Managing Customers for Profit

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Chapter – 4
Managing Customers Profitably

Instructor's Presentation Slides

Relevant Issues

How do we build and sustain profitable customer loyalty?

What are the drivers of profitable customer loyalty and how do they help in managing customers?

Diverse Customers

Customers are diverse in their preferences and goals within the company

- Long-term vs Short-term
- Channel Selection
- Profitability
- Breadth of Purchase

How can the company measure and understand how its individual marketing actions are affecting the purchase behavior of such a diverse group of customers?

Profitable Customer Loyalty (CLV)

- The guiding rule in making strategic decisions based on CLV is simple:

  "Do the actions taken by the company maximize CLV?"

- If yes, then continue with the strategy, if not, then abandon or modify the current methods.

Drivers of CLV

The drivers of CLV are the main factors that affect the lifetime value of a customer.

These drivers determine the nature of the relationship between the firm and the customer, and help estimate the level of profitability and the CLV of each customer.

Drivers of CLV

Exchange Characteristics

Customer characteristics

Product characteristics

Firm Marketing Actions

Drivers of CLV (For a B2B company)

- Spending level
- Cross Buying
- Focused Buying
- Average Inter-Purchase Time
- Returns
- Loyalty Instrument
- Frequency of Marketing Contacts
- Bidirectional Communication

Profitable Customer Loyalty/CLV

A B2C Case Study in Retailing

- Background
  - A study was carried out involving a major retailer who sold apparel, shoes and accessories, for both men and women
  - A large sample of over 300,000 customers was taken from the firm's customer database for this study, and their individual CLV scores were calculated

Does Loyalty Drive Profitability?

Correlation between profitability and different measures of loyalty

	Regularity	Frequency	RFM	Tenure
CLV	r= -0.09	r= 0.17	r= 0.19	r = 0.44

The correlation is very weak between the regularity and frequency of purchase and the future profitability of the customer.

Firms cannot rely on traditional loyalty metrics like RFM there is only a weak correlation between the RFM scores of the customer and the future profitability

Firms should adopt a forward-looking metric like the CLV to identify profitable loyal customers and invest their resources towards such customers.

Customer Segmentation

Based on the study customers were divided into Segments which allowed the retailer to implement segment-specific marketing strategies

Typical High CLV Customer	Typical Low CLV Customer
Gender: Female	Gender: Male
Age: 35-54 years	Age: 25-34 years
Marital Status: Married	Marital Status: Single
Presence of Children	Presence of no children
Estimated Household Income: $125,000+	Estimated Household Income: < $50,000
Stays closer to retailer	Stays further away from retailer
Loyalty Card Member	Not necessarily a Loyalty Card Member
Mail Order Shopper	Single Channel Shopper
Shops frequently in upscale stores	

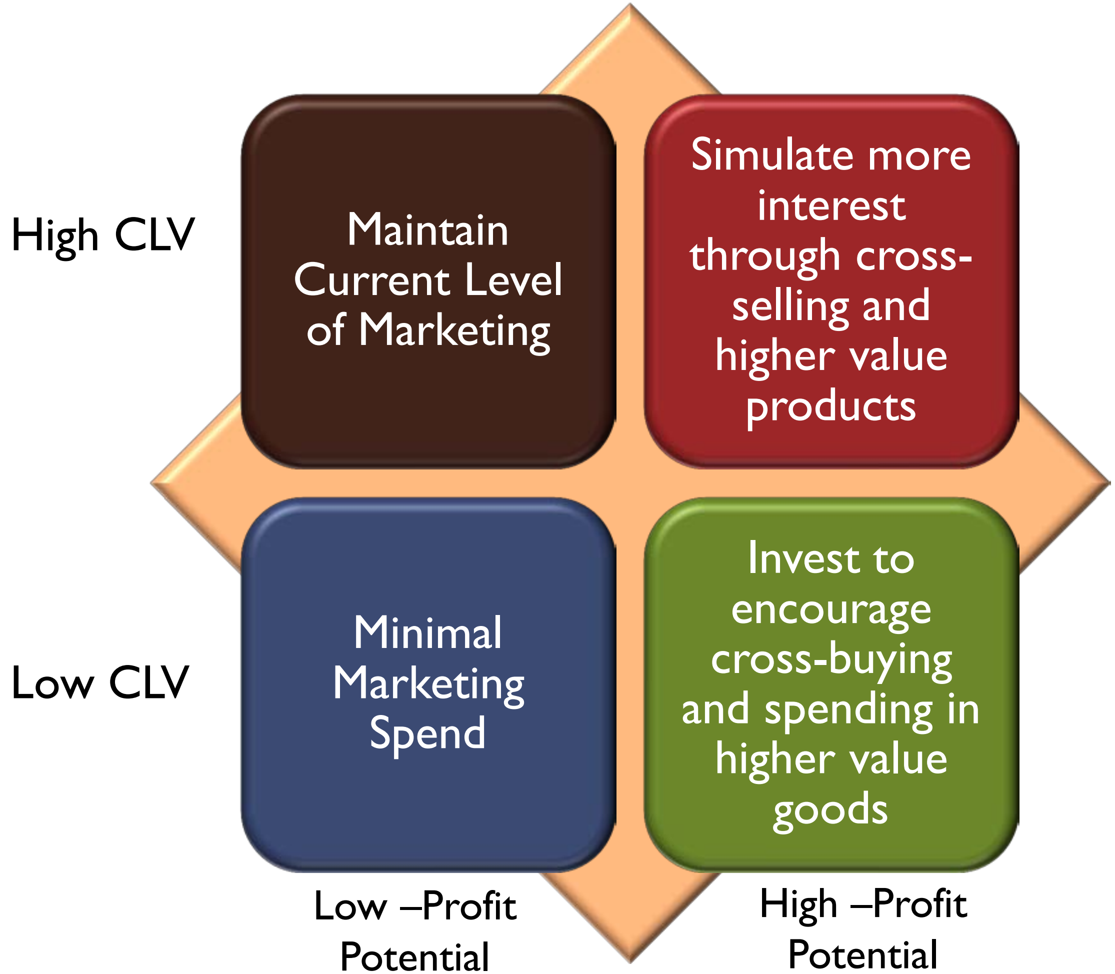
Effectiveness and Impact of Drivers

- Only high CLV customers considered
- The results show the increase in the CLV of a customer given a 15% increase in any of the categories of the drivers.

Results

- One would expect loyal customers to be profitable and hence would expect a strong positive correlation between loyalty and profitability
- The correlation is very weak between the regularity and frequency of purchase and the future profitability of the customer
- It is clear that firms cannot rely on traditional loyalty metrics like RFM (Recency Frequency Monetary Value Method, as described in Chapter 3) to manage their customers, as there is only a weak correlation between the RFM scores of the customer and the future profitability.

Results - An Example of CLV Score Application



End of Chapter 4