

Is it worth it? ROI on CRM

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Abstract

There are reports of grave disquiet about the performance of CRM systems. Vendors and consultants are accused of overselling the benefits of CRM. Clients are accused of buying naively without formulating clear performance expectations. Client satisfaction is undoubtedly low and there is a growing demand for more precise measurement of CRM's impacts. This paper reviews the evidence of client dissatisfaction, and explains how companies can set about measuring CRM performance at three levels: Strategic, Operational and Analytical.

Introduction

This paper addresses the topical issue of CRM performance.

Brewton (2000) reports that between 70% and 90% of CRM implementations have failed, and that 'there is a growing view among organisations adopting CRM that their projects are not delivering the hoped-for value' (Forsyth 2001a). Another report claims 55% have failed. One in five CRM implementations are thought to have actually damaged customer relationships (Bain and Co 2001).

An Internet survey of some 2200 CRM clients (CRMGuru.com 2001), including many who have installed GoldMine, Onyx, Oracle, PeopleSoft, Pivotal, SalesLogix, SAP and Siebel Systems products, concluded that customer satisfaction with the CRM product was 'very low indeed' (Forsyth 2001c). The average customer satisfaction index score across all vendors was 63.1 out of 100, lower than reported in studies of other comparable IT sectors. The survey measured 5 attributes – ease of implementation, customer focus, price satisfaction, support and functionality. Ease of implementation scored lowest, at 55, whereas functionality scored highest, at 68, across all vendors. Siebel, the market leader, ranked fifth. It scored relatively highly on functionality and support, and poorly on pricing, implementation and customer focus. A key finding was that clients do not want 'out-of-the-box functionality', but adaptation to their own requirements.

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It is particularly larger companies that have experienced these CRM problems since they have already moved down the CRM road, but it does appear that mid-sized and smaller organisations are following. Only 40% of mid-sized businesses currently have CRM initiatives underway (Peppers and Rogers Group, 2001a). There is considerable potential for the CRM market to grow, since, according to Cap Gemini Ernst and Young (2001) “67% of European companies and 74% of US companies had undertaken a CRM initiative in the [previous] two years”. Bayer (2002) notes research from Forrester, that 45% of companies are presently considering CRM projects whilst only 37% have a project underway.

Despite the apparent dissatisfaction of clients with CRM performance, CRM investments still are rising. The CGEY (2001) survey reported that “most [companies] expect a considerable growth in their CRM budgets over the coming year or so.” An IDC/Cap Gemini report (1999) reports that one third of US corporations surveyed were planning a CRM spend of at least \$5 million. Only 7% of respondents were anticipating spending less than half a million.

International Data Corporation claim that CRM investments are growing at 25% compound per annum, and that world revenues will lift from \$61 billion in 2001 to \$148 billion in 2005 (Helms 2001). AMR Research estimated more conservatively that revenues would reach \$75 billion by 2005 (Anon 2002).

The Hewson Group is predicting a 15% growth in the European market for CRM products compared to 9% for the USA market in 2002 (ECCS, 2001).

It is expected that the UK market for CRM product will reach £6 billion by 2005 (Forsyth 2001a).

At a recent conference Tom Siebel, the founder of Siebel Systems, the CRM market leader with a share estimated at 30%, was challenged to provide evidence that CRM actually benefited clients. Worryingly, he failed to provide support for his product (Forsyth 2001a). Yet, simultaneously, Oracle had been running an advertising campaign promising CRM in 90 days, and salesforce.com’s promised a 9-day CRM program!

Whilst there is client-side concern about CRM’s performance, vendors and consultancies are, perhaps unexpectedly, more bullish. A recent report from Accenture (2001) claims that 28-60% of the variance in companies’ return on sales is due to CRM performance. A PricewaterhouseCoopers study concludes that CRM strategies produced an 8% increase in sales. The same study claims that a 1% increase in sales increases shareholder value by 7%. Perhaps best known is the oft quoted claim from Reichheld (1996) that 5% improvement in customer retention can enhance profit by up to 85%.

The initial enthusiasm for CRM implementations, which was founded on the notion that it must intrinsically be good for business to manage its customer portfolio for more profit, has dissipated. ‘The market [is] moving away from evaluating software products on

functions and features, and instead [is] focussing on return on investment' (Forsyth 2001b).

Helms (2001) reports that 45% of companies have been able to compute ROI from their CRM investments in the previous year. Only one-third of companies in the CGEY (2001) survey could provide any estimate of their expected return on CRM investments. Other surveys have found that between 44% (Imhoff 2001) and 46% (Peppers and Rogers 2001b) of companies did not measure ROI of their CRM activities.

Measuring ROI

It does appear that some consultancies are beginning to recognise the importance of presenting business cases for CRM investments. Bayer (2002) quotes Gartner's report that 'the larger consultancies are presenting evidence that successful CRM initiatives are leading to enhanced profits and stock prices'. Peppers and Rogers Group also report that companies they have serviced are reporting 'solid ROI from their CRM investments'.

The formula for return on investment is simple:

$$\frac{\text{Profits} \times 100}{\text{Investment}} = \text{ROI} (\%)$$

If you invest \$1000 into a 1-year certificate of deposit, and earn interest of \$40 then your ROI is 4%, as computed below

$$\frac{40 \times 100}{1000} = \frac{4000}{1000} = 4\%$$

A simple formula for sure, but one which begs several questions in the context of CRM:

First, what counts as an investment in CRM?

Second, what counts as a return on that investment?

Third, over what time period should the return be measured?

We'll address these questions in turn, but first we need to establish just what is meant by CRM. We need to remember that we are not dealing with an idea that has a long history and has reached a consensus on boundaries and content. There is no universally acceptable definition of CRM, as the following selection shows:

CRM is about the development and maintenance of long-term mutually beneficial relationships with strategically significant customers (Buttle 2001)

CRM is a business strategy combined with technology to effectively manage the complete customer life-cycle (Smith 2001)

CRM is the establishment, development, maintenance and optimisation of long-term mutually valuable relationships between customers and organisations (CRM (UK)

2001)

A CRM system is comprised of 2 major components: a set of functions that allows the organisation to build an understanding of customer behaviour, and a second set of functions that allow us to communicate with customers, across many channels, to meet their service requirements, and to try to persuade them to behave more profitably (Forsyth 2001a)

CRM is an e-commerce application (Khanna 2001)

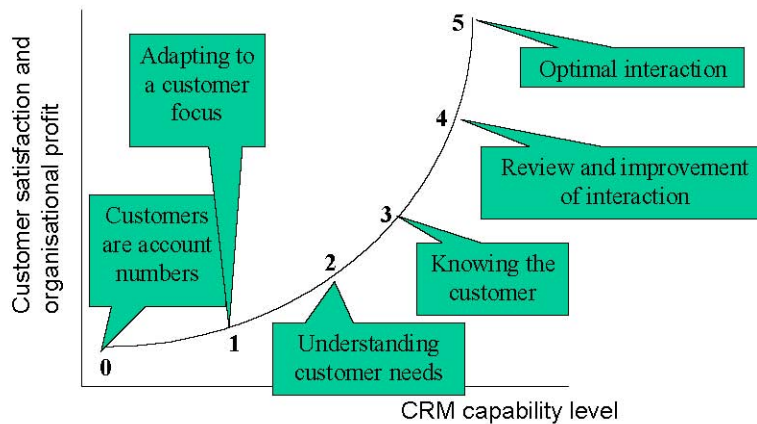
CRM aligns business processes with customer strategies to build customer loyalty and increase profits over time. (Rigby 2002)

A good CRM program enables customers to easily access the information they need at any time and includes a 24-by-7 web-site, fast email tools and the ability to discuss problems with a human being rather than an electronic answering system (Rembrandt 2002)

There is even a view that “there is no one correct definition of CRM. Moreover, the definition of CRM will evolve and change over time” (Goldenberg 2000). Some people equate CRM to loyalty schemes; others think of it as database marketing; others represent it as key account management.

Figure 1: The AIT model of the CRM life-cycle

The CRM life-cycle



Source: AIT 2001

CRM applications do indeed vary in their complexity and sophistication. Therefore, a CRM life-cycle has been proposed to describe how companies move from product-centricity to customer-centricity. AIT (2001) proposes a 6-level conceptualisation of the process. At level-0, there is no CRM solution in place. Customer data is likely to be

stored in product silos with considerable duplication. The most advanced CRM- implementations, at level-5, organisations can make real-times changes to the way they interact with customers based on the knowledge they have of their customer base, the market and the environment. This is a true multi-channel organisation with integrated customer database, analytical expertise, mapped business processes, and customised value propositions. Figure 1 shows the AIT model.

CRM is also debated at three levels of abstraction as shown in table 1. These 3 perspectives on CRM - strategic, operational and analytical – represent different levels of management exposure to the implementation of CRM initiatives. The strategic level of exposure represents board-level concern with CRM, whereas the analytical level represents the exposure of those levels that have to understand and exploit the customer database.

Form of CRM	Dominant characteristic
Strategic	A perspective of CRM which takes a principled position, either for or against, as a matter of strategy, e.g. CRM must be a good thing because it will help us become more customer-centric
Operational	A perspective on CRM which focuses on major projects such as call centre integration, sales force automation or marketing automation
Analytical	A perspective on CRM which focuses on the intelligent mining of customer data for strategic or tactical purposes

Table 1: 3 perspectives on CRM

What counts as an investment in CRM

If CRM is the IT-enabled management of a company’s portfolio of customers with a view to generating optimal long-term value for customer and company (another definition!), then the task of identifying investments becomes easier. Companies adopting the CRM way of doing business are likely to incur costs in a number of areas. Some of these may be capital costs; some may be expensed. They largely fall into 3 major categories:

IT costs

People costs
Process costs

IT costs include investments in IT infrastructure, database development, and software. According to Reed (2001b) IT investments represent only one-fifth of the total cost of the typical CRM project; or, one-third according to Clark (2001). Indeed the cost of hardware and software is falling, but the cost of IT professionals is rising because of a talent shortage.

Software may be purchase outright or licensed. Several software components may be required for a large-scale CRM investment: Among them are:

Sales force automation: contact management, account management, order processing, proposal generation

Sales management automation: pipeline analysis, territory design, sales reporting

Call-centre automation: auto-dialing, scripting, AVR, CTI

Customer-service automation: incident analysis and escalation, problem resolution, warranty management

Marketing automation: campaign management, opportunity management, market segmentation, lead generation and reporting, event management

Operations management: customisation, production control, quality assurance

E-commerce functionality: extranets, EDI, e-procurement

Knowledge management: customer service, complaints resolution

The customer database is at the heart of IT-enabled CRM. Creating a single database by combining internal data from several channels and divisions, with relevant external data is a huge challenge that has been faced by many companies, particularly those that have grown through merger and acquisition. Home shopping companies, for example, can generate customer data at several touch points: traditional retail stores, web site, catalogue stores, call centre and agencies. To create a coherent picture of customer behaviour, which is a precondition for successful data mining, may involve importing of additional geo-demographic and life-style data, and may take many person-years.

People costs include recruitment, redeployment and training costs. Not every company implementing CRM is blessed with analytically- skilled talent. Statisticians and operations researchers may be needed. The analytical side of CRM may require expertise in segmentation analysis, migration modelling, lifetime value estimations, customer

acquisition planning, and customer churn analysis. Recruitment of CRM talent in direct marketing, campaign management and many other areas may also be required. Other employees may need to be retrenched or re-skilled.

Process costs may also be significant. Current working practices and workflow may need to re-engineered. For example, the market segmentation process may need to be overhauled to accommodate notions of customer value. The selling process and campaign management process may need reinvention. This takes time and money.

As we have seen, in CRM introductions to large companies, the IT cost alone may reach beyond \$10 million. Typically, these investments will be incurred over a number of years as the overall CRM implementation is rolled out as a series of smaller projects. Even small-scale implementations in which only a single activity, say selling, is automated, can reach six figures. CRM is not cheap.

What counts as a return on investment?

The board level, or strategic, perspective on CRM would want an answer to the question: 'How much additional profit has this investment in CRM yielded?' For complex, long-term, multi-phase projects this is an impossible question to answer. To compute the gain associated with a CRM initiative would require all other variables impacting the profit equation to be held constant, or an experimental design to be constructed. Large-scale implementations take between 2 and 5 years to accomplish. During that time, the competitive environment might have changed dramatically, with new players entering, mergers and acquisitions, new products on the market, customer expectations lifted.

Despite the expectation of shareholders that boards will measure performance against a set of hard financial indicators, they are also likely to employ some very soft indicators of CRM's impacts too. One survey (Cap Gemini Ernst and Young 2001) suggests that 'customer-centric visioning, in which executives develop an enterprise view of their strategy from the customer perspective' is the most valuable CRM initiative. How is this meaningfully measured in terms of ROI?

Every large-scale implementation is composed of a number of smaller projects: database development, market segmentation, customer portfolio analysis, campaign management, web-site upgrade, customer contact centre integration, for example. Each of these will have cost profiles and time scales. However, not all generate revenue streams. Investments in database development and market segmentation, for example, typically represent sunk costs without which it would be impossible to run CRM-driven campaigns and events. They are necessary costs that enable CRM to function.

With small-scale implementations the task of measuring return is easier. If only a single function is automated, it is possible to establish clear performance targets. For example, it might be possible to measure the number of proposals written before automation with the number afterwards, or the number of prospects converted into first-time customers, or the

number of quintile two customers who are migrated to quintile one. Even so, without appropriate controls in place, management could not be sure that the cause of the change is the CRM investment.

As large projects are broken down into smaller units (the operational and analytical perspectives in table 1) it does become easier to set some very specific ROI targets. For example, Peppers and Rogers (2001a) suggest that clients expect a number of outcomes from their CRM implementations: improved customer service, greater customer retention, increasing customer life-time value, improved customer acquisition, and ability to identify strategically significant customers. These tend to be somewhat 'softer' measures, thought nonetheless important, than ROI at the strategic level.

This somewhat 'softer' view of CRM returns would capture its direct impact on costs and revenues, for example, customer acquisition costs, cost-to-serve, average transaction margin, average customer value, and basket value for example.

Many CRM implementations employ even more indirect measures of the impact of CRM upon ROI. These assess neither cost nor revenue, but rather, some driver of either or both. Amongst these metrics are customer satisfaction, customer retention, number of new customers acquired, customer attrition rates, cross-sell rates, up-sell rates, average number of products owned per customer, inventory turns, average number of transactions, share of wallet, customer complaints rates, process costs, rework, employee satisfaction and employee retention.

The softness of some of these metrics is debatable. Fornell (2001) for instance is clear that high levels of customer satisfaction do drive profitability; Reichheld (1996) is equally clear that customer retention drives profitability.

Different industries face different CRM problems and therefore need different metrics to assess ROI. Telecom companies' biggest customer problem is churn that can be up to 40%. Their CRM objective is to hang on to the most valuable customers, and to cross-sell them data and other communication services thus building a multi-product bond that is harder to break. In financial services, the CRM goals are to reduce transaction costs by shifting customers from branches to phone to web, and to cross-sell and up-sell to customers based on their past behaviour and propensity to buy, thus earning a greater share of customer wallet. An ECCS survey (Reed 2001a) identifies customer retention and cross-selling as the major CRM objectives in retail banking. Customer retention dominates insurance, whereas persuading existing customers to buy more (basket value) dominates retail. Where specific strategic goals such as these are the drivers of the CRM investment ROI objectives can be specifically translated into retention, share of wallet, win-backs and other metrics that feed ROI.

Different types of CRM project need different metrics. Operational (table 1) CRM projects such as consolidation of call centres or the development of web-based e-service will be measured against cost reduction objectives; cross-selling and up-selling projects will be measured against revenue objectives; customer loyalty projects will be measured

against retention, tenure, and share of customer/wallet objectives. Generic ROI objectives may be utterly irrelevant, depending on the scope of the project.

Profits are what remain after costs are subtracted from revenues. As we have seen, CRM investments can impact both sides of the profit equation. Cost-to-sell and cost-to-serve are important influences of cost. In a business-to-business context, it is not unusual to find that large volume customers are unprofitable. A high cost-to-serve can be caused by short customized production runs, just-in-time requirements, a high level of before- and after-sale service, discounts negotiated for volume, logistics inefficiencies from delivery of part-loads. Process (in)efficiencies impact on the cost side as do customer retention rates. A high level of retention is associated with improved marketing efficiency, since customer recruitment costs are reduced. On the revenue side, price paid, cross-selling and up-selling to earn a greater share of retained customers' wallet are important enablers of better revenue performance.

Over what time period should ROI be measured?

For some companies CRM is a long-term investment that is expected to pay off over periods of up to ten years. However, as noted earlier, even big projects such as these are composed of smaller projects with more clear-cut objectives and time-frames. One observer suggests that 'CFOs need to stop trying to get immediate ROI. CRM systems are large and complex. Changes in the corporate culture are required before they will work. CFO's should be thinking strategically, not small' (Greenberg 2001). As the perspective on CRM shifts from strategic to operational to analytical, so does the time frame over which performance should be measured. This moves from long-term to medium-term to short-term. Whether the organisation becomes more customer-centric following the adoption of CRM practices is a question that can only be answered over the long-term. However, it is certainly possible to measure the costs and revenue impacts of CRM-enabled promotional campaigns over a matter of weeks, if not days.

suggesting that 'the biggest mistake is to let the technology features drive CRM functionality.'

Evidence of poor project management skills is found when ownership of the CRM initiative is heavily identified with a single silo, typically IT, marketing or sales. The programme's effects are diluted because there is inadequate buy-in from other parts of the organisation. A CRM project that is championed by IT is unlikely to flourish if the organisation's processes and products are misaligned with customer requirements. Cap Gemini Ernst and Young (2001) found that 41% of European CRM projects were undertaking CRM projects at a departmental level instead of taking a cross-functional or enterprise wide approach. Strong programme management skills are needed to ensure that all functions impacted by the implementation are aligned with its objectives. Similarly a CRM Guru report (2001) identifies that CRM systems' 'ease of implementation' was a major source of dissatisfaction.

Barnes (quoted in Forsyth 2001c) suggests that inadequate leadership from the CEO lies behind many CRM failures. He writes, 'It is patently wrong to delegate responsibility for customer relationships to the marketing department or the development of a CRM program to the IT folks. Since long-term customer satisfaction is the single most important factor that drives shareholder value in a company, the CEO must take a singular interest in and responsibility for the creation of long-term customer satisfaction'. This is corroborated by research undertaken by ECCS (Reed 2001a) that identified the lack of senior-level buy-in as the single most important cause of CRM failure.

Many CRM implementations require the organisation to be redesigned. Most companies are designed around products or geographies, 41% and 20% respectively according to Cap Gemini Ernst and Young (2001). CRM implementations require joined up strategy focussed on customers regardless of product or geography. At the very least, cross-functional teams should be established to develop and implement CRM strategy. Sometimes a better long-term solution is to reorganise marketing, sales and service around customers. Strategic issues around reinventing the organisation may undermine CRM efforts, as product and geographic champions find themselves under threat.

Furthermore, since CRM is essentially cross-functional in nature, vertical processes may need to be abandoned and redesigned horizontally. Automation of processes that are not working very well currently makes little sense.

Also threatening the success of CRM implementations is the inertia of people who are reluctant to abandon or adapt current working practices. People who do not buy in to the programme may hinder its advancement. Clearly, people whose work is going to be influenced by the programme need to be involved in its development and roll-out. Furthermore, they may need to be rewarded for performances that are aligned with the programme's goals. Rogers (2001) suggests that 'a customer-based company must align its compensation, budgeting and incentive policies according to a customer centric model'. Rigby (2002) agrees, adding 'companies that don't redefine people's jobs and change performance measures, compensation systems and training programs' are more likely to experience a failed CRM implementation. People may also inhibit success because they have not been appropriately trained. The IT investment is only an enabler. If people are not skilled in analytical processes they will not be able to use the new data to improve their customer decisions.

A way forward

Given the complexity and time-frames of most CRM implementations, measuring ROI in the conventional sense of tracing the project's unique contribution to profit is a non-starter. In abandoning this effort, it helps to acknowledge that the investments in IT, people and process, large as they may be, are simply enablers, and can be treated as sunk costs.

At a Strategic level, an enterprise-wide view of CRM can be associated with a balanced scorecard approach to CRM metrics. Based upon the work of Kaplan and Norton (1996),

the balanced scorecard classifies objectives into 4 groups, i.e. financial, customer, internal processes, and learning and growth. There is an implied, and sometimes explicit, link between these forms of objective. From a CRM perspective, highly satisfied employees may quickly convert a customer enquiry into an order, leading to high customer satisfaction and profit on sales. The Hilton Hotel group is one company that has adopted a balanced scorecard approach. It measures its CRM performance by reference to 5 different sets of metrics: operational effectiveness, revenue maximization, customer loyalty, brand standards and learning and growth.

CRM impacts become more visible at the Operational or Analytical levels.

CRM benefits are reaped when skilled people exploit the information in the customer database to develop strategies and tactics that improve customer profitability (i.e. analytical CRM). This is done in two ways, by reducing cost-to-sell and/or cost-to-serve and by increasing the product margins earned over the customer's lifetime of buying from the company.

CRM implementations may reduce costs at a number of points in the customer's journey: acquisition costs, retention costs, selling costs, marketing costs, communication costs, service costs. For example, an American bank reduced its customer acquisition costs from \$100-150 to \$20-25 after implementing a CRM strategy (AIT 2001). In the UK, First Direct reduced its High Interest Savings Account customer acquisition cost from £123.07 to £22.17. Equally CRM can impact the revenue side. First Direct's CRM-driven campaign for unsecured loans generated opening balances of £86,000 as opposed to £54,000 under the conventional direct marketing approach.

Operational CRM projects may include the development of new segmentation models, new service propositions, new product offerings, new channels (routes to market), new pricing structures, and new forms of customer communication. Lastminute.com has appointed consultancy *dunnhumby* to develop a new segmentation of customers so that customer communication can become more bespoke. It will not be known how cost-effective this is until the segmentation model is rolled out and experimentally tested against the current segmentation model. Technology firm 3Com reinvented its service offer, shifting service from call centre to web self-service. It enjoyed \$16.8 million savings in 2000 as fewer calls entered the call centre, talk times fell, call transfers fell and training costs fell.

Many CRM implementations have focused on the strategic issue of channel integration. Charles Schwab, for example, has attempted to create a more integrated personal experience whether customers use branches, call centre or visit *schwab.com*. Others have focussed on new product launches at carefully targeted customers (Egg, First Direct). These are high-level strategic moves that reflect the adoption of an Operational CRM approach.

CRM tactics, on the other hand, reflect an Analytical CRM approach. CRM tactics can be many and varied. Indeed, Capital One is reputed to have run over 40,000 unique tactical

campaigns in a single year, all tightly focussed and specifically designed to achieve specific goals. It is at this level that many CRM investments pay off.

Results from CRM implementations are often stronger when they are rolled out in modular fashion, proving their merit en route (Rigby 2002)

In the absence of any better approach to customer segmentation, Recency-Frequency-Value data can be very useful for campaign planning. Evidence is strong that customers who have bought recently are most likely to buy again, similar but less strong associations exist for customers who buy frequently, and customer who spend most. All 3 groups are amongst the most likely to buy in the next period. For example customers who have been inactive for a month may have a 20% probability of responding to a targeted offer; 2 months (10%), 3 months (2%) and 4 months (<1%).. CRM tacticians can experiment with different cohorts of customers. For example, it is possible to check whether a 10% or 15% discount is the most profitable way to ‘win- back’ a customer who has not bought for a year. As the customer database’s accuracy and completeness improves, and mining and modelling become more sophisticated, companies will be able to extract greater value.

Tactical CRM campaigns are generally designed to achieve one of 3 CRM goals: customer acquisition, customer development and customer retention. Each campaign can become a live experiment that enables the business to become more efficient (reduce cost) and/or more effective (increase revenues or margins) in its deployment of marketing resources. Data which are particularly valuable are propensity data which, if deployed in real-time to customer facing staff, can lift conversions significantly. Goldschlager (2001) proposes a matrix approach to campaign planning that is founded on the idea that CRM attempts to migrate customers from prospect to loyal customer (advocate) status whilst creating value for both parties along the journey (see table 2).

A model of excellence is the winner of the first international CRM Industry awards, the Royal Bank of Canada. Their CRM journey began in 1995 and has cost them over \$100 million. Today, the VP for CRM claims that ‘we no longer view CRM as a program. [It] is our core strategy’. Revenue growth is running at 10-15% p.a. and profit growth approaches 25% p.a. ‘We absolutely conclude that CRM is paying us back in spades. It has enabled us to grow both the top of house revenue line and at the same time achieve huge cost savings.’ Among the ROI indicators that RBC employ are Internal Rate of Return for investments in major CRM functionality or initiatives such as a new pricing strategy. They also track measures such as deposit rates, credit limits, direct mail response rates, experimentally testing new tactics on subsets of customers before rolling them out across the chosen customer segments. The Bank also focuses on major metrics such as revenue growth, profit growth, cost control, risk, and debt write-offs. The Bank also credits CRM with reducing the costs of acquiring each dollar of revenue from 63 cents to 55 cents. RBC is presently reorganising its structure around customer groups, and has introduced a system of accountability for P&L at the segment level.

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