Can Net Promoter Score really predict a firm's performance?

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The Net Promoter metric, also known as Net Promoter Score (NPS)[1], was introduced by Frederic Reichheld and his team at Bain Consultants in 2003. It has since been embraced by many large and well-respected corporations as well as medium-sized firms as an indicator of customer loyalty and firm performance. Many of these firms benchmark the Net Promoter metric and/or use it as a key performance indicator.

Reichheld's Net Promoter metric was popular because it supposedly proved that positive word of mouth, as opposed to customer satisfaction or retention, resulted in additional sales, driving growth as a result. However,

while it has been scientifically proven that word of mouth does have a major impact on customer responses to a product, the relationship between word of mouth and the cross-industry financial performance of firms has remained largely un-explored.

A more recent study by Keiningham et al analysed data from 21 large firms in a wide variety of household service industries, tracked by the Norwegian Customer Satisfaction Barometer (NCSB). The study was made up of over 15,500 telephone interviews with households during a period of 2 to 4 years. Each firm was represented by 100-200 existing customers. Criteria included intention to recommend, overall satisfaction, repurchase intentions, and a NCSB-developed satisfaction index score.

Keiningham et al has raised concerns over previous research in which the Net Promoter metric was linked to past growth as opposed to future growth, suggesting that word of mouth

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[1] The Net Promoter metric is based on asking customers the following question: "How likely or unlikely is it that you would recommend company XYZ if a friend or business relations asked you for advice?" (0="very unlikely", 10="very likely"). Customers who rate either 9 or 10 are classified as "promoters", whereas those rating 6 or lower are classified as "detractors". Customers rating 7 or 8 are considered neutral. The Net promoter Score is calculated as the proportion of a firm's promoters minus the proportion of a firm's detractors.

is a consequence rather than an antecedent of sales.

For five industries, banking; petrol stations (with convenience stores); home furnishings retailers; security systems; and transportation, data analysis revealed no significant correlation between firms' growth rates and Net Promoter or satisfaction/loyalty metrics.

Subsequent examination of 11 satisfaction/loyalty metrics, including the Net Promoter metric, also revealed that none of these metrics added to the predictive power of scientific models for industry growth.

The American Customer Satisfaction Index (ACSI) was then compared with Net Promoter. The ACSI is a metric which Net Promoter metric advocate Reichheld and his team at Bain Consultants believe is unrelated to industry growth. In fact, re-analysis by Kleiningham et al of accurately replicated data demonstrated that ACSI outperformed NPS in predicting industry growth in 2 of the 3 industries examined. However, there was not sufficient data available to reinvestigate the remaining 9 of the 12 industries originally investigated by Reichheld (2006).

Despite data limitations and careful consideration of a number of possible methodological concerns, including data quality; question wording; use of a 10- versus 11-point scale; and cultural differences, Kleiningham et al concluded that the study found no support for the claim that Net Promoter is the "single most reliable indicator of a company's ability to grow."

They argue that executives erroneously believe that the acclaimed superiority of the Net Promoter metric has been based on solid academic research, resulting in the worldwide adoption of the metric by many prestigious firms.

To prevent misallocation of resources firms should think twice before solely relying on the Net Promoter metric for strategic guidance on firm performance, company value, and shareholder wealth.

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The full reference for this study:

Keiningham, T.L., Cooil, B., Andreassen, T.W. & Cooil, B., 2007, A Longitudinal Examination of Net Promoter and Firm Revenue Growth, Journal of Marketing, Vol. 71 (July), 39-51.

Additional references:

Reichheld, F.F., 2003, The One Number You Need to Grow, Harvard Business Review, Vol. 81 (December), 46-54. / Reichheld, F.F., 2006, The Ultimate Question: Driving Good Profits and True Growth, Boston: Harvard Business School Press.