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+ enterprise loyalty in practice

COLLOQUY's Journal of Innovation in Loyalty

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Towards Transformation

Today's forward-thinking marketers are increasingly aware of the power of gaining customer insights through understanding data. But transforming business — traditionally product-centric and silo-based — towards customer-centricity means embarking on a journey that will create shifts across the entire enterprise. Join us on that trek — the journey to Enterprise Loyalty.

COLLOQUY® | Published by: LoyaltyOne

What About the Shareholders?

+ KYLE MURRAY with JIM SULLIVAN

Don't worry — shareholders are bullish on Enterprise Loyalty.

Research shows that refocusing on employee engagement as a driver of customer loyalty, reducing variability in both employee and customer attitudes towards the firm, and taking a "whole-enterprise" approach, can unleash significant sources of largely untapped economic value. Senior management can build attractive shareholder returns through an Enterprise Loyalty strategy.

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Thirty years ago, Motorola had enjoyed early success in the promising new field of mobile cellular communications. Yet, the precision demanded of manufacturing and assembling hand-held phones required more granular measurement than Motorola's then-current "defects per thousand items" standard. So a Motorola engineer named Bill Smith invented "Six Sigma" — a quality measurement and improvement program that focused on controlling a process to six standard deviations from a centerline, or 3.4 defects per *million* items.

Six Sigma was a value-creating method that reduced process variation against customer expectations for quality. Motorola figures it had saved $16 billion from using Six Sigma in its first 15 years alone. Countless manufacturing firms the world over have embraced Six Sigma as economic gospel, and the quality and value of manufactured goods have improved radically as a result.

Now consider that since that time, our economy has shifted from manufacturing to services. In 1978, manufacturing accounted for about 42% of U.S. GDP. Services now make up 80% of GDP, and account for 82% of non-farm jobs.

In the next 10, or 20, or 30 years, how will firms in the service economy create the kind of value Six Sigma delivered for manufacturers? Is there a similar source of value — currently locked up in excess cost and poor quality — that retail, financial services, travel and hospitality, and other service firms can

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Focal Point | Building Stakeholder Value

Studies show the share-value power of loyal employees

- **Enterprise Loyalty can drive stock value of product and service organizations the way Six Sigma drove stock value of tech companies.**
- **High employee engagement, loyalty and satisfaction are key drivers in the Enterprise Loyalty impact, studies show.**
- **Engaged employees lead to consumer "emotional advocacy"—critical because studies show that "rationally loyal" customers perform no better than "dissatisfied" customers.**
- **True loyalty emerges from the inside out, as an "attractive reaction" to the customer's value perception of your brand.**

take aim at? Bet on it. In fact, invest in it. It's called Enterprise Loyalty.

Enterprise Loyalty is also a value-creation strategy. It recognizes that the great well of untapped value in most firms, especially those in services, lies in reducing the variation in employee engagement and customer loyalty, ranging from excellent to awful across individuals, teams, and locations *within the same firm*. Reducing or eliminating this variability is the next frontier in creating superior shareholder returns. Management teams that understand this fact will be the ones who win — big — for all stakeholders.

Prior to the implementation of Total Quality Management (TQM) and Six Sigma, poor product quality represented a serious threat to sustainable economic growth and corporate profitability. Business leaders responded by implementing rigorous, systematic and data-driven solutions that touched every level of the organization. A similar approach is needed to address the current crisis of distrust and disengagement among customers and employees.

Value destroyed — disengagement and distrust

In its annual nationwide poll, The Gallup Organization recently reported that fully 75% of employees surveyed are either not engaged or actively disengaged at work, meaning they don't really care about their employer or its mission. Gallup describes these people as either "going through the motions" or "actively disengaged and infecting their co-workers with negativity." Further, fewer than one in three employees trusts senior leaders to do what is right in a crisis. Worst of all, these worrisome trends had been building for at least the decade prior to the 2008 meltdown, solidifying with every new corporate scandal (not to mention downsizing, off-shoring, and the effects of recession itself). As a result, within many companies, employee emotional investment, trust in leadership, devotion to the cause, alignment with peers, and support for customers are all casualties.

This is a vast energy crisis, and a waste of productive capacity and human potential. And yet, within every crisis lies opportunity. Business leaders who work to restore trust, full engagement, and loyalty as the pillars of their enterprises will tap a huge reservoir of upside value.

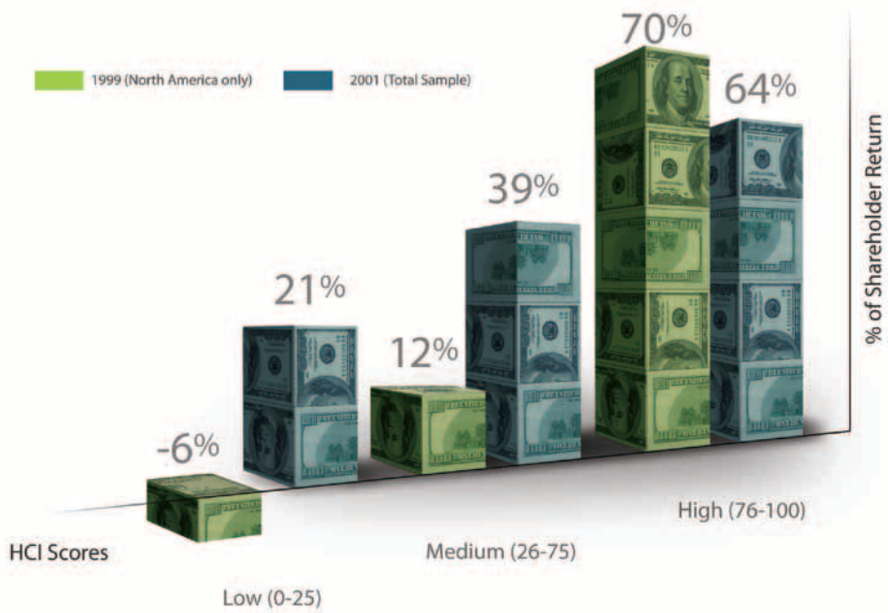
Recent academic and industry research provides the key to unlock this value:

Reignite employee engagement

If charity begins at home, loyalty seems to begin at the office. So says research from Gallup and other industry observers. In 2005, Gallup studied how a company's overall engagement with employees correlated with its financial performance. Gallup had long known that high levels of employee engagement correlated to better

INDEXING LOYALTY CAPITAL

In a now-classic statistical study, Human resources management firm Watson Wyatt (now Towers Watson) developed the "Human Capital Index" (HCI). Using a proprietary statistical formula and based on a 0-100 scale, the Index was correlated to return on shareholder investment. Three studies, from April 1996 to April 2001, produced "a complete respondent base of more than 750 companies in the United States, Canada and Europe with at least three years of shareholder returns, 1,000 or more employees and a minimum of $100 million in revenues or market value." Correlations revealed that the higher the company's HCI score, the higher the company's return — results that, as discussed below, have been supported in other studies.



performance at the business unit level, but this was the first time they had looked at data at the corporate enterprise level. For the study, they turned to their Q^{12} system, which measures employees' emotional and cognitive commitment to their companies. Review of the Q^{12} database (with employee engagement data from 4.5 million employees in 332 organizations) allowed Gallup to select 89 companies that met the following criteria, set in place to get a clean read of the data:

- To facilitate gathering financial data, the companies were publicly traded
- Similarly, the studied companies' competitors were publicly traded — again, for access to data, and to enable comparison with similar organizations within the studied companies' industries
- Gallup had surveyed the entire company and not just a portion of it, so the numbers would reflect a total employee view and allow accurate comparisons to company-level earnings

After pulling the financial data and industry comparables of these 89, Gallup assigned the companies into the top quartile of the Q^{12} database (the Study group) and the bottom half of Gallup's database (the Contrast group). Each group reflected similar proportions of U.S. and international companies.

The EPS growth rate of top-quartile organizations (relative to the industry peers) was 2.6 times that of below-average organizations. This difference in EPS growth rate illustrates one of the principal shareholder benefits of building a critical mass of engaged employees.

Other notable research backs up Gallup's findings with very similar results. A study conducted in 2007 by Vanderbilt University and Hewitt and Associates, a global human resource development firm, found that shareholders could do over twice as well investing in companies who made employee engagement a priority. Specifically, the Vanderbilt study found that a hypothetical investor who in 1998 had purchased the stocks of publicly traded companies that showed up on *Fortune*'s 2007 list of 100 Best Companies to Work For and held them for ten years would have received an average annual return of 18.9%, more than double the 8.4% return of the S&P 500 over that decade.

Connect with customers through a connected front line

Engaged employees create a range of hard-dollar financial benefits, including lower costs from lower

turnover and more effective teamwork. They also help drive top-line revenue and loyalty as they engage customers on the front lines of sales, client account management, customer service and support, and service delivery. All of this is very rational, but research suggests that the emotional connection between employees and customers is the single critical element to consider for both short-term profits and long-term loyalty. Based on the research, emotional engagement is a core value driver, the activating cause of return on investment.

Across multiple consumer categories such as retail banking, lodging, airlines, and specialty retail, Gallup has uncovered something it calls "emotional advocacy" among customers who are deeply connected and engaged to certain brands. This is a distinction over "rational advocacy." Gallup's research shows that among "extremely satisfied" customers, "rationally satisfied" customers behave more like "dissatisfied" customers, while those who expressed emotional loyalty to the brand were, in all cases and categories, the brands' most valuable customers. In the case of a large retail bank, emotionally loyal customers account for 70% more revenue and are 37% less likely to leave than their rationally loyal counterparts.

And that's not all. The effects of emotional engagement operate in two directions (employees to customers and back again), not just one (employee to customer). That means your employees and customers, connecting emotionally as humans, affect each other's emotional engagement levels, and create synergistic business benefits when both are engaged together. The problem is, these emotional connections are not being managed as a core value driver. The effects seem to happen almost accidentally in practice.

From extensive research published in their 2007 book, *Human Sigma: Managing the Employee-Customer Encounter*, Gallup scientists John Fleming and Jim Asplund point out that there is little evidence of managerial control over the factors of employee and customer engagement. The authors explain that such a high degree of variation exists across store and branch locations with regard to these factors, they appear to be unmanaged. That's a critical priority to address in a service business. Why? Because in those locations where both employees and customers are committed to the brand together, business is twice as good as in locations where either employees or customers are engaged, but not both. And it's 3 to 6 times higher than in those locations where neither are engaged.

> *In those locations where both employees and customers are committed to the brand together, business is twice as good as in locations where either employees or customers are engaged, but not both.*

Given these findings, and many others supporting them, it would not be surprising if shareholders and financial analysts begin investigating these factors in public companies, and investing in those businesses with strategies centered on employee and customer engagement and Enterprise loyalty.

In this regard, loyalty can no longer be thought of as a set of initiatives that the marketing department owns. To overcome the crisis of loyalty and engagement present among employees in so many companies, the entire company must take responsibility for earning the trust and admiration of both employees and customers. True customer loyalty in a services firm depends entirely on the quality of the customer's engagement with employees. Trying to gain the former without work on the latter is self-defeating. There's an adage in business: "The quickest way to kill a lousy brand is to advertise it." True loyalty emerges from the inside out, as an "attractive reaction" to the customer's value perception of your brand.

Enterprise Loyalty, therefore, embraces a concept of the business as a high-performance, integrated whole, centered on creating customer value and dedicated to winning the loyalty of all key stakeholders.

Including shareholders. +

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