MANAGEMENT COMPETENCIES FOR SUCCESSFUL CUSTOMER RETENTION

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Abstract

Customer retention has been a hot topic since the mid-1990s, but little research has been conducted into the management competencies that are associated with outstanding customer retention performance. We address that shortcoming. Our research investigates the associations between excellent customer retention and a number of management structures and processes, including customer retention planning, budgeting, and accountability, insight into customer reasons for defection, the search for advance indicators of customer switching intention and the presence of a documented complaints handling process. We find that excellence at customer retention is positively and significantly associated with the presence of a documented complaints-handling process and confidence that the company understands the reasons that customers switch.

Keywords: CRM, customer retention, ISO10018, complaints management, planning
**Introduction**

Peter Drucker (1973) wrote that the sole purpose of a business is to create a customer. In recent years, there has been increasing recognition that creating a customer is not enough. Keeping the customer has become regarded as equally, if not more important, since Dawkins and Reichheld (1990) found that a 5% increase in customer retention generated an increase in customer net present value of between 25% and 95% across a wide range of business environments. This finding generated a huge amount of interest and activity in academic and business communities, as researchers and consultants attempted to verify these claims and to identify a set of management practices that would enhance the prospects of successful customer retention. There was a growing recognition that customers, like products, have a life-cycle that companies can attempt to manage. Customers are acquired, retained and can be grown in value over time. They climb a value staircase (Gordon, 1996) or value ladder (Christopher, Payne and Ballantyne, 1991) from suspect, prospect and first-time customer, to majority customer and ultimately to partner or advocate status. Recently, Gupta et al (2004) have justified companies’ focus on customer retention by pointing to the connections between customer value and shareholder value. They found that a 1% increase in customer retention had almost 5 times more impact on firm value than a 1% change in discount rate or cost of capital.

The mainstream marketing literature focuses on processes for customer management, such as market segmentation, targeting and positioning, but offers very little on specific managerial competencies for customer retention (DeSouza 1992). We are interested in the question of whether there are, indeed, specific competences that enable companies to excel at customer retention.

Practically every marketing management scholar makes the claim, often without justification, that it makes good sense to plan for the achievement of business outcomes. Kotler (2003), for example, writes that ‘successful companies… practice the art of market-oriented strategic planning’, with the clear implication that failure can be traced to artlessness in planning disciplines. Plans are developed and implemented to achieve specific, measurable objectives; results are measured and corrective action is taken if there is unacceptable variance. There is almost universal agreement throughout the modernist literature that establishing measurable
key performance indicators, creating a budgeted plan and assigning responsibility for their
achievement, are norms of good management practice that enable companies to achieve their
objectives. Indeed, research generally supports the idea that formal planning processes are
associated with better business performance (Miller & Cardinal 1994). Yet, does this also
apply to customer retention? Our aim in this research has been to identify managerial
competences that are associated with excellent customer retention.

**Literature review**

Customer management theory, or marketing as we now know it, emerged on the back of large-
scale industrial development and mass production, and became widely associated with the 4Ps
framework and a transactional, rather than relational, model of customer engagement. There
was no thoughtful consideration of a role for customer retention. However, from the 1980’s,
researchers began to question the relevance of this one-size-fits-all approach to industrial
(Håkansson, 1982; Ford, 1997) and service markets (Berry, 1983; Grönroos, 1990). In these
contexts, customer management became more clearly identified with relational practices.
Business-to-business relationships were found to be relatively stable and enduring, and to
exhibit adaptation to the other party’s requirements. Adaptations act as structural bonds, and
serve as investments in a relationship, which may or may not be recovered when a relationship
breaks down. In many service environments there is face-to-face interaction between service
providers and customers from which social bonds may develop. Clearly a relational perspective
fits well within these contexts, where there is an opportunity, if not imperative, to promote
longer customer tenure, and gain the associated economic benefits.

There has been recent debate over whether the relational approach found in services and
industrial markets can be transferred into consumer markets where a transactional approach is
the norm (O’Malley & Tynan, 2000; East & Hammond, 2000). In these markets there appear to
be fewer opportunities for social and structural bonding.
Whatever the context, customer retention strategies aim to increase customer tenure. As tenure lengthens, it is claimed that purchase volumes rise, customer management costs fall and customer referrals increase. In addition, some customers may be willing to pay a price premium (Reichheld 1996b). These causes generate the effect of an increase in customer net present value. Given the importance that has become attached to customer relationship management, unsurprisingly researchers have begun to focus on customer retention. In recent years, customer retention researchers and commentators have focused on a number of important questions, including the following:

1. What is meant by customer retention and how can it be measured? (Aspinall *et al*, 2001)
2. Which customers should be the focus of customer retention efforts? (Koch, 1998; Ganesh *et al*, 2000; Buttle, 2004)
3. Why do customers switch or defect, taking all or some significant part of their business to competitors? (Keaveney, 1995; Reichheld, 1996a; Yeung *et al*, 2002)
4. How should a customer retention plan be constructed? (DeSouza, 1992)
5. How can companies develop stronger customer attachment? (Moorman, Zaltman and Deshpandé 1992; Oliver, 1999; Hofmeyr & Rice, 2000)
6. What is the role of relationship marketing instruments such as loyalty programs and customer clubs on customer retention? (O’Brien & Jones, 1995; Dowling and Uncles 1995; Stauss *et al*., 2001; Verhoef, 2003)
8. What are the effects of complaints handling on customer retention outcomes? (Johnston 2001)

In general, this research supports the idea that companies can benefit from managing customer churn proactively. This involves putting in place contextually-varied plans and strategies to identify significant potential defectors, building exit barriers and winning back customers who
are at risk, or who have already taken all, or some significant part, of their business elsewhere. Weinstein (2002) has observed that ‘80% or more of marketing budgets are often earmarked for getting new business….. a preferable approach may be to invest at least 75% … on relationship marketing activities and customer retention strategies… developing a sound and profitable customer retention strategy must be a top priority.’

What is not clear from this body of research is the relative significance of management competencies such as planning, budgeting and accountability in promoting successful customer retention. In addition to these issues, we also decided to investigate the role of complaints management in customer retention. There are two reasons for this. First, researchers have found that well-executed complaints-handling can prevent customers from switching (Fornell and Wernerfelt, 1987). Indeed, customers who complain and are well recovered can be more satisfied, and much less likely to switch than customers who had no cause for complaint at all (TARP, 1979; Nyer, 2000). Complainants who are exposed to high standards of complaints handling experience the service quality attributes of empathy and responsiveness. These attributes are not routinely on display when services are delivered or products function right first time (Buttle, 2004).

Our second reason for investigating complaints handling is the recent creation of complaints-handling standards. The International Organization for Standardization (ISO) has developed a new international standard intended to guide the design and implementation of an effective complaints handling process. Known as ISO 10018, it is expected that the standard will be rolled out in 2004. The standard claims that a major benefit from excellent complaints handling is maintained or enhanced customer loyalty (ISO, 2003). It is drafted to be compatible with the quality management system, ISO 9000, although it is also expected to be used independently of ISO 9000.
Research questions

Our main goal in conducting this research was to identify important organizational competencies associated with successful customer retention. We wanted to be able to identify the practices or conditions that enable companies to achieve their customer retention objectives. From the literature summarized above we derived the following hypotheses:

H1: Companies that excel at customer retention have an explicit, documented customer retention plan

H2: Companies that excel at customer retention have budget dedicated to customer retention activities

H3: Companies that excel at customer retention have nominated a particular person or group to be responsible for customer retention

H4: Companies that excel at customer retention are confident that they understand why they lose customers to competitors

H5: Companies that excel at customer retention look for clues or signals which indicate customers might be likely to take some, or all, of their business elsewhere in the future

H6: Companies that excel at customer retention have a documented process for handling customer complaints

Methodology

Our methodology involved gathering data by mail-administered survey of a stratified random sample of companies. Details of the sampling strategy, data collection methods, instrument development and analysis follow.
**Sampling.** Our population of interest was Australian industry, across the full range of primary, secondary (manufacturing) and tertiary (service) sectors. A stratified random sample of 732 companies was selected from the Dun and Bradstreet database of the top 1000 companies in Australia. The population was stratified into 3 annual turnover groups: $50 to $99 million, $100 to $500 million, and above $500 million.

**Data collection.** A mail questionnaire was developed. Following an initial telephone solicitation to participate, the instrument was mailed to the sample. Follow-up calls and reminders were issued after one month. The invitation to participate was addressed to the person in charge of customer relations, customized by name where this was known. We encouraged response by offering a summary report of the study. This has now been distributed to respondents.

**Instrument.** Items in the instrument were developed from the literature review, and piloted and refined over several versions of the questionnaire. The majority of the questions measuring the independent variables were nominal in nature, and required ‘yes’, ‘no’, or ‘don’t know’ responses. These questions investigated the presence or absence of a range of customer retention management practices, objectives and tactics. As is clear in the hypotheses, we wanted to identify management practices associated with ‘excelling at customer retention’. In the questionnaire excellence at customer retention was operationalized thus: ‘In the last 12 months, to what extent has the number of customers retained by your company met your expectations?’ This variable was measured on a 7-point metric scale, anchored at three points. The point 1 anchor read ‘greatly under-performed expectations’, the mid point (point 4) read ‘met expectations’ and the point 7 anchor was ‘greatly exceeded expectations’. When a company reported that their expectations had been exceeded (scale points 5-7), this was recoded as ‘excellent at customer retention’.

**Analysis.** Data were analyzed using procedures within SPSS_PC version 10. Two basic forms of analysis were carried performed. First, simple descriptive uni-variate statistics were
computed for the measured variables; second bi-variate correlations were performed to test the hypotheses.

To enable non-parametric bi-variate correlations to be performed all data were transformed into ordinal form according to procedures recommended by Siegal and Castellan (1989). The metric data were recoded as follows: all responses above the midpoint (i.e., 5-7) were recoded to ‘1’. Those below, including the midpoint (i.e., 4-1), were recoded to ‘2’. Non-parametric (Kendall’s tau) correlations were computed\(^1\). If Kendall’s tau revealed a significant correlation between any customer retention practices, objectives or tactics and the dependent variable, Chi-square tests also conducted to confirm the association.

**Results**

**Response rate.** One hundred and seventy responses were obtained, representing a 23% response rate. Forty-three had annual turnover between $50-$99 million, forty-six were between $100-$500 million, and forty-two were above $500 million. Thirty-nine companies declined to divulge their annual turnover. Participants represented all major standard industrial classification (SIC) codes. Dominant sectors were manufacturing (43 companies); wholesale and retail (24); and health, community services, accommodation, cultural/recreation, personal and other services (23).

Before discussing the hypotheses we summarize briefly the state of customer retention across the sample.

**Descriptive results.**

Australian companies are generally not very advanced in customer retention management. Only 39% have an explicit, documented, customer retention plan, and even fewer (28%) have a

\(^1\) It should be noted, that even though the dependent variable was measured on an interval scale (1-7), non-parametric procedures were used in these analyses because the assumptions of homogeneity and normality were violated (significant Levene statistics, and small sample size), when attempting to use parametric tests like Anova.
specific budget dedicated to customer retention activities. However, 70% claim to have a nominated person or group in charge of customer retention.

Of the companies that have a retention plan (only 39% of our sample), very few think in terms of customer profitability when setting retention objectives. The customer retention objectives of companies with plans, in order of frequency are:

- 74% - revenues to be earned from retained customers
- 68% - retention of specific customer segments
- 59% - retention of specific named customers
- 55% - margins to be earned from retained customers
- 50% - numbers of current customers to be retained

Sixty-seven percent of respondents are confident (scale points 4-7) that they understand the reasons customers take their business elsewhere. Indeed, 85% look for clues or advance warnings that their customers are about to switch, and 19% use formal models (for example, ‘propensity to switch’ models) to predict defection. The most common indicator of likelihood to switch is the receipt of a customer complaint. Seventy-nine percent of companies that looked for advance warnings cited customer complaints as an important indicator.

A large proportion of Australian companies also do not segment their customer base when implementing retention strategies. Forty-one percent of respondents chose ‘we don’t want to lose any of our customers’ over the alternative answer ‘we focus our retention efforts on particular customers’.

Finally, in terms of handling complaints, 79% of Australian companies have a documented complaint handling process, of whom 74% believe it is effective. A total of 55% of companies reported that they had exceeded their customer retention expectations in the previous 12 months.
We now turn to our analysis of the hypothesized relationships. What are the managerial competences that are associated with excellent customer retention?

**Bi-variate correlations.** Kendall’s tau was used to measure the hypothesized relationships. Where a significant correlation was identified, chi-square tests also performed. The results are as follows (see also table 1).

**H1:** Companies that excel at customer retention have an explicit, documented customer retention plan

There is no statistically significant correlation between having a retention plan and exceeding customer retention expectations (r =0.07; p>.05). H1 is therefore rejected.

[Insert table 1 about here]

**H2:** Companies that excel at customer retention have a budget dedicated to customer retention activities

There is a positive but statistically insignificant correlation of r =.24 (p >.05) between having a retention budget and exceeding customer retention expectations. H2 is therefore rejected.

**H3:** Companies that excel at customer retention have nominated a particular person or group to be responsible for customer retention.

Table 1 shows a negative, but insignificant, correlation of r = -0.1 (p>.05) between having a nominated person or group responsible for retention and exceeding retention expectations. H3 is therefore rejected.

**H4:** Companies that excel at customer retention are confident that they understand why they lose customers to competitors
There is a positive and statistically significant correlation between retention expectations being exceeded and the company’s confidence that it understands why customer defect (r = .20, p < .05; $\chi^2 = 6.1; p < 0.01$). H4 is therefore supported.

H5: Companies that excel at customer retention look for clues or signals which indicate customers might be likely to take some, or all, of their business elsewhere in the future. This hypothesis is not supported. Companies that look for early cues or signals that their customers might defect are no better at customer retention than companies that do not (r = .13; p > .05). Similarly, there is no statistically significant relationship between use of mathematical models (e.g., a ‘propensity to switch’ models) and exceeding customer retention expectations (r = .01; p > .05).

H6: Companies that excel at customer retention have a documented process for handling customer complaints.

There is a strong positive relationship between exceeding retention expectations and the presence of a documented complaints handling process. H6 is therefore supported. Indeed, this is the strongest of all the associations investigated (r = .28, p < .00; $\chi^2 = 12.3; p < 0.00$).

Discussion

Of the six hypotheses tested, four were rejected. We found no statistically significant relationship between the standard management practices of formal planning, budgeting and accountability and customer retention performance. This result flies in the face of conventional management wisdom that in order to achieve desired business outcomes it is necessary to build a plan, provide a budget and ensure accountability. We found no support for such a claim. Perhaps the reason that the association is not verified is that it is the quality of the plan and its execution that makes the difference, not accountability or budget per se. Neither did we find any support for the hypothesis that companies excelling at customer retention monitor their customer base for early indications of intentions to defect.
However, we did find strong support for 2 hypotheses – H4 and H6. Our evidence suggests that companies that excel at customer retention are confident that understand why they lose customers to competitors, and have a documented process for managing customer complaints. These findings turn out to have important managerial significance.

We are not surprised that insight into the reasons for customer defections is associated with excellent customer retention. If companies understand the reasons behind customer churn they are better placed to identify root causes and fix the problems. A number of authors (Keaveney 1995; Hart et al, 1990) have suggested that it is important for companies to conduct research into the reasons for customer defection and create appropriate managerial responses.

For our second finding, we also established a clear link between having a well-documented complaints management process and excellent customer retention. Other academic research (Johnston, 2001) has also identified a strong association between an organization’s complaints handling prowess and improvements in three outcomes: customer retention, employee performance and process improvement. These three outcomes are in turn highly correlated with overall financial performance. Companies that capture customer complaints and handle them well enjoy two benefits. First, they are better placed to resolve the particular complainant’s problem and retain that customer’s future value. Second, they can begin to identify problems that are repetitive and therefore can develop solutions to those problems. As noted in the documentation supporting ISO 10018 (ISO, 2003) excellent complaint-handling processes ‘enhance the ability of an organization to identify trends and eliminate root causes of complaints, and improve an organization’s operations.’

Further exploration within our data set has revealed significant associations between having a documented complaints-handling process and other variables investigated in this study (figure 1). We found that companies that have a documented complaints-handling process are more likely to:

1. have an explicit customer retention plan (r=.20, p<0.01; $\chi^2 = 6.9; p<0.01$)
2. have a person or group in charge of customer retention ($r = .17, p < .03; \chi^2 = 5.0; p < .03$)
3. use a formal switching model to predict defection ($r = .21, p < .01; \chi^2 = 7.0; p < .01$).

Interestingly, none of these three variables has a direct, statistically significant, association with the ultimate dependent variable - exceeding customer retention expectations. This is clear evidence of the importance of the role of complaint handling in facilitating customer retention. In other words, having a retention plan, designated officer and budget are in and of themselves not sufficient to drive up customer retention performance. What is needed is a complaints handling process.

Further exploration shows that the more effective the complaints handling process, the more confident companies are that they understand the reasons for the customer defection ($r = .34; p < .00; \chi^2 = 17.7; p < .00$). Furthermore, if a company has a simple metric in place to guide customer retention (the number of customers they want to retain) they are also more effective in handling customer complaints ($r = .40; p < .00; \chi^2 = 8.5; p < .00$).

**Conclusion**

There are three major conclusions to this study. First, the data suggest that the standard management practices of planning, budgeting and assigning accountability for customer retention are not associated with excellent customer retention performance. Our second conclusion is that excellence is strongly associated with the presence of a documented complaints-handling process. Third, we conclude that it is important to understand the reasons for customer defection.

Perhaps we should not be surprised by the importance to customer retention of having a customer complaints handling process in place. Effective complaints handling, as noted earlier, can generate two benefits. First, when a customer complains, companies are being
given a chance to fix the particular customer’s problem, and to retain the customer’s current and future business. Second, a well-designed complaints handling process allows management to collect and analyze complaints data over time, identify systemic and repetitive problems, and fix root causes, whether they be problems caused by product, people, process or something else.

In summary, the twin factors of ‘having a documented complaint handling process’ and ‘confidence in knowing the reasons for defection’ are critical to exceeding customer retention expectations. Put simply, the better the complaint handling processes and the more companies understand customers’ reasons for taking some or all of their business elsewhere, the greater the likelihood of retaining their business.

Managerial implications

The most important management implication from this research is to implement a documented customer complaint handling process that can identify and act upon the problems that motivate customers to take some or all of their business to competitors. This is much more important than having a budgeted customer retention plan under the control of a responsible manager. Such a process will enable companies to understand why customers defect. The more confident companies are that they understand these reasons, the more refined they can be in directing their retention efforts.

Having a documented complaints-handling process is critical to customer retention excellence. A number of published standards offer guidance on the development of a complaints-handling process. There are similar national standards in Australia (AS 4269) and the United Kingdom (CMSAS 86:2000). The former is administered by Standards Australia and the latter by British Standards Institution. However, a new international standard, ISO 10018, aims to supplant the national standards and provide companies with ‘guidance for the elements of a complaints handling process within an organization, including planning, design, operation, maintenance and improvement’ (ISO, 2003).
The ISO 10018 document outlines how handling complaints well provides benefits both to customers and to organizations. ISO 10018 is international in its scope and intended to be applicable across all contexts - large organizations and SME’s, for-profit and not-for-profit, and in both conventional and e-commerce environments. The standard is presented in 9 sections. Among the more managerially relevant sections are numbers 4, 6, 7 and 8.

- Section 4 sets out guiding criteria for effective complaints handling processes: visibility, accessibility, responsiveness, objectivity, no charges, confidentiality, customer-focus, accountability and continual improvement.
- Section 6 provides guidance on the planning and design of the processes: setting objectives, establishing processes and providing adequate resources.
- Section 7 covers operational issues: communicating the process to customers, complaint reception and tracking processes, assessment and investigation, response approaches and closure.
- Section 8 advises on the importance of assessment and improvement of the processes by measuring, analyzing and auditing various parts of the total process and presenting the results for management review.

If the complaints handling process is effective then companies can be more confident that they understand the reasons for customer switching. ISO 10018, like the other national standards, suggests that companies should monitor the influence of complaints handling on customer satisfaction levels and future buying behavior. Customer feedback on their experience of the complaints handling process is critical to its improvement over time.

This research shows that the more commonplace managerial concerns with having a plan that is budgeted, and a responsible individual or group, are inconsequential alongside the clearly identified significance of effective complaints handling.
Limitations and future research

There are two notable limitations to this study. First, it was conducted in a single geographic region, and the results therefore may not transfer into a different geography. Secondly, it employs self-reports from executives charged with responsibility for managing customer relationships. We have not objectively corroborated their self reports. These limitations apply to much published academic research.

Given the significance that this research attaches to the customer complaints handling process, there is potential for future research into the effectiveness of ISO 10018, when it is rolled out. An important research question is the following. Do companies that have a complaint handling process that is standards-based (i.e. aligned with ISO 10018) achieve better customer retention outcomes than companies that either have no complaints-handling process or a process that is not based upon an acknowledged standard? At this time, although the ISO 10018 standard is to be integrated into the ISO 9000 family of standards, it is not clear whether there is to be a formal accreditation process. In the UK, there is an accreditation process against the CMSAS 86:2000 standard, whereas in Australia there is no formal requirement that companies be accredited against the AS 4269 standard. However, AS 4269 is mandated for all public sector agencies under federal regulation. This research would require the development of an audit tool to measure compliance with the standard. If the answer to the research question were ‘no’, this would call into question the integrity and value of the proposed standard.

Our finding that a budgeted customer retention plan managed by a nominated executive is not associated with excellent customer retention performance deserves further examination. This is a counter-intuitive result that is at odds with other academic research that confirms the value of well planned and implemented strategy. We propose a more qualitative investigation that examines the composition and implementation of customer retention plans across a wide variety of contexts. The goal would be to identify structural and/or process attributes in retention plans that are more strongly associated with excellent retention outcomes.


Figure 1: Statistical associations with ‘exceeding expectations of retaining customers.’
(statistics are Kendall’s tau)
<table>
<thead>
<tr>
<th></th>
<th>Exceeding retention expectations</th>
<th>Documented complaint process</th>
<th>Have a person/group in charge of retention</th>
<th>Use formal models</th>
<th>Confident know why customers defect</th>
<th>Effectiveness of complaint process</th>
<th>Number of customers to retain</th>
<th>Look for clues/signals of defection</th>
<th>Have budget for retention activities</th>
</tr>
</thead>
<tbody>
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<td>Exceeding retention expectations</td>
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<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>Documented complaint process</td>
<td>.28**</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Have a person/group in charge of retention</td>
<td>.07</td>
<td>.20*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use formal models</td>
<td>0.10</td>
<td>.21*</td>
<td>.22*</td>
<td>.17*</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Confident know why customers defect</td>
<td>.20*</td>
<td>.12</td>
<td>.14</td>
<td>.08</td>
<td>.02</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Effectiveness of customer complaint process</td>
<td>.17</td>
<td>N/A</td>
<td>-.02</td>
<td>-.03</td>
<td>-.02</td>
<td>.34**</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Number of customers to retain</td>
<td>.08</td>
<td>-.14</td>
<td>N/A</td>
<td>-.09</td>
<td>-.02</td>
<td>.06</td>
<td>.40**</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Look for clues/signals of defection</td>
<td>.13</td>
<td>.10</td>
<td>.02</td>
<td>.20*</td>
<td>.07</td>
<td>.12</td>
<td>.09</td>
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<td>1</td>
</tr>
<tr>
<td>Have budget for retention activities</td>
<td>.24</td>
<td>-.19</td>
<td>N/A</td>
<td>.02</td>
<td>.05</td>
<td>-.01</td>
<td>-.06</td>
<td>.07</td>
<td>.08</td>
</tr>
</tbody>
</table>

** Correlation is significant at the .01 level (2 tailed)
* Correlation is significant at the .05 level (2 tailed)

Table 1: Correlations matrix