Understanding the Processes of Customer Acquisition, Customer Retention and Customer Relationship Development

by
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Abstract. Attracting new customers is an objective pursued by any organization, which in the actual competitive environment is almost inevitably facing with a phenomenon of customer migration. Therefore, lost customers must be replaced and this process involves specific activities of prospects identification, communication channels selection and choice of the adequate supply for targeting potential customers. Processes of customer retention and customer relationship development are a logical continuation of customer acquisition plans. A retention strategy aims to maintain relationships with a highest proportion of the current customer base by decreasing their migration rate. A relationship development strategy involves additional efforts to increase the value or profitability of existing customers. These strategies are differently designed in relation with various customer segments, depending on their current attractiveness and their development potential. Retention strategies may be classified into two main categories, positive and negative, in light of the influence they have on customer repurchase behaviour and attitudes. Development objectives relate primarily to selling additional products and services to customers in the current database and selling higher value or higher profit margin products and services to the same customer segments.

Key words: customer acquisition, relationships development, relationship marketing, retention rate.
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1 Introduction

In recent decades, international business environment has experienced a number of significant changes at economic, technological and also social levels, fact that has impacted on the purchasing behaviour of individuals and has thereby affected companies' marketing strategies.

Motivated to identify new sources of competitive advantage, organizations began to realize the importance of customer retention and customer loyalty in order to enhance business strength and maximise long term profits (Filip, 2011c).

In this context, the relationship marketing approach has gradually replaced the transactional philosophy, as enterprises from various fields of activity have understood the enduring value that customers develop throughout the business relationship life cycle (Filip, 2011b).

A relationship is considered to exist when customers consider exchanges as being in conjunction with past experiences and with those that will take place in the future. In conclusion, a relationship is defined as one or more exchange activities between a buyer and a seller, which are perceived by the customer to be correlated with past and future exchanges (Dwyer *et al*, 1987).

Customer relationships have their own life cycles and the organization should adapt its behaviour according to the specific stages of relationships evolution. Relationship life cycle management requires finding the appropriate tools of action to identify and attract new customers and then to preserve and increase their profitability.

2 The process of customer acquisition

Attracting new customers is an objective pursued by any organization, which in the actual competitive environment is almost inevitably facing with a phenomenon of customer migration.

Even in cases where different loyalty or retention programs are implemented, some companies can achieve a migration rate of 25%

per year or more. In the consumer goods market, buyers will move into another age or income class, they will modify their home addresses or they will experience different lifestyle changes. Given these changes, they will no longer have the target audience profile. Even in the business to business market, organizational customers may switch suppliers from various reasons that will not be always determined by the company's performance; for instance, giving up to the production of some products that require the supply of goods from the current company.

Therefore, lost customers must be replaced and this process involves specific activities of prospects identification, communication channels selection and choice of the adequate supply for targeting potential customers. The emphasis is on the early stages of the relationship, in order to move up on the "loyalty ladder" and to conclude a first transaction (Egan, 2008).

A new customer can be viewed from two perspectives, new for a product category or new for the company. In mature markets, most companies try to attract customers with whom they have never conducted businesses, but that can be found in competitors' portfolio. Often, individuals and organizations choose to buy a certain type of product or service from several suppliers, having the intention to decrease dependence on a single source of supply or sometimes, just for variety seeking reasons. In other cases, buyers seek the best price on every purchase made.

Thus, it is observed that the number of customers who buy exclusively the goods of one single supplier is quite small, most of them choosing products from several alternatives or from a portfolio of competitive offers.

There are situations when some customers haven't buy from the company for a certain period of time, although it remains a viable option for future purchases. Companies often set different rules to revitalize relationships with these buyers. For instance, promotional offers will be sent to those customers from the data base, which haven't made purchases in the last four months.

These examples prove that customer acquisition and retention indices are not enough to measure organizational performance. A customer of the company will buy in the same time from other competitors, thus additional efforts will be need to gain a higher share of wallet.

2.1 Prospects identification

Prospects identification is the first activity to be undertaken in order to implement a customer acquisition plan and it is the result of the market segmentation process.

In business to business environment, prospecting is a task that falls under the responsibility of the sales force (Filip, 2011a). Agents start with an initial action of buyers' qualification, which after that will have to be targeted by determining their specific needs and payment capacity.

In some industries, such as the banking field, prospects qualification is an automated process, algorithms being developed for assessing the creditworthiness of those applying for loans.

2.2 Contacting potential customers

Once qualification activities have been completed, the organization must decide on the channels that will be used to *initiate contacts*. The principal distinction must be made between channels of direct or personal communication and those of indirect or impersonal communication.

The first involves communication actions made by phone, mail, e-mail or direct contacts with the sales force, while the second category mainly involves mass-media promotions, communication unfolding in a single direction, from the transmitter to the messages recipients. Usually, the use of direct channels is presumed to have a greater influence on consumer behaviour than indirect channels and developing the quality of data bases allows many companies to benefit from this advantage (Voinea and Filip, 2011).

Choosing to identify satisfied customers from the data base and then to request recommendations from them, will enable the organization to attract new buyers. This opportunity is especially important as marketing studies show that the duration of business relationships with customers that have been acquired through referrals drawn higher than average (Verbeke *et al*, 1995).

2.3 Development of communication activities

Promotional activities are initiatives often undertaken by companies to attract new customers, but there are differences regarding their use and effectiveness in consumer and business to business markets.

Thus if in the case of consumer goods and services, the greater part of the promotional budget is allocated to advertising and sales promotion techniques, *in organizational markets* these techniques are rarely used to attract new customers, the *advertising* role being especially informative, to create awareness, not having as main purpose to influence the effective purchasing behaviour of buyer organizations.

In this case, relationships initiation and new contract negotiation are made by *sales force*. Similarly, participation in *fairs and exhibitions*, congresses and seminars are considered very useful means to identify prospects and develop lists of potential customers.

Outbound telemarketing activities are also useful techniques in actively prospecting organizational customers and they are usually performed by contact centres' employees. Besides prospecting, internal agents are also involved in complaint management, cross-selling and lost customer regaining activities.

In the *consumer goods market*, communication efforts to attract new buyers are differently distributed. Due to the large number of prospects, promotional activities are primarily conducted through the use of indirect channels, but which have the advantage of targeting a broad audience.

Advertising is the most commonly used promotional tool, followed by *sales promotion techniques* designed to stimulate the free trial of products, such as distribution of samples or free trial periods.

Special offers or discount coupons also stimulate buying acts. Positive results in terms of sales are also achieved through the use of *merchandising techniques*, product positioning on the shelf at the eye level proving to be more productive than other levels.

Although customer acquisition may be achieved through multiple activities, decisions regarding what techniques and activities to be used must take into account cost considerations and the estimated duration of business relationships or the quality of acquired customers. For instance, advertising and sales promotion activities are costly, but they will attract in the same time a large number of new customers. However, the disadvantage consists of a lack of stability related to this type of buyers, who are either variety seeking persons, either opportunistic shoppers aiming to choose the products with the lowest prices.

Referrals programs have a lower cost, but also attract only a small number of customers. However, customers that have been acquired through recommendations tend to be more loyal and spend more on the company's products (Buttle, 2004).

Customer prospecting activity may be facilitated by CRM systems. Data mining techniques can be used to identify which of the current customers have the highest profitability potential (Boja, 2011). An analysis of these customers' profile, of the channels through which they were initially attracted and of the first products purchased will provide important clues, useful to identify prospects that have a similar profile.

3 Customer retention plans

Processes of customer retention and customer relationship development are a logical continuation of customer acquisition plans.

A *retention strategy* aims to maintain relationships with a highest proportion of the current customer base by decreasing their migration rate. A *relationship development strategy* involves additional efforts to increase the value or profitability of existing customers. Of course, these strategies are differently designed in relation with various customer segments, depending on their current attractiveness and their development potential.

In developing a customer retention plan, the company must find answers to a number of questions: Which are the target customers or customer segments? What retention objectives should be established? What strategies will be used to achieve them? And how will be measured the plan performances? (Buttle, 2004).

Retention and migration are opposite concepts; a high retention rate is equivalent to a low migration rate and vice versa. Conventionally, the retention rate is measured by "the number of customers that are in business with a company at the end of a financial year, expressed as a percentage of the total number of active customers at the beginning of the year" (Dawkins and Reichheld, 1990). However, the one year interval is not appropriate in any case, because the specific repurchase rate of a certain industry must be taken into account.

There are also situations when organizations are not able to clearly identify customer migration. This problem often arises from the specific manner of storing customer information in the data bases. For instance, assurance companies usually organize their informatics systems by focusing on products. In other words, the firm sees an insurance policy as representing a customer. If the policy is renewed, the customer is considered to be active; otherwise it is assumed that he has migrated.

The same problem is encountered when companies use multiple channels for customer acquisition, with no integration in order to obtain a single image of the customer profile.

Although they are useful in forming an overview of business stability, using only the average values in the calculation of migration or customer retention rates cannot be considered sufficient.

Customers differ significantly in terms of sales, cost of service, buying frequency, etc. In many industries, a small number of customers are responsible for the greatest part of a company's revenue.

Using average values, the loss of 50 customers from a total of 500 that form a company portfolio, translates into a migration rate of 10%. If, however, these customers have a significant contribution to the company's sells and profits, their migration will have a higher unfavourable influence, leading to a real decrease of 30% or even 50% in the firm's revenue. There is also the opposite case in which the lost customers have an insignificantly contribution to the company's revenue or the firm even record losses in relationships with these buyers. In this situation, customer migration is a more favourable behaviour from a business perspective (Payne, 2005).

To address the problems noted above, retention objectives should be set by using three different indices:

a). *The gross retention rate*, defined as the percentage ratio between the number of customers involved in business relationships with the organization after a certain period of time and the number of individuals that were active customers at the beginning of the same period.

b). *The sales adjusted retention rate*, defined as the percentage ratio between the sales value derived from customers who have remained in business relationships with the organization after a certain period of time and the sales value achieved from all the active customers at the beginning of the same period.

c). *The profits adjusted retention rate*, defined as the percentage ratio between the profits value derived from customers who have remained in business relationships with the organization after a certain period of time and the profits value achieved from all the active customers at the beginning of the same period.

The three indices definitions show that a high value of the gross retention rate is not always equivalent with the implementation of an efficient customer retention program. Moreover, the sales and profits adjusted retention rates should be analyzed in conjunction with the company's share of wallet that is achieved from those customers who are maintaining business relationships.

Retention and loyalty programs are mainly oriented towards customers with high profitability or who may bring other benefits to the organization, due to their technological knowledge or opinion leader status.

Some companies prefer to focus their retention efforts on recently attracted customers. Their decisions are based on a series of studies, which show that retention rates tend to increase over time, and if migration can be prevented in the first years of the relationship, the company will benefit more in the future (Reichheld, 1996).

Retention strategies may be classified into two main categories, *positive and negative*, in light of the influence they have on customer repurchase behaviour and attitudes.

Positive retention strategies support the willingness of customers to imply in business relationships and have a favourable influence on both customer attitudes and behaviour. Emphasis is placed on rewording customers who continue the business relationship, through quality products and services and unique experiences leading to greater satisfaction, trust and commitment among customers. The most popular tools used for this purpose are loyalty schemes and customer clubs.

Negative retention strategies penalize customer switching behaviour by imposing exit barriers translated into economic, legal or other type of costs, which are designed to coerce the customer to remain in the business relationship. Customers feel trapped sometimes when they perceive such barriers, expressing their dissatisfaction by negative word of mouth.

Assessing the effectiveness of customer retention programs involves quantification of the results obtained for each of the indices contained in the objectives initially established. Simplifying, those responsible for implementing these programs must find answers to a specific set of questions such as: What is the value recorded by gross retention rate both overall and within each customer segment? What is the value recorded by sales and profits adjusted retention rates both overall and within each customer segment? What is the cost of customer retention activities? What is the share of wallet achieved by the organization among retained customers? etc.

4 Relationship development process

Relationship development process involves efforts to increase the value of existing customers, without neglecting their satisfaction (Payne, 2005).

Development objectives relate primarily to:

a) Selling additional products and services to customers in the current database (cross-selling).

b) Selling higher value or higher profit margin (in the same category) products and services to the same customer segments (up-selling).

However, this process must be based on a detailed knowledge related to customer requirements and how will evolve their needs. In general, customers do not react well to insistent and repeated attempts of the sales agents, especially if the promoted products are not appropriate or are not adapted to their specific needs.

Up-selling activities, which seek to replace the current product with a more expensive one from the same category, are sometimes considered to be opportunistic, thus having a negative effect on the level of customer trust in a certain supplier.

To be successful, relationship development activities must meet several conditions (Buttle, 2004):

- Products that are supplied to customers must be based on a thorough analysis of past individual transactions and of customer demographic and psychographic profile.
- Products must be adapted to customer segments or even to individual customer requirements; customization relates also to communication channels and to the messages that are sent to customers.
- All channels used for customer interactions must be integrated. Therefore situations must be avoided when customers receive several offers from the same organization that are sent to different channels.
- The use of integrated marketing communication is another feature. Messages sent to customers must be consistent, regardless of the media used.

5 Conclusions

In mature markets, where the objectives of attracting new customers are difficult or costly to meet, customer relationship development becomes an important alternative for achieving additional income.

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