Investing in Customer Satisfaction Improvements

If greater customer satisfaction results in more revenue and profit, then it makes sense to invest in improving satisfaction levels. LOMA has the tools available to help your company quantify customer satisfaction and loyalty.

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Everyone "knows" that improving customer satisfaction is a worthwhile goal for life insurance companies. We all believe that satisfied customers are more likely to continue to pay their premiums or renew their coverage, to buy additional products, and to tell other people positive things about our company's products and services, all behaviors which have a positive impact on revenue and ultimately on profits. With all these potential benefits, it makes sense that a company should invest whatever it takes to improve customer satisfaction, right?

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The answer to this question may not be a simple "yes". The obvious answer is that a company should not invest unlimited funds in customer satisfaction improvement, if for no other reason than that no company has unlimited funds. Instead, a company needs to manage this investment process, just like it manages investment in technology or other capital expenditures. If greater customer satisfaction does result in more revenue and profit, then it should be possible to calculate a return on specific company efforts to improve customer satisfaction.

Therefore, I would like to outline one process which may be used to manage investments to improve customer satisfaction. This process is based on two assumptions:

- That we understand how a company's investment actually improves customer satisfaction and ultimately produces a return on that investment.
- That a company has the necessary measurement tools in place to quantify the impact of these investments.

With this information, a company can evaluate alternative customer satisfaction investments, and select those which will produce the greatest return for the company.

The Process

Figure 1 shows a simple model which describes how an investment intended to improve customer satisfaction actually produces a return for the company. In explaining this model, it is important to define customer satisfaction, then examine factors which lead to customer satisfaction and customer behaviors which are influenced by customer satisfaction. Finally, an example which demonstrates how a specific investment might be evaluated is presented.

Customer Satisfaction: Satisfaction is a positive feeling about a particular entity. In customer satisfaction surveys, this is usually measured with one or two questions which ask the respondent to agree or disagree with statements like "I am satisfied with XYZ company" or "I am happy with XYZ company" or by questions which ask the respondent to indicate how satisfied they are with the company.

If this is the only data we have and our goal is to use this information as a tool to help evaluate investment decisions, two problems emerge. First, these general types of measurements do not provide much guidance concerning where to invest company resources. Should a company provide more training to its customer service representatives? Should a company invest in systems which will shorten turnaround times? Should a company institute a policy that all phone

calls will be answered before the third ring? Simple measures of customer satisfaction do not provide a means to choose between these different options. Choosing the best course of action requires that we know specifically where the problem lies. Toward this end, a company might address this issue by asking more specific questions. For example, the respondent might be asked to indicate how satisfied he or she is with the company overall, the product's features and benefits, the product's price, the agent or broker with whom the respondent interacts, and the service he or she received when dealing directly with the company. This information would at least help the company target its investment decisions.

The second problem in relying solely on these measurements of customer satisfaction is that it is very difficult for a company to directly influence an individual's feelings. For example, how do your employees change the way they perform their jobs if they are given a goal of "make a customer happy today?" While it is certainly possible to treat each customer interaction as a "Moment of Truth," it is very difficult to establish measurable goals for making customers happy which can be used to guide investment decisions. To remedy this issue, we need to understand how investments we make ultimately result in greater customer satisfaction.

Service Quality: In Figure 1, the factor which predicts customer satisfaction is service quality, or the difference between a customer's expectations and his or her perceptions of the company's performance[1]. Most readers will recognize this as "meeting or exceeding customer expectations." If your company delivers what your customer expects, he or she is generally satisfied. If your company delivers more than what your customer expects, he or she is "delighted." In other words, if we know how positively the customer views service quality, we should be able to predict customer satisfaction. Thus, if a company can identify specific areas in which its performance fails to meet or exceed expectations, it can target its investments to specifically address these shortfalls.

However, different areas will be more or less important to some individuals than to others. For example, some individuals may be very concerned about their relationship with their agent. The agent's performance in terms of explaining different options and selecting the best policy based on the needs of the customer may be the primary factors which influence the customer's decision to purchase a policy from your company or from another company. Other individuals may be primarily concerned with price and value issues. They seek the lowest cost alternative, and are relatively unconcerned with agent performance per se. A decision to invest in improving agent performance should have a positive impact on perceptions of service quality (and ultimately, customer satisfaction) for the first group, but will probably have little impact for the second group. Thus, in deciding how to invest to improve customer satisfaction, two questions are important. First, where is the company's performance failing to meet or exceed expectations, and second, which of these areas are most important to the customer's satisfaction.

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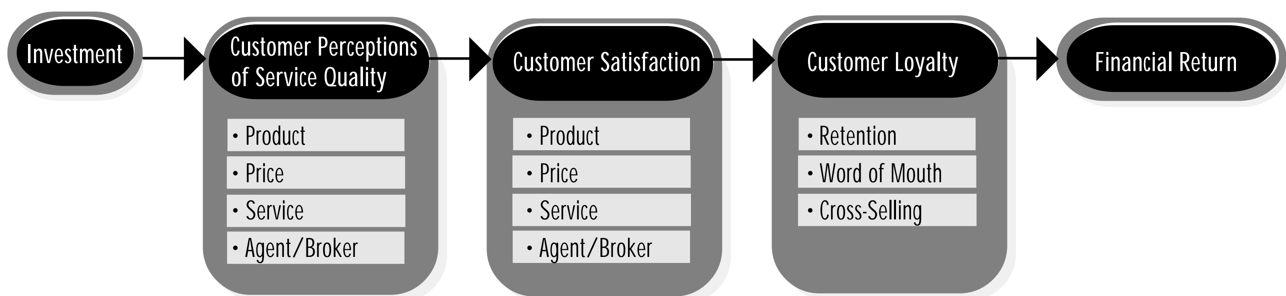
Let's walk through an example of how this might work. LOMA currently administers a survey which asks policyowners to tell whether their insurance company meets or exceeds expectations with respect to four specific areas – product performance, price or value, customer service performance, and agent performance. Within each of these more general areas, we ask a number of questions which relate to specific performance issues. We also ask about satisfaction with each of these performance areas and about overall satisfaction with their insurance company. With this information, we can identify specific areas in which the company's performance is below expectations, and we can also develop a model which quantifies the relationship between specific performance issues and overall satisfaction. For example, we might find that the technology used by the company to provide customer service is below customer expectations. However, we might also find that technology performance is not a very good predictor of overall satisfaction. In this situation, we would expect that an

[1] Zeithaml, V., Parasuraman, A., & Berry, L. (1990). *Delivering Quality Service*, New York: The Free Press.

Figure 1



investment to improve customer service technology would have a relatively low return in terms of its impact on improving customer satisfaction.

Customer Loyalty: To this point, the discussion has focused on improving customer satisfaction. However, satisfaction per se is not necessarily our ultimate objective. Instead, we are interested in specific behaviors in which satisfied customers are more likely to engage and which ultimately result in more revenue and more profits. For example, satisfied customers are more loyal, which means that they are more likely to keep their policies in force. Satisfied customers are more likely to buy additional products from your company when given the opportunity to do so, which means that your company generates additional revenue from that customer. An added benefit is that it costs less to

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sell them a new product than to sell that product to a totally new prospect. Satisfied customers are more likely to tell their friends and acquaintances positive things about your company, which means that these other people may be more receptive to your marketing efforts. In essence, satisfied customers are more loyal to your company, and this loyalty means that they are more valuable to your company than other customers.

It is not that customer satisfaction is not important. It is. But customer satisfaction by itself is of limited use to directing investment decisions. Customer satisfaction is important because satisfied customers do things like pay their premiums or buy additional products which ultimately improve the financial performance of the firm. These behaviors produce the financial return which allows us to compare the potential impact of investment alternatives. Thus, investments in service quality which are targeted specifically at areas in which customers feel the company's performance is lacking *and* which are important predictors of satisfaction lead to higher customer satisfaction, which in turn leads to greater customer loyalty and ultimately, a positive return on the original investment.

The Investment Model

The preceding discussion has explained how a specific investment targeted at a service quality improvement issue identified through a customer opinion survey can ultimately generate a positive return for the insurance company. However, to use this information to evaluate alternative investment opportunities, it is necessary to actually quantify the expected impact of service quality improvement in terms of dollars. This requires that we know the value of a customer, and how customer behaviors can influence the value of a specific customer.

The value of a customer may be defined as the profit which that customer will generate over the span of time in which he or she is actually a customer. To calculate this value, we need to identify all the possible revenue streams that customer may generate and all the costs associated with attracting that customer, with administering or service the policy(s) that customer may have, and with paying the benefits defined in the policy(s). For example, in simplistic terms, the value of a customer who owns only a life insurance policy may be calculated as the premium that individual will pay over the life of the policy less the benefit paid at time of death, selling costs associated with that policy (including up-front and ongoing agent commissions), and administrative costs associated with the policy. However, this single policy is not the only potential revenue (or cost) stream which this individual represents. He or she could purchase other products or services, or he or she could tell other people about the insurance company or provide referrals, which would enable the company to make additional sales. Thus, the value of a customer is potentially much larger than the value represented by a single policy.

There are at least three ways in which improving customer satisfaction may increase the value of a customer. First, by reducing the likelihood that an individual will allow his or her policy to lapse, the revenue stream from that policy should be greater. Second, by increasing the likelihood that the customer will be receptive to offers for additional products and services, the revenue stream from all products should be greater. Third, by increasing the favorable "word of mouth" comments from the customer, revenue should be increased from sales of products to friends and acquaintances of the customer. Thus, if we can quantify how much these types of customer behaviors will change as a result of investments to improve customer satisfaction (and we do this by estimating the model presented in Figure 1), then we can estimate how much the value of a

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customer will change as a result of specific investments to improve customer satisfaction.

Measurement Tools

You may be thinking "this may be a good idea, but we don't have the information necessary to quantify all these relationships." Yes, there are significant requirements for detailed information which may or may not be readily available in your company. You need to be able to quantify the impact of service quality improvements on customer satisfaction and customer loyalty, and you need to be able to quantify the value of your existing customer base. The latter requirement will be specific to your company, based on your actuarial assumptions and your accounting data. The customer satisfaction model may be estimated on the basis of customer opinion survey results. In next month's issue of *Resource,* we will report on the results of a survey administered for several life insurance companies which is designed to provide the information necessary to build such a model. ❑

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