Calculating the ROI of CX: Complete Guide 2020

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About the author

Alyona Medelyan is the CEO & Co-founder of Thematic, an AI startup that uses the power of natural language processing & machine learning to help companies all over the world understand their customers.

Alyona has a PhD in natural language processing & machine learning and was inspired to write this guide after listening to countless stories of CX professionals struggling to prove the value of CX & NPS.
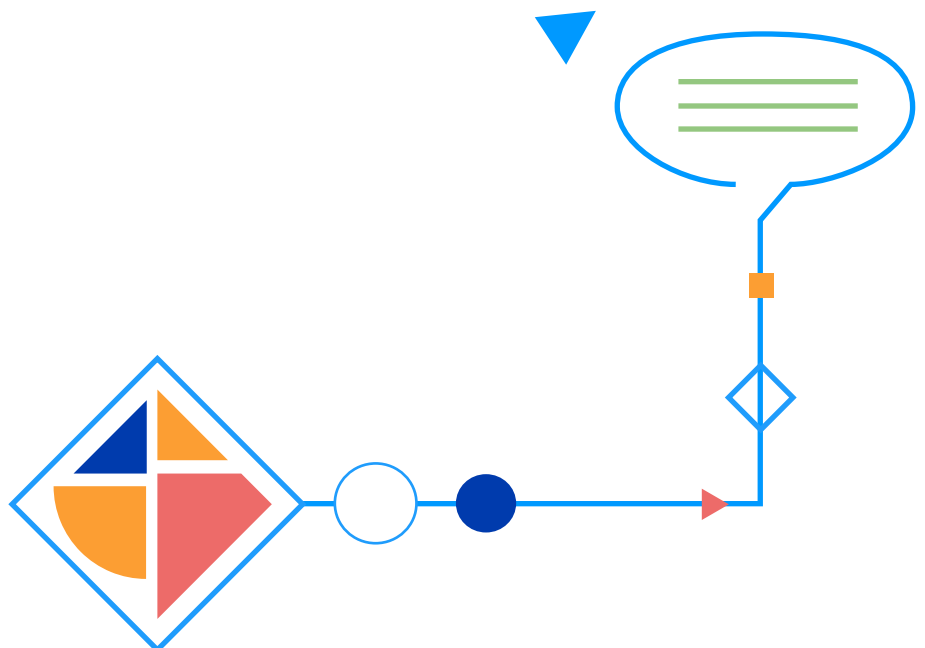
Chapter 1
Introduction – ROI or Die!

"Demo or die!"

– my PhD supervisor was very clear on what is the most critical path to success in academic research.

As I later learned, in the business world, ROI or Return on Investment calculations play a similar role.

You won't be able to get executive buy-in, approval for budget, communicate success and ultimately progress in your career, unless you can estimate and then validate the ROI.

Metrics such as NPS have become currency, accepted in blind faith by many, but CX professionals still have difficulty getting companies to take action on what can move these metrics.

We believe what's missing here is the ROI of taking action on identified metric drivers. For the remainder of the post, we'll use NPS as our metric of choice, but you can substitute a different metric instead.

So how can you get people to take action on insights, demonstrate program impact and gain visibility?

Showing the linkage between NPS and financial metrics first, and then demonstrating ROI is the key here.

So, where do we start?
## How can we calculate the ROI of CX?

By showing the impact of increases in NPS on financial metrics!

In this guide we break down different methods and give step-by-step instructions on how to create your own ROI of CX models in our pre-made spreadsheets.

We believe what's missing here is the ROI of taking action on identified metric drivers. For the remainder of the post, we'll use NPS as our metric of choice, but you can substitute a different metric instead.

There are three key reasons why proving the ROI of CX is hard:

1. Speed & precision of insights - having hard data rather than anecdotes is still something many CX professionals struggle with (and which is why we started Thematic!)

2. CX is perceived as fluffy, non-quantified and therefore not trusted.

3. People don't truly understand the impact of even small increases in NPS on revenue
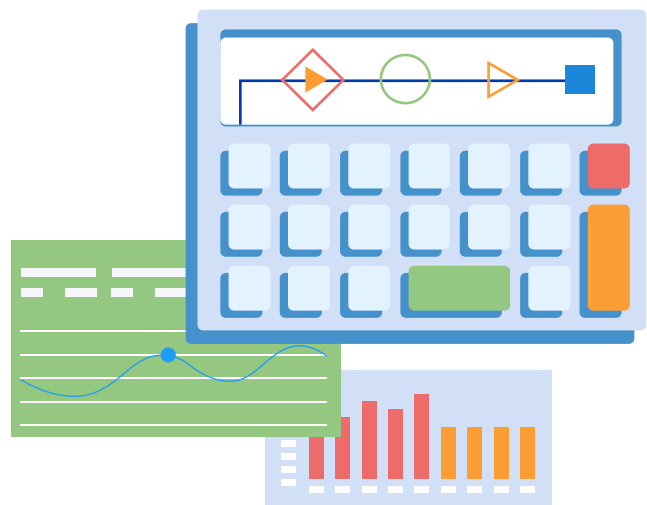
Chapter 2
Why calculating ROI of CX is hard

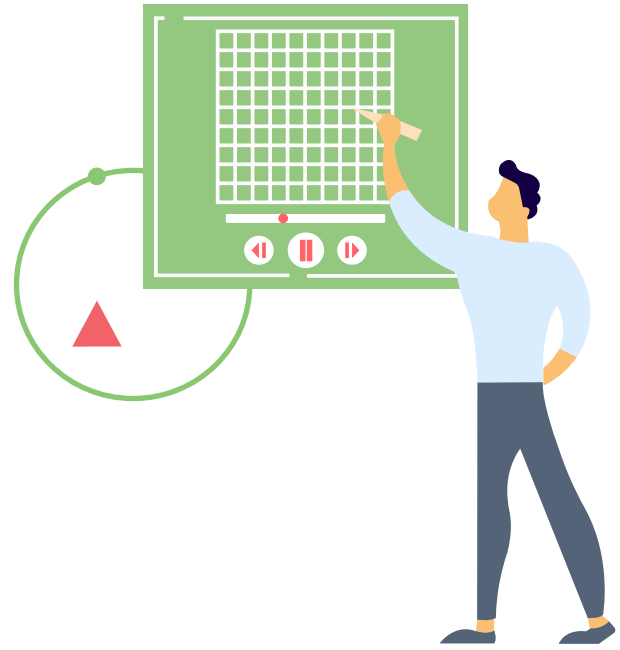$$\frac{\text{Value of Facebook leads}}{\text{Cost of Facebook leads}} > 3$$

ROI is easy to calculate for any investment that has immediate results.

For example, if I spend $1000 on Facebook ads, I can see within a week what kind of leads I can get from this investment.

Established businesses know the value of leads, because they know how well this convert to customers.

So, it's easy to calculate the ROI.

You need not just a positive ROI, but ideally greater than 2 or 3.

Calculating ROI of CX investments can be hard because it's not clear how long it would take to implement Step 2 and 3, and how effective might be the solution.

However, **not investing into CX will result in significantly worse outcomes** than not investing into advertising, such as Facebook ads.

When it comes to seeing improvements in CX, it can take months or even years to obtain the results, and it's a multi-step process:

Step 1. Measure CX using a metric like NPS and identify its drivers. (Some companies run a driver analysis. At Thematic, we can identify drivers by showing how themes in customer feedback can impact NPS.)

Step 2. Implement improvements

Step 3. Wait for customers to notice improvements

Step 4. Measure again and evaluate change in behaviour. Are customers mentioning the same themes? What's their impact on NPS

Due to 3 reasons:

1. Customer expectations are continuously rising;

2. It is easier than ever to start a business and advertise to people world-wide;

3. Customer loyalty is difficult to both win and retain.

Chapter 3
The fundamentals for calculating ROI of CX

First off, you will need the following basic research completed in order for the ROI calculations to be valid.

Choose your metric. In our case, it's NPS.

The premise behind NPS is simple...
It categorizes people into those who are more likely to recommend the company to others (Promoters) and those who are less likely to do so (Passives and Detractors).

People are more likely to recommend companies where they have great experiences and where they are treated well by the company and its employees. All examples of great CX!

This should translate into financial metrics that result in faster growth: lower churn, higher customer lifetime value and decreasing cost of customer acquisition.

Given the results from your last NPS survey, you will need two sets of metrics. Average annual spend and average number of referrals per NPS category. For example:

NPS Category	Average annual spend	Average number of new customers referred
Promoter	$2,000	3
Passive	$1,000	1
Detractor	$500	0

The referrals might be more difficult to measure, but there is no way around it. Get creative!

In B2C it could be linking customer IDs via referral codes (like in this Instacart's example), in B2B it could be asking new customers who referred them. At Thematic, we keep a special field for this in our CRM.

Your numbers might not be exactly the same, but they should follow the same pattern...

~ Promoters spend more than Passives ~

~ Passives spend more than Detractors ~

If your numbers don't follow this pattern, something isn't right.

The most likely reason is that the NPS isn't measured correctly.

Here are the common measurement mistakes we've been seeing:

1. Offering people a financial incentive for filling out the survey can lead to people giving high scores instead of a truthful ones.

2. Making NPS into KPIs of individual

   people and even departments can lead to poor practices, such as "Give me a 10 or don't respond". (this is an especially common practice in some industries, such as car dealerships).

I hope you get to a state where the numbers make sense.

Chapter 4
The logic behind ROI of CX calculations

So how does one quantify the investment into CX to help a brand to stay on top of these rapid changes in consumer expectations and behaviours?

Let's follow the similar formula as we used for the ROI of Facebook ads.

4.1 Value of investment into CX

Unlike in advertising on Facebook, the steps required to see in improvement in CX will take longer than one month.

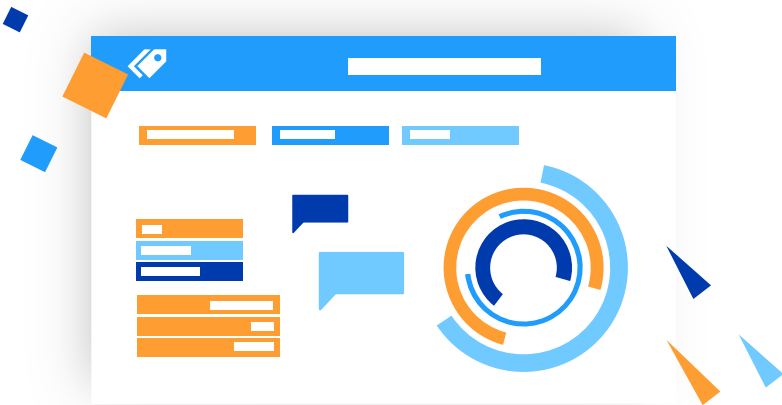To keep things simple, let's assume it will take at least 6 months.

When estimating the ROI, the value of the CX program is **the difference between the financial metrics today** and **the metrics that are to be realistically expected 6 months from now.**

When calculating the ROI 6 months into the program, the value of the CX program is the difference between the **financial metrics 6 months ago** and **the same metrics today.**

4.2 Cost of investments into CX

When calculating the costs of investments into CX, these are the typical areas companies invest into:

1. **Measuring NPS** of their customers at various touchpoints and identifying under performing touchpoints.

2. **Benchmarking their own NPS against competitors** in their industry to understand what good vs. bad performance looks like relative to a set of peer companies.

3. **Identifying the drivers of NPS** by doing a driver analysis, or calculating which themes have positive and negative impact on NPS.

Tip: When benchmarking data is available, insights into what works and doesn't work for competitors is incredibly insightful.

4. Programs to drive improvements to NPS:

- Better experience when people evaluate your product by using your website and marketing materials
- Better processes for onboarding new customers, delivering goods or services, as well as payment and billing,
- Better UX when using digital products
- Better training of staff to keep customer needs and the desired behaviours top of mind
- Investment into employee experience

With the growth of NPS, many companies have been investing heavily in element 1: Introducing technologies to collect customer feedback across all different touchpoints.

Far less companies – often those only heavily invested in the Net Promoter System approach – invest in element 2, as well.

The challenge often lies in elements 3 and 4.

Companies often under-invest (or fail to invest at all) in understanding the why behind NPS (what impacts its) and in the programs to actually improve NPS over time

Deep analysis of customer feedback will help you not only identify which programs are the most important to customers, but also whether customers have noticed an improvement in these areas over time.

Now let's look at how to calculate the impact of NPS on revenue.

Chapter 5
How to calculate the impact of NPS on revenue (ROI of NPS)

Let's get into calculating the value of investment into CX by linking its metric, NPS, to revenue. NPS ROI.

First, you will need the total number of customers and a breakdown of the percentage of customers that fall into each NPS category.

This is an estimate but hopefully close to reality.

Number of Customers	40,000
Customers by NPS category (real data)	
Percentage of Promoters	74%
Percentage of Passives	15%
Percentage of Detractors	11%
NPS	63%

Next, you will need one of the metrics described in Chapter 1: the average spend per customer, aggregated for each NPS category.

Average annual customer spend per NPS category (real data)	
Promoters	$2,346
Passives	$2,089
Number of Detractors	$1,908

Now you can multiply the two numbers to calculate the total revenue per NPS category.

These numbers alone are already quite insightful.

Estimated revenue per NPS category (assuming the same distribution over total customer base)	
Promoters	$69,426,800
Passives	$12,535,200
Number of Detractors	$8,394,760
Estimated total revenue	**$90,356,760**

The sum is the estimated total revenue for the company and hopefully matches the actual total revenue.

Make sure to cross-reference here.

So, what would be an impact of an increase in NPS by a few points?

We need to make some assumptions here.

The table on the next page illustrates a conservative example that shows some revenue growth in any case and models two scenarios:

A small increase in NPS (with CX programme) distributed among all NPS categories and no increase in NPS (without CX programme).
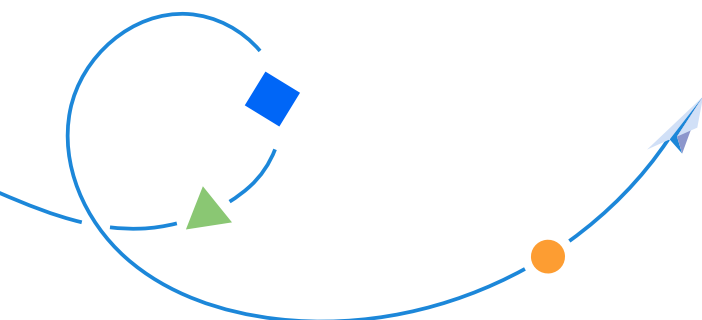
	Today	In 6 months		Notes
		with CX programme	**without CX programme**	
Number of Customers	40,000	40,400	40,400	Assuming 1% growth over the next 6 months
Customers by NPS category (real data)				
Percentage of Promoters	74%	77%	74%	Increasing percentage of Promoters by 2pp
Percentage of Passives	15%	13%	15%	Moving 3pp of Passives into Promoters
Percentage of Detractors	11%	10%	11%	Moving 1pp of Detractors into Passives
NPS	63%	67%	63%	Increasing NPS by 4 percentage points

If we assume that the spend per customer stays the same, we arrive at the following numbers:

	Today	In 6 months	
		with CX programme	**without CX programme**
Number of Customers	40,000	40,400	40,400
Estimated revenue per NPS category (assuming the same distribution over total customer base)			
Promoters	$69,426,800	$72,963,814	$70,121,068
Passives	$12,535,200	$10,972,478	$12,660,552
Detractors	$8,394,760	$7,707,916	$8,478,708
Estimated total revenue	$90,356,760	$91,644,208	$91,260,328

The increase in revenue with the CX program may not seem impressive, but it's 42% higher than without it:

In Percent	In Percent	In Value
Growth without CX program	1.00%	$ 903,568
Growth with CX program	1.42%	$1,287,448
Value attributed to CX		$ 383,881

You can tweak the numbers and download this **spreadsheet in our free CX toolkit.** Or request it via our Tools page to get the Excel spreadsheets.

The numbers will be especially meaningful if you can validate them against the metrics in the past.

For this specific example, the value of NPS increase of 4 percentage points is around $384K.

A good ROI of 3x would be if this company spent $127K towards that increase.

Chapter 6
How to calculate the impact of NPS on Customer Acquisition Costs (CAC) (ROI of NPS)

Investment into a CX program also can have positive effects on lowering the customer acquisition costs.

You will need the total number of customers and a breakdown of the percentage of customers that fall into each NPS category.

In addition, you will need:

- Current CAC (cost of customer acquisition) via marketing;
- Cost of CAC via referral (in most cases it would be $0, but some companies may pay both those who refer a customer and the new customers a small amount);
- · Percentage of customers acquired through marketing vs. referrals
- An estimate of how many customers promoters actually do refer (e.g. 1 in 10 promoters may actually refer new customers)

We suggest to also model churn, as customer acquisition programs typically counter-balance churn.

With that you would get numbers like these:

How many promoters you need due to churn	4,000
Number of customers acquired via marketing	3,200
Number of customers acquired via referrals	1,480
Cost of replacement customers	$1,600,000

In 6 months, what would happen if there were significant changes to these numbers?

Here is an example of what these numbers might look like:
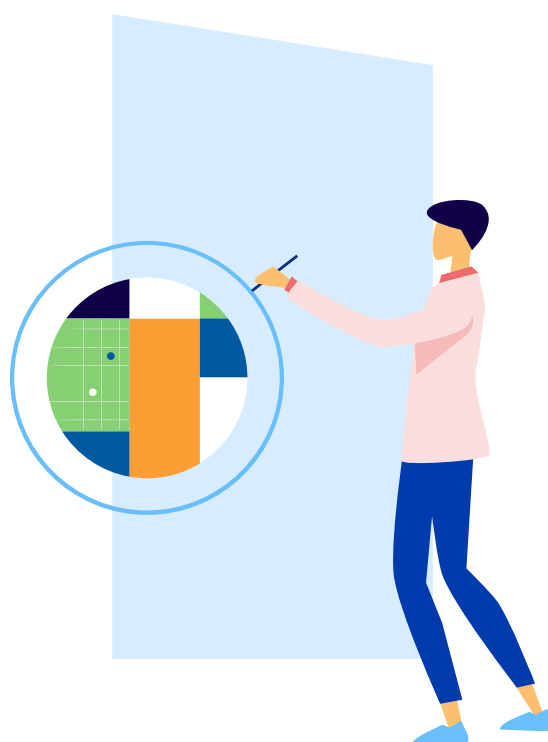
Variables	Today
Total number of customers	40,000
Cost of acquisition via marketing	$500
Cost of acquisition via referrals	$0
% of customers acquired via marketing	80%
% of customers acquired via referrals	20%
% of customer churn/ decrease in spend	10%
Promoters	74%
Passive	15%
Detractors	11%
Net Promoter Score	63%
Number of promoters	29,600
Referral activity: Number of referrals per promoter	5%

If the NPS increased by 13%, most likely your churn might drop too.

Let's say it dropped by 2 points and is now 8%. The total percentage of customers you would need to replace using marketing is 8% * 40,000 = 3208 customers.

Since the NPS increased and the number of Promoters increased by 7 percentage points to 32,080, they are now generating more referrals, a total of 1604.

That's exactly 50%, and significant reduction in costs required to replace churned customers.

In this scenario, the value of the CX program is almost $800,000.

You could also calculate the new CAC here, as the average across these two channels.

What's clear though is that if you do nothing, it's unlikely that CAC is going to drop.

Variables	Today	In 6 months	Notes
Total number of customers	40,000	40,100	
Cost of acquisition via marketing	$500	$500	
Cost of acquisition via referrals	$0	$0	
% of customers acquired via marketing	80%	50%	(potential outcome of increasing NPS)
% of customers acquired via referrals	20%	50%	(potential outcome of increasing NPS)
% of customer churn/ decrease in spend	10%	8%	(potential outcome of increasing NPS)
Promoters	74%	80%	(by focusing on user needs, you'll get more promoters)
Passive	15%	15%	(assuming the same number of passives)
Detractors	11%	5%	(by focusing on user needs, you'll decrease the number of detractors)
Net Promoter Score	63%	75%	
Number of promoters	29,600	32,080	
Referral activity: Number of referrals per promoter	5%	5%	(assumption: 5% of Promoters bring in Referral)
How many promoters you need due to churn	4,000	3,208	(calculated from churn x number of user)
Number of customers acquired via marketing	3,200	1,604	
Number of customers acquired via referrals	1,480	1,604	(calculated from number of promoters x referral activity
Cost of replacement customers	$1,600,000	$802,000	
How much less you spend due to NPS increase	**$798,000**		

Chapter 7
Key take-aways when it comes to calculating ROI of CX

ROI or die!

Investment into getting the financial metrics behind your program and its influence are critical to your professional success.

You need to make sure you have the key metrics (average spend per NPS category) and that these metrics align.

If they don't, there may be an issue with the survey.

Calculating customer experience ROI is hard because steps towards improving CX metrics might be expensive and take a long time to implement.

Depending on the company, you could save a lot on the costs of measuring NPS. For example, we are running our NPS survey for free via <u>Vitally.</u>

Remember that surveying alone won't result in change.

Make sure you invest into:

- Knowing what to improve,
- And working on improving it

I hope this guide has provided insight into the ROI of CX, and that you can now take the necessary steps to make your own calculations.

Time to prove to the C-suite the value of CX.

Thank you for reading, and please feel free to get in touch. I'd love to hear how you're calculating customer experience ROI at your company.

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