FischerJordan

The Cost of Bad Customer Service

And the need for back-end service recovery

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INTRODUCTION

While most companies recognize the importance of good customer service, they are often not aware of the financial benefits of good customer service and the potential costs of a service failure.

The definition of a service failure is simple – any customer service call that results in a dissatisfied customer. There could be many reasons for dissatisfaction. Some customer dissatisfaction is due to control issues at the service center such as long hold times, a customer service representative's lack of knowledge, or accent and language barriers.. Other reasons not under the service center's control may include dissatisfaction with the company's product, company policies, forces of nature, and more.

Today, many large companies have giant call center networks that comprise tens of thousands of customer service agents, located locally and offshore, dealing with millions of calls per year. Servicing such a large number of calls will inevitably lead to some service failures.

While most call center managers are tasked with improving customer satisfaction, they face significant constraints:

1. Call centers are viewed as cost centers: Company management often requires costs to be held constant despite growing servicing volumes.
2. Finding qualified agents is difficult: In recent years, attrition has been high – as average tenures have declined, the quality of customer service agents has declined.
3. Legacy technology systems: Important improvements often require significant technology investment to replace legacy systems.

In this environment, investing large amounts in preventing every potential failure upfront is not cost-effective. However, our analysis indicates that in many cases, aggressive back-end recovery may be a less expensive and more effective strategy.

Further, Bitner et al.[1] have shown that it is not necessarily the failure itself that leads to customer dissatisfaction, but rather the lack of a quick response to a service malfunction. Companies that have internalized this insight have seen great benefit from the implementation of a service recovery mechanism. Starbucks is a good example: Baristas are empowered to solve almost any situation leading to a dissatisfied customer by such means as exchanging the product or refunding the payment. By so doing, Starbucks assures that any failure is addressed as soon as possible and that almost no customer leaves a Starbucks branch dissatisfied.

[1] Bitner, M. J., Booms, B.H. and Tetreault M.S. (1990), "The Service Encounter: Diagnosing Favorable and Unfavorable Incidents", Journal of Marketing, 54 (January), 71-84

SERVICING CATASTROPHES – A RECENT EXAMPLE

In the last few months alone, a few large companies have suffered from substantial public service failures. One such firm was JetBlue. The low cost airline with a reputation for great customer service had to deal, like all other airlines, with a February storm that shut-down several airports on the east coast and caused delays all around the country. While an ice storm may be out of the company's control, servicing the stranded customers is nonetheless the company's responsibility and serves as a source of differentiation. JetBlue suffered from a customer service "meltdown" that left customers angry and frustrated.

The day after the customer service fiasco, JetBlue's market capitalization fell by more than $100MM. JetBlue's CEO at the time stated that he was not concerned with the $30M cost of refunding airfares and lost revenue, but rather that he was more focused on "rebuilding JetBlue's reputation in the eyes of their customers" after this "defining moment". Following its large scale service failure, JetBlue has decided to launch several service recovery initiatives such as a "Customer Bill of Rights", refined service procedures, and an enhanced refund policy that will be applied retroactively to customers who were impacted by the ice storm.

TYPES OF SERVICE FAILURES

In JetBlue's case the service meltdown was a large, one-time event and hence received a lot of attention from the public and the company's management. However, more often than not, customers experience similar frustration and dissatisfaction on a smaller, more ongoing basis. These service failures are caused by day-to-day service issues that don't receive as much publicity. The damage caused to a company from this type of dissatisfaction varies by the service failure type. Some examples include:

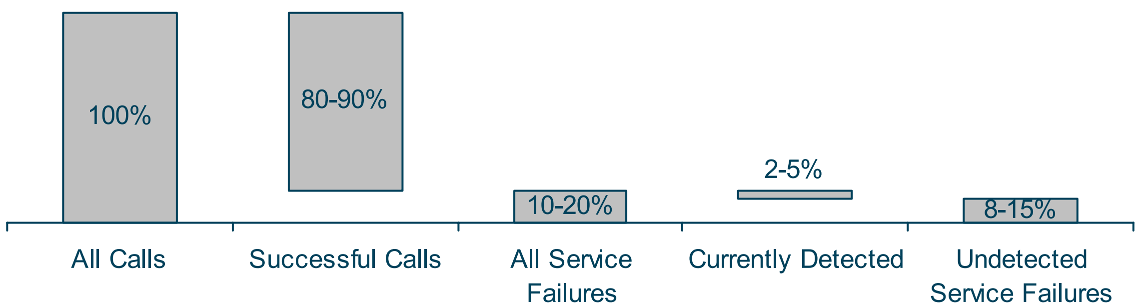
Figure 1 – Service Failure Types

Service Failure Type	Examples
Manpower / Infrastructural Related Issues	• Long hold time • Representative accent (due to offshore servicing) • Slow fulfillment
Customer Service Policies	• Dissatisfaction with service policies, e.g., lack of representative empowerment • Representatives are cross selling additional products during a service call
Incompetent Service	• Conflicting information • Multiple calls to resolve issue • Multiple transfers between representatives • Representative lacking knowledge • Lack of follow-up • Rude service
Dissatisfaction from the company's product	• General dissatisfaction with product • Damaged product

HOW OFTEN DOES A CUSTOMER EXPERIENCE A SERVICE FAILURE?

While the ratio varies by industry and type of service requested, our experience (even with companies that are perceived to have superior customer service) is that 10-20% of all customer service calls result in a dissatisfied customer. Today, the systems that companies have in place typically detect only a small portion of these service failures. Undetected (and thus untreated) failures lead to customer disengagement and, in extreme cases, customer attrition.

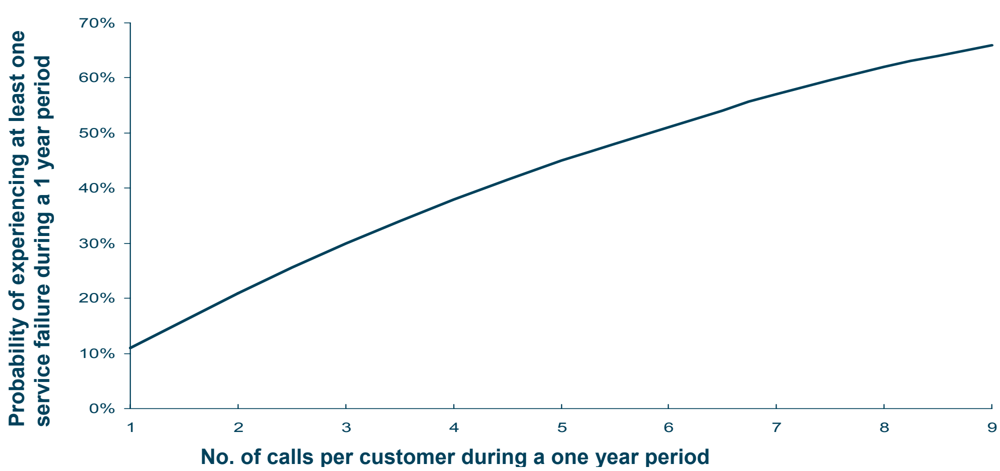
Figure 2 – Distribution of Calls Handled by Customer Service



* Source: FischerJordan analysis

For large companies like cellular service providers, financial institutions, airlines and more, the average customer usually contacts customer service several times a year. The customer is at risk of experiencing a service failure in each of these calls. In most cases, one service failure in one of these calls is enough to cause dissatisfaction and eventually lead to a disengaged customer. As illustrated below, for customers calling more than 5 times each year, the probability of experiencing at least one undetected service failure during a one year period may be higher than 50% – clearly an unacceptable situation.

Figure 3 – Probability of a customer experiencing at least one undetected service failure during a year

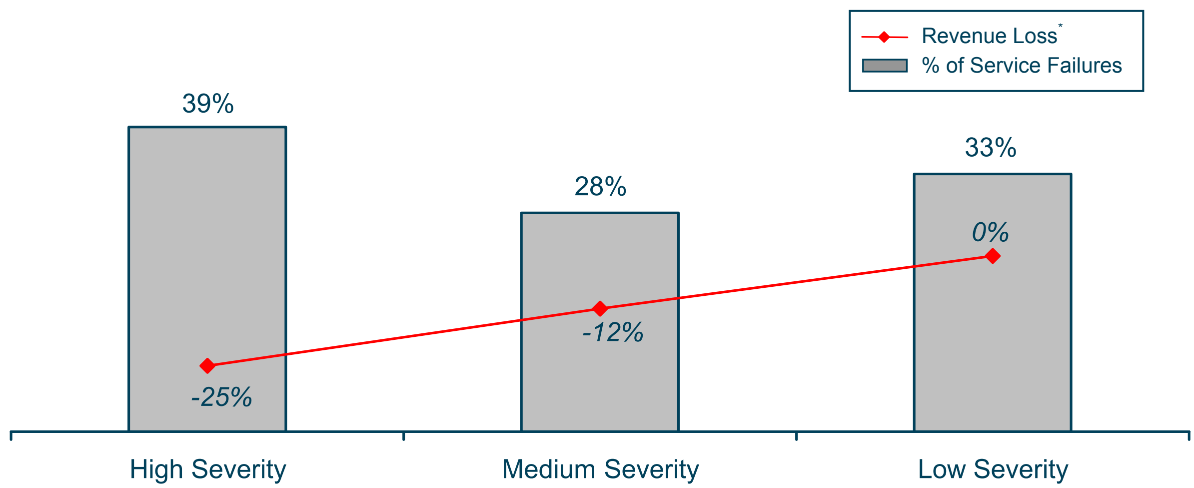


* Figure is presented at an 11% undetected service failure ratio

SERVICE FAILURE ECONOMICS

While the probability of a customer experiencing service failures is high, it is important to understand that not all service failures are equal as far as impact on satisfaction is concerned. When creating a service recovery methodology, a company needs to look at the overall potential negative impact that a specific service failure can have on customer satisfaction. This is governed by both the frequency of the service failure and severity of disengagement caused.

<u>Figure 4 – Frequency and impact on engagement level by service failure type</u>



Examples:

High Severity:
- Long hold Time
- Representative Lacking Knowledge
- Conflicting Information
- Multiple Transfers Between Representatives

Medium Severity:
- Dissatisfaction with Service Policies
- Lack of Follow-Up

Low Severity:
- Cross Sell
- General Dissatisfaction with Product

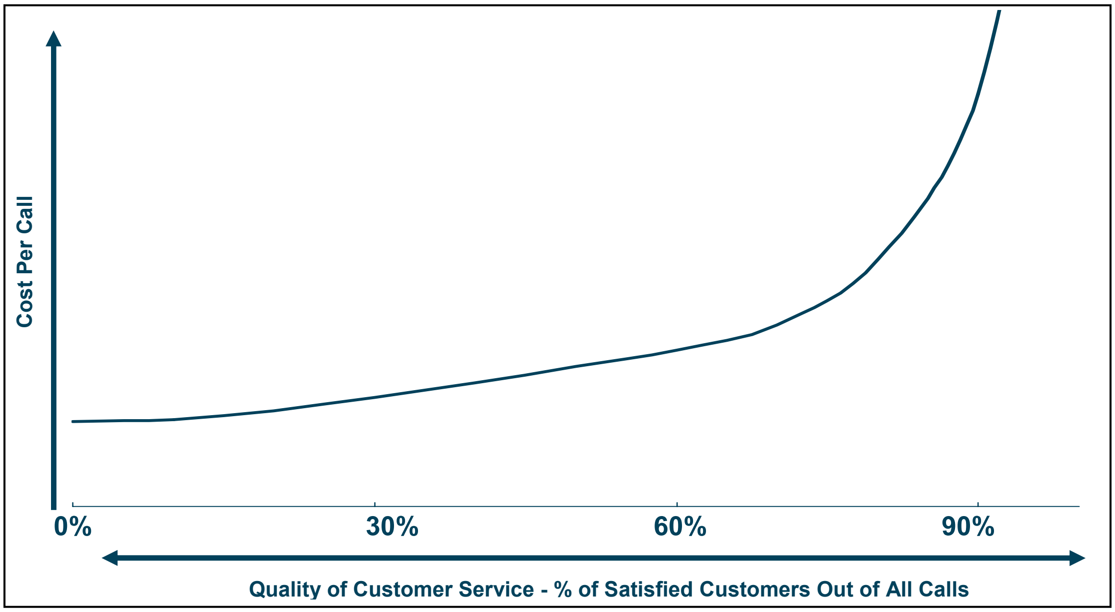
* "Revenue Loss" measures the change in revenue between the 3 months period preceding and following the service failure. Seasonality effects have been eliminated by taking a random sample of service failures across a calendar year

** Source: FischerJordan Analysis

IMPLEMENTING SERVICE RECOVERY: WHEN AND HOW?

Companies tend to focus efforts primarily on prevention. While this is cost-effective for high-frequency failures, it becomes increasingly expensive to fix less frequent failures. Further, as overall failure rates decline, the marginal cost of improvement climbs steadily.

Figure 5 – Cost per call by quality of service (illustrative)



As companies get closer to 100% satisfaction, back-end recovery can often be more cost effective than upfront prevention. The main steps for successful service recovery are:

1. Acknowledge: Recognize that a failure has occurred and acknowledge it
2. Apologize: and explain the reason for the failure
3. Solve: or escalate to someone who can solve
4. Make good: Depending on severity of failure, provide compensation to show the customer how much the company values the relationship

We have observed that existing processes and systems aren't always aligned with implementing service recovery. Some key changes required include:

1. Appropriate incentive structures: Call center representatives often have a disincentive to escalate problems. Similarly, they are often rated on how quickly they can complete a call. Neither are aligned with ensuring effective service recovery
2. Highly qualified recovery team: A group of highly empowered and highly experienced representatives with the ability and authority to solve and make good.
3. Good detection: Clear instructions to representatives defining situations where escalation is required (voice auto-detection may be an option).
4. Limiting "make goods": Clear rules on when reps should offer "make goods" to prevent overuse.
5. Varying treatment based on customer value and severity of failure.

CONCLUSION

Most companies tend to under-invest in service recovery. Complementing prevention efforts with appropriate recovery processes can lead to a differentiated customer experience, particularly during critical customer interactions. Further, our experience indicates that implementing a well thought out service recovery process pays for itself very quickly through reduced attrition and increased engagement.

About FischerJordan

FischerJordan, headquartered in New York City, is a boutique management consulting firm founded in 2004 by alumni of the Mitchell Madison Group and Inductis. FischerJordan has delivered hundreds of millions of dollars of bottom line impact to Fortune 100 financial services companies through its focus on analytics-driven marketing strategy, rewards/loyalty strategy, and reengineering strategy.

About Asaf Zentler

As an associate at FischerJordan, Asaf Zentler has participated in various strategy and reengineering projects in the financial services industry. He has experience in liability provisioning, reengineering, customer analytics and profitability optimization. Prior to joining FischerJordan, Asaf worked at Ernst & Young where he was involved in IPOs and Sarbanes-Oxley implementation projects. Mr. Zentler holds a B.A. in business and a JD from Tel-Aviv University.

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