performing branches. TD is now rolling out the NPS methodology throughout the bank to include all functions that impact customer service.

**The research behind the net promoter score**

Below is an excerpt from the net promoter score website that provides its rationale:

To determine a useful metric for gauging customer loyalty, Fred Reichheld did something rarely undertaken with traditional customer surveys: match survey responses from individual customers to their actual behavior — repeat purchase and referral patterns — over time.

Working with Dr. Laura Brooks of Satmetrix, a research team tested numerous different questions to see which one(s) would be the best gauge of future repurchase and referral behavior. The test was administered to thousands of customers recruited from public lists in six industries: financial services, cable and telephony, personal computers, e-commerce, auto insurance, and Internet service providers. The team obtained a purchase history for each person and asked them to name specific instances in which they had referred someone else to the company in question.

The results allowed the team to determine which loyalty questions had the strongest statistical correlation with repeat purchases and referrals. The team hoped they would find at least one question for each industry. They found something more: One question was best for most industries. "How likely is it that you would recommend [Company X] to a friend or colleague?"

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Next, the team looked at relative growth rates for competitors in a given industry. In the first quarter of 2001, Satmetrix began tracking the "would recommend" scores of a new universe of customers, many thousands of them from more than 400 companies in more than a dozen industries. In each subsequent quarter, they then gathered 10,000 to 15,000 responses to a very brief e-mail survey that asked respondents (drawn again from public sources) to rate one or two companies with which they were familiar.

Where the team could obtain comparable and reliable revenue-growth data for a range of competitors, and where there were sufficient consumer responses, the team plotted each firm's NPS against the company's revenue growth rate.

The results were striking. In most industries, this one simple statistic explained much of the variation in relative growth rates; that is, companies with a better ratio of Promoters to Detractors tend to grow more rapidly than competitors.

Implementing this in your business

In the question and answer period after his talk, Reichheld was asked about categories like investing or airlines where there are extraneous events (market downturns and snowstorms) that depress satisfaction in the short term. In those cases, should companies look at NPS scores relative to their industry to gauge how they’re doing, rather than absolute benchmarks?

His answer was that this is eminently reasonable in the short term. He went on to say, however, that industries that chronically have low satisfaction scores can be vulnerable to new entrants. Even if your customers are more satisfied than your competition’s customers (or as the old expression goes “in the land of the blind, the one-eyed man is king”), this creates an opportunity for dramatically new business models to shift the competitive landscape. If you look at the collapse of traditional business models (like the legacy airlines and the Big Three US auto manufacturers), dissatisfaction was masked by the lack of alternatives – right until better alternatives presented themselves.

Make it easy for customers to answer the NPS question honestly, Reichheld said. Because people are polite and don’t want to hurt your feelings, asking them directly will reveal scores that are higher than their real satisfaction levels. That’s why successful companies collect their NPS readings either through written or online surveys that administered by third parties; Charles Schwab’s branch managers follow up with customers to get their scores, talk about their experience and determine how the advisors serving them can improve.

Follow up with customers is key. Reichheld said that asking customers for their opinion initially creates a boost in attitudes – after all, the person they’re doing business with is
showing they care. If there is no follow up or indication that their opinion is being taken seriously, however, that initial boost quickly evaporates.

One final note: If you are going to follow up with clients to talk about their rating on the “How likely would you be to recommend us” question, make it clear that your motivation is to find ways to better serve them, rather than to get referrals to friends and family. You need to explicitly clarify this to engage clients in an honest and frank conversation.

Dan Richards is a top-rated presenter at advisor conferences and an award winning instructor in the MBA program at the University of Toronto, as well as author of Getting Clients Keeping Clients: The Essential Guide for Tomorrow’s Financial Advisor. To learn more about his conference keynotes and workshops, email dan@clientinsights.ca.

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