

Customer Equity Management By George Yang Yong

The basic premise of customer equity is straightforward: Your customer is a financial asset that your company or organization should measure, manage, and maximize, just like any other asset. Customer equity is more directly related to the bottom line in the financial statement than any other business parameter such as brand value and equity, product portfolio and proprietary technologies, etc., and should be maneuvered to maximize the contribution. Meritus considers customer equity management to be the foundation of a truly customer-centric focused organization and strategy.

Customer equity management is a dynamic, integrated marketing system that uses financial valuation techniques and data about customers to optimize acquisition, retention and opportunities to sell additional products and services to a firm's customers. This in turn maximizes the value to the company of the customer relationship throughout its life cycle. Although many of the concepts that underlay customer equity management, such as customer retention marketing and customer lifetime value measurement, are not new, the way that a true customer equity approach unifies and moves beyond them, is innovative.

In the last two decades, managerial trends have tended to focus on either cost management or revenue growth. Customer equity management balances the two, creating market-based growth while carefully evaluating the profitability and ROI of marketing investment.

But customer equity management is more than just a method for calculating the asset value of customer relationships. It is a total marketing practice and system and requires integrative business strategies. Firms will need to develop strategies that simultaneously manage products and customers throughout the customer life cycle and that reframe brand and product strategies within the context of their efforts toward customer equity. In addition, customer equity framework changes the way a business allocates resources and efforts. Today, most marketing functions allocate resources by product line but with a customer orientation, the customer life cycle determines how managers distribute resources. Companies that adopt customer equity management also need to build organizations, processes, and performance measures that work together to maximize customer asset value.

A North American investment brokerage firm, Charles Schwab, offers an excellent example. In its early days, Schwab focused on customer acquisition by providing self-reliant investors with a value-priced alternative to full-service brokerage houses. The company invested little in understanding its customers' needs and wants at anything beyond the aggregate level. Its competitors used to know more about Schwab's customers than Schwab did. Later, in response to competitive pressures, Schwab began to apply the two other levers of customer equity: add-on selling and retention. It expanded its offerings to develop multiple relationships with customers who stay longer with Schwab. Schwab's OneSource mutual fund marketplace provided a multi-branded alternative that appealed to more investors than did the single-branded mutual fund offerings of brokerage houses and investment companies. Schwab outflanked the competition by creating a "best of breed marketplace" that gave unbiased access to the funds of multiple providers. The firm captured a higher share of customers' investment assets and raised retention rate.

There are two fundamental reasons for companies to move to a customer equity management approach. First, several critical new technologies are converging to make customer asset-based management feasible. This approach is possible in part because of intersecting advances in four areas: affordable information technology, low-cost communications, sophisticated statistical modeling and flexible fulfillment.

Customer equity management depends on technology because it requires the ability to build and use databases of customer purchases. Computing costs are continuing to decline to the point that even small businesses can have computing power sufficient to manage large databases at a fraction of what it would have cost in the 1980's. The ability to work with large, sophisticated databases is improving; software to manage customer relationships now exists, and its capabilities are expanding.

The rapid growth of the Internet as a medium for targeted communications allows firms to reach and communicate with customers at less than one-hundredth of the cost of more traditional techniques. Using direct marketing through the mail costs anywhere from 0.4 to 1\$ per piece, whereas communication through the Internet to customers equipped with email is virtually free; the speed of transmission allows customers to retrieve communications almost instantaneously.

Firms have access to their preferred customers at costs that early direct marketers could only dream about. Combined with an unprecedented ability to tailor messages to individual recipients and provide electronically driven lead generation techniques and offers to selected prospects, more traditional methodology is being surpassed in lieu of these techniques.

In addition, technologies ranging from POS at checkout and other scanning or information storage such as RFID to Internet cookies are making it increasingly possible to track customers' buying behaviors. Companies now have the opportunity to predict future consumer behavior using the best possible indicators. Instead of relying on focus groups and surveys to ask customers what they want - or think they want - firms can examine actual historic purchase data and use advanced analytical tools to turn the data into insight.

Enterprise IA systems, data warehousing, and data marts which facilitate statistical modeling and computing in the form of software, have been created to help enterprises integrate, mine and analyze data. There always seem to be opportunities to identify hidden insights and automatically feed back in the form of dashboards or score cards to all decision makers on a real-time basis. Having noted this, the often finite nature of pre-formatted software solutions is also evolving and companies have more flexible options to handle complex data mining and analytics, primarily by building the capability internally or outsourcing.

Data mining, analytics and management through a Knowledge Process Outsourced model is now and will continue to evolve as a benefit to the business and as a way to focus on real customer equity management. There are many benefits to choosing KPO, the first and most obvious being a lower average fixed cost of service delivery by a KPO provider and Centre of Excellence. This exists not only in terms of the talented and specially trained professionals but also in the cost savings represented by not making a capital investment in a Centre of Excellence.

Second, companies can get immediate access to best-in-class technologies and first-rate expertise. Trained and experienced statisticians, econometricians and highly trained analysts with domain expertise can be hard to come by in many markets and outsourcing generally provides a cost and human resources relief.

Third, companies can fully focus on its core business management while leveraging on partners' capabilities through a KPO model to facilitate customer equity management practices and implementation.

The second compelling and always evolving reason for companies to move to this approach involves not only these same technological capabilities, but also changes in how markets work in today's turbulent business environment. Proliferation of media, segments and consumers alone are making it a requirement to manage marketing to maximize the value of companies' customer assets in order to maximize shareholders' equity.

Organizations that use customer equity management as an acknowledged and strategic marketing practice and system benefit because they can do the following:

- Compute the asset value of customers to make informed decisions regarding investments in acquisition, retention, add-on selling as well as manage and recover valuable attritions
- Adjust marketing investment levels as customer relationships move through their dynamic life cycles
- Organize processes and structures around acquisition, retention, and add-on selling to maximize the profitability of each over the customer life cycle
- Utilize customer interactions to reinforce relationships and acquire new customers
- Address the needs of segmented customers through tailored offering of services and products

Managing the customer as an asset is more critical to a firm's success than ever before for three reasons. First, marketers who take an asset-based view of the customer make better decisions than those who limit themselves to product, brand, or transaction views. Second, today's computing technology makes precise customer asset management possible. Companies can now efficiently obtain and process the information they need to understand customer equity. Finally, changes in market conditions, driven by advances in information systems, communications, and production, will help companies that understand and manage the value of each individual customer to overtake, and then displace, mass marketers.

Once the concept of maximizing customer asset value is pointed out, it seems obvious. Yet most firms do not act as if they consider customers as assets. Instead they maximize product line or transaction profitability. Product-line maximizers use traditional accounting measures and product management as tools. By focusing on product and transaction profitability to the exclusion of customer asset value, they often increase near-term profits but forfeit longer-term prosperity.

A look at General Motors's strategy in the late 1980s helps to show the difference. The goal of GM's management was to increase short-term profits and shareholder returns. Based on financial analyses that showed small cars were relatively unprofitable, they de-emphasized small cars in the product line in favor of larger, more profitable vehicles. Not surprisingly, the strategy worked. GM's profits showed immediate improvement. At the same time GM was pruning its product line, however, Japanese automakers were offering smaller, higher-quality, lower-priced cars than GM, and importantly, as a mechanism for acquiring young first-time buyers. When these same customers began to purchase larger cars as they evolved through the customer life cycle, they continued to buy Japanese cars.

GM inadvertently created a generation of young American consumers who grew up buying Japanese and German cars. GM did not practice customer equity management, but even at low profits, the sale of high-quality, low-priced car was critical to its long-term franchise value. It lost sight of the importance of and linkage between, customer acquisition and customer retention in the automobile business. GM's product management strategy led to a decrease in its market share of approximately 15% over twenty years.

Managing customers as assets requires measuring, managing, and maximizing. Managing what is measured becomes easier because decisions are no longer opinion based but fact based. With analytical tools around customer equity management, marketers can not only quantify and qualify key drivers but also predict the impact of all factors affecting the future direction of the business. In addition, marketers know better where and how much to invest marketing dollars in order to capture profitability at each stage along customer acquisition, retention, add-on selling and attrition management, and consequently the ROI of the investment in marketing mix is maximized.

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