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CUSTOMER PROFITABILITY ANALYSIS

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CUSTOMER LIFETIME VALUE (CLV)

It is the prediction of the total revenue that a single customer will generate for a brand throughout the entire duration of their relationship, focusing on the long-term overview rather than just the initial purchase. This data helps businesses make cost-effective decisions regarding new customer acquisition and develop relationship management strategies to efficiently increase long-term business value.

EXAMPLE

- **Customer A: Purchases a 5,000 THB product only once and never returns.**
- **Customer B: Purchases a 1,000 THB product but returns to buy every month for 2 years.**

If looking only at the first purchase, Customer A might seem more valuable. However, when calculating CLV, it becomes clear that Customer B has a much higher long-term 'value' to the business (1,000 THB x 24 months = 24,000 THB).



WHY IS CLV IMPORTANT?

Measuring and understanding CLV benefits businesses in multiple dimensions, including:

- Helps in making better investment decisions for new customer acquisition.
- Increases profits from existing customer retention.
- Helps segment customers effectively.
- Serves as a guideline for product and service development.
- Indicates the stability and sustainability of the business



CUSTOMER LIFETIME VALUE MODELS

The CLV models are divided into two main categories: Historic, which uses actual past purchase data, and Predictive, which uses behavioral data to forecast future revenue. Selecting the appropriate model helps brands make investment decisions and manage customer relationships effectively.

	Historical CLV	Predictive CLV
Objective	Understands customer's past contributions	Forecasts customer's future value/behavior
Data used	Historical (such as past transactions)	Historical, demographic, and behavioral
Approach	Retrospective	Forward-looking
Advantages	<ul style="list-style-type: none">- Gives understanding of customer's past behavior patterns- Identifies successful interactions- Useful for short-term customer value assessment	<ul style="list-style-type: none">- Enables proactive strategy planning- Identifies high-value customers for long-term growth- Guides marketing campaigns and resource allocation
Limitations	<ul style="list-style-type: none">- Limited by available historical data- May not account for future changes in customer behavior or market trends	<ul style="list-style-type: none">- Requires advanced algorithms and data analysis techniques- Needs regular updates to maintain accuracy
Best-suited for	Businesses with limited data or seeking insights on past performance	Businesses aiming to invest in long-term customer retention strategies

HISTORICAL CLV

Historical CLV is calculated from actual revenue generated in the past to identify the highest-value customer groups at present. However, it has a limitation in that it cannot predict future potential. This data is therefore most accurate when used to segment customers based on actual spending or when analyzing the lifecycles of customers who have already ended their relationship with the business.





PREDICTIVE CLV

Predictive CLV uses statistics and Machine Learning to forecast future spending and the duration a customer will remain with a brand. It is calculated based on past behavior and churn risk, allowing businesses to proactively allocate budgets to retain high-value customer segments. Although it is complex and requires high-quality data for analysis, it enables early strategic decision-making.

HOW TO CALCULATE CLV (BASIC FORMULA)

There are many methods to calculate CLV, ranging from simple to complex versions that require statistical models. Here, we introduce a simple CLV calculation formula, which is a Historic CLV.

CLV Calculation Formula

$$CLV = AOV \times APF \times ACL$$

Where:

- **AOV (Average Order Value):** The average value of each order

Formula: Total Revenue / Total Number of Orders

- **APF (Average Purchase Frequency):** The average frequency of orders.

Formula: Total Number of Orders / Total Number of Customers

- **ACL (Average Customer Lifespan):** The average duration a customer stays with the brand.

Formula: (Sum of Customer Lifespans for each individual) / Total Number of Customers



If you want to know how much profit a specific customer generates, you can use the profit calculation formula:

$$CLV (\text{Profit}) = CLV \times \text{Profit Margin} (\%)$$

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- **CLV (Customer Lifetime Value):** The customer lifetime value calculated previously.
- **Profit Margin:** The percentage of profit derived from investment.

Starting from: Profit = Revenue - Cost

Then find the percentage: Profit Margin = (Profit / Cost) * 100



CLV CALCULATION EXAMPLES

1. Coffee Shop A

Suppose you own a coffee shop and want to calculate the CLV of a regular customer, based on the following data:

- The customer spends an average of 120 THB per visit (AOV).
- The customer visits an average of 4 times per month (APF).
- The customer has been a regular for 24 months (ACL).

Using the formula above, the CLV is calculated as follows:

$$\text{CLV} = 120 \text{ THB} \times (4 \text{ times/month}) \times 24 \text{ months} = 11,520 \text{ THB}$$

2. Coffee Shop B

Suppose a coffee shop has 4 branches with an average sale of 50 THB. General customers are locals who visit twice a week for 50 weeks per year, staying for an average of 5 years.

Calculation formula:

$$\text{CLV} = 50 \text{ THB (Average Sale)} \times 100 \text{ (Visits per year)} \times 5 \text{ (Years)} = 25,000 \text{ THB}$$

CLV CALCULATION EXAMPLES

3. Software Subscription

For this example, a UX designer uses a subscription-based software service with various pricing plans, but on average, customers pay 375 THB per month. Typically, customers subscribe for a period of 4 years and use a monthly payment model.

Calculation Formula:

$$\text{CLV} = 375 \text{ THB (Average Sale)} \times 12 \text{ (Purchases per year)} \times 4 \text{ (Years)} = 18,000 \text{ THB}$$

4. Car Dealership

A car dealership is a good example of a business with a high average sales value but low purchase frequency. Customer A buys a new car at a price of 750,000 THB every 5 years. Based on spending data and purchase frequency, Customer A is brand loyal and continues to purchase cars over a period of 15 years.

Calculation Formula:

$$\text{CLV} = 750,000 \text{ THB (Average Sale)} \times 0.2 \text{ (Purchases per year)} \times 15 \text{ (Years)} = 2,250,000 \text{ THB}$$





HOW TO INCREASE CLV

After understanding the approaches to calculating CLV, the next step is to study how to increase the CLV of our business customers. There are 5 methods as follows:

- **Building Strong Customer Relationships**

Build relationships through trust by keeping promises and sincerely listening to customer problems. Use Social Media to develop communication channels and create supportive communities rather than just for advertising. Additionally, sharing new product directions will help customers feel a sense of belonging and stay with the brand long-term to receive continuous value.



HOW TO INCREASE CLV

- **Always Improve Customer Service**

This is the key to long-term customer retention. Brands must regularly monitor and resolve flaws in the service journey, such as inadequate contact channels, lack of staff expertise, or unfair return policies. This is to eliminate obstacles that prevent customers from making repeat purchases and to create a lasting impression.

Methods that help brands collect data regarding problems include:

- **Conducting surveys to receive customer feedback.**
- **Receiving suggestions from various internal teams.**
- **Conducting social listening or checking reviews.**



HOW TO INCREASE CLV

- **Offer Special Deals to Customers**

This involves providing personalized special deals to stimulate repeat purchases and increase CLV. Brands should pay attention to new customers through after-sales follow-ups and provide exclusive benefits to regular customers through Loyalty Programs, such as free shipping coupons or early access to new products. This aims to build ongoing relationships and reward customer loyalty sustainably.



HOW TO INCREASE CLV

- **Create Valuable Content**

Creating valuable content must focus on solving problems and providing clear benefits to customers, rather than just offering promotions. Avoid content that is too broad or lacks a specific target audience. Good content will help build engagement and make customers continuously see the value in using the product, resulting in repeat purchases and an increased CLV.



HOW TO INCREASE CLV

- **Up-sell and Cross-Sell**

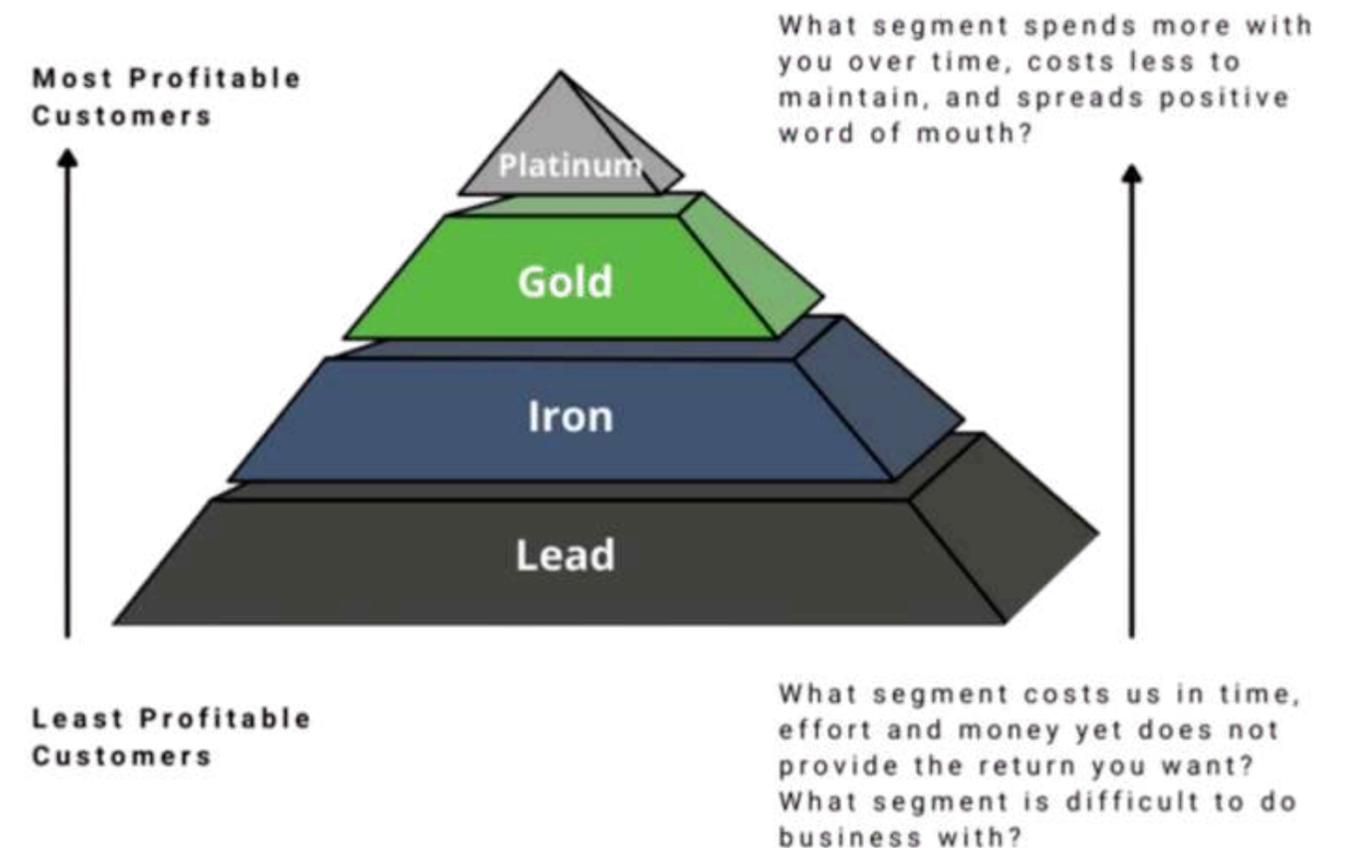
Up-selling and cross-selling are additional methods that directly help increase CLV in terms of revenue, as they are ways to increase the order value of each customer purchase.

Tips for Up-selling and Cross-selling include:

- **Selling in sets/bundles.**
- **Offering temporary upgrades.**
- **Running ads to recommend best-selling products.**
- **Offering free shipping.**
- **Avoiding overly detailed or overwhelming offer information.**

CUSTOMER PYRAMID MODEL

This is a model that prioritizes customers based on their purchasing behavior, loyalty, and the profitability they provide to the brand. The structure is divided into four levels based on value: Lead (the widest base), Iron, Gold, and Platinum (the top tier with the highest value). This allows businesses to appropriately manage relationships and resources according to these levels.





LEAD

The Lead level refers to new customers who have just discovered or started purchasing products for the first time. This group typically requires high investment from the business in terms of advertising and promotions but currently generates low profit for the brand. This segment carries a high risk if they have a poor experience, as they are prone to spreading negative word-of-mouth; however, if satisfied, they can evolve into higher-level customers.

Example:

An aesthetic clinic offering a free first-time trial to attract new customers is considered a "double-edged sword" strategy. If the service is good, it helps convert customers to a higher level. But if it fails, the brand not only loses the initial cost for free but also risks negative word-of-mouth, which severely damages its reputation.



IRON

This is compared to 'general customers' who purchase products or services from our brand regularly but still have a low purchase value or volume. Importantly, this is a customer group with high price sensitivity.

Example:

Customers who choose to buy only essential items or during discount periods, with low brand loyalty and readiness to switch to competitors immediately if a cheaper offer is available.



GOLD

Gold-level customers are the VIP group who purchase products regularly and have high spending levels, generating satisfactory profits for the brand. However, they still require stimulation through promotions or Loyalty Programs, such as earning points to redeem privileges, to maintain purchase consistency and prevent them from switching to competitors in the future.



PLATINUM

Platinum-level customers represent the top of the pyramid with the highest loyalty, purchasing consistently and willing to pay without focusing on discounts. This group also provides free word-of-mouth marketing for the brand through referrals and positive reviews. Therefore, businesses should prioritize this group as they have low maintenance costs while generating the highest sustainable profit.

CUSTOMER PORTFOLIO MANAGEMENT

Customer Portfolio Management (CPM) is the process of dividing the entire customer base into subgroups based on strategic importance, such as behavior or needs, in order to manage them with appropriately different methods. This information helps businesses plan their outreach to each customer group precisely, maximizing benefits in terms of both sales growth and profitability.

PORTFOLIO

In a customer context, this refers to the clustering of all non-overlapping customer groups of a business, categorized by variables of strategic importance.



DIFFERENCES IN CUSTOMER PORTFOLIO MANAGEMENT: B2C VS. B2B CONTEXTS

B2C

- Larger number of customers
- Lower order value per transaction
- Less close relationship
- Demand products for personal consumption



B2B

- Smaller number of customers
- Higher order value per transaction
- Focus on long-term relationships
- Demand products based on end-consumer needs



5 FUNDAMENTAL DISCIPLINES AS THE PILLARS OF CUSTOMER PORTFOLIO MANAGEMENT

To achieve success in Portfolio management, a brand must rely on 5 tools and disciplines:

- **Market Segmentation**
- **Sales Forecasting**
- **Activity-Based Costing - ABC**
- **CLV**
- **Data Mining**



MARKET SEGMENTATION

The process of dividing a market into subgroups that share similar needs.

SALES FORECASTING

Predicting future trends to identify which customer segments will become strategically important.



ACTIVITY-BASED COSTING - ABC

A cost accounting system that identifies and allocates indirect costs to products, services, or customers based on the actual activities that generate those costs.

CLV

The calculation of the total net present value of profits expected to be received from a customer throughout the entire duration of their relationship with the business.



DATA MINING

The use of advanced statistical technical tools to find hidden relationships within large datasets in order to predict customer behavior.





STRATEGICALLY SIGNIFICANT CUSTOMERS - SSCS



THESE ARE THE PRIMARY TARGET GROUPS THAT DIRECTLY IMPACT THE SUCCESS AND LONG-TERM VALUE OF THE BUSINESS, SELECTED THROUGH AN ANALYTICAL PROCESS TO IDENTIFY THE POTENTIAL TO ACHIEVE ORGANIZATIONAL GOALS. ACCURATELY IDENTIFYING THESE GROUPS HELPS BRANDS CHOOSE TO DELIVER OFFERS AND RELATIONSHIP MANAGEMENT STRATEGIES SUITABLE FOR EACH TYPE OF CUSTOMER, CATEGORIZED INTO 5 IMPORTANT GROUPS AS FOLLOWS:



High Future Lifetime Value Customers

These are the customers who are the 'core heart' of long-term growth. The company anticipates they will generate substantial profits through consistent repeat purchases, with high potential for higher-value purchases (Up-selling) or a greater variety of products (Cross-selling). Therefore, businesses must prioritize maintaining relationships with this group to ensure future revenue stability.



STRATEGICALLY SIGNIFICANT CUSTOMERS - SSCS



High volume customers

These are customer groups that focus on massive purchase quantities. Although the profit per unit may not be as high as other groups, their importance lies in helping create "Economies of Scale," which reduces the production cost per unit. This provides the company with a competitive advantage and strong total sales.

Benchmark customers

These are "model" customer groups that the company uses as case studies or references to build market credibility. The success in product usage or the satisfaction of this customer group serves as a testimonial that helps motivate new customers to make buying decisions more easily. While this group may not generate the highest profit, they hold immense value in terms of marketing strategy and brand image building.





STRATEGICALLY SIGNIFICANT CUSTOMERS - SSCS



Inspirations

These are customer groups that serve as "essential consultants" by reflecting on problems, providing deep insights, or suggesting new functions that the market demands. Information from this group helps the brand develop various innovations and improve services accurately. While this group may not generate the most monetary profit, they possess immense value as a source of ideas that help the business grow and stay ahead of competitors.



Door openers

These are customer groups that help the brand reach new customers or markets that were previously inaccessible. Although they may not generate profit or might even incur a loss in the short term, they hold very high strategic value as a "gateway" that allows the business to learn about new consumer behaviors and build a reputation to expand the customer base on a larger scale in the future.

THE CUSTOMER MANAGEMENT STRATEGIES

This is a crucial step that transforms data analysis results into actual practice, focusing on designing different customer care methods tailored to the values and behaviors of each customer group in the portfolio. Selecting targeted strategies helps businesses manage resources cost-effectively and build a sustainable competitive advantage.

The main strategies for customer management are as follows:

- **Protect the relationship**
- **Re-engineer the relationship**
- **Enhance the relationship**
- **Harvest the relationship**
- **End the relationship**
- **Win back the customer**
- **Start a relationship**





PROTECT THE RELATIONSHIP



This is a strategy for 'highly guarded' customer groups or those with high value and strategic importance, who are often the primary targets that competitors attempt to poach. Therefore, the company must employ proactive measures, such as providing premium exclusivity, exceptional personalized service, or creating long-term commitments to prevent customers from switching to competitors.

RE-ENGINEER THE RELATIONSHIP



This is a 'turning loss into profit' strategy, focusing on reducing the cost of service for customers with low purchase volumes or those who are not cost-effective. For instance, transitioning from staff-based care to automated systems or online services to lower operational expenses until the profit margin from this customer group becomes positive and more worthwhile for the business.





ENHANCE THE RELATIONSHIP



This is the 'increase spending from the existing customer base' strategy, focusing on expanding purchase value through two primary methods: Upselling (encouraging the purchase of higher-end or more premium models) and Cross-selling (offering related products that complement usage). The goal is to increase the share of the customer's wallet and strengthen the bond to make it harder for competitors to penetrate.

HARVEST THE RELATIONSHIP



This is the 'maximize returns' strategy at a point where the relationship has reached saturation. The company will focus on generating the maximum possible cash flow and net profit from this customer group without making additional investments in building new relationships or engaging in costly marketing activities. It is suitable for groups whose future value is expected to no longer increase, or those likely to defect to competitors, ensuring the brand gains the final maximum benefit cost-effectively.





END THE RELATIONSHIP

This is the 'termination of customer' strategy, which is necessary when a customer has no potential for profitability and no strategic importance in the future. Although it may contradict the sentiments of the sales department, ending this relationship helps the brand stop wasting resources and reduce sunk costs, allowing those resources to be redirected toward managing higher-potential customer groups.

WIN BACK THE CUSTOMER



This is the 'relationship recovery' strategy for customers who have stopped using the service or switched to competitors. The company must selectively win back only those who are Strategically Significant Customers (SSCs). The key is to conduct a 'Win-back Audit' to identify the root causes of their departure, such as service issues or pricing, and then provide targeted offers to incentivize their return. This is because winning back former customers who are already familiar with the brand typically incurs lower costs than acquiring entirely new customers.





START A RELATIONSHIP

This is the 'identifying and converting prospects into actual customers' strategy, focusing on screening only those with the potential to grow into key customers or generate high profits in the future. Once targets are identified, the brand must create an attractive plan to stimulate the first purchase and lay a strong foundation for the relationship, in order to further develop them into loyal customers and generate maximum customer lifetime value (CLV) in the long run.

Q & A

