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The Financial Impact of Satisfying Wireless Customers

A Special Report by
J.D. Power and Associates
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In June of 2010, the wireless penetration rate in the United States was 93%, representing an increase of 174% during the past 10 years, according to J.D. Power and Associates wireless industry data. While the overall penetration rate may be slowing, carrier market shares are in a constant state of flux. To maintain subscriber growth and positive financial performance in the midst of this competitive tug of war, wireless carriers must continue to meet and exceed their customers' evolving expectations and provide a satisfying and rewarding experience.

Most industry executives acknowledge the value of having a highly satisfied subscriber base, but not all have embraced measuring this intangible tenet with the same vigor. Those executives who are less inclined to dedicate adequate resources to customer experience or loyalty programs question their short-term shareholder value. However, there are quantifiable links between customer satisfaction and profit, and, in fact, customer satisfaction may be used as a mechanism to drive profitability. While customer satisfaction impacts each wireless carrier differently, the most notable benefits are increases in customer recommendations; service and device upgrades; and premium plan package subscriptions, as well as lower operating costs and increased frequency of sale transactions. J.D. Power and Associates' research findings also show that there are positive returns on investment (ROI) for providing a highly satisfying wireless customer experience, and that these payoffs most often occur in the short term.

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In their search for a leading indicator to gauge the success of their most recent marketing and customer care initiatives, some wireless carriers have narrowly focused on the importance of measuring customer advocacy using metrics such as net promoter score (NPS) as their bellwether. While a valuable tool, measuring advocacy alone is not sufficient, and is perhaps an oversimplification.

Wireless carriers must understand which actions to take to develop advocacy. To gain more insight into the customer experience and develop successful, enduring service and marketing action plans, J.D. Power recommends a holistic approach of measuring customer satisfaction that includes loyalty metrics, key performance diagnostics, and competitive strengths—all of which will serve as more comprehensive, if not leading indicators of profitability.

The objective of this special report is to illustrate how wireless carriers may use Voice of the Customer metrics to assess and eventually create predictive financial and operational performance models. In addition, this report provides examples of the financial impact of enhanced focus on customer satisfaction and the customer experience. Although rankings in J.D. Power's wireless industry studies vary from year to year, one fact remains constant: the highest-ranking carrier provides its customers with a top-quality network for calling (and, more recently, texting and Web surfing); competitive pricing; and highly knowledgeable, courteous, and helpful customer service and sales representatives. More importantly, the highest-ranking carriers also typically achieve high financial performance.

To examine the financial impact of satisfying wireless customers, J.D. Power conducted analyses using financial metrics and data from its wireless studies. Provider-level satisfaction and loyalty metrics were compiled by quarter from 2008 to 2010 and merged with publicly available provider-level financial metrics such as net subscriber additions (i.e., the number of new customers minus the number of lost customers) and operating revenue. The relationship between wireless service provider customer satisfaction and financial performance was examined at point in time and at various time lags (e.g., 2009 first-quarter satisfaction in relation to 2009 second-quarter financial metrics). To control for potential seasonality impacts and to boost the sample size, the data were stacked at the various time lags. For example, 2009 first-quarter satisfaction data were aligned with 2009 second-quarter financial data, and 2009 second-quarter satisfaction data were aligned with 2009 third-quarter financial data.

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Impact of Wireless Customer Satisfaction on the Bottom Line

Overall, the analyses showed a positive relationship between provider-level satisfaction and subsequent financial outcomes. That is, the overall customer satisfaction index score was positively related to net subscriber additions and operating revenue one quarter later. This relationship held across increased time lags (i.e. two-, three-, and four-quarter lags), but was strongest after one quarter.

To graphically illustrate the impact of customer satisfaction on financial metrics, data were grouped into three categories based on overall provider satisfaction and examined in relation to financial outcomes. (Figure 1) These categories segmented customers with low satisfaction (scores lower than 695 on a 1,000-point scale), moderate satisfaction (scores of 695-719 points), and high satisfaction scores (scores of 720 and higher). The mean satisfaction score among the low satisfaction group was 674, while in the moderate and high satisfaction groups they were 707 and 729, respectively. On the surface, the differences among these three groups may seem nominal, yet the differences are statistically significant, leading to dramatic differences in financial performance. Taken at face value, some wireless carriers may shrug off a gap in satisfaction between their company and the highest-performing competitor. However, the drivers of these scores can have far-reaching consequences.

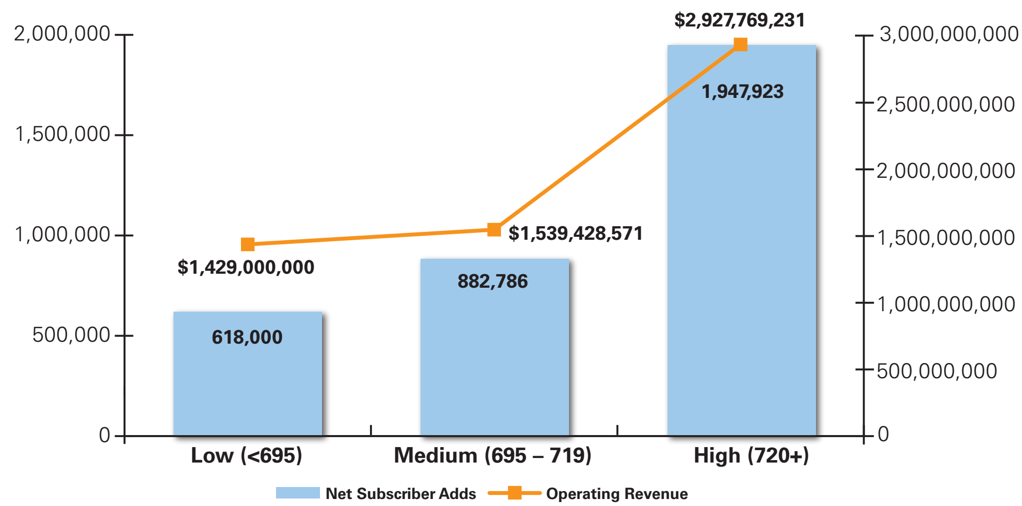
In the low satisfaction group, the subscriber base is still growing—on average, this group nets 618,000 subscriber additions one quarter later. Further, carriers included in this satisfaction group average $1.4B in operating revenue per quarter. While positive, these figures are still well below those of the moderate satisfaction group. The average net addition for this group is 882,786 new subscribers per quarter, which is nearly 265,000 more than for carriers in the low satisfaction group. Operating income is also higher in the moderate satisfaction group (more than $1.5B, on average), and carriers in this group average $9 more in quarterly income per subscriber than carriers in the low satisfaction group.

However, financial indicator metrics are significantly more positive among carriers in the high satisfaction group. Average operating income exceeds $2.9B per quarter, which is more than double that of the low satisfaction group. Further, the average number of net subscriber additions (more than 1.9M per quarter) is also more than three times as high as the low satisfaction group.

It does not pay to be average. While only 22 index points separate mean satisfaction scores of the high and moderate satisfaction groups, the differences in carrier financials are quite dramatic. Carriers that truly satisfy their customers achieve double the number of subscribers gained per quarter, compared with those carriers that simply meet expectations. These carriers also achieve double the operating income, and the average revenue per subscriber is $12 more than among those carriers that are in the moderate satisfaction group.

Financial Outcomes by Subscriber Group

(Net Subcriber Additions vs. Average Operating Income)



Source: J.D. Power and Associates 2008 – 2010 Wireless Customer Satisfaction Study[SM] **Figure 1**

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Customer Satisfaction Index as a Predictor

The Customer Satisfaction Index score is an effective predictor of average revenue per subscriber. There is a strong correlation between the CSI index score achieved in J.D. Power's wireless studies and average revenue per subscriber (ARPU) the following quarter. To further illustrate, in Q2 of 2010, Verizon Wireless ranked highest in customer satisfaction among the largest wireless carriers with an index score of 739. The following quarter, Verizon Wireless reported an operating income of more than $4.8B, which equated to $52 per subscriber and several dollars more per subscriber than any other competitor.

While there are certainly numerous other factors contributing to subscriber additions and losses, existing customers can serve both as proponents and detractors of the brand.

Word of mouth is actually effective in garnering market share and valued customers, and brand advocates serve as uncompensated marketing representatives. J.D. Power finds a strong correlation between a customer's propensity to recommend their wireless carrier and increases in actual subscribers the following quarter. While Sprint has struggled with regard to subscriber churn, the carrier's recommendation propensity rate increased by more than 5% from Q4 of 2009 to Q2 of 2010. This coincided with Sprint's first net subscriber gain in several quarters.

Value of Satisfying Customers

To recognize the macro-level financial benefits of satisfying wireless customers, it is critical for carriers to understand the value of satisfying the individual. J.D. Power notes the following from recent industry data:

- Nearly three-fourths (72%) of customers who rate their wireless experience 8, 9, or 10 on a 10-point scale indicate they "definitely will" or "probably will" purchase additional products and services from their carrier within the next 6 months, compared with just 48% among customers who rate their carrier 7 or below. Furthermore, customers who rate their carrier a 10 are three times more likely to indicate they "definitely will" purchase new products, compared with those who rate their carrier 8. (Figure 2) Similarly, customers who rate their carrier 10 are nearly 40% more likely than those who rate their carrier 8 to currently subscribe to plan upgrades, such as extended device warranties and insurance programs.
- In response to the economic downturn, customers who are less satisfied with their carrier (ratings of 1-7) are 36% more likely to have downgraded their wireless services, compared with customers who are more satisfied (ratings of 8-10).
- Satisfying existing customers translates to fewer resources needing to be allocated to retention programs. Just 6% of customers who rate their carrier 8, 9, or 10 are likely to switch to another service provider in the next 12 months, compared to 22% among those rating their carrier 7 or below. Further, customers who provide their carrier a rating of 8, 9, or 10 recommend that carrier nearly three times as often, leading to a significantly higher number of added subscribers. Again, notable differences exist between switching intention rates even among those who are considered satisfied customers: those rating their carrier 10 are half as likely to say they "definitely will" or "probably will" switch their carrier within the next 12 months, compared with customers who rate their carrier 8 (4% vs. 8%, respectively).

Wireless Carrier Satisfaction by Rating

Satisfaction with Wireless Carrier	1-7	8, 9, or 10	10
% "Definitely Will" or "Probably Will" Purchase Additional Products within Next 6 Months	48%	72%	79%
% Downgraded Service in Past Year	15%	11%	11%
% "Definitely Will" or "Probably Will" Switch Carriers	22%	6%	3%

Source: J.D. Power and Associates 2010 Wireless Customer Satisfaction Study[SM] **Figure 2**

- In 2009, J.D. Power reported that customers who were dissatisfied with their carrier's network quality and switched service as a result spent an average of $5 more per month with their new carrier, suggesting customers will pay a premium for an exceptional network. This equals an average of $60 in additional annual revenue per subscriber.
- Providing a satisfying sales experience is also reflected in financial performance. According to the *J.D. Power and Associates 2010 Retail Sales Satisfaction Study*SM*—Vol. 2*, customers whose sales experience exceeded their expectations spent an average of $6 more per month than the industry average on their wireless service. Effectively pairing customers with well-trained, enthusiastic sales representatives and offering current devices and plans that meet customers' needs not only results in a positive financial return at the point of transaction, but also may mean increased revenue in the months following.

While industry analysts and the media seem to focus mainly on exclusive device offerings as the primary contributor to revenue growth, it is clear that financial performance is a function of much more than promotions and the next "hot" product. Solid revenue growth is predicated upon ongoing marketing and service processes that focus on the overall wireless experience in price, product, and people. Plan and device upgrades will come organically when carriers are focused on—and succeed in delivering—high-quality network performance, value for the price paid, and rewarding customer care and sales interactions.

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In the fast-paced wireless environment, which is driven by exponential improvements in technology and increased reliance on product innovation, customer satisfaction remains paramount. Customers' expectations of their service provider are constantly being elevated, and carriers must adapt accordingly to this rising bar and to increased customer dependence on their products. However, wireless customers have grown less forgiving, as the rate of switching intent increased by 47% between 2007 and 2010 among customers experiencing just 5 to 9 problems per 100 calls.

To adapt to industry changes and to continue providing shareholder value, J.D. Power and Associates recommends the following actions.

- **Implement post-transactional and post-plan and device upgrade tracking programs.** J.D. Power 2010 study findings show that sales transactions and customer service experiences of smartphone customers may actually be more satisfying than those of feature phone customers, despite significantly more time required for this group of customers. Moreover, it is crucial that carriers ensure that customer needs are still being met in the days and weeks following a plan or device upgrade, as new technology may pose new challenges to some of them. Offering device operation and optimization training and soliciting feedback in the weeks following an upgrade may serve as ways to instill consumer confidence in their wireless investment, reduce customer service inquiries, and foster long-term customer loyalty.
- **Provide a distinct, consistent value to customers.** This is the common denominator among the highest-ranking carriers in J.D. Power and Associates' wireless studies over time. Value is not purely a function of providing service at low cost—value can be recognized in the price, product, or people with whom the customer interacts. Wireless customers may be willing to pay a premium for an outstanding network when they recognize the value in it. However, identifying competitive strengths and redefining or reinforcing the value proposition are unending endeavors. More importantly, understanding what drives value and satisfaction in the subscriber base will lay the foundation for improved lifetime customer value and advocacy.

- **Provide a satisfying total ownership experience.** J.D. Power and Associates has identified quantifiable links between loyalty, brand advocacy, and customer satisfaction, which clearly impact financial performance. A satisfying total ownership experience is paramount, as it leads to the creation of sustainable revenue and brand advocacy. This measurable ROI further reinforces the need to create and maintain a culture in which satisfying each customer is held in utmost importance, given the impact total ownership experience has on the bottom line.

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