

**MK282**  
**Customer Relationship Marketing**  
 Lecture Nine  
 Customer Equity Management  
 Dr. Paurav Shukla

### Why customer equity management (CEM)?

- Scenario 1
  - The chief marketing officer (CMO) of an automobile firm is faced with a dilemma: invest £2 million to develop a frequent user programme to reduce customer churn, or spend £2 million to improve customer service support through the company's web site and its toll-free number. Which investment will bring it the greater return?
- Scenario 2
  - The CMO of a leading apparel firm is considering reducing prices by 5% across the board but eliminating in-store sales and price promotions. How can this executive determine if this is the best use of firm's marketing resources?

### Why customer equity management?

- The goods to service shift
- Transaction to relationship shift
- Marketing products to managing customers shift
- Linking customer management to financial returns

Vargo, S. and R. Lusch (2004), Evolving to a New Dominant Logic in Marketing, *Journal of Marketing*, 68 (1), 1-17.  
 Berger, P., Bolton, R., Bowman, D., Briggs, E., Kumar, V., Parasuraman, A. and Terry, C. (2002), Marketing Actions and the Value of Customer Assets: A Framework for Customer Asset Management, *Journal of Service Research*, 5 (August), 39-54.  
 Rust, R., Lemon, K. and Zeithaml, V. (2004), Return on Marketing: Using Customer Equity to Focus Marketing Strategy, *Journal of Marketing*, 68 (1), 109-127.

### Key challenges to marketing managers

- What is the best way to attract new customers?
- How to keep current customers happy and make sure they don't switch to the competitors?
- What is most important to the customers?
- How to know which customers are the most important customers?
- How to build the business without resorting to endless price promotions?

### The probable solution

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  graph TD
    A[Corporate strategy] --- B[Marketing strategy]
    B --- C[Customer strategy]
    A --- S1[Strategic]
    B --- S2[Tactical/strategic]
    C --- S3[Tactical/strategic]
  
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### CEM framework

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  graph TD
    A[Customer Analysis] --> B[Firm & Competitor Analysis]
    B --> C[Strategy development & Design]
    C --> D[Measure, Monitor & Evaluate]
    D --> A
  
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## What is customer equity?

- The total of the discounted lifetime values summed over all of the firm's current and potential customers.

Blattberg, Robert and Deighton, John (1996), Managing Marketing by the Customer Equity Test, Harvard Business Review, 75 (4), pp.136-44.

## Exercise I

- Think of a product or service that you purchase or pay for regularly (e.g. Mobile phone, mobile phone plan, groceries, fast food, airline tickets). Estimate how valuable you are as a customer to the firm.
  - Consider in your estimate:
    - How often you purchase,
    - The monetary value of each purchase,
    - How likely are you to continue purchasing this product or service,
    - The firm's approximate cost of having you as a customer.

## The customer equity approach

- A brand manager's dilemma
  - How do I manage a brand?
  - How will my customer react to changes in the product or service offerings?
  - Should I raise prices?
  - What is the best way to enhance the relationships with current customers?
  - Where should I focus my efforts?
- These questions (and many others) can be broken down into three categories

## The customer equity approach

- Value equity
  - Customer's objective evaluation of the firm's product and/or service offerings
- Brand equity
  - Customer's subjective evaluation of the firm's product and/or service offerings
- Relationship equity
  - Customer's view of the strength of the relationship between the customer and the firm

Gale, B. (1994), *Managing Customer Value*, New York: The Free Press.  
Parasuraman, A. (1997), Reflections on Gaining Competitive Advantage Through Customer Value, *Journal of Academy of Marketing Science*, 25 (2), 154-61.

## The equity drivers

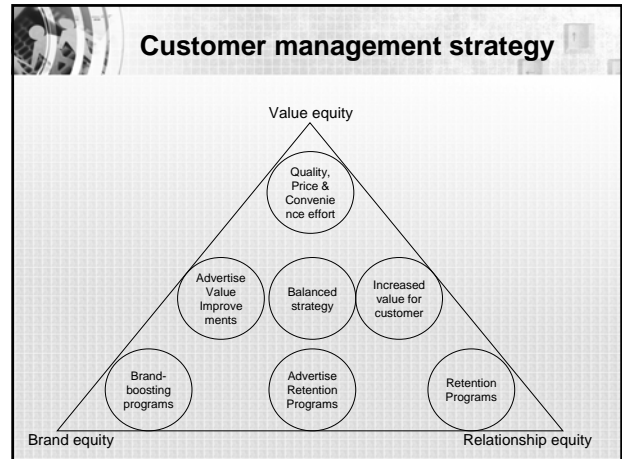
- Value equity
  - Quality
    - Encompasses the tangible and intangible aspects of the product and service offerings under the firm's control
  - Price
    - Represents the aspects of 'what is given up by the customer' that the firm can influence
  - Convenience
    - Encompasses those actions the firm can take to reduce the customer's costs and efforts in doing business with the firm

## The equity drivers

- Brand
  - Acts as a 'magnet' to attract new customers
  - Serves as a reminder
  - Customer emotional tie to the firm
- Brand equity
  - Brand awareness
    - Encompasses the tools under the firm's control that can influence and enhance the brand awareness such as marketing communications
  - Brand attitude
    - Encompasses the extent to which the firm is able to create close connection or emotional ties with the customer
  - Corporate ethics
    - Encompasses the actions the firm can take to influence customer perceptions of the organization

## The equity drivers

- Relationship equity
  - Customer's tendency to stick with the brand, beyond objective and subjective assessments of the brand
- Loyalty programmes
  - Encompass the set of actions that firms may take to reward customers for specific behaviours with tangible and intangible benefits
- Affinity programmes
  - Create strong emotional connection with customers, linking the customer's relationship with the firm to other important aspects of customer's life
- Knowledge building programmes
  - Create structural bonds between the customer and the firm creating an exit barrier



## Customer management plan: Analysis

1. Analyzing the market
  - a. Determine the key drivers (and sub-drivers) of customer equity for the chosen market
2. Analyzing the firm's performance
  - a. How is the firm doing in terms of customer equity and in relation to the competitors
    - i. How is the firm doing on all drivers?
    - ii. How is the firm doing on the key drivers (those most important to customers)?
      - a) Where are the necessary points of parity (on what attributes do you have to be 'good enough')?
      - b) Where are the opportunities for differentiation (Where can the firm really shine?)
    - iii. What portion of the customer equity share does the firm hold in the market? What points do the competitors hold?

## Customer management plan: Analysis

3. Comparing firm's performance to that of competitors
  - a. Analyze the past and intended future behaviour of the customer of both the firm and its competitors in the market
  - b. By examining the switching matrix, determine if:
    - i. Customers are switching from the firm to the competitors (bad indicator)
    - ii. Customer are switching from the competitors to the firm (good indicator)
    - iii. Customers are staying with the firm and the firm has a high share of retained customers (good indicators)
    - iv. Customers are staying with the competitors and they have the high share of retained customers (bad indicator, or indicator of key opportunity)
4. Determining where to focus your efforts
  - a. Given the examination in first 3 sections of analysis
    - i. Determine key weaknesses to overcome
    - ii. Determine key opportunities to exploit

## Customer management plan: Strategy development & design

5. Given the analysis above, determine key priorities and where the analysis suggests key resources should be invested
6. Determine the appropriate mix of customers and appropriate target customers. Particularly if the firm determines it needs to gain additional customers from the competitors, it needs to determine which customers to select

## Customer management plan: Strategy development & design

7. Given the appropriate set of current and target customers the firm needs to determine where the maximum ROI would come from:
  - a. Improving brand equity
    - i. Firm needs to focus on brand building strategies and managing brand equity
  - b. Improving value equity
    - i. Firm needs to focus on value building strategies and managing value equity
  - c. Improving the relationship equity
    - i. Firm needs to focus on managing relationship equity, relationship building strategies and relationship touchpoints and personalization

### Customer management plan: Measure, monitor & evaluate

8. Once the firm has determined the appropriate customer mix and the key actions to grow long-term profitability, it needs to measure and monitor the results
9. If necessary, utilize appropriate CRM software that will enable the firm to collect the appropriate data to measure and monitor the success of customer management efforts
10. On a recurring basis, analyze the key drivers and sub-drivers of customer equity and determine the firm's performance relation to the critical (and rising) competitors

### Case 1: A large electronics goods supplier

1. What is most important to customers in this market?
  - a) Component: Value equity
  - b) Driver: Quality
  - c) Sub-driver: Physical product
2. How is the firm doing on those aspects that are most important?
  - a) Value equity: Not very well
  - b) Quality: Not very well
  - c) Physical product: Not very well
3. How are the competitors doing on those important aspects?
  - a) Competitor 1: Not very well
  - b) Competitor 2: Very well (worrying point)

### Case 1: A large electronics capacitors supplier

4. What must we do at least as well as our competitors (points of parity)?
  - a) We must perform as well as (or better than) our competitors on those aspects that are most important to the customers in the market (e.g. physical product quality)
5. On what aspects do we need to do better than our competitors?
  - a) We may want to perform better than our competitors on those aspects that are important to customers, but not the most critical element (e.g. service products, corporate ethics, knowledge building)
6. What key weaknesses must we overcome?
  - a) Improve on value: We must improve on the driver of quality and, in particular the sub-driver of physical product.
  - b) Improve on relationship: We should improve on the knowledge-building driver and appropriate sub-driver that are important to the customer in this area.
7. What, if any, opportunities for differentiation do we see?
  - a) Possibilities: service product, price, convenience, or knowledge-

### Case 2: At United, Food is Uniting the Airline With Travelers



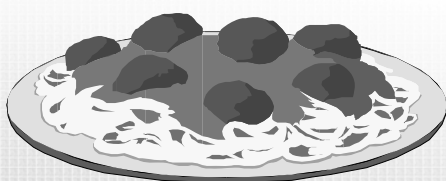
United Airlines, as other major airlines, had to deal with passenger loyalty (management decision problem: how to attract more and more loyal passengers).

The basic answer is to improve service. Exploratory research, theoretical framework, and empirical evidence revealed that the consumers' choice of an airline is influenced by: safety, price of the ticket, frequent-flyer program, convenience of scheduling, and brand name.



A graphical model stipulated that consumers evaluate competing airlines based on factors of the choice criteria to select a preferred airline. The problem was that major airlines were quite similar on these factors. Indeed, "airlines offer the same schedules, the same service, and the same fares." Consequently, United Airlines had to find a way to differentiate itself. Food turned out to be the solution.





Secondary data, like the J. D Power & Associates' survey on "current and future trends in airline food industry", indicated that "food service is a major contributor to customers' loyalty". This survey also emphasized the importance of food brands.

The airline's Marketrak survey told United Airlines that "customers wanted more varied and up-to date food."

The following research questions and hypotheses may be posed.

RQ1 How important is food for airline customers?

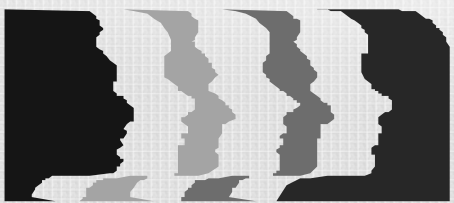
H1: Food is an important factor for airline travellers

H2: Travellers value branded food

H3: Travellers prefer larger food portions, but with consistent quality

H4: Travellers prefer exotic food

Characteristics which influence the research design included the identification of competing airlines (Delta, American, etc.), factors of the choice criteria (already identified), measurement of airline travel and loyalty.



This kind of research helped United Airlines to define their problem, and develop the approach. Focus groups and surveys were conducted to check customers' perceptions of food in United Airlines' aircraft. The results provided support for all the hypotheses (H1 to H4). United Airlines then made a few changes: new "culinary menus," larger portions of food, new coffee and branded products (e.g., Godiva chocolates). This resulted in better service, increasing customer satisfaction and fostering loyalty.

