Customer equity: dimensions and realisation process

Karin P.N. Abele

A thesis submitted in the partial fulfilment of the requirements of
De Montfort University for the degree of Doctor of Philosophy.

October 2008

De Montfort University

Leicester Business School

Abstract

A number of researcher and practitioners have identified a dramatic increase in competition and market transparency as the driving force behind the decline in customer loyalty in the financial services sector (e.g. Caruana, 2002). However, the costs for selling a product to a new customer are much higher than the costs for selling the same product to an existing customer, particularly when the customer is loyal to the company (Duffy, 2003). Due to these facts, strengthening customer relationships is necessary to achieve higher customer equity. Blodgett (2000) claims that the successful implementation of a customer equity strategy involves an organisation's customer focus, operations, systems, and culture.

Companies can offer value to customers through their services and products (added value and innovations), their personnel (service quality), and their processes (speed and quality). When the customer buys financial products and services, he creates customer equity for the company, which is in this thesis presented as company profit. Company profit is the sum of all customer profits and represents the value of each customer in the form of monetary aspects. This thesis aims at investigating if communication, price, process, product and human resource management influence company profit (customer equity) and, thus, whether they are drivers of customer equity (Chapters 5-10). In total, seven dimensions have been investigated.

Recent customer equity models of value-based management are examined from the literature and based upon this, the construction of a new conceptual model for value building in competitive markets is proposed (Chapter 4). The framework identifies value propositions such as brand or product leadership, value sources for determining value creation strategies, and finally customer touch points for value delivery. Touch points are referred to as advertising, use of a logo, presence of sales persons, websites, branch outlets etc i.e. the human and physical interactions with customers over their relationship with an organisation. Together with products such touch points are designed to deliver value to customers with the objective of increasing customer equity.

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Acknowledgements

This thesis was written while I was enrolled as a PhD student at Leicester Business School, De Montfort University. Several individuals and institutions have contributed to the making of this thesis, and I would like to take this opportunity to thank them.

First of all, I would like to thank the school for providing a good and stimulating research environment. Additionally, the school's financial support, which allowed me to attend various courses and conferences, is greatly appreciated.

Second, many thanks to my first supervisor, Professor Wright, for giving me enough freedom in carrying out my research and for welcoming my initiatives. I would also like to thank my second supervisor, Michael Starkey, for his support and guidance, particularly, for his helpful contacts in the financial services sector. A special thanks to Emeritus Professor Peter Baron for his contributions to the statistical part of my thesis.

Finally, I want to express my gratitude to my family and my friends, above all my parents. During my PhD's ups and downs, I always had a special source of enjoyment and support. My friends always ensured that I could see the light at the end of the tunnel.

Karin Abele
Leicester, October 2008

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1   Chapter 1: Introduction

1.1   Introduction

The research in this thesis extends customer equity research by embracing an empirical approach and strives to examine strategic dimensions from the point of view of a company, henceforth called the company perspective. The research aims to identify what factors make up customer equity and to empirically investigate the relationship between these factors and customer equity in the financial services sector. It is important to know which factors an organisation needs to focus on for increasing the lifetime value of each customer in a way that maximises customer equity and to validate these in the changing marketplace. Such a value-based company perspective will constitute a key element for creating long-term relationships with customers and ensuring company success.

The thesis begins with the conceptualisation of the process of realising customer equity in an organisational environment by describing key aspects of how customer management can be done in today's competitive economy. Marketers are struggling to identify more effective ways to develop and implement strategies that can lead to sustainable profit streams. Therefore, comprehensive approaches, such as the process of realising and managing customer equity, become essential to the success of value-based strategies.

Both the conceptualisation process and the research contribute to the customer management literature that is concerned with the study of the sources of customer equity (e.g. Forbes, 2007; Hansotia, 2004; Kothandaraman and Wilson, 2001) and the mechanisms through which it comes about. Existing literature of customer equity could be described as either a measurement literature focusing on the calculation of customer equity (see, for example, Rogers and Peppers, 2005; Zeithaml et al, 2001; van Raaij, 2005) or a prescriptive literature that views customer equity from a strategic perspective (e.g. Christopher, 1996; Payne et al., 2000; Payne and Frow, 2005). This thesis contributes to both kinds of literature streams.

The concept of customer equity views customers as a company's most important asset, since customers generate revenues and an organisation's investments aim at increasing those revenues. "Managing customer equity therefore means determining which customer investments a company should make and how it should make them" (see Hansotia, 2004). Most researchers define customer equity as the total of the discounted lifetime values summed over all of the firm's customers (e.g. Blattberg and Deighton, 1996; Rust et al, 2000; Bayón et al, 2002). This work agrees to this definition. However, the discounted customer lifetime values are usually based either on single-period customer profitability or on forecasts of customer lifetime value (CLTV) (see Ryals and Knox, 2005). Both customer lifetime value and customer profitability are used interchangeably in this thesis (see also Mulhern, 1999).

On the one hand, organisations profit from customer equity in the form of increased customer satisfaction, service loyalty, up-selling, and cross-selling (e.g. Macintosh and Lockshin, 1998). Hence, the profits obtained from customers over their lifetime with the organization augment and improve the financial performance. Besides this monetary-based benefit, customer equity also leads to non-monetary benefits, such as improved corporate image, greater differentiation from competition, or increased customisation. Overall, one can imply that customer equity aims at creating customer satisfaction and maintaining an ongoing, long-term relationship with customers and by doing so building competitive advantage.

Customer equity is by definition customer-centric and is often explained with a logic wherein employees, products, technology, and processes contribute to the creation of value for customers. Value creation also requires a combination of customer-focused service and marketing strategies, the right product, and high-performance organizational practices. To become differentiated from the competitors by providing more value, it is essential to a company to know which value sources it needs to focus on. Hence, it's all about creating value for the customer.

The concept of customer equity, which is closely related to customer lifetime value (CLV), is central to make better business decisions across the organisation. "A customer equity construct allocates customer profits through the analysis of customer revenues offset by true cost to serve" (Stevens, 2006). This means that customer equity estimates need to be made at the customer level, or at least at the customer segment level. Therefore, customer equity constructs comprise the processes, tools, and techniques that support the growth of customer equity. In other words, customer equity constructs aim at measuring, managing, and exploiting value sources for maximising customer equity and guiding business strategies.

1.2   Practical relevance

These studies have noted that practitioners around the globe have started observing keenly the state of customer equity research. This interest is based on various reasons. On the one hand, the economy has undergone a shift from product-centered to customer-centered businesses in which customer equity is becoming important to measure customer profitability and to identify the underlying factors that drive customer profitability. On the other hand, there is a dramatic increase in competition resulting from worldwide mergers and acquisitions, cost and time pressure, and higher market transparency. This increased competition requires that organisations adapt their resources and strategies to customer profitability, i.e. the higher the profitability, the better the service.

Based on the above, one can conclude that there are two major reasons for the interest of practitioners in customer equity: *customer-centered business and increased competition.* These two reasons justify the research on customer equity and, therefore, are considered in the following.

Customer equity represents a performance measure that reflects customer's answer to corporate strategies. These strategies contain any kind of changes, such as product innovations, new sales channels, price reductions, advertising campaigns, new services etc. The more value these strategies deliver to

customers, the higher the levels of customer satisfaction, customer loyalty and retention leading to greater business success and higher customer equity (e.g. Ulaga and Chacour, 2001). Hence, customer equity assists management in making the right strategic decisions and monitoring their impact on customer's purchase behaviour. There is no doubt that customer equity is an adequate measure for considering the important role of the customer in a customer-centred business.

Customer equity represents a snapshot of the financial performance of a customer at a particular moment. This means that it considers the continuously changing customer's purchase behaviour and purchase volume when it is regularly calculated. For a customer-focused organisation, it is essential to take into account these changes for surviving and excelling in the global marketplace. Hence, customer equity is best suited to a customer-centred business.

The growing economic importance of customer equity in customer-focused organisations has been investigated by research on customer relationship management and global investment management. A study showed that the investments in customer relationship management systems will double from 2% to 4% of revenue over the next three years (Jeffreys, 2006). This confirms the increasing role of customer equity in organisations. Organisations use customer relationship management systems to calculate the customer lifetime value of each customer and to sum it up for determining customer equity.

A further study carried out by a well-known consulting concluded that most companies (66%) achieve profit growth through retention and cross-selling strategies (52%) combined with the introduction of new products and services (32%) (Schuler et al, 2005). This confirms that customer equity, which is the sum of a firm's customer lifetime values, is increased through augmenting the number of purchases customers make. Finally, a further study found that 46% of the companies attempt to increase retention of profitable customers and 44% of the companies aim at acquiring new, more profitable customers (Clay and Meyer, 2004). Hence, one can conclude that customer profitability (customer

equity) is becoming an important element for improving the financial success of a company.

Only when the value delivery to customers is higher than that of competition, an organisation can increase customer equity (e.g. profit per customer or turnover per customer), as the customers are more willing to buy their products and services. This is extremely important in a highly competitive environment in which customers more frequently compare competitive market offerings. Additionally, customer relationships have become weaker in nature (Lang and Colgate, 2003) and consumers are more critical of their relationship with an organisation and more willing to do business with numerous suppliers (O'Loughlin et al, 2004). Customer equity considers the competitive situation of an organisation by calculating the financial performance of new, "old", and lost customers. Hence, customer equity reflects the degree of value delivery to customers from a monetary perspective.

To be able to increase value delivery to customers, organisations need to know which factors influence customer equity. In general, such factors must be viewed from a comprehensive corporate perspective to make it possible to maximise the value output to customers. In the literature, besides product attributes, value sources, such as staff, business processes, or servicelandscape have an impact on customer equity (e.g. Payne and Holt, 1998; Forbes, 2007; Hansotia, 2004; McNaughton et al, 2002; Kothandaraman and Wilson, 2001). Hence, customer equity is a good measure for identifying the value sources, which mostly influence customers' financial performance. This information can also be used for developing a consistent competitive advantage.

1.3 Theoretical relevance

Most research is focused on either the determination of customer equity (e.g. Rogers and Peppers, 2005; Zeithaml et al, 2001; van Raaij, 2005; Küng et al, 2002 ; Dorrington and Goodwin, 2002) or the identification of factors influencing customer equity (e.g. Kothandaraman and Wilson, 2001; Payne and Holt, 1998;

Christopher, 1996; Srivastava et al, 2001; Hogan et al, 2002; Sanchez and Sanchez, 2005; Forbes, 2007). Such factors include human resource, finance, distribution, sales, marketing, or core production. However, these approaches are of a conceptual nature with little research being done to explore and empirically examine the relationship between these value sources and customer equity. Therefore, this thesis aims at defining this relationship by means of company assessment of customer equity. The key determinants for this from a resource-based view are also included.

There are limitations in the literature as few models explain the process of realisation of customer equity (see, for example, Rust et al, 2000; Doyle, 2004; De Bonis et al, 2003). These models lack either market orientation for benchmarking or a monitoring process for determining the impact of value strategies on customer performance measures and company performance measures. Furthermore, some models are limited to the marketing perspective, i.e. they do not investigate the management perspective for creating value, but focus on relationship management activities. Thus, little effort has been made to integrate these criteria into one model and provide managers with information required for both short- and long-run positioning of a customer-focused organisation. Only when practitioners have a definite knowledge on how customer equity can be realized and applied in an organisational environment, they are able to transfer a customer equity approach from theory into practice.

Although many studies have locked at business performance, most limit their focus to the overall performance (e.g. Parasuraman, 2002; Duncan and Elliott, 2004), market performance (e.g. Han et al, 1998) or new product performance (e.g. Akamavi, 2005). Hence, empirically investigating business performance from the point of view of the customer performance is needed in the marketing area. Customer equity is an appropriate means for measuring how a company performs with its customers which would contribute to the overall financial performance of an organisation.

1.4 Research questions and objectives

In summary, the growing interest in customer equity on the part of service organisations led to the following research questions:

- What is understood about customer equity from the literature?

- How is customer equity measured from analysis of the literature?

- Which practical company perspective requirements exist in connection with customer equity?

- How can customer equity be strategically managed within organisations?

- Which critical factors (dimensions) influence customer equity?

- How is customer equity applied in financial services organisations?

So the research objectives of this thesis following from the above questions are:

(1) to identify the state of customer equity from the literature;

(2) to identify the critical factors (dimensions) of customer equity from an organisational view, i.e. a company perspective;

(3) to investigate the state of customer equity in the British and German financial services sector by using a quantitative survey;

(4) to evaluate the identified factors of customer equity in the British and German financial services sector from a quantitative study;

(5) to develop a customer equity process to provide an effective instrument for realizing and measuring customer equity in practice and for drawing strategic conclusions.

To summarize, this thesis makes a contribution to research by empirically investigating the applicability of critical factors (dimensions) of customer equity in the financial services sector. A further main contribution of this research is the development of a conceptual framework called the customer equity process for implementation in organisations.

The overall results of this study will be useful to managers, financial services practitioners and researchers to help gain a better understanding of the impact of marketing factors on customer equity. The findings also contribute to clarifying the implementation and effectiveness of customer equity in practice.

1.5 Research methodology

Table 1 provides an overview of the applied research methodology in this thesis.

Chapter	Research methodology applied
Chapter 1 – Introduction	
Chapter 2 – Customer equity theory and development from the literature	Desk research
Chapter 3 – Customer equity development from the company perspective	Desk research
Chapter 4 – Conceptual framework of the market-oriented customer equity process (company perspective)	Desk research
Chapter 5 – Hypotheses setting	Desk research
Chapter 6 – Qualitative data analysis	Qualitative interviews
Chapter 7 – Application of statistical procedures	
Chapter 8 – Quantitative data collection	
Chapter 9 – Quantitative data analysis	Quantitative study
Chapter 10 – Conclusions, managerial implications and future research	

Table 1: Applied research methodology by chapter

In the following sections, the applied research methodology in this thesis is outlined: desk research, survey (quantitative methods) and interviews (within the scope of qualitative interviews).

1.5.1 Desk research

Within the scope of desk research, relevant literature to the research objectives were worked up to ensure a fundamental basis for the identification of the dimensions of customer equity and for the development of the customer equity process. In this thesis, the following sources were used:

- online sources, such as Internet, databases, etc;

- offline sources, such as books, journals, etc.; and

- public statistical offices.

The desk research covered literature in the field of marketing, customer relationship management, customer equity management, project management, cost management, process management, strategic management, value management, and general management theories.

1.6 Survey (quantitative method)

In this dissertation, **a web-based and paper-based questionnaire was used** to get an overview of current management tools, management trends, and customer equity methods applied by companies. Furthermore, this standardized questionnaire was designed to test the relationships between the dimensions of customer equity and customer equity itself. A pre-testing of the questionnaire was conducted ensuring that the questions were clear, meaningful, relevant, and easy to interpret.

The questionnaire was addressed to marketing managers of financial services firms because customer equity is normally positioned in marketing. The financial services sector was chosen as more corresponding conclusions can be drawn without any dilution from the research questions. Furthermore, this sector is very interested in customer orientation as service industries in general have to focus more on customers due to high competitive pressure.

In total, seven dimension of customer equity were derived from the literature: distribution channel management, communication management, service quality management, price management, product and service management, process

management, and human resource management. Each of these seven dimensions of customer equity was presented in the form of five items or questions in the questionnaire. The respondents could evaluate the questions by using a five-point Likert scale ranging from "strongly disagree" (1) to "strongly agree" (5).

To statistically analyse the hypothesised seven dimensions of customer equity, a series of statistical procedures were used. **The procedures comprised**

- **reliability analysis** (assessing the internal consistency reliability of each dimension of customer equity),

- **content validity and face validity** (standardizing the measurement scales),

- **exploratory factor analysis** (reducing the data set to those dimensions which appear to best measure customer equity),

- **correlation analysis** (ensuring that the independent variables are not sufficiently correlated) and

- **multiple regression analysis** (dimensions of customer equity were the independent variables and customer equity the dependent variable).

As organisations measure customer equity in different ways, company profit was used to measure customer equity. This made it possible to compare customer equity among organisations. Furthermore, it is an objective measure and numerous models in the literature use it for determining customer equity. A more detailed description of the quantitative analysis is illustrated in a later chapter.

1.6.1 Interviews (within the scope of the quantitative method)

Within the scope of the quantitative method, twelve interviews with experts in the field of customer management and customer equity were conducted. The interviewees were academics and practitioners to ensure that both perspectives were taken into account. The interviews aimed at investigating whether the developed measures were valid or true. This is the case when the measure represents accurately those features of the phenomena, that it is intended to

describe, explain, or theorise. In this thesis, content validity and face validity were applied to make sure that the measures were valid. As content validity refers to reviews by experts rather than interviews with experts, the twelve interviews aimed at performing validity checks (face validity).

1.6.2 Relevance of quantitative and qualitative approaches

The quantitative approach was applied for a number of reasons as the main research study. While the qualitative method generated rich, detailed data and focused on processes and "reasons why", the quantitative method addressed correlations between variables. So a quantitative method more suited to achieving the research objective of this thesis could be supported by findings from the qualitative interviews. The main advantages of the qualitative method were the richness of data, the depth of inquiry, and the flexibility of qualitative studies (Miles and Huberman, 1994). The twelve interviews conducted within the scope of the thesis ensured that the developed measures had face validity.

Second, as the time and effort involved in qualitative research makes the examination of large numbers of organisations difficult, the generalizability of findings to entire populations is often questionable (Martin, 1990). The small sample size leads to a greater risk of obtaining a non-representative picture of the investigation's results. So the quantitative approach was used in the thesis to draw the important companies that were representative of the financial services industries. Although the sample of one hundred and twelve companies would not appear to be a large sample, it is representative of the large companies that focused on customer equity from the population of interest. Therefore, crucial generalisations regarding the population as a whole could be drawn. Quantitative methods therefore ensure generalizability of findings and are better suited to demonstrate the relationship between the dimensions of customer equity and customer equity itself. Reliability of a measure is the ability to yield consistent results (Nunnally, 1988) and can be calculated by means of statistical software, such as SPSS. This was a further reason for applying the quantitative methods in the primary research study for this thesis.

Furthermore, in quantitative research participants are selected randomly from the study population in an unbiased manner and receive a standardized questionnaire or intervention. The researcher is considered external to the actual research and results are expected to be replicable no matter who conducts the research. All these points support objectivity and therefore, the researcher preferred a quantitative study.

Moreover, the weakness of quantitative research, the fact that complex organisational realities cannot be reduced to numbers (Bentz and Shapiro, 1998), was compensated for, by the application of interviews within the scope of the qualitative approach. Twelve interviews were conducted to ensure the validity of the developed measures.

While qualitative methods are more susceptible to researcher bias and reliability problems (Snow and Thomas, 1994), the fact that the study was primarily quantitative in scope meant that the two approaches of quantitative and qualitative were integrated and were also mutually supported.

1.7 Overview of the direction of flow in the thesis structure

Chapter 2	Chapter 3	Chapter 4	Chapter 5
Understand customer equity	Develop customer equity from the company perspective	Realise value-building strategies for enhancing customer equity	Possible components of a value proposition that deliver superior value to customers and enhance customer equity (7P's)

Define customer equity

Know how to calculate customer equity

Benefit from customer equity

Know how customer equity works

Consider technology-based aspects as basis for customer equity

Consider performance management systems as basis for calculating customer equity

Step 1: customer segmentation
Step 2: data gathering
Step 3: Development of value proposition
Step 4: realisation of value proposition through strategies
Step 5: monitoring of customer and company performance

product
price
place
promotion
Physical evidence
process
people

Superior value delivery to customers

Improve loyalty and satisfaction of customers

Enhance customer equity:
-Revenues,
-Profitability, or
-Lifetime value of all customers

Chapters 6- 9   Quantitative and qualitative analysis of these seven components

Chapter 10   Conclusions, managerial implications and future research

Figure 1: Thesis structure

The direction and organisation of this thesis is as follows: The introduction in Chapter 1 contains the research questions and objectives derived from theories about customer performance in the literature and studies about companies applied to the field of customer equity. A conceptual process of realising customer equity is proposed by the researcher as a rationale for the research. Figure 1 provides an overview of the thesis structure.

Part I (Chapters 2, 3 and 4) contains the literature review and the development of the customer equity process for the company perspective.

Chapter 2 provides a theoretical overview of the customer equity literature. The research literature is classified into three categories: monetary customer equity approaches, non-monetary customer equity approaches and strategic customer

equity approaches. Subsequently, the theories and models of customer equity are investigated for developing possible drivers of customer equity.

Chapter 3 starts with a brief introduction into the field of customer performance to offer some understanding of how and why organisations apply customer performance indicators, such as customer satisfaction, customer loyalty, or customer equity. It also presents performance measurement systems frequently used by organisations to measure customer and corporate performances.

In Chapter 4, a theoretical framework of the market-oriented customer equity process is developed that enables organisations to realise, identify, determine, manage, and monitor customer equity. This process consists of five steps: segmenting customers according to their profitability (customer equity), gathering data on customers and competitors, determining the value proposition and value strategies, realising the value strategies, and monitoring the performance of these strategies by means of key indicators.

In Part II (Chapters 5 and 6), the hypotheses are derived from the literature and the validity of these hypotheses is ensured by the qualitative data collection and analysis.

In Chapter 5, the seven hypotheses are set by deriving them from the literature. For each factor of customer equity one hypothesis is developed. In total, seven factors were identified: distribution channel management, communication management, service quality management, price management, product and service management, process management, and human resource management.

Chapter 6 contains the qualitative data collection and analysis. The results of twelve interviews conducted for verifying the validity of the seven hypotheses derived from the literature in Chapter 5 are presented.

Part III (Chapters 7, 8, and 9) covers the statistical procedures for the quantitative method and the quantitative data collection and analysis of this thesis.

In Chapter 7, the research methodology applied in this thesis is explained. To test empirically the seven hypotheses developed in the previous chapter, the quantitative method was used. Overall, the statistical procedure included four main analyses: validity assessment (content validity and face validity – assessing if proposed variables correspond with research content), exploratory factor analysis (reducing variables to more meaningful factors), reliability analysis (assessing internal consistency / quality of factors), and multiple regression analysis (investigating relationships between independent variables and dependent variable).

In Chapter 8, the data used, the questionnaire development, the pre-testing, and the survey administration are described. Some general descriptive statistics are provided (e.g. number of employees, company turnover) to get some feeling for the data used in this study.

In Chapter 9, a company survey of customer equity carried out for this thesis highlights the importance of this research and shows benefits, problems, and requirements associated with customer equity. This chapter also contains the empirical results of testing the relationship between the possible factors of customer equity and customer equity itself. It reports the findings of this empirical research and explains the output from SPSS.

In Part IV (Chapter 10), conclusions, managerial implications, recommendations to companies, limitations and future research are presented.

In Chapter 10, the managerial implications of the analyses are discussed. Based on the major findings of the study, conclusions on the effects of the factors on customer equity are formulated. Finally, a replication of this work in other European countries and other industries is recommended to determine the degree to which these findings could be generalised. Chapter 10 ends with a discussion of the limitations of this study and the implications of the results for future research on customer equity.

Table 2 provides an overview of the entire structure of this dissertation.

Chapter 1	Introduction
Part I: Chapters 2, 3 and 4	
Chapter 2	Customer equity theory and development from the literature
Chapter 3	Customer equity development from the company perspective
Chapter 4	Conceptual framework of the market-oriented customer equity process (company perspective)
Part II: Chapters 5 and 6	
Chapter 5	Hypotheses setting
Chapter 6	Qualitative data collection and analysis
Part III: Chapters 7, 8 and 9	
Chapter 7	Application of statistical procedures
Chapter 8	Quantitative data collection
Chapter 9	Quantitative data analysis
Part IV: Chapter 10	
Chapter 10	Conclusions, managerial implications and future research

Table 2: Structure of the dissertation

Part I.

LITERATURE REVIEW AND DEVELOPMENT OF THE CUSTOMER EQUITY PROCESS FOR THE COMPANY PERSPECTIVE

2 Chapter 2: Customer Equity Theory And Development From The Literature

2.1 Introduction

A firm's emphasis on deriving benefits from opportunities arising from the implementation of customer equity reflects the important role that a customer plays in the decision-making process. Today, business is centred in customer needs and customer performance that are the basis for maximising cross-selling, up-selling, customer satisfaction, or customer loyalty.

The rapid and radical changes in today's marketing environment resulted in an emphasis on relationship marketing, i.e. the importance of building and keeping a close relationship between companies, customers, and other business parties. Now, the focus is not on a single transaction but on the length of more technologically-based relationships.

Since each customer relationship is characterised by a variety of monetary and non-monetary criteria, such as purchase amount, product types purchased, frequency of purchases, or duration of the relationship with a company, not all aspects can be used for calculating customer equity. In general, customer equity is determined on a monetary basis by summing up the discounted lifetime values from all customers. However, in the literature, researchers also use customer lifetime value interchangeably with customer profitability and customer profit. Besides these monetary aspects, non-monetary criteria, such as the number or frequency of purchases, can be added to a customer equity matrix. A good example of such an approach is the recency-frequeny-monetary (RFM) analysis.

Researchers have paid modest attention to such value-delivering sources during the interaction-relationship processes between customers and firms. Such value-delivering sources are a tool for satisfying customer needs and enhancing the purchase volume of customers and, hence, customer equity.

The processes of applying value-delivering sources to build customer equity in an organisational environment is very complex and needs to be based on different streams of research to present a complete picture. Besides calculating customer equity, such a process consists of other activities, such as segmenting, managing, and retaining relationships with customers.

2.2 Interpretation of customer equity and customer perceived value

In the literature, there are two ways to interpret customer value from the;

(a) _company perspective_ i.e. how the company itself interprets customer equity and customer value (see Figure 2).

(b) _customer perspective_ i.e. what the customer perceives to be the value of what he or she is getting called the customer perceived value (see also Figure 2).

From the _company perspective,_ customer value is defined as an evaluation of the customer base by organisations. In general, organisations carry out this evaluation by measuring the financial performance of a customer. An appropriate performance measure is the customer lifetime value, which is then summed over all of the firm's customers (e.g. Blattberg and Deighton, 1996; Rust et al, 2000). This sum represents the customer equity of an organisation.

From the _customer perspective,_ customer value is defined as customer perceived value. It is a measure that shows how customers assess the positive and negative consequences of the utility of a product (e.g. Snoj et al 2004, Flint and Woodruff 2001). In other words, customers evaluate the benefits and costs resulting from the purchase of the product.

Therefore, section 2.2.1 will deal with the _company perspective_ and section 2.2.2 will provide explanations as to how integration of the _customer perspective_ could assist the company to improve its marketing strategy.

```
Company perspective                    |  Customer perspective
                                       |
        ┌─────────────────┐           |
        │ Building        │           |
┌──────────────┐│ strategies     │     |   ┌──────────────────┐
│              ││ for delivering │     |   │                  │
│ Customer     │→│ value to       │ Value│→│ Customer perceived│
│ equity       │ │ customers      │ delivery│  value           │
│              │ │ through customer│    |   │                  │
└──────────────┘ │ equity dimensions│   |   └──────────────────┘
                 │ (e.g. process   │    |
Measure for       │ management, brand│   |   The difference between the
determining       │ management etc.)│    |   perceptions of benefits
the total of the └─────────────────┘    |   and the total cost of ownership
discounted                              |   when customers purchase
lifetime values summed                  |   a product.
over all of the firm's customers.       |
```

Figure 2: Customer equity and customer perceived value
Source: own

2.2.1 Customer equity

Customer equity is seen as a measure that determines the financial performance of a firm's customer base *from the angle of a company*. This means that organisations evaluate customers as a kind of asset by determining the financial potential of their current and future customers. In the literature, a number of definitions of customer equity exist. To avoid confusion, the following sections distinguish between customer equity as a performance measure (CLV) and as a strategic measure.

2.2.1.1 Customer equity as a performance measure

Most researchers define customer equity as the total of the discounted lifetime values summed over all of the firm's customers (e.g. Blattberg and Deighton, 1996; Rust et al, 2000; Bayón et al, 2002) (see Table 3).

In the literature customer equity is the discounted value, or present value, of the net cash flows that a firm can expect to receive from its customers over time (Carpenter, 1995). All these definitions add to a general interpretation of customer equity as the sum of all customer lifetime values (see also Berger and Bechwati, 2001).

Definitions of customer equity	Authors
Customer equity is the total discounted lifetime values from all customers.	e.g. Rust et al (2000), Bayón et al (2002), Blattberg and Deighton (1996), Berger and Bechwati (2001)
Customer equity is the excess of a customer's revenues over time over the company costs of attracting, selling, and servicing that customer.	e.g. Kotler and Armstrong (1995)
Customer equity is "the profit from first-time customers, minus the cost of acquiring the customers, plus expected profits from future sales to these newly acquired customers, summed across all customer segments and cohorts".	e.g. Blattberg et al (2001)
Customer equity is "the product of the number of customers multiplied by the average lifetime value of its customers".	e.g. Hansotia (2004)
Customer equity is the combined discounted customer lifetime values of all of the company's current and potential customers.	e.g. Kotler et al (2008)

Table 3: Definitions of customer equity

Customer equity can also be expressed in the form of formulas. In the following, three examples of customer equity formulas are presented.

(a) Blattberg and Deighton (1996) express customer equity as the sum of two net present values: the return from acquisition spending and the return from retention spending. They propose the following equation:

$$\text{Customer equity} = am - A + a(m-R/r)*[r' / (1- r')]$$
$$\text{with } r' = r / (1+d)$$

where a is the acquisition rate (i.e., proportion of solicited prospects acquired) and depends on A, the level of acquisition spending per solicited prospect (i.e., money per prospect), m is the margin (in monetary units) on a transaction, R is the retention spending per customer per year, r is the yearly retention rate (as a

proportion) and d is the yearly discount rate appropriate for marketing investments (again, as a proportion).

(b) Libai et al (2002) provide a segment-based approach dividing a customer base into segments by using customer-level profitability or other data (e.g. demographic and lifestyle, family life cycle, purchase patterns). They suggest using the so-called Markov probability series where customers can either stay in their current segment or move to another segment. Using this approach, the vector equation for the number of customers in each segment is:

$$C_t = MM_t * C_{t-1}$$

where C*t* is the vector of the number of customers in each segment in year *t*, MM*t* is the movement matrix containing the probability of switching to the segment from other segments in a given year. When combined with a profit vector, P*t*, defined as the profit from each segment in year *t*, then the customer equity calculation generalizes to:

$$\text{Customer Equity}^1 = \sum_{t=0}^{T} MM_i * C_i * P_i$$

where customer equity is equal to the sum of the customer lifetime values of all the firm's customers. Authors, such as Rust et al (2001) or Pfeifer and Carraway (2000), have also used a Markov process to manage brand switching or customer switching.

(c) Hansotia (2004) defines customer equity as "the product of the number of customers multiplied by the average lifetime value of its customers". He proposes the following formula for calculating customer equity:

Total customer equity = (Number of customers) * (Average customer lifetime value)

He goes into more detail and decomposes this formula into two components: namely the new customer equity and the veteran customer equity. New customer equity covers the time until the customer makes the second purchase. Veteran customer equity is defined as the time from the second purchase on.

Hansotia (2004) proposes the following more detailed formula of customer equity:

Customer equity = (New customer equity) + (Veteran customer equity)

where
New customer equity = (Cash flow from initial purchase)
    - (Marketing and servicing costs prior to the second purchase)

New customer equity = (Revenues from initial purchase)
(more detailed)   - (Cost of goods sold)
    - (Cost of processing and fulfilling the initial order)
    - (Marketing acquisition cost of the new customer)
    - (Marketing and customer servicing costs prior to the
      second purchase)

Veteran customer equity = Present value of cash flows from future purchases,
    starting with the second purchase

Finally, Hansotia (2004) suggests applying customer acquisition, customer development (add-on selling / selling additional products and services), and customer retention for continually increasing total customer equity.

2.2.1.2 Customer equity as a strategic measure

In recent studies, customer equity was more and more integrated into management systems enabling companies to use customer equity in a strategic way. In particular, in the marketing area it is important to know the financial performance of customers to adjust appropriate marketing strategies. Therefore, organisations use **customer equity as a basis for a variety of marketing decision problems, such as determining pricing strategies** (Berger and Nasr, 1998), selecting **media** (Keane and Wang, 1995), setting **acquisition programs** (Berger and Nasr, 1998), and setting optimal **promotion budgets** (Blattberg and Deighton, 1996).

In the literature, there is a growing number of customer equity frameworks that view customer equity from a strategic perspective. Hogan et al (2002), for example, propose a framework in which a firm's tangible assets (e.g. plant or equipment) and intangible assets (brand or channel relationships) are used for increasing customer equity. Besides these assets, the framework points out the

importance of customer equity management skills that identify, initiate, develop, and maintain profitable customer relationships for maximising customer equity.

Another model developed by Rust et al (2000) is composed of three key drivers of firm growth (customer equity), namely value equity (e.g. price, quality, and convenience), brand equity (e.g. brand awareness, attitude toward the brand, and corporate ethics), and relationship equity (e.g. brand loyalty). The framework provides information about how marketing strategies, in particular customer-centred strategies, can increase customer equity.

A further example of a customer equity framework is that developed by Blattberg et al (2001). They suggest that an increase in customer equity is achieved through customer acquisition, customer retention, and add-on selling of additional products. One can conclude that many customer equity frameworks are based on traditional relationship management, i.e. attracting, maintaining and enhancing customer relationships for maximizing customer equity.

In general, customer equity is defined as a measure that is calculated by summing up the individual customer lifetime values (CLV). From a strategic point of view, customer equity is used for determining prices, budgets, or media selection, and for making brand decisions, retention decisions, or quality decisions.

2.2.2 Customer perceived value

In the marketing literature, there are many definitions and interpretations of customer perceived value (see Table 4). Two common themes are discussed in most definitions of customer perceived value, namely the notions of "trade-off" and "benefit-sacrifices" (e.g. Snoj et al, 2004; Flint and Woodruff, 2001; Slater and Narver, 2000; Ulaga and Chacour, 2001; Normann and Ramirez, 1993). The trade-off is the difference between benefits and sacrifices perceived by the customer in a market offering (see Ulaga and Chacour, 2001). In other words, value is created when the customer perceives more benefits than sacrifices (Slater and Narver, 2000). By means of a formula, customer perceived value can be expressed as follows (see Day, 1999):

Vc = Bc – Cc

where Vc is the customer perceived value, Bc the perceived benefits and Cc the perceived life time costs arising from making the purchase.

Definitions of customer perceived value	Authors
Customer's perceived net trade-off received from all relevant benefits and costs or sacrifices delivered by a product or service or supplier and its use.	e.g. Snoj et al (2004), Flint and Woodruff (2001), Slater and Narver (2000), Ulaga and Chacour (2001), Normann and Ramirez (1993), Christopher (1996)
Customer value is the relationship between the degree of customer satisfaction with the products and services received and the satisfaction with the price paid.	e.g. Laitamaki and Kordupleski (1997), Best (1997)
Perceived value is a trade-off between perceived quality and perceived psychological as well as monetary sacrifice.	e.g. Dodds et al (1991), Teas and Agarwal (1997)
Customer's assessment of what is received (benefits provided by the service – get component), and what is given (costs or sacrifice in acquiring and utilising the service – give component).	e.g. Hellier et al (2003), Zeithaml et al (1990), Zeithaml (1988)
Customer delivered (perceived) value is the difference between total customer value (bundle of benefits customers expect from a given product or service) and total customer cost (bundle of costs customers expect to incur in evaluating, obtaining, and using the product or service).	e.g. Kotler (1997)
Customer perceived value is the core value (benefits of a core solution minus price paid) plus or minus added value (positive added value = additional services, such as quick delivery, attentive and supportive service employees; negative added value = complicated systems, non-user friendly technology etc.).	e.g. Grönroos (2000)

Table 4: Definitions of customer perceived value

Perceived customer value can be improved in two ways. The first possibility is to increase the level of benefits perceived by a customer. The second possibility is to decrease customer's costs arising from the purchase of the product.

When an organisation intends to transform perceived customer value, it always has to consider additional expenditures resulting from the transformation. For example, by giving greater emphasis to certain existing product attributes a salesperson may increase the customer's perception of the benefits of a purchase (Blois, 2003). However, developing appropriate product features causes additional expenditures due to the need of financial and human resources.

In this context, it is important to note that an organisation needs to exceed value delivery of competition to attract customers. Customers compare the value delivery of companies and decide in favour of the company providing the highest value. One can conclude that the higher the value delivery of a company is, the higher customer perceived value (Laitamaki and Kordupleski, 1997; Porter, 1996). **Hence, customer perceived value is relative to competition**.

Furthermore, customer perceived value is oriented towards a **strategic level.** This means that organisations use it as a basis for identifying value sources that may improve value delivery to customers (Eggert and Ulaga 2002). By developing appropriate strategies, organisations benefit from this knowledge.

Besides the previously mentioned characteristics of customer perceived value, there are also some advantages. One main advantage is the use of customer perceived value as **pre- and / or post-purchase construct.** This is a very important advantage because most customer measurement scales in the literature are limited to the measurement of post-purchase behaviour and thus not independent of the timing of the use of market offerings (Woodruff and Gardial 1996). A good example of a post-purchase construct is the customer satisfaction scale, which determines the satisfaction of the customer after the purchase of a product or service.

Finally, a further advantage of this scale is the fact that it measures the individual value perceived by each customer. This is extremely important because each customer perceives value in a different way and thus evaluates individually a market offering. Hence, one can deduce that customer perceived value is a **subjective assessment** of positive and negative consequences of using a product and service.

In the following sections, the two components of customer perceived value, namely (a) perceived benefits and (b) perceived sacrifices / costs, are discussed.

(a) Perceived benefits.

Many researchers have defined perceived benefits in the past (e.g. Snoj et al, 2004; Lapierre, 2000). However, a singular definition cannot capture all factors associated with perceived benefits. On the one hand, some researchers argue that economic, technical, service, and social benefits are the main factors (see for example Anderson et al, 1993; Monroe, 1990). Examples are service quality, service customisation, responsiveness, flexibility, reliability, technical competence, image, trust, and solidarity (see Lapierre, 2000; Monroe, 1990). On the other hand, authors such as Snoj et al (2004) define perceived benefits as a combination of different attributes of products (tangible and intangible; intrinsic and extrinsic etc.), available in relation to a particular buy and use situation.

(b) Perceived sacrifices / costs.

As customer perceived value is a multidimensional construct, perceived sacrifices are multidimensional as well. Thus, most authors state that perceived sacrifices consist of monetary and non-monetary costs (e.g. Kotler, 2000; Monroe, 1990; Zeithaml and Bitner, 1996; Snoj et al, 2004). In other words, perceived sacrifices are a combination of a nominal price and all other costs of product acquisition and its use (e.g. Slater and Narver, 2000; Ulaga and Chacour, 2001). These other costs can be tangible costs related to the service, such as transportation, repair, maintenance, as well as perceived costs such as risk of failure or poor performance (see Monroe, 1990). Day (1999) proposes a

similar definition and lists ordering costs, set-up costs, operating and maintenance costs, financing costs and disposal costs as other costs besides the purchase price. One can conclude that other costs are mainly time cost, energy cost, search cost, and psychic cost (see Kotler, 2000; Zeithaml and Bitner, 1996; Patterson and Spreng, 1997).

> *In general, customer perceived value can be defined as the difference between what a customer receives from the company (perceived benefits) and what he has to give up (perceived sacrifices / total costs of ownership) when he makes a purchase.*

2.2.3 Defining customer equity for this thesis

Customer value has been studied under the name of customer lifetime value, customer equity, and customer profitability (see Hwang et al, 2004). All these terms describe methods that aim at identifying the monetary performance of customers from the company perspective. However, customer value is also used for defining customer perception of value (see Blocker and Flint, 2007) (customer perspective). This means that the term customer value is used interchangeably for explaining two different perspectives of value, namely the customer perspective and the company perspective.

The focus of this thesis is the company perspective, i.e. this research aims at investigating how customer performance is improved and which strategies are necessary for realising this. Hence, a clear definition of customer value from the company perspective is needed. As customer lifetime value and customer profitability reflect the performance of only one customer and not the complete customer base, customer equity is better suited to this thesis. An evaluation of the performance of the complete customer base, for example, by means of segmentation techniques, facilitates the realisation and implementation of strategic decisions. Therefore, this thesis refers to the following definition of customer equity:

Customer equity is the total of the discounted lifetime values summed over all of the firm's customers (e.g. Blattberg and Deighton, 1996; Bayón et al, 2002).

Finally, it is important to note that there exists confusion surrounding the terms customer lifetime value and customer profitability. On the one hand, many researchers use these terms interchangeably and loosely (see, for example, Mulhern, 1999). "Customer lifetime value" becomes "profit" which becomes "customer profitability". On the other hand, other authors such as Ryals and Knox (2005) distinguish between these two terms because they argue that customer profitability is generally a single-period measure and customer lifetime value is based on forecasts. However, the researcher uses both terms interchangeably in this thesis because customer profitability can be calculated for the single period or in net present value terms, hence only slight differences exist (see Mulhern, 1999).

2.3 Benefits of customer equity to the firm

Customer equity means identifying cost and revenues streams of each customer for calculating customer lifetime value and summing up all lifetime values of the firm's customers. In other words, an organisation segments its customers according to their financial performance. This enables organisations to apply different strategies to different segments that help the customer to grow. Strategies for enhancing revenues with existing customers include increasing cross-selling (selling new additional products) and up-selling (selling similar more expensive products), and customising products, solutions, and pricing policies. Hence, revenues are managed through identifying the right service or product at the right price for the right target group. Besides this monetary benefit, better meeting customer needs increases customer satisfaction and exceeds customers' expectations. Hence, measures of satisfaction and loyalty increase.

Another opportunity for transforming unprofitable to profitable relationships or increase revenues from profitable relationships, arises from delivering a value proposition that is recognised by the target market as a better proposition than that presented by competitors. Creating superior customer value enables companies to secure their niche in a competitive environment and to maintain

their leadership position. One can imply that value delivery should be at the heart of any strategy to manage customer profitability and customer equity.

To summarize, organisations benefit from customer equity management in different ways. Examples are:

- better customer segmentation,

- more customisation,

- reduced price competition (through customised pricing) (Day, 1999),

- better meeting customer needs,

- increased customer satisfaction (Reichheld and Teal, 2001),

- improved customer loyalty (Macintosh and Lockshin, 1998), and

- greater differentiation from competition (Christopher, 1996).

2.4   The new role of marketing

There is a recent shift in strategic marketing thinking emphasising the role of customer equity in an organisational environment (see Kotler et al, 2002; Hogan et al, 2002). Whereas traditional strategic marketing views the marketing department as a single unit that plans and integrates marketing activities focusing on after-sales service, sales, or product development, the new strategic marketing mind-set proposes new marketing activities that integrate the work of exploring, creating, and delivering customer lifetime value and deploying tangible and intangible assets.

The new strategic marketing supports customer equity management at all organisational levels (Hogan et al, 2002) to help the marketers to analyse, identify, and satisfy markets, which have the greatest potential for maximizing customer equity. By understanding which existing and potential markets are of importance to an organisation, the markets can be targeted in an appropriate way that better addresses customer needs. Furthermore, the new strategic marketing focuses on customer retention rather than customer acquisition supporting Reichheld and Teal's findings, which say that it costs five to seven

times more to find new customers than to retain current customers (Reichheld and Teal, 2001). This monetary benefit is intensified by segmenting customers according to their profitability and differently serving them. Hence, the traditional marketing perspective aims at treating each customer in the same way, whereas the new marketing perspective concentrates on improving customer lifetime value (customer equity) and building cost-saving strategies for less profitable customers.

For supporting the new role of marketing at an organisational level, it is necessary to transform a functional organisational structure into a horizontal organisational structure (see Christopher, 1996). This means that cross-functional process teams, which offer a more integrated perspective of the issue, replace departments. A cross-functional process team consists of team members from different areas, such as sales, marketing, or production, to ensure that there is a sound basis of knowledge, which makes it possible to translate strategic goals into process plans, i.e. create specific programs for each core process. Examples of core processes that should be managed on a cross-functional basis are the development of brands, products, consumers, customer relationships, relationships with suppliers, and supply chains. One can conclude that new strategic marketing centres in a broader business orientation where the delivery of superior customer value becomes the key objective (Christopher, 1996).

Hansotia (2004) emphasises the necessity of managing customers based on their financial performance, i.e. their profitability and revenue, by redesigning the marketing organisational structure. He suggests extending the marketing functions to make the data more accessible, which is necessary for the decision-making process pertaining to resource allocations and customer investments. Besides acquiring new customers and winning back lapsed customers, the marketing department should be responsible for deepening customer relationships to increase customer profits (customer equity) and the duration of the lifetime of a customer. These marketing core activities are supported by activities, such as the calculation of budgets and financial plans, the development of contact strategies and ongoing market research studies,

and decisions on product development, product bundling, and price levels. Figure 3 illustrates an example of a marketing organisational chart for managing customer equity.
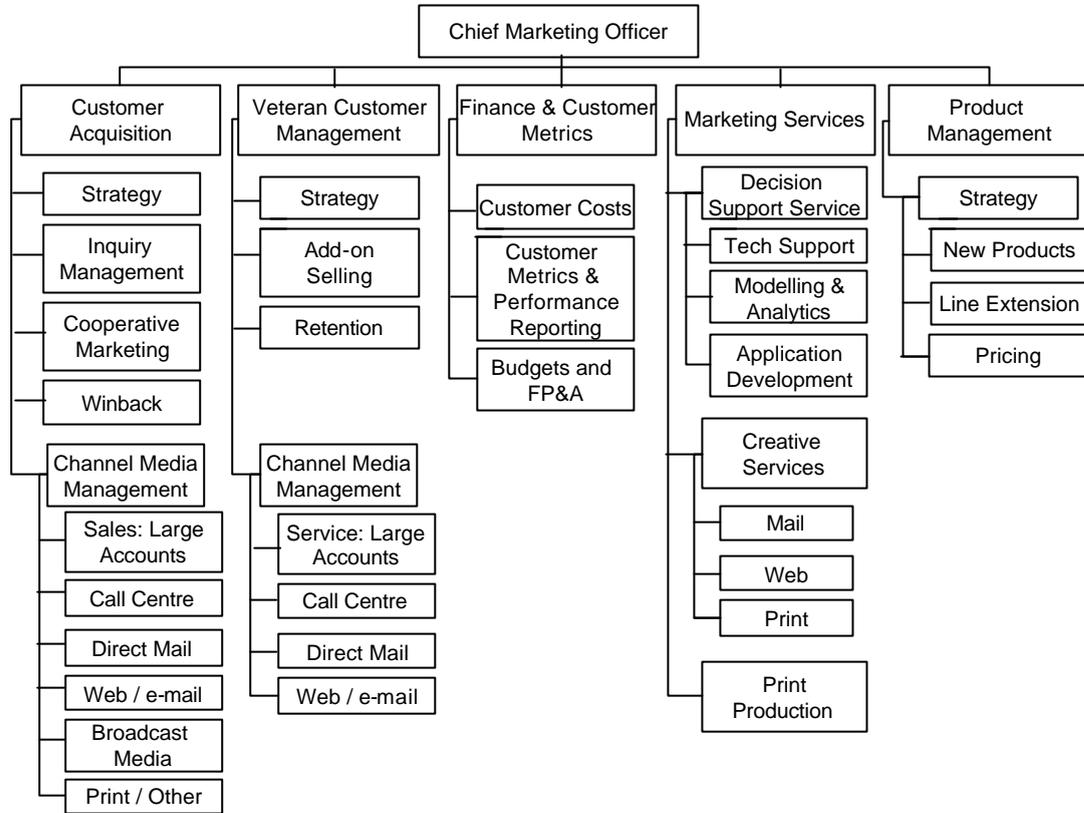
Figure 3: Marketing organisational chart for managing customer equity
Source: Hansotia (2004)

To summarize, marketing is getting a new role as the organising force behind the management of relationships with customers and suppliers, and customer lifetime value (customer equity) that generally advocates allocation of resources away from low-value customers and toward those of highest value to the firm. Besides these new functions, new strategic marketing maintains traditional activities, such as product and brand development. It has been recognized that the marketing division needs a new structure, which is centred on customers' monetary and non-monetary needs (e.g. Hansotia, 2004).

2.5 Methods for calculating customer equity (monetary)

Customer equity is a „profit maximising" equation that underlies efforts to maximise customer profit and reduce marketing, sales, and acquisition spending. The calculation of customer equity is made by summing up all lifetime values (CLTV) from the firm's current and future customers. However, customer lifetime value (CLTV) is differently interpreted in the literature and in practice. This means that customer lifetime value is used interchangeably with customer profitability and customer revenue. Hence, customer equity can be calculated in three different ways that are discussed in the following sections.

- *CLTV.* The CLV measures the profit streams of a customer across the entire customer life cycle (see Blattberg and Deighton, 1996; Bauer and Hammerschmidt, 2005). "The combined lifetime values of all current and future customers yield customer equity (the value of the customer base), which represents the entire operating cash flow of a firm" (Bauer and Hammerschmidt, 2005). In contrast to the non-operating assets, the operating cash flow (customer equity) is generated by selling products and services. Hence, the value of a firm (free cash flow) is the sum of customer equity and all cash flows generated from non-operating assets, i.e. it is the difference between all revenues and all expenditures over a given time period.

- *Customer profitability.* Not all researchers describe customer equity as a future-oriented measure. Stevens (2006), for example, sees customer equity as a descriptive measure explaining "past behaviour without making assumptions about future behaviour". It is calculated by summing up customer profitability of all firm's customers, i.e. it is the undiscounted sum of customer profitability (see Ness et al, 2001). Customer profitability itself is the difference between the revenues earned from and the costs associated with the customer relationship during a specified period (e.g. van Raaij, 2005).

- *Customer revenue.* As already mentioned above, customer equity is the sum of all lifetime values of all current and future customers of a firm.

However, many organizations base CLTV only on a customer's revenue contribution rather than their profit contribution because they have no access to the information necessary for calculating the cost stream of the cash flow. As an alternative to customer profit, they use customer revenue, which is better accessible. Hence, customer lifetime value has been equated most often with lifetime revenue stream (see Reichheld, 1996) instead of the discounted profit stream. Some researchers take into account the problematic derivation of the profit streams (cash flows) and suggest calculating CLTV on the basis of customer revenues (see, for example, Tirenni et al, 2007) considering neither discounted cash flows nor costs. Hence, one can conclude from the above that customer revenue is also a means for calculating customer equity.

2.5.1 Customer lifetime value (CLTV)

Customer equity is the total discounted lifetime values from all customers (see Rust et al, 2000; Bayón et al, 2002; Berger and Bechwati, 2001). Hence, customer lifetime value is a key element in the calculation of customer equity and therefore explained in detail in the following.

Customer lifetime value (CLTV) is a future-oriented measure, which can be used to determine profitable and unprofitable customers and to adapt the firms marketing programs towards individualised marketing strategies. Many researchers have expressed CLTV as the present value of the future profit streams of a customer across the entire customer life cycle (see Blattberg and Deighton, 1996; Bauer and Hammerschmidt, 2005). Table 5 provides an overview of the definitions of CLTV in the form of a discounted measure. These definitions mention "discounted", "expected", or "present value" for connecting the value in CLV to the finance concept of present value.

Definitions	Authors
CLTV is the **net present value** of a future stream of contributions to	Jackson, 1994; Courtheoux, 1995

overheads and profit expected from the customer.	
CLTV is **the total discounted net profit** that a customer generates during her life on the house list.	Bitran and Mondschein, 1996; Jain and Singh, 2002; Niraj et al, 2001
CLTV is **the discounted present value** of the forecasted stream of profits attributable to the customer.	Bell et al, 2002
CLTV is the **expected profits** from customers, exclusive of costs related to customer management.	Blattberg and Deighton, 1996
CLTV is the **present value** of the future cash flows associated with a customer.	Pfeifer et al, 2005
CLTV is the **net present value** of the profit that a firm stands to realize on the average new customer during a given number of years.	West et al (2006)

Table 5: Definitions of CLTV

However, the term customer lifetime value has also been used most often to mean lifetime revenue stream, as opposed to the discounted stream of profit net of acquisition investment (see, for example, Reichheld, 1996). Furthermore, CLTV is also used to refer to the undiscounted sum of customer profitability as advocated by Ness et al (2001). Hence, customer lifetime value is equated with customer revenues and customer profitability over several periods. In contrast to CLTV, both measures are past-oriented.

Dorrington and Goodwin (2002) stress this differentiation and propose to calculate customer lifetime value as follows:

Customer lifetime value = total revenues – (fixed costs + variable costs).

This formula calculates the monetary value of a customer in the same way as customer profitability does, i.e. customer lifetime value is equated with customer profitability. The revenues are determined by adding up the total of all of the orders placed with the organisation, whereas for the determination of the fixed

and variable costs, an activity-based accounting system is necessary (Dorrington and Goodwin, 2002).

From a strategic perspective, a CLTV-based approach can be used for developing revenue-enhancing strategies, such as up-selling, cross-selling, or special loyalty programmes. To increase CLTV, three different strategies are possible: **increasing lifetime, increasing sales, or cutting the costs of serving a customer** (Pitt et al, 2000). An increase in lifetime can be achieved by rewarding customer loyalty and providing high-quality services. For revenue growth, more individualised products that are better targeted on customer needs are necessary. Finally, cutting service costs for low-value customers results in a greater profit margin.

2.5.1.1 The components of CLTV

CLTV can also be expressed in the form of an equation, which can be seen as the basis for most CLTV assessments (e.g. Blattberg and Deighton, 1996; Berger and Nasr, 1998). The equation is as follows (Libai et al, 2002):

$$CLTV = \sum_{t=0}^{n} \frac{p*r^1}{(1+d)^1}$$

where r is a firm's average retention rate, p is the average profit from a customer per period, d is the discount rate, and n the years. In this equation, CLTV is seen as the net present value of a customer's profit stream accounting for the firm or segment-level retention rate. One can conclude that customer lifetime value consists of three different types of variables, namely revenue, costs and retention rate (Reinartz and Kumar, 2000).

The variable "revenue" can be divided into "autonomous" revenue (basis sales), up-selling revenue (selling of higher priced substitutes), cross-selling revenue (selling of complementary products or product categories), and contribution margins resulting from word-of-mouth (see Bauer and Hammerschmidt, 2005). All four types of revenue are generated by customers. The variable "costs" comprises acquisition costs, marketing costs, production costs and costs of

serving the customer. The last two types of costs can also be called sales costs. It is important to include acquisition costs, i.e. costs incurred to attract customers, because only if the remaining "net value" (the value exclusive of acquisition costs) exceeds the acquisition costs, the present value is positive and the customer is profitable (Jain and Singh, 2002). Finally, the variable "retention rate" reflects the probable degree of customer loyalty, i.e. it considers the expected relationship durations with customers.

CLTV provides not only advantages, such as the use of individualised strategies or a continuously and regularly determination of the monetary value of a customer taking into account customers changing profitability. A main disadvantage of the customer lifetime method is the fact that it is only reliable for the near-to-medium term and can be dramatically affected by unforeseen circumstances, such as an economic downturn or changes in interest base rates (Dorrington and Goodwin, 2002). This sensitivity has been criticised by many researchers (e.g. Jain and Singh, 2002).

Furthermore, CLTV depends on assumptions about the future stream of income from a customer, the appropriate allocation of costs to customers, the discount factor, the expected "life" of a customer, and the probability that the customer is "alive" at a particular point in time. As one might expect, small changes in the assumptions associated with key model variables can give rise to vast changes in the computed values.

In addition, the assumption about assigning costs to customers requires an activity-based costing system that allocates all costs to activities, such as marketing or sales, which in turn are linked to customers, services, products, and orders. As most organisations have traditional accounting systems that divide costs into either fixed or variable and hence do not provide the information necessary for calculating costs per customer, the application of CLTV in practice is difficult.

In general, customer lifetime value is defined as the net present value of a customer's profit streams over his lifetime. Organisations can influence CLTV by increasing

lifetime, enhancing sales, or cutting the costs of serving a customer.

2.5.1.2 A CLTV-based measure - Return on customer

Return on customer (ROC) is a CLTV-based measure that helps organisations to calculate the value of their entire customer base. In contrast to CLTV, which considers only the future stream of cash flows from a firm's current and future customers, return on customer takes into account both the current-period cash flows and the future cash flows from customers and prospects.

ROC "equals a firm's current-period cash flow from its customers plus any changes in the underlying customer equity, divided by the total customer equity at the beginning of the period" (Rogers and Peppers, 2005). Customer equity is defined as the sum of all the future lifetime values (cash flows) of a firm's current and future customers discounted back to the present. The following ROC equation shows the mix of current-period and future profits (cash flows):

$$ROC = \frac{p_i + ?CE_i}{CE_{i-1}}$$

p_i = cash flow from customers during period i,

$?CE_i$ = change in customer equity during period i, and

CE_{i-1} = customer equity at the beginning of period i.

An organisation can maximise return on customer by enhancing its current-period and future cash flows from customers. This means that an organisation needs to take actions that contribute to trust building, for example, by improving service quality or fulfilling the brand promise made in its advertising campaigns. These trust-building activities ensure that customers have a good experience with the company and are more willing to buy further products resulting in an increase in the cash flows. However, to estimate the costs and benefits of these actions, it is important to consider a long-term perspective because the revenues generated will result in higher future cash flows.

As return on customer is based on CLTV, the same advantages and disadvantages discussed in the previous section apply. In short, the main advantage is the forecast of the future monetary customer purchase behaviour. In contrast, the main criticism is the sensitivity of customer lifetime value projections to forecasts of customer cash flows and the timing of the cash flows (Jain and Singh, 2002), as well as the irreducible uncertainties associated with these forecasts.

> *Return on customer (ROC) was developed by Rogers and Peppers (2005) and equals a firm's current-period cash flow from its customers plus any changes in the underlying customer equity, divided by the total customer equity at the beginning of the period.*

2.5.2 Customer profitability

Customer equity can also be calculated by summing up undiscounted customer profitability of all firm's customers (see, for example, Ness et al, 2001; Stevens, 2006). Hence, this second possibility of determining customer equity sees customer profitability as key measure for calculating customers' profit streams.

Customer profitability analysis determines the **difference between revenues per customer and costs per customer** for a single period or several periods (see van Raaij, 2005). Since customer profitability focuses on individual customers, for its calculation a customer-level tracking of revenues and costs is necessary. As this type of calculation is very time-consuming and expensive, most organisations calculate customer profitability not for a single customer, but for customer segments.

In comparison to customer lifetime value (CLTV), which is forward looking, customer profitability refers to an arithmetic calculation of present and past revenues and costs. However, for both CLTV and customer profitability, it is imperative that the organisation understands customer's profit streams.

When the difference between the revenue and costs per customer is positive, the customer relationship is profitable. It is important to consider both the customer revenue and costs streams because a customer can generate high

revenue without being profitable. In other words, **two customers with identical revenue can be either profitable or unprofitable** depending on their costs structure. Figure 4 shows an example in which customer A is profitable and customer B is unprofitable. Customer A causes lower costs-to-serve a customer than customer B because he buys standard products generating low production costs, uses frequently low-cost sales channels such as Internet or call centre that reduce sales costs, orders high quantities, and needs only sometimes post-sales service, which results in low service costs. In contrast, customer B is a high-to-serve customer as he buys customised products, orders small quantities, uses frequently high-cost sales channels (salespeople) and needs high post-sales support (installation, training etc.).
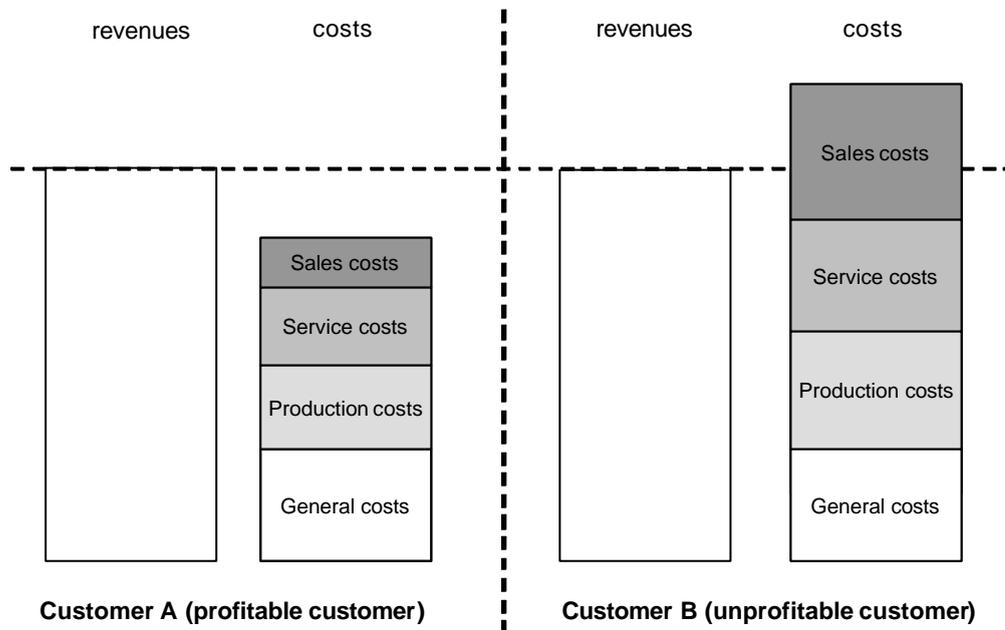
Figure 4: Comparison of profitable and unprofitable customers
Source: adapted from van Raaij (2005)

Given that unprofitable customers lead to a decrease in corporate profits, organisations tend to reduce the number of unprofitable customers. However, not all unprofitable customers should be eliminated (see for example Smith and Dikolli, 1995) because these could be new and growing customers that can be

profitable in the near future. Furthermore, among these customers can be opinion leaders who can provide guidance for other customers in the segment. Hence, an organisation should carefully decide on how to treat unprofitable customers.

Customer profitability analysis enables organisations to apply one-to-one marketing and to adapt their marketing and customer service mix to customers. This means that marketing and sales need to decide which customers they want to build closer relationships with in the future and develop appropriate strategies that enhance the monetary customer performance in the long run.

"A frequently-encountered difficulty for companies wishing to measure customer profitability is that management accounting and reporting systems tend to reflect product profitability rather than customer profitability" (Ryals and Knox, 2005). Hence, for being able to apply customer profitability, an organisation needs to use accounting methods such as activity-based costing that assign costs to customers. Such data can also be used by other systems such as customer relationship management (CRM) that automatically calculates customer profitability at a customer level and a segment level. CRM also supports the calculation of customer profitability on a regular basis and, hence, considers the continuously changing purchasing behaviour of customers.

Customer profitability can be graphically illustrated at an aggregate level by means of CPA figures. The most common ways to depicting customer profitability are the customer pyramid (Zeithaml et al, 2001) and the inverted Lorentz or Stobachoff curve (see Mulhern, 1999). Both CPA figures are discussed in the following sections.

> *Customer profitability is the difference between customer revenues and customer costs, i.e. it determines the profit stream of a customer or a customer group.*

2.5.2.1 The customer pyramid

The customer pyramid developed by Zeithaml et al (2001) divides customers into four tiers by using the names of four metals to indicate profitability:

platinum, gold, iron, and lead. Most commonly, the tiers are based on profitability, with a large group of low profitability customers and unprofitable customers at the base of the pyramid and a small group of high profitability customers at the apex. Hence, the customer pyramid also refers to the "80-20" rule, which says that 80 percent of the corporate profit is generated by 20 percent of the customers. The platinum customers represent these 20 per cent in the customer pyramid.

The first two tiers, platinum and gold customers are of value while the iron and lead customers are less valuable. In other words, the platinum customers are the most profitable customers of an organisation and are characterised by high purchase volume, high commitment, and high future purchase potential. The gold customers are less profitable than the platinum customers are but have still good profitability levels. The customers of this tier frequently purchase products, but mainly products at a lower or discount price. Their commitment to the company is lower than that of the platinum customers. Iron customers are less profitable than the platinum and gold tier and have low loyalty and spending levels. Therefore, for organisations it is not worth specially treating this tier. The last tier, the lead customers are unprofitable and should be eliminated as they cause losses. Figure 5 shows the customer pyramid approach developed by Zeithaml et al (2001).

Organisations can use this customer pyramid for tailoring sales strategies to different customer segments. Such strategies enhance customers' purchase volume, which, in turn, increases customer profitability and corporate profit. A very common method for enhancing revenues is to provide highly profitable customers with a higher level of service than normal.

Most profitable
customers

What segment spends more with us
over time, costs less to maintain,
spreads positive word of mouth?

Platinum

Gold

Iron

Lead

Least profitable
customers

What segment costs us
in time, effort, and
money yet does not
provide the return we
want? What segment is
difficult to do business
with?
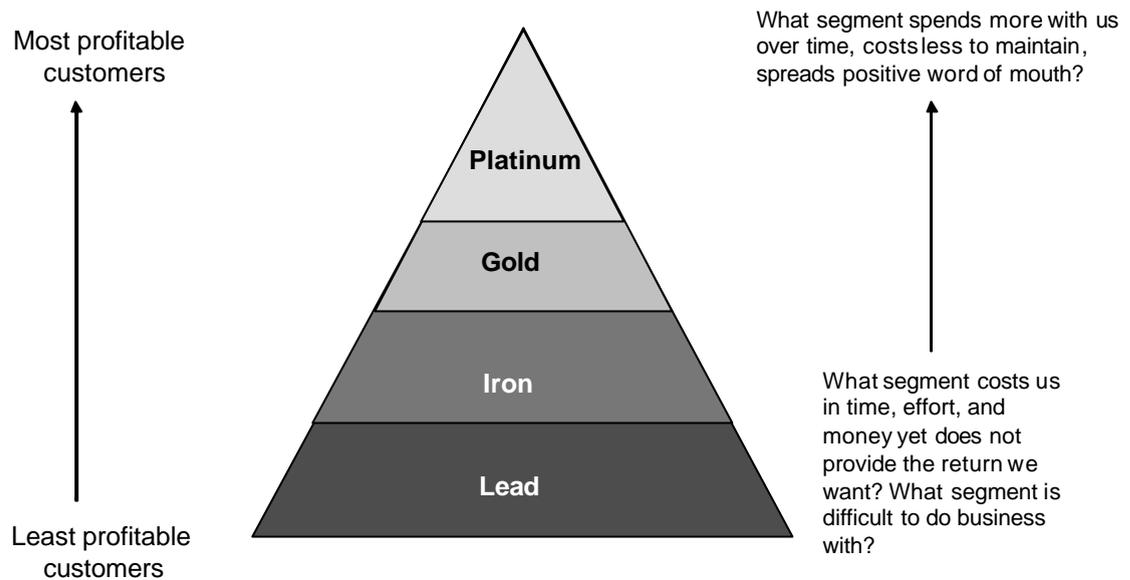
Figure 5: The customer pyramid
Source: Zeithaml et al (2001)

In the literature, there are also customer pyramids that view customer profitability from a more comprehensive perspective. Curry and Curry (2000), for example, have developed a customer pyramid that looks at customer-oriented actions, such as continuous improvements in customer processes, communication with customer, gathering of customer data, or staff's customer care skills and experience. These improvements optimise interactions with customers leading to more satisfied customers and higher customer profitability. For monitoring the impact of these actions on customer profitability, Curry and Curry (2000) propose four process control techniques, namely registration, analysis, planning, and realisation. These four techniques identify and analyse the status of customer profitability, customer behaviour, customer satisfaction, and customer-oriented actions to develop and execute customer focus plans. Such plans aim at achieving profitability, revenue, and satisfaction targets for each customer (segment).

To summarize, the centre of the discussed customer pyramid provides a more comprehensive perspective of customer performance by measuring customer value, customer behaviour, and customer satisfaction. The parameter of

customer value can be both profit per customer and customer lifetime value. However, all parameters aim at maximising corporate profit (see Figure 6).
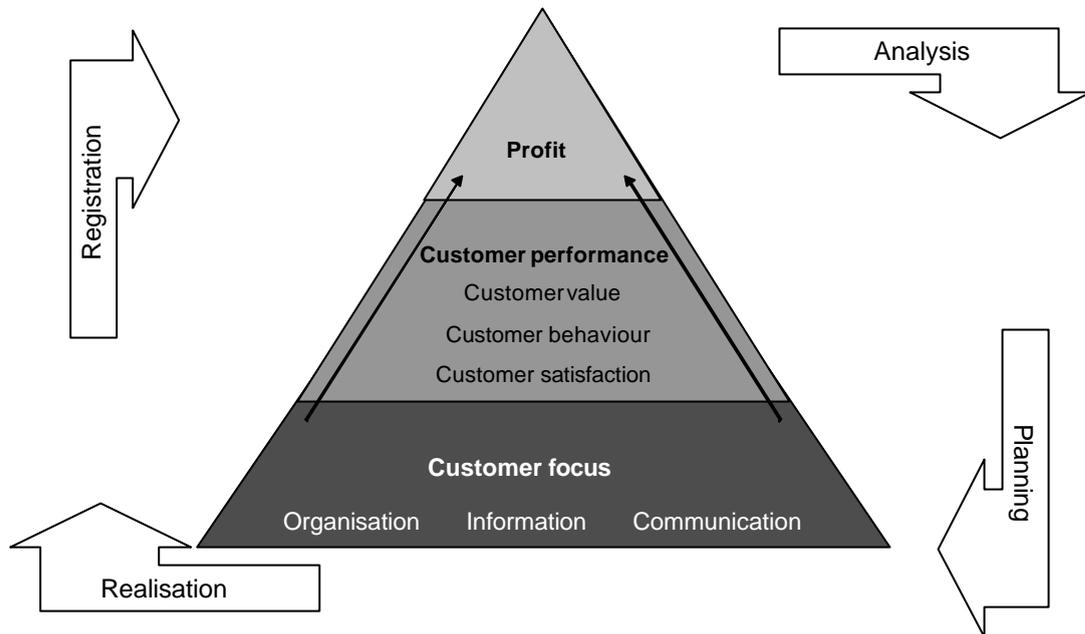
Figure 6: The 3C method
Source: Curry and Curry (2000)

The customer pyramid is a method for visualising customer profitability at an aggregate level. In the literature, there are also more strategic-oriented customer pyramid models that propose the customer focus of an organisation as the motor of customer profitability.

2.5.2.2 The inverted Lorentz or Stobachoff curve

Another possibility of visualising customer profitability at the aggregate level is the inverted Lorentz or Stobachoff curve (see Mulhern, 1999; Storbacka, 1997). This CPA figure is drawn by lining up all customers on the horizontal axis from highest absolute profitability to lowest (in many cases negative) profitability, while plotting cumulative profitability on the vertical axis. Similar to the customer pyramid, the Stobachoff curve is a method that enables the organisations to

apply the 80-20 rule, i.e. to identify the 20 per cent of the customers who generate 80 per cent of the corporate profit.

Figure 7 illustrates graphically an example of the Stobachoff curve. As the curve shows, the top 10 per cent of the customers generate almost 50 per cent of, and the first 30 per cent generate almost 110 per cent of the total customer profitability. Overall, around seventy per cent of the customers are profitable, whereas around thirty per cent of the customers are unprofitable.
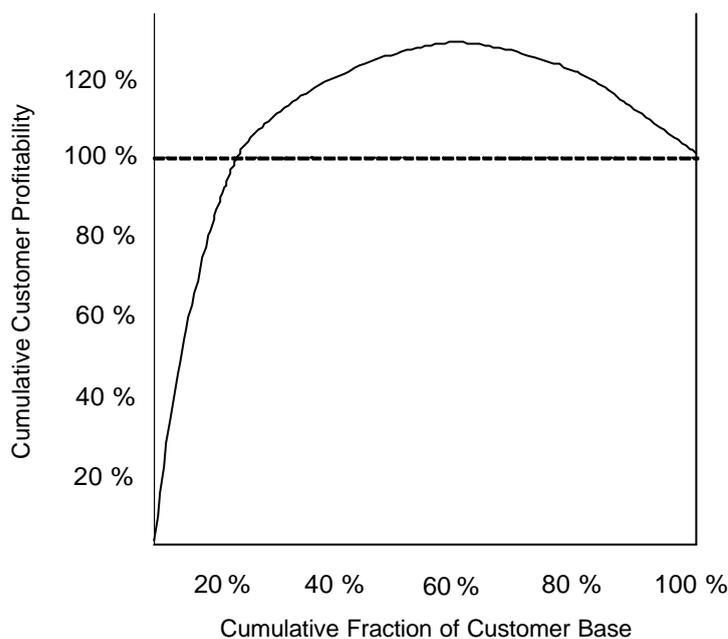
Figure 7: Example of the Stobachoff curve
Source: Storbacka (1997)

In contrast to the customer pyramid, which assigns unprofitable customers to the base of the pyramid, the Stobachoff curve assigns them to the end of the horizontal axis. However, both CPA figures analyse the customer profitability structure of an organisation and provide information for making strategic decisions in the areas of cost and revenue management and strategic positioning.

The inverted Lorentz or Stobachoff curve is a CPA figure that enables organisations to

depict customer profitability at an aggregate level.

2.5.3 Customer revenue

As already discussed in previous sections, customer equity is a CLTV-based measure that calculates the monetary customer performance. However, customer lifetime value (CLTV) is differently determined in theory and in practice. On the one hand, one can use future-oriented profit streams (CLTV) and past-oriented profit streams (customer profitability) and, on the other hand, one can apply past-oriented revenue streams (customer revenue). All three possibilities are seen as a type of lifetime value calculation (see Reichheld, 1996; Stevens, 2006).

Tirenni et al (2007), for example, determines customer lifetime value on the basis of customer revenues by summing up all revenues of a customer for a given period. They suggest the following formula:

$$CLTV_i = \sum_{t=0} r_{i,t}$$

where *CLV i* is the lifetime value of customer *i*, *t* is the time unit in days, and *r i,t* is the revenue generated by customer *i* at time unit *t*. Hence, they calculate CLTV without considering discounted cash flows and costs.

Customer revenue can be depicted at an aggregate level by applying key account management (the inverted Lorentz curve), decile analysis, or the customer pyramid. As the latter has been already discussed in the previous section, key account management and decile analysis are explained in the following.

2.5.3.1 Key account management (KAM)

Key account management is used in all kinds of industries (Kempeners, 1997). It is based on the phenomenon that not all customers contribute to company growth in the same way (see 80-20 rule). In many markets, the bulk of sales

turnover or profit comes from a handful of customers (Millman and Wilson, 1999). Key account management helps organisations to segment their customers according to their turnover and to identify their key accounts, i.e. the customers who are most valuable (see Walter et al, 2001; McDonald, 2000). Key account management (KAM) does not aim at building good, strong relationships at all costs, it pays attention to relationships that are most valuable. That might well mean reducing investment in certain cases (Spencer, 1999).

KAM or ABC-turnover-analysis illustrates the inverted Lorentz curve by representing the cumulative percentage of customers ordered from the most to the least valuable on the horizontal axis and the percentage of cumulative turnover on the vertical axis (Homburg, 1997; Rieker, 1995). This method identifies four different types of customers, namely key accounts, A-customers, B-customers, and C-customers. Key accounts are customers with the highest revenue, A-customers have lower revenue, and, finally, B-customers and C-customers have the lowest revenue streams (see Figure 8).
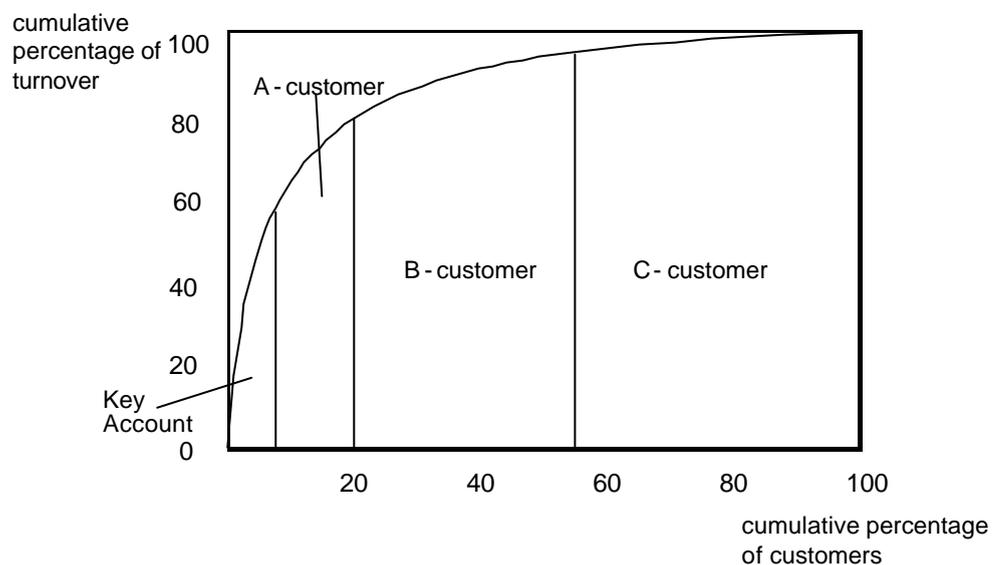
Figure 8: Example of key account management portfolio
Source: Küng et al (2002)

Millman and Wilson (1995), proposed a relationship development model that was build on earlier constructs (as seen earlier in Ford, 1980) and emphasised the strategic importance of KAM. The Millman-Wilson (1995) Relational Development Model was based on exploratory research and concepts drawn from the sales strategy (Wotruba, 1991) and interaction literature (Ford 1980 and Dwyer et al 1987).

By using the model, it is possible to assess the position of selling companies (suppliers) at various stages of key account development. This model demonstrates the progression of the relationship, showing five of the six stages identified by Millman and Wilson:

(1) Pre-KAM,

(2) Early-KAM,

(3) Mid-KAM,

(4) Partnership-KAM and

(5) Synergistic-KAM.

A sixth stage, the Uncoupling-KAM could happen at any stage in the development of a relationship, meaning that for some reason the relationship cannot develop further and will result in a break-up of the partnership. In Table 6 the objectives and strategies for each stage are presented.

Relationship stage	Description	Objectives	Selling strategies
Pre-KAM	- develop networks of contacts - gain knowledge about the customer's operations	- Identify/Explore as key account - Establish account potential - Secure initial order	- Make basic product or service offerings available (product need) - Attempt to gather information about customers - Build trust and open communications
Early-KAM	- win some business, - concentrate its efforts into fulfilling the	- Account penetration - Increase	- Tentative adaptations made to the offer to

	customer's demands in order to convince the buyer	volume of business - Become preferred supplier	match more closely customer requirements. - Build trust through consistent performance and open communications. - Manage implementation of product improvements
Mid-KAM	- the selling company is classified as preferred supplier, - the level of trust and commitment between the partners has become considerable	- Build towards partnership - Become first-tier or single source supplier - Establish key account status	- Focus upon cost reduction and value creation - Address facilitation issues relating to culture, language, etc. - Build inter-organisational teams - Review constantly activity of competitors
Partnership KAM	- the supplier becomes a strategic source for the customer - sharing of the sensitive company information occurs, and partners are engaged in joint strategic and operational collaboration	- Develop spirit of partnership - Lock in customer by providing external resource base	- Focus on joint value creation - Establish semi autonomous project teams - Establish joint strategy planning
Synergistic KAM	- supplier and customer plan and act together in the process of value creation - the interactions are present on every level and between all functions in the organisations, with joint teams established	- Continuous improvement - Shared rewards	- Maintain and exploit relationship - Assess if appropriate

Table 6: Key account relational development cycle

Source: adapted from Wilson (1999), Speare et al (2001), and Wilson et al (2001)

Companies that define and identify key accounts are much more successful in defining customer-oriented strategies and display a deeper understanding of customer needs (Millman and Wilson, 1999). They more often reward customer loyalty, apply cross-selling and up-selling, and identify product preferences of customers. Hence, KAM assists managers in developing strategic alternatives that improve revenue growth in the long run (Pardo et al, 2006).

KAM also supports achieving efficiency targets in the area of business processes. If, for example, the segmentation shows that there are many single orders or potential for bundling service activities, then the organisation can improve internal efficiency and provide certain interactions with customers at reduced costs (see McDonald et al., 1997).

As customer revenue is a type of customer data that is accessible in each organisation across many industries, key account management is applied by many firms. Furthermore, KAM is a good basis for continuous customer evaluation that considers changing customers' purchase volume.

Key account management categorises the customer base of an organisation into key accounts, A-customers, B-customers, and C-customers by using customer revenue as a segmentation criterion. It provides information on customer-specific strategies and actions that aim at maximising customers' revenue streams.

2.5.3.2 Decile analysis

The decile analysis is a revenue-based method that provides an utile aggregation and presentation of customer performance information for organisations. Besides customer revenue, it also lists information on contribution to margin or average purchase amount over a certain period to provide opportunities for strategy identification and improvements at a customer level.

The decile analysis sorts the customer base of an organisation according to customer revenue (turnover) and then categorises all customers into ten evenly numbered segments. Table 7 illustrates an example of a decile analysis

showing the ten evenly numbered groups (second column), the yearly spend of each decile (column 3), the yearly average spend of each decile, the total spend of each decile (column 5), the contribution to margin of each decile (column 6), and the percent of the contribution to margin of each decile (column 7).

The example in Table 7 shows that 20% of the customers (the first two deciles) represent 77% of sales. This is calculated by multiplying the sum of the total spends of the first two deciles (14.047.290) by one hundred and then dividing it by the sum of total spends of all deciles (18.198.717). Hence, the decile analysis refers to the "80/20 rule" and enables organisations to find out which 20% of their customers represent 80% of their revenue.

Decile	Number of customers	Yearly spend of decile	Average spend per year	Total spend of decile	Contribution (30% margin)	Percent
1	5.776	Over $690	$ 1.959	11.314.664	3.394.399,25	62,2%
2	5.776	$330 to $690	$ 473	2.732.626	819.787,68	15,0%
3	5.776	$195 to $330	$ 261	1.509.269	452.780,64	8,3%
4	5.776	$135 to $195	$ 164	944.492	283.347,46	5,2%
5	5.776	$90 to $135	$ 106	611.101	183.330,24	3,4%
6	5.776	$60 to $90	$ 72	418.182	125.454,72	2,3%
7	5.776	$45 to $60	$ 49	284.641	85.392,38	1,6%
8	5.776	$30 to $45	$ 32	184.832	55.449,60	1,0%
9	5.776	$15 to $30	$ 19	112.285	33.685,63	0,6%
10	5.776	$15 to $15	$ 15	86.625	25.987,50	0,5%
				?18.198.717	?5.459.615,10	?100%

Table 7: Example of decile analysis

Source: adapted from http://www.crmtrends.com/downloads/Decile.xls

(Note: 20% of customers represent 77% of sales)

To create an extensive basis for the decision-making process, it is important that the decile analysis considers a long-term view of customer relationships. This means that the decile analysis should be regularly applied and the different results compared among each other. In this way, an organisation can develop fundamental customer-oriented strategies that contribute to revenue growth.

> *The decile analysis sorts the customer base of an organisation according to customer revenue (turnover) and then categorises all customers into ten evenly numbered segments.*

2.6 Methods combining customer equity with non-monetary customer performance measures

When non-financial information is added to financial-based customer performance measures, a clear picture of customer performance becomes transparent. This is fundamental to direct marketing, where non-financial customer-related data is necessary for deciding on whether it is worth to additional contact the customer. Customers have different purchase volumes and an organisation can optimise financial and human resources by contacting not all customers with the same effort. Finally, non-financial information on customer performance is important to decide whether customers are likely to meet sales and marketing objectives.

In the following, two approaches combining customer equity with non-monetary customer performance measures are presented: the RFM-method and customer portfolio analysis. Both instruments are useful to organisations for enhancing and promoting marketing planning and communication.

2.6.1 The recency, frequency, and monetary (RFM) analysis

The recency, frequency, and monetary (RFM) analysis summarizes customers' prior behaviour in terms of their recency (time of most recent purchase), frequency (number of prior purchases), and monetary value (average purchase amount per transaction), that is, their RFM characteristics (see Rust, 2000).

Hence, the RFM-method categorizes customers into cells and enables organisations to treat these customer segments (cells) in different ways.

In the RFM matrix, customer equity is presented in the form of the average purchase amount of the customer, i.e. the average customer revenue of each customer. Besides this financial measure, non-financial measures are also included in the RFM matrix, namely recency and frequency.

Table 8 shows an example of a RFM matrix. In this example, each customer receives a starting value of twenty-five points. The example consists of the following four factors that determine customer performance: the time that has elapsed since a customer's last purchase (recency); the number of purchases of a customer within the last eighteen months multiplied by six (frequency); the average purchase amount of a customer within three months (monetary); and the number of returns of a customer (additional factor). The lower the recency and the higher the average purchase amount (monetary), the higher the points assigned to the customer. In contrast, an increasing number of returns leads to a decrease in score. The sum-up of each score leads to a final score permitting a company to subdivide the existing customer base into several segments and using customer-focused strategies.

Starting value	25 points					
Recency in month	0 – 6 +40 points	0 – 9 +25 points	0 – 12 +15 points	0 – 18 +5 points	0 – 24 -5 points	25+ -15 points
Frequency – number of purchases within the last 18 months	Number of purchases multiplied by six					
Average purchase amount within 3 months	£0 – £50 +5 points	£0 – £100 +15 points	£0 – £200 +25 points	£0 – £300 +35 points	£0 –£400 +40 points	£ 400+ +45 points

Number of returns	0 -1 0 points	2-3 -5 points	4 – 6 -10 points	7 – 10 -20 points	11– 15 -30 points	15+ -40 points

Table 8: Example of RFM Method

Source: Link and Hildebrand (1993)

RFM analysis optimizes the response rates of a firm's marketing efforts (Hughes, 1994) because the sales and marketing strategies are better tailored to customer needs. For example, cross-selling and up-selling actions can be much more successful by focusing on customers with low recency and high average purchase amount. Information resulting from RFM analysis also supports retention-oriented tactics which typically focus on strengthening customer relationships early on, for example, by sending new customers a welcome letter, or trying to win back customers who have not been in for a while (Marcus, 1998).

Further advantages of this method are the consideration of both monetary and non-monetary factors, accessible data, and the possibility of continuously evaluating customer performance and, hence, considering changing customers' purchase volume.

A RFM-method categorises customers according to the following three factors: recency (the time that has elapsed since a customer's last purchase), frequency (the number of purchases of a customer over a certain period), monetary value (the average purchase amount of a customer over a certain period).

2.6.2 Customer portfolio analysis

The application of portfolio theory to customers is not widely accepted in practice. Most companies use product portfolios, such as the Boston Matrix, or the classic portfolio theory. However, several authors have proposed various kinds of customer portfolio analysis methods (e.g. Smith and Dikolli, 1995; Kotler, 1994; Fiocca, 1982; Smith, 2002) that assess the relative attractiveness

of customer relationships against the relative competitive position of the selling company.

In general, a customer portfolio consists of two dimensions or variables that form the horizontal axis and vertical axis of either a four-cell matrix or a nine-cell matrix. Most researchers use individual strategic variables such as cost to serve customers or profitability of customer relationships instead of composite dimensions that mainly focus on customer behaviour, product features, and characteristics of the company or industry. Hence, a customer portfolio can consider either only non-financial variables (e.g. characteristics of product or industry) or a combination of both financial and non-financial variables. When the latter is the case, customer equity can be presented in the form of customer profitability or customer revenue. Table 9 shows some examples of customer portfolio dimensions.

Dimensions of customer portfolio models	Past empirical studies of the model
Shapiro et al (1987) Cost to serve Net price (sales revenue)	Turnbull and Zolkiewski (1995)
Krapfel et al (1991) Relationship value Interest commonality Perception of relative power balance	Turnbull and Zolkiewski (1995)
Smith (2002) Relative costs Relative market share	Kotler (1994)

Table 9: Examples of customer portfolio dimensions

The process of constructing a customer portfolio includes several steps. First, the criteria for the two dimensions are determined. Then each customer is rated by these criteria and the resulting coordinates are used for plotting each

customer in the portfolio. The portfolio is then the basis for making decisions on long-term strategic market positioning.

A good example of a two-step customer portfolio is that developed by Yorke and Droussiotis (1994) (see Figure 9). In the first step, a customer portfolio is generated that enables the organisation to identify highly profitable customers. The horizontal axis of the first portfolio represents the strategic importance of each customer account (account potential, future capacity expansion, links with export markets, and account prestige) and the vertical axis represents the difficulty in managing the customer account (degree of competitor, entrenchment, payment problems, claims put forward, and buying behaviour). In a second step, the customers that are of interest to the company, for example highly profitable customers, are analysed by determining the share of a customer, i.e. by comparing the net revenue from each customer with the maximum possible revenue (vertical axis). The horizontal axis represents the strength of the relationship, which consists of seven externally-based variables, such as customer experience or speed of response, and three internally-based variables, such as the length of the relationship.

Step 1: Identifying profitable customers   **Step 2:** Analysing profitable customers
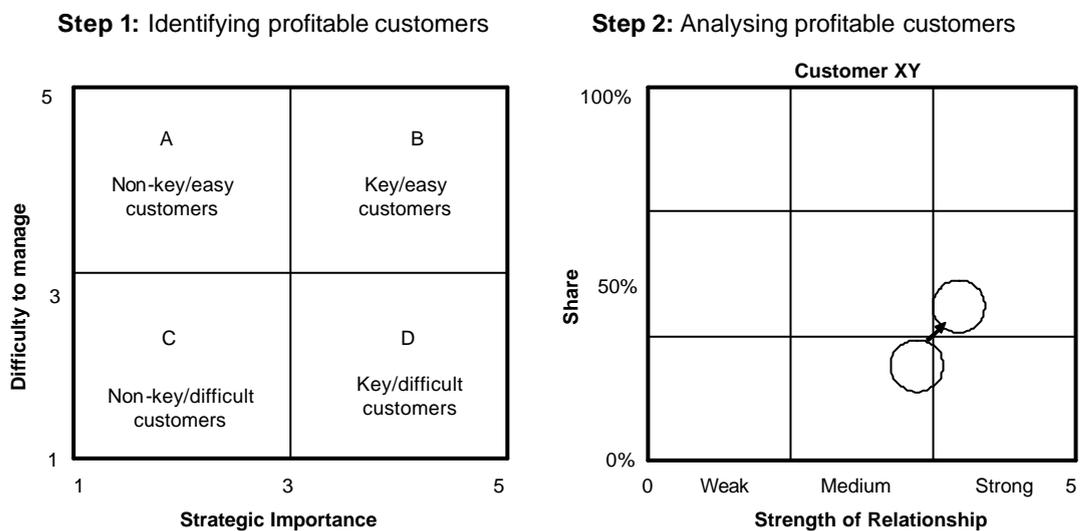
Figure 9: Example of a customer portfolio method
Source: Yorke and Droussiotis (1994)

To summarize, this customer portfolio method allows managers to develop appropriate segment-based strategies and make a financial plan for the cost-effective use of resources (Yorke and Droussiotis, 1994).

A major advantage of customer portfolio models is the fact that the type of strategic variables used for developing the dimensions are selected by the firm and, hence, reflect the firm's objectives. Due to this free choice of the variables, an organisation can use accessible data and no further investments are needed. However, the assessment of each customer according to these variables is subjective, expect for financial criteria, such as customer profitability or customer revenue. Hence, non-financial criteria implicitly involve subjective judgements and therefore become more difficult to assess. Nevertheless, they can be very useful if the aim is to sort out the major customers from the mass of customers.

Customer portfolio theory assists managers in taking decisions on the strategic reallocation of resources to enhance specific relationships in order to achieve future growth. However, an effective and detailed information system, using the range of variables described above, would need to be established in order to monitor and evaluate such resource reallocation strategies.

> *Customer portfolio theory assesses customer performance by means of strategic variables that are represented on the horizontal and vertical axis of the portfolio matrix. Examples of such variables are market share, market growth, customer costs, customer's business attractiveness, or relative stage of competitive position. Overall, the customer portfolio method enables organisations to develop cost-effective resources and make long-term customer-related decisions.*

2.7 Underlying factors for customer equity

The purpose of this section is to investigate and describe key factors of customer equity that support the development and implementation of revenue-building strategies. On the one hand, there is a strong body of research supporting the idea of market-based assets as a source of value to the customer (see Hogan et al, 2002; Sheth and Sisoda, 1999). On the other hand,

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there are two further major research streams that view value chain elements (e.g. Tierney, 2003; Forbes, 2007) and stakeholders (Payne and Holt, 1998; Flint et al, 1997) as factors of customer equity. These factors support a firm in its attempt to improve value delivery to customers and develop sustainable customer profit streams, which are equal to customer equity when summed up. However, the underlying philosophy is that customers have goals that they seek to achieve and that the role of customer equity management is to help customers achieve those goals by adapting the value sources to customer preferences.

2.7.1   Market-based assets

"The extant body of marketing orientation theory, no matter the sector in which it is applied, focuses on the processes whereby market orientation creates customer value" (McNaughton et al, 2002). Several researchers have developed conceptual frameworks in which market-based assets enhance financial performance (customer equity) by satisfying better customer needs and increasing customers' purchase volume. Despite continuous debate over the specific dimensions of market-based assets, the link to organisational performance is almost universally accepted (see, for example, Sheth and Sisoda, 1999). To throw light on the market-based assets construct, in the following, three approaches are discussed that see market-based non-relational assets as key to an increase in customer equity.

The first approach is a conceptual model of customer equity management developed by Hogan et al (2002). They suggest that to maximise customer equity, which is the sum of current and potential customer assets, an organisation can, on the one hand, optimize its customer equity management skills, and, on the other hand, combine and coordinate its nonrelational assets (see Hogan et al, 2002). Customer equity management skills include all skills needed to identify, initiate, develop, and maintain profitable relationships with customers and, hence, to enhance revenue growth. Nonrelational assets consist of a firm's tangible assets and intangible assets. Tangible assets, such as new technology, plant, and equipment; innovative and efficient supply

chains; or new product development processes improve customer assets (customer equity) by being more responsive to customer needs (Hogan et al, 2002). Intangible assets are a firm's knowledge (or potential knowledge through research and development) and influence customer assets by successfully serving customers and creating new products and services. Hence, nonrelational assets become a tool in growing the overall customer asset by providing the means (products and services) through which the firm provides value to the customer and, therefore, the customer chooses to do business with the firm.

The second approach was developed by Srivastava et al (2001) and centres in market-based processes to optimise the use of a firm's resources and to improve the delivery of superior value to customers. Market-based processes drive a firm's financial performance and lead to repurchases by transforming the intellectual and relational market-based assets of an organisation into an offering that customers prefer over that one of competitors. These market-based processes include product development management, supply chain management, customer relationship management and the acquisition, development and deployment of human resources. Besides these processes, the intellectual and relational market-based assets of an organisation are necessary for creating competitive customer-oriented offerings. Intellectual assets are the types of knowledge a firm possesses about its external (marketplace) and internal (organizational) environment and are used to develop and implement marketing, product, and sales strategies. Factors of relational assets are, for example, trust or reputation and depend on the individual firm's objectives which makes it difficult for rivals to imitate them.

The third approach is a conceptual model of market-oriented value creation developed by McNaughton et al (2002). This model identifies the steps between market orientation and value for the owners of the firm (see Figure 10). Market orientation is linked to the creation of market-based assets and other asset types, which lead to enhanced value creation for customers. Customers perceive this higher value, are more satisfied and loyal, and act as marketing agents by spreading positive word-of-mouth (Reichheld and Sasser, 1990).

Market-based assets are intellectual assets (knowledge of the market), skills and resources that are unique and difficult to imitate (Barney, 1991) so that a firm is able to build strong barriers to entry that divert competitors to higher cost or less effective strategies (Grant, 1991). The need of a non-market asset, such as a new store location or technology, can be determined by the information gathered from the market-based assets. Figure 10 depicts the process of value creation developed by McNaughton et al (2002).
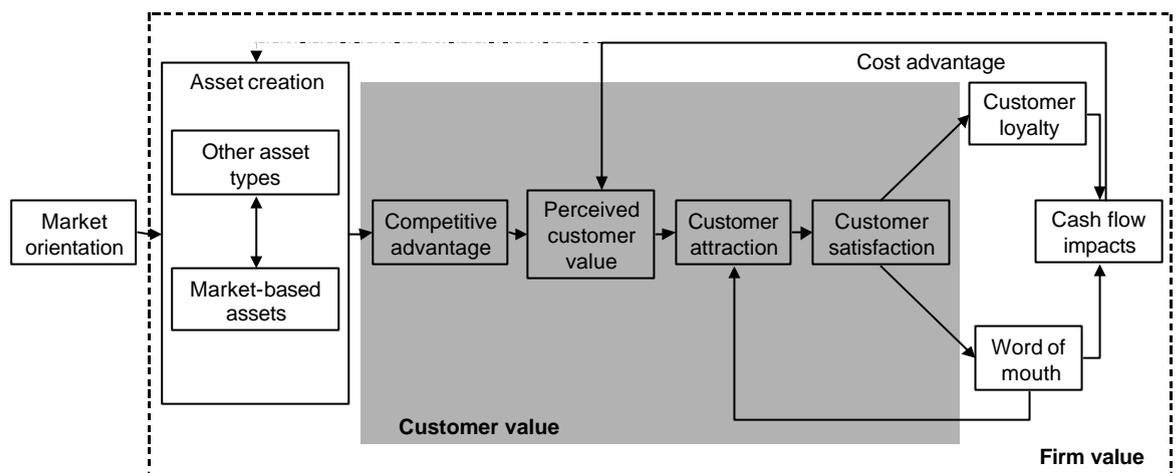
Figure 10: A model of market-oriented value creation
Source: McNaughton et al (2002)

From the above, one can imply that customer equity is influenced by a firm's tangible assets and intangible assets (Hogan et al, 2002). The term tangible assets (Hogan et al, 2002) is used interchangeably with the terms market-based processes (Srivastava et al, 2001) and non-market assets (McNaughton et al, 2002). However, all three different terms mean tangible elements, such as technology, supply chain, product development, point of sale, or human resources. The term intangible assets (Hogan et al, 2002) is used interchangeably with the term intellectual assets (McNaughton et al, 2002; Srivastava et al, 2001). Both terms mean a firm's current and potential knowledge of the market and organisation. To summarize, tangible and

intangible assets of a firm drive customer equity and, hence, a firm's financial performance.

2.7.2 *Value chain elements*

"The value chain is a tool to disaggregate a business into strategically relevant activities. This enables identification of the source of competitive advantage by performing these activities more cheaply or better than its competitors" (Brown, 1997). However, besides competition, customers as a second external source play an increasingly important role in achieving competitive advantage. Researchers, such as Holmstrom et al. (2000), add emphasis to the argument that a pure value chain focus is inadequate if an organisation seeks to add value for customers because customers form a central part of the enterprise (see also Tierney, 2003). Recently, one can observe a shift from traditional value chains to customer-oriented value chains that are centred in the creation of value for customers to maximise customer equity.

The secret of a successful customer-oriented value chain is demand-led management, which encourages managers to identify sales patterns and customer preferences and to match those by reengineering product activities, service activities, human resource activities, and marketing and sales activities, resulting in increased sales and profitability (see Forbes, 2007). In other words, each interaction with the customer provides insights in customer behaviour that can be used for adapting business processes to customer needs. This, in turn, results in greater customer satisfaction and customer loyalty, which drive customer profitability (customer equity). Hence, a customer-oriented value chain influences customer profitability.

Walters and Lancaster (1999b) suggest that by applying a differentiation analyses within the value chain, "value chain alternatives" can be considered, i.e. the firm's capacity that may create differentiation can be matched with the attributes that customers prefer most (Grant, 2002). Hence, the differentiation analysis aims at creating value for customers by reducing customers' costs or assisting customers in their own product differentiation.

In contrast to Forbes' (2007) customer-oriented value chain, Walters and Lancaster (1999a) propose gaining more favourable customer outcomes by considering a more comprehensive value chain that consists of twelve value chain elements, namely suppliers, core production, distribution, sales, marketing, service, infrastructure, finance, human resource, government relations, IT, and partnerships. Figure 11 depicts these value chain elements of an organisation and Figure 12 lists examples of value drivers of each value chain element.
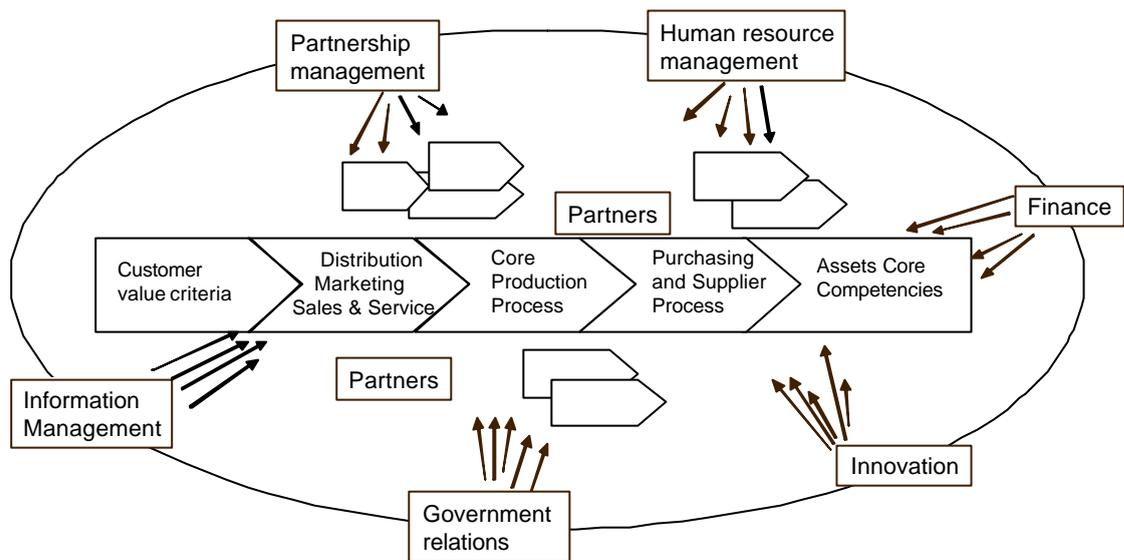
Figure 11: A customer-focused value chain
Source: Walters and Lancaster (1999a)

Value chain element	Value driver	Value chain element	Value driver
Purchasing and supplier process	Relationship quality Materials inventory costs Unit costs…	Finance	Financial gearing WACC Debt maturity Investor profile and relations Cash flow...
Core production process	Productivity Quality Time spans Unit costs…	Human resource management	Application rates Staff turnover Productivity Management Structure...
Distribution	Time to market Finished goods inventory…	Government relations	Exposure to regulatory change Lobbying capability…
Sales and marketing Sales and service	Channel complexity Channel control Market responsiveness…	Information management	IT expenditure Communications networks…
Marketing	Customer targeting Customer loyalty Customer acquisition…	Partnership Management	Number of external partners Location in the value chain…
Infrastructure Innovation	R&D Patents…		

Figure 12: Matching value elements and value drivers

Source: Walters and Lancaster (1999a)

Besides core competencies, which are a firm's competency in technology and business processes (Prahalad and Hamel, 1990), a value-creating network is the key to providing customers with superior value. A value-creating network is an association of member firms with the objective of benefiting from each other by combining the core capabilities in a most effective and efficient way so that the value delivery is maximised (see Kothandaraman and Wilson, 2001). In general, a company tends to develop strong relationships with those member firms that can add value to its core competency and market offering. The more unique the capabilities of the member firms are, the more likely it is that the company wants to develop relationships with these member firms. Such relationships can be strategic alliances, partnerships, or even mergers and acquisitions. If, for example, a company wants to improve its speed of delivery, it is likely that this company will look for member firms that have superior logistical capabilities. Hence, a value-creating network explores value chain elements for finding the right member firms that help a company to improve

value delivery to customers and enhance satisfaction, loyalty, and customer performance (Kothandaraman and Wilson, 2001).

From the above, one can conclude that a transformation of a traditional value chain into a customer-oriented value chain has an impact on customer performance and, hence, customer profitability (customer equity). This means that improvements in the value drivers of value chain elements support the degree of customer orientation in an organisational environment. Examples of such improvements can be higher productivity, less channel complexity, higher market responsiveness, or better product quality. However, the most important thing is to investigate customer preferences before transforming anything to know which value drivers should be changed and how they should be changed. Hence, developing a customer-oriented value chain assists managers in understanding individual customer profitability and analysing the drivers of customer profitability.

2.7.3 Stakeholders

"Value delivery comprises all those activities involved in delivering the product-service attributes that are considered to be necessary to create customer satisfaction and to maintain an ongoing, long-term relationship with customers and in so doing build competitive advantage" (Walters and Lancaster, 1999a). However, human beings belonging to institutions carry out value delivery and therefore play a significant role in the buyer-seller process. Such human beings are also called stakeholders that can be presented in the form of different stakeholder groups, such as competitors, employees, customers, shareholders, and suppliers. For an organisation, it is essential to base value-building strategies on the analysis of stakeholders to identify opportunities of delivering superior value to customers. These opportunities are the key to improving all important aspects of a product-service purchase and to enhancing customer profits (customer equity). The following three approaches discuss the role of stakeholders in the value delivery process.

The value-based portfolio approach developed by Sanchez and Sanchez (2005) centres in three stakeholder groups, namely the organisations (competitors), the suppliers, and the customers. According to them, an organisation is successful when it has a strong brand, attractive products and services, and a sound knowledge of its customers and competitors to provide a market offering that exceeds customer expectations. The model assumes that a high functional value would raise the market power of the organization, enhance customer loyalty, develop long-term relationships, and increase customer profits (customer equity). The functional value can comprise operational aspects such as accessibility, efficiency, customer service, communications, accuracy, or product and service quality. The model also emphasises a highly efficient distribution system and a good technology transfer between suppliers and the organisation itself to optimise speed of delivery. Overall, for being able to develop long-term relationships with customers and achieve a maximum of customer profit (customer equity), an organisation needs to provide strong and sustainable organisational values (product, brand, processes etc.) in the given competitive environment.

Payne and Holt (1998) developed a stakeholder model of relationship marketing, which focuses on three value domains (stakeholder groups): employee group, customer group, and shareholder group. By managing the key activities of each stakeholder group, an organisation can achieve a maximum of value creation, which it can deliver to each group (see Payne et al., 2000). Key activities are the attraction, the satisfaction, and the retention of each stakeholder group. Overall, the organisation receives revenues from its customers in exchange for its products and services and added value actions, such as advertising, customer advice, financing, delivery arrangements etc. For maximising customer profits (customer equity), the organisation strengthens profitable customer relationships and turns less profitable or unprofitable relationships into profitable ones.

The last approach is a framework proposed by Flint et al (1997) that aims at better satisfying customer needs and enhancing customer retention by changing trigger events. These trigger events are based on three different types

of stakeholders, namely suppliers, customers, and competitors. Supplier-located events comprise changes in product attributes (e.g. product performance or product quality), service attributes (e.g. service quality), or interpersonal attributes (e.g. personnel turnover or training). Customer-located events are changes that occur at a strategic level (e.g. reengineering), an operational level (e.g. teams or procedures), or a tactical level (e.g. point of contact). Environmental-located events occur outside of the customer's and supplier's organizations. They comprise macro environmental changes (e.g. regulatory issues), actions by competition (e.g. product or service innovations), and actions by channel members (e.g. new suppliers or new alliances). To summarize, the purpose of this model is to enhance customer satisfaction by changing and adapting the trigger events to customer needs and, hence, by increasing value delivery to customers (see Flint et al, 1997). Greater value delivery and customer satisfaction lead to a higher repurchase rate, which improves customer profits (customer equity). Figure 13 illustrates the different types of trigger events.
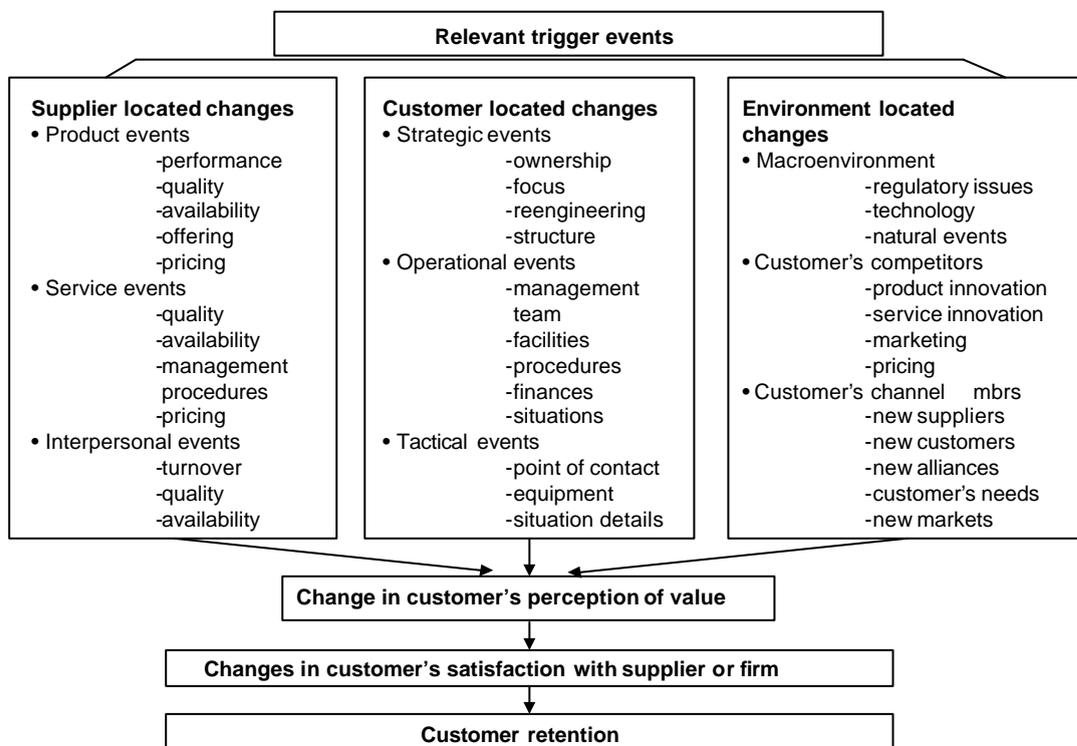
Figure 13: A value change model

Source : Flint et al (1997)

The three approaches discussed above show that in total five different stakeholder groups are important for the value delivery process. Besides the customer group, which was seen from all three approaches as necessary, Sanchez and Sanchez (2005) and Flint et al (1997) identified the competitor group and the supplier group, while Payne and Holt (1998) added the employee group and the shareholder group. By analysing these five stakeholder groups, an organisation can develop appropriate value-building strategies that strengthen relationships with customers and improve repurchase behaviour resulting in higher customer profits (customer equity). Value-building strategies should mainly focus on improving product and service attributes (Flint et al, 1997), building a strong brand (Sanchez and Sanchez, 2005), developing highly efficient business processes, and providing a good technology transfer with external stakeholders. To conclude, a sound knowledge of customer preferences, competitors' actions, and employees' behaviour supports the creation of a market offering that encourages customers to make repurchases.

2.8 The customer equity process

If the organisation's goal is to apply customer equity to its organisational environment and, hence, transform its structure into a customer equity organisation, a guide is needed for implementing customer equity step-by-step. Such a guide should provide information that helps marketing managers make better decisions in terms of developing value-building strategies and making improvements in value delivery. The process of implementing customer equity should focus on strategic insight regarding customer segmentation and selection, aggregate capacity planning, and the tie between service effort allocation, lifetime value, and service profit. In the following, existing frameworks for implementing customer equity are described.

Rust et al (2000) provide a ten-step approach to build a customer equity organisation. In their framework, investments in value equity, brand equity, and

retention equity lead to an improvement in customer lifetime value (customer equity), i.e. product quality building activities, brand building activities, and relationship building activities are of importance. The ten steps for transforming a traditional organisation into a customer equity organisation are as follows:

(1) measuring a firm's customer equity;

(2) determining a firm's key competitors;

(3) customizing the potential drivers of value, brand, and retention equity;

(4) choosing the population of interest;

(5) developing the survey instrument;

(6) collecting data;

(7) analysing the data to determine the key equities and drivers of each equities;

(8) benchmarking against competitors;

(9) determining the key areas for improvement; and

(10) determining return on equity for each improvement, and the investment in the drivers that provide maximum return on customer equity.

Considering the above, one can categorize Rust's et al (2000) approach into four main phases, namely customising value proposition (drivers of value, brand, and retention equity), selecting customers, determining improvements, and monitoring investments (see Figure 14).
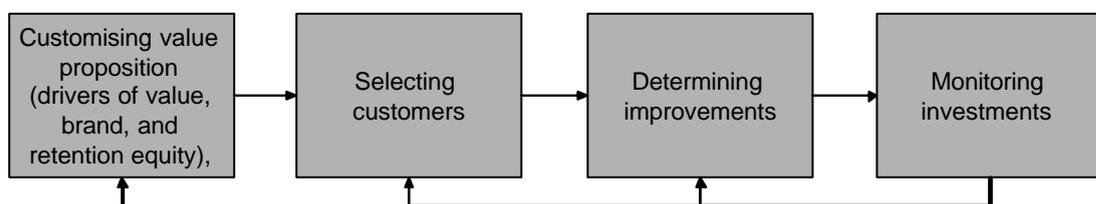
Figure 14: An approach for building a customer equity organisation
Source: own

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Another customer equity process approach is the QCi-model, which is a leading customer relationship management (CRM) assessment approach enabling organisations to measure the value delivered to their customers and to compare the results with a global benchmark (Woodcock et al, 2003). Furthermore, the QCi-model helps organisations to identify a value proposition, which exceeds that of competition. Besides involving a customer relationship management (CRM) system, this model views a company's people, processes, technology, policies, and suppliers as source of value delivery to customers. Overall, the model consists of the following phases (see Figure 15):

- *analysis and planning phase.* Segmenting customers and determining their value according to retention, efficiency, acquisition, and penetration (REAP);

- *proposition phase.* Defining value propositions for each customer segment;

- *customer management activity (CMA) phase.* Targeting, welcoming, understanding, supporting, retaining, and winning back customers; and

- *measurement phase.* Measuring the effect of all elements of the customer management activity phase, which forms the feedback into the planning process.
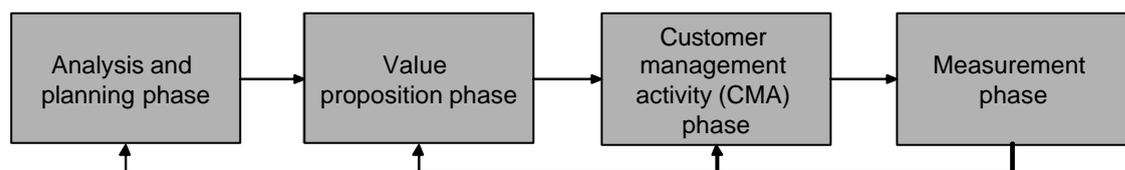
Figure 15: Phases of the QCi-model
Source: Woodcock et al (2003)

Payne and Frow (2005) have developed a process-oriented conceptual framework (see Figure 16) that illustrates five underlying processes helping organisations to develop customer relationship management (CRM) strategies and maximising customer lifetime value (customer equity). The first step is the development of the customer strategy following the business strategy, which

considers the competitive situation. In a second step, the value proposition is determined and the customer base is analysed by the customer lifetime value to identify the most profitable, less profitable and unprofitable segments. In a further step, it is attempted to provide a standard for each sales channel that creates positive customer experiences. The fourth step focuses on gathering, analysing, and applying customer information from all customer contact points to enable organisations to form marketing strategies that are suited to customer needs. Finally, the last step aims at monitoring the success of customer relationship management (CRM) strategies and ensuring a continuous future improvement in CRM activities.
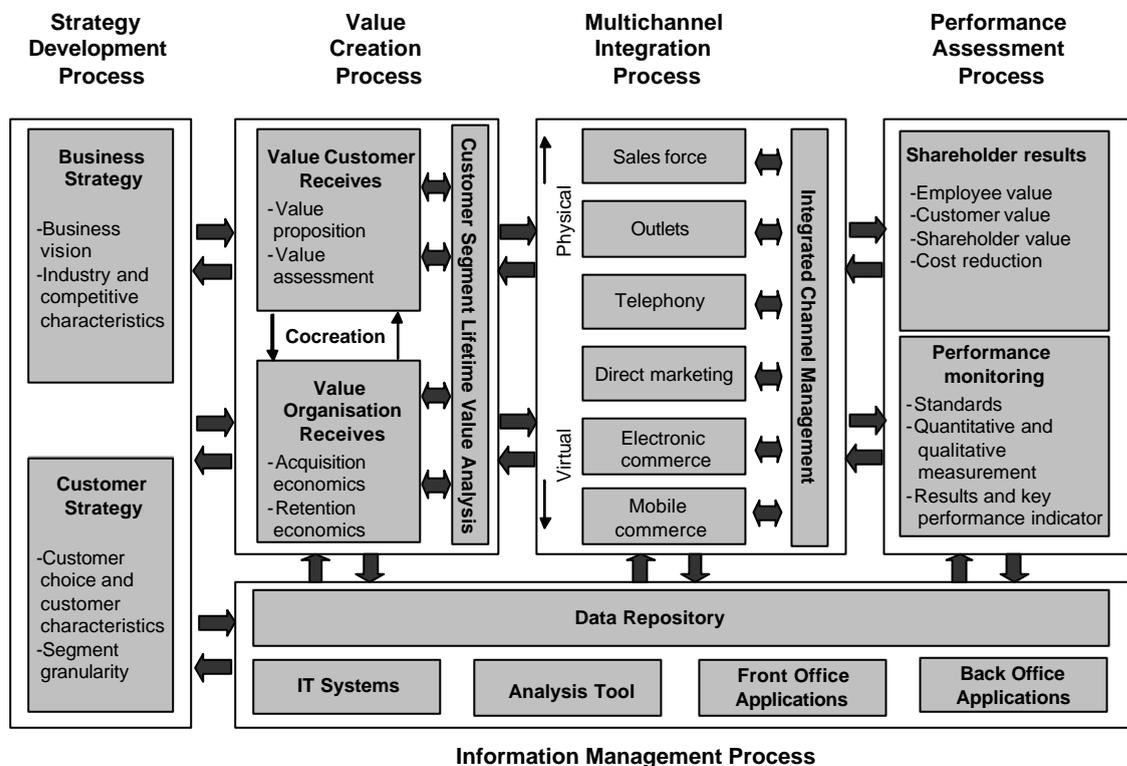
Figure 16: A strategic framework for CRM
Source: Payne and Frow (2005)

The strategic framework for CRM is graphically illustrated in a simpler way in Figure 17.

Developing customer strategy	→	Determining value proposition	→	Integrating multichannels	→	Gathering and analysing customer information	→	Monitoring performance
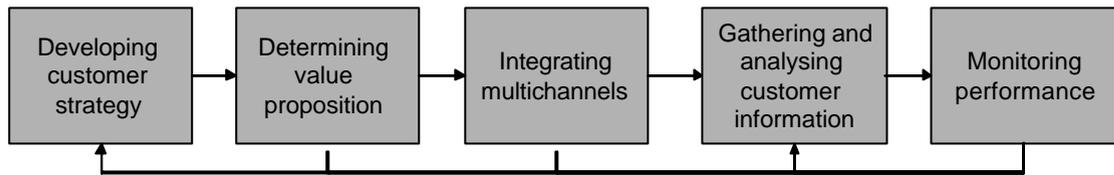
Figure 17: A strategic framework for CRM – simplified illustration
Source: Payne and Frow (2005)

A further example of a customer equity process is the framework for customer value-based strategy developed by Doyle (2004). In his framework, he proposes five steps for improving customer performance: defining the value proposition, selecting customers, customising the value proposition, developing the relationship with the customer, and building trust (see Figure 18). Feedback from the customers is generated by measuring customer loyalty, customer satisfaction, and trust. Doyle's (2004) framework assists managers in answering strategic questions, such as how to serve customers in a most efficient way or how to achieve long-term relationships with customers, by identifying the most profitable, less profitable, and unprofitable customer segments.

Value proposition	→	Customer selection	→	Customise value proposition	→	Developing the relationship	→	Building trust partnerships

Feedback:
-Customer satisfaction
-Customer loyalty
-Trust measures
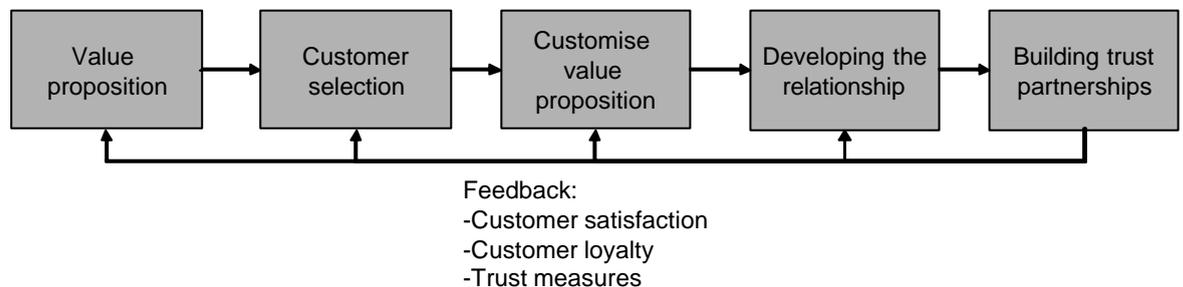
Figure 18: A value-based strategy
Source: Doyle (2004)

De Bonis et al (2003) have developed a further process of customer equity, which helps companies to organise their business, make decisions, develop their staff and business processes, and allocate capital for meeting the needs and expectations of their customers (see Figure 19). The approach comprises five steps: understanding the customer, committing to the customer, creating

customer value, obtaining customer feedback, and measuring and improving customer value. The first step is to identify customer segments by analysing the underlying value drivers that guide the buyer's decision making while the second step is to determine segment-based strategies, develop superior offerings, and identify key performance indicator. In the third step, organisations create customer value by improving customer touch points like Internet or branch, planning value-delivering processes, defining skills and competencies of staff, and investing in the infrastructure. The fourth step is to analyse regularly the reasons for won and lost business, interpret customer feedback, and resolve customer complaints. Finally, the last step is to redefine continuously customer value commitments as customer expectations are changing in the course of time.
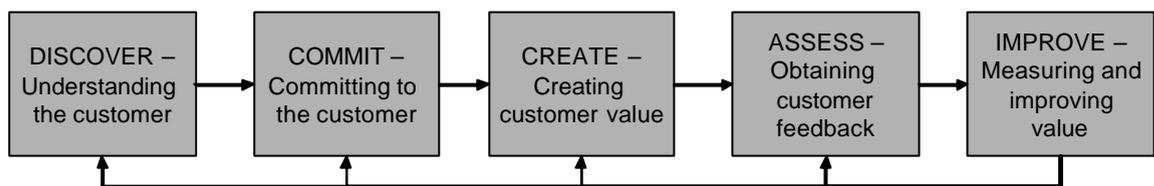
Figure 19: A value-based marketing approach
Source: De Bonis et al (2003)

2.8.1 Requirements of the process of customer equity

The process of customer equity is a framework for building a customer equity organisation, which improves a firm's customer orientation by centring in customer performance and developing customer-focused strategies. For the implementation and realisation of a customer equity organisation, several steps are necessary, namely identifying, determining, managing, and monitoring customer equity. However, such a process of customer equity also needs to meet various requirements, such as a certain degree of market orientation. In the following, three requirements of the customer equity process are discussed and applied to the approaches explained in the previous sections.

2.8.1.1 *Market orientation*

Organisations have undergone four changes in their strategic orientation in the past twenty years ranging from product and selling orientation to customer and market orientation (see Figure 20). Production orientation prioritises the production process, while sales orientation aims at increasing sales turnover by aggressive selling and promotions. Customer orientation is the process of satisfying customer needs by providing them with appropriate and competitively viable offerings (see Kotler and Andreasen, 1996). Finally, market orientation considers besides customer preferences, the competitive situation and the coordination and sharing of resources and information with other departments (see Slater and Narver, 1994).
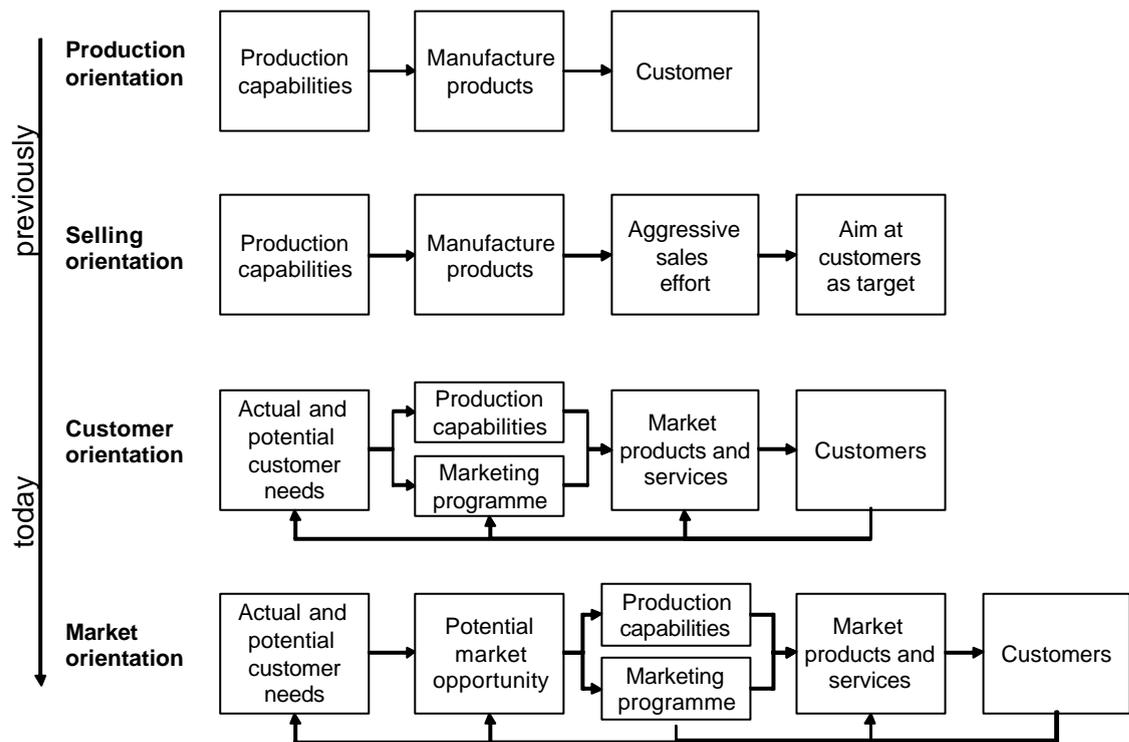
Figure 20: Types of strategic orientation
Source: adapted from Doyle (2004)

Today, market orientation is vital to the financial health of every corporation because it makes possible to track new entrants into the market and analyse

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the performance of established players. Systematic gathering and sharing of information regarding present and potential customers and competitors ascertains a firm's position within a sector because it enables a firm to respond quickly to changing customer needs and competitor activities and, hence, to improve value delivery to customers. Benchmarking competitive performance can comprise information about products and services, prices, brands, value chains, main customers, or internal procedures of competitors.

In particular, in very transparent markets where buyers can easily compare prices and product attributes, it is necessary to consider the performance of competing offerings to be able to provide an offering that delivers a maximum of value to customers. Thus, a market-oriented customer equity process would contribute to identify new value opportunities and improve value delivery of existing offerings.

2.8.1.2 Monitoring and assessment of customer and organisational performance

The dynamic process of developing internal resources and relationships with customers and suppliers is the basis for improving profit streams (and the customer equity stream) and achieving a competitive advantage in the business environment. For identifying the monetary and non-monetary benefits from this process, it is necessary to measure the performance of internal resources, such as technology, business processes, or employees, and external resources, such as customers, partners, or suppliers. Hence, the implementation of customer equity in companies requires the measurement of both organisational performance and stakeholder performance.

Such an analysis from different perspectives helps firms to compete successfully and survive in the long-term because they can apply existing knowledge and develop new knowledge that shapes the results of implemented customer equity strategies. Furthermore, an inclusion of long-term and short-term indicators in the measurement framework complements the actual forward-looking measures and gives a better picture, which supports the development of customer equity strategies. Therefore, a monitoring phase within the process of

customer equity should always consider a balanced combination of short-term and long-term indicators.

When all indicators are closely related to corporate and process goals, the communication and diffusion of strategic intent throughout the organisation is facilitated. Such a communication is extremely important to a customer equity organisation because customer orientation is only achieved when employees and management are informed and know how to realise it. Hence, it is important to link performance indicators to corporate strategic goals and continuously inform staff about the progress made.

Besides the consideration of financial indicators, the monitoring of customer and organisational performance also requires the inclusion of non-financial indicators to ensure an adequate basis for strategic decision-making. By linking the non-financial metrics to financial numbers, managers are more likely to accept such information. In particular, in the context of customer equity, non-financial information on customers is crucial.

Customer and organisational performance are a snapshot of the value of a customer or company respectively, which changes over time. Therefore, it is necessary to continuously assess the performance level by regularly updating the performance indicators. One can imply that such a regular assessment, which won increasing attention both from academic and practical circles, is also necessary for the process of customer equity.

2.8.1.3 Value-building organisational sources

For increasing customer equity, it is necessary to maximise value delivery to customers by adapting a company's value sources to customer needs and expectations. Value sources can be the organisational structure and the effective management of operations in terms of purchasing, production, marketing, sales, and logistics (see Walters and Lancaster, 2000). In other words, all elements of a firm's value chain can be used for improving value delivery to customers and, hence, maximising customer equity (Grant, 2002). As a result, customer equity is seen as a proactive development towards a

customer-oriented organisation, i.e. it contributes to the realisation of a unique selling position, which, in turn, creates a competitive advantage and improves customer performance.

Higher value delivery is only possible when a firm's value chain elements create a market offering that is better than that of competition and when these elements are characterised by continuous improvement, change, flexibility, and responsiveness to allow the organization to respond quicker to changing customer needs (see Kothandaraman and Wilson, 2001). Furthermore, to bring stability in the process of value creation and value delivery, a customer equity organisation emphasises partnerships and strategic alliances with both customers and suppliers, and focuses on relationship building through repetitive, rather than single, sales transactions. Hence, to achieve the goal of maximising customer equity, a creative mix of market offerings, processes, technologies, information resources, and people is essential that become part of the implementation of customer equity strategies.

2.8.1.4 Discussion on the requirements

In the previous sections, three requirements of a customer equity process were derived: the systematic gathering and sharing of information on customers and competitors, the regular assessment and monitoring of customer and corporate performance, and the consideration of organisational sources as basis for value-building strategies. In the following, all three requirements are discussed in the context of the five approaches described previously.

Three out of the five approaches consider market orientation, whereas the rest of them are limited to customer information and do not take into account data from competition to develop a differential advantage, although differentiation is not possible without comparing the own offering with that of competition. The three market-oriented approaches are those developed by Rust et al (2000), Woodcock et al (2003), and Payne and Frow (2005).

The second requirement is met by Rust's et al (2000) and Payne and Frow's (2005) framework. These two frameworks measure the impact of value-building

strategies on both the customer performance and the corporate performance by providing appropriate indicators. The other three frameworks use customer feedback methods and customer-based performance measures, which support the "closeness to the customer" and the degree of customer orientation among firms. However, for the presentation of a complete picture of the effects of value-building strategies on a firm, the assessment of both customer and corporate performance is necessary.

Two out of the five approaches fulfil the third requirement, namely the consideration of value-building organisational sources, which satisfy constantly changing customer expectations by creating value. Both approaches view processes, infrastructure, and relationships with employees and customers as value-delivering sources. Such sources assist managers in achieving customer equity maximisation and better targeting customers. The two approaches are proposed by Woodcock et al (2003) and De Bonis et al (2003). Table 10 provides an overview of the discussion on the requirements.

Requirements → Approaches ?	Market orientation	Monitoring of customer and corporate performance	Value-building organisational sources
Rust et al (2000)	X	X	----
Woodcock et al (2003)	X	----	X
Payne and Frow (2005)	X	X	----
Doyle (2004)	----	----	----
De Bonis et al (2003)	----	----	X

Table 10: Discussion on the requirements of the customer equity process
Source: own

One can conclude from this discussion that none of the existing approaches meets all requirements (see Table 10), which is subject for future research. The research cited here (e.g. Payne and Frow, 2005; De Bonis et al, 2003)

recognises the necessity of these requirements and emphasises the need of additional research on a conceptual framework for implementing a customer equity process that integrates all requirements. Such a framework would improve insights into the distribution of customer profitability, the sources of value delivery to customers, and the performance of competition facilitating the implementation of value-driven differentiated customer service strategies.

3 Chapter 3: Customer Equity Development From The Company Perspective

3.1 Introduction

With stronger trends such as the deconstruction of traditional value chains and customer involvement in business development, customers are playing an increasingly important role in business success. These trends are also reflected in the performance management literature and in the changing nature and character of organizational variables, which have the potential for influencing business performance. Instead of a focus on the rate of financial return, market share change, or sales growth, (Paple-Shields and Malhotra, 2001), organisations nowadays take into account more softer non-financial issues such as customer satisfaction or customer loyalty. In this chapter, section 3.2 examines the changes in performance metrics and analyses that help firms compete successfully.

Customer performance management is a concept of marketing used for analysing customer relationships and helping managers make the right strategic decisions ensuring long-term profitability of customer relationships (Morgan and Hunt, 1994; Reichheld and Teal, 2001; Brady and Cronin, 2001). By assessing customer performance, organisations can develop continuous improvement programs and build a competitive success in the global marketplace. Section 3.3 discusses theory-based customer performance approaches that aim at building long-term relationships with customers to achieve a competitive advantage and improve business performance.

Many organisations attempt to achieve a progress on customer-focused performance by implementing customer management software. Such software supports and facilitates the determination of monetary and non-monetary measures, such as customer equity. It also enables organisations to develop relationship specific activities to complete the sales process. However, the most important thing is to associate IT with business goals and processes to improve relationships with customers and other stakeholders. Section 3.4 explains

several practices that have formulated tactics for enhancing relationship building activities and improving customer orientation.

To take into account the efforts of the firms to widen their vision of the measures used within their business strategy, section 3.5 discusses the importance of non-financial customer performance measures by means of two examples. These examples are customer satisfaction and customer loyalty.

3.2 Performance measurement systems from the organisational perspective

In the 1990s, there was a tremendous shift from traditional performance metrics to more modern performance metrics that also emphasize non-financial measures. The traditional performance metrics were criticised for being inadequate for strategic decisions (e.g. Kaplan and Norton, 1992), considering only short-term financial measures (Hayes and Garvin, 1982), being too historical and backward-looking (e.g. Ittner and Larcker, 1998), and not being externally focused (Kaplan and Norton, 1992). To overcome these criticisms, new performance frameworks have been developed that include internal and external measures as well as financial and non-financial measures.

Nowadays, decisions cannot only be made on the basis of efficiency and cost indicators, such as company profit or sales. An organisation needs to consider external, developmental, and non-financial measures, such as customer satisfaction or service quality, for being able "to understand the (sometimes conflicting) objectives of its stakeholders and set its objectives accordingly" (Slack et al., 2004). Stakeholders' objectives have an influence on all business level performance objectives such as good working conditions for employees, a clean environment, community well-being, and customer and supplier relationships. Hence, it is important to organisations to use performance measurement frameworks that provide a balance between internal and external measures and between financial and non-financial measures.

The most popular methods developed under this stream are the pyramid of measures, which integrates performance through the hierarchy of the

organisation (Cross and Lynch, 1989), and the balanced scorecard (Kaplan and Norton, 1992). These methods integrate non-financial and financial performance measures with a process approach, giving greater importance to forward-looking measures such as customer equity, customer lifetime value, customer satisfaction, employee satisfaction, or defect rates. Hence, there is a trend towards a proactive closed loop control system that, on the one hand, assesses the performance of stakeholders, i.e. of customers, employees, and suppliers and, on the other hand, enables organisations to manage their performance in line with the stakeholders' objectives and their corporate and functional objectives. This reflects the importance of stakeholders such as customers who dominate demand-driven markets and, therefore, need to be investigated. In particular, customer profitability or customer satisfaction play a significant role in the decision-making process of an organisation.

So far, the first stream of research on new measurement frameworks has been discussed. Another research stream is focusing on the adjustment of financial metrics in such a way that they have more explanatory power. This second stream is discussed in the following.

Under this second stream, better financial tools have been developed that overcome the criticism of traditional financial performance measures. Examples of new approaches of measuring performance are the economic value added (EVA) and activity-based costing (ABC) (Kaplan and Cooper, 1997). In comparison with traditional measures, the economic value added takes into account the cost of capital by subtracting a company's net operating income after taxes from its cost of capital. Although EVA is criticized heavily for not being very different from traditional financial measures, such as the internal rate of return, there is a consensus that it provides a better understanding of the value creation capability of the organization.

Activity-based costing is often claimed to be superior to traditional costing methods since it reflects causality between cost object and how costs occur (Kaplan, 2006), i.e. it deconstructs costs traditionally seen as fixed. In the context of customer profitability, it is necessary to allocate costs resulting from

purchasing, delivery, accounting, and inventory to customers. Hence, activity-based costing is an ideal tool for calculating customer profitability because it allows organisations to identify costs per customer.

From the above, one can conclude that both research streams support the application of customer performance measures in an organisational environment. Therefore, one method from each research stream is discussed in the following. These methods are the balanced scorecard and activity-based costing.

3.2.1 The balanced scorecard

The balanced scorecard is a multidimensional framework that encourages the use of non-financial information by organisations. It employs a greater mix or range of measures than traditional performance metrics and provides a better process to capture and display those measures. This process is divided into four perspectives, namely the financial perspective, the customer perspective, the internal business process perspective, and the learning and growth perspective (see Kaplan and Norton, 2000). First, about 20-25 strategic objectives are identified and allocated to the four perspectives. Then one or more appropriate measures are assigned to each strategic objective. In other words, the performance measures are chosen to relate to specific strategic goals – usually documented in tables with one or more measure associated with each goal. Figure 21 shows an example of a balanced scorecard.

```
                    ┌─────────────────────────────┐
                    │ Financial perspective        │
                    ├──────────────┬──────────────┤
                    │ Goals        │ Measures     │
                    ├──────────────┼──────────────┤
                    │              │              │
                    └──────────────┴──────────────┘
```

┌─────────────────────────────┐   ┌──────────────────────────────────────┐
│ Customer perspective   │   │ Internal business process perspective │
├──────────────┬──────────────┤   ├──────────────┬──────────────────────┤
│ Goals   │ Measures   │   │ Goals   │ Measures   │
├──────────────┼──────────────┤   ├──────────────┼──────────────────────┤
│   │   │   │   │   │
└──────────────┴──────────────┘   └──────────────┴──────────────────────┘

How do customers see us?

How do we look to shareholders?

Can we continue to improve and create value?

```
                    ┌─────────────────────────────┐
                    │ Learning and growth perspective │
                    ├──────────────┬──────────────┤
                    │ Goals        │ Measures     │
                    ├──────────────┼──────────────┤
                    │              │              │
                    └──────────────┴──────────────┘
```

What must we excel at?
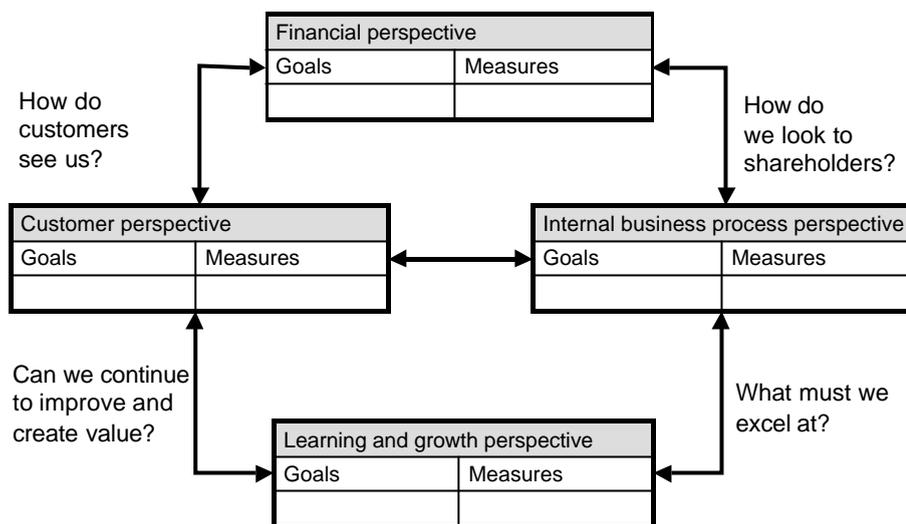
Figure 21: The balanced scorecard
Source: Kaplan and Norton (2000)

The BSC methodology ties departmental and individual performance measures into an organization's strategic planning process (Ziegenfuss, 2000) by linking them at all levels with business unit strategy (Dabhilkar and Bengtsson, 2004). It reflects company performance and progress in meeting the organisation's mission and objectives. Furthermore, the four perspectives contribute to linking long-term strategic objectives with short-term goals, translating the vision, communicating and linking business planning, and collecting regular feedback for learning purposes (Ziegenfuss, 2000). Hence, the four perspectives of the balanced scorecard provide not only information on the financial key drivers of a company but also on stakeholders such as employees and customers.

In the context of customer equity, the balanced scorecard is an important monitoring tool that helps organisations to prioritize a customer focus not only at a marketing level, but also at a management level. If, for example, the strategic objective for the customer perspective is to achieve a higher retention rate, further goals are set in the internal business process perspective. Such a goal could be higher service quality for enhancing the customer retention rate. A higher retention rate (non-financial measure) is also reflected in higher customer equity and customer lifetime values (both financial measures). Hence,

it is important to mix financial and non-financial measures in each perspective to achieve an optimal output.

In the literature, most academics support the BSC proposed by Kaplan and Norton (e.g. Basnett, 2001). This emphasises the high quality of this performance measurement framework.

3.2.2 Activity-based costing

"Activity-based costing (ABC) can assign activity costs to the product, service, or customers that consume resources in order to measure profitability and provide cost-effective and timely information better than traditional accounting systems" (Stapleton et al, 2004). By providing more accurate costing information, ABC enables organisations to distinguish between profitable and non-profitable customers and products. This means that by applying activity-based costing, the costs per customer can be calculated and used for determining customer profitability, which is the difference between the revenue and cost stream of a customer. This information is also necessary for calculating customer equity and customer lifetime value (see also Abele, 2007b). Hence, ABC supports the customer focus of a firm.

In comparison with the traditional accounting method, activity-based costing has a better classification of costs. The traditional accounting method classifies a cost either variable or fixed. By contrast, ABC assigns all costs to activities that in turn are linked to customers, services, products, and orders. Hence, ABC assists managers in understanding their business processes and their profitability in detail, particularly the profitability of customer segments. Table 11 shows the differences between the data available under the traditional method and the data available under ABC.

ABC assigns costs to activities, such as marketing or sales by using multiple cost drivers. Examples of cost drivers are labor hours, machine hours, material processed, or units produced. The costs of each activity are calculated by multiplying the number of units of cost driver with the rate per unit of cost driver

for each activity (see Table 11). These activity costs are then assigned to customers, services, products and orders (see Stapleton et al, 2004).

Traditional accounting method:			
	Volume measure	Rate (€)	Order cost (€)
Variable	500 hours	€ 15 / Direct labour hour worked in sales	€ 7,500
Fixed	-	-	€ 31,000
Total			€ 38,500
ABC:			
Activity (sales service)	Units of cost driver	Rate per unit of cost driver	Order cost (€)
Cost of volume discounts	150 / Number of discounts	€150 / number of discount	€22.500
Cost of field service to maintain products	50 / Number of telephone calls (NOTC)	€10 / NOTC	€500
Cost of sales support	100 / Number of visits (NOV)	€11 / NOV	€11,000
Total			€ 34,000

Table 11: Comparison of traditional accounting method with ABC
Source: own

The example in Table 11 clearly shows that the expenses for the sales services calculated with the traditional accounting method are much higher than those calculated with activity-based costing. This emphasises the accuracy of ABC, which facilitates the decision-making process related to profitability. ABC lists all activity costs necessary for serving a customer and is therefore a good tool for monitoring the business of improving processes. It provides the marketer with information on the impact of possible changes on customer profitability.

Researchers, such as Plowman (1997), propose a classification of the costs of all corporate resources into four headings, namely infrastructure, sustaining, support, and frontline. Under infrastructure, all costs of being in business are listed, for example, performing the annual audit or expense of electricity. "Sustaining" are costs for ensuring future business, such as product

development. "Support" are costs resulting from doing business, such as expenses of training. Finally, "frontline" comprises all activities that have a direct impact on products, services, customers, and orders. One can conclude that it is important to organisations to define main activities to understand how resources are used.

However, a detailed cost analysis through ABC is justified if the cost of obtaining and maintaining information is not excessive and thus not too expensive. An organisation must always balance costs for the analysis and the revenues resulting from improvements to justify the usefulness of ABC in developing and making strategic decisions that positively influence customer profitability.

3.3 Theory-based considerations of customer equity approaches

The aim of a theory-based customer performance approach is the identification of customer needs and preferences. This information is then used for developing appropriate products and services, which, in turn, enhance customer performance. In this context, customer performance is defined as a monetary measure, such as the customer lifetime value or customer profitability. Customer lifetime value, which is the total discounted net profit that a customer generates during his life, can be summed over all of the firm's customers to calculate customer equity.

Three types of theory-based customer performance approaches have been identified in this thesis, namely relationship marketing, customer orientation, and market orientation. These three approaches have one thing in common, they all aim at building long-term relationships with customers to achieve a competitive advantage and improve business performance. Furthermore, all three approaches view the creation of a customer-oriented organisational environment as crucial to an increase in customer profitability.

However, there are also differences between these approaches. Relationship marketing is an approach that builds long-term relationships with customers through identifying customer segments and appropriate marketing strategies. In

contrast to market orientation and customer orientation, which view information gathering as primary success criterion, relationship marketing focuses on relationship-building strategies such as loyalty programmes or customer contact programmes.

Market orientation is a combination of customer orientation, competitor orientation, and inter-functional co-ordination (Narver and Slater, 1990). In contrast to customer orientation, which considers only customers, **market orientation also takes into account the competitive situation, and the co-ordination and sharing of resources with other departments**. Despite these differences, both approaches are seen as the basis for organizational learning and for achieving a competitive advantage (Slater and Narver, 1995). Figure 22 provides an overview of all three approaches illustrating graphically the differences between them.
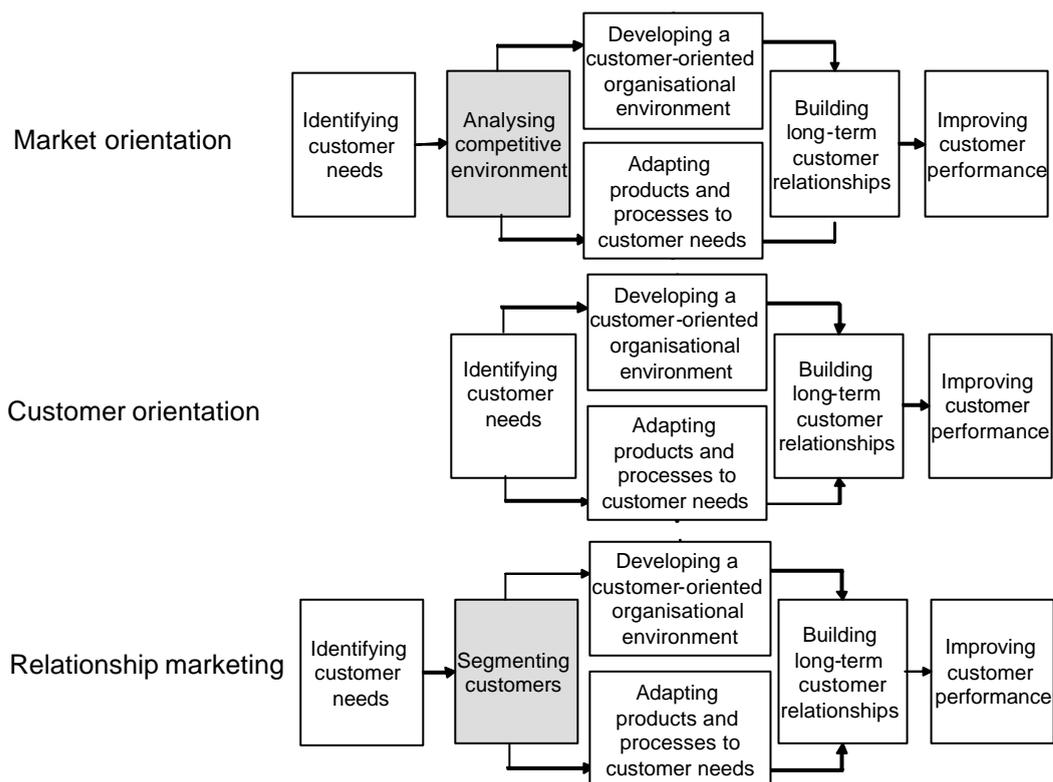
Figure 22: Differences between theory-based customer performance approaches
Source: own

3.3.1 Relationship Marketing

The term relationship marketing is not clearly defined in the literature. However, most authors explain relationship marketing as the **identification, development, and maintenance of long-term relationships with customers and other stakeholders** (e.g. Morgan and Hunt, 1994) to gain a competitive advantage (see also Wright, 2007). These stakeholders can be internal markets, customers, referrals, suppliers, influencers, and employee recruitment markets (see Christopher et al, 1991).

Relationship management can be viewed from a tactical level, a strategic level, and a philosophical level. The tactical level sees relationship marketing as a technology that is similar to data mining, i.e. relationship marketing means identifying purchase patterns and segmenting customers. The strategic level attempts to maintain customers through legal, economic, technological, geographical, and time bonds. Finally, the philosophical level focuses on customer relationship life cycles and transforms marketing towards customer orientation, competitor orientation, and inter-functional coordination (see Palmer, 1996). Hence, relationship marketing means identifying valuable customer segments through technology, developing strategies that meet the needs of those customer segments, and transforming the firm into a customer-oriented organisational environment.

In the 1990s, the marketing exchange process has shifted from transactions to relationships (Shapiro, 1991) and the academics started to investigate relationship marketing. In contrast to product-oriented transaction marketing, relationship marketing is a long-term investment in customers and encourages customer contact. As long-term relationships with customers are difficult to imitate by competitors, an organisation achieves a competitive advantage by using relationship marketing.

Relationship marketing has a positive impact on customer profitability because it increases cross-selling potential, which, in turn, leads to increased sales. In particular, profitable customers are more likely to be loyal (see Reichheld and Teal, 2001) and to purchase further products. One can conclude that the key

concept of relationship marketing is to increase customer retention. To achieve this objective, Payne (1995), for example, has developed a framework, which centres value delivery to customers. His so-called relationship management chain outlines four steps to create long-term relationships:

- defining the value proposition;

- identifying appropriate customer segments;

- designing value delivery systems; and

- evaluating their value performance.

Several other authors also see value delivery to customers as a cornerstone of relationship marketing (e.g. Woodruff, 1997).

Relationship marketing focuses on customers and encourages customer contact. By knowing more about customers, organisations can identify, develop, and maintain long-term relationships with customers and other stakeholders.

3.3.2 Customer orientation

In the literature, a customer-orientation philosophy is defined as "**success that will come to that organization which best determines the perceptions, needs, and wants of target markets** and satisfies them through the design, communication, pricing and delivery of appropriate and competitively viable offerings" (Kotler and Andreasen, 1996). Hence, in large part, customer orientation means that companies are continuously learning from changing customer needs and can, therefore, offer services and products that are more adapted to customer preferences (Brady and Cronin, 2001; Day, 1994; Davies, 1998). In general, it can be said that the more information is available the more a firm can adapt to customer needs. This creates long-term relationships and increases customer satisfaction (Slater and Narver, 1995), which, in turn, results in company growth.

It is widely acknowledged that customer-oriented firms achieve a higher level of business performance outcomes than those that are product-oriented (Sawhney

and Piper, 2002). This means that customers prefer organisations with a high level of customer orientation because they better satisfy their needs. Furthermore, organisations that regularly measure customer performance through, for example, customer equity or customer lifetime value, attempt to achieve a high level of customer orientation. In doing so, such organisations need to continuously improve employee training, management support, internal communication, personnel management, and external communication involvement (see Conduit and Mavondo, 2001).

Besides human and communicative capabilities, technical capabilities are necessary for achieving customer orientation (see Baker, 2002). One can conclude that customer orientation requires

- a structural change (Baker, 2002),

- a transformation of the staff into a customer-focused team (Baker, 2002),

- an emphasis on teamwork skills (Homburg et al, 2000),

- more employees that possess high levels of capability, motivation, empowerment, and strategic intent (Doyle and Wong, 1998),

- more flexibility in being able to respond to changing business conditions (Homburg et al, 2000),

- a main emphasis on planning customers' needs and researching markets continuously to reflect what the customer wants (Brady and Cronin, 2001), and

- a change of the organisational accounting systems, information systems, and reward systems to facilitate a division into customer groups.

> *Customer orientation means that organisations focus on customers and continuously learn from changing customer needs. As a result, they can offer services and products that are more adapted to customer preferences. This, in turn, results in organisational growth.*

3.3.3 Market orientation

The idea of market orientation as a unifying focus for the organization has prompted considerable research (e.g. Kirca et al., 2005). By collecting and sharing information about the customers' needs and competitors actions, an organization can be sensitive to customer needs, responsive to competitor threats, and prepared to respond rapidly (Kohli and Jaworski, 1990; Kulp et al., 2004). A "market-driven culture supports the value of thorough market intelligence and the necessity of functionally coordinated actions directed at gaining a competitive advantage" (Day, 1994). Hence, market orientation means gathering data on customer markets and competitors and viewing this information from a strategic perspective.

Besides this strategic perspective, market orientation can also be viewed from a behavioural perspective, a cultural perspective, and a system-based perspective (see also Becker and Homburg, 1999; Helfert et al, 2002). The behavioural perspective comprises the process of gathering information about customers, i.e. it analyses an organisation's information-related behaviour. The cultural perspective encourages the importance of the corporate culture for creating value in a most effectively and efficient way. The third perspective, a system-based view, points out the need of a market-oriented management system. Hence, successful market orientation requires a change in behaviour, corporate culture, and IT.

In general, market-oriented firms tend to be more innovative and more successful (Han et al, 1998) than product-oriented firms. Market orientation also encourages value delivery to customers because more information about customers and competitors is available (e.g. Day, 1994). A correlation between market orientation and business performance has been proved in several studies (e.g. Pitt et al, 1996; Boles et al., 2001; Jaworski and Kohli, 1993).

Market orientation is extremely important for value creation for customers because the information about customers and competitors can be used for exceeding value delivery of competitive organisations and thus attracting more

customers and better satisfying existing customers. This leads to an increase in buying, customer profitability, and company profit.

To summarize, market orientation is the coordinated application of interfunctional resources, the ability of the organisation to gather and share systematically information, and the communication of this information across departments as a basis for decision-making (Dobni and Luffman, 2000).

Market-oriented organisations consider not only customer needs, but also their competitive environment to gain a competitive advantage. They then share this information among their departments to co-ordinate their human and technical resources. Thus, information gathering is much more complex in market-oriented organisations than in product-oriented organisations.

3.4 Technology-based considerations of customer equity approaches

Technology-based customer performance approaches, such as customer relationship management (CRM) or data mining, aim at enhancing customer relationships through a better understanding of customer behaviour. Organisations can then form more effective strategies that better target customer needs and improve customer's willingness to buy. The main difference between CRM and data mining is the fact that besides the analysis of customer data, CRM additionally automates the process of interacting with customers, i.e. it supports sales automation, marketing automation, and service automation. Furthermore, both approaches offer the possibility of calculating customer lifetime value, customer profitability, and customer equity.

The CRM architecture consists of three areas: back-end systems, data-handling technology, and front-end systems (see Figure 23). The back-end operations include all enterprise wide applications, such as SAP or SQL-databases, that deliver the data and information about the customers. Customer data can be transaction data (e.g. price paid, products purchased), contact data (sales and service requests), or descriptive data on customers (e.g. age, salary, gender). The data-handling technology consists of a data warehouse's database that

collects the whole customer information and data mining tools that are then used to analyse the data and generate appropriate reports and graphs. Finally, front-end systems like campaign management automate the processes of sales, marketing, and service.

To summarize, a CRM systems also incorporates a data mining tool for analysing customer data. Both CRM and data mining are based on a data warehouse that provides them with customer data and company data. The role of a data warehouse to generate and collect data from the whole organisation is an important one. Through a data warehouse, the variety and the freshness of the data can be regulated. However, both tools make it possible to target the right customer at the right time with the right offer, for saving time and effort, and putting the organisation's marketing resources to its best use.
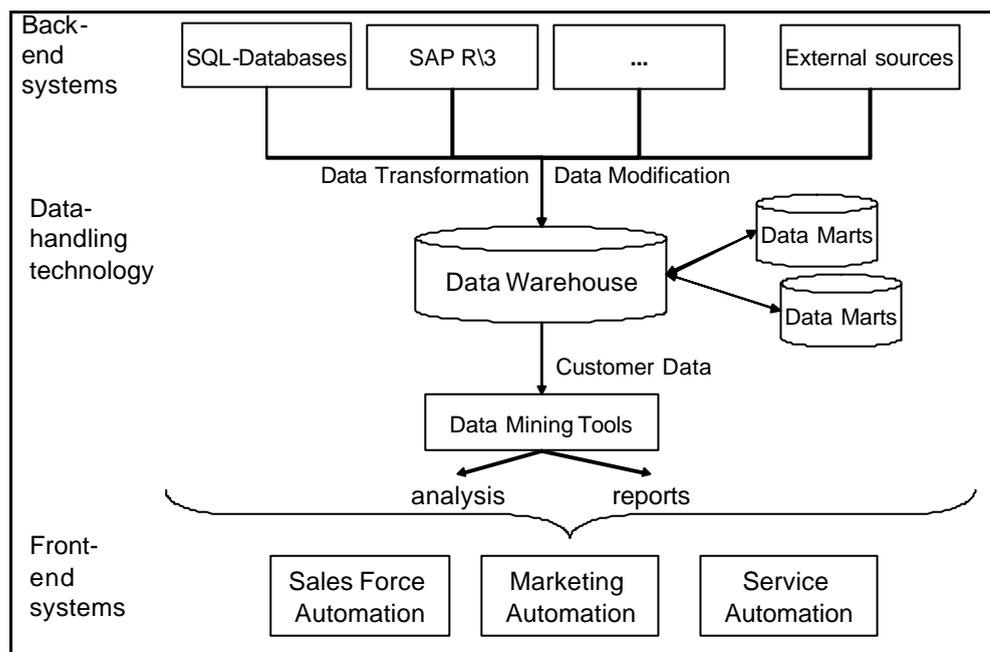
Figure 23: The CRM architecture
Source: own

3.4.1 Customer relationship management

In the literature, there is no generally agreed definition of customer relationship management (CRM). On the one hand, customer relationship management is seen as **a technological innovation in the form of software** (e.g. Xu et al, 2002) and**, on the other hand, it is seen as a specific business strategy for different customer treatment** (e.g. Kracklauer et al, 2001; Woodcock et al, 2000).

From a technological perspective, the main aim of CRM is to automate the processes of sales, marketing, and service (see also Abele, 2006). Sales force automation is achieved by using forecast reports on all phases of the sales cycle, having access to customer contact details, contact history, and using contact management tools. Marketing automation comprises all strategic and operational processes that are necessary for forging and nurturing strong customer relationships. Service automation means that the service teams can track, manage, and resolve all customer issues, including technical support and product delivery by having a look at the CRM screen.

To summarize CRM aims at automating the processes of sales, marketing, and service resulting in the following benefits:

- better contact management through automated customer contacts,

- easier development of products and services that match customer needs,

- quicker responses to customer questions and complains, and

- better access to information on sales, marketing, and employees as needed to better serve the customer (see Bannon, 2001; Xu et al, 2002).

By implementing CRM, the firm primary aims at understanding and influencing customer behavior through meaningful communications in order to improve customer acquisition, customer retention, customer loyalty, and customer profitability (Swift, 2001). It is widely acknowledged that CRM software performance (as measured relative to expectations) has a positive relationship with both ROI and company profitability (Ang and Buttle, 2006), if the company develops and realises the right CRM strategy. Hence, the financial success of a

CRM system is strongly dependent on the right interpretation of customer data and the degree of automation resulting from CRM.

From a theoretical perspective, CRM or "customer management is about finding the right customers (those with an acceptable current and future net value), getting to know them (as individuals or groups), growing their value (if appropriate), and retaining their business in the most efficient and effective way" (see Woodcock et al, 2000). In doing so, organisations should consider three main steps: acquiring new and profitable customers by offering them superior products with outstanding service, improving the profitability of existing customers by cross and up-selling, and retaining profitable customers by applying specific and focused marketing (Kracklauer et al, 2001).

Besides measures, such as cross-selling potential, product penetration, customer retention rate, customer reactivation, channel penetration, customer purchase volume, or purchase amount per customer, a CRM system also calculates customer profitability, customer lifetime value, and customer equity. Hence, CRM facilitates the identification, the development, and the monitoring of customer management strategies by regularly tracking these measures.

From the above, one can conclude that technology is certainly one of the key enabling or supporting factors in CRM, but by itself it does not constitute CRM (Starkey et al, 2002).

> *Customer relationship management helps companies to get information about customers and to use this information for better meeting customer needs and preferences. It improves communication with customers, makes it possible to develop more personalised products, supports quicker responses to customer questions and complaints, increases customer satisfaction, and improves customer profitability.*

A framework for measuring customer performance and monitoring customer management is the QCi's REAP concept developed by Woodcock et al (2003). This concept provides a range of financial and non-financial performance measures that helps organisations to manage their customers. R stands for retention performance and includes customer retention rates and customer

satisfaction or commitment. E stands for efficiency performance and comprises the costs to serve a customer and the efficiency of media optimisation. The third letter, the A, stands for acquisition performance and includes measures, such as the quantity of customers acquired or the quality value of customers being acquired. Finally, the last letter of the word REAP, the P, comprises share of wallet which is the amount of the product category that is being sold to customers as a percentage of the available spend, and the number of products an organisation have sold to each customer versus market norms.

In this context, it is important to note that only few companies determine figures, such as number of new customers, number of reactivated customers, or number of inactive customers although this would be useful, especially on a monthly basis. Table 12 shows some examples of customer performance measures used in the QCi's REAP concept.

Customer acquisition rate = (number of new customers / number of all customers) * 100
Market penetration rate = (number of customers / total consumers in the market) * 100
Customer retention rate = (the number of customers still buying in period two / the number of customers who bought in period one) * 100

Table 12: Examples of customer performance measures

Organisations frequently use customer performance measurement frameworks, such as the QCi's REAP concept, to determine and manage the financial and non-financial performance of their customer base.

3.4.2 Data mining

"Data mining provides an effective approach to discover and understand patterns in customer behavior thereby helping the decision maker to better group customers" (see Hoontrakul and Sahadev, 2008). Leading data mining products can be integrated into today's complex information technology environments. They use techniques, such as clustering for identifying relevant patterns and relationships between variables, e.g. region or product, and customer behaviours. Hence, data mining is used for automating the detection of relevant patterns in a database and segmenting customers. For an organisation, it might be of interest to know which persons prefer to buy a particular product. If these persons are, for example, young people between 30 and 40 years, the organisation can adapt the product features and advertising campaigns to the needs of this target group and thus better attract customers' attention.

One can imply that data mining helps organisations to align marketing campaigns more closely with the needs, wants, and attitudes of customers and prospects. The closer data mining and campaign management work together, the better the business results, i.e. the higher buying, cross-selling, and customer profitability. It is important to combine customer behaviour with financial indicators, such as profit or cost, to give the marketer a sense of context that can quickly ground the results in reality.

By using data from a database, usually a data warehouse, data mining builds scores that predict customer behaviour such as cross-selling potential. Each record in the database represents a customer and is evaluated with a score, which is a numerical value. For example, if a model predicts customer attrition, a high score indicates that a customer is likely to leave, whereas a low score indicates the opposite. After scoring a set of customers, these numerical values are used to select the most appropriate prospects for a targeted marketing campaign (see Berson et al, 2000).

Similar to CRM, data mining supports the calculation of key indicators such as customer lifetime value, customer profitability, or customer equity.

3.5 Non-financial measures of company determinants of customer equity

In the 1990s, there was a tremendous shift from pure financial performance metrics to approaches that also emphasize non-financial measures. With the implementation of customer management software, many executives perceive the importance of non-financial customer performance measures and use them extensively. For example, Standard Chartered, a British financial services organisation, presents its results of the business year on its Website in the form of financial and non-financial measures. The firm highlights its successful year by providing a Consumer Banking Loyal Index that gauges customer satisfaction and loyalty to the products and services. A further index, the Wholesale Banking Service Quality Index, measures customer satisfaction and engagement with Standard Chartered relative to the best competitor bank in each of the key markets.

However, besides customer loyalty and customer satisfaction, other non-financial customer performance measures exist. Table 13 provides an overview of both financial and non-financial customer performance indicators.

Financial customer performance measures	Non-financial customer performance measures
- Customer turnover	- Customer complaints
- Market share	- Customer retention rate
- Customer profitability	- Average number of repeat purchases
- Customer lifetime value	- Customer satisfaction
- Customer equity	- Customer loyalty
- Costs per customer etc.	- Customer perceived value etc.

Table 13: Examples of financial and non-financial customer performance measures

Source: own

In the following, the most popular non-financial measures, namely customer satisfaction and customer loyalty, are discussed.

3.5.1 Customer loyalty

Customer loyalty expresses an intended behavior related to the service or the company. In the literature, customer loyalty is mainly defined as repurchase behaviour (see for example Gwinner et al, 1998). According to Kandampully (1997), customer loyalty, is "the process of keeping customers longer reflecting an organisation's commitment to its customers - to think, anticipate and innovate products and services in accordance with customers' evolving needs".

Conceptually, **loyalty strategies seek to build stronger and more durable relationships with customers** (Duffy, 1998). The objective of terms such as customer relationship management, relationship marketing, or retention marketing is to build customer loyalty (Duffy, 2003). Bowen and Chen (2001) propose a classification into three approaches: behavioural, attitudinal, and composite measurement of loyalty. The behavioural measurements consider consistent, repetitious purchase behaviour. Attitudinal measurements use attitudinal data to reflect the emotional and psychological attachment inherent in loyalty. The third approach, composite measurements of loyalty, combine the first two dimensions and measure loyalty by customers' product preferences, propensity of brand-switching, frequency of purchase, recency of purchase and total amount of purchase (Hunter, 1998).

Customers are loyal due to satisfaction, high switching barriers, trust, and / or lack of real alternatives (Ranaweera and Prabhu, 2003). When switching barriers, such as search costs, transaction costs, learning costs, are high, firms may continue to retain customers even if they are not highly satisfied.

In comparison to customer equity, which is a monetary-based performance indicator, customer loyalty is a non-monetary measure and easier to calculate because the necessary data is better accessible. In general, organisations use the following formulas:

Customer loyalty = average number of repurchases (per customer segment), or

Customer retention rate = (the number of customers still buying in period two / the number of customers who bought in period one) * 100

Customer loyalty has been found to be directly related to corporate profitability (Bowen and Chen, 2001; Reichel and Sasser, 1990) and provides, therefore, a key source of competitive advantage for companies. Considering the fact that corporate profitability is the sum of all customer profitability ratios, one can imply that customer loyalty has also an impact on customer profitability. This means that the cost stream of loyal customers is lower than that of non-loyal customers because loyal customers already know the product and cost less to serve (Duffy, 2003). Additionally, they will provide strong word-of-mouth and provide reference (Duffy 2003). On the other hand, loyal customers generate higher revenues because they are more likely to buy further products. Furthermore, loyal customers are less price conscious than new customers are and spend in more expensive products, which leads to higher margins (see Reichheld and Teal, 2001; Duffy, 2003). To summarize, loyalty generates lower cost streams and higher revenue streams resulting in higher customer profitability.

> *Customers who are highly satisfied with the product want to stay with that company and have no interest in switching to competitors. These customers are loyal and contribute to company profitability as they cost less and buy more frequently.*

3.5.2 Customer satisfaction

In the literature, there is no unique definition of customer satisfaction. Some researchers define customer satisfaction as transaction-specific (e.g. Cronin and Taylor, 1992). Other researcher view customer satisfaction as an overall evaluation based on the total purchase consumption and experience (e.g. Anderson et al., 1994) (cumulative measure). The cumulative satisfaction approach assumes that satisfaction is determined by satisfying or dissatisfying encounters with a product or service over time while the transactional approach emphasizes encounter satisfaction, that is, satisfaction with a product or service in a single transaction. In general, researchers see customer satisfaction as a measure that identifies customer needs and expectations (e.g. Zeithaml and Bitner, 2000).

Customer satisfaction can improve a company's financial performance (e.g. Rucci et al, 1998) and strongly correlates with customer loyalty (Rust et al, 1995). It is proved **that when satisfaction reaches a certain level, loyalty increases dramatically**; at the same time, when satisfaction declined to a certain point, loyalty dropped equally dramatically (Bowen and Chen, 2001).

Customer satisfaction is a post-decision customer experience while customer equity measures the monetary stream resulting from the purchase of a product. Furthermore, customer equity is an organisation's assessment of customer's financial performance, whereas customer satisfaction means that customers assess the company performance. Hence, customer satisfaction differs strongly from customer equity due to the different perspectives.

Similar to customer equity, customer satisfaction should be regularly assessed to ensure a good basis for strategic plans and decisions (see Katcher, 2003). The main reason for a continuous assessment is the changing customer experience that influences customer satisfaction. Regarding customer equity, it is important to estimate the continuously changing purchase volume of customers.

Customer equity views the monetary performance of customers, whereas customer satisfaction measures the satisfaction of customers with factors, such as competence, employees, reliability, product innovation, value for money, physical environment, availability, and convenience (Athanassopoulos et al, 2001; Cronin and Taylor, 1992). In general, each factor is presented in the form of a single question or multiple questions on the customer-satisfaction questionnaire: "Overall, how satisfied are you with … [the product]?". Responses for all satisfaction questions can be made on 1-7 Likert-type scales labelled "very satisfied" (1) and "very dissatisfied" (7) at each extreme.

Traditional customer satisfaction research typically takes a generalist view of the customer base and hence does not consider different customer segments. This disadvantage should be avoided because it is important to organisations to know the different degrees of satisfaction of each segment. By segmenting customers according to their profitability, organisations can better improve

revenues from customers through adapting sales and marketing strategies to the needs of each customer segment.

Overall, organisations that focus on customer satisfaction consider the following points (see Boyd, 2001):

- delivering a product that the customer desires or needs;

- delivering quality consistent with the price;

- delivering the project in a timeframe the customer desires or needs;

- delivering the desired degree of feedback that the customer desires; and

- having a system of conflict resolution that is fair to both the customer and the business.

In general, researchers see customer satisfaction as a measure that identifies customer needs and expectations. It is widely acknowledged that increased customer satisfaction augments customer loyalty. To enhance customer satisfaction, organisations should improve factors such as convenience, good value for money and availability.

3.6   Concluding remarks

In today's turbulent environment, customers are playing an ever more important role in business competition, and many means have been advocated of understanding customer performance from both the non-financial and financial perspective, so that an optimum result can be achieved and translated into business strategies and actions. Organisations insist on complementing financial performance with a view on non-financial performance because they want to have more detailed information about customers for identifying ways to reduce costs of serving the customer, for redesigning and developing products, and for reconstructing their process of service and sales. Furthermore, to be able to focus their resources on the "right" customers and to remain competitive, organisations tend to orientate themselves to the financial contribution of customers to their business growth.

A revolution in performance measurement has thus emerged driven by stronger competition and an increasing importance of satisfying customer needs. Performance metrics, such as the balanced scorecard (BSC), view business performance from different perspectives and thus facilitate strategy development and decision making. In particular, the utility of non-financial data, such as customer satisfaction or customer's purchase behaviour, leads to improved decisions that help organisations to survive in the long-term.

As activity-based costing (ABC), a further performance metric, improves cost transparency in organisations, it contributes to cost optimisation by means of the analysis and reduction of activity costs. This has a positive influence on business performance. Furthermore, activity-based costing provides a basis for business process re-engineering (BPR) or restructuring leading to long-running changes in the business environment. These changes help an organisation to become more customer-oriented and to better satisfy customer needs. Furthermore, ABC is a tool that makes it possible to calculate costs per customer and thus to determine customer profitability and customer lifetime value. Hence, one can imply that ABC is the key to a successful realisation of customer performance measures.

The calculation of customer equity, customer lifetime value, and customer profitability is strongly dependent on the state of IT within an organisation. Hence, IT played an important role in emerging performance measurement approaches and customer performance measures. With improved IT infrastructure, new measurement practices that aim to aggregate the operational-level metrics into strategic-level metrics became possible to implement.

Theory-based customer performance approaches, such as relationship marketing, market orientation or customer orientation can mainly be realised by using technology. For a successful application of these approaches, customer data is necessary, which are only accessible if large databases in an organisational environment exist. This means that IT, such as data mining or

customer relationship management (CRM), is important for building long-term relationships with customers and improving customer performance.

4 Chapter 4: Theory And Company Perspective Of Customer Equity For Market Orientation

4.1 Introduction

A number of constructs (see Section 2.8) related to the process of applying customer equity have been developed and explored in marketing, to include *customer segmentation, value proposition, value-building strategies*, and *assessment of performance* (Rust's et al, 2000; Doyle, 2004, Woodcock et al, 2003; De Bonis et al, 2003; Payne and Frow, 2005). However, not these frameworks for customer equity management address all four constructs and their potential benefits. What is missing is the integration of a customer equity process in terms of defining variables, and their interrelationships and outcome measures. This chapter draws together the components of customer equity from Chapters 2 and 3 and investigates how at a strategic marketing level, customer equity can be employed to improve the marketing orientations of firms.

In view of this, it appears important to investigate the concept of customer equity at a strategic marketing level to assess and enhance the overall financial value of a firm's customer base. Superior value for customers is created when an organisation's offer is qualitatively better and more cost-effective than its competitors' offers (Woodruff, 1997). This means that the process of creating customer equity is based on market orientation, customer orientation, complex organisational sources, and business processes supporting the development of those innovations/strategies that might reduce the lack of profits of particular customers or customer groups.

An approach is proposed, which pulls together different streams of research and tries to incorporate them into a more useful, practical, and coherent framework. It endeavours to build an integrative configuration of the concept of customer equity that reflects its richness and complexity. The aim is to make the customer equity concept more helpful in designing of and studying service offerings and in developing competitive value-building strategies.

The resulting market-oriented approach attempts to synthesize and extend the literature on this subject. It considers market orientation with the primary role of stakeholder integration being the transfer of value-building chain elements to facilitate greater responsiveness to changing customer needs. In contrast to most other frameworks in the literature, the market-oriented customer equity process considers not only marketing activities for improving the value delivery to customers, but also improvements in the organisational structure, technology and core competencies.

This is because in today's world, the customer is an equal player in an organisation's network of value-creating elements (see also Abele, 2003). Customers are involved in the development of product, sales and marketing strategies and, hence, play an important role in gaining competitive advantage. Furthermore, customers are the engine of a firm's financial growth, which requires regularly assessing customer performance, i.e. measuring the financial value of each customer by means of indicators, such as customer profitability, customer lifetime value, or customer revenue.

The market-oriented framework consists of five steps (see Figure 24):

Step 1 - Customer segmentation stage (Section 4.2)

The customer segmentation stage is where the organisation classifies the customers according to their profitability i.e. identifying profitable, less profitable and unprofitable segments or customer groups and preferences of each segment.

Step 2 - Data gathering (Section 4.3)

The second step is a data gathering (on competition) stage where the organisation carries out competitor analyses by means of key figures and performance / price indicators.

Step 3 - Development of the value proposition (Section 4.4)

This is at the value proposition stage where the organisation determines the value proposition, which identifies value that the firm's clients desire and value that the firm can deliver.

Step 4 - Realisation of marketing strategies (Section 4.5)

This is a realisation stage of market orientation where an organisation can improve its marketing from value-building strategies in the previous stage for its project management, target marketing and so on.

Step 5 - Monitoring phase (Section 4.6)

Finally, the last step is a monitoring process stage in that the impact of the value-building strategies on customer equity, people, business processes, and financial business performance is measured.
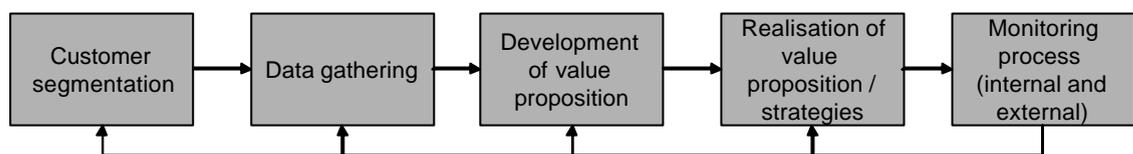
Figure 24: A market-oriented customer equity process
Source: own

To summarize, the proposed market-oriented customer equity framework in this thesis would assist managers in

- determining customer equity,

- categorising customers into segments,

- identifying new value opportunities,

- developing value propositions,

- identifying appropriate value-building strategies,

- adapting offerings and processes to customer needs,

- delivering more value than competition does,

- monitoring the impact of the value strategies on the customer and corporate performance, and

- continuously improving customer equity.

4.2 Step 1: Customer segmentation

In this step, the customer base of an organisation is categorised into customer groups by applying customer segmentation techniques. There are two methods allowing organisations to identify customer groups with homogeneous characteristics: the priori segmentation and the post hoc segmentation. In this step, first the priori segmentation is carried out because it is necessary for determining customer profitability, and then the post hoc segmentation is explained. This post hoc segmentation is optional because it is based on the priori segmentation, i.e. it only provides additional information on the profitability of the customer segments. In the following, both methods are described in detail.

4.2.1 Priori segmentation

Priori segmentation focuses on demographic and economic criteria (Harrison, 1994) often used in uni-dimensional form. Most banks prefer priori segmentation and use criteria such as profession, age, income, wealth, or the stage in the family life cycle. In particular, the stage in the family life cycle is an important aspect since it has been noted that individuals do have different financial needs and objectives as they progress through life. However, priori segmentation leaves out the consideration of the psychological feeling and the consumer behaviour (e.g. Machauer and Morgner, 2001). This problem is avoided in this proposed approach by providing the possibility of using the post hoc segmentation after the priori segmentation has been carried out.

In this approach, the priori segmentation is applied by categorising the customer base of an organisation into profitable, less profitable and unprofitable segments or customer groups. There are three different ways for calculating the monetary value of such segments, namely customer profitability, customer lifetime value, or customer revenue.

Customer profitability is the difference between revenues per customer and costs per customer. Expressed as a formula, customer profitability is determined as follows:

Customer profitability = total revenues per customer – costs per customer

Most researchers define customer lifetime value as the total discounted net profit that a customer generates during his / her lifetime, i.e. the average profit from a customer per period is calculated and then discounted to present by means of the discount rate. A formula that calculates customer lifetime value can be as follows (see Libai et al, 2002):

$$CLTV = \sum_{t=0}^{n} \frac{p*r^1}{(1+d)^1}$$

where r is a firm's average retention rate, p is the average profit from a customer per period, d is the discount rate, and n the years.

Customer equity is then calculated by summing up all monetary values from all customers, which can be customer revenue, customer profitability, or customer lifetime value. Section 2.5 provides a more detailed discussion on the calculation of customer equity.

Figure 25 shows an example of how the customer base can be segmented according to their profitability.
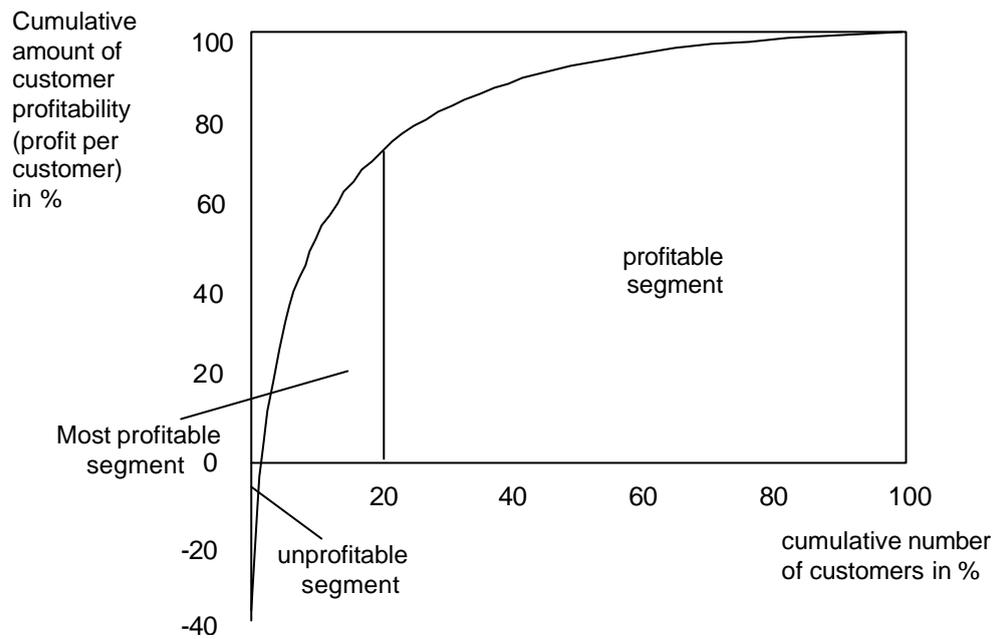
Figure 25: Example of customer segmentation by customer profitability
Source: adapted from Küng et al (2002)

The number of customer segments dependents on the objectives of the organisations. In general, a small number of segments is recommendable because this makes the handling and updating relatively simple and reduces the necessary time and effort.

There are three possibilities of improving customer profitability: increasing segment profitability, altering the switching probabilities, and reducing or eliminating unprofitable segments. Enhancing segment profitability means finding out which preferences a segment has and adapting services and offerings to these preferences. The investigation of customer preferences is briefly discussed in the next section. Altering the switching probabilities means increasing the probability that a customer will move to a more profitable segment and reduce the probability of a move to a less profitable segment. Finally, a reduced number of customers belonging to the unprofitable segment can be achieved by supporting a move to a profitable segment through, for example, appropriate offerings.

To show the important role customer profitability plays for organisations, an example is provided in Figure 26. In this example, the number of highly

profitable customers was reduced from 300 to 250 and the number of less profitable customers was decreased from 200 to 100. Finally, the unprofitable customer segment was strongly reduced by 350 customers to 150 customers. Overall, due to these reductions in the customer base and the greater emphasis on highly profitable customers, the organisations could increase its profit by £35,000 to £45,000. Furthermore, the organisation can benefit from long-term cost reductions resulting from serving less customers than before. Figure 26 provides an overview of the example.

	Segment	Number of customers	Profit per Customer (£)	Total profit (£)	Cumulative amount of customer profitability in %
before optimisation	Highly profitable segment	300	250	75,000	750%
	profitable segment	200	50	10,000	100%
	unprofitable segment	500	-150	-75,000	-750%
		1,000		10,000	100%

	Segment	Number of customers	Profit per Customer (£)	Total profit (£)	Cumulative amount of customer profitability in %
after optimisation	Highly profitable segment	250	250	62,500	138.9%
	profitable segment	100	50	5,000	11.1%
	unprofitable segment	150	-150	-22,500	-50.0%
		500		45,000	100%

Figure 26: Optimising the size of the customer segments
Source: Mudie (1997)

4.2.2 Comment on priori segmentation

However, in connection with the calculation of customer profitability several problems can occur. One problem could be the access to the necessary data, in particular the costs per customer. For calculating customer profitability, it is necessary to know the revenues per customer and the costs per customer.

While the revenues per customer can be easily determined by adding up the total of all of the orders placed with the organisation, the fixed and variable costs per customer are more difficult to determine because they require that the costs of the production process, sales process and marketing process are assigned to activities. In contrast to traditional cost behaviour, which divides costs into variable and fixed categories, an activity-based costing (ABC) system divides these same costs into activities. For each activity, a cost driver is identified and a cost per unit of cost driver is determined. For example, for the activity 'customer acquisition' the value driver is 'number of new customers' and the cost per unit of this cost driver is £14.8 per new customer. It is this information that makes the activity-based costing system a powerful tool for determining costs per customer. When an organisation does not use an activity-based costing system, it is almost impossible to calculate customer profitability.

Furthermore, the implementation of a customer relationship management (CRM) system facilitates the determination of customer profitability because it offers an automated process that assists organisations in segmenting their customer base according to either customer profitability or customer lifetime value. CRM provides matrixes and other tools to graphically segment customers and provides access to customer data like customer lifetime value (CLTV) that forecasts current profitability over the predicted life of customers within the segment. Sections 3.2 and 3.4 discuss both subjects in more detail.

4.2.3 Post hoc segmentation

A post hoc segmentation first surveys a heterogeneous population and then segments it by finding out homogeneous response patterns from within the population. Depending on the aim of the survey, most researchers ask customers questions on product features or product usage, whereas others refer to questions on psychological determinants of customers such as values, beliefs, or lifestyle.

Based on the priori segmentation determined discussed previously, a post hoc segmentation can be carried out if the organisation desires to find out more

about the previously identified most profitable, less profitable, and unprofitable customer segments. This could be of interest because the priori segmentation does not consider information on different personalities within the customer segment. For example, a highly profitable customer can prefer other product features or sales channel usage than another highly profitable customer. Therefore, it is interesting to know which preferences customers within the different customer segments have. An example of a post hoc segmentation is shown in Figure 27. The two dimensions of this two-dimensional segmentation map represent the average result of the questions on perceived service quality and perceived product performance. In this case, the customers belonging to the most profitable segment had to evaluate various items by using a scale of 1 to 10, where 1-5 represent a low performance and 6-10 represent a high performance. Figure 27 graphically illustrates the two-dimensional segmentation map.
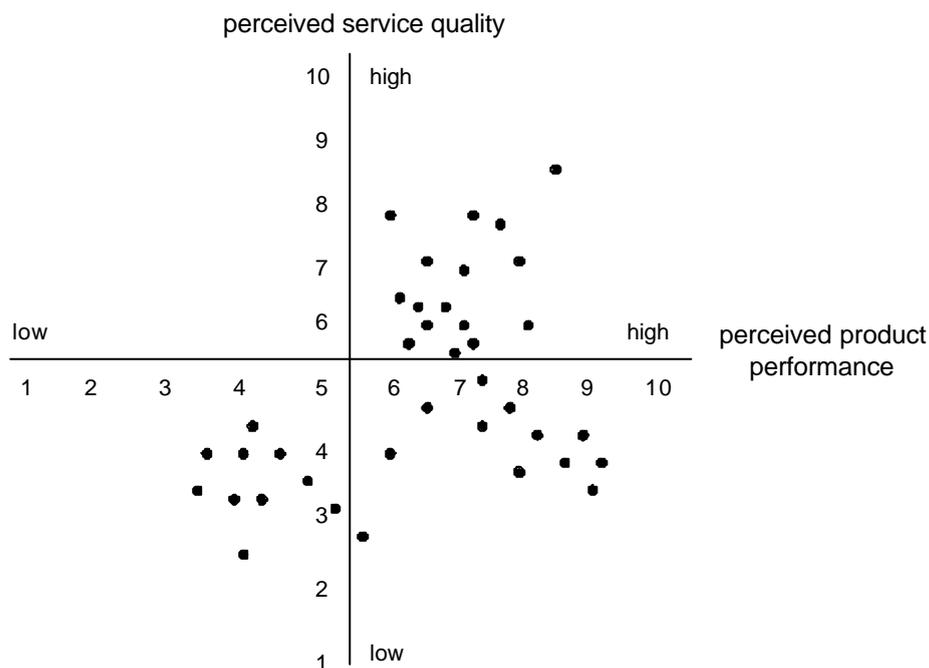
Figure 27: Two-dimensional segmentation map (most profitable customers were surveyed)

Source: own

4.2.4 Comment on post hoc segmentation

Besides this post hoc segmentation, organisations have also access to customer data from databases, CRM systems, or data mining tools. This data enriches the information on the identified highly profitable, less profitable, and unprofitable customer segments. Examples of such customer data are:

- market penetration for high- value customers identifying the percentage of high-value customers who have been acquired compared to the potential prospect population;

- cross-selling potential, which reflects the number of different product categories in relation to add-on features or services for each customer;

- product penetration, which identifies the proportion of customers within each segment that have purchased within each product category;

- customer retention, particularly segment-level retention percentages, which compare the performance for the low, average and high-value customers within each segment;

- customer reactivation that is the number of previously inactive customers who have been enticed to purchase again; and

- channel usage or penetration, which tracks the number and type of channels utilized. This measure is important for many industries because the use of multiple channels, such as retail, telephone, catalog and Internet channels, enhances customer profitability and is therefore seen as an indicator of customer loyalty.

In general, a customer relationship management (CRM) system provides three kinds of information: of-the-customer information, for-the-customer information, and by-the-customer information (see Park and Kim, 2003). Of-the-customer information is transaction data and personal data, whereas for-the-customer data is relationship data and product data. Finally, by-the-customer data is feedback data and monitoring data.

4.3 Step 2: Gathering of data from competitors

Benchmarking competitive performance is an established business practice. Understanding who one's competitors are and comparing one's performance with that of these players is vital to the financial health of every corporation. Therefore, many researchers see benchmarking oneself against competitors as a robust method to ensure a long-term, sustainable, and substantial competitive advantage (Porter, 1998).

4.3.1 The process of benchmarking

The process of benchmarking is categorised into several sub-processes. First, the company needs to determine the functional area(s) that should be benchmarked. Second, benchmarking is best used and described as a framework for strategic planning in that key success factors of an industry and other elements, such as the financial resources and product strategy, are identified and compared with competition. Thus, it is important for the company to identify the key factors and variables with which it intends to measure the performance of the functional area(s). These measures or "benchmarks" are then used to develop future quality and market initiatives for the firm to enhance its overall competitive position. Third, the company needs to select the competitors for the functional area(s) to be benchmarked. Fourth, the own performance and the performance of the competitors for each variable or key success factor is measured. In this phase, the company needs to gather information from sources like companies themselves, articles in the press or trade journals, analysts in the market, credit reports, clients and vendors, trade associations, the government or from interviews with other organizations willing to share their prior research. Finally, developing plans, programs, and actions that closes the performance gap between the own performance and that of competition is necessary. After implementing these programs, often a monitoring process is developed for reviewing and updating the competitor analysis over time.

In the following, two methods or tools for carrying out a competitor analysis are presented: benchmarking by means of key figures and benchmarking by means of performance / price evaluation. Both methods make it possible to compare the constituent processes of the company with direct or indirect competitors.

4.3.2 Benchmarking by means of key figures

In order to get an overview of key data on the main competitors, a company can use key indicators that measure the own performance and the performance of the competitors. Table 14 shows examples of the most relevant general key indicators for a competitor analysis. In this example, the competitor performance of only one competitor is shown. However, it is also possible to additionally list the performance of further competitors by inserting additional columns.

Key success factors / variables	Own performance	Competitor performance	Performance gap
Market share	10%	22%	-12%
Relative price	107	100	+7
Relative product quality	106	101	+5
Relative service quality	97	102	-5
Number of distributors	223	300	-77
Sales force (number)	175	200	-25
Advertising & promotion (% of sales)	1%	1%	0
Marketing budget (% of sales)	20.0%	17.0%	+3%
Return on assets (%)	15%	19%	-4%
Return on sales (%)	7%	11%	-4%
Company turnover	2,000,000,000	2,500,000,000	-500,000,000
Sales per employee	1,500,000	1,000,000	+500,000

Table 14: Examples of key measures for competitor analysis
Source: adapted from Doyle (2004)

In the following, the formula of each key measure is given expect for the company turnover, number of distributors, and size of sales force because they are simple figures.

Market share = (own business share / total share of chosen competitors) x 100

Relative price = (product price / average price) x 100

Relative product quality = (product quality / average product quality) x 100

Relative service quality = (service quality / average service quality) x 100

Advertising & promotion (% of sales) = (sales revenue / marketing expenses) x 100

Marketing budget (% of sales) = (sales revenue / marketing budget) x 100

Return on assets (%) = (net income / total assets) x 100

Return on sales (%) = (a fiscal year's pre-tax income / total sales revenue) x 100

Sales per employee = (total sales revenue / number of employees)

4.3.3 Benchmarking by means of performance / price evaluation

Once a company has analysed the chosen competitors by applying the above discussed key indicators, it is important to engage in a more detailed analysis of these competitors. By asking customers to evaluate its own performance against those of competition, a firm can gain a better understanding of its competitive position and key competitors. In the example shown in Figure 28, the relative performance was measured by carrying out a customer survey and the relative price was determined by comparing the own price with those of competitors. A graph of relative performance versus relative price allows the company to create a perceptual map of competition. Figure 28 graphically illustrates this two-dimensional perceptual map of competition. With such a map, a company can easily investigate its competitive position relative to the competitors and better identify value-building sources.

Product	Overall performance	Relative performance	Product price	Relative price
Own product	81	96.2	70	99.2
Competitive product A	77	91.4	65	92.1
Competitive product B	89	105.7	89	126.1
Competitive product C	95	112.8	60	85.0
Competitive product D	79	93.8	69	97.7
Average	84.2	100	70.6	100

Table 15: Relative performance and relative price

Source: adapted from Doyle (2004)

The overall performance, shown in the second column of Table 15, is the average of all performance questions asked customers by means of a customer survey. The relative performance presented in the third column is calculated by dividing the product performance by the average performance and multiplying it by 100. In the fourth column, the product price is listed, whereas in the last column the relative price of the product is shown. This relative price is calculated by dividing the product price by the average price and multiplying it by 100. In the following, formulas and examples of the perceived performance and the perceived price are presented.

Relative performance = (product performance / average performance) x100

Relative performance of own product = (81 / 84.2) x 100 = 96.2

Relative price = (product price / average price) x 100

Relative price of own product = (70 / 70.6) x100 = 99.2

The resulting data can serve as a basis for the classification of products into four quadrants (see Figure 28). The matrix graphically illustrated in Figure 28 is

a simple tool that can provide for sophisticated comparisons of product performance between organisations.

Relative price
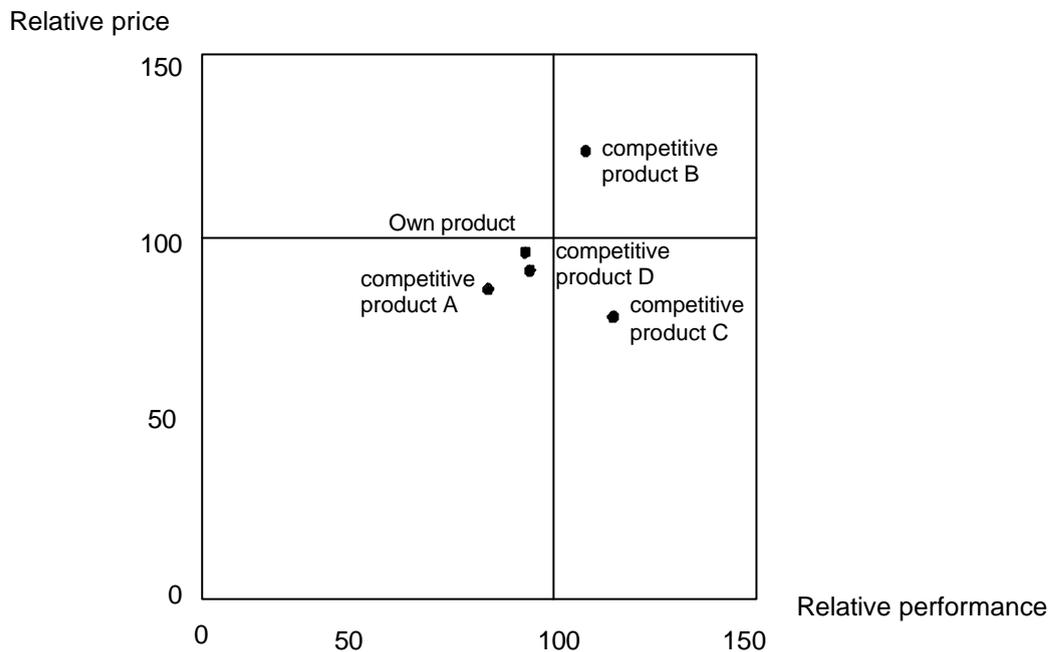
Figure 28: Price-performance matrix
Source: adapted from Doyle (2004)

4.3.4 Comment on step 2

For the success of a competitor analysis, company-wide support for competitive intelligence is vital. Senior support is essential to establish legitimacy and importance, while sales representative support is linked to gathering critical field-level data. This support facilitates the development of a competitive network, which makes it possible to circulate competitive intelligence through the organization, collect competitive information from internal sources, and raise credibility and awareness of goals and roles. The support is also necessary for accepting the outcome from the competitor analysis, i.e. the changes in product strategies, technology, culture, and organisational structure.

Furthermore, it is essential to create competitive intelligence groups that regularly collect information on competitors and make reports and plans. These groups push information out to users, establish regular communication with

groups, conduct informative seminars, and establish reciprocal relationships with key stakeholders. With multiple departments supporting competitive intelligence activities, competitive intelligence teams can leverage their influence to develop and implement recommendations to brand strategies, product strategies and other important corporate strategies. In the organisational structure, the competitive intelligence groups could assign to the strategic planning department or the business development department. These two departments are best suited because they are the centre for decision-making processes in an organisational environment.

4.4 Step 3: Development of the value proposition

4.4.1 Interpretation of the term value proposition

A value proposition is one of the most essential elements of a successful firm as it is (a) a statement of the **uniqueness of a business that sets it apart from all competitors** and (b) a statement of how to **meet the customer needs** of the target market. In short, a value proposition is a statement that identifies value: value that the firm's clients desire and value that the firm can deliver.

Doyle (2004) also proposes two determinants of a value proposition: seeking a differential advantage based on a value proposition of product innovation, superior service, brand image or low cost and matching the wants of customers. In order to be able to develop a value proposition, a firm needs to investigate the size of the key customer segments, their growth, the amount of competition, average operating margins, and investment requirements.

Webster (1994) defines a value proposition as:

"...the verbal statement that matches up the firm's distinctive competencies with the needs and preferences of a carefully defined set of potential customers. It's a communication device that links the people in an organization with its customers, concentrating employee efforts and customer expectations on things that the company does best in a system for delivering superior value. The value

proposition creates a shared understanding needed to form a long-term relationship that meets the goals of both the company and its customers."

He equates a value proposition to a positioning statement because it answers questions, such as "who is the target customer?" as well as "why should the customer buy it?" and "what are we selling?".

One can conclude from the above that a good value proposition is specific enough to recognize the unique nature of subjective and interactive consumption experiences but general enough to attract adequate customer segments with homogenous value needs (Ballantyne and Varey, 2006; McDonald et al, 2007).

4.4.2 Types of value propositions

In the literature, different types of value propositions are presented. Treacy and Wiersema (2003), for example, propose three different types: product leadership, customer intimacy, and operational excellence. Doyle (2004) states that there are four types of value proposition strategies, namely product leadership, service leadership, customer intimacy, and brand leadership. Rintamäki et al (2007) use the term customer value proposition instead of the more general term value proposition and distinguish between economic customer value propositions, functional customer value propositions, emotional customer value propositions, and symbolic customer value propositions. Figure 29 provides an overview of the different types of value propositions. All types are discussed in more detail in the following.

Types of value propositions

product leadership	product leadership	symbolic propositions (social value)
customer intimacy	service leadership	economic propositions (price)
operational excellence	customer intimacy	functional propositions (product and process)
	brand leadership	emotional propositions (brand)
Wiersema and Wiersema (1995)	Doyle (2004)	Rintamäki et al (2007)
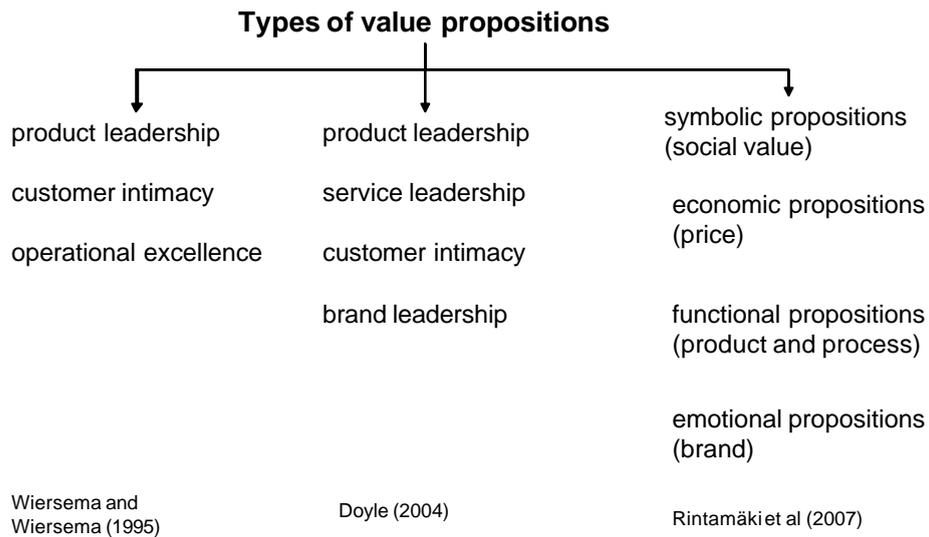
Figure 29: Types of value propositions
Source: own

(a) Product leadership:

Companies choosing a product leadership value proposition typically offer one-of-a-kind products and services, state-of-the-art features, and innovative solutions. These companies invest heavily in research and development, prioritise hiring employees with outstanding skills, and build cultures that focus on innovation and creativity to achieve the financial advantages of successful product leadership. Customers purchase from these companies because of their unique capabilities that makes it difficult to get the product anywhere else. These companies don't strategically stress low price or world-class service. Microsoft, Intel, and Harley-Davidson are examples of product leadership strategy companies. Researchers, such as Treacy and Wiersema (2003) and Doyle (2004), investigated such a type of value proposition in their research.

(b) Service leadership:

These companies focus on delivering high value to customers by providing an outstanding service. In general, service companies prefer this kind of leadership because the service quality in this industry is often the only way of achieving differentiation from competition. Examples of companies centring in service leadership are British Airways, American Express or Hyatt.

(c) Operational excellence:

Organizations that choose an operational excellence value proposition opt to excel at attributes such as price, quality, on-time delivery, selection, availability, that their competitors can't match. As expected, they tend not to be big product innovators or strategically offer high levels of customer service because they execute extraordinarily well. Examples of operational excellence firms are Charles Schwab, Hertz, FedEx, Wal-Mart and Southwest Airlines.

(d) Customer intimacy:

Firms adopting a customer intimacy value proposition will choose to focus on the quality of their relationships with customers and offer "complete solutions" as their value proposition. These firms enhance the creation of knowledge of their customers to be able to develop solutions that are tailored to customer needs. In general, customer orientation plays a central role in such organisations and people, technology, culture, and processes are customer-driven. They don't try to have the lowest price or the most innovative products. Customers that value intimate vendor relationships will tend to buy from them. Examples here are The Home Depot, Nordstrom Stores, and IBM. Companies that base their strategy on personalized service will maintain acceptable levels of product innovation or operational excellence but these levels are lower than the level of customer intimacy. Generally, an organisation focuses on one type of value proposition because it is impossible to focus on all value propositions at once.

(e) Brand leadership (emotional value proposition):

Organisations that centre on brand leadership attempt to create a strong emotional bond with their customers to strengthen the relationship. The primary aim of these firms is to fulfil the promise they made in their advertising campaigns by satisfying the experiential needs and wants of their customers. These include enjoying shopping with friends and family, bargain-hunting, and seeking adventure or relaxation. For customers preferring companies that focus on brand leadership, the shopping experience is an important element for their purchase decision. Therefore, organisations attempt to provide appropriate

store environment, personal service, and visual, auditory, sensory, and even gustatory clues to create emotional customer value.

(f) Economic value proposition:

Some customers place emphasis on the price of a product when they make their purchase decision. For them the product quality and shopping experience is of secondary importance. Companies pursuing price leadership, i.e. an economic value proposition, aim at optimising their organisational structure, business processes, and supplier network regarding costs. In other words, such companies are characterised by efficient supply chain processes, high production volumes, and high level of technology. Furthermore, to achieve the lowest price in their sector they attempt to benefit from the economies of scale that is generated by producing large quantities. Examples of companies pursuing this value proposition are Wal-Mart or Aldi.

(g) Functional value propositions:

To provide customers with functional value, the company seeks a differential advantage by offering more convenience at different stages of the shopping experience. In general, organisations adapt their products to the needs of their customer to facilitate the process of finding the right product. Moreover, such companies reengineer their business processes to increase convenience during the buying process. Tesco is a good example because it enhanced customer-focused commitment to design more convenient shopping experience.

(h) Symbolic value propositions:

Positive consumption meanings are created by the symbolic value of a product or customer experience, i.e. symbolic value emphasizes self-expression through socially interpreted codes embedded in consumption. Companies pursuing a symbolic value proposition offer symbols or special kinds of social objects that have a special meaning for customers. A good example is The Body Shop offering only products that correspond with their five symbolic values: "against animal testing, support community trade, activate self esteem, defend human rights, and protect our planet".

4.4.3   Value-building strategies

Organisations have two main possibilities of creating value: rationalisation or growth. Rationalisation means cutting costs, cutting investments, or raising prices, whereas growth results from the revenues generated by existing and new customers, and new markets (businesses). For increasing customer profits, it is important to improve customer loyalty, continuously optimise the product range, and involve customers in the product development process. Growth resulting from new businesses comprises either the development of new channels or the sale of products in new markets. Figure 30 provides an overview of the possibilities of value creation.
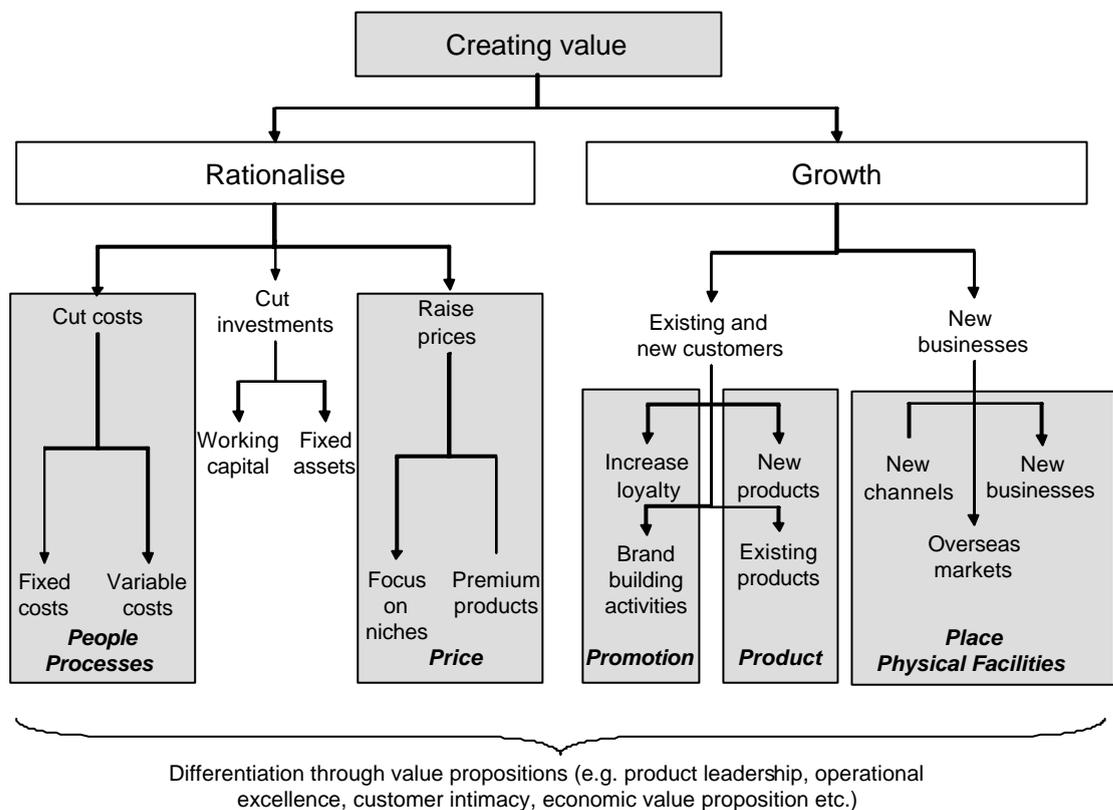
Figure 30: Possibilities of value creation
Source: adapted from Doyle (2004)

Figure 30 shows how value-building strategies are related to the 7Ps marketing mix, which comprises product, price, place, promotion, people, physical facilities (service environment and service quality), and processes. Cuts in cost, for example, can be realised by reducing staff or improving business processes. Managing products, communicating with customers, adapting prices, or developing new sales channels helps companies to improve their value delivery to customers with the objective of increasing customer profits (customer equity).

These value-building strategies are the basis for the realisation of the chosen value proposition. For example, if an organisation centres on an economic value proposition, value-building strategies aiming at cost reduction and process optimisation play an important role in achieving a low-cost business that makes it possible to offer products at low prices. In the following, some examples of value-building strategies are explained in detail.

(a) Revenue growth of existing and new customers through customized products

Revenues of existing and new customers can be increased by offering products that better meet customer needs. Customised products and services that are tailored to customer wants and preferences help firms to more satisfy customers and increase their willingness to buy from them. Customisation of offerings is a technique that makes it possible to deliver superior value to customers by providing as many products until the variety of customer needs is fulfilled. In general, special technology makes customisation possible. However, it is important that the firm determines base components and additional components that can be combined with each other to reduce the costs of customisation to a certain limit. A too wide range of customised products would lead to a time-consuming production and thus high costs. Furthermore, to reduce the complexity of customization, it is also possible to bundle the most successful components and offer them as standard-feature bundles. In this context, it is also important to choose components with high margin and high turnover to ensure a positive financial contribution to a firm's success in the long run.

(b) Revenue growth of existing and new customers through improving loyalty

A key concern is that firms need customers who are profitable, and profitability depends on the company's ability to sell customers further products(cross-selling). This cross-selling in turn mainly depends on personalised customer contact plans and loyalty programmes that reward the customer for his purchases. It is important to reward customers not only with 'hard benefits' of point-based rewards, but also with 'soft benefits' such as exclusive events or workshops. Such measures support customer loyalty and customers' trust in an organisation and let customers feel that they are important to the firm.

Studies found that special customer loyalty programs should contact customers during the first ninety days of their relationship with a firm because in this period they have the highest purchase potential. Furthermore, sales personnel should regularly contact profitable customers who have recently purchased products and sent them additional messages presenting offers that are tailored to customer needs. A recent study from Peppers & Rogers Group, Carlson Marketing Worldwide, and Market Tools (Peppers and Rogers 2007) that surveyed 1,909 consumers of financial services organisations points out the importance of customer loyalty programmes regarding the increase in the purchase volume of customers. The study found that twenty-six percent of the consumers buy financial products due to regular personalised messages presenting appropriate offerings. Fifty-one percent of the respondents are willing to join a loyalty programme when one is offered.

One can conclude from the above that a contact programme and loyalty programme aim at strengthening customer relationships, improving customer loyalty, and increasing customers' purchase volume.

(c) Rationalisation by cutting costs

The most popular tool for reducing costs is business process management (BPM) that transforms business processes so that an organisation is more responsive to customers, customer-centric, productive, cost-effective, and flexible. By automating processes and avoiding paper-based steps, the organisation reduces mistakes, saves time and money, and improves process

efficiency. New technology that generally supports BPM, can, for example, automatically routing work and altering staff when they receive the next work item or when they need to take an action. All these new automated processes lead to cost reductions.

Besides the effort of companies to support their technology by overcoming internal barriers and developing an integrated flow of business processes, it is important to look at the financial benefit that result from the redesign of business processes. Recently, there is a trend towards powerful service-oriented architectures that are based on Web services standards and enterprise applications. However, the structural flexibility and integration capabilities underlying these technologies can be only as effective as the business processes they support. A study carried out by The Economist Intelligence Unit (2005) shows that among three hundred interviewed executives, 61% rank 'reducing the unit costs of business processes' first followed by 'achieving product differentiation' (59%), and 'increasing brand value' (58%). This shows the importance of business process management in today's organisational environment.

(d) Growth in revenues of existing and new customers through brand-building activities

For attracting prospects and customers, convincing them of buying the branded product, enhancing their purchase volume, and building trust, it is important that a brand fulfils the promises of future performance. The better the performance is, the higher the trust of the customers is in the brand, and the more they are willing to buy further products. Increased brand trust reduces customer's perceived financial, social or safety risk and augments the perceived benefits resulting from the purchase and consumption of the branded product. This means that a customer is willing to pay more for a branded product than an unbranded product because he is convinced of the quality of the product and the risk reduction, such as the risk of buying a product that will perform badly.

In general, brand trust can be seen as a key element for developing long-term customer relationships (Delgado-Ballester and Munuera-Alemán, 2001) and for

improving the emotional contact between the organisation and the customer. Emotional value is mainly created through customer interactions with an organisation. Customers evaluate the way in which an organisation treats them during the interaction, for example, if employees make them feel important, valued, or special. Barnes (2003) adds respect, appreciation, recognition, understanding, and acknowledgement of customers as important emotional value creator. However, a strong brand has not only advantages for a customer, but also for an organisation. Benefits are for instance increased brand loyalty that represents a substantial entry barrier for competitors, increased customer turnover, a more competitive position in the market, and less marketing costs as retaining customers is cheaper than acquiring new ones (see also Delgado-Ballester and Munuera-Alemán, 2001).

4.4.4   *The impact of value-building strategies on customer touchpoints*

Customers can profit from the previously discussed value-building strategies by improved customer touchpoints. Customer touchpoints are customer interactions over the customer relationship with a company (see also Abele, 2007a). Over this time, the customer experiences the product and the company and, if he is satisfied with this experience, he tends to be more loyal and more willing for positive word-of-mouth and repeat purchases. Companies communicate their value through each customer touchpoint, i.e. that the customers perceive the benefit from the value-building strategies through these touchpoints (see Figure 31). As these touchpoints influence customers' buying behaviour, it is important to companies to continuously improve them by means of appropriate value-building strategies.

In general, these touchpoints or points of contact begin before a customer starts a relationship with a company. The first of the three stages of a customer relationship, the presence stage, considers this pre-purchase process, whereas the other two stages, namely the relevance / performance stage and the bonding stage, do consider the purchase process and the post purchase process (e.g. Fey, 2002). As each stage has different customer touchpoints, it is necessary to assign the appropriate touchpoints to these three stages. Figure

31 provides and overview of the discussed impact of value-building strategies on the customer touchpoints.
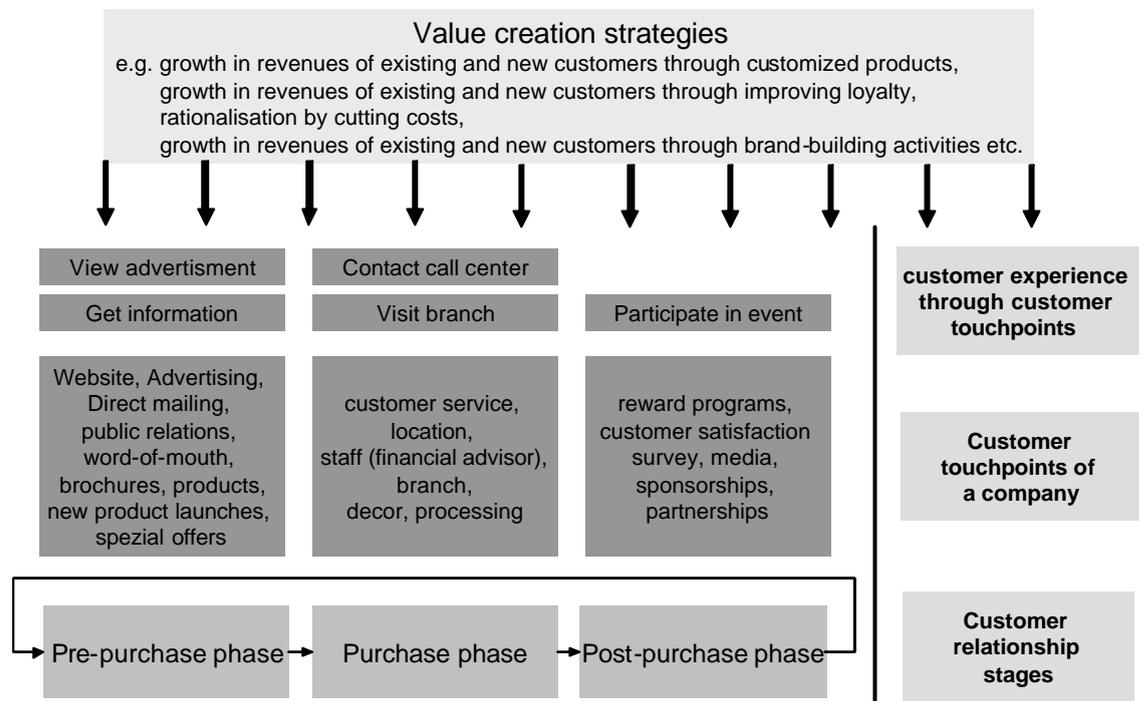
Figure 31: The impact of value-building strategies on customer touchpoints
Source: own

The first stage, the pre-purchase stage, is crucial to the success of a company because in this period, the customer has to be convinced of the quality and superior value of the branded services or products. Touchpoints, such as advertising, Website, product launches, public relations, or special offers (special prices) are crucial for this phase. In the second stage, the prospect has made a purchase decision and has decided to get in touch with the company. Therefore, the sales channels, customer service, location, or processing are important for creating value for customers. Finally, the relationship moves into the most profitable stage, the post-purchase phase, where loyalty and high customer experience lead to customer satisfaction and increased customer turnover. In this last phase, reward programs, customer satisfaction survey,

media, or sponsorships help to maintain customer's loyalty (e.g. Davis and Dunn, 2002).

4.4.5 Comment on step 3

In general, successful companies **concentrate on one type of value proposition and strategically maintain acceptable levels of performance in some of the other seven listed types above**. One main reason for this is that a value proposition defines and expresses the uniqueness of the firm's offerings. This uniqueness attracts customers and fulfils their needs in a better way than competition does because the resources and capabilities of a firm are focused on customer needs. Customers perceive the uniqueness of the value proposition as a set of attributes with different levels of performance including innovative products, low price points, high service levels etc. This means that one perceived attribute has a superior performance level, whereas the rest of the perceived attributes have a lower performance level. These different performance levels are necessary because it is impossible to focus on more than one value proposition. In contrast, firms that do not pursue a value proposition do not send customers and prospects the appropriate signals that animate them to buy from them. Choosing makes a statement as to what a firm's structure, core competencies, business process, and culture will look like, and provides the customer profile upon which the firm can build a well-constructed business strategy.

The implementation of new technology, such as databases, call distribution systems, and electronic services is a very popular value-building strategy because it reduces costs, improves the efficiency of a company's information flows, leads to quicker responses to customer needs and thus to improved customer experience. Besides the implementation of new technology, customer involvement in the planning process of value-building strategies, particularly regarding the product development and product design, is also very common because it enhances the degree of customer orientation. In general, the greater the attention paid to customer involvement at every step of the value creation process, the greater will be customer satisfaction, customer retention, and

customer delight and, hence, the higher will be the market share, and corporate profitability. One main reason for this positive impact is that customer involvement brings renewed market freshness and competitive vigour to the suppliers, employees, designers and engineers, which facilitate adapting processes and products to changing customer preferences. Organisations become more and more aware of the importance of customers in the value creation process, which is why they involve customers for discovering better ways of improving customer relations, products, business processes, and services.

4.5 Step 4: Realisation of the value proposition and the value creation strategies

For realising the developed value-building strategies in the previous step, it is necessary to work out a project management framework suitable for the scope and the length of the thesis and work to be performed. In this step, some general guidance on thesis management is given and useful methodologies for facilitating the planning and the realisation of a project are presented. For successfully realising projects, in this case value-building strategies, such as cost cutting actions, it is important to (a) generate options by means of creativity tools, (b) list 3-4 critical success factors that are important for the project to be successful, and (c) use good planning methodologies for determining who will do what, when, where, how and why, and at what cost (e.g. cost-benefit analysis, Gantt Chart).

In this context, it is necessary to note that for most projects, there is more than one way to approach the work and achieve the objectives. Therefore, organisations need to think through several methods, assess the pros and cons, and come up with the one, which is best. Hence, the proposed three criteria for a successful project realisation presented in the next sections provide rough guidance for organisations.

4.5.1 Generating options by means of creativity tools

When an organisation intends to realize a value-building strategy, it is aware of the possible benefits that can result from the strategy because it has already checked the main possibilities of value creation (see step 3). Examples of value-building strategies are revenue-based activities, brand-building activities, loyalty-driven activities, or cost-cutting activities. All these examples were discussed in step 3. However, for generating sub-options, special creativity tools, such as brainstorming or the reframing matrix, are suited. Brainstorming is a technique that collects the ideas of the project members and changes and improves them step by step until the best result is achieved. The reframing matrix assists the project members in looking at value creation strategies from a number of different viewpoints, namely the product perspective, the planning perspective, the potential perspective, and the customer perspective. All four perspectives aim at discovering as much value creation potential as possible. Figure 32 shows an example of the reframing matrix covering the value creation strategy for improving the sales of a new product. To summarize, the four perspectives of the reframing matrix answer the following questions:

- Product perspective: Is there something wrong with the product?

- Planning perspective: Are our business plans or marketing plans at fault?

- Potential perspective: If we were to seriously increase our targets, how would we achieve these increases?

- Customer perspective: Why do customers choose one product over another?

Product perspective:	Planning perspective:
-Untried product -Is it technically correct? -Is it attractive? -Is it well priced?	-Are we approaching the right markets? -Are we using the right sales strategy?

Problem: New product not selling well

Potential perspective:	Customer perspective:
-How could we raise sales?	-How do customers see the product? -Are they convinced that it is reliable? -Why are they choosing other products?

Figure 32: Example of the reframing matrix
Source: adapted from Morgan (1993)

4.5.2 Identifying critical success factors for marketing

From the developed options in the previous section, the most important ones are identified and in the form of critical success factors (CSFs) presented to the project team and management. Critical success factors are the essential areas of an activity that must be performed well if the organisation wants to achieve the mission, objectives or goals for the project. As a common point of reference, critical success factors help everyone in the team to know exactly what is most important and to perform their own work in the right context for contributing to the same overall aims. Table 16 shows an example of critical success factors for the project on improving the sales of a new product.

Objective	Critical success factors (CSFs)
Gain market share of 12%	- Advertise new product - Change design of new product
Increase customer retention rate by 7 %	- Improve customer satisfaction with new product - Improve customer orientation of front-

	line staff
	- Implement loyalty program
Expand product range to attract more customers	- Develop further new products

Table 16: Example of critical success factors for the project on improvements in sales

Source: own

4.5.3 Using planning methodologies in marketing

Detailed planning is the process of working out the most efficient and effective way of achieving the aim that the project team has defined. It is the process of determining who will do what, when, where, how and why, and at what cost. When drawing up the plan, techniques such as Gantt Charts can be immensely helpful in working out priorities, deadlines and the allocation of resources. Furthermore, the use of methodologies such as the cost-benefit analysis assists the project team in investigating the impact of the project on the financial success of the organisation. This requires adding up all the costs involved with the plan, and comparing them with the expected benefits. Both the Gantt Chart and the cost-benefit analysis are discussed in the following.

(1) The Gantt Chart

The Gantt Chart is a tool that makes it possible to determine the resources for the project, the times when these resources will be needed, the order in which tasks need to be carried out, the quickest possible time in which a project can be completed, and the "critical path" for a project. The "critical path" sorts the tasks according to their priority, i.e. it identifies which tasks have to be carried out first. These are sequential tasks that are dependent on other tasks being completed first because otherwise they could not be done. Tasks that are independent of any other tasks are called parallel tasks and can be done at any time before or after a particular stage is reached. Figure 33 graphically shows an example of a Gantt Chart.

WEEK				
1	**2**	**3**	**4**	**5**

(1) Change design of new product

(5) Advertise new product

(6) Improve customer satisfaction with new product

(2) Implement loyalty program   (4) Improve customer orientation of front-line staff

(3) Develop further new products
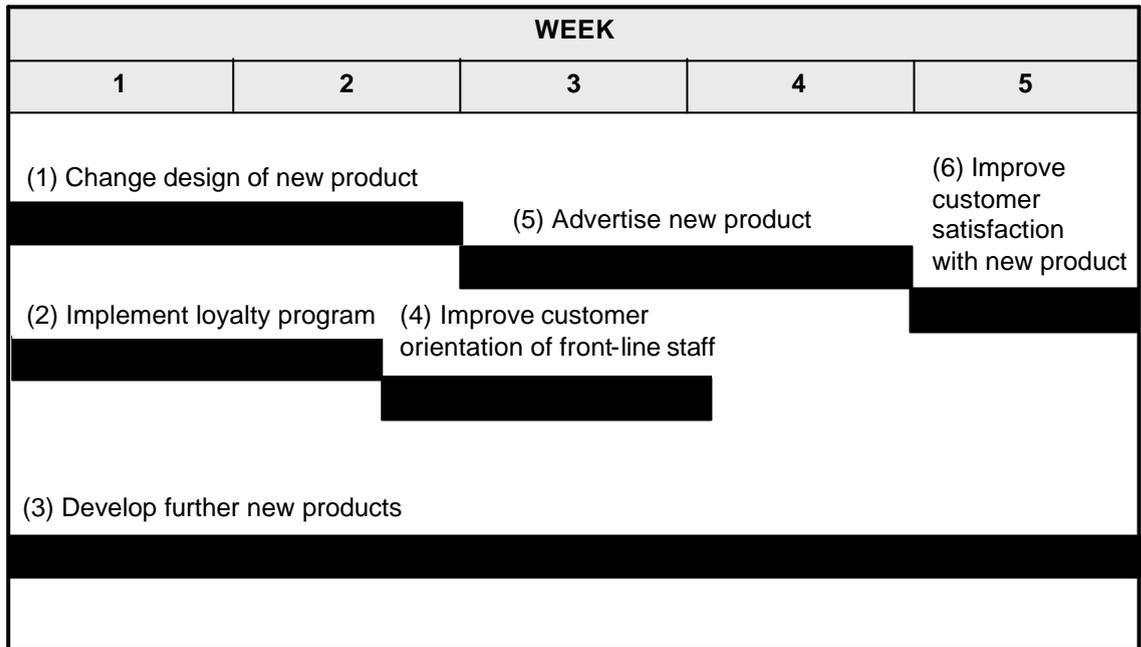
Figure 33: Example of a Gantt Chart for the project on improvements in sales
Source: adapted from Wysocki (2006)

The example shown in Figure 33 is a project with a length of five weeks. During this time, six tasks are carried out for achieving the overall aim of the project, which is the improvement in the sales of the new product. At the beginning of the project, three tasks were carried out parallel.

(2) The cost-benefit analysis

This method is suited to investigate whether the realisation of the project, particularly the value-building strategy, is worthwhile or not. For determining the economic benefit of the thesis, the costs are subtracted from the revenues of the project. In the following, an example is shown that calculates the economic benefit of the project on improving the sales of a new product (see Table 17).

Costs:	
Advertise new product	- € 50,000
Change design of new product	- € 5,000
Improve customer satisfaction with new product	- € 5,000
Improve customer orientation of front-line staff	

through training (in total 20 people)	- € 20,000
Implement loyalty program	
Develop further new products	- € 100,000
Other costs (e.g. lost time, lost sales through disruption)	- € 50,000
	- € 20,000
Total costs in year 1	- € 250,000
Revenues:	
Estimated basis sales of new product	+ € 220,000 / year
Estimated sales resulting from improved customer service and retention	+ € 40,000
Estimated sales resulting from campaigns	+ € 50,000
Total revenues in year 1	+ € 310,000
Total economic benefit in year 1	+ € 60,000

Table 17: Example of cost-benefit analysis
Source: Brealey et al (2008)

4.5.4 Comment on step 4

For realising value-building strategies, it is necessary to select and adapt the methods to the nature of the project and the outcomes to be achieved. In this context, it is important to note that step 4 only refers to the most relevant methods for carrying out a project. This means that the more complex a project is, the more complex methods it needs and the more time it should be invested in the planning phase. With planning, projects can run on time and interact effectively with both customers and suppliers. Everyone involved understands what is wanted and emerging problems are seen (and dealt with) long before they cause damage. Therefore, it is important to invest enough time in planning. In general, a project requires a clearly designated project manager, a written agreement on the project tasks, and the proportion of time the responsible individual will devote to project management. This should be documented in the project plan and agreed with the program manager.

4.6   Step 5: The monitoring process (internal and external)

This monitoring process considers the impact of value-building strategies on customer equity, people, business processes, and financial business performance. All these areas of performance reflect the organisation's strategy in a simple way. Table 18 shows an example of key indicators measuring the success of value-building strategies. Each organisation needs to carefully design and select measures that are consistent with meeting their goals. Due to the importance of customer's assessment of the improvements resulting from the value-building strategies, in the following, the difference between the two measures customer satisfaction and customer perceived performance is discussed.

For regularly assessing the feedback from customers, it is necessary to determine measures such as customer satisfaction or customer perceived performance ratio. Critics have argued that traditional customer satisfaction models rate a company's performance as perceived by existing customers, but do not integrate potential customers, non-customers, or competition in the set of analysis (Gross, 1997). Customer satisfaction focuses on a company's offer or performance and does not take into account competition. Furthermore, customer satisfaction measurement has been criticized as being limited to a tactical level, providing simple product improvement and a correction of defects and errors of existing products and services.

In contrast, the customer perceived performance method is oriented towards a strategic level and answers questions, such as how value can be created for customers and by which means a company's offering can best meet customers' requirements (Eggert and Ulaga, 2002). Finally, satisfaction is a post-purchase construct and can only be determined after the purchase of a product or service, whereas customer perceived performance is independent of the timing of the use of a market offering and can be considered as a pre- or post-purchase construct. Grounded on these arguments, Gross (1997) has called for a replacement of the satisfaction construct by the value construct as a better predictor of outcome variables in business markets. However, a complete

replacement of customer satisfaction is questionable, but in the long run customer perceived performance will be of greater importance to companies.

What needs to be assessed	Examples of key indicators (What to measure)
Assessing changes in customer equity (=sum of all customer lifetime values)	*(a)* change in costs per customer / average costs per segment *(b)* change in revenues (or customer turnover) per customer / average revenues per segment *(c)* change in profit per customer / average profit per segment (often profit per customer is equal to the customer lifetime value [CLV])
Assessing customer's feedback and value expectation	*(a)* customer satisfaction = customer satisfaction index *(b)* customer retention and loyalty = customer retention rate *(c)* customer perceived performance ratio = desired benefits – relative costs
Assessing people, processes, systems, budgets etc.	*(a)* employee training and education = percentage of employees involved in training and education *(b)* employee satisfaction = employee satisfaction index *(c)* innovativeness = percentage of sales from new service *(d)* new service development = average new service development time *(e)* productivity = error-free products processed per employee *(f)* process improvements = average process cycle time *(g)* quality = number of customer complaints per 1,000 orders filled
Assessing impact on financial business performance	*(a)* sales growth = percentage change in revenue from one period to the next *(b)* market share = business market share *(c)* return on investment = net income / invested capital

Table 18: Examples of key indicators measuring the success of value-building strategies

Source: adapted from De Bonis et al (2003)

4.6.1 Comment on step 5

In order to know if the value-building strategies realised are successful or not, organisations need to examine regularly and systematically customer feedback. This means that all customer interfaces should be identified and integrated into

appropriate feedback systems, such as customer relationship management (CRM) systems.

A CRM system is usually associated with a massive corporate data warehouse, run by the company IT department. The warehouse contains all of the information available to the company about customers (e.g. purchase history, names, addresses, demographics, complaints, web activity, promotion history etc.), employees (e.g. sold products per employee, average time spend on serving customers etc.), products (e.g. product details, prices, special offers etc.), sales (e.g. number of products sold), costs (e.g. marketing costs, sales costs, service costs, production costs etc.), inventory (e.g. number of available products etc.), shipments, and other data sources. Furthermore, external data such as enterprise data from competitors dealing with the organisation's customers, data about customer needs collected by web surveys, and data from communities or clubs with a common interest, can be additionally added. Due to this variety of data, CRM is a good platform for establishing enterprise-wide measures of success and customer performance indicators. In particular, analytical CRM offers the possibility of automatically calculating performance measures in the area of:

- customer analytics (e.g. customer behaviour modelling, customer value assessment, customer portfolio analysis etc.),

- marketing analytics (e.g. marketing planning and optimization tools providing marketing management measure; campaign planning and optimization tools using response rates, contribution margins per campaign, conversion rates, campaign ROI; product and brand analysis functions providing performance measures of products),

- sales analytics (e.g. team performance analysis, sales performance analysis),

- service analytics (e.g. customer satisfaction, product quality, and trends related to complaints, resolution quotes, workload in the organization, detailed analysis of service revenues and costs etc.), and

- channel analytics (e.g. web traffic and performance analysis; e-commerce analysis providing measures such as conversion rates, number of unique visitors, and Web site frequency; customer interaction center analytics providing performance and workload of the customer interaction center etc.).

To summarize, a CRM system helps organisations to gain a clear picture of their performance in the area of customer management, marketing, sales, service, and sales channel management. Additional information on the overall business performance can be gathered by implementing or having access to a further performance measurement system that is also based on the data warehouse system and provides information on more general measures, such as employee turnover, employee satisfaction, productivity, services costs, average process cycle time and so on.

4.7 Implications for marketing

The foregoing work has proposed and articulated a marketing framework for customer equity management. The researcher called this framework market-oriented customer equity process. The framework advocates that managers, through the realisation of value-building strategies, **create an organisational system that facilitates the use of customer equity**. In turn, the use of the customer equity process creates and maintains an organisational culture that supports customer equity management and the ability continuously to improve the organisation's business processes, products, and services to enhance customer turnover (or customer lifetime value respectively). Feedback mechanisms throughout the organisation continue to fine-tune the organisational systems and processes.

By focusing on the key elements of customer equity management, a company can develop a stable customer base becoming an integral part of their continued success, thereby developing a competitive advantage.

In customer equity management, one of management's primary duties becomes that of developing and maintaining an organisational system in which value can be continuously created. **Management must create value by means of**

rationalisation and / or growth, i.e. management has the opportunities to reengineer business processes and implement new technology for increasing process efficiency, offer premium products for being able to raise prices, maintain existing customers by increasing loyalty and offering new products, and cover new markets and new channels for increasing sales. Management must also decide how the organisation achieves differentiation, i.e., which value proposition the organisation wants to focus on. In general, an organisation centres on one value proposition and maintains acceptable levels of two or three other value propositions. In total, eight value propositions exist, namely product leadership, service leadership, customer intimacy, operational excellence, brand leadership, economic proposition, functional proposition, and symbolic proposition. The proposed framework for customer equity consists of five steps that allow organisations to develop value-building strategies, choose one value proposition, and continuously enhance customer equity by means of these strategies. The five steps are customer segmentation, gathering of data from competition, development of the value proposition, realisation of the value proposition, and monitoring of the process.

This work provides a common base of understanding that can **reduce some of the existing confusion surrounding customer equity management**, thereby creating a more focused research base and more productive efforts on the part of managers to implement and maintain customer equity management. This work contributed to research by enriching the subject of customer equity management and enabling researchers and practitioners to **better understand the complex nature of customer equity and its value sources.** It visualizes the value sources of customer equity by providing different value-building strategies aiming at creating a maximum of value to increase customer equity. Moreover, the proposed framework gives an overall picture of the level of customer equity achieved by an organisation. Managers can keep these indices as a yardstick, on which improvement efforts in the form of value-building strategies can be focussed.

Part II.

RESEARCH METHODOLOGY: HYPOTHESES AND

QUALITATIVE DATA COLLECTION AND ANALYSIS

5 Chapter 5: Deriving And Setting Hypotheses For Investigation

5.1 Introduction

In today's turbulent environment, customers are playing an ever more important role in business competition because they are the engine of a firm's profit growth. This chapter attempts to investigate which factors influence the profit growth and, hence, drive customer equity. Since in the literature little progress has been achieved in identifying and exploring the causal links between different factors and firm performance, this investigation makes a significant contribution to research. By analysing the body of literature that pays more attention to customer management and distinguishes between a firm's products and its resources and capabilities, this chapter attempts to bridge the gaps that currently exist in our understanding of customer equity.

5.2 The derivation of the underlying factors of customer equity

Many factors may influence customer performance in practice, and all have a significant impact on business performance, especially on profitability. In section 2.7, the researcher identified three main types of customer equity factors, namely market-based assets, value chain elements, and stakeholders.

Research on market-based assets shows that besides intellectual assets, which is a firm's knowledge of competitors and customers, tangible assets have an impact on customer equity (see Srivastava et al, 2001). Tangible assets can be the point of sales, technology (see McNaughton et al, 2002), product development, supply chain management (Hogan et al, 2002), customer relationship management and the acquisition, development and deployment of human resources (see Srivastava et al, 2001).

Academic literature on value chain analysis emphasises the transformation of traditional value chains into more customer-oriented ones (see also Tierney, 2003). By reengineering value chain activities in the area of product

development, production, human resource, marketing, sales, suppliers, distribution, service, infrastructure, finance, government relations, IT, and partnerships (see Forbes, 2007; Walters and Lancaster, 1999a), organisations can create more value for customers. This, in turn, enhances the purchase volume of customers, which results in higher customer profitability (customer equity). Hence, one can see the value chain elements of an organisation as factors of customer equity.

The third research stream focuses on stakeholders, such as competitors, suppliers, customers, or employees, as value-delivering elements. If the relationships with stakeholders are optimised, the value output increases. Optimisation actions can be improvements in product performance, product quality, business processes, skills of employees, prices, point of contact, marketing, or technology (Payne et al., 2000; Flint et al, 1997).

By comparing the three main types of customer equity factors, one can conclude that all these factors tend to fall into seven categories: product, place, price, promotion, process, people, and physical facilities. In particular the frameworks proposed by Walters and Lancaster (1999a), Forbes (2007), Srivastava et al (2001), and Hogan et al (2002) are multi-dimensional in nature and comprise a great number of these categories. The proposed seven categories are identical with the 7Ps marketing mix developed by Booms and Bitner (1981) and support the viewpoint of researchers, such as Rust et al (2001), Blattberg et al (2001), and Berger and Nasr (1998) who see the marketing mix as a crucial element of customer lifetime value and, hence, customer equity.

Organisations use the marketing mix for positioning themselves in the market (e.g. Harrell, 2002). The marketing mix is "a set of controllable variables that the firm blends to produce the response it wants in the target market" (Kotler and Armstrong, 1993; 2005). This means that organisations use the marketing mix for optimising sales and, thus, for increasing customer profits (customer equity). Given the importance of the marketing mix to customer equity management, it is

clear why the use of it for the derivation of the underlying factors of customer equity is justified.

Since the 7Ps marketing mix was developed for the service industry, it is best suited to this study, which also focuses on the service sector, namely the financial services industry. The four Ps of the traditional marketing mix are place, price, promotion, and product and completed by further three Ps, namely process, physical evidence, and people. These three additional components of the 7Ps marketing mix widen the view of researchers to investigate and study customer equity. Overall, the adaptation of the variables of the marketing mix to customer needs assists marketers in creating value and achieving differentiation, which is a key element for ensuring companies' success (Higgins, 1998) and, thus, customer equity.

Both the 4Ps marketing mix developed by McCarthy (1960) and the 7Ps marketing mix for services proposed by Booms and Bitner (1981) represent marketing tools that companies can use for selling their products and influencing consumers' buying behaviour. Hence, the 4Ps and 7Ps stand for the company viewpoint. Researchers, such as Kotler et al (2008) go further and suggest using the 4Ps for developing an integrated marketing programme that delivers superior value to customers. This value delivery leads to highly satisfied customers who buy more and, hence, to an increase in customer lifetime values (customer equity) (see Kotler et al, 2008). Thus, the 4Ps for the manufactured goods sector and the 7Ps for services are suited as dimensions of customer equity.

In the marketing literature, the 4Ps can also be viewed from the consumer perspective, which are then called the 4Cs (Lauterborn, 1990). The 4Cs are: customer needs and wants (product), cost to the customer (price), communication (promotion), and convenience for the customer (place) (see Kotler et al, 2008). Other researchers, such as Dennis et al (2004, 2005) or Kearney (2000) added further components to the 4Cs. Dennis et al (2004, 2005), for example, propose a '7C' for the e-retail mix, adding computing and category management issues, customer franchise, and customer care and

service. The consumer perspective of the marketing mix shows the importance of providing value for customers, which increases customer satisfaction, purchase frequency, and, hence, customer profits (customer equity). However, as this thesis investigates customer equity from the company perspective and focuses on the financial services sector, the 7Ps were used.

The qualitative interviews with marketing experts during the development phase of the hypotheses supported the existence of a close relationship between the 7Ps marketing mix and customer equity. The experts emphasised the fact that the marketing mix variables encourage the concept of value creation and delivery in order to offer a distinctive and meaningful value proposition, which is better than that of competition. They further argued that successful interactions between internal marketing practices can create a strong team spirit and lead to the creation of a motivating and customer-oriented working environment, which enables the organisation to effectively deliver high value.

From the above, one can conclude that the 7Ps marketing mix is an adequate instrument representing the main underlying factors of customer equity. Therefore, it is used as basic concept for the study in this thesis. Table 19 lists the 7Ps on the left hand side and the corresponding factors of customer equity on the right hand side. In this context, it is important to note that only the terms are slightly changed, not the meaning of the terms. In other words, price was labelled price management, place was labelled distribution channel management, promotion was labelled communication management, product was labelled product and service management, process was labelled process management, people was labelled human resource management, and physical evidence was labelled service quality management. The latter referred to service quality as it is similar to the meaning of physical evidence: analysing customer's opinion of how and in which environment the service is delivered. To summarize, all seven factors aim at creating a maximum of value for customers, increasing the managers degrees of freedom in designing their offerings and developing value-based strategies, and enhancing customer equity (see also Abele et al, 2004).

7P marketing mix	Dimensions of customer equity
Price (How much does the product / service cost?)	Price management
Place (Where is the product /service sold?)	Distribution channel management
Promotion (How are the chosen target groups informed about the product / service?)	Communication management
Product (What are the characteristics of the product /service ?)	Product and service management
Process (How are the underlying processes designed?)	Process management
People (How are employees involved?)	Human resource management
Physical evidence (How and in which environment is the service delivered?)	Service quality management

Table 19: The 7Ps marketing mix as guidance for the identification of the dimensions of customer equity

Source: own

To summarise, the seven hypotheses are derived from the literature in the following sections. The main basis for this derivation are the three research streams identified by the researcher in Section 2.7, namely market-based assets, value chain activities and stakeholders. All three research streams use the 7 Ps marketing mix for generating customer equity. In the following, each element of the marketing mix or, in other words, each of the seven dimensions of customer equity is investigated in more detail against the background of these three research streams. Each dimension represents one hypothesis.

5.2.1 Distribution channel management

Distribution channel management is now increasingly seen as one of the key marketing variables (Thornton and White, 2001), capable of providing significant competitive advantage, particularly in service sectors where consumer, technological, and regulatory trends have increased competitive pressures. This increased competition requires improving customer experience with the various sales channels of an organisation through, for example, facilitating the use of a

sales channel or providing price incentives on low-cost sales channels like the Internet. Wright et al (2006), for example, found that consumers are increasingly expecting a service, which is available 24 hours and seven days a week through the year. Hence, financial services firms can influence customer experience by means of distribution channel management. The better customer experience with an organisation is, the more likely it is that a customer makes repurchases, which increase customer profits (customer equity). In general, the financial services sector uses sales channels, such as branch network, salesforce, direct mail, telephone, mobile, or Internet. Overall, finding the right channel strategy that best satisfies customer needs is the aim of distribution channel management. For measuring distribution channel management, the following five items were used in the questionnaire:

- degree to which distribution channel management optimizes service delivery costs,

- degree to which distribution channel management meets more different customer needs,

- degree to which distribution channel management enhances information gathering about channel use of customers,

- degree to which distribution channel management enhances the selling of products, and

- degree to which distribution channel management enhances differentiation from competition.

In the following sections, the connection between these five items and the financial performance of a company (is equal to customer equity because it is measured in the form of company profit in this study) is discussed in more detail.

One opportunity for improving customer profits is providing customers with low cost channels that deliver the product to the customers in the most efficient and cost-effective manner at a very low price. Traditional sales channels, such as salesforce or branch network, are high cost channels because they require

large expenses, whereas direct marketing channels, such as direct mail, telephone, or Internet, require low expenses as they have low levels of personal contact and, thus, do not require a great number of employees. By rewarding customers with price incentives for using low cost channels and by promoting low cost channels through advertising campaigns, organisations might be able to reduce their distribution costs in the long-run (Wright, 2002). **Besides low cost channels, channel support activities**, such as trade discounts, advertising and promotional support, are commonly used motivational tools that attract customers' interest and improve customer profits.

A further opportunity for improving customer profits is to provide an appropriate variety of both high cost and low cost sales channels that meet customer needs. By analysing existing customer data in databases, collecting new data by means of customer surveys, or buying customer data from external data sources, organisations can identify the "ideal" sales channel mix for each customer segment or group. Information such as customers' desired service output from the sales channel or the maximum amount of money customers want to pay for the channel (see Stern et al, 1996) are of importance here. Overall, multi-channel strategies generate sales growth resulting from an extended market coverage, the possibility of offering a broader and deeper assortment of financial products, and a better satisfaction of customer needs (Thornton and White, 2001). Furthermore, multiple sales channels, particularly low cost channels, such as Internet, facilitate cross-selling by means of direct marketing as they offer more opportunities of targeting customers in the most suitable way (see for example Dannenberg and Kellner, 1998).

To summarize, multiple sales channels enable organisations to offer a broader and deeper assortment of products, to reduce service delivery costs by optimizing efficiency of each sales channel, to better and easier contact customers for encouraging repurchases and promoting products, and to reduce waiting time as customers are not dependent on one channel anymore. Thus, sales channel management is a tool for influencing customers' decisions regarding purchase behaviour and related purchase activities, which are the

engine for customer profit growth. Therefore, the researcher addresses H1 as follows:

***H1.* Distribution channel management is significantly related to customer equity (company profit).**

5.2.2 Communication management

Communication from the service provider to the customer is important to improve the financial success of customer relationships in the long run. Written communication by means of letters, direct mail or Web site interactions as well as oral communication with service staff is helpful to customers, generates a positive and pleasant atmosphere, and enhances sales growth. Moreover, communication through non-personal media, such as magazines or TV, attracts new customers and maintains existing customers leading to a better business performance of a company.

The questionnaire used for this study comprised the following five items for measuring communication management:

- degree to which communication management informs customers,

- degree to which communication management encourages customer trust,

- degree to which communication management enhances customer relationships,

- degree to which communication management enhances information gathering about customers, and

- degree to which communication management enhances credibility.

The connection between the dimension communication management and company profit (customer equity) are discussed in the following.

More effective and efficient communication strategies that deliver the right information at the right time to the right customer, increase customer's interest in the organisation and its market offerings, which leads to

an increase in customer profits (customer equity). Developing the right communication strategies requires contacting customers as frequently as they desire. Moreover, it is important to find out which information should be communicated and which kind of communication means should be chosen. Both frequency of communication and content of communication lead to better informed customers if they meet customer requirements.

Communication has a positive impact on trust building among customers (e.g. Sharma and Patterson, 1999), which, in turn, supports the transformation of one-shot purchase transactions with limited profitability into continuous strings of repeat purchases with potential for greater long-term profitability. To improve trust building, communication should be open and honest, advisory suggestions should be transparent, information in advertising campaigns should be meaningful and helpful, the promise of service should be fulfilled (Buttle, 1996), and references and recommendations of satisfied customers and partners should be published (see Plötner, 1996).

Communication can also be effective for **building stronger and more profitable relationships with customers** (e.g. Emerson, 1998), when the communication means are adapted to the three relationship stages: pre-relationship phase, negotiation phase and relationship development phase (Andersen, 2001). The use of different communication means in each stage catches customer's attention and motivates him to make repurchases, which, in turn, enhances customer profits.

In order to develop communication that is relevant to customer needs, organisations attempt to gather as much information on customers as they can. Contact points with customers can generate personal and transactional data about the customer and feedback data from customer complaints, propositions etc. (see Park and Kim, 2003). It is widely acknowledged that **more customized communication** leads to improved purchase behaviour of customers (e.g. Zahay and Griffin, 2003; Storey and Easingwood, 1996; Huang and Lin, 2005), increased purchase volume and thus a better financial business performance (customer equity). In particular, when an organisation intends to

introduce a new financial service, knowing which customers might be interested in the product is essential to a successful product launch.

Given that communication management is an important means for creating financial success, the following hypothesis is proposed:

H2. **Communication management is significantly related to customer equity (company profit).**

5.2.3   Service quality management

In the "age of customer", delivering quality service is considered an essential strategy for success and survival in today's competitive environment. Many researchers have investigated the impact of service quality on customer loyalty, customer satisfaction, and company performance (see for example Zeithaml, 2000; Butcher et al, 2001). It is this impact that requires investigating service quality in the context of customer profits (customer equity).

Service quality management comprises the attributes customers use to judge a service offering and the development of the steps needed to be taken to monitor and enhance the service performance. It further encompasses all aspects of the service firm with which the consumer may interact, including its personnel, its physical facilities, and other tangible elements, i.e. it includes both interpersonal and non-human interactions with service providers (Meuter et al., 2000). In this study, for measuring the dimension service quality management the following five items were used:

- degree of differentiation by means of service quality,

- degree to which service quality enhances customer loyalty,

- degree to which service quality enhances company performance (company profit),

- degree to which service quality attracts customers, and

- degree to which the organisation improves service quality.

The dimension service quality management and its influence on customer profit (customer equity) is discussed in the following sections.

Service quality positively influences customer satisfaction and customer loyalty (see for example Butcher et al, 2001) resulting in sales growth through increased cross-selling (loyal customers purchase more), price premium paid (loyal customers purchase not only cheap products but also expensive products), and positive word-of-mouth communication (loyal customers tend to recommend the company more often than non-loyal customers). Customers are loyal when the delivered level of service quality matches their expectations (Lewis and Booms, 1983). Since each customer has different expectations and preferences, financial services organisations attempt to focus on the determinants of service quality that customers prefer mostly. For identifying customer expectations, organisations continuously collect and analyse data from markets and customers.

Customers purchase more frequently when they are convinced that **the quality of the service provided by an organisation exceeds that of competition**. Therefore, service organisations use service quality as means for differentiation (see for example Stafford et al, 1998). As services are highly intangible in nature due to their lack of physical presence, organisations can only focus on two elements for achieving differentiation: their equipment such as technology or servicescape, and personnel. As a result, service organisations invest in the optimisation of IT-based services and in the development of a consistent service performance from frontline employees. The latter is extremely important because the human factor plays a crucial role in the service delivery process. Unwilling, unfriendly, unknowledgeable, and rude personnel that makes multiple mistakes and is not in a position to take responsibility for errors can even cause customer defection (Allred and Addams, 2000) and, hence, destroy customer profits (customer equity). To conclude, the more the own service exceeds the quality of competitive services, the more customers want to consume this service, which leads to an increase in customer profits (customer equity).

Furthermore, many authors found that service quality has a positive impact on corporate profits (see for example Zeithaml, 2000). Zeithaml (2000) investigated the link between service quality, behavioural intentions, behaviour and financial consequences on the company. She found that the degree of service quality positively influences business performance and, thus, customer profits (customer equity). However, service quality strategies are long-term investments and have a long-term impact on corporate profits. Following the above discussion on service quality, the following hypothesis is established in this thesis:

H3. **Service quality management is significantly related to customer equity (company profit).**

5.2.4 Price management

Because product quality and price directly influence customer's buying decision, it is no surprise that the efforts of marketers have focused on improving product quality and reducing price in order to enhance customer's purchase volume (Grewal et al., 1998). In other words, besides product quality, price plays an important role in increasing customer profits (customer equity). Price management comprises all pricing strategies aiming at optimising prices of products. In the following sections, the relationship between price management and business performance of a company (company profit) is discussed in more detail. To measure the construct price management the following five items were used in the questionnaire:

- degree of price differentiation from competition;

- degree to which the organisation offers reasonable account fees;

- degree to which the organisation offers competitive prices;

- degree to which price enhances customer loyalty; and

- degree to which the organisation offers short-term offers e.g. on savings.

Competitive prices attract customers and enhance customer profits. Therefore, organisations lower prices by either reducing costs and being as cost-efficient as possible or offering the same product at different prices on different channels. Jayawardhena et al (2007), for example, found that price sensitives are the largest cluster among online shopping consumers. However, most customers evaluate the price against the quality of the product to make sure that the purchase of the product is worthwhile. In any case, a favourable price-quality ratio will enhance customer satisfaction (Lam et al., 2004), loyalty (Sirdeshmukh et al., 2002), and customer profits. Whether the price-quality ratio is good or not is strongly dependent on customers' internal reference price, which serves as a standard against which newly encoded prices are compared (Oh, 2003). This means that each customer evaluates the price of a product in a different way and comes to different conclusions concerning the buying decision. Therefore, organisations always need to analyse the price preferences of large customer segments to make sure that the average price preferences are significant and can be used as a clue to develop reasonable prices.

The financial services sector is a very transparent market due to new technology, such as Internet, that facilitates the comparison of market offerings for customers. However, this transparency only applies to simple services that customers can easily understand (see Devlin, 2000), which is why financial services firms attempt to provide **short-term lower-priced offerings and customised bundled offerings** in this area (see for example Campo and Yagüe, 2007). Bundled offerings provide more value to customers as unbundled offerings because the savings on the bundle are higher than the savings on the components. Both short-term offerings and customised bundled offerings have a positive effect on the service purchase decision of a customer, i.e. they lead to an increase in customer profits.

Given the importance of pricing strategies in the context of profit growth, the researcher addresses the following hypothesis:

H4. **Price management is significantly related to customer equity (company profit).**

5.2.5 Product and service management

Organisations need to sell products and services to achieve market share and generate profits. Hence, one can view the products of an organisation as crucial element for sales growth, which is why product management plays a central role. Product management comprises activities, such as product design, product development, prototype testing, and product financing, i.e. it enables organisations to manage and optimise their products. In this study, product and service management is represented in the form of the following five items:

-    degree of product and service differentiation from competition,

-    degree of customization,

-    degree of customer involvement in the product development process,

-    variety of products and services (product and service range), and

-    degree of added value to products and services.

The effect of product management on the financial performance of a company is discussed in the following sections.

Organisations tend to increase the sale of their products and, hence, customer profits, by **launching new innovative services and products** (Claycomb and Martin, 2001), **focusing on cross-selling, and / or customising products**. Customization means creating needs-based products for customer segments (see Jiang, 2000) by involving customers in the customization process (see also Huang and Lin, 2005). For reducing the production costs of customization, organisations use base components, which can be combined with additional components, and offer the most successful bundles as standard-feature bundles.

Gathering data from customers and involving customers in the product development process helps organisations to identify the "right" key features of a product or service, which call customer's attention and stimulate his buying

intention. Hence, continuous feedback from customers by means of customer satisfaction surveys, hot line numbers, or personal interviews, is essential to the financial success of an organisation and, hence, to profit growth (Prahalad and Ramaswamy, 2003). A product development process can comrpise improvements to existing products, cost reductions, repositionings, additions to existing product lines, style changes or new product lines (Akamavi, 2005).

A further means for increasing customer profits is the augmentation of services, i.e. giving customers something extra and **providing them added value** (see for example Duffy, 1998). Examples for service augmentation are sales promotion (e.g. sponsoring workshops and seminars of interest to customers), entertainment (e.g. taking customers to lunch or sporting events), and affinity clubs (e.g. establishing senior clubs that offer travel opportunities) (Claycomb and Martin, 2001). In today's competitive environment, customers expect different added value depending on the kind of the product or service (Devlin, 1998).

To summarize, many studies found a positive relationship between product and service launches (Claycomb and Martin, 2001), customer involvement in the product development process, added value features, and customised products (e.g. Camarero, 2007) and sales growth itself (see, for example, Akamavi, 2005). Therefore, the researcher proposes that:

H5. **Product and service management is significantly related to customer equity (company profit).**

5.2.6 Process management

By definition, reengineering is a "fundamental rethinking and transformation of an integrated set of business processes" (Shin and Jemella, 2002) to create a customer-oriented culture, reduce needed resources, develop a flatter organisational structure, and improve productivity, efficiency, and competitiveness (Hammer and Stanton, 1995). All these factors make an organisation more competitive and attract more customers as the organisation

speaks better "the language" of its customers. This leads to improved business results (Shin and Jemella, 2002) and, hence, higher customer profits. To measure process management in this study, five criteria have been used:

- degree of process efficiency,

- structure of business roles and business rules,

- number of outsourced processes,

- number of redesigned business processes within a company, and

- state of IT.

In the following, the impact of process management on the business performance of a company is discussed.

The main aim of business process management is to achieve significant improvements in business operations and performance by **making the interaction between internal and external business processes and IT more effective** and efficient (Attaran, 2003), e.g. by cutting costs, and increasing quality of goods and services (Andersson et al, 2005). In particular, external processes, which comprise relationships with suppliers and partners, provide huge saving potentials (Champy, 2002) that can be passed on to customers by, for example, reduced prices. Hence, organisations can benefit from redesigned and optimised business processes in two ways: reduced costs and improved customer profits.

The **quicker the service processes** during the service delivery are, the more likely it is that customers make repurchases, which result in an increase in customer profits. For example, the implementation of a new automated credit approval feature coupled with automated business rules and business roles enables banks to decide on credit inquiries on the same business day. This is only possible through an automated decision-making process, which requires that the business roles of employees are adapted to the new software.

Focusing on core activities enables companies to set new standards in their business and to create unique value to customers, which positively stimulates customers' purchase intention and, hence, customer profits. For example,

innovative, reliable, and secure financial services and products with a degree of service quality that differs extremely from competition are an enormous competitive advantage and maintain the existing customer base as well as attract new customers who are willing to pay for this. Outsourcing processes, which do not belong to the core competencies of a firm, helps to maintain a good level of both process types. Common outsourcing areas are software development outsourcing, and web and e-business outsourcing (e.g. Gonzalez et al, 2005). However, to make sure that the outsourcing project has a positive impact on the business performance of the organisation, a pre-project justification and assessment processes must be carried out (see Lin et al, 2007).

To summarize, reengineering business processes in connection with IT implementations and outsourcing non-core processes (Tas and Sunder, 2004) has a significant and positive impact on firms 'financial performance (e.g. Haynes and Thompson, 2000) because it supports product development, cost cutting, and the creation of effective and convenient customer services (Chang-Soo and Davidson, 2004). Therefore, the following hypothesis is proposed:

H6. Process management is significantly related to customer equity (company profit).

5.2.7 Human resource management

Besides technology and servicescape, employees play an important role during the service delivery process as they are in direct contact with customers. This means that employees constitute the interface between a firm's internal and external environment and can have a powerful impact on how customers experience the service organisation. If customer experience is positive, then employees contributed to customer profits through excellence in service delivery. Due to the crucial role of staff, human resource management is becoming important and activities, such as employee empowerment, employee development, or training for improving soft skills (e.g. friendliness) and hard

skills (e.g. knowledge) are necessary. In this study, the following five items were used in the questionnaire for measuring human resource management:

- degree to which the organisation creates a customer-oriented mindset,

- degree to which the organisation informs staff about company planning,

- degree to which the organisation tailors company information to employees' needs,

- degree to which the organisation involves employees in decision-making, and

- degree to which the organisation ensures high job satisfaction.

The connection between human resource management and the business performance of an organisation is discussed in detail in the following sections.

Several studies show that **the employees' level of customer orientation** is an important criterion for increasing a service firm's economic success (e.g. Sergeant and Frenkel, 2000). Customer-oriented service staff focus on long-term customer relationships and attempt to fulfil customer needs rather than just selling a product. Customers benefit from the better treatment and are more willing to buy further products, which in turn increases customer profits (customer equity). Moreover, customer-oriented service staff help an organisation to differentiate itself and to achieve long-term competitive advantage, as customer-oriented service quality is difficult to imitate. To improve customer orientation of service staff, continuous training of employees' social skills and knowledge and intrinsic and extrinsic rewards for performance achieved in terms of service quality and customer focus (e.g. Papasolomou-Doukakis, 2002) are essential.

Better informed employees represent a strategic advantage in terms of customer loyalty and profit growth that can be gained by organisations that succeed in providing quality service to consumers. Therefore, more and more organisations develop well-coordinated programs that aim at **educating and training employees on the service message** and instructing them in how to incorporate this knowledge in their work. Besides communicating what the

service stands for, it is also necessary to inform employees about the aims of new strategies, the success of past strategies, and departmental activities. In this way, employees can communicate successfully the idea of service quality becoming the organisation's mission from staff to the customers. Furthermore, the development of customer-related and service-related information systems that provide information targeted and tailored to the needs of employees support the delivery of high service quality.

Organisations with a high level of hierarchy or bureaucracy perform poorly whereas more innovative organisations with a low level of hierarchy achieved better performance (Hurley, 2002) as they can quicker satisfy customer needs. This means that **employee empowerment**, i.e. making decisions at a lower level of hierarchy, has a direct impact on customers' purchase intentions and customer profits because it encourages employees to deliver the service in a quicker way.

One can conclude that besides empowering and rewarding employees, the employees' level of customer orientation is an important driver of a service firms' economic success (see Bove and Johnson, 2000; Brown et al., 2002; Donavan et al., 2004). By the above discussion of the importance of human resources in the context of profit growth, one can propose the following hypothesis:

H7. **Human resource management is significantly related to customer equity (company profit).**

5.3   Concluding remarks

Managers are giving much attention to the customer equity concept as the cornerstone of the marketing discipline as well as a business philosophy. This customer equity concept emphasises the creation of superior value for customers as key element for ensuring company's financial success (Huber et al, 2001). Since customers are responsible for generating the company's cash flows and since a company's customer equity is the net present value of its

cash flows, it is important to investigate the underlying factors that drive customer equity. In this chapter, the researcher derived seven factors from the literature that might lead to customer equity growth: distribution channel management, communication management, service quality management, price management, product and service management, process management, and human resource management. The links between these seven factors and customer equity are empirically examined in the following chapters. Overall, customer equity factors are the basis around which business strategy and planning, which aim at satisfying market needs, revolves.

6   *Chapter 6: Qualitative Data Collection And Analysis*

Qualitative interviews may be used either as the primary strategy for data collection, or in conjunction with other techniques (Bogdan and Biklen, 1982), such as the quantitative method. In this thesis, the main research technique is the quantitative method combined with the qualitative method, which ensures the validity of the proposed construct, i.e. the dimensions of customer equity. Researchers, such as Strauss and Corbin (1990) or Patton (1990), believe that an effective combination of qualitative and quantitative research in the same research project is useful because the use of both quantitative and qualitative data gives insights that neither type of analysis could provide alone. Hence, applying both types of methods helps to compensate the disadvantages of each method. For example, quantitative research makes it possible to test hypothetical generalisations by using quantitative measures. In this thesis, quantitative research tested the relationships between the dimensions of customer equity and customer equity itself. However, quantitative research is not able to take full account of the many interaction effects that take place in social settings (see Cronbach, 1975). In contrast, qualitative inquiry accepts this complex and dynamic quality of the social world and hence compensates the disadvantage of the quantitative method explained previously. Thus, qualitative methods are appropriate in situations where one needs to first validate the variables that might later be tested quantitatively. In Section 1.6.2, further reasons for the use of a combination of both methods in this thesis are listed.

In this chapter, the qualitative research is presented to ensure the validity of the dimensions of customer equity identified in the previous chapter. Qualitative interviewing utilizes open-ended questions that allow for individual variations. Patton (1990) writes about three types of qualitative interviewing: a) informal, conversational interviews; b) semi-structured interviews; and c) standardised, open-ended interviews. The informal, conversional interviews are spontaneous and loosely structured, i.e. no interview protocol is used. For semi-structured interviews, an interview protocol listing the open-ended questions is used and the questions are asked in any order by the interviewer. Furthermore, the

question wording can be changed by the interviewer if it is deemed appropriate. Finally, the standardised, open-ended interviews are also based on an interview protocol containing open-ended questions, which are asked in the exact order given on the protocol. In contrast to semi-structured interviews, the wording of the questions cannot be changed.

In this thesis, standardised, open-ended interviews are applied because the researcher wanted to use a standardised interview guide with set questions, which are asked of all respondents in an exact order and format to make a form of comparison between answers possible. The interview guide is shown in Appendix 3. Overall, such types of interviews, which are based on an interview guide, ensure good use of limited interview time, make interviewing multiple subjects more systematic and comprehensive, help to keep interactions focused, and make sure that basically the same information is obtained from each person. The information about the respondents from the organisations interviewed are presented in Table 20. In total, twelve interviews were conducted with nine practitioners from the financial services sector and three academics.

So as to ensure this study answered the research questions, as well as to ensure consistency among the interviews, a measurement instrument, in the form of an interview guide, was developed. Based on the review of the literature and the literature used for the derivation of the hypothesis in Chapter 5, twenty probing questions were developed to aid in the collection of data.

The purpose of this study was to explore the perspective of managers who guide or influence customer behaviour with the objective of increasing customer equity. In reviewing the organisational structure of the financial service organisation, it was the middle management that has maximum strategic interaction with customers, thus directing their behaviour by developing appropriate product, marketing, acquisition and retention strategies. As such, a sample of middle management representative of the marketing or customer management division within the service operation, were selected for interviews. In other words, marketing directors, marketing managers, professors of marketing who have been working in that area, marketing assistants (similar

responsibility as marketing manager), and customer relationship managers were addressed for the interviews.

For the selection of the interviewees, three criteria were considered: company size, working experience, and discipline. The first criterion, company size, was met by selecting large financial services organisations with a number of employees ranging from 2,500 to 5,000 employees. This company size was specifically chosen to ensure that the middle management had experience of a wide range of different customer segments and also had significant influence over the strategic use of customer equity and its dimensions. Such experience is less evident in very large financial services organisations (global players), where specialisation can result in teams working in one specific area. Furthermore, for considering regional differences and aspects, organisations from the northern and southern part of Germany and Great Britain were contacted. The second criterion was to capture respondents with a middle working experience ranging from four to eight years as the study addressed the middle management. In addition, such a limitation of the working experience facilitates the comparison of the views, opinions, and perspectives regarding customer equity. Finally, the third criterion required a selection of interviewees who had professional expertise on the same disciplines in the area of customer management with a long-term exposure to a spectrum of practices adopted by the financial services industry. Such disciplines include, for example, the acquisition and rentention of customers, the development of strategic measures for improving customer profits, and the strategic use of technology, such as customer relationship management (CRM). The academics interviewed also have such a background and working experience in the area of customer management. In this context, it is important to mention that the twelve interviewees did not participate in the quantitative analysis, i.e. they did not complete the questionnaire containing questions about the dimensions of customer equity as they would have had an advantage over the other participants.

Contacts with the interviewees were made by sending out letters to financial services organisations that meet all three requirements. Follow-up phone calls

to the marketing managers were successful in obtaining nine interviews. The procedure for the interviews with the marketing professors was identical. The conditions under which the interviews took place were kept as consistent as possible. The introduction to the interview was read so that the same atmosphere and expectations were set. The interviews, ranging in duration from one hour to one and a half hours, were recorded for ease of comprehensive and systematic analysis. This included a process of "reduction" and "interpretation" (Marshall and Rossman, 1999).

To summarise, as the aim of this qualitative analysis was to find out whether the dimensions of customer equity used for the quantitative analysis (see Chapter 9) were valid, standardised open-ended interviews were best suited because they allow the researcher to systematically ask the interviewee questions on the dimensions. Additionally, at the end of each interview, the quantitative questionnaire (see Appendix 2) was checked for content, questionnaire structure, evaluation criteria, scaling used, and wording. Table 21 provides an overview of the key information about the qualitative analysis.

Respondent	Organisational position	Length of working for organisation	Sector	Work responsibilities / area of interest
1	Marketing director	4 years	Banking sector	Strategic marketing, Customer management, Product development
2	Customer relationship manager	5 ½ years	Banking sector	Management of key accounts, Customer relationship management, Marketing
3	Marketing assistant	7 years	Banking sector	Customer relationship management, Marketing management
4	Marketing director	4 years	Insurance sector	Marketing, Strategic customer management, Product

				management
5	Customer relationship manager	8 years	Insurance sector	Management of key accounts, Strategic management
6	Professor of marketing	5 years	University	Customer management, Marketing
7	Professor of marketing	7 years	University	Marketing, CRM, Product management
8	Professor of business management	4 years	University	E-business, International Management, International Marketing
9	Marketing director	7 ½ years	Insurance sector	Strategic marketing, Customer management
10	Marketing manager	4 years	Insurance sector	Campaign management, Strategic customer management, Marketing
11	Marketing director	6 ½ years	Banking sector	Customer relationship management, Strategic marketing
12	Marketing director	8 years	Building society	Strategic marketing, Customer management, Product management

Table 20: Information about respondents

Respondent	Summary of key statements
1	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - providing a balanced variety of high-cost sales channels and low-cost sales channels - using channel support activities to better serve the markets - developing different brands, which are sold through different channel strategies *Measures in the area of communication management for*

	increasing customer profits (customer equity): - avoiding extended periods of time during which customers are not contacted - besides mass media continuously contacting highly profitable customers - enhancing speed of response and quality of information for increasing customer's trust - analysing information on customers to find out which kind of communication is useful for the customer *Measures in the area of service quality management for increasing customer profits (customer equity):* - providing a high level of service quality for highly profitable customers - continuously improving the quality levels of their service surroundings *Measures in the area of price management for increasing customer profits (customer equity):* - following a low-price strategy to differentiate from competition - achieving a better cost structure by providing a limited product range and less distribution channels - using price bundling for customer segments *Measures in the area of product and service management for increasing customer profits (customer equity):* - providing customised services for profitable customer segments - offering standardized routines, such as transactions - providing comprehensive service solutions - using customer relationship management (CRM) system for cross-selling - involving target customers in the product development process - providing added value by encouraging service simplicity *Measures in the area of process management for increasing customer profits (customer equity):* - investing in IT to stay competitive - automating individual procedures, such as wrong transfers - outsourcing IT-based transaction processes to achieve a higher level of service quality *Measures in the area of human resource management for increasing customer profits (customer equity):* - rewarding employees by means of gifts or travels to motivate them and create a customer-oriented mindset - empowering employees because then the service can be provided much faster
2	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - investing in low-cost channels to attract more customers - developing promotion campaigns for new or low-cost channels

	- using multi-channel strategies for interacting with customers
	Measures in the area of communication management for increasing customer profits (customer equity): - sales staff regularly contacts customers or complete customer segments - creating open communication and building customer trust - considering the different customer relationship phases for creating more effective and efficient communication strategies *Measures in the area of service quality management for increasing customer profits (customer equity):* - improving service quality for better satisfying customer needs - regularly monitoring the level of service quality because it is strongly dependent on the performance of the customer-contact employees *Measures in the area of price management for increasing customer profits (customer equity):* - operating as cost-efficient as possible and transferring the economic benefit on to the customer in the form of lower prices - offering bundled products at a reduced price *Measures in the area of product and service management for increasing customer profits (customer equity):* - offering customised services by human tellers - automating routines for reducing the error rate - extending product range by combining own services with those of strategic partners - cross-selling - analysing customer feedback for better satisfying customer needs - informing customers about added value by appropriate promotional activities *Measures in the area of process management for increasing customer profits (customer equity):* - investing in IT to offer reliable and quick services - outsourcing business processes to reduce costs *Measures in the area of human resource management for increasing customer profits (customer equity):* - improving customer orientation by means of rewards for employees - using customer-oriented performance standards for evaluating and rewarding sales and front-stage staff with high customer contact - empowering employees because this creates employee satisfaction, which in turn positively influences customer satisfaction

3	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - increasing the number of sales channels - using segment-based channel support activities - for the branch network, a special brand was developed that highlights the advisory competence of the sales force *Measures in the area of communication management for increasing customer profits (customer equity):* - regularly sending customers personal letters and making telephone calls - supporting open communication with customers - using different communication means for different relationship phases *Measures in the area of service quality management for increasing customer profits (customer equity):* - reducing errors during service delivery process - providing more accurate banking transactions *Measures in the area of price management for increasing customer profits (customer equity):* - offering standard products, such as routine transactions, at competitive prices *Measures in the area of product and service management for increasing customer profits (customer equity):* - providing a balanced range of customised financial services - standardizing transactions for reducing costs and improving speed of service - developing comprehensive solutions for customer segments - focusing on cross-selling - customer involvement in product development - providing added value for filling and exceeding the expectation gap *Measures in the area of process management for increasing customer profits (customer equity):* - using newest technology for improving speed of service delivery - outsourcing complex technologies to use the resources for core competencies, such as financial advice, product development etc. *Measures in the area of human resource management for increasing customer profits (customer equity):* - recruiting people who have the potential to develop a sense of customer responsiveness - informing all employees about visions and corporate objectives - empowering employees to enhance service flexibility and better satisfy the changing needs of customers

	Measures in the area of distribution channel management for increasing customer profits (customer equity): - providing the right combination of low-cost and high-cost channels - using channel support activities, such as sales promotional material, advertising support etc. - offering different kinds of sales channels to provide the most appropriate way of delivering the service to customers *Measures in the area of communication management for increasing customer profits (customer equity):* - avoiding extended periods of time during which customers are not contacted - service employees fulfil the promise made in the service campaigns *Measures in the area of service quality management for increasing customer profits (customer equity):* - improving performance of customer-contact personnel - increasing speed of response and facilitating navigation of the online systems *Measures in the area of price management for increasing customer profits (customer equity):* - having a look at the prices of competition and then analysing customer data for making accurate pricing decisions on new products and services - eliminating price-sensitive customers because they are not loyal *Measures in the area of product and service management for increasing customer profits (customer equity):* - providing a wide range of standardized products and services - investing in customised services - providing additional services delivered by strategic partners - developing cross-selling strategies - gathering information on customer needs by open houses etc. for using it in product development *Measures in the area of process management for increasing customer profits (customer equity):* - investing in IT-based transaction processes and online services for improving service quality - having hosted web-centric solutions at secure data centers to minimize the risk of data abuse *Measures in the area of human resource management for increasing customer profits (customer equity):* - involving front-stage employees in marketing strategy
5	*Measures in the area of distribution channel management for*

	increasing customer profits (customer equity): - attracting young customers by low-cost channels - attracting customer's attention to channels by promotion campaigns - providing different sales channels to realise more various marketing and pricing strategies *Measures in the area of communication management for increasing customer profits (customer equity):* - regular contact with customers to enhance repurchases - promoting the security of service transactions in advertising campaigns to enhance customers' trust - sending customers well-structured, valuable, and personalised messages *Measures in the area of service quality management for increasing customer profits (customer equity):* - continuously improving service delivery process - providing lower level of service quality for unprofitable customers *Measures in the area of price management for increasing customer profits (customer equity):* - offering products at competitive prices - checking customers for price sensitivity - using price bundling - adding monetary value to services *Measures in the area of product and service management for increasing customer profits (customer equity):* - offering insurance services that are highly standardised because this reduces the complexity of such services - customising simple services - using customer data for developing cross-selling strategies - developing up-to-date products by analysing customer needs - adding value by transmitting the customer a feeling of information satisfaction during the purchase search process *Measures in the area of process management for increasing customer profits (customer equity):* - investing in IT applications for automating routines - outsourcing web-centric solutions to increase security *Measures in the area of human resource management for increasing customer profits (customer equity):* - rewarding customer-contact personnel by using customer-focused key indicators - empowering employees for enhancing speed of service delivery
6	*Research on customer equity in the context of distribution channel management:*

	- organisations develop low-cost channels to save costs and stay competitive - increasing number of promotion campaigns combining the sales of a product with a particular sales channel - researchers found that the more channels a firm provides, the higher are the prices of the firm's products and the greater customer's interest *Research on customer equity in the context of communication management:* - respondent observed that regular campaigns encourage customers to increase their purchase frequency - trend towards open communication and more qualitative advertising campaigns - analysing customer experiences in the context of communication management is essential to a profitable customer relationship *Research on customer equity in the context of service quality management:* - service quality is a key differentiation factor in the financial services sector - financial services firms invest high amounts of money in training for optimising knowledge and skills of customer-contact personnel *Research on customer equity in the context of price management:* - trend towards price bundling - importance of analysing price sensitivity of customers *Research on customer equity in the context of product and service management:* - trend towards customisation in the financial services industry - researchers found positive relationship between product management, customer loyalty, and corporate performance (customer profits) - trend towards customer involvement in product development *Research on customer equity in the context of process management:* - decision-making processes can be very complicated and time-consuming and, therefore, need to be simplified - need for outsourcing processes in the area of human resources and IT to stay competitive *Research on customer equity in the context of human resource management:* - organisations need to work on the motivation and skills of employees to develop a more customer-oriented culture - reducing bureaucracy to achieve a higher level of customer orientation

7	*Research on customer equity in the context of distribution channel management:* - trend towards low-cost channels, such as Internet, mobile etc. - researchers found a positive relationship between channel support activities and sales growth - multi-channel strategies are often the case in the financial services sector *Research on customer equity in the context of communication management:* - increasing research on the impact of communication management on sales growth - financial services firms encourage trust-building communication activities with the objective of increasing customer profitability *Research on customer equity in the context of service quality management:* - researchers found a positive relationship between service quality and profit growth - services are intangible and, therefore, service quality plays a crucial role in the financial services sector *Research on customer equity in the context of price management:* - competitive prices are important in the financial services sector due to high price competition - the necessity of differentiating from competition by various bundled offerings at different price levels *Research on customer equity in the context of product and service management:* - trend towards customisation in the financial services industry - researchers found positive relationship between customer profits and product management - more and more organisations seek customer feedback during the product development process *Research on customer equity in the context of process management:* - researchers found that improvements in IT reduce operating or processing costs and increase future economic benefits and customer profitability *Research on customer equity in the context of human resource management:* - rewards, coaching and employee assessments are necessary to achieve a high level of customer orientation
8	*Research on customer equity in the context of distribution channel management:* - financial services organisations provide low-cost channels to better satisfy customer needs

	- channel support activities in the financial services industry are a tool for enhancing customer performance - much research on multi-channel management exists that investigated the positive effects of traditional and new sales channels on the financial performance of a company *Research on customer equity in the context of communication management:* - trend towards individualised communication strategies for better attracting customer's attention - generating positive customer experiences by communication *Research on customer equity in the context of service quality management:* - service quality has an integrating role between the organisation and its customers *Research on customer equity in the context of price management:* - trend towards price bundling in the financial services sector - more and more banks provide short-term price reductions *Research on customer equity in the context of product and service management:* - more and more financial services firms customise their products to attract customers' attention and increase purchase frequency (customer profits) - innovative products always lead to profit growth - trend towards customer involvement in product development *Research on customer equity in the context of process management:* - the highly competitive environment in the financial services sector requires investments in technology for remaining competitive - trend towards empowerment in the financial service sector to improve service quality
9	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - analysing customer data for finding out the most appropriate channels - providing higher levels of channel support to customers - using multi-channel strategies for better marketing products *Measures in the area of communication management for increasing customer profits (customer equity):* - using both personal and non-personal media to keep customers informed about new products, trends etc. - regularly using the campaign management tool provided by customer relationship management (CRM) technology

	- using customer information to provide more customised communication *Measures in the area of service quality management for increasing customer profits (customer equity):* - continuously improving service quality for differentiating from competition - providing higher levels of service quality for key accounts *Measures in the area of price management for increasing customer profits (customer equity):* - offering products in the middle-price segment to stay competitive - analysing the effects of price strategies on customers' financial performance and perception *Measures in the area of product and service management for increasing customer profits (customer equity):* - providing the right balance between standardized and customised products and services - cross-functional team develops products because then products are more innovative - focusing on segment-based cross-selling - organising workshops with customers and other experts to discuss the newest trends, research, and preferences - giving customers with high purchase frequency a bonus *Measures in the area of process management for increasing customer profits (customer equity):* - investing in IT-based insurance processes to reduce labour cost and total administrative expenses - outsourcing IT-based applications and services with the objective of smoothing service delivery cycles
10	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - using customer data and customer feedback for developing channels - coordinating advisory activities to help customers to understand the products and channels - using information on customer purchase behaviour to develop the right multi-channel strategies *Measures in the area of communication management for increasing customer profits (customer equity):* - using personal media, such as personal emails and visits, besides non-personal media - using (CRM) technology to generate more personalised communication *Measures in the area of service quality management for*

	increasing customer profits (customer equity): - developing segment-based service quality strategies - optimising speed of service delivery *Measures in the area of price management for increasing customer profits (customer equity):* - eliminating unprofitable, price sensitive customers because in case of aggressive price offers by competitors customers immediately switch to competitors - making more accurate decisions on pricing by analysing customer data *Measures in the area of product and service management for increasing customer profits (customer equity):* - offering a wide range of standardized products and services - offering only few customised services - developing innovative products for generating additional profit - developing special cross-selling strategies for enhancing customer profits - gathering information about customer needs by means of workshops with customers, open houses etc. - providing customers with added value *Measures in the area of process management for increasing customer profits (customer equity):* - automating business roles to ensure high service quality - improving cycle time by means of outsourcing - implementing employee empowerment programs
11	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - using CRM data for developing the right sales channel - getting the product to the customer in the most efficient and effective manner - using multi-channel strategies *Measures in the area of communication management for increasing customer profits (customer equity):* - contacting customers by conferences, exhibitions, or open houses - preferring customer visits and newsletters to enhance the profitability of customer relationships at a later stage - using CRM technology for managing campaigns *Measures in the area of service quality management for increasing customer profits (customer equity):* - developing service quality strategies on the basis of customer data - optimising marketing and human resources necessary for service delivery

	Measures in the area of price management for increasing customer profits (customer equity): - offering low-price products in the short run - analysing customer perception in the context of price bundled products *Measures in the area of product and service management for increasing customer profits (customer equity):* - analysing customer needs and developing appropriate customised products and services - cross-functional teams ensure that products better meet customer needs - using cross-selling strategies - using the insights from customer satisfaction surveys, and customer complaints as basis for product innovations and improvements - creating consumer delight with additional services *Measures in the area of human resource management for increasing customer profits (customer equity):* - improving behaviour of service employees to increase customer satisfaction - sales staff can now decide on whether credits are approved or not (empowerment)
12	*Measures in the area of distribution channel management for increasing customer profits (customer equity):* - developing low-cost channels, such us the mobile channel - using sales promotional material and advertising campaigns - distributing products by means of multiple sales channels *Measures in the area of communication management for increasing customer profits (customer equity):* - contacting customers for selling products - using customer information for developing more accurate communication strategies *Measures in the area of service quality management for increasing customer profits (customer equity):* - regularly measuring level of service quality - realising service quality improvements (e.g. speed of service etc.) *Measures in the area of price management for increasing customer profits (customer equity):* - providing profitable customer with low-price products in the short run - analysing customer perception on pricing *Measures in the area of product and service management for increasing customer profits (customer equity):* - customisation of financial products as an integral part of market

	segmentation - using segment-based cross-selling strategies - gathering data from customer interaction and participation for the product development process - generating a strong, positive and emotional customer reaction by added value *Measures in the area of human resource management for increasing customer profits (customer equity):* - improving degree of customer orientation

Table 21: Key information about qualitative analysis

6.1 Qualitative analysis of distribution channel management

6.1.1 Low-cost channels

Respondents 1-5 and 12 mentioned that they provide, on the one hand, high-cost sales channels and, on the other hand, low-cost sales channels. By encouraging customers to use low-cost channels, they attempt to save money and reduce costs of customers. When the costs per customer are lower than before, the profits per customer are higher, i.e. these companies can increase customer equity. They also emphasised that they continuously invest in the development of low-cost channels, such us the mobile channel, to attract customers and enhance the creation of customer equity (company profit). They made the experience that low-cost channels lead to profit growth due to better accessible services for a large segment and a large geographical coverage without large-scale investments. Respondents 1-5 emphasised that besides the investments in the new technology, investments in people are necessary to operate and control the more complex distribution structure. Furthermore, they mentioned that the products and other promotional tools have to be adapted to different existing and new channels, which causes additional costs. However, all five respondents viewed such investments as essential and worthwhile because they create higher value for customers, which leads to greater customer satisfaction and, thus, profit growth (increase in customer equity). Overall, the interviews with the respondents 1-5 revealed a trend towards low-cost sales

channels, such as the telephone and the Internet, although this form of sales is more impersonal.

Respondents 9-11 mentioned that their budget for investments in such new low-cost sales channels is limited and, therefore, they attempt to find out customer preferences and then use the knowledge for developing the right sales channel. They emphasised that although they do not provide the complete range of low-cost channels, they made the experience that customers are still satisfied with their service and tend to buy more frequently, which leads to profit growth and an increase in customer equity.

The three interviewed academics (respondents 6-8) also observed this trend. According to them, low cost channel management is becoming important to financial services organisations because they are under pressure due to high competition and, therefore, need to cut costs. Respondent 6 mentioned customers' changing needs as a further reason for this trend. Nowadays, customers more and more expect flexible and cheap sales channels, which support their lifestyle. Respondent 8 explained that financial services organisations provide low-cost channels to better satisfy customer needs and enhance customer's purchase volume, i.e. to increase customer profits.

6.1.2 Channel support activities

Respondents 1-5 reported that they use channel support activities to better serve their markets and counter competition. The most frequently used activities are sales promotional material, advertising support, discounts (special offers), and financial advice. Respondents 1 and 3 mentioned that they first select a sales channel, identify the appropriate customer segment, and then develop their promotion campaigns. In this way, they can better meet customer requirements. All respondents made the experience that customer-focused channel support activities positively influence customers' decisions and behaviours during the purchase process. They further mentioned an increase in customer profits shortly after the promotion campaigns have taken place. This

means that channel support activities lead to profit growth and, hence, increasing customer equity.

Respondents 9 and 10 emphasised the need of providing higher levels of channel support to customers due to the complexity of the insurance products. They mentioned that they regularly coordinate their advisory activities to help customers to understand their products and channels, and make the right decisions. According to them, customers are then more satisfied and tend to take out a further insurance, which results in profit growth (and customer equity growth).

Respondents 11 and 12 viewed sales channels as resources to be managed, i.e. they attempt to get the product to the customer in the most efficient and effective manner. For calling customer's attention to the different sales channels, they use sales promotional material and advertising campaigns. In this way, they can achieve better financial results, i.e. higher profit.

The three academics (respondents 6-8) who have been interviewed also stated that channel support activities in the financial services industry are a tool for enhancing customer performance and, hence, customer profits. They referred to researcher such as Siu (2002) or Mehta et al (2002) who found a positive relationship between channel support activities and sales growth. Respondent 6 observed an increasing number of promotion campaigns that combine the sales of a product with a particular sales channel. This means that a customer can only get the product when he uses the particular sales channel. Respondent 6 emphasised that financial services organisations promote such sales channels with special campaigns to attract more customers and increase customer profits.

6.1.3 Multi-channel strategies

The interviews with respondents 1-5 and 12 revealed that all interviewed financial services institutions use multi-channel strategies for interacting with their customers. The respondents 1-5 and 12 reported that their distribution structure comprises telephone, Internet, branch network, call centre, mobile,

and sales force. Respondents 1 and 2 mentioned the competitiveness of their organisations as key reason for their multi-channel structure. By offering different kinds of sales channels, they can provide the most appropriate way of delivering the service to their customers. They further mentioned that this has a positive impact on the buying behaviour of their customers, i.e. customers make more repurchases, which results in profit growth. All respondents (1-5, 12) agreed to the statement that many different sales channels make it possible to realise more various marketing and pricing strategies, which attract customers' attention. According to them, multi-channel strategies encourage customers to buy further products and, hence, enhance customer profits (customer equity).

Respondents 9 - 11 reported that they also use multi-channel strategies although they provide only a limited range of sales channels. In comparison to the other respondents, their sales channels are mainly sales force and branch network. They mentioned that their customers prefer personal financial advice, which requires the distribution of their products by their sales employees. In their opinion, other technology-based sales channels, such as the Internet, should be provided but are not always appropriate due to their impersonal nature. They made the experience that personal contact with customers is the best way of enhancing profits and, hence, customer equity.

Respondents 1-5 and 12 mentioned that for the improvement in existing sales channels and the development and integration of new sales channels, they regularly use customer data from databases. Information on customer purchase behaviour, such as number of sales transactions or frequently used sales channels, helps them to develop the right multi-channel strategies. Respondents 2 and 3 reported that the more accurate the information on sales transactions is, the better is the financial result of the strategy. In other words, good planned sales channel strategies lead to higher customer profits.

Respondents 1 and 3 mentioned that they have developed different brands, which they sell through different channel strategies. They reported that the use of more than one brand enables them to address more different customer groups and, hence, to enlarge their customer base. In other words, the creation

of various brands supports profit growth because more customers can be targeted. Respondent 1 said that for the online sales channel a completely different brand was created with the objective of attracting young customers. Respondent 3 reported that for the branch network, a special brand was developed that highlights the advisory competence of the sales force. Overall, respondents 1 and 3 made the experience that the involvement of various brands in multi-channel strategies results in a positive and increasing customer equity.

Overall, all respondents (1-5, 9-12) mentioned that multi-channel strategies enable them to better market their products and increase their profits because they support a better understanding of the product portfolio. While simple services do not need to be explained by the sales force and, therefore, can be mainly distributed through impersonal channels, such as the Internet, more complex services need a high level of financial advice, which requires a distribution through the branch network. Respondents 1-5 and 9-12 emphasised the different nature of the financial services products, which requires their distribution through various sales channels.

The three academics (respondents 6-8) who were interviewed also reported that in the literature, much research on multi-channel management exists that investigated the effects of traditional and new sales channels on the financial performance of a company. Respondent 6 mentioned researchers such as Pan et al. (2002) or Ancarani and Shankar (2004) who found that the more channels a firm provides, the higher are the prices of the firm's products. However, customers are willing to pay for the greater.

6.2 Qualitative analysis of communication management

6.2.1 Communication strategies

The interviews with the financial services firms revealed that respondents 1-5 avoid extended periods of time during which customers are not contacted. They

emphasised the importance of a regular contact with customers to enhance repurchases and, hence, increase customer profits (customer equity).

Respondents 1-5 and 9-12 mentioned that they use both personal and non-personal media to keep customers informed about new products, trends etc. Respondents 9 and 10 reported that besides non-personal media they often use personal media, such as personal emails and visits. According to them, customers respond better to personal media because it gives them the feeling of being important. They also mentioned that due to this feeling, customers are more willing to make repurchases, which results in an increase in customer equity.

Respondents 1-3 reported that they regularly send customers personal letters and make telephone calls. The latter is extremely important to the financial success of new products, when mass media parallel stimulates customers' purchase behaviour concerning the new products. They mentioned that this combination leads to a good financial results in the form of profit growth and, hence, increasing customer equity. Furthermore, they reported that they achieve an ongoing contact with customers through open houses for clients and quarterly and annual user conferences. However, all five firms confirmed that the most important thing is to keep alive the relationship with customers by continuously asking for feedback, recognizing events or celebrations in customers' lives, or checking whether customers understand the product.

In particular, respondents 11 and 12 emphasised the need for contacting customers by conferences, exhibitions, or open houses. The two respondents made the experience that customers appreciate an invitation to such an event because they can directly talk to experts and sales staff and get used to new products. Overall, respondents 11 and 12 noticed an increase in profit after such events.

The three interviewed academics (respondents 6-8) also referred to the increasing research on communication management and highlighted the impact of it on sales growth. They mentioned researchers such as Ball et al (2004) who investigated the positive effect of communication strategies on customer loyalty

and the financial corporate performance. Respondent 6 emphasised that regular campaigns encourage customers to increase their purchase frequency.

6.2.2 Open communication

Respondents 4 and 5 reported that they promote the security of their service transactions in their advertising campaigns to enhance customers' trust in the organisation. They made the experience that the more the customers trust a company, the more they are willing to make repurchases. This, in turn, leads to higher customer equity. Respondents 4 and 5 also mentioned that each service employee should be aware of the promise made in the service campaigns and integrate the fulfilment of this promise into his daily work. According to them, this is crucial to a good communication strategy because it positively influences the overall level of trust towards the organisation and its systems.

Respondents 1-5 emphasised the importance of open communication with customers, no matter whether the communication is written or oral. In their opinion, speed of response, quality of information and security play a significant role in creating open communication and building customer trust. When customers have the impression that they are treated fairly, they tend to purchase more frequently. Respondents 1-5 were convinced of the positive effect of open communication on customers' purchase behaviour and, thus, on customer profits (customer equity). Respondents 4 and 5 reported that their account executives belong to the same academic ambience as the addressed customers, i.e. the lifestyle of these executives is similar to that of their customers. In this way, the message is better communicated to the customers and a higher level of trust is created. Overall, respondents 1-5 and 9-12 agreed to the statement that communication is essential to the development of a trustworthy and profitable relationship with a customer. In particular, respondents 9-10 emphasised the need for open communication in the context of the management of highly profitable customer relationships. They reported that key customers with high profitability need to be treated in a special manner, which also includes a fair, quick, and open communication strategy. Only in this way, the profitability of these customers can be guaranteed and enhanced.

The three academics (respondents 6-8) interviewed for this thesis also mentioned a trend towards open communication and more qualitative advertising campaigns. Respondent 7 observed that financial services firms encourage trust-building communication activities with the objective of increasing customer profitability.

6.2.3 Relationship stages

Respondents 1-5 and 9-12 mentioned that they have access to detailed customer information thanks to a customer relationship management system. They also reported that this information is the basis for decisions on when, how and why a customer should be contacted. This means that for a good communication strategy they analyse their information on customers and attempt to find out which kind of communication is useful for the customer. They made the experience that the better the communication strategies are adapted to customer needs, the higher is the response rate and the more customers tend to make repurchases (increase in customer equity).

Respondents 2, 3, 11, and 12 emphasised that they consider the different relationship phases for creating more effective and efficient communication strategies. As customers go through different phases over their lifetime, the respondents adapt the communication means and contents to these phases. According to them, such adaptations have a positive effect on the purchase frequency and, hence, on customer profits (customer equity) because the messages better meet customers' requirements. Respondents 2 and 3 mentioned that for example, in the first phase, the presence of the organisation plays an important role in attracting customers. Therefore, they use communication tools such as mass media advertising, conferences, reputation management, or referrals in this phase. They reported that these types of communication means are best suited to call customers' attention to the financial products. Respondents 11 and 12 mentioned that they prefer customer visits and newsletters to enhance the profitability of customer relationships at a later stage. In their opinion, these two communication means are the best way of contacting customers, presenting products and enhancing customer profits.

Respondents 6-8 said that the principle of learning and transfer of customer experiences in the context of communication management is essential to a profitable customer relationship. This means, primarily, that very good experiences of a customer within the business connection have wide implications on profitability. Such experiences also include the degree of communication displayed by the organisation.

6.2.4 *Customized communication*

The interviews with respondents 1-5 and 9-12 revealed that it is important to gather information about customers and use this information to provide more customised communication. Respondents 1-4, 9, and 10 reported that they regularly use the campaign management tool provided by customer relationship management (CRM) technology to generate more personalised communication. This tool considers person-specific customer information, i.e. data that is specific to a particular person or group of similar people. Such data enables them to develop more accurate campaigns and to better target customers. They further reported that after such campaigns customer profits increase, which results in higher customer equity.

Respondents 3, 5, and 9 also highlighted that the expenditures for generating personalised communication are much higher than those for mass communications although a personalised campaign addresses not only one customer, but also customer groups with similar preferences. In their opinion, these investments are worthwhile because personalised communication increases the probability of repeat purchases and thus improves customer profits (customer equity). This is consistent with the opinion of the interviewed academics (respondents 6-8) who stated a trend towards personalised communication in the financial services sector.

Respondents 10-12 viewed personalised communication as essential to the management of customer relationships, the delivery of higher satisfaction to customers, and the generation of higher profits (customer equity) to the organisation. The respondents recognised that well-structured, valuable, and

personalised communication has a strong effect on customer profits. They mentioned that they regularly analyse customer contact points, such as mass communications, personalised written or digitized communications, and contacts with company personnel, for the qualities of communication and its outcomes. In their opinion, all such communications should be used as relationship-enhancers, offering the customer useful and needed advice and information.

6.3 Qualitative analysis of service quality management

6.3.1 Service quality

Respondents 1-5 and 9-12 reported that they use data from their customer base to identify segments that either are unprofitable or have the highest potential of defection. For these segments, they provide only limited marketing resources and lower service quality. In their opinion, such unprofitable customer segments are too expensive and therefore the service costs for these segments need to be reduced. They mentioned that the loss that such unprofitable customer segments generate also affects customer equity. Therefore, it is necessary to decrease the number of unprofitable customers, which also justifies lower service quality.

Respondents 9-12 emphasised the need for improving service quality for profitable and highly profitable customer segments. They made the experience that superior service quality during the process of service delivery has a positive impact on customer satisfaction. They further mentioned that the more satisfied customers are with the organisation the more willing they are to make repurchases. Overall, in their opinion, service quality plays an important role in the generation of customer profits because it improves not only customer satisfaction, but also the degree of differentiation from rivals. In this context, they also reported that often customers want to do business with their firm because of their high level of service quality. This, in turn, improves the number of new customers and enhances customer equity.

Respondents 2-4 mentioned that the degree of service quality during the process of service delivery is important to customers. In their opinion, both psychological and behavioural factors that include the accessibility to the provider are crucial to high quality service. They reported that they regularly monitor the level of service quality because it is strongly dependent on the performance of the customer-contact employees. They made the experience that customers react positively when service employees perform their task well and have good advisory skills. This reaction includes higher customer satisfaction and higher customer profits (customer equity). Therefore, respondents 2-4 pay attention to the knowledge and skills of their customer-contact employees.

Respondents 1-5 and 9-12 reported that they focus on continuously improving the quality levels of their service surroundings, customer service, and online systems. In this way, they can provide the customers with enhanced quality services and meet their constantly changing needs. Respondents 2 and 4 mentioned an increase in speed of response and easier navigation of the online systems as an example of an improvement in service quality. Respondent 3 reported that a recent improvement in the banking transaction process led to a reduced number of errors and more accurate banking transactions, which resulted in more satisfied customers and increased purchase volume. Overall, respondents 1-5 and 9-12 could identify a relationship between high service quality and increasing customer profits (customer equity). However, the respondents confirmed that it is difficult to investigate what aspects signify high quality to customers. They emphasised the need for a continuous monitoring of service quality and customer profitability.

The interviewed academics (respondents 6-8) stated ongoing research on service quality due to the important role it plays in practice. This research provides evidence that service quality has an integrating role between the organisation and its customers. Respondent 6 mentioned that service quality is a key differentiation factor in the financial services sector, i.e. financial services firms often attempt to achieve high levels of service quality to attract customers and generate customer profits.   Respondent 6 viewed service quality as the

outcome of internal organisational policies and practices that leads to customer value (customer equity), customer satisfaction, and customer loyalty. He mentioned research conducted by Cronin et al (2000) and Butcher et al (2001) as cornerstones in this area.

6.4 Qualitative analysis of price management

6.4.1 Competitive prices

Respondents 1 and 2 reported that they follow a low-price strategy to differentiate from competition. They operate as cost-efficient as possible and transfer the economic benefit on to the customer in the form of lower prices. They made the experience that after reducing the prices of some financial products, the profits of the customer segments or target groups of these products increased. Respondents 1 and 2 further mentioned that such actions, no matter whether they are short-term or long-term, positively influence customer profits and, hence, customer equity.

Respondent 1 reported that the firm achieved a better cost structure by providing a limited product range and less distribution channels. This enables them to be a price leader in the financial services sector. According to respondent 1, the low-price products attract new customers and support the development of long-term relationships with "old" customers. Overall, he reported that low-price products are the key differentiation factor and the motor for profit growth. Respondent 1 named a price reduction in the form of price per transaction as the most frequently used low-price action. In his opinion, this is the most important criterion when customers choose a bank and, hence, should be used as key differentiation factor. Respondents 1 and 2 emphasised the importance of information technology in an organisational environment to create a cost-efficient business structure. They further reported that information technology enables them to reduce prices and provide a good service, which enhances their number of customers and customer equity.

Respondents 3-5 and 9 reported that they first have a look at the prices of competition and then analyse customer data for making accurate pricing decisions on new products and services. They viewed the evaluation of competition as very important because consumers and customers first compare prices and then choose a product. They emphasised that only when one offer financial products at competitive prices, profits (customer equity) can be generated in the long run.

Respondents 4, 5 and 10 pointed out that they segment their customer base according to profitability and then analyse whether customers are price-sensitive or not. They saw unprofitable, price sensitive customers as ballast because in case of aggressive price offers by competitors they will lose these customers immediately. They further mentioned that this type of customer destroys customer equity because he generates losses and not profits. Therefore, they emphasised the importance of identifying price sensitivity.

Respondents 11 and 12 said that they only offer low-price products in the short run to attract customers' attention. They noticed that such price strategies result in higher customer profits and customer equity.

In this context, it is important to note that respondents 6 and 8 referred to the importance of evaluations, which combine loyalty and price sensitivity with profitability based segmentation, to avoid to high price competition and ensure a stable increase in profits. They referred to research conducted by Zeithaml et al. (2001). Respondent 7 mentioned that nowadays there exist banks, which sell their products mainly on the Internet. He further reported that such banks can save costs for sales staff and branch network, which in turn enables them to offer products at very low prices. These products are the key driver of their profits.

Respondents 1-5 and 9 confirmed high price transparency in their sector due to new technology, such as the Internet. Such technology enables customers to easily get a clear, comprehensive, current and effortless overview about a company's quoted prices. Respondents 2 and 3 mentioned that they have installed web-based advisors, which help the customers get all the product- and

price-related information they need for their buying decisions. In this way, customers can select the appropriate financial product that best meets their needs. The interviewees also reported an increase in trust, satisfaction, and profits (customer equity) resulting from such price advisors.

6.4.2 Bundled offerings

Respondents 1, 2, and 5 mentioned that they use price bundling to decrease price sensitivity among customers. They explained that the savings on the component are smaller than the savings on the bundle as a whole and, therefore, customers attach less importance to price and are less likely to search for better prices for the component. They noticed an increasing interest in such price bundled offerings by customers. This customer interest is reflected in an increase in customer profits and customer equity. Respondents 1, 2, and 5 agreed to the statement that adding value to services, no matter whether monetary in the form of price reductions or non-monetary in the form of additional services, leads to an improvement in customer profits (customer equity). According to them, it is essential to develop price strategies that prevent loss of customers and aim at maintaining long-term relationships with customers.

Respondents 9-12 reported that they regularly analyse the effects of price strategies on customers' financial performance and perception. In this way, they are able to make more accurate decisions on pricing. They said that the more the price strategy corresponds to customer needs, the better is the financial result (customer equity). Respondents 10 and 11 emphasised the need for analysing customer perception in the context of price bundled products. They made the experience that for price bundling, the products that are in great demand should be used because then customer profits can be maximised.

Respondents 6-8 observed a trend towards price bundling in the financial services sector. They said that bundled offerings at a reduced price generate a high degree of customer satisfaction, which results in higher customer profits (customer equity). Respondent 7 emphasised the necessity of differentiating

from competition by various bundled offerings at different price levels. In his opinion, financial services firms need to reduce price pressures by developing new price strategies.

6.5 Qualitative analysis of product and service management

6.5.1 Customised products

The interviews with respondents 4, 5, 9 and 10 from the insurance sector revealed that most insurance services are highly standardised, especially statutory ones, such as motor and workers' compensation insurance, whose terms and conditions are specified by the law. In their experience, more standardised insurance services make it easier for customers to choose the most suitable alternative. A greater variety of insurance services would lead to confusion because it would be more difficult for customers to understand more complex services. Despite these problems, they provide a certain degree of customised services to achieve differentiation from competition. Overall, in their opinion it is important to find the right balance between standardised and customised insurance services. They further mentioned that a good structured product range ensures continuous profit growth and, hence, an increase in customer equity.

The three interviews with respondents 1-3 from the banking sector showed that many bank services are standardised and automated, particularly transfers and other routines. In their opinion, there is a trend towards more individual customised financial services offered by human tellers, whereas routines will be completely automated. They mentioned that customisation is necessary to augment customer satisfaction and customer profits.

Respondents 6-8 also stated a trend towards customisation in the financial services industry because customers are becoming ever more demanding. In their opinion, customisation better targets customer needs and increases purchase frequency and customer profits. Overall, they said that it helps an organisation to stay competitive.

Respondents 11 and 12 viewed the customisation of financial products as an integral part of market segmentation because this offers the best way to satisfy individual customer needs without being too expensive. In their experience, customers are highly satisfied with customised products and services and, therefore, they are in great demand. Respondents 11 and 12 further reported that this is reflected in higher customer profits (customer equity).

6.5.2 Innovative services and products

Respondents 1, 2, and 4 mentioned that they attempt to provide comprehensive service solutions. Such solutions include support features that cover some of the activities the customer usually performs to acquire and maintain the product. This means that on the one hand, they offer extensive advisory support encouraging a better understanding of the product and, on the other hand, they provide additional services delivered by strategic partners. The three respondents emphasised the positive effect of such innovative services on customer profits, which requires a continuous development of new financial products and services.

Respondent 3 mentioned that besides a credit approval, customers can also get information on activities around the purchase of a car or a house. He made the experience that customers appreciate such comprehensive solutions and are more willing to try them out. He also mentioned that such solutions generate more customer profits than "normal" products.

Respondents 9, 10, and 11 reported that a cross-functional team develops products and services in their organisations. Such teams are composed of managers from different departments, such as marketing, sales, accounting and IT. They said that this composition ensures that the new products are feasible, not too expensive, and more customer-focused. In particular, the latter leads to higher customer profits because customer needs are better met.

Two out of the three interviewed academics (respondents 6 and 8) referred to the importance of superior value of products and services delivered to customers in the context of customer loyalty, which is the real driver of financial

performance. They mentioned the work of Reichheld et al. (2000) and Heskett et al. (1997) that investigated the relationship between product management, customer loyalty, and corporate performance. Respondent 8 also emphasised that in the financial services sector product innovations always lead to profit growth because such innovations are rare. However, he also said that this profit growth often slows down in the long run because competitors imitate the product innovation.

6.5.3 Cross-selling

Respondents 1-5 and 9 reported that they use their customer relationship management (CRM) platform to gain knowledge on customers. This knowledge enables them to make intelligent decisions as to which customer to acquire and develop, what channels to use when contacting the customer, what products/services to sell, acquire and develop, and how to get the business to deliver excellence. They further mentioned that all this information is needed to cross-sell. They made the experience that the better the offer is, the more the customer tends to buy the offer. This, in turn, enhances customer profits and customer equity. They emphasised that cross-selling, i.e. the sale of additional similar products and services that the customer has never bought before, is a crucial element for achieving profit growth.

Respondents 10 and 11 mentioned that they develop special cross-selling strategies for enhancing customer profits. Respondents 9 and 12 pointed out the importance of cross-selling for increasing profits through every channel from call centre to the web. They also mentioned that cross-selling is only possible when a strategy of market segmentation exists that facilitates the identification of customers perceptions of product characteristics, price, advertising, personal selling etc. They emphasised the need for accurate cross-selling strategies to achieve profit growth.

6.5.4 Customer involvement in the product development process

Respondents 1-5 reported that they involve target customers in the product development process because this brings renewed market freshness and competitive vigour to the employees, designers, systems, subsystems, processes and products. In their experience, such an involvement is one of the best ways of improving product characteristics and meeting customer needs. They further reported that these products are more successful than other products that have been developed without customers. The financial success of these products is reflected in higher customer profits. Respondents 1, 2, and 4 said that customer involvement also facilitates the consideration of the continuously changing customer preferences and makes it possible to offer up-to-date products. Furthermore, they mentioned that for a continuous profit growth, the identification of problems from two perspectives, namely the company perspective and the customer perspective is essential. Customer involvement makes such an evaluation possible.

Respondents 9 and 10 mentioned that they organise workshops with customers and other experts to discuss the newest trends, research, and preferences. In their experience, the output of such workshops helped them to develop new products that are more useful, convenient and state-of-the-art. They said that such products increase customer profits. Respondents 11 and 12 use the insights from customer interaction and participation, customer satisfaction surveys, and customer complaints as basis for product innovations and improvements. Such continuous customer feedback supports their product development process.

The remaining three academics (respondents 6-8) also mentioned a trend towards customer involvement, in particular in the financial services sector and the automotive industry. In their opinion, this trend is the result of increased competition. However, they also mentioned that some financial services firms still take shortcuts by taking a product that one of their competitors has launched and try to improve it without fully appreciating all the elements that went into the original creation and product development. Respondent 7

emphasised that more and more banks and insurance companies organise open houses that expose target customers with "prototypes" and seek their feedback or offer seminars that involve the customers in the concept.

6.5.5 Added value

Respondents 1, 2, and 5 said that they attempt to provide added value by encouraging service simplicity, service convenience, the image of security, and costumer risk reduction. They made the experience that the more additional value is provided, the more customers' attention is attracted. They also reported that this attention also leads to higher customer profits and customer equity. Respondent 1, for example, said that the security of service transactions is continuously monitored and improved to reduce customer's risk. He further reported that customers feel much more secure and it is then more likely that they make repurchases. Respondent 2 emphasised that it is important to inform customers about added value by appropriate promotional activities transmitting the customer a feeling of information satisfaction during the purchase search process and a feeling of satisfaction over his relationship with the company. He also said that customers more and more expect added value, which requires appropriate strategies ensuring profit growth.

Respondents 3, 9 and 10 pointed out the importance of filling and exceeding the expectation gap. Respondent 3, for example, mentioned that credit consumers appreciate additional services, such as information on house building, because they reduce their effort for achieving the aim. He further said that customers are very satisfied with such added value and the organisation uses it for improving customer loyalty. This loyalty also leads to higher customer profits. Respondent 9 said that customers receive a bonus from a certain level of investment. He mentioned the following example: when a customer has a savings account and adds a car loan, the bonus of maybe 0.25 percent for the savings account is calculated based on customer preferences and profitability.

Respondents 11 and 12 pointed out the need for creating consumer delight with additional services. In their experience, customers react positively to additional

services because they generate unexpected value and unanticipated satisfaction. They said that a strong, positive and emotional reaction to a product or service enhances their willingness to make repurchases. Therefore, they viewed added value as driver of customer profits.

6.6 Qualitative analysis of process management

6.6.1 Business process management

The interviews with respondents 1-3 revealed that investments in IT always need to match with the business strategy. They pointed out that investments, which are not worthwhile destroy customer equity because they increase costs. On the other hand, they said that investments in IT are necessary to stay competitive and offer reliable and quick services. They further said that the latter is extremely important in their sector because financial services are highly intangible and, therefore, need to be performed in the best way. Customers often compare the level of service among banks and choose the bank with the best service. They explained that, therefore, technology plays a crucial role in their business and is often used for attracting customers and generate additional customer profits.

Respondents 4, 5, 9, and 10 mentioned the strategic importance of technology and business process management for achieving profit growth. Thus, manager's first consideration is the strategic combination of IT and business performance. Respondents 4 and 5 mentioned that they recently invested in IT-based transaction processes and online services for improving the quality and speed of their standard services. They also reported that customers are now much more satisfied with these services and customer complaints have reduced. They also noticed that customers more frequently take out these insurances, which leads to an increase in customer profits. Respondents 9 and 10 mentioned the modernisation of the service environment and IT-based insurance processes as crucial. They said that these investments enabled them to reduce labour cost and total administrative expenses. Overall, all four

respondents saw IT as a strategic tool that assists them in finding ways of enhancing customer profits (customer equity).

Two out of the three interviewed academics (respondents 6 and 7) referred to the comprehensive research on process management indicating that improvements in IT reduce operating or processing costs and increase future economic benefits and customer profitability (e.g. Krishnan and Sriram, 2000; Dewan and Kraemer, 2000). They also mentioned the highly competitive environment, which requires investments in technology for remaining competitive.

6.6.2   Automated business rules and business roles

Respondents 1 and 2 reported that often for performing special orders many different functions and roles are involved. They also said that normally the fulfilment of a special order requires people from the front, the middle, and the back offices, all of which may be located in different areas. Only standard procedures are automated, but individual procedures, such as wrong transfers, have to be corrected manually. The two bankers further explained that this makes the business process slow and time-consuming. Customers are often frustrated because they expect that their complaints are processed fast. Both respondents made the experience that customers tend to switch to another bank when mistakes or other individual services take long time. This can cause a decrease in customer profits. Therefore, they said that during the reengineering process it is important to update the business roles for reducing the cycle time of individual processes. Furthermore, they concluded that this tendency is the result of the era of internet and mobile commerce in which customers expect orders to be performed much more rapidly than in the past. When an organisation fails to meet this expectations it will no longer stay competitive.

Respondents 9 and 10 reported that the automation of business roles is important to ensure high service quality. In their opinion, employees who work quickly and know what have to be done positively influence the service quality

during the service delivery process. This, in turn, has a positive impact on customer profits and customer equity.

Respondents 6 and 7 mentioned that a decision-making process can be summarized in the following steps: defining which ground documents are needed to support a particular decision, acquiring each document, assessing them, preparing a proposal, and finally passing a resolution. Financial services organisations need to clarify problems referring to these steps. They said that the faster the process is, the less costs it generates and the more satisfied customers are. Overall, they saw this as a motor of profit growth. Respondent 6 also pointed out that depending on the situation, decision-making processes can be very complicated and, therefore, need to be simplified.

6.6.3 Focus on core activities

Respondents 1-5 stated a trend towards outsourcing. Respondents 1-3 mentioned cost reductions as primary motive for outsourcing business processes and complex technologies. They emphasised that cost reductions also positively influence customer equity because costs for providing and delivering the service are decreased. They further mentioned that they have now more time and money, which they invest in their core competencies, such as financial advice, product development, credit approvals etc. In their experience, outsourcing IT-based transaction processes helped them to achieve a higher level of service quality and to develop a greater variety of financial products. Overall, they reported that this led to an increase in customer profits and customer equity. Respondents 4 and 5 said that they have hosted web-centric solutions at secure data centers to minimize the risk of data abuse. In these centers, expert security analysts perform management and maintenance activities for a monetary fee that the organisation has to pay. However, they also stated that the fee is much lower than the investments in manpower, training, and infrastructure, which would have been necessary. Respondents 4 and 5 emphasized the important role of security in the financial services sector and the much higher level of security achieved by outsourcing. They made the experience that customers feel much more secure now and

appreciate the more reliable services by making repurchases, which lead to higher customer profits. Overall, respondents 1-5 were convinced of the cost reduction, increase in profits, and improvements in cycle time resulting from outsourcing. They also mentioned that outsourcing helps them to focus more on their core capabilities, such as advisory competences, which then attracts more customers and increases customer profits (customer equity).

Respondents 9 and 10 mentioned that they also have outsourced IT-based applications and services with the objective of smoothing service delivery cycles and benefiting from specialization. They also reported that they have noticed a positive association between the rate of outsourcing and profit growth. Their outsourced IT-based applications now better reflect the needs of existing and new customer relationships.

Respondents 6 and 7 referred to the work of Carr and Pearson (2002) and Cousins and Spekman (2003) that found a positive influence of outsourcing decisions on an organisation's success and, hence, customer profits. Respondent 6 mentioned the need for outsourcing processes in the area of human resources and IT to stay competitive. In his opinion, cost reductions normally play a crucial role in the outsourcing process.

6.7 Qualitative analysis of human resource management

6.7.1 Employees' level of customer orientation

Respondents 1, 2 and 5 stated that they reward employees by means of gifts or travels to motivate them. They also mentioned that this motivation is essential to the creation of a customer-oriented mindset. When employees benefit from their own efforts in the form of rewards, they are more willing to encourage customers to make repurchases, which results in higher customer profits. Respondent 5 mentioned that in his organisation the performance of customer-contact personnel is measured by using customer-focused key indicators, such as customer's purchase volume or purchase frequency. He further explained that the higher the key indicator is, the higher is the reward. In this way, a high

degree of customer orientation is achieved. Respondent 2 said that besides sales and performance figures they use customer-oriented performance standards for evaluating and rewarding sales and front-stage staff with high customer contact. Respondents 1, 2, and 5 noticed that customer orientation has a positive impact on customers' buying behaviour and, thus, customer profits.

Respondents 3 and 4 mentioned that it is important for human resource management to find people who have the potential to develop a sense of customer responsiveness. For supporting customer orientation, they involve front-stage employees in marketing strategy and regularly inform all employees about visions and corporate objectives to ensure that they have a great deal of knowledge of the organisation's capabilities and resources and of customer needs. They emphasized that employees need to recognize that they are a key component in developing and sustaining a customer orientation for the organisation. In their experience, employee involvement in strategic decision-making is necessary to motivate them and to make the importance of customer orientation clear to them. Overall, they stated that a high degree of customer orientation leads to higher customer profits (customer equity).

Respondents 11 and 12 also emphasised the importance of customer orientation for achieving profit growth. They said that the better the behavior of service employees is, the better is customers' perception of the service and the more likely it is that customers increase their purchase frequency. Both respondents mentioned that regular coaching and staff assessments for determining personal qualities and motives are essential to create a customer-oriented mindset.

The interviewed academics (respondents 6-8) stated that few studies have addressed the construct of customer orientation of service employees and its impact on service firms' success. Respondent 6 mentioned the studies by Brown et al. (2002) or Donavan et al. (2004). He said that the latter study has suggested a three-dimensional conceptualization of customer orientation of service employees, which distinguishes between the employee's motivation to

serve customers, his or her customer-oriented skills, and his or her self-perceived decision-making authority. In his opinion, organisations need to work on these three dimensions to develop a more customer-oriented culture. Respondent 7 mentioned that it is very difficult for firms to achieve a high level of customer orientation and, therefore, rewards, coaching and employee assessments are necessary.

6.7.2 Employee empowerment

Respondents 1, 2 and 4 mentioned that empowerment of employees, particularly service employees, is applied in their firms. They emphasised the important role of customer-contact employee in the service delivery process, which requires empowered employees because then the service can be provided much faster. Respondent 2 reported that empowered employees are much friendlier to customers because they are more satisfied with their job. In his opinion, this higher employee satisfaction leads to higher customer satisfaction because the customer perceives a higher service quality. He made the experience that the higher customer satisfaction is, the higher are customer profits (customer equity).

Respondents 3 and 5 made the experience that the higher the degree of empowerment, the better employees can deliver the service with sufficient degrees of responsiveness and flexibility to satisfy the changing needs of customers. They further asserted that empowerment also leads to greater levels of satisfaction among staff and customers, which results in profit growth.

Respondents 9, 10 and 11 also reported that empowering employees ultimately leads to increased customer profits, while improving customer satisfaction. They said that they, therefore, implemented employee empowerment programs. Respondent 11 said that sales staff can now decide on whether credits are approved or not. He also said that this is only possible due to new technology, which provides sales staff with the necessary information. Overall, all three respondents stated that empowerment is important because it gives service

employees more freedom, responsibility and sense of ownership to satisfy and meet the variable needs of the different customers.

The three academics (respondents 6-8) interviewed for this thesis also mentioned a trend towards empowerment in the financial service sector to improve service quality and the overall process of service delivery. Respondent 6 emphasised the need for reducing bureaucracy to achieve a higher level of customer orientation.

6.8   Summary

This chapter presented the research results of the twelve interviews conducted for ensuring the validity of the seven dimensions of customer equity within the scope of the quantitative analysis.

With regard to *distribution channel management*, the respondents emphasised the need of investing in low-cost channels to attract new customers and retain existing ones. A balanced mix of both low-cost and high-cost sales channels, i.e. multi-sales channels, enables the respondents to develop long-term relationships with their customers which result in a better business performance in the form of increasing customer turnovers.

According to the majority of the respondents, *communication management* should be applied by regularly contacting customers and enhancing the speed of response and quality of information for increasing customer's trust and customer's profitability. In their opinion, trust-building and open communication helps sales personnel to increase sales growth (customer equity).

All respondents agreed that *service quality* plays an important role in attracting customers and encouraging them to buy products because of the lack of tangible products in the service industry. They argued that the level of the service quality is harder to copy for competition than new or modified products and services. Therefore, they spend huge amounts of money in the skills of their staff and in the physical facilities.

With regard to *price management*, one must say that some respondents focus on a low-price strategy which is realised by achieving a better cost structure or / and by providing a limited product range. Other respondents see bundled offerings at different price levels as relevant to improving their position in the market and generating sales growth.

In the context of *product and service management*, most of the respondents mentioned the provision of customised services, the involvement of customers in the product development process and the use of a customer relationship management system as a good basis for improving business performance (customer equity).

Process management was also seen as an important driver of customer equity because by automating individual procedures or outsourcing IT-based standard transactions, the overall service can be improved and costs can be reduced.

Finally, the key statements regarding *human resource management* are mainly focused on empowering and rewarding employees to create a customer-oriented mindset that encourages customer orientation. Both have a positive effect on the service and, hence, on customer turnovers (customer equity).

Part III.

**RESEARCH METHODOLOGY: STATISTICAL PROCEDURE AND
QUANTITATIVE DATA COLLECTION AND ANALYSIS**

7 Chapter 7: Application Of Statistical Procedures

7.1 Introduction

This chapter provides an overview of the research methodology applied in this thesis. To test the seven hypotheses developed in the previous chapter, the following statistical procedure is proposed: validity assessment (content validity and face validity – assessing if proposed variables correspond with research content), exploratory factor analysis (reducing variables to more meaningful factors), reliability analysis (assessing internal consistency / quality of factors), and multiple regression analysis (investigating relationships between independent variables and dependent variable). Figure 34 illustrates this procedure in more detail.

I. Validity assessment
   (a) Content validity
   (b) Face validity

II. Exploratory factor analysis
   (1) Assessment of the suitability of the data for exploratory factor analysis
     (a) Sample size
     (b) Factorability of the correlation matrix
     (c) Outliers
   (2) Factor Extraction
   (3) Factor rotation

III. Reliability analysis

IV. Multiple regression analysis
   (1) Assessment of the suitability of the data for regression analysis.
     (a) Sample size
     (b) Outliers
     (c) Multicollinearity
     (d) Normality
   (2) Model Summary table
   (3) ANOVA table
   (4) Coefficients table

Figure 34: Overview of statistical procedure

Source: own

7.2 Validity assessment

For assessing the validity, the content validity and the face validity are applied. Both methods are explained in more detail in the following sections.

7.2.1 Content validity

Content validity depends on how well items cover the content domain of the variable being measured (Nunally 1978). The evaluation process of this method is undertaken on a qualitative basis. Parasuraman et al (1988) defines content validity as a method that is based on the extent to which the scale items represent a construct's domain and the rigour with which this domain is specified by the generated items that exhaust it (Churchill 1979). Apart from face validity, content validity is the only type of validity for which the evidence is subjective and logical rather than statistical (Kaplan and Sacuzzo, 1993). If the items representing the various constructs of an instrument are substantiated by a comprehensive review of the relevant literature, content validity can be ensured (Bohrnstedt, 1983).

7.2.2 Face validity

Face validity is the mere appearance that a measure is valid (Kaplan and Sacuzzo, 1993). In face validity one looks at the measure and see whether "on its face" it seems a good reflection of the construct. Although face validity is probably the weakest way of demonstrating the construct validity, it does not in any way mean it is wrong, as the researcher on most occasions relies on subjective judgement throughout the research process. When the construct is identified from the literature, its selection is justified, thereby ensuring the face validity of the instrument.

7.3 Exploratory factor analysis (EFA)

"The general purpose of factor analytic techniques is to find a way to condense (summarise) the information contained in a number of original variables into a

smaller set of new, composite dimensions or variates (factors) with a minimum loss of information – that is to search for and define the fundamental constructs or dimensions assumed to underlie the original variables" (Hair *et al.*, 1998). Exploratory analysis examines "possible relationships in the most general form and then allows the multivariate technique to estimate relationships" (Hair et al., 1998). It is used to reduce the many variables to a more manageable set of factors (Aaker and Day, 1986).

7.3.1 Assessment of the suitability of the data for EFA

For the exploratory factor analysis (EFA), it is important to assess whether the data is suitable to this kind of analysis or not by having a look at (a) the sample size, (b) the factorability of the correlation matrix, and (c) the outliers.

(a) Sample size.

For the application of exploratory factor analysis, academics suggest an absolute minimum of five subjects per variable and not less than one hundred cases per analysis (e.g. Tabachnick and Fidell, 2001). However, suggested minimums for sample size include from 3 to 20 times the number of variables (Mundfrom et al, 2005). Most researchers recommend a minimum sample size of 100 to 200 cases for factor analysis (see Loo, 1983; Hair et al., 1979).

(b) Factorability of the correlation matrix.

For an exploratory factor analysis, at least some correlation coefficients in the correlation matrix should show correlations of r=0.3 and greater (Pallant, 2005). In this context, it is important to mention that correlations vary from 1 to -1 and 0 means no correlation. Furthermore, to check whether the data is suitable to exploratory factor analysis, the Kaiser-Meyer-Olkin (KMO) statistics and the Bartlett's test of sphericity should be performed. The KMO statistics varies between 0 and 1. A value of 0 indicates that the sum of partial correlations is large relative to the sum of correlations. In other words, exploratory factor analysis is inappropriate as there is a diffusion in the pattern of correlations. A value close to 1 indicates that the patterns of correlations are relatively compact and factor analysis is appropriate. The factors resulting from the exploratory

factor analysis then are distinct and reliable. The Kaiser-Meyer-Olkin value should be greater than 0.5 (Kaiser, 1974). The second test is the Bartlett's test of sphericity that should be significant (i.e. have a significance value less than 0.05). When this test is significant then exploratory factor analysis is appropriate.

(c) Outliers.

Exploratory factor analysis is sensitive to outliers, i.e. cases with values well above or well below the majority of other cases. One possibility of checking data for outliers in SPSS is the boxplot. Boxplots summarize the scores on a variable by displaying the median, the 25th and 75th percentiles as the lower and upper edges of a box surrounding the median. SPSS defines outliers as any cases which are between 1.5 and 3 boxlengths from the edge of the box, and Extremes are more than 3 boxlengths away (see e.g. Foster, 2001). If the median is not in the middle of the box, the distribution of scores is skewed.

7.3.2 Factor Extraction

Factor extraction means identifying (extracting) the underlying factors or dimensions. There are a number of techniques allowing researcher to extract factors. SPSS offers seven techniques from which principal components is the most frequently used method. Statisticians, such as Kline (1994), also suggest applying an exploratory factor analysis with principal components analysis because it derives as many components as there are variables. For determining the number of factors to extract, the Kaiser's criterion or the scree test can be applied. The Kaiser's criterion means that factors with an eigenvalue of greater than one should be chosen as factors. The eigenvalue of a variable is the amount of variance the variable accounts for. The scree test is available in the form of a scree plot that shows the eigenvalues plotted against the number of factors. The cut-off point for selecting factors should be at the point of inflexion of the curve illustrated in the scree plot (see Cattell, 1966).

7.3.3 Factor rotation

In order to be able to interpret and label the number of factors selected in the previous step, the factors are rotated. SPSS provides a pattern of factor loadings that can be used for interpretation. In statistics, there are two main techniques for rotating factors: orthogonal method and oblique method. The results of orthogonal rotation are easier to interpret and to report although they do require the researcher to assume that the underlying constructs are not correlated (see also Tabachnick and Fidell, 2001). Varimax is the most frequently used orthogonal method (e.g. Kline, 1994) and attempts to minimise the number of variables that have high loadings on each factor. Oblique rotation allows for the factors to be correlated, but they are more difficult to interpret and report (Tabachnick and Fidell, 2001). The most commonly used oblique technique is Direct Oblimin.

The rotated component matrix shows the factor loadings of each variable. In general, all factor loadings below 0.3 or 0.4 are suppressed because they do not represent substantive values (see Stevens, 1996). A factor loading is the correlation of a variable with a factor. Foster (2001) state that factor loadings of or above 0.3 are meaningful and can be retained. Other statisticians suggest a factor loading above 0.4 for a meaningful interpretation (e.g. Stevens, 1986). In other words, exploratory factor analysis identifies a factor structure and deletes variables with low factor loadings.

7.4 Reliability analysis (RA)

Before the dimensions of customer equity are subjected to any further analysis, their statistical reliability should be assessed (Ahire et al., 1996). "Reliability of a measure is the ability to yield consistent results" (Nunnally, 1988). Several measures of reliability can be ascertained in order to establish the reliability of a measuring instrument. These include test-retest method, equivalent forms, split-halves method and internal consistency method. Of all the above methods, the internal consistency method requires only one administration and consequently is supposed to be the most effective, especially in field studies. Moreover, this

method is considered to be the most general form of reliability estimation (Nunnally, 1988). In this method, reliability is operationalized as internal consistency, which is "the degree of intercorrelations among the items that constitute a scale" (Nunnally, 1988). Internal consistency is estimated using a reliability coefficient called Cronbach's alpha (Cronbach, 1951). Peter (1979) states that the most popular measure of reliability is Cronbach's coefficient alpha, which "should be routinely calculated to assess the quality of measure" (Churchill, 1991). Most authors suggest a Cronbach's alpha value above 0.70 for achieving good reliability (e.g. Bagozzi and Yi, 1988). However, other authors, such as Moss et al (1998), suggest that an alpha score of 0.6 is generally acceptable, although this criterion is not as stringent as the more widely recognised 0.7 threshold (Nunnally, 1978).

7.5   Multiple regression analysis

Linear regression investigates the relationship between one independent variable and one dependent variable. Multiple regression analysis is a statistical tool for the investigation of relationships between several independent variables and one dependent variable. In multiple regression, the term predictor variable can stand for independent variable and the term criterion variable can stand for dependent variable. It is valuable for quantifying the impact of various simultaneous influences upon a single dependent variable. In general, multiple regression allows the researcher to ask the general question "what is the best predictor of ...".

To be able to use the factors determined in the previous exploratory factor analysis, it is necessary to calculate the averages of the factors. Each factor then represents an independent variable.

7.5.1   Assessment of the suitability of the data for RA

Before starting with performing the multiple regression analysis, it is necessary to have a look at (a) the sample size, (b) the outliers, (c) multicollinearity, and (d) normality.

(a) Sample size.

Most authors recommend ten to twenty cases per predictor (independent variable). Stevens (1996), for example, recommends that "for social science research, about fifteen subjects per predictor are needed for a reliable equation".

(b) Outliers.

The procedure here is the same as described for the exploratory factor analysis. All independent and dependent variables have to be checked for outliers. Outliers can either be removed from the data set or replaced by less extreme values.

(c) Multicollinearity.

Multicollinearity is caused when two X variables are highly correlated and, therefore, both convey essentially the same information. In this case, neither may contribute significantly to the model (high individual P values) after the other one is included although together they contribute a lot (low overall P value). In other words, multicollinearity is associated with a high degree of correlation between independent variables. As highly correlating independent variables do not make a contribution to the overall prediction of the dependent variable, they have to be avoided. To assess multicollinearity, a correlation matrix like the Pearson correlation matrix has to be analysed. If a correlation coefficient matrix demonstrates correlations of .75 or higher among variables, there may be multicollinearity. Grimm and Yarnold (1997) state that predictors are too highly correlated if they show a correlation higher than .80. Kerr et al (2002) suggest that multicollinearity is the case, if the correlation exceeds 0.70. Other statisticians suggest that correlations of .90 or greater may indicate multicollinearity.

In this context, some general words on the Pearson's correlation analysis are necessary. Pearson's correlation analysis can be applied to measure the strength and direction of a linear relationship between the X and Y variables. The Pearson correlation coefficient is a measure of how highly correlated two variables are. It is a value between 1 and -1, where 1 indicates that the

variables are perfectly correlated, 0 indicates no correlation, and -1 means they are perfectly inversely correlated (e.g. Bower, 2000). Positive correlation indicates that both variables increase or decrease together, whereas negative correlation indicates that as one variable increases, so the other decreases, and vice versa. When there is no relationship between two variables the effect of one variable based on values on the other variable cannot be predicted. In other words, as values on one variable increases there is no predictable change in the other variable.

(d) Normality.

For assessing normality, SPSS provides among other things the following three techniques: boxplots, histogram, and Normal Q-Q plot. All three techniques allow researcher to check visually whether the data is normally distributed or not. The boxplot shows in the middle of the box the median of the data. If this median is not in the middle, then the data is skewed. The histogram plots on the vertical axis the frequency of a variables' scores and on the horizontal axis the variable's scores. The researcher can then assess normality. The Normal Q-Q plot plots the observed value for each score against the expected value from the normal distribution. This plot shows a horizontal line passing through 0 when the data is normally distributed.

In general, data is gathered through a five-point or seven-point Likert scale giving the respondent the possibility of answering more precise. When most respondents rate the variables (questions) towards the higher end of the scale, the data is negatively skewed. In contrary, when most respondents rate the variables towards the lower end of the scale, the data is positively skewed. This skewness can be analysed through the three methods described above. Despite the fact that normality is one assumption of multiple regression analysis, a violation of this assumption has little effects on the results. Research on the performance of linear regression when the normality assumption is violated suggests that the hypothesis tests for b (and therefore r) are fairly robust to violations of normality (e.g. Edgell and Noon, 1984). So even if the

normality assumption is violated, hypothesis tests on b and r tend not to be substantially affected.

7.5.2 Model Summary table

The Model Summary table shows the multiple r (R) which is the correlation between the independent variables combined and the dependent variable. R-square (R^2) is an indicator of how well the model fits the data. It can be used to interpret the observed variance in the dependent variable. An R-square close to 1.0 indicates that the researcher has accounted for almost all of the original variability with the variables specified in the model. In statistics, no rule exists which value of R^2 represents a 'good' regression. In general, in the social and behavioural sciences, an 'R-square' of 0.3 is often considered as a 'good' value (see Freund and Wilson, 1998). The Adjusted R Square is an estimate of R^2 for the population.

7.5.3 ANOVA table

The analysis of variance (ANOVA) table shows the F statistic. If F is significant (the probability value labelled Sig is less than 0.05), R^2 is significantly different from zero. This means that one can assume that there is a linear relationship between the independent variables and the dependent variable.

7.5.4 Coefficients table

The Coefficients table shows the unstandardized coefficients, the standardized coefficient (Beta), and t values and their probabilities (Sig.). The standardized beta coefficient shows how much the independent variables contribute to explaining the dependent variable (e.g. Kerr et al, 2002). The independent variable with the largest standardized beta coefficient has the most impact on the dependent variable. B, the partial regression coefficient, is unstandardized. This means that the value of B is influenced by the scale upon which the independent variables are measured. As different independent variables may be measured on scales of very different units, it is very difficult to compare their

relative influence. Therefore, the standardized coefficient (Beta) is the basis for making comparisons and identifying the degree to which independent variables influence the dependent variable. Finally, the t values and their probabilities (Sig.) show which independent variables are significant.

8   Chapter 8: Quantitative Data Collection

8.1   Introduction

In this chapter, information on the data collection, questionnaire, and industry is given (see Figure 35).

In section 8.2 the sample frame, the sampling procedure, and the sample characteristics are explained in detail. This study addressed sales and marketing managers from the German and British financial services sector.

In section 8.3 the questionnaire used in this study is explained including the questionnaire development, the two pre-tests, the pilot-test, the research administration, the questionnaire design, and the measurement scales. The questionnaire consisted of two parts: a general part with questions about customer equity assessing the state of customer equity in the financial services sector and a second part containing five questions for each hypothesis. The results of the first part are reported in Section 9.1 and the research findings of the second part are presented in Sections 9.2 and 9.3.

Industry:	financial services sector
Sampling procedure:	questionnaires were sent to sales and marketing managers; 54 questionnaires from German financial services companies and 58 from British financial services companies were returned;
Questionnaire:	section one included questions about the state of customer equity management in practice (e.g. advantages, reasons etc.); section two contained 35 items assessing the participants' perception of the seven dimensions of customer equity;

Figure 35: Overview of key data on quantitative data collection
Source: own

8.2   Sample

8.2.1   Sample frame

The sample frame for this study was comprised of marketing executives, sales executives, and customer relationship managers from the German and British financial services industry, and covered a wide spectrum of customer management activities, such as marketing research, customer acquisition, customer retention, strategic planning, customer management technology, logistics, and financial planning. In the following, the financial services sector is described and analysed in detail.

8.2.1.1   Characteristics of the financial services sector

Practitioners and researchers (e.g. Caruana, 2002) have acknowledged a dramatic increase in competition from both traditional and non-traditional financial services institutions, along with a decline in consumer loyalty. To remain competitive, financial services firms train and inform staff, optimise business processes, and implement technology supporting the service process. Overall, these measures lead to reductions in cycle time and improvements in service quality, which, in turn, positively influence customer loyalty. Particularly, new technology, such as e-business platforms or enterprise mobilization, plays an important role in satisfying customer requirements and providing individualized services (see Luarn et al, 2003). Furthermore, such individualised services can increase sales, enhance customer loyalty by improving relationship with customers, or in other words, increase profit and profit (Huang and Lin, 2005). To summarize, all these mentioned factors have driven a fundamental shift from product-centered, supply-based firms to customer-centered, demand-based firms, in which identifying customer needs and customer profitability play an important role.

8.2.1.2 General development of the banking sector

During the 1980s, the industry experienced significant deregulation (Flier et al. 2001), resulting in rapid growth in market opportunities. For example, as building societies began competing directly with banks, the number of products and services on offer to customers rose sharply (O'Brien and Meadows 2003). Through the late 1980s and 1990s, the banking industry in the UK and in other European countries struggled to provide new delivery channels to customers, including telephone and PC banking (Sievewright 2001). In addition, the worldwide recession of the 1990s produced pressures on profit margins, leading to reductions in staff numbers and a narrower range of product offerings (O'Brien and Meadows 2003). At the beginning of the 21th century banks suffered from a worldwide economic downturn caused by weakened markets. Since the second half of 2007, global capital markets have been affected by a credit crisis, which began with a decline in US house prices and high default rates on "subprime" and other mortgage loans made to customers with weak credit histories or poor creditworthiness. This credit crisis led to liquidity difficulties of major financial services organisations and significant losses. In the long run, the financial services sector will be faced with problems in cutting costs and reducing staff.

8.2.1.3 General development of the insurance sector

Through the 1990s, the insurance sector was characterised by largely stagnant or falling prices and surplus capacity. The market was also characterised by rising pension provision and life insurance and stagnant premium income from general business because of high competition. Additionally, through the 1990s, large insurance companies were formed by means of mergers and acquisitions. Since 2000, the insurance sector has been in a phase of rising prices due to a number of losses and a weak global economy in recent years. Liberalization policies, the globalization process, and the developments in information technology are also factors that influence the performance of the insurance sector (Barkur et al, 2007). In particular, the liberalization process encourages

insurance organisations to engage internationally as to date the sector is liable to regulatory obstacles. For the life insurance sector, significant growth is predicted due to increasing life expectancy and a falling birth rate in developed countries.

8.2.1.4 Key figures for the British and German banking industry

The UK financial services industry is one of the most important economic segments in the country, paying a third of all corporation tax. The seven major players are HSBC Holdings, Royal Bank of Scotland, Barclays Bank, HBOS, Lloyds TSB Group, Standard Chartered, and Abbey National (Maslakovic, 2005). In the German market, the seven major players in the banking industry are Deutsche Bank, Commerzbank, Dresdner Bank, DZ Bank, Landesbank Baden-Württemberg, KfW Bankengruppe, and HVB Group (Ranking German Banks, 2006).

UK banking sector deposits are with a value of $4,555 billion ranked second in the world and ranked first in Europe at the end of 2005 (Maslakovic, 2005). German banking sector deposits are the fourth largest in the world and the second largest in Europe. They amount to $3,071 billion. The country with the largest banking deposits is the US with a value of $5,153 billion. The top position of the UK banking sector results mainly from the fact that half of its banking sector assets are foreign owned.

Another important indicator in the banking sector is the cost/income ratio indicating the banking efficiency. The figure measures bank's operating costs as a proportion of total income. In 2006/07, the cost/income ratio for the UK banking industry amounted to 50.2% and was ranked first in the world. The cost/income ratio for the German banking industry reached 61.5% in 2006/07 (Maslakovic, 2005). The worst performer was Japan with a cost/income ratio of 69.4%.

8.2.1.5 Key figures for the British and German insurance industry

The largest UK long-term insurance companies are Prudential, Standard Life, AVIVA, HBOS, Lloyds TSB Group, Legal & General, and AXA (Maslakovic, 2005). In Germany, the largest insurance companies are Münchener Rück, Allianz, Hannover Rück, R+V, Debeka, HDI, SIGNAL / IDUNA, and Victoria (Insurance ranking, 2004).

The UK insurance market was ranked third in the world and ranked first in Europe with a premium income of $294.8 billion and a market share of 9.1% in 2004. The market share of the UK insurance market increased by 3.3% compared to 1996. The German insurance market totalled $190.8 billion and reached a market share of 5.9% in 2004 (Maslakovic, 2005). In comparison to 1996, the German market share decreased from 9.9% to 5.9% while the premium income rose from $89.8 billion to $190.8 billion. In total, the premuim income of all insurance markets in the world rose from $909.1 billion in 1996 to $ 3,243.9 billion in 2004 indicating a strong growth of the capital base over the last eight years. The country with the largest insurance market is the US with a premium income of $1,097.8 billion and a market share of 33.8%, whereas Belgium is the country with the smalest insurance market. The latter has a premium income of $38.9 billion and a market share of 1.2% (Maslakovic, 2005).

8.2.2 Sample frame justification

For a number of reasons, the research setting chosen for this study was the financial services industry. The financial services industry is applicable as relationships between service providers and their customers have been noted to be of importance in this industry and customer equity research encourages the development of long-term relationships.

Second, it is essential that this study is carried out in a sector where IT has a strong impact on customer relationships. Studies showed that the financial services sector has a higher growth rate concerning the implementation of customer relationship management systems (CRM) (e.g. Pierre Audoin

Consultants, 2006) than most other industries. CRM helps these firms to identify, analyse, and manage their relationships with customers and view these relationships from a financial perspective, i.e. to calculate customer lifetime value, customer profitability, and, hence, customer equity. It is clear from the above that this sector shows a greater interest in customer equity research than other industries and, therefore, was chosen for this study.

Third, the focus on a particular industry has the advantage of a high level of internal validity. Fourth, it allows a more facilitated consideration of the entire organisation and its processes, and the possibility of drawing more corresponding conclusions without any dilution due to a variety of branches. Hence, confining this study to one industry, namely the financial services industry, was of great importance.

8.2.3 Sampling procedure

For investigating the various dimensions of customer equity, a survey in the British and German financial services industry was conducted. The sample was drawn from several databases that contain information and data on financial services companies. Banks, insurances, and building societies were selected for the survey. In total, the questionnaire was sent to 132 British companies and 150 German companies addressing managers in the area of sales or marketing. This target group was selected because customer equity management is normally positioned in the marketing department, sales department or service department and marketing directors or sales directors are qualified for a comprehensive evaluation of a firm's marketing practices.

The questionnaire asked for respondents' perceptions on a range of organisational variables including the nature of distribution channel management, communication management, service quality management, price management, product and service management, process management, and human resource management. This information was collected using a five-point Likert scale (1= strongly disagree to 5 = strongly agree) indicating varying degrees of agreement to statements about these variables. A more general part

at the beginning of the questionnaire asked the respondents questions about methods, importance, requirements, benefits, problems in relation to customer equity.

Questionnaires were distributed by email and post with a cover letter describing the study. All participants could choose between an online questionnaire and a paper-based version. Finally, 112 questionnaires, 54 from German financial services companies and 58 from British financial services companies, were returned and used for the empirical analysis.

8.2.4 Improving the response rate

Fieldwork in the financial services sector was constrained by both time and limited financial resources, which were further frustrated by a number of unanticipated access difficulties, although the multi-strategy research employed in this study did prove effective in generating useful data. As some of the survey questionnaires have been affected by missing data, the researcher made a call encouraging the participants to provide information on incomplete items. Furthermore, to improve the response rate, the researcher made two reminder calls to who had not responded, one after two months and a second one after a further month. The researcher was also constrained by time, financial support and the nature of the fieldwork, as data collection often depended on the researcher's personal relationship with contacts.

8.2.5 Sample characteristics

Characteristics of the respondent sample are exhibited in Table 22. For the purpose of investigating the association between the dimensions of customer equity and customer equity itself, a cross-section of 112 banks, building societies, and insurance companies was utilised in generating the data. 34.8% of them had a turnover lower than 1,000 million Pounds, 30.4% had a turnover between 1,000 million Pounds and 5,000 million Pounds, whereas 34.8% had a turnover higher than 5,000 million Pounds (see Table 22). With regard to the company size, the number of employees of almost half the companies is below

2,000 employees, whereas around 21% of the companies employ more than 7,500 employees.

Turnover in Mio £	%	N
< 1,000	34.8%	39
1,000 – 5,000	30.4%	34
> 5,000	34.8%	39
Number of employees	%	N
< 2,000	46.4%	52
2,000 – 7,500	33.0%	37
> 7,500	20.6%	23
Profit in Mio £	%	N
< 50	53.6%	60
50 – 500	36.6%	41
> 500	9.8%	11

Table 22: Sample characteristics
Source: own

8.2.6 Independent-samples t-test

The t-test is the most elementary method for comparing two groups' mean scores. In this thesis, independent-samples t-tests were run to determine if significant differences exist between the German and British respondents, on the selected variables, i.e. on company turnover, number of employees and profit. Before performing these independent-samples t-tests, a number of assumptions have to be checked for violation, namely (a) independence of observations, (b) normal distribution and (c) homogeneity of variance. Each of these assumptions is discussed in the following.

(a) Independence of observations. The observations that make up the data for the study must be independent of one another. This means that any situation where the observations or measurements are collected in a group setting, or subjects are involved in some form of interaction with one another, should be considered suspect. As data for this study were gathered by asking managers of different firms for filling in a questionnaire, the observations are independent and hence do not violate this assumption.

(b) Normal distribution. For checking normality, the distribution of the three variables used in the t-tests was analysed by using histograms. The results showed that all three variables were positively skewed and hence violated this assumption. However, with large enough sample sizes (e.g. 25+), which was the case in this study, the violation of this assumption should not cause any major problems (see discussion of this in Gravetter and Wallnau, 2000; Stevens, 1996).

(c) Homogeneity of variance. The Levene's test for equality of variances checks whether the variance (variation) of scores for the two groups, in this case the German and British companies, is the same. The results of the Levene's test are presented in the output of the t-test. If the Sig. value is larger than 0.05, one should use the first line in the table, which refers to equal variances assumed. In contrast, if the significance level of Levene's test (Sig. value) is 0.05 or less, this means that the variances for the two groups are not the same. Then one should use the information in the second line of the t-test table, which refers to equal variances not assumed. Tables 24, 26, and 28 show the results of the Levene's test for the three variables company turnover, number of employees, and company profit. Each variable violated the assumption of equal variance as all three Sig. values were less than 0.05, namely 0.008 for company turnover, 0.030 for company size and 0.015 for company profit.

Therefore, the second line of the t-test tables was used for finding out whether there is a significant difference between German and British companies. If the value in the column labelled Sig. (2-tailed) is above 0.05, there is no significant difference between the two groups. No differences between German and British

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companies were found for company turnover (Sig.=0.096), company size (Sig.=0.200) and profit (Sig.=0.075) as all three values were above 0.05.

	Country	N	mean	Std. Deviation	Std. Error Mean
company turnover 2004 in £	German companies	54	18939.712	67840.9382	9231.9823
	British companies	58	3249.074	5029.3642	660.3879

Table 23: Group statistics for the variable company turnover

Source: Output from SPSS

	Levene's Test for Equality of Variances		T-Test for equality of means							
company turnover 2004 in £	F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference		
									Lower	Upper
Equal variances assumed	7.182	.008	1.757	110	.082	15690.638	8931.23	-2008.96	33390.24
Equal variances not assumed			1.695	53.542	.096	15690.638	9255.57	-2869.29	34250.57

Table 24: Independent Samples Test for the variable company turnover

Source: Output from SPSS

	Country	N	mean	Std. Deviation	Std. Error Mean
number of employees	German companies	54	6823.48	12832.268	1746.250
	British companies	58	13395.55	36323.003	4769.444

Table 25: Group statistics for the variable company size

Source: Output from SPSS

	Levene's Test for Equality of	T-Test for equality of means

number of employees		Variances							95% Confidence Interval of the Difference	
		F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference		
									Lower	Upper
	Equal variances assumed	4.842	.030	-1.258	110	.211	-6572.07	5223.514	-16923.8	3779.70
	Equal variances not assumed			-1.294	71.916	.200	-6572.07	5079.073	-16697,2	3553.07

Table 26: Independent Samples Test for the variable company size

Source: Output from SPSS

	Country	N	mean	Std. Deviation	Std. Error Mean
company profit	German companies	54	121.981	453.9476	61.7744
	British companies	58	396.929	1058.6679	139.0099

Table 27: Group statistics for the variable company profit

Source: Output from SPSS

company profit		Levene's Test for Equality of Variances		T-Test for equality of means						
		F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
									Lower	Upper
	Equal variances assumed	6.111	.015	-1.763	110	.081	-274.948	155.9444	-583,99	34,09
	Equal variances not assumed			-1.807	78.446	.075	-274.948	152.1178	-577,76	27,86

Table 28: Independent Samples Test for the variable company profit

Source: Output from SPSS

8.3 Questionnaire

8.3.1 Questionnaire development

For analysing and testing the seven hypotheses identified in Chapter 5, a survey questionnaire was used. This questionnaire was developed from the literature review as well as from the results of the twelve in-depth interviews. Two pre-tests and one pilot test were carried out to ensure that the questionnaire was meaningful and covered a wide range of customer equity research.

8.3.1.1 First pre-test with experts

Nine professionals and three professors were asked to assist in the piloting of the questionnaire to ensure that a spectrum of perspectives were included. At the beginning of each interview, interviewees were briefed about the main objectives of the study. Each respondent was told that the interview would be conducted anonymously, and assurances were given that all information would be treated as confidential, only being used for research and academic purposes.

The objective of the piloting procedure was to refine and streamline the questionnaire. The experts checked the questionnaire by posing for instance the following questions: are the questions too vague?; are the questions too precise?; or, perhaps biased?; is the question by any chance too demanding, or is it within reach for an expert?. Furthermore, the questionnaire was also checked regarding content, i.e. experts were asked about what they considered to be important past and future research contributions, and major limitations in customer equity research. Overall, feedback on the instructions, evaluation criteria, scaling used, questionnaire structure and time taken were taken into consideration. Some minor changes were made to the wording. In this context, it is important to note that Chapter 6 contains information on the key findings of these in-depth interviews.

8.3.1.2 Second pre-test with students

After the consideration of the amendments by the experts, a further pre-test was carried out to optimise the wording of the questionnaire and make sure that respondents will understand the questions. Hence, less attention was paid to the content of the questionnaire as this has already been discussed with experts in the first pre-test. In this second pre-test, students evaluated each question and insights were obtained on how to structure communication in the questionnaire.

8.3.1.3 Development of the web-based questionnaire

Besides a paper-based questionnaire, respondents had also the possibility of filling in a web-based questionnaire. To develop the web-based questionnaire, the researcher contacted a service provider that offers services for creating customized online surveys, distributing them via the internet or email, and tabulating results automatically. The researcher programmed the complete questionnaire by using the software module of the service provider. The internet link of the questionnaire was then mentioned in the cover letter, which was sent to the marketing and sales executives together with the paper-based questionnaire. In this context, it is important to note that the content of both the paper-based and web-based questionnaire is identical.

8.3.1.4 Pilot-test with students

After developing the questionnaire by means of the online software module, it was checked for mistakes by students, i.e. ten students filled in the web-based questionnaire and looked for errors in the programming and possible spelling mistakes. It turned out that the web-based questionnaire is understandable and easy applicable.

8.3.2 Administration of the questionnaire

The administrative handling process of returned paper-based questionnaire was completely separated from that of returned web-based questionnaires, because

for the latter an online software module was used, which stored automatically the complete results in a downloadable format. Hence, it was possible to transfer the results of the survey to SPSS. Data from paper-based returned questionnaires was manually typed into SPSS.

8.3.3 Questionnaire design

The questionnaire was designed from the literature review as well as from the results of the twelve in-depth interviews. The questionnaire for this study was divided into two parts and was designed to measure the influence of various factors on customer equity. Part one was created to determine the state of customer equity management in the financial services industry, in particular customer equity methods, risks, advantages and reasons of customer equity management. Part two contained 35 items assessing the participants' perception of the seven dimensions of customer equity. During the development of the questionnaire, several interviews with experts were conducted to ensure that the content is adequate for a good customer equity construct. The questionnaire was first developed in English and at a later stage translated into German. In the appendix, an overview of the complete questionnaire is provided.

8.3.3.1 Measurement scale used in part one

As already mentioned above, section one of the questionnaire included general questions about customer equity, which were presented in Section 9.1. These questions are informative in nature and were not used for the empirical investigation of the underlying factors of customer equity. Therefore, not only multi-item scales, but also single-item scales were used although multi-item scales are favoured by researchers because they are a more comprehensive evaluation instrument, which makes it possible to assess reliability. However, it was not necessary to measure reliability of these questions.

8.3.3.2 *Measures of part two*

The seven dimensions of customer equity consisted of 35 individual items (see Table 29), which were derived from the marketing literature in Chapter 5. These seven dimensions of customer equity can be described as follows:

(a) Dimension 1. Distribution channel management consisted of items, which were related to adapting distribution channels such as internet banking or mobile banking to customer needs in order to better meet customer preferences and to optimize costs.

(b) Dimension 2. Communication management consisted of items that were related to the use of the right communication tool at the right time and the communication of the right information.

(c) Dimension 3. Service quality management consisted of items, which were related to the development of consistent service performance from frontline employees and IT-based services.

(d) Dimension 4. Price management related to items that were associated with price differences in the financial services sector.

(e) Dimension 5. Product and service management referred to items that were associated with the development and management of customised and differentiated product offerings.

(f) Dimension 6. Process management consisted of items, which were related to changes in technology and corporate structure by organisations to create more unique customer-oriented processes.

(g) Dimension 7. Human resource management related to items that were associated with training, rewarding, and empowering staff to improve employees' skills and to increase employee satisfaction.

Table 29 illustrates the variables of each dimension in more detail. Each variable represented a question in the questionnaire.

Dimensions	Variables
Dimension 1: Distribution channel management	*distrib1* - degree to which distribution channel management optimizes service delivery costs
	distrib2 - degree to which distribution channel management meets more different customer needs
	distrib3 - degree to which distribution channel management enhances information gathering about channel use of customers
	distrib4 - degree to which distribution channel management enhances the selling of products
	distrib5 - degree to which distribution channel management enhances differentiation from competition
Dimension 2: Communication management	*communi1* - degree to which communication management informs customers
	communi2 - degree to which communication management encourages customer trust
	communi3 - degree to which communication management enhances customer relationships
	communi4 - degree to which communication management enhances information gathering about customers
	communi5 - degree to which communication management enhances credibility
Dimension 3: Service quality management	*service1* - degree of differentiation by means of service quality
	service2 - degree to which service quality enhances customer loyalty
	service3 - degree to which service quality enhances company performance (company profit)
	service4 - degree to which service quality attracts customers
	service5 - degree to which the organisation improves service quality
Dimension 4: Price management	*price1* - degree of price differentiation from competition
	price2 - degree to which the organisation offers reasonable account fees
	price3 - degree to which the organisation offers competitive prices
	price4 - degree to which price enhances customer loyalty
	price5 - degree to which the organisation offers short-term offers e.g. on savings
Dimension 5: Product and service management	*product1* - degree of product and service differentiation from competition
	product2 - degree of customization
	product3 - degree of customer involvement in the product development process
	product4 - variety of products and services (product and service range)
	product5 - degree of added value to products and services
Dimension 6: Process management	*process1* - degree of process efficiency
	process2 - structure of business roles and business rules

	process3 - number of outsourced processes
	process4 - number of redesigned business processes within a company
	process5 - state of IT
Dimension 7: Human resource management	*human1* - degree to which the organisation creates a customer-oriented mindset
	human2 - degree to which the organisation informs staff about company planning
	human3 - degree to which the organisation tailors company information to employees' needs
	human4 - degree to which the organisation involves employees in decision-making
	human5 - degree to which the organisation ensures high job satisfaction

Table 29: Variables of dimensions used in the empirical analysis

Source: own

8.3.3.3 Measurement scale used in part two

The dimensions of customer equity were measured using a combination of five items (multi-item scales). In other words, each dimension was represented with five items (questions) in the questionnaire and was measured with a five-point Likert-type scale ranging from "strongly disagree" (1) to "strongly agree" (5). The researcher used multi-item scales because they have a number of advantages in comparison to single-item scales. By using multi-item scales, survey respondents were not just asked to give an overall evaluation of the influence of the dimensions on customer equity but were also asked to rate the key components of the dimensions. In other words, marketing experts were asked to evaluate the influence of the items of each dimension on customer equity. Thus, the use of multi-item scales leads to a more comprehensive evaluation of the construct as multi-item scales are more reliable and the exact reliability rate can be measured. Furthermore, the preference in marketing seems to be for the use of multi-item scales (Churchill, 1979; Nunnally, 1978).

In contrast, a single-item scale cannot provide information on components and cannot assess various dimensions separately, therefore it may not capture the complexity of the dimensions of customer equity entirely. Second, it is very

difficult to assess reliability with a single-item measure. Thus, to overcome these shortcomings, multi-item scales were used in this study.

8.3.4 Justification for the measure customer equity

In this study, customer equity was measured by using company profit, which is the sum of customer profits (profitability) from all customers. As this information was already available from the database, which was used for generating the sample frame, it was not necessary to ask for the company profit in the questionnaire.

The researcher identified three different possibilities of measuring customer equity, namely company turnover, company profit and the sum of all customer lifetime values from all customers of a company. As company turnover leaves out the profit side of a customer, company profit and the sum of all customer lifetime values are more suited to measure customer equity. However, for the latter, it is necessary to know the number of customers over the next periods and the amount of money the customers will spend. As these two aspects are very critical in practice, companies find it difficult to determine the lifetime values of their customers. Furthermore, companies use different methods for calculating this figure. Since company profit has not such disadvantages, it was seen as the most appropriate figure for measuring customer equity (see also Ness et al, 2001; Stevens, 2006).

In this thesis, company profit was used to measure customer equity for a number of reasons. First, company profit represents a common basis for measuring customer equity because it is a simple and easy accessible figure. Hence, company profit was suited to generalize customer equity and to make it comparable among organisations.

Second, models presented in the literature review also use company profit for determining customer equity. For example, the customer pyramid, a method that segments all customers according to their profitability in order to identify the most valuable customers, refers to customer profit as a measure for identifying

customer equity. Another example is the inverted Lorentz or Stobachoff curve, a method that illustrates the profitability of all customers in the form of a curve.

Third, company profit is easy to calculate and, in general, always accessible as it is a standard figure in each organisation. The use of simple, easy accessible figures allows organisations to reduce the risk of miscalculation, which is also advantageous for the determination of customer equity.

Fourth, company profit is an objective measure and does not include any subjective evaluations of performance. It is a very accurate measure of performance and makes it possible to determine customer equity on an objective basis.

Fifth, company profit is a figure that is continuously and regularly renewed. This is a good basis for calculating customer equity as the continuous change in customers' purchase behaviour is considered.

9 Chapter 9: Quantitative Data Analysis

A total of 282 questionnaires were distributed to potential respondents. This resulted in a usable sample of 112 surveys. Study participants were marketing and CRM managers of financial services firms in the UK and Germany. The web-based questionnaire was sent to all. Alternatively, it was also possible to fill in a paper-based questionnaire.

Section 9.1 deals with the first part of the quantitative survey where the respondents were asked to evaluate their experience with customer equity with regard to interpretation, importance, benefits, problems, and requirements. The last four items were measured using multi-items scales, which had a five point Likert scale anchored by "very important" and "very unimportant". The complete questionnaire appears in the Appendix. Section 9.3 will show the research findings where the hypotheses are tested for the second and major part of the questionnaire which deals with the dimensions of customer equity.

9.1 Assessing managerial experiences of customer equity

The survey included questions on assessing managerial experiences of customer equity and the analysis is provided in this section.

The interpretation of customer equity is based on two different research streams, namely the value identification stream and the value delivery stream. These streams answer two questions: what is a customer worth and how can value delivery to customers be maximised? The survey showed that most organisations interpret customer equity as means for determining the value of a customer. This is in line with the literature, in which customer equity is interpreted as the total discounted lifetime values from all customers (e.g. Rust et al, 2000; Bayón et al, 2002).

The second interpretation of customer equity emphasizes the value delivery to customers by considering customer needs for adding value to products or delivering customer benefits more effectively. This study showed that only few

financial services organisations interpret customer equity in this way (see Figure 36).
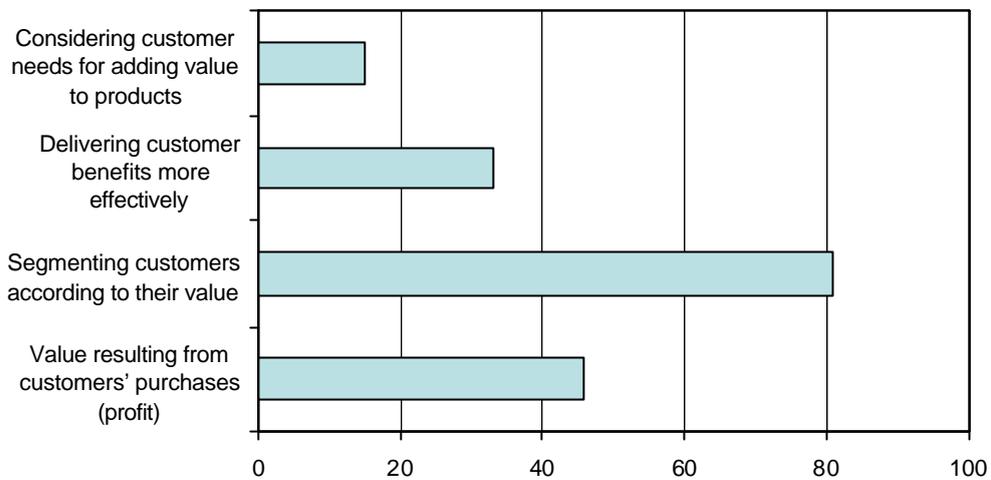
Figure 36: Interpretation of customer equity and customer perception of value in the financial services sector

Source: Survey on customer equity for this thesis

9.1.1 Importance and benefits

The survey conducted for this thesis found that financial services organisations see customer equity as a method that is becoming more and more important to companies. For 50.0 % of the financial service organisations customer equity is very important today (the survey was conducted in 2004/2005). The organisations estimated that the importance is steadily increasing from 57.1% in two years to 81.3% in five years (see Figure 37). One reason for this trend could be the fact that the economy is changing from a product-driven to a customer-driven business, in which strategic decisions focus on customer profitability.
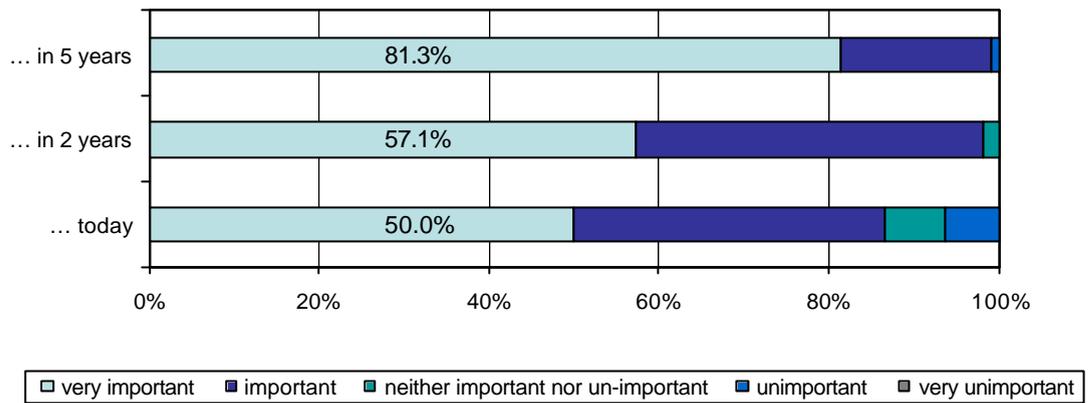
Figure 37: Importance of customer equity today and in the future

Source: Survey on customer equity for this thesis

Customer equity is a means for determining customer profitability and, hence, for identifying unprofitable, profitable, and highly profitable customers. This information is the basis for sales strategies, such as cross-selling or up-selling, marketing strategies, such as image campaigns, or product strategies, such as customisation. All these strategies aim at improving value delivery to customers, which in turn leads to increased customer satisfaction, customer loyalty, and customer profitability (e.g. Hartnett, 1998; Walters and Jones, 2001). The results of the survey show that financial services organisations see an increase in cross-selling (65.2%), customer satisfaction (59.8%), accuracy of targeting customers (57.1%), greater differentiation from competition (55.4%), efficiency (54.5%), and up-selling (49.1%) as very important benefits of an implementation of customer equity (Figure 38).
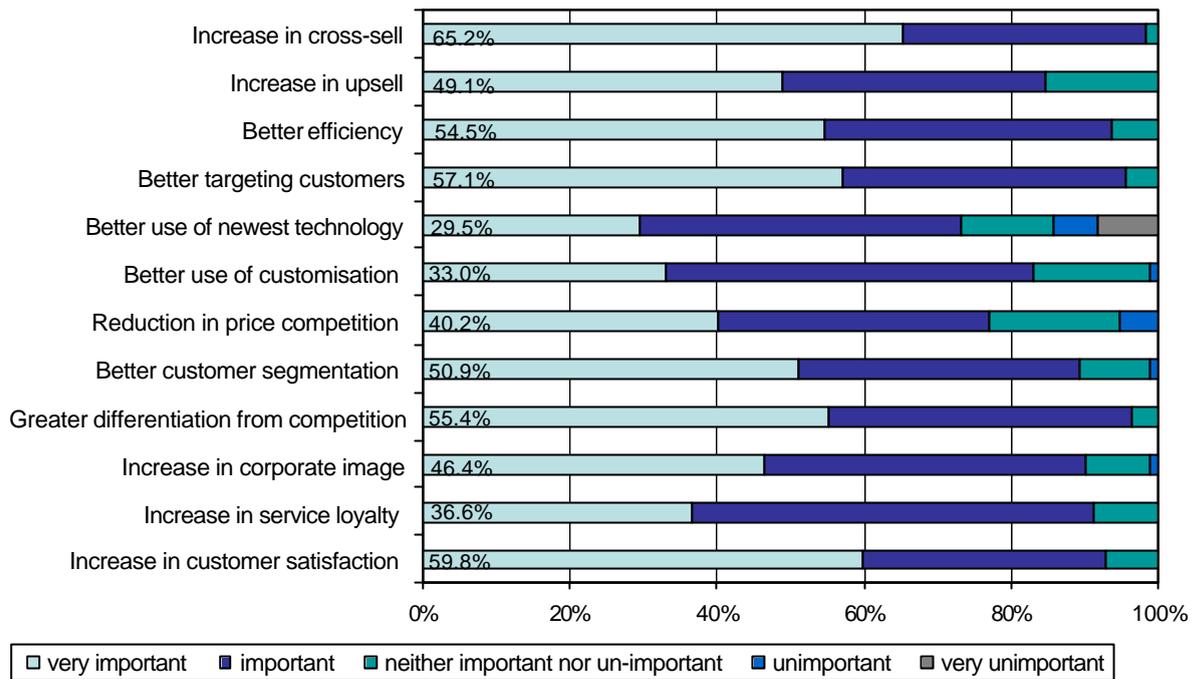
Figure 38: Benefits of an implementation of customer equity
Source: Survey on customer equity for this thesis

9.1.2 Calculation and analysis

Customer equity can be calculated by monetary factors, such as customer lifetime value, customer profit or customer profitability, and / or non-monetary factors, such as frequency (total number of purchases), recency (time elapsed since a customer made his last purchase), duration of customer relationship, or attractiveness of a customer relationship. This part of the survey investigated the application of monetary and non-monetary customer equity in the financial services sector (see Figure 39). The results found that almost half the organisations (40%) use monetary and non-monetary customer equity approaches. Only 21 % of the participants do not apply customer equity approaches.
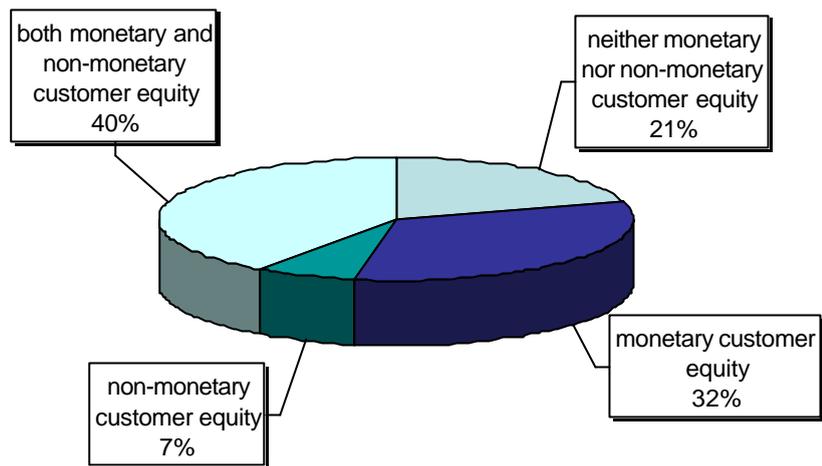
Figure 39: Application of customer equity in the financial services sector
Source: Survey on customer equity for this thesis

The survey also examined how many organisations plan to implement customer equity in the near future. The research result clearly showed that there is a trend towards customer equity with 47 % of the organisations planning to implement both monetary and non-monetary customer equity approaches. Further 23 % want to focus on non-monetary customer equity and 16 % on monetary customer equity (see Figure 40). Finally, only 14 % of these organisations do not intend to introduce customer equity approaches in the future.
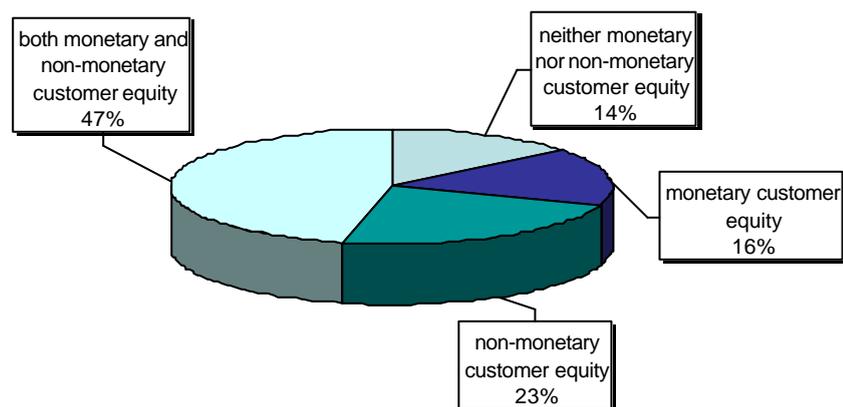
Figure 40: Planned implementation of customer equity
Source: Survey on customer equity for this thesis

The following part of the survey refers to the customer equity approaches discussed in previous sections. The survey investigated which kind(s) of customer equity approach(es) the participants use in their organisation. The survey found that financial services organisations frequently use key account management (84.3%) and customer lifetime value (48.6%) for determining the monetary value of a customer (see Figure 41). Key account management is a method that segments customers according to their turnover. Customer lifetime value is the discounted net profit of a customer. 51.4% of the participants reported that they use methods which allow them to focus on profitable and future, profitable customers. Only 28.4% of the financial services organisations use customer portfolio analysis or consider the cost-revenue ratio of customers in planning activity. Customer portfolio analysis forms a matrix with two dimensions that use factors such as duration of customer relationship or attractiveness of customer relationship for the vertical axis and horizontal axis. 18.9% determine the volume and margin managed by each channel. Decile analysis, another method that segments customers according to their turnover, was presented with 16.2%. Only 9.5% of the participants use acquisition rate, penetration rate, or retention rate for determining the value of a customer. 9.5% are regularly measuring retention rates. Finally, 4.1% of the financial services organisations determine either costs of servicing customers through the various channels or the potential value of a customer. Figure 41 provides an overview of the application of customer equity approaches in the financial services sector.
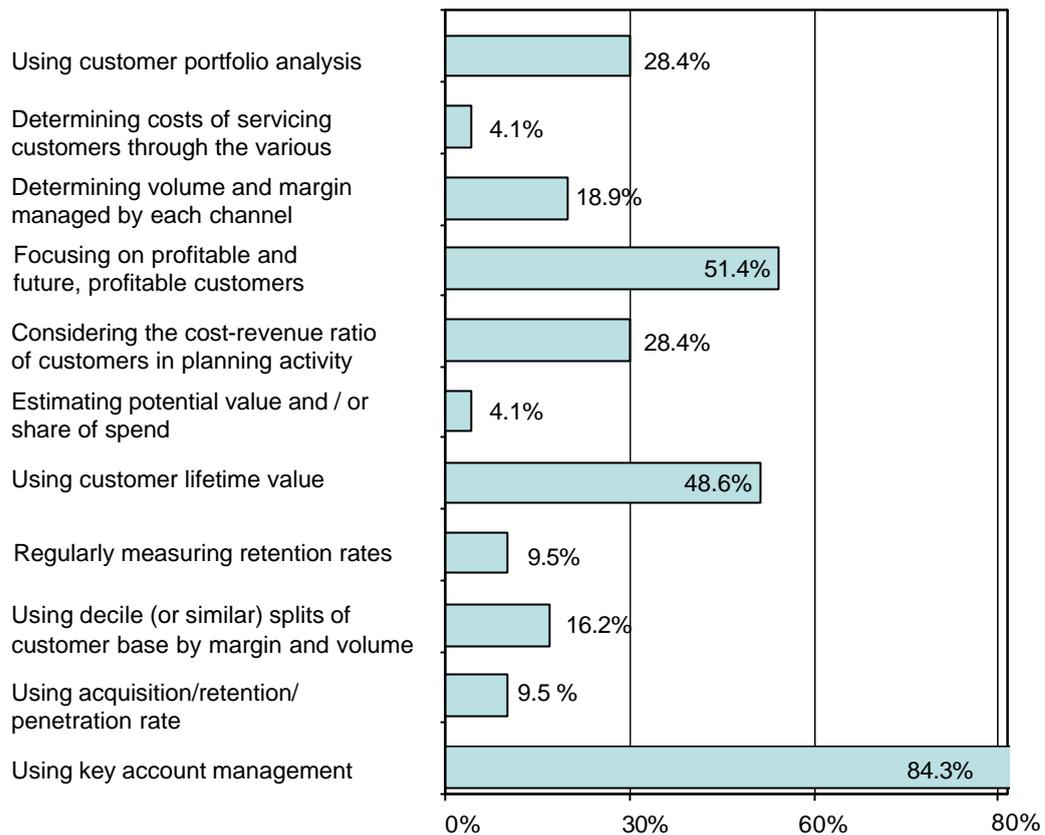
Figure 41: Application of customer equity approaches
Source: Survey on customer equity for this thesis

This study also investigated which department customer equity is assigned to in organisations. In the literature, there is no information about such an assignment. Therefore, it was interesting to throw light on it. The findings of the study showed that 47.2% of the participants assign customer equity to their marketing department, whereas 19.1% assign it to the customer relationship management (CRM) department. This indicates that customer profitability plays a central role in selling products, i.e. customer equity is becoming more important and therefore integrated into marketing strategies. As a result, most organisations assign customer equity to the marketing department. However, a number of financial services organisations assign customer equity to other departments, such as management board (9%), the finance department (6.7%), or the product and service management department (5.6%). All other participants use customer equity approaches within special projects (3.4%),

cross-functional teams (1.1%), or other functions (7.9%) that are not mentioned in this study (see Figure 42).
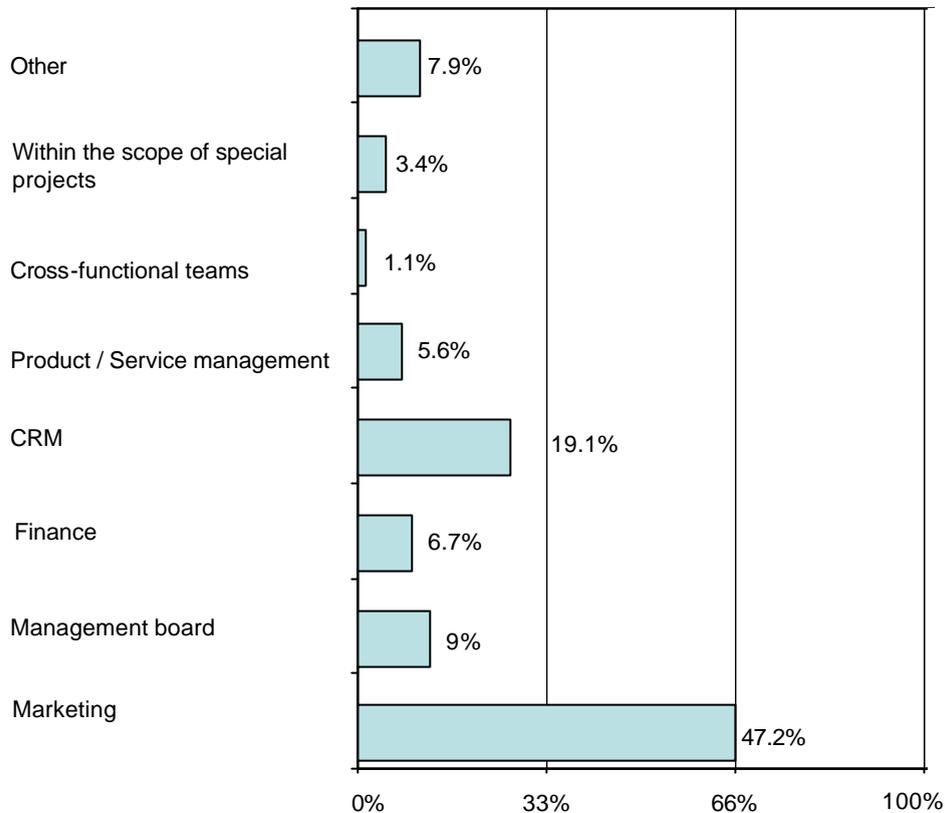
Figure 42: Integration of customer equity into the organisational structure
Source: Survey on customer equity for this thesis

9.1.3 Requirements

When organisations realise and implement a customer equity approach they want to benefit fully from its advantages and, therefore, have a number of requirements of a customer equity approach. For example, a simple implementation and application of the approach is necessary to avoid huge investments in time and money. This study found that 47.3% of the financial services organisations put emphasis on an easy and quick implementation of a customer equity approach, whereas 41.1% see an easy and quick application as very important. Only 37.5% claim that the approach should support the development of a customer-oriented value chain (see Figure 43). The low

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importance of this criterion could be attributed to the complexity of the value chain of a company. The same applies to the support of an effective organisational structure and operations management, which were also of low importance to financial services organisations. This study also illustrated that the availability of customer data (67.9%) and a continuous customer evaluation (66.1%) play the most important role in determining customer equity (see Figure 43). This means that organisations have realized how crucial it is to use updated data for determining customer equity. This is extremely important as customer needs and customer profitability change in the course of time and the determination of customer equity shows only a snapshot of the value of a customer at a certain moment.
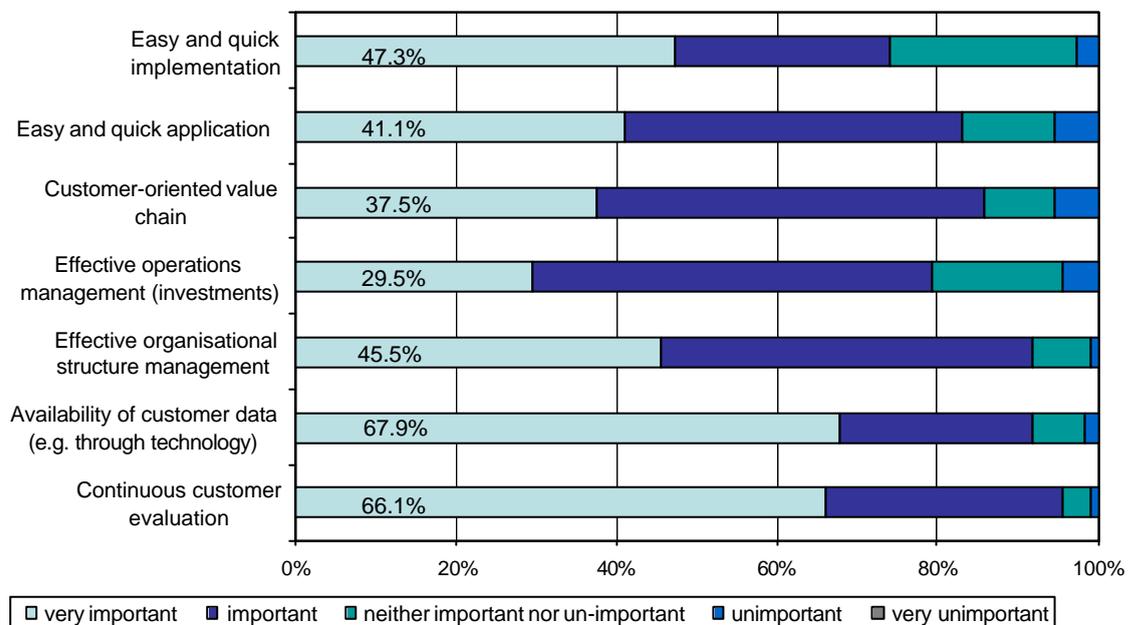
Figure 43: Requirements of customer equity approaches

Source: Survey on customer equity for this thesis

9.1.4 Problems

The implementation of a customer equity approach is often connected with problems, such as getting the necessary financial and human resources, data, training or workshops. Additionally, support on the part of staff and top management is often very limited. More than half the respondents (53.6%) see

cost barriers as the most important reason for the failure of the implementation of customer equity approaches. 56.2% of the participants said that a lack of cross-functional processes is often the case and prevents a successful application of customer equity as the necessary data is not available. Further problems are the lack of resources (47.3%) and people with relevant skills (29.5%). 27.7% of the participants were of the opinion that an insufficient accounting system is a problem, whereas 26.8% said that the lack of training after the implementation causes problems (see Figure 44). As less important problems were mentioned the lack of support from top management (23.2%), customer serving employees (23.2%), and central staff (18.8%). In this section, all percentages were calculated by adding up the first two categories (very important and important).
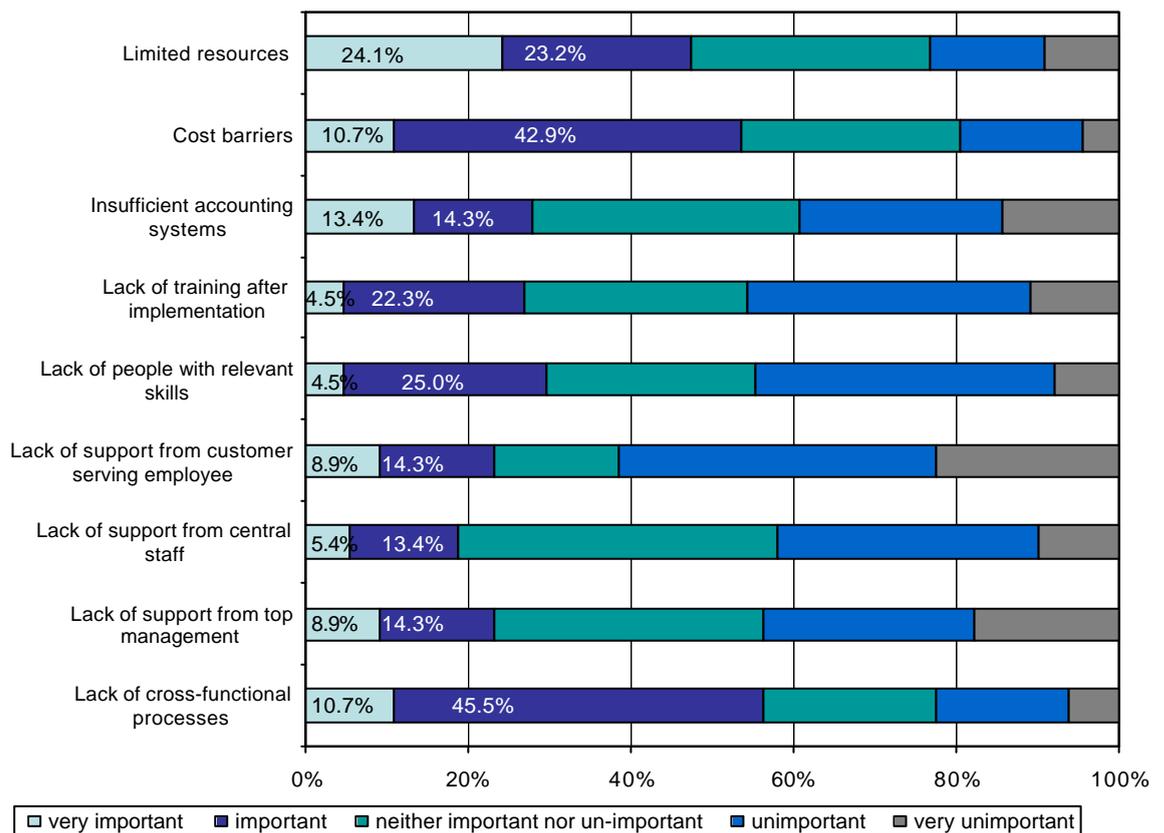
Figure 44: Problems with customer equity approaches
Source: Survey on customer equity for this thesis

9.1.5 Implications

From the research findings discussed above, one can draw four major conclusions concerning customer equity in the financial services sector. The first conclusion refers to the importance of customer equity in the future. The study found that customer equity is becoming more important over the next five years (by 30%) reflecting the increasing interest of practitioners in the benefits resulting from customer equity, such as increased customer satisfaction, cross-selling and up-selling. Second, this investigation demonstrated that almost 75% of the organisations use either both monetary and non-monetary customer equity approaches or only monetary approaches, whereas 21% do not apply customer equity approaches. This highlights the trend towards customer equity management for supporting customer management activities, such as customer development or customer retention. Both research results presented in this section imply that further research is necessary in the area of customer equity to support practitioner's understanding of the organisational forces that determine the degree and shape the direction of customer equity orientation.

Third, most of the financial services organisations use key account management (84.3%) and customer lifetime value (48.6%) for determining customer equity. Both methods are monetary-based and segment customers according to their profitability or revenue. A further research result of the study was the fact that more than half the organisations (56.2%) see the lack of cross-functional processes as major problem during the application of customer equity. Cross-functional processes are based on cross-functional teams consisting of employees from different areas, such as sales, marketing, or production, to ensure a comprehensive basis for decision-making and the formulation of strategies and tactics that satisfy market needs and improve customer equity. This means that further research is needed, which embraces both monetary-based customer equity and the strategic application process of customer equity. Only when the indicator customer equity is used in a strategic context, a systematic decision-making with long range focus on maximising customer equity, is possible.

9.2   Overview of hypotheses

In Chapter 5, the seven hypotheses were developed by deriving them from the literature and carrying out in-depth interviews with experts. These hypotheses are listed in the following:

H1. Distribution channel management is significantly related to customer equity (company profit).

H2. Communication management is significantly related to customer equity (company profit).

H3. Service quality management is significantly related to customer equity (company profit).

H4. Price management is significantly related to customer equity (company profit).

H5. Product and service management is significantly related to customer equity (company profit).

H6. Process management is significantly related to customer equity (company profit).

H7. Human resource management is significantly related to customer equity (company profit).

Figure 45 illustrates graphically the seven hypotheses, i.e. the relationships that are tested in Section 9.3. The statistical procedure applied for testing the hypotheses is as follows:

-    validity assessment (content validity and face validity),

-    exploratory factor analysis,

-    reliability analysis, and

-    multiple regression analysis.
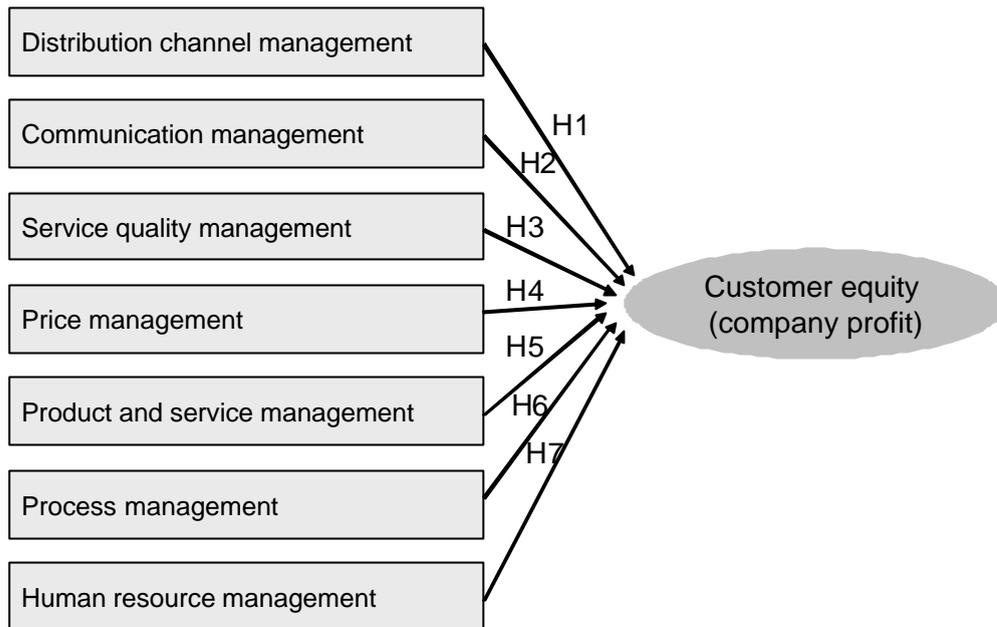
Figure 45: Proposed customer equity dimensions
Source: own

9.3   Research findings

9.3.1   Validity assessment of customer equity dimensions

9.3.1.1   Content validity

In this study, the customer equity dimensions are the result of a comprehensive literature review which states that the items appear to have high content validity, although a subjective judgement. The present dimensions have been developed based on a detailed analysis of the prescriptive, conceptual, practitioner and empirical literature. Moreover, the content validity of the instrument was also ensured through a thorough review by experts (both academia and practitioners) in the field.

9.3.1.2   Face validity

Furthermore, face validity checks were performed on the constructs to ensure that items would be meaningful to the sample and capture issues, which were intended to be measured. These checks were performed with financial services

marketing executives and scholars who had a good knowledge of financial services operations and marketing management.

9.3.2 Exploratory factor analysis of customer equity dimensions

9.3.2.1 Assessment of the suitability of the data for exploratory factor analysis

Before further analysis, the data was checked for its suitability for exploratory factor analysis. For the thirty-five variables the boxplots were performed and checked whether the variables contain outliers or not. The outliers found were replaced by less extreme values. Most researchers suggest a minimum sample size of 100 to 200 cases for factor analysis (see Loo, 1983; Hair et al., 1979). This study had 112 cases. Moreover, the correlation matrix (see Tables 30, 31, 32 and 33) was checked for correlation coefficients of 0.3 or above. As the matrix showed some correlation coefficients above 0.3, the factor analysis was considered to be suitable. The Kaiser-Meyer-Olkin (KMO) value was 0.671 and the Bartlett's test of Sphericity was significant at p=0.000 (see Table 22). Both values indicated that exploratory factor analysis is appropriate.

	Distrib1	Distrib2	Distrib3	Distrib4	Distrib5	Communi 1	Communi 2	Communi 3	Communi 4	Communi 5
Distrib1	1.000									
Distrib2	.283	1.000								
Distrib3	.342	.400	1.000							
Distrib4	.100	.320	.190	1.000						
Distrib5	.195	.147	.321	.323	1.000					
Communi1	.160	.047	.030	.181	.212	1.000				
Communi2	.164	.165	.465	.116	.356	.369	1.000			
Communi3	.086	.246	.140	.002	.131	.374	.434	1.000		
Communi4	.088	.085	.231	.079	.113	.234	.429	.361	1.000	
Communi5	.084	.108	.206	.066	.128	.174	.250	.525	.354	1.000
Service1	.213	.138	.282	.048	.068	.351	.371	.233	.292	.122
Service2	.250	.075	.239	.175	.173	.343	.186	.037	-.005	.072

Service3	.154	.185	.283	.230	.182	.179	.190	.119	.140	.154
Service4	.154	.053	.105	-.075	.076	.272	.173	-.003	.238	-.107
Service5	.233	.072	.214	.137	.198	.266	.313	.148	.075	-.013
Price1	.241	.092	.326	.008	.178	.089	.250	.049	.069	.066
Price2	.110	.203	.211	-.032	-.006	-.088	.024	.103	-.081	.001
Price3	.168	-.010	.115	-.111	.075	.064	-.083	-.060	.102	-.059
Price4	.015	-.061	.051	-.018	.014	-.179	-.127	-.039	.065	.145
Price5	.260	-.050	.161	-.042	.120	.025	-.041	.015	.053	-.003
Product1	.184	.067	.166	.064	.187	.050	.055	.153	-.100	.012
Product2	.221	.033	.139	-.046	.072	.172	.124	.329	.171	.241
Product3	.157	-.060	.144	-.143	.005	-.009	-.068	.016	.069	.105
Product4	.172	-.054	.154	.000	.106	.029	.014	.104	.031	.132
Product5	.084	-.033	.000	.054	.068	.053	.067	.119	-.051	.007
Process1	.163	.018	.103	.090	.189	.204	.186	.217	-.099	.072
Process2	.038	.016	-.012	-.073	.143	-.037	.072	.032	-.050	-.004
Process3	.066	-.028	.198	-.054	.132	.011	.203	.116	.214	.195
Process4	.061	-.237	-.007	-.018	.054	.023	-.033	-.052	.075	.112
Process5	.123	.078	.250	-.007	.089	-.071	.179	.121	.069	.181
Human1	.191	.295	.280	.021	.177	-.010	.286	.350	.028	.111
Human2	.167	.151	.235	-.001	.053	.096	.214	.075	.127	.113
Human3	.117	.009	.278	-.120	.109	-.127	.291	.004	.119	.116
Human4	.149	.109	.283	-.039	.024	.116	.298	.150	.110	.187
Human5	.109	.130	.174	.085	.155	.240	.286	.267	.079	.188

Table 30: Correlation matrix (Part I)

Source: Output from SPSS

	Service1	Service2	Service3	Service4	Service5	Price1	Price2	Price3	Price4	Price5
Service1	1.000									
Service2	.554	1.000								
Service3	.377	.274	1.000							
Service4	.468	.477	.325	1.000						

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Service5	.423	.516	.207	.493	1.000				
Price1	.194	.337	-.027	.216	.146	1.000			
Price2	.144	.152	.118	.074	.008	.379	1.000		
Price3	.133	.171	.148	.231	.139	.480	.379	1.000	
Price4	.034	.098	.182	-.022	-.112	.306	.582	.473	1.000
Price5	.078	.114	-.005	-.009	.011	.402	.323	.464	.404	1.000
Product1	.015	.172	.148	-.032	.055	.184	.211	.197	.273	.323
Product2	.188	.117	.265	.133	.084	.033	.130	.089	.076	.221
Product3	.053	.060	.135	.118	-.024	.131	.190	.325	.348	.171
Product4	.123	.188	.171	.200	.071	.210	.163	.135	.199	.253
Product5	.037	.087	.055	-.043	.153	.068	.031	.140	.051	.080
Process1	.046	.194	.094	.021	.325	.003	.004	.119	-.053	-.079
Process2	-.111	-.136	.032	-.162	-.103	.000	.035	.010	.057	-.046
Process3	-.013	.071	.091	.049	.045	.029	.115	.114	.141	.103
Process4	-.050	.082	.028	-.015	.055	-.101	-.157	.089	.088	.011
Process5	.010	.090	-.033	-.013	.027	.160	.038	.044	.099	.136
Human1	.057	.034	.051	-.009	.122	.183	.238	.086	.052	.304
Human2	.075	.038	.080	.171	.037	.275	.138	.189	.102	.101
Human3	-.040	.013	.003	.188	.060	.358	.147	.172	.157	.099
Human4	.175	.095	.174	.086	-.015	.379	.285	.174	.229	.159
Human5	.157	.151	.142	.146	.171	.228	.155	.100	.066	-.023

Table 31: Correlation matrix (Part II)

Source: Output from SPSS

	Product1	Product2	Product3	Product4	Product5	Process1	Process2	Process3	Process4	Process5
Product1	1.000									
Product2	.512	1.000								
Product3	.450	.520	1.000							
Product4	.325	.660	.544	1.000						
Product5	.409	.315	.526	.348	1.000					
Process1	.309	.307	.253	.245	.368	1.000				
Process2	.307	.192	.148	.080	.199	.252	1.000			

Process3	.045	.182	.174	.225	-.017	.325	.276	1.000		
Process4	.091	.171	.280	.228	.272	.207	.250	.470	1.000	
Process5	.250	.254	.220	.292	.215	.397	.219	.595	.502	1.000
Human1	.294	.261	-.032	.163	.071	.289	.244	.204	-.145	.305
Human2	.197	.032	.062	.005	.001	.102	.224	.279	-.011	.199
Human3	.031	-.084	.066	.006	-.044	.068	.192	.352	.067	.272
Human4	.065	.036	.127	-.038	-.044	.095	.265	.166	-.131	.076
Human5	.139	.075	.018	-.018	.048	.253	.338	.137	-.103	.089

Table 32: Correlation matrix (Part III)

Source: Output from SPSS

	Human1	Human2	Human3	Human4	Human5
Human1	1.000				
Human2	.458	1.000			
Human3	.430	.616	1.000		
Human4	.459	.570	.620	1.000	
Human5	.509	.584	.573	.673	1.000

Table 33: Correlation matrix (Part IV)

Source: Output from SPSS

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		,671
Bartlett-Test of Sphericity	Approx. Chi-Square	1787,719
	df	595
	Sig.	,000

Table 34: KMO and Bartlett's test of Sphericity

Source: Output from SPSS

item	initial	extraction
distrib1	1.000	.438
distrib2	1.000	.650

distrib3	1.000	.685
distrib4	1.000	.653
distrib5	1.000	.602
communi1	1.000	.650
communi2	1.000	.641
communi3	1.000	.816
communi4	1.000	.699
communi5	1.000	.617
service1	1.000	.652
service2	1.000	.698
service3	1.000	.693
service4	1.000	.750
service5	1.000	.669
price1	1.000	.669
price2	1.000	.717
price3	1.000	.627
price4	1.000	.820
price5	1.000	.669
product1	1.000	.644
product2	1.000	.782
product3	1.000	.750
product4	1.000	.633
product5	1.000	.555
process1	1.000	.682
process2	1.000	.530
process3	1.000	.762
process4	1.000	.739
process5	1.000	.769
human1	1.000	.744
human2	1.000	.655
human3	1.000	.799
human4	1.000	.762

human5	1.000	.805

Extraction Method: Principal Component Analysis

Table 35: Communalities

Source: Output from SPSS

9.3.2.2 Factor Extraction

The factor extraction was performed by using the principal components analysis. For identifying the factors, the Kaiser's criterion and the scree test was applied. The Total Variance Explained table showed ten components that had an eigenvalue of 1 or more (see Table 36). These ten components explained a total of 68.64 per cent of the variance. Thus, according to the Kaiser's criterion ten factors should be extracted. The scree plot showed three changes (or elbows) in the shape of the plot: one after the second component, one after the fifth component, and one after the eighth component (see Figure 46). Thus, according to the scree test two, five, or eight factors could be retained. Given that the first five components explain much more of the variance than the remaining components (see Table 36) and that most of the variables in the component matrix load quite strongly on the first five components, the researcher decided to extract five factors. This decision is also supported by the scree test showing a change after five components.
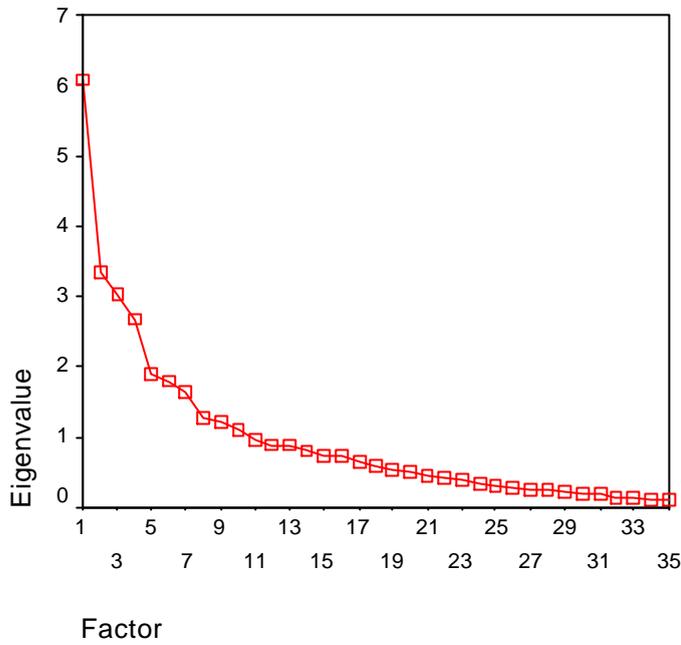
Figure 46: Scree plot

Source: Output from SPSS

Components	Initial Eigenvalues			Rotation Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	6.099	17.427	17.427	6.099	17.427	17.427
2	3.326	9.504	26.930	3.326	9.504	26.930
3	3.028	8.651	35.581	3.028	8.651	35.581
4	2.670	7.627	43.209	2.670	7.627	43.209
5	1.910	5.457	48.665	1.910	5.457	48.665
6	1.798	5.136	53.801	1.798	5.136	53.801
7	1.618	4.622	58.424	1.618	4.622	58.424
8	1.265	3.614	62.038	1.265	3.614	62.038
9	1.222	3.492	65.530	1.222	3.492	65.530
10	1.089	3.111	68.641	1.089	3.111	68.641
11	.951	2.718	71.360			
12	.894	2.555	73.914			
13	.870	2.484	76.399			
14	.801	2.290	78.688			

15	.730	2.086	80.774			
16	.705	2.015	82.789			
17	.628	1.794	84.584			
18	.587	1.677	86.261			
19	.529	1.511	87.772			
20	.495	1.414	89.186			
21	.442	1.264	90.450			
22	.422	1.205	91.655			
23	.375	1.070	92.725			
24	.338	.966	93.691			
25	.291	.833	94.524			
26	.273	.779	95.303			
27	.257	.733	96.036			
28	.253	.724	96.759			
29	.228	.653	97.412			
30	.203	.581	97.993			
31	.182	.520	98.513			
32	.149	.426	98.938			
33	.133	.379	99.317			
34	.123	.351	99.668			
35	.116	.332	100.000			

Extraction method: Principal Component Analysis

Table 36: Total Variance Explained table

Source: Output from SPSS

9.3.2.3 Factor rotation

For rotating the five factors Varimax was applied. Varimax is the most frequently used orthogonal method and easier to interpret than other methods. Factor loadings below 0.4 were surpressed (see Stevens, 1996) and factor loadings above 0.4 were retained (e.g. Stevens, 1986). The Rotated Component Matrix (see Table 37) showed five components / factors representing the original seven dimensions of customer equity. In total, 32 variables had factor loadings

above 0.4. However, four out of these 32 variables were crossloading items that loaded higher than 0.32 on two factors (for more information see Tabachnick and Fidell, 2001). When there are several adequate strong loaders (0.50 or better) on each factor then the crossloading items should be dropped from the analysis (Tabachnick and Fidell, 2001). Since this was the case in this study, the items human1, product3, process3 and product1 were deleted and not considered for further analysis. Furthermore, the item communi1 loaded on factor 3. As the meaning of a factor is determined by the majority of identical items, in this case service 1-5, and the interpretation of a factor is arguable, the item communi1 was omitted from further analysis.

The first factor consisted of the items human 2,3,4,5 and, therefore, was labelled "human resource management". The second factor integrated the product dimension and process dimension into a single factor that was labelled "product and process management". This factor consisted of seven variables: product 2,4,5, and process 1,2,4,5. The third factor comprised all five "service" variables. Therefore, this factor was labelled "service quality management". All "price" variables load highly on factor four that, therefore, was labelled "price management". The last factor contained three variables from the communication dimension (communi 2,3,5) and three variable from the distribution channel dimension (distrib 2,3,4). Therefore, this factor was labelled "communication and distribution channel management" and integrated the communication dimension and distribution channel dimension into a single factor.

variables	components				
	1	2	3	4	5
human3 - degree to which the organisation tailors company information to employees' needs	.858				
human2 - degree to which the organisation informs staff about company planning	.750				
human4 - degree to which the organisation involves employees in decision-making	.747				
human5 - degree to which the organisation ensures high job satisfaction	.718				

human1 - degree to which the organisation creates a customer-oriented mindset	.548				.438
process4 - number of redesigned business processes within a company		.670			
product2 - degree of customization		.646			
product3 - degree of customer involvement in the product development process		.639		.417	
process5 - state of IT		.632			
product4 - variety of products and services (product and service range)		.625			
product5 - degree of added value to products and services		.592			
process1 - degree of process efficiency		.582			
process3 - number of outsourced processes	.473	.521			
product1 - degree of product and service differentiation from competition		.507		.437	
process2 - structure of business roles and business rules		.403			
service4 - degree to which service quality attracts customers			.776		
service2 - degree to which service quality enhances customer loyalty			.740		
service1 - degree of differentiation by means of service quality			.716		
service5 - degree to which the organisation improves service quality			.712		
communi1 - degree to which communication management informs customers			.503		
service3 - degree to which service quality enhances company performance (company profit)			.402		
communi4 - degree to which communication management enhances information gathering about customers					
price2 - degree to which the organisation offers reasonable account fees				.709	
price4 - degree to which price enhances customer loyalty				.706	
price5 - degree to which the organisation offers short-term offers e.g. on savings				.667	
price3 - degree to which the organisation offers competitive prices				.645	
price1 - degree of price differentiation from competition				.579	
communi3 - degree to which communication management enhances customer relationships					.673
distrib2 - degree to which distribution channel management meets more different customer needs					.602
communi2 - degree to which communication management encourages customer trust					.506

| distrib5 - degree to which distribution channel management enhances differentiation from competition | | | | | |
| distrib1 - degree to which distribution channel management optimizes service delivery costs | | | | | |

Extraction method: Principal Component Analysis.

Rotation Method: Varimax with Kaiser-Normalization.

a Rotation converged in 7 iterations.

Table 37: Rotated Component Matrix

Source: Output from SPSS

9.3.3 Reliability analysis of customer equity dimensions

To check the internal consistency of each factor, Cronbach's alpha was used in this study. A Cronbach's alpha value above 0.70 is considered to be the criterion for demonstrating internal consistency of new scales and established scales respectively (e.g. Bagozzi and Yi, 1988; Nunnally, 1988). However, an alpha score of 0.6 is generally also acceptable (see Moss et al, 1998).

Table 38 indicates the Cronbach's alpha for each factor identified in the previous exploratory factor analysis. The results for all factors are greater than the suggested cut-off level of 0.6 and, hence, lend support to reliability of the constructs. Factor 5 originally had a reliability of 0.6639. To improve the alpha value, the item distrib4 was deleted and the reliability augmented to 0.6768. Factor 5, "Communication and distribution channel management", has the lowest reliability with 0.6768, all other factors are greater than 0.7. This reinforces the reliability of the internal consistency of the factors / dimensions of customer equity. Table 39 shows the reliability of the items of the factors.

Factors	Cronbach's alpha
Factor 1: human resource management	0.8591

(contained variables: human 2-5)	
Factor 2: product and process management (contained variables: product 2,4,5, process 1,2,4,5)	0.7212
Factor 3: service quality management (contained variables: service 1-5)	0.7778
Factor 4: price management (contained variables: price 1-5)	0.7828
Factor 5: communication and distribution channel management (contained variables: communi 2,3,5 and distrib 2,3)	0.6768

Table 38: Reliability of facto rs

Source: Output from SPSS

Factor 1: human resource management
(contained variables: human 2-5)

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Alpha if Item Deleted
HUMAN2	11.1339	5.5945	.6813	.8311
HUMAN3	11.2411	5.7882	.7030	.8210
HUMAN4	11.2054	5.5340	.7252	.8116
HUMAN5	10.9911	5.9549	.7125	.8185

Reliability Coefficients

N of Cases = 112.0 N of Items = 4

Alpha = .8591

Factor 2: product and process management
(contained variables: product 2,4,5, process 1,2,4,5)

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Alpha if Item Deleted
PRODUCT2	23.7589	6.3468	.4581	.6877
PRODUCT4	23.9196	7.8944	.5142	.6866
PRODUCT5	23.8929	7.5920	.4411	.6896
PROCESS1	23.5089	7.0269	.4731	.6788
PROCESS2	23.4643	7.6023	.3135	.7171
PROCESS4	23.5357	7.2239	.4284	.6899
PROCESS5	23.9375	6.5816	.4996	.6713

Reliability Coefficients

N of Cases =   112.0   N of Items = 7

Alpha =   .7212

Factor 3: service quality management
(contained variables: service 1-5)

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Alpha if Item Deleted
SERVICE1	16.2500	4.8559	.6201	.7142
SERVICE2	16.2768	4.8506	.6217	.7137
SERVICE3	16.3393	5.5956	.3785	.7893
SERVICE4	16.5714	4.4453	.5981	.7217
SERVICE5	16.3125	5.0096	.5536	.7361

Reliability Coefficients

N of Cases =   112.0   N of Items = 5

Alpha =   .7778

Factor 4: price management
(contained variables: price 1-5)

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Alpha if Item Deleted
PRICE1	15.6607	5.3613	.5097	.7577
PRICE2	15.8839	5.0585	.5609	.7414
PRICE3	15.6429	5.0605	.6037	.7277
PRICE4	15.9554	4.7097	.5969	.7297
PRICE5	15.6786	5.3192	.5235	.7535

Reliability Coefficients

N of Cases =   112.0   N of Items = 5

Alpha =   .7828

Factor 5: communication and distribution channel management
(contained variables: communi 2,3,5 and distrib 2,3,4)

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item-Total Correlation	Alpha if Item Deleted
COMMUNI2	20.8125	4.4060	.4777	.5898
COMMUNI3	20.8839	4.5720	.4465	.6025
COMMUNI5	20.8839	4.7342	.3724	.6294
DISTRIB2	20.7143	4.8005	.3891	.6233
DISTRIB3	20.7768	4.4092	.4569	.5976
DISTRIB4	20.6161	5.4639	.2084	.6768

Reliability Coefficients

N of Cases = 112.0   N of Items = 6

Alpha = .6639
(item DISTRIB4 was deleted: new alpha = 0.6768)

Table 39: Reliability of items

Source: Output from SPSS

9.3.4 Multiple regression analysis of customer equity dimensions

9.3.4.1 Assessment of the suitability of the data for regression analysis

For investigating the relationships between the five identified factors (independent variables) and customer equity (dependent variable), multiple regression analysis was performed. Multiple regression analysis requires about fifteen cases per predictor (independent variable) (see for example Stevens, 1996). This study had five predictors, which means that about seventy-five cases were necessary. In total, this study had 112 cases representing an adequate sample size for performing multiple regression analysis.

First, the five factors were calculated by summing up the variables of each factor and dividing this sum by the number of variables. This means that each factor was the average of all variables belonging to the factor. SPSS provides the opportunity of saving the factor scores for each factor extracted to use them for further analysis. Since these factor scores include the crossloading items, it was not possible to use them and, therefore, the average of each factor was calculated as described above. Then, before the researcher started with

multiple regression analysis, the five factors and customer equity were checked for outliers. In total, nine outliers were found and replaced by less extreme values. Afterwards, normality was assessed for all five factors and for customer equity by using boxplots, histogram, and Normal Q-Q plot. All five factors (independent variables) were positively skewed and violated the normality assumption. The dependent variable, customer equity, was also positively skewed. However, research indicates that a violation of normality does not affect hypothesis tests (see for example Edgell and Noon, 1984) and, therefore, the investigation was carried on.

The Pearson's Correlation Matrix showed no correlation higher than .70 indicating that no multicollinearity was present (see Table 40). When the independent variables are not sufficiently correlated they do not cause significant multicollinearity problems in the regression analysis.

	PRODUCT	SERVICE	HUMAN	PRICE	COMMUNI
PRODUCT	1.000	.126	.150	.142	.206
SERVICE	.126	1.000	.144	.190	.295
HUMAN	.150	.144	1.000	.284	.324
PRICE	.142	.190	.284	1.000	.106
COMMUNI	.206	.295	.324	.106	1.000

Table 40: Pearson's Correlation Matrix of independent variables
Source: Output from SPSS

9.3.4.2 Model Summary table and ANOVA table

The construct has an R^2=0.107 (see Table 41) which is significant at p=0.033 (F) (see Table 42). The significance level associated with the observed value of F is 0.033 indicating that there is a significant linear relationship between the set of independent variables and the dependent variable.

Model	R	R-Square	Adjusted R-Square	Std. Error of the Estimate
1	.326	.107	.064	226.2072

a Predictors: (Constant), COMMUNI, PRICE, SERVICE, PRODUCT, HUMAN

b Dependent Variable: company profit 2004 in Pounds

Table 41: Model summary

Source: Output from SPSS

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	646565.650	5	129313.130	2.527	.033
	Residual	5423986.875	106	51169.687		
	Total	6070552.524	111			

a Predictors: (Constant), COMMUNI, PRICE, SERVICE, PRODUCT, HUMAN

b Dependent Variable: company profit 2004 in Pounds

Table 42: ANOVA

Source: Output from SPSS

9.3.4.3 Coefficients table

(a) *H1 and H2.* The findings indicated a non-significant association between the variable "communication and distribution channel management" (COMMUNI) and customer equity (company profit). This variable had no significant effect on customer equity (company profit) at p=0.288. Thus, H1 and H2 were not established.

(b) *H3.* The service quality variable (SERVICE) also had a significant relationship with customer equity at p=0.025. The positive beta (beta = 0.223) indicates that an improvement in service quality leads to an increase in customer equity. Thus, H3 was established.

(c) *H4.* The results also indicated that the price variable (PRICE) had a non-significant relationship with customer equity at p=0.497. Thus, H4 was not established.

(d) *H5 and H6.* The "product and process" variable (PRODUCT) was not significant at p=0.903. Thus, H5 and H6 were not established.

(e) *H7.* With a p-value of 0.016, the human resource variable (HUAMN) itself was also found to be significant to customer equity. An improvement in *human resource management* (beta=-0.247) contributed to a decrease in customer equity. Thus, H7 was established.

To summarize, communication and distribution channel management, price management, and product and process management had all non-significant relationships with customer equity, i.e. that these variables had no impact on customer equity. Service quality management and human resource management had a significant relationship with customer equity. Table 43 shows the detailed results of the multiple regression analysis indicating partial coefficients (B), standard errors (SE B), standardised regression coefficients (beta) and t-statistics (T and Sig T).

	unstandardized coefficients		standardised coefficients				
	B	Standard errors	Beta	T	Sig T (Significance)	significant	Hypotheses
PRODUCT	6.270	51.562	.012	.122	.903	No	H5 + H6
SERVICE	99.095	43.446	.223	2.281	.025	Yes	H3
HUMAN	-74.237	30.273	-.247	-2.452	.016	Yes	H7
PRICE	28.246	41.440	.066	.682	.497	No	H4
COMMUNI	54.456	50.942	.109	1.069	.288	No	H1 + H2

a Dependent Variable: company profit

Table 43: Coefficients table
Source: Output from SPSS

9.4   Summary

The quantitative analysis of the dimensions of customer equity shown in the previous three chapters addressed marketing executives, sales executives, and customer relationship managers from the German and British financial services industry. This industry was chosen because it is especially interested in building long-term relationships with their customers, implementing customer

relationship management (CRM) systems, calculating customer lifetime value, identifying profitable and unprofitable customers, and, hence, applying customer equity. The questionnaire distributed contained a more general part regarding importance, requirements, benefits, problems in relation to customer equity at the beginning and five questions for each of the seven dimensions of customer equity at the end.

The results of the general part presented in Section 9.1 revealed that only 21% of the financial services companies do not use customer equity approaches, i.e. customer equity is regularly applied in this industry (74%) by means of, for example, key account management (84.3%) and customer lifetime value (48.6%). Besides this main finding, this part also presented interesting results, such as the fact that most firms assigned their customer equity activities to the marketing department or that the main reason for the implementation of customer equity is an increase in cross-selling (65.2%) and customer satisfaction (59.8%).

The second part of the questionnaire was dedicated to the investigation of the seven dimensions of customer equity. The research results were shown in Section 9.3. The three independent-samples t-tests (Section 8.2.6) ensured that there were no differences between German and British companies for company turnover, company size and profit. The statistical procedure used for the quantitative analysis, i.e. for testing the seven hypotheses (each dimension represents one hypothesis), was as follows: validity assessment (content validity and face validity), exploratory factor analysis, reliability analysis, and multiple regression analysis. The results of the validity assessment were presented in Chapter 6 and ensured that the items were meaningful to the sample. In the exploratory factor analysis, the seven dimensions were reduced to five dimensions. The following reliability analysis reinforced the reliability of the internal consistency of all five factors / dimensions of customer equity. Finally, in the multiple regression analysis it turned out that only two factors were significant, namely service quality (H3) and human resource (H7).

With regard to the conclusions, which can be drawn from the research results, one must say that it is not surprising that service quality has a positive

significant relationship with customer equity because in the financial services industry, services are intangible and have no physical presence which increases the importance of the way of how the service is delivered or, in other words, of service quality. Overall, this research provided insights into the drivers of customer equity that can help managers to improve customer profitability and company turnover. It also improved the knowledge of customer management and segmentation, which is useful for managers to better predict customer equity and sales growth. However, more research is necessary in this area not only because this investigation focused on one sector, but also because little research on customer equity exists in the literature. In the following chapter, the conclusions, limitations, managerial implications and future research are presented in more detail.

Part IV.

**CONCLUSIONS, MANAGERIAL IMPLICATIONS, LIMITATIONS
AND FUTURE RESEARCH**

10 Chapter 10: Conclusions, managerial implications and future research

This chapter discusses the research results of this study regarding conclusions, future research, and strategic and managerial implications. This research results refer on the one hand, to the identification and empirical analysis of the underlying factors of customer equity, and on the other hand, to the development of the conceptual process of customer equity. Both results reflect the two main research objectives of this thesis.

Furthermore, in the following, each hypothesis of the customer equity construct is strategically analysed and implications for the management are given. This customer equity construct provides useful guidelines for developing strategies that aim at improving customer equity. In the following sections, the conclusions and practical ways to achieve a maximum of customer equity at the management level, employee level, and customer level were indicated. Insights drawn from this study therefore benefit marketing practitioners and service providers seeking to effectively improve customer equity.

In the main, companies should pay attention to the realisation process of customer equity that:

- determines customer equity from the monetary and non-monetary perspective;

- considers data on markets and competitors for building the right strategies;

- adapts offerings, services, technology, organisational structure, and business processes to customer needs;

- continuously assesses customer and corporate performance for monitoring the effects of value-driven strategies and considering the changing purchase volume of customers.

10.1 Conclusions

This section deals with the research findings of this study, i.e. the conclusions drawn from the main research objectives, which were the development of a conceptual process of customer equity and the identification and empirical analysis of the dimensions of customer equity.

10.1.1 Conclusions - Process of customer equity

The developed process of customer equity enables organisations to differentiate themselves strategically from their competitors by either reducing costs (e.g. optimising business processes) or improving growth (e.g. offering new products or conquering new markets). Furthermore, since the framework makes it possible to segment customers, analyse customer needs and identify profitable customers, it also helps to anticipate problems before they actually occur and ensure that the service and value delivered to the customers is of high quality in the first place. This also makes it possible to avoid hidden costs associated with lost business when customers decide to switch to competitors due to poor value delivery. Overall, the proposed process of customer equity supports the creation of value delivery, which improves the business performance of a company.

The benefit of the proposed process lies in the combination of market orientation, value creation by means of organisational forces and the assessment of company and customer performance. All three aspects have been identified by analysing the existing literature on customer equity and customer management. In this context, it is important to note that none of the five approaches that the researcher found in the literature meets all three requirements mentioned above. Since the developed process in this thesis provides managers with all three aspects, it makes a significant contribution to research. Overall, it allows for a cost-benefit balance, the reactions and performance of competitors, the dynamics of changing customer needs, and the potential for a profitable allocation of marketing resources. The framework provided in this thesis also makes it possible to measure customer and

corporate performance on a regular basis and yield improvements by identifying and eliminating waste in internal operations. Improved insights into the distribution of customer profitability can be combined with value creation and delivery at a strategic level. Organisations can then plan realistically to develop and implement value-driven differentiated customer equity strategies, which is what this thesis has contributed to.

The developed process of customer equity is a strategic framework that allows for the calculation of customer equity in three different ways: the sum of all customer lifetime values, the sum of all customer profits or the sum of all customer profits. Companies can select from these three opportunities and decide on the measure that best corresponds with the accounting system applied in the organisation, i.e. organisations that have an activity-based costing system tend to use customer lifetime value or customer profit rather than customer profits. The implementation of this process can be based on a customer relationship management (CRM) system because such a system supports the calculation of customer equity and the other performance measures necessary for the monitoring of the effect of the value-based strategies on the company and customer performance. CRM further helps to segment customers, develop value propositions and create reports for strategic decisions. Due to the two aspects mentioned before, the proposed process of customer equity is easy to implement, which 47.3% of the financial services organisations mentioned as crucial point for a successful use of customer equity. The study was carried out in the context of the quantitative analysis of the dimensions of customer equity. In this study, 67.9% of the financial services organisations saw the availability of customer data as important and 66.1% of them view a continuous customer evaluation as crucial. The developed process of customer equity meets both aspects.

Finally, the proposed framework can be allocated to the marketing department, which 47.2% of the financial services organisations did with a customer equity approach. This is also in line with the trend in strategic marketing toward a marketing mind-set that integrates activities not only focusing on sales, product development and promotion, but also on exploring, creating, and delivering

customer lifetime value (see, for example, Kotler et al, 2002; Hogan et al, 2002; Hansotia, 2004). The proposed framework also helps managers to treat customers in a different way, i.e. building cost-saving strategies for less profitable customers. Hence, it contributes to the new marketing perspective emphasising customer lifetime value and not the development of one strategy for all customer segments.

10.1.2 Conclusions – Dimensions of customer equity

The literature review shows that definitions of customer equity can, generally, be grouped into three categories, with some variations within each category: customer lifetime value, customer profitability, and customer revenue. Customer equity is then calculated by summing up one category, i.e. the monetary values of a firm's customers. From a management point of view, customer equity, being the management of purchasing, production, sales, marketing, and / or logistics processes (e.g. customer selection, channel management, relationship management, etc.) directed towards financial important customers in business and industrial markets, can be seen as a practical implementation of long-term buyer/seller relationships.

Although the extant literature offers a valid theoretical support, the frameworks presented in this literature review need empirical testing (hence the quantitative and qualitative inputs) before they can be used as guiding rules for action. Towards that purpose, this thesis contributes to research by investigating empirically the underlying factors of customer equity. In the literature, three research streams were identified, namely a market-based stream, a value-chain-based stream, and a stakeholder-based stream, which are based on seven components influencing customer equity. These seven components are similar to the 7 P's marketing mix, which is why the researcher decided to base the empirical investigation on it. All the research streams emphasise the conceptual nature of customer equity dimensions, which requires extending the equity context and using empirical data to measure and model the conceptual relationships depicted in the frameworks. Such conceptual relationships mainly focus on managing business processes throughout the chain to create a

customer-centric organisation and adapting physical surroundings, promotion, point of sales, people, prices, and products to customer needs.

This study contributes to empirical research studies on customer management by examining the relationships between the dimensions of customer equity and customer equity itself in the British and German financial services industry. This customer equity construct was shown to have seven dimensions. These dimensions were price management, distribution channel management, communication management, product and service management, process management, human resource management, and service quality management. As it was mentioned earlier, the instrument, which is used in this study was originally designed by Booms and Bitner (1981) in the form of the 7Ps marketing mix. An adaptation to the financial services sector was not necessary as their instrument already focuses on the service sector. To summarize, the empirical study covers two major research objectives of this thesis: the identification of the critical factors (dimensions) of customer equity from the company perspective and the empirical analysis of the identified factors of customer equity in the British and German financial services sector.

In total, seven hypotheses were set. The researcher hypothesised significant relationships between distribution channel management (H1), communication management (H2), service quality management (H3), price management (H4), product and service management (H5), process management (H6), human resource management (H7) and customer equity (presented in the form of company profit). To statistically analyse these hypothesised seven dimensions of customer equity, a series of statistical procedures were used. **The procedures were (a) content validity and face validity, (b) exploratory factor analysis, (c) reliability analysis, and (d) multiple regression analysis.**

10.1.2.1 *Validity*

A critical aspect in the evolution of a fundamental theory in any management concept is the development of good measures to obtain valid and reliable

estimates of the constructs of interest. Without establishing the reliability and validity, it is difficult to standardize the measurement scales, and hard to know whether they truly measure what they intend to measure. Therefore, both reliability analysis and validity assessment were applied in this study. For the validity assessment, the content validity and the face validity were used. The content validity was ensured through a detailed analysis of the existing literature and a thorough review of this literature by academics and practitioners who are experts in this field. Furthermore, financial services marketing executives and scholars ensured the meaningfulness of the construct through *face validity* (see Chapter 6).

10.1.2.2   Exploratory factor analysis

The exploratory factor analysis was applied with varimax rotation, the most frequently used orthogonal method, and principal component analysis for identifying (extracting) the underlying factors or dimensions. Overall, five of the original seven dimensions were identified and labelled as follows: product and process management, service quality management, human resource management, price management, and communication and distribution channel management. Factor loadings above 0.4 were retained, in total 27 variables, and all other variables were removed. The removed eight variables were human1, product1, product3, process3, communi1, communi4, distrib1, and distrib5.

10.1.2.3   Reliability analysis

The reliability analysis assessed the internal consistency reliability of each dimension of the customer equity construct, which were derived from the literature. For the reliability analysis, Cronbach's alpha was used and items below an alpha value of 0.60 were removed. It turned out that all five factors identified in the previous exploratory factor analysis were reliable because they showed an alpha value greater than 0.7 except for the factor "Communication and distribution channel management", which had the lowest reliability with 0.

6768. For improving the reliability of this factor, the item distrib4 was omitted from the scale.

10.1.2.4 Multiple regression analysis

The Pearson's Correlation Matrix, an output of the multiple regression analysis, showed no correlation higher than 0.70 indicating that the independent variables are not sufficiently correlated to cause significant multicollinearity problems in the regression analysis.

The multiple regression analysis was conducted to verify that the seven dimensions of customer equity are significantly related to customer equity. The several dimensions of customer equity were used as independent variables, whereas company profit representing customer equity was used as dependent variable. Company profit was used for measuring customer equity because this is consistent with existing approaches in the literature, such as the customer pyramid or the Lorenz curve that also apply profit. Furthermore, company profit is an objective measure that is easy accessible for organisations. It makes customer equity comparable among organisations and considers changing customers' purchase behaviour because it is regularly renewed.

Research outcomes indicate that the hypothesized relationship between the factor service quality management (H3) and company profit (customer equity) is supported with statistical significant results (p=0.025; beta=0.223). The relationship between human resource management (H7) and customer equity also turned out to be significant at p=0.016 (beta=-0.247). However, the results do not support the relationships between communication and distribution management (H1+H2: p=0.288, beta=0.109), price management (H4: p=0.497, beta=0.066), and product and process management (H5+H6: p=0.903, beta=0.012) and company profit (customer equity). This customer equity construct accounts for about 11 per cent of the variance of the dependent variable (R-square=0.107) and is significant at p=0.033 (F=2.527) indicating that there is a significant linear relationship between the set of independent variables and the dependent variable. This means that 11 per cent of the

observed variance in customer equity (dependent variable) could be explained by these input factors (predictor variables). In other words, although the construct explains a statistically significant amount of the variance, it still leaves most of it unexplained. Figure 47 shows the results of this study.
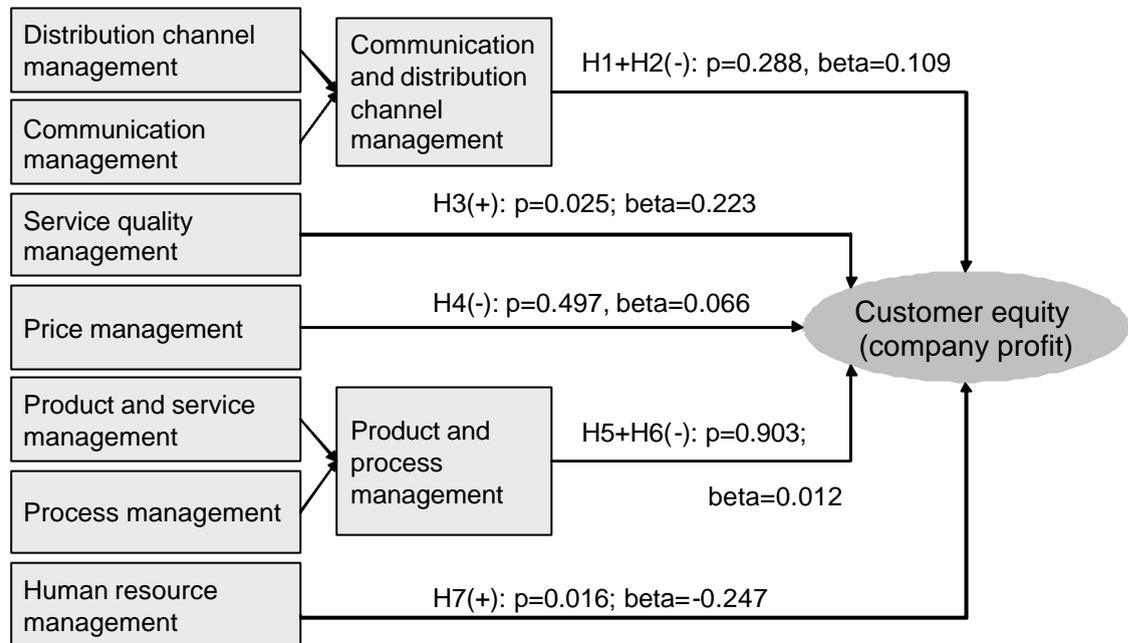
Figure 47: Results of the empirical study
Source: own

The developed construct for the empirical investigation explained only 11 per cent of the variance in customer equity, although all three research streams identified in the literature refer to the factors of this construct for improving customer equity (see, for example, Hogan et al, 2002; Tierney, 2003; Forbes, 2007; Payne and Holt, 1998; Flint et al, 1997). In other words, besides these seven factors, there must be further factors, which have not been identified in the literature yet. Furthermore, this study focused on the financial services sector, i.e. carrying out the same study in other sectors could lead to another result, which could show a higher R-squared and, hence, the 7 P's marketing mix could explain much more of the variance in customer equity.

However, in this context it must be noted that yet no equivalent studies exist in the literature and, hence, no reference value for the R-squared could be found in the customer equity literature. The absence of such equivalent studies also made it difficult to develop a construct that explains much of the variance in customer equity (dependent variable). However, researchers, such as Hair et al (1998) view an R-squared of 11 per cent as very low because 89 per cent of the variance in the dependent variable (customer equity) remains unexplained. Finally, it must be emphasised that the quantitative method, i.e. statistical research, is not able to take full account of the many interaction effects that take place in social settings (see Cronbach, 1975). In contrast, qualitative inquiry accepts the complex and dynamic quality of the social world. In the context of this thesis, one must say that this phenomenon also applied to the results of the quantitative and qualitative methods used in this thesis. Whereas the qualitative results indicate that there are relationships between the seven components of customer equity and customer equity itself, the quantitative analysis found only one significant relationship between service quality and customer equity. Hence, qualitative analysis results in a different type of knowledge than does quantitative inquiry. Where quantitative researchers seek causal determination, prediction, and generalization of findings, qualitative researchers seek instead illumination, understanding, and extrapolation to similar situations.

The qualitative method was applied for ensuring the validity of the construct within the scope of the quantitative analysis. The qualitative analysis of the dimensions of customer equity showed that the respondents saw all seven dimensions as important for increasing customer profits (customer equity). In particular, the degree of service quality during the financial services delivery process was viewed by all nine financial institutions as crucial to financial success because it is an efficient means to differentiate from competition and to satisfy customers better. Furthermore, three respondents mentioned that the monitoring of customers' perceptions of a financial service is important to detect product design faults, waiting times, and other delays that hinder efficient delivery processes. Communication management and distribution channel management was also viewed as one of the most essential factor to improve

value delivery to customers and increase customer profits (customer equity). The respondents reported that their electronic databases make sales-related and profit-related customer information readily available at any time, upon request, which facilitates the development of more adequate communication and distribution strategies. Overall, the main practical implication of the qualitative study is that it is no longer sufficient to only focus on the monetary outcome aspects of customer equity, but to consider the strategic factors, such as service quality or communication, for improving customer equity.

Overall, it must be noted that managers should use the results of the quantitative and qualitative methods only as a yardstick because the value-based strategies resulting from the application of customer equity must be developed individually depending on the individual company and customer structure. Furthermore, the value-based strategies must always be in line with the overall corporate objectives and strategies (see Payne and Frow, 2005). However, the results of both methods help managers to identify the value drivers of customer equity in their organisations.

With regard to the related literature on customer relationship management (CRM), one must say that this study provides more detailed insights into the underlying factors that drive business performance. Most studies of CRM are IT-oriented and analyse the effect of CRM software on business performance such as Sin et al (2005) who found that CRM is a critical success factor for business performance. The study of this thesis was more strategy-oriented and analysed the impact of strategic factors, such as price management or product management, on company profit (customer equity).

However, both the customer equity literature and the CRM literature aim at applying the 80/20 rule, which emphasises that 80 percent of a firm's profit comes from 20 percent of its customers (e.g. Hoffman and Kashmeri, 2000; Ryals and Knox, 2001). Both research streams calculate customer lifetime values (the sum of the customer lifetime values from all customers is customer equity) from each customer to make it possible to identify unprofitable, profitable, and highly profitable customer segments. By focusing on the

individual needs of these segments, organisations can then develop appropriate strategies that enhance customer profits (customer equity).

In the following, the findings of each hypothesis are explained in detail.

10.1.2.5 *Communication and distribution channel management (H1+H2)*

In this study, communication management (H1) and distribution channel management (H2) were reduced to one factor that was not significantly related to customer equity at $p=0.288$ with a positive beta value of $b=0.109$. This means that both communication management and distribution management do not influence customer equity (company profit), i.e. the right way of communication does not enhance customer trust, customer relationships and credibility and has no effect on customer equity. Furthermore, organisations do not benefit from the information gathering about channel use of customers for improving customer's purchase volume.

Interpreting this research result from an organisations' perspective, one can conclude that effective and efficient communication strategies that deliver the right information at the right time to the right customer to satisfy customer needs is not necessary to enhance customer profitability. Overall, communication tools, such as advertising, direct mail, or newsletters, have no effect on customer profits even if they are customised for better targeting customer needs. However, most financial services organisations that have been interviewed reported that they use customised communication for high-value customers and for customers who can identify with such communication. They further mentioned that they regularly use person-specific customer information from customer relationship management (CRM) systems to identify the target group for customised communication.

With regard to distribution channel management, one can conclude that it is not important in the context of customer equity whether financial services organisations follow a multi-channel strategy for meeting customer needs or

not. The findings of the in-depth interviews show a trend towards multi-channel strategies, in particular, cheap sales channels, such as telephone and internet.

10.1.2.6 Service quality management (H3)

The research findings show that service quality management had a significant relationship with customer equity (company profit) at p=0.025. This relationship is of a positive nature as the beta is 0.223 indicating that an improvement in service quality leads to an increase in customer equity. These findings are in line with other studies like that from Duncan and Elliott (2004) who found that there is a positive correlation between service quality and the financial performance of a company. The findings also support the results of the in-depth interviews with marketing experts who reported that service quality is a means of differentiation and, hence, necessary for attracting customers and increasing customer profitability. Hence, the research findings of this study signified that financial services organisations have realized the competitive advantage resulting from service quality and that those financial service organisations see service quality as a means for attracting and retaining customers.

For organisations, this also means that they must deliver higher quality than competition to attract customers and generate customer profits (customer equity). To achieve a high level of service quality, organisations must improve either their equipment, such as technology and servicescape, or their personnel. Hence, this study revealed that organisations aim at improving service quality by mainly investing in IT-based services and the skills of their staff. It can be concluded that the degree to which service quality management enhances customer loyalty, improves service quality, or attracts customers has a significant impact on customer equity.

10.1.2.7 Price management (H4)

This study found that financial services organisations viewed price management as a non-significant predictor of customer equity (p=0.497, beta=0.066). In other words, price differences among competing offerings, short-term offers at special

prices, or offerings with reasonable account fees have no effect on customer equity.

One main reason for this result could be the fact that prices in the financial services sector are very close to those of competition due to regulatory restrictions and a highly competitive environment, i.e. there is a price war in this sector. This means that most financial services firms do not use prices as a means of attracting customers and generating customer equity. Only a minority uses price advantages and provides short-term lower-priced offerings for special target groups. This is consistent with the managers' opinions in the interviews who reported that for pricing strategies competition is decisive and not customer preferences, which is why prices are only sometimes a suited instrument for attracting customers and satisfying customer needs.

10.1.2.8 *Product, service, and process management (H5+H6)*

In this study, product and service management (H5) and process management (H6) were reduced to one factor. The results of the multiple regression analysis showed that this factor had no significant relationship with customer equity (company profit) at $p=0.903$ (beta=0.012). This means that product and service management (H5) and process management (H6) have no influence on customer equity.

With regard to product and service management, the results indicated that customising products, adding value to products, and / or launching new innovative services and products do not lead to an increase in customers' purchase volume and, hence, customer equity. This is partially consistent with the findings of the in-depth interviews, which showed that financial services organisations tend to offer more standard services instead of customised services due to the complexity of the services. Overall, the non-significant relationship of product management with customer equity is not in line with other research results, such as those of Claycomb and Martin (2001).

Regarding process management, the research results indicated that providing efficient and fast service delivery by outsourcing and reengineering business

processes or updating technology had no influence on customer equity (company profit) although quick service processes encourage customers to make repurchases. This is partially consistent with the findings of the in-depth interviews, which revealed that investments in IT and reengineering projects are always checked for their contribution to profit growth. By considering the empirical findings, one can conclude that most IT-based projects are not worthwhile due to their negative financial contribution even from a long-term perspective.

10.1.2.9   Human resource management (H7)

The findings of this study also showed that human resource management was significantly related to company profit (customer equity) at p=0.016. However, this relationship is negative due to a negative beta value of -0.247, i.e. applying human resource management leads to a decrease in customer equity. Most financial organisations are aware of the benefits of teamwork, employee motivation, rewards etc., but have no experience how and why these criteria are influencing customers' buying behaviour and company profit. Therefore, they could have evaluated human resource management as a non-significant factor of company profit. The findings of the interviews with experts revealed that most financial services firms tend to motivate their employees by rewarding them with the objective of creating a customer-oriented mindset. However, the empirical results do not support the effect of a customer-oriented staff on customers' purchase behaviour and, hence, customer equity. According to this study, the degree to which the organisation creates a customer-oriented mindset, informs staff about company planning, tailors company information to employees' needs, involves employees in decision-making, and ensures high job satisfaction to improve customer orientation of staff and to better serve the customer, has no effect on customer equity.

10.2 Managerial implications

Based on the conclusions drawn from this study, managerial implications and recommendations to banking and insurance management are summarised as follows.

10.2.1 Managerial implications - Process of customer equity

As a conclusion, the researcher can suggest that while customer equity has traditionally been considered as a marketing task, managers are realizing that **customer equity needs to be considered from the management perspective** in order to model and develop company activities and resources and achieve a maximum of value creation. This value creation in turn enhances the purchase volume of customers and thus customer equity. The proposed framework contributes to research by considering not only marketing activities for improving value delivery to customers like most other models do, but also improvements in the organisational structure, technology and core competencies.

Moreover, to assess the **impact of the value-building strategies on the financial and non-financial performance** of the company, the proposed customer equity process provides a wide range of customer-focused and company-focused performance indicators explained in Chapter 2 and Chapter 3. In the literature, the researcher found only one model that considers up to ten different customer and company performance indicators. As it is the main aim of customer equity management to deliver value to customers for enhancing customer equity, this work makes a significant contribution to research by making it possible to cover the comprehensive impact of value-building strategies on customer equity itself and other performance indicators, such as change in process efficiency, profit growth, and change in customer retention and market share.

Furthermore, the proposed framework **considers both customer data and information on competitors** to ensure that the value-building market-oriented strategies. As the researcher found only three models in the literature that

consider both the customer and competitor perspective (see, for example, De Bonis et al, 2003), this work makes a significant contribution to research.

10.2.2 Managerial implications – Dimensions of customer equity

A major contribution of this study is in relation to the development of customer equity orientation. Although there is an increasing body of research into strategic customer equity approaches, considerably **less is understood of the underlying variables or dimensions of customer equity development**. The identification of strategic customer equity frameworks in the literature emphasizes the importance of customer equity but does not consider that such knowledge is pointless without an empirical investigation of the underlying variables or dimensions through which customer equity can be developed and managed. The finding of relationships between human resource management, service quality management and customer equity provides a first indication of how customer equity can be developed. It is clear that further research is necessary for investigating the effect of these dimensions on customer equity in other industries and countries. In this sense, an understanding of the underlying factors or dimensions that drive customer equity development is crucial.

A valid customer equity construct was presented in this study. The construct provides a valuable insight into the effect of staff, businesses processes, sales channels, products, price, promotion, and service quality on financial services firms' profit (customer equity). In particular, an emphasis placed on customer equity differentiated this study from previous ones as these mostly focus on the effect of customer relationship management software on a firm's business performance. The most important reason for this is that many organisations use customer relationship management (CRM) software for improving their customer management strategies, particularly customer development and customer retention. By providing empirical evidence of the underlying factors of customer equity covering a more comprehensive perspective than previous studies of CRM software, this study contributes significantly to the research domain of customer management.

In addition, by using both non-financial (e.g. human resource) and financial (e.g. price) factors of customer equity to examine their relationship with customer equity, this study provided a different view on the effect of these factors on customer equity. In this way, **the comprehensive nature of customer equity could be better captured** and, for example, the contribution of the workforce to an organisation's business performance (customer equity), such as service employees' efforts to satisfy and retain customers, could then be measured. An organisation's customer equity could thus better be predicted.

In summary, this research makes a positive contribution in the direction of customer equity management in the financial services industry. It provides clear implications and recommendations for both practitioners and researchers as well. Researcher and financial services organisations are encouraged to see and investigate the relationship between both financial and non-financial factors of customer equity. Usually, they put more emphasis on end results, such as profit, revenues, or customer satisfaction, **ignoring the importance of the source of these outcomes**. However, to be able to improve such end results it is necessary to know the underlying factors influencing them. This study contributes to research by providing information on if, how and why these factors improve the level of customer equity.

10.3 Limitations and future research

This research has uncovered a number of areas that require further research before customer equity driven integration could become a reality. In the following, future research and limitations of the two main research objectives, namely the development of the process of customer equity and the identification and empirical investigation of the dimensions of customer equity, are discussed in detail.

10.3.1 Limitations and future research – Process of customer equity

As the developed process of customer equity is a theoretical framework, which is based on the literature review in Chapters 2 and 3, it may need further

validation quantitatively based on real world customer equity implementation data. The proposed framework for managing market-oriented customer equity provides a solid foundation for developing testable hypotheses for the primary research in this thesis. These hypotheses could be tested by using data from financial services industries and between companies from Germany and the UK.

Companies could learn from each other and it would be interesting to know whether the proposed steps (Sections 4.2 - 4.6) could be applied despite differences existing between applications of customer equity management in various countries. A generalizable process to include these steps would benefit both academics and practitioners. This is because the investigation of how managers apply customer equity and how they derive appropriate strategies for enhancing customer equity have a direct impact on enhancing the competitiveness of market-oriented companies.

Future research should be directed towards fine-tuning the development of value propositions by using qualitative data from different industries. This additional research could review and test the context in which value related structures, for example value-chains, deliver value in order to better understand the propositional aspects. New topics of research would include the development of value propositions from a customer perspective, i.e. how the value of an integration is perceived from the point of view of the primary consumer or benefactor.

10.3.2 Limitations and future research – Dimensions of customer equity

From an academic perspective, this study has its limitations. Since the sample of this study was drawn from British and German financial services companies, the applicability of these findings to other countries should be considered with caution. As the developed approach is very comprehensive and covers a wide range of corporate issues, which depend on the corporate culture, differences between the financial services sectors of each country could appear. Therefore, further research is necessary to investigate the strength of the underlying

cultural effect and to make comparisons between different markets. Replication of this work could be conducted in Europe or North America to determine the degree to which these findings could be generalised. In particular, a comparative study in Europe would be of great interest for getting insights into the importance of customer equity and its dimensions.

This study focused on the financial services sector and managers in other industries should employ the reported content with caution. This study should be replicated in other industries to find out more about the extent to which customer equity is applied in different industries. It would be interesting to investigate differences and similarities between industries in order to draw generalisation from the analyses as in this area little research has been done so far.

Moreover, further in-depth qualitative and / or quantitative research needs to be conducted not only for further investigating the dimensions of customer equity, but also for empirically analysing these effects with larger sample sizes and drawing conclusions from the research.

Considerable future research on the dimensions of customer equity, however, is needed and possible. The approach could be improved to include further dimensions of customer equity, and this could help managers in assessing what specific steps to take to influence customer equity. Researcher could also develop a more detailed framework and splitting the existing dimensions of customer equity into further sub dimensions. The approach developed in this study already covers a wide range of dimensions of customer equity, seven in total, and, therefore provides a good starting point for further research.

Future research can be conducted by measuring the effect of the dimensions of customer equity on different measures of customer equity. For example, researchers may find it interesting to use the seven dimensions of customer equity identified in this study as predictors of customer retention or customer lifetime value (CLTV). Both customer retention and CLTV are frequently used methods in practice for measuring customer equity. This would further contribute to establishing the importance of customer equity and its dimensions.

This study focused on identifying and analysing the dimensions of customer equity from the point of view of a company. However, in the literature, there is a second perspective, the customer perspective which sees customer perceived value as a trade-off between benefits (e.g. quality of the product) and sacrifices (e.g. price paid for product, psychological investment and time needed for searching for and buying the product) perceived by customers in a supplier's offering (Ulaga and Chacour, 2001). This calls for in-depth consumer research to gain further insight and analysis on the nature, meaning and importance of the value that customers perceive when they buy a product (customer perceived value). In particular, the attributes of benefits and sacrifices should be investigated in more detail. This research opportunity could give more insights into the reasons for customer's purchase behaviour and be a better basis for developing customer value strategies that exactly target customer needs.

10.4 General conclusions

The results of the quantitative study showed that around eighty per cent of the respondents apply customer equity in their organisations indicating the important role that customer equity plays in strategic marketing. In particular, the calculation of the monetary value of a customer, which is customer equity, enables these organisations to enhance cross-selling and up-selling, which leads to increased customer profits and, hence, customer equity. In the study, cross-selling was mentioned as driver of business performance by 65.2% of the respondents and up-selling by 49.1%. Hence, one can conclude that organisations applying customer equity perceive an increase in customer profits and, thus, an improved business performance.

This main aspect is also reflected by the increasing importance of customer equity in the near future. The study found that today 50% of the respondents see customer equity as very important, whereas in five years around 80% of the respondents view it as very important. Finally, the most popular methods for calculating customer equity in the financial services sector was key account management, which was applied by 84.3% of the respondents, and customer lifetime value, which preferred 48.6% of the respondents.

One main research objective of this thesis was the development of the conceptual process of customer equity, which helps managers to realise, implement and improve customer equity in their organisations. An extensive review in this thesis of both academic and managerial customer management literature leads to three distinct requirements, namely a high degree of market orientation, the creation of value by means of organisational forces and a regular monitoring and assessment of corporate and customer performance. Existing frameworks for realising and applying customer equity do not meet all these requirements necessary for achieving an optimal monetary output in the form of increasing customer profits. However, the thesis provides an integration of the three aspects e.g. a customer equity map and a strategic application process into one framework with the objective of meeting the major requirements of organisations. Overall, the developed conceptual framework assists managers in building profitable long-term relationships with customers by building value-based strategies that make the product-dependent customers into life-time customers with the objective of maximising customer equity. The practice-oriented process of customer equity can be quickly and easily implemented and integrated into existing customer relationship management (CRM) platforms for the purpose of strategic implications. To conclude, the process in this thesis allows for the calculation of customer equity and its strategic use, which is essential to management for improving value delivery to customers and enhancing business performance.

Both conceptual and empirical research concerning the customer equity dimensions is still scarce justifying the second main research objective of this thesis, which is the empirical investigation of the factors of customer equity in the financial services sector. In this thesis, three different research streams analysing the underlying factors of customer equity were identified: a market-based stream, a value-chain-based stream, and a stakeholder-based stream. By analysing the basic components of all three streams, the researcher could identify and empirically investigate the 7 P's marketing mix as dimensions of customer equity (see Boom and Bitner, 1981; Kotler and Armstrong, 2005; Kotler et al, 2008). This investigation assists managers and practitioners in

creating value for customers, designing more effective value-focused strategies (Hogan et al, 2002) and, hence, developing expertise in value delivery, which enhances customer equity. Since the identified dimensions have been studied in the customer equity context, they cover a comprehensive perspective regarding value creation, i.e. managers can profit from the identification of the dimensions by creating value for customers through not only improvements in products, price, promotion, or place, but also improvements in processes, people, and physical facilities.

Appendix

Appendix 1: Company information from which the respondent sample was drawn

British financial services organisations:

Company name	Sector	Number of employees	Profit 2004 in Mio £	Company turnover 2004 in Mio £
Abbey National plc	Banking	24,361	79.9	6313.0
Alliance & Leicester plc	Banking	8,692	437.6	3002.5
Allianz Cornhill Insurance plc	Insurance	4,407	173.2	2367.4
AXA UK plc	Insurance	10,500	216.0	7632.3
Barclays PLC	Banking	77,000	3248.4	10774.7
Benfield Group Limited	Banking	1,700	54.5	304.6
Berkeley Berry Birch plc	Banking	492	-7.8	63
Bradford & Bingley plc	Insurance	6,450	32.1	2085.5
Brit Insurance Holdings PLC	Insurance	500	71.9	988.4
Britannia Building Society	Building Society	3,762	71.3	1147.7
Cattles plc	Banking	4,977	95.4	734.8
Chelsea Building Society	Building Society	943	31.1	3405.0
Cheshire Building Society	Building Society	899	7.6	219.3
Churchill Insurance Company Ltd	Insurance	2,000	-123.8	1202.4
Clerical Medical Investment Group Ltd	Banking	3,500	302.2	3070.4
Close Brothers Group plc	Banking	2,400	63.6	379.1
Clydesdale Bank PLC	Banking	6,176	178.6	857.2
Cox Insurance Holdings Plc	Insurance	1,684	22.2	406.5
Devitt Insurance Services Limited	Insurance	528	3.0	22.1
Egg plc	Banking	2,702	-91.3	1184.6
Endsleigh Insurance Services Ltd.	Insurance	1,110	6.7	57.3
Freedom Finance plc	Banking	324	6.5	30
Friends Provident plc	Insurance	4,532	178.8	6402.0
Groupama Insurance Company Limited	Insurance	897	21.1	439.9
HBOS plc	Banking	69,243	3053.1	26901.2

Henderson Group plc	Banking	3,100	38.0	3321.0
Highway Insurance Holdings Plc	Insurance	597	14.6	281.9
HSBC Holdings plc	Banking	253,000	6139.0	12787.7
Jardine Lloyd Thompson Group plc	Insurance	5,003	50.3	468.1
Lloyds TSB Group plc	Banking	71,609	2406.9	15712.4
Nationwide Building Society	Building Society	15,759	300.9	5405.8
Northern Rock plc	Banking	4,980	305.8	2741.5
Norwich and Peterborough Building Society	Building Society	960	8.3	179.6
Old Mutual plc	Banking	41,336	483.4	10922.1
Pinnacle Insurance plc	Insurance	554	9.0	742.0
Portman Building Society	Building Society	2,133	54.9	766.6
Principality Building Society	Building Society	791	12.8	218.3
Provident Financial plc	Banking	8,140	151.2	1166.7
Royal & Sun Alliance Insurance Group plc	Insurance	32,000	-148.3	9598.2
Royal Liver Assurance Limited	Insurance	2,181	-59.4	334.7
Sainsbury's Bank plc	Banking	1,025	17.1	220.1
Schroders plc	Banking	2,307	134.0	394.7
Scottish Equitable plc	Insurance	3,135	41.1	6360.3
Scottish Widows plc	Insurance	4,000	396.7	6645.1
St. James's Place Capital plc	Insurance	505	36.8	1940.8
Standard Chartered PLC	Banking	33,000	766.9	4004.8
Tesco Personal Finance Limited	Banking	162	141.6	578.6
THB Group plc	Banking	409	2.1	29,0
The 4Less Group plc	Banking	40	0.2	302.5
The Co-operative Bank p.l.c.	Banking	4,356	83.7	703.0
The Royal London Mutual Insurance Society Limited	Insurance	3,500	121.8	2853.0
The Standard Life Assurance Company	Banking	14,586	2796.0	15425.9
Westbury plc	Banking	1,516	69.9	852.5
Willis Group Holdings Limited	Insurance	15,800	221.4	1144.7
Woolwich Limited	Insurance	4,333	117.5	1039.9
Yorkshire Bank PLC	Banking	3,640	122.5	494.7

Yorkshire Building Society	Building Society	2,265	53.1	744.3
Zurich Global Corporate UK Limited	Insurance	441	0.2	74.9

German financial services organisations:

Company name	Sector	Number of employees	Profit 2004 in Mio £	Company turnover 2004 in Mio £
Allianz AG	Insurance	77,000	1558.6	15,188.0
Allianz Lebensversicherungs-AG	Insurance	5,043	198.4	7,214.0
ALTE LEIPZIGER Lebensversicherung auf Gegenseitigkeit	Insurance	2,358	26.1	1190.3
AXA Konzern Aktiengesellschaft	Insurance	7,937	165.4	4,516.0
Bausparkasse Mainz AG	Building Society	300	2.6	1.723
Bausparkasse Schwäbisch Hall AG	Building Society	662	231.7	25,785.8
Bayerische Hypo- und Vereinsbank AG	Banking	20,134	-1799.5	349,625
Berliner Volksbank eG	Banking	2,850	8.4	7,842.7
Berlinische Lebensversicherung AG	Insurance	677	3.5	437.4
BHF-Bank Aktiengesellschaft	Banking	1,451	7.4	14,383.9
BMW Bank GmbH	Banking	703	315.3	10,626.9
Citibank Privatkunden AG & Co. KGaA	Banking	3,792	493.8	8,509.3
Continentale Krankenversicherung a. G.	Insurance	1,500	9.2	850.1
DBV-Winterthur Krankenversicherung AG	Insurance	1,947	16.7	685.0
Debeka Lebensversicherungsverein	Insurance	12,012	21.0	2,881.0
Debeka-Hauptverwaltung	Insurance	13,799	364.7	4,444.0
Deutsche Bank AG	Banking	26,732	1751.3	15,528
DKV Deutsche Krankenversicherung AG	Insurance	6,312	33.0	2,356.0
Dresdner Bank Aktiengesellschaft	Banking	36,636	18.4	371,226
Ecclesia Versicherungsdienst GmbH	Insurance	950	0.4	46.6
Frankfurter Sparkasse AG	Banking	1,879	0.4	9,752.0
Gothaer Allgemeine Versicherung AG	Insurance	6,610	39.9	2,881.0
HALLESCHE Krankenversicherung auf Gegenseitigkeit	Insurance	1,026	9.1	554

Hamburg Münchener Krankenkasse	Insurance	698	9.1	520.7
Hamburg-Mannheimer Versicherungs-AG	Insurance	6,065	9.9	2,269.0
Hannover Rückversicherung AG	Insurance	ca. 800	219.0	6,778.0
HDI Versicherungen AG	Insurance	9,257	93.5	3,901.0
HUK-Coburg Haftpflicht-Unterstützungs-Kasse kraftfahrender Beamter Deutschlands a.G. in Coburg	Insurance	7,412	89.9	3,063.0
KarstadtQuelle Krankenversicherung AG	Insurance	989	1.1	11,335.3
Kreissparkasse Esslingen-Nürtingen	Banking	1,704	7.2	5,681.1
Kreissparkasse Heilbronn	Banking	1,484	10.4	4,962.8
Kreissparkasse Ludwigsburg	Banking	1,782	11.4	5,603.2
Kreissparkasse München Starnberg	Banking	1,615	10.6	4,109.8
Landessparkasse zu Oldenburg	Banking	1,788	9.8	4,967.0
Münchener Rückversicherungs-Gesellschaft AG	Insurance	40,962	1298.6	15,840.0
Nassauische Sparkasse	Banking	2,253	7.7	12,279.0
NRW.BANK	Banking	948	-181.2	249
Öffentliche Lebensversicherung Braunschweig	Insurance	ca. 500	0.5	74.0
Ostsächsische Sparkasse Dresden	Banking	2,200	13.4	7,252.5
R + V Lebensversicherung AG	Insurance	1,140	559.7	2,190.0
R+V Versicherung AG	Insurance	10,928	67.3	5,343.0
SIGNAL IDUNA Gruppe	Insurance	11,382	503.4	3,230.0
Sparda-Bank Baden-Württemberg eG	Banking	742	11.8	5,431.8
Sparda-Bank West eG	Banking	877	9.0	4,316.6
Sparkasse Hannover	Banking	3,089	1.1	9,822.1
Sparkasse KölnBonn	Banking	3,692	16.2	15,766.8
Stadt- und Kreissparkasse Leipzig	Banking	1,904	-5.7	5,803.7
Stadtsparkasse München	Banking	2,845	30.5	9,234.8
Stuttgarter Lebensversicherung a.G.	Insurance	491	1.4	434.6
Techniker Krankenkasse	Insurance	9,667	127.5	9465
UniVersa Krankenversicherung a.G.	Insurance	606	4.3	260.9
VICTORIA Versicherung AG	Insurance	5,766	106.3	3146.3
VOLKSWOHL-BUND LEBENSVERSICHERUNG a.G.	Insurance	605	3.5	485.3

Westfälische Provinzial Lebensversicherung AG	Insurance	1,967	64.0	687.1

Interviewees (validity analysis within the scope of the quantitative method):

Position	Sector
Marketing director	Banking sector
Customer relationship manager	Banking sector
Marketing assistant	Banking sector
Marketing director	Insurance sector
Customer relationship manager	Insurance Sector
Professor of marketing	University
Professor of marketing	University
Professor of business management	University
Marketing director	Insurance sector
Marketing manager	Insurance sector
Marketing director	Banking sector
Marketing director	Building society

Appendix 2: Questionnaire used in the thesis

For company information please refer to Appendix 1

General data

Company turnover

	< 250 000 £
	250 000 £ - 500 000 £
	500 000 £ - 1 000 000 £
	1 000 000 £ - 2 500 000 £
	2 500 000 £ - 5 000 000 £
	> 5 000 000 £

Company profit (e.g. profit before tax)

	< 250 000 £
	250 000 £ - 500 000 £
	500 000 £ - 1 000 000 £
	1 000 000 £ - 2 500 000 £
	2 500 000 £ - 5 000 000 £
	> 5 000 000 £

Number of employees

	< 250
	250 - 500
	500 - 1 000
	1 000 - 2 500
	2 500 - 5 000
	5 000 - 10 000
	> 10 000

Industry

	Retail banking
	Corporate banking
	Commercial insurance
	Automotive insurance
	Health insurance
	Life insurance
	Homeowners insurance
	Travel insurance
	Other

Major players in the UK and German insurance and banking sector participated in this survey. Besides Abbey National plc, HSBC Holdings plc, Barclays PLC, HBOS plc, Lloyds TSB Group plc, and Standard Chartered PLC, which are the largest banks in the UK, AXA UK plc, Royal & Sun Alliance Insurance Group plc, and Willis Group Holdings Limited from the UK insurance sector took part. From the German banking sector three large banks were presented, namely Deutsche Bank AG, Dresdner Bank AG, and Bayerische Hypo- und Vereinsbank AG, and from the German insurance sector seven global players were presented, namely Münchener Rückversicherungs-Gesellschaft AG, Allianz AG, Hannover Rückversicherung AG, HDI Versicherungen AG, Debeka, SIGNAL IDUNA Gruppe, and VICTORIA Versicherung AG. Besides respondents from these large firms, also respondents from well-known smaller organisations, such as Egg plc, Cattles plc, Provident Financial plc, Sainsbury's Bank plc, Gothaer Allgemeine Versicherung AG, or R+V Versicherung AG, answered the questionnaire.

II. State of customer equity management in practice

The value of a customer can be determined in various ways. The most common method is the segmentation of customers according to their monetary value like customer profitability or customer turnover (like key account management). Sometimes the excess of a customer's revenues over time over the company costs of attracting, selling, and servicing that customer is calculated. However, non-monetary factors, such as the lengths of the relationship with the customer or cross-selling potential, are not considered in customer equity measures. This investigation project attempts to find out how customer equity is used in practice and which determinants are important.

- Customers can be intermediaries, commercial customers, or private customers. -

1. Is customer equity management <u>used </u>in your company? (only one answer possible)
No, neither monetary nor non-monetary customer equity.
Yes, monetary customer equity.
Yes, non-monetary customer equity.
Yes, both monetary and non-monetary customer equity.

2. Is customer equity <u>planned</u> in your company? (only one answer possible)
No, neither monetary nor non-monetary customer equity.
Yes, monetary customer equity.
Yes, non-monetary customer equity.
Yes, both monetary and non-monetary customer equity.

If customer equity management is not applied in your company, please continue with question 6 and leave out question 3,4 and 5.

3. How is customer equity interpreted in your company?
Value resulting from customers' purchases (profit)
Segmenting customers according to their value
Delivering customer benefits more effectively
Considering customer needs for adding value to products

4. Which area is customer equity management assigned to in your company?	
Marketing	Within the scope of special projects
Management board	Cross-functional teams

	Finance		Product or service management
	Customer relationship management		Other

5. Which method is used to determining customer equity in your company?
	Using key account management (segmentation according to customer turnover)
	Using acquisition/retention/penetration rate
	Using decile (or similar) splits of customer base by margin and volume
	Regularly measuring retention rates
	Using customer lifetime value (total discounted profit of a customer relationship)
	Estimating potential value and / or share of spend where data are unavailable
	Considering the cost-revenue ratio of customers in planning activity
	Focusing on profitable and future, profitable customers
	Determining volume and margin managed by each channel
	Determining costs of servicing customers through the various channels
	Using customer portfolio analysis (monetary and non-monetary segmentation)

6. How important is customer equity management …					
	very important	important	neither important nor un-important	un-important	very un-important
… today					
… in 2 years					
… in 5 years					

7. Which requirements on customer equity management are important or unimportant respectively in your opinion?					
	very important	important	neither important nor un-important	un-important	very un-important
Continuous customer evaluation					
Availability of customer data (e.g. through technology)					
Effective organisational structure management					
Effective operations management					
Customer-oriented value chain					
Easy and quick application					
Easy and quick implementation					

8. Why is customer equity management important in your opinion?					
	very important	important	neither important nor un-important	un-important	very un-important
Increase in customer satisfaction					
Increase in service loyalty					
Increase in corporate image					
Greater differentiation from competition					
Better customer segmentation (e.g. according to customer behaviour)					
Reduction in price competition					
Better use of customisation (= products tailored to customer needs)					
Better use of newest technology					
Better targeting customers					
Better efficiency					
Increase in upsell					
Increase in cross-sell					

9. Which problems occur or would occur in connection with the application of customer equity systems and strategies?					
	big problem	often a problem	more or less a problem	some-times a problem	no problem
Lack of cross-functional processes (team structure instead of departments)					
Lack of support from top management					
Lack of support from central staff					
Lack of support from customer serving employee					
Lack of people with relevant skills					
Lack of training after implementation					
Insufficient accounting systems (data not available)					
Cost barriers					
Limited resources (e.g. technology etc.)					

10. How important is customer equity management in your company?				
very important	important	neither important nor unimportant	unimportant	very unimportant

III. The new customer equity management dimensions

The proposed construct consists of **seven dimensions***, which influence customer equity:*

• *distribution channel management;*	• *process management;*
• *communication management;*	• *human resource management; and*
• *service quality management;*	• *service and product management;*
• *price management;*	

In the following the value creation of each dimension is discussed in more detail.

11. Does <u>distribution channel management</u> help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to optimise service delivery costs?					
… to meet more different customer needs?					
… to gather customer information about different channel use?					
… to enhance the selling of products?					
… to differentiate from competition?					

12. Does <u>communication management</u> (newsletter, advertising) **help …**

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… customers to be better informed?					
… to encourage customer trust?					
… to enhance customer relationship?					
… to enhance information gathering about customers?					
… to enhance credibility?					

13. Does service quality management help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to differentiate from competition?					
… to increase customer loyalty?					

… to increase company profit?					
… to attract new customers?					
… to enhance service quality?					

14. Does <u>price management</u> help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to differentiate from competition?					
… to offer reasonable account fees?					
… to offer competitive prices?					
… to increase customer loyalty?					
… to offer short-term offers e.g. on savings?					

15. Does <u>service and product management</u> help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to differentiate from competition?					
… to tailor products to customer needs?					
… to use customer information for product development?					
… to offer comprehensive range of products / services?					
… to add value to products / services?					

16. Does <u>process management</u> help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to improve continuously process efficiency?					
… to determine clearly employee's role and responsibility?					
… to outsource specific IT applications?					
… to redesign business processes?					
… to use latest information and communications technologies?					

17. Does human <u>resource management</u> help …

	Strongly disagree	Disagree	Neither agree or disagree	Agree	Strongly agree
… to create a customer-oriented mindset?					
… to inform employees about company planning?					
… to tailor company information to employees' needs?					
… to involve employees in decision-making?					
… to ensure high job satisfaction?					

Thank you for participating in this survey. If you wish to receive the research results of this survey, please give us your email address:

Email address:	

Appendix 3: Interview guide

For testing the validity of the questionnaire (in Appendix 2) used for the quantitative analysis (in Chapter 8), twelve interviews with academics and practitioners have been conducted. The researcher applied standardised open-ended interviews by using an interview guide, which ensured a comparison between answers. Chapter 9 shows the results of this qualitative analysis.

Distribution channel management:

- Which low-cost channels do you provide for increasing customer profits (customer equity)?

- Which channel support activities do you use for increasing customer profits (customer equity)?

- Which multi-channel strategies do you use for increasing customer profits (customer equity)?

Communication management:

- Which communication strategies do you develop for increasing customer profits (customer equity)?

- To which degree do you use open communication for increasing customer profits (customer equity)?

- Which relationship stages do you consider for increasing customer profits (customer equity)?

- Which type of customized communication do you use for increasing customer profits (customer equity)?

Service quality management:

- Which degree of service quality do you consider for increasing customer profits (customer equity)?

Price management:

- Which products do you offer at competitive prices for increasing customer profits (customer equity)?

- Which bundled offerings do you provide for increasing customer profits (customer equity)?

Product and service management:

- Which types of customised products do you offer for increasing customer profits (customer equity)?

- Which new innovative services and products do you launch for increasing customer profits (customer equity)?

- To which degree doe you use cross-selling strategies for increasing customer profits (customer equity)?

- To which degree do you involve customers in the product development process for increasing customer profits (customer equity)?

- To which degree do you provide your customers with added value for increasing customer profits (customer equity)?

Process management:

- To which degree do you use business process management for increasing customer profits (customer equity)?

- To which degree do you automate business rules and business roles for increasing customer profits (customer equity)?

- To which degree do you focus on your core activities for increasing customer profits (customer equity)?

Human resource management:

- To which degree do you improve employees' level of customer orientation for increasing customer profits (customer equity)?

- To which degree do you use employee empowerment for increasing customer profits (customer equity)?

Appendix 4: Glossary

This glossary provides an overview of definitions for terms related to customer equity. Most terms have more than one definition and, therefore, the most frequently used definitions are included in this glossary.

Terms	Definitions
"80-20" rule	Eighty percent of the corporate profit is generated by twenty percent of the customers of an organisation.
7P's marketing mix	The 7P's marketing mix is adapted to the service industry and comprises place, price, promotion, product, process, people, and physical evidence.
Added value	Added value is the value that organisations add to their products and services to attract customers (e.g. paying the same price for more content etc.).
Cross-functional teams	To achieve a more integrated perspective of strategic goals, organisations form teams with employees from different departments. Huber et al (2001), for example, propose cross-functional teams consisting of trend scouts, creative designers, and marketing controller who analyse the actual values, form customer segments and transfer the values and benefits into product attributes.
Cross-selling	Cross-selling means selling customers additional products, which they have never bought before.
Customer acquisition rate	Customer acquisition means increasing the customer base by attracting new customers. The customer acquisition rate is calculated by dividing the number of new customers by the number of all customers and then multiplying it by one hundred.
Customer	Customer development is equal to the term add-on selling

development	and means selling additional products and services to customers.
Customer equity	Most researchers define customer equity as the total of the discounted lifetime values summed over all of the firm's customers (e.g. Blattberg and Deighton, 1996; Rust et al, 2000).
Customer experience	Customer experience is generated by the market offering and the interactions between the organisation and the customer before, during and long after product use. Customer experience is a mixture between physical and emotional elements along all the stages of the value chain.
Customer lifetime value (CLTV)	Customer lifetime value is a measure that categorises customers into most profitable, less profitable, and unprofitable customer segments. The lifetime value of a customer can be expressed as the net present value of a future stream of contributions to overheads and profit expected from the customer (e.g. Courtheoux, 1995). Libai et al (2002) calculate CLTV as the net present value of a customer's profit stream accounting for the firm or segment-level retention rate.
Customer loyalty	Customer loyalty reflects the repurchase behaviour of customers. Some researchers propose a further classification of customer loyalty. Bowen and Chen (2001), for example, propose a classification into three approaches: behavioural, attitudinal, and composite measurement of loyalty. The behavioural measurements consider consistent, repetitious purchase behaviour. Attitudinal measurements use attitudinal data to reflect the emotional and psychological attachment inherent in loyalty. The composite measurements of loyalty measure loyalty by customers' product preferences, propensity of brand-switching, frequency of purchase, recency of purchase and total amount of

	purchase.
Customer needs	Customer needs reflect the wants and desires of customers regarding product, customer, and environment aspects. Consumer behaviour research aiming at identifying customer preferences, found that product preferences change over different times or different situations. Customer characteristics such as mood, emotion, or impulse feeling can also change customer needs / preferences. Finally, the environmental situation such as familiy or social environment can also lead to a change in customer needs.
Customer orientation	Customer orientation is a company's focus on customer needs. An orientation towards customer-focus generates an emphasis on teamwork skills, more breadth of experience, greater empathy for goals and constraints of people in other functional areas, and more flexibility in being able to respond to changing business conditions (Homburg et al, 2000).
Customer perceived value	Customer perceived value is customer's perceived net trade-off received from all relevant benefits and costs or sacrifices delivered by a product or service or supplier and its use (e.g. Snoj et al 2004, Flint and Woodruff 2001).
Customer portfolio analysis	A customer portfolio consists of two dimensions that form the x-axis and y-axis of either a four-cell matrix or a nine-cell matrix. Dimensions focus on, for example, the nature and attractiveness of a customer relationship, market share, competitive position, or other customer data. Customer portfolio analysis enables a firm to formulate appropriate marketing strategies for different customers or groups of customers and to focus on the most profitable customers or on those with the greatest potential.
Customer profitability	Customer profitability analysis aims at calculating the profit of a customer or customer segment and enables organisations to identify the key differences between the segments.

	Customer profitability analysis determines the difference between revenues per customer and costs per customer. Customer costs can include sales costs, service costs, production costs, and other general costs.
Customer pyramid	This method segments customers according to their profitability and categorises them into tiers (e.g. platinum, gold, iron, and lead) (Zeithaml et al, 2001).
Customer relationship management (CRM)	On the one hand, customer relationship management is seen as a technological innovation in the form of software, on the other hand, it is seen as a specific business strategy for different customer treatment. Researchers define customer relationship management as an approach that automates and centralizes customer contacts, facilitates the development of more personalised products and services, encourages staff to quicker answer customer questions and complains, and provides direct immediate information to sales, marketing, and employees as needed to better serve the customer (Bannon, 2001).
Customer retention	Customer retention means maintaining long-term relationships with customers to avoid that customers switch to competitors. A growing pool of retained customers helps to increase corporate profit due to the fact that loyal or satisfied customers will pay price premiums (they buy more expensive products), adopt line extensions more readily (Keller, 1993), try and refer products more frequently, and have lower sales and service costs (Reichheld and Sasser, 1990; McNaughton et al, 2002). Most organisations improve customer retention by learning from former customers, analysing complaints and service data, implementing retention management programs, and identifying and raising barriers to customers' switching.
Customer retention	The customer retention rate is a measure that determines

rate	how loyal customers are. The rate is calculated by dividing the number of customers still buying in period two by the number of customers who bought in period one and multiplying it by one hundred.
Customer satisfaction	Customer satisfaction either refers to the evaluation of one transaction or all transactions made until that moment. The latter means that customer satisfaction as an overall evaluation based on the total purchase consumption and experience (e.g. Anderson et al., 1994) (cumulative measure). The disconfirmation-of-experience paradigm states that when a purchase of a product or service is made the customer expects to receive a benefit greater than the cost (Eggert and Ulaga, 2002).
Customer segment	A customer segment is a customer group with homogeneous preferences and needs.
Customer value	Customer value has been studied under the name of customer lifetime value, customer equity, and customer profitability (see Hwang et al, 2004) and customer perceived value. Therefore, there is no common definition of customer value in the literature.
Customer-centered organisation	A customer-centered organisation focuses on the customers and develops products and services that are in line with customer needs. Moreover, it continously improves its business processes and value chain to achieve customer orientation.
Customer-oriented value chain	A value chain comprises value chain elements, such as purchasing, production, distribution, sales, marketing, infrastructure, finance, human resource, information systems, partnerships etc. To transform a value chain into a customer-oriented value chain, all value chain elements have to be compared with those of competition and then transformed so that a higher value delivery is possible (see Walters and

	Lancaster, 1999a).
Customisation	Customisation means tailoring product and / or services to customer needs.
Data mining	Data mining techniques like clustering enables organisations to successfully segmenting and targeting customers across various industries. Data mining provides an effective approach to discover and understand patterns in customer behavior and to form appropriate marketing strategies.
Data warehouse	A data warehouse is a repository of an organization's transaction and non-transaction data specifically structured for dynamic queries and analytics. A data warehouse extracts electronic data and information from different data sources and provides analytical tools for analysing and reporting the data (e.g. sales invoices, order receipts, customer turnover etc.).
Decile analysis	The decile analysis is similar to the key account management analysis and uses customer turnover to form customer segments (or deciles). It categorises all customers into ten evenly numbered segments and then sorts them according to their turnover.
Key account management	This method builds customer segments according to their turnover or profit margin respectively. Customers are categorized into four customer groups (customer segments): key accounts, A-customers, B-customers, and C-customers. Key accounts are customers with the largest share of turnover, whereas A-customers have a lower turnover than key accounts. B-customers have a lower turnover than key accounts and A-customers, and C-customers represent the group with the lowest turnover.
Market orientation	Market orientation is a combination of customer orientation, competitor orientation, and inter-functional co-ordination

	(Narver and Slater, 1990). In contrast to customer orientation, which considers only customers, market orientation also takes into account the competitive situation, and the co-ordination and sharing of resources with other departments.
Market penetration rate	A third performance measure that organisations use to compare the customer segment with a representative sample of consumers from a national consumer database is the penetration rate. The penetration rate is calculated by dividing the number of customers by the total consumers in the market and then multiplying it by one hundred.
Monetary factors of customer equity	Monetary factors are factors that see the value of a customer from a financial perspective. Examples are customer turnover, customer profitability, or customer costs.
Non-monetary factors of customer equity	Non-monetary factors are factors that see the value of a customer from a non-financial perspective. Examples are number of purchases, frequency of purchases, or customer lifetime (duration of the customer relationship).
Perceived benefits	In the literature, there is no common defintion of perceived benefits. Researchers, such as Lapierre (2000), suggest that perceived benefits comprise service quality, service customisation, responsiveness, flexibility, reliability, technical competence, image, trust, and solidarity. Monroe (1990) proposes a similar comprehensive definition and describes perceived benefits as a combination of physical attributes, service attributes, and technical support available in relation to the particular use of a product or service.
Perceived sacrifices	Perceived sacrifices are a combination of a nominal price and all other costs of product acquisition and its use (e.g. Slater and Narver, 2000). Most researchers define the other costs as time cost, energy cost (or search costs), and psychic cost (e.g. Kotler, 2000; Zeithaml and Bitner, 1996).

	In contrast, other researchers, such as Monroe (1990), for example, defines perceived sacrifices as tangible costs related to the service, such as purchase price, acquisition costs, transportation, repair, maintenance, as well as perceived costs such as risk of failure or poor performance.
Product-centered organisation	A product-centered organisation focuses on its products and services for increasing corporate profit. This means that the company does not consider customer needs for developing its products.
Profit per customer	Profit per customer is calculated by subtracting customer costs from customer's revenues over a certain period.
Return on customer (ROC)	ROC equals a firm's current-period cash flow from its customers plus any changes in the underlying customer equity, divided by the total customer equity at the beginning of the period. Customer equity is the sum of all discounted future cash flows a firm expects its customers to generate (Peppers and Rogers, 2005).
RFM analysis	The recency, frequency, and monetary (RFM) analysis uses buying behaviour to categorize customers into cells allowing organisations to treat these cells in different ways. Recency refers to the time elapsed since a customer made his last purchase. Frequency is the total number of purchases that a customer has made within a designated period. Monetary is each customer's average purchase amount.
The 3C method	This method uses process control techniques to measure, manage, and improve customer performance and customer focus (Curry and Curry, 2000).
Transaction marketing	Transaction marketing is more product-oriented with a limited customer commitment, and a moderate customer contact. It is more focused on a short-term scale. In recent years, there was a shift from transaction marketing to relationship

	marketing as the consideration of customer needs is becoming important for enhancing corporate profits.
Up-selling	Up-selling means that organisations sell customers more expensive but similar products to those that they have already bought.
Value proposition	The value proposition is a statement of how value is delivered to customers.

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