



## What is Customer Lifetime Value (LTV) And Why Do I Need to Know About it?

The lifetime value of a customer is the net profit that you will receive from transactions with a given customer during the time that this customer continues to buy from you. Some customers buy once and disappear forever. Their lifetime value is the profit on that one transaction. Others keep coming back, again and again.

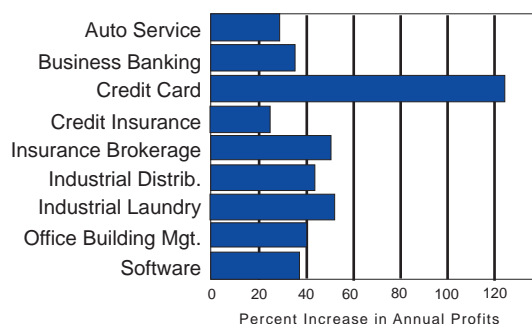
The lifetime of a customer varies across industries. For example insurance companies' customer relationships can cover several decades, while the life of a customer relationship with the local newsstand might last 8 years (equivalent to the period of time that the customer resides in that neighborhood). Calculating this value and monitoring its changes is critical to the success of your marketing ventures.

### Why Do I Need to Know?

Lifetime value naturally leads to the subject of customer retention. Studies show that small increases in customer retention can drive substantial increases in profitability. Studies also show that the value of customer relationships grow over time, consequently company profits increase too.

Consider this information on customer retention and profit from Bain and Company:

**Figure 1. Increased Profits From Retention Increase**  
Profit Improvement from 5% Increase in Retention



Source: Bain & Company



Remember, what you are looking at here are INCREASES in profit from a relatively small increase in customer retention. Knowing your Customer LTV and monitoring its variations can help you plan and execute programs which will improve retention and grow LTV.

"Getting" the customer is an investment and may not show a profit--immediately. Rule of thumb: It costs, on average, 5 times more to sell to a new customer than to an existing customer. In other words, it costs 80% less to sell to existing customers. Powerful words! Knowing and tracking your customer LTV will help you to gauge whether your marketing programs are producing the type of customers who will contribute to your company's profitability.

Satisfied, established customers:

- Generate regular, recurring revenue
- Are receptive to cross-selling
- Take less time and expense to service
- Know how to find you and your products
- Are advocates for you with their friends
- Are less likely to expect discounts



Measuring customer LTV helps to build, justify, test, and measure the value of key strategic activities such as:

- Loyalty programs
- Customer retention campaigns
- Customer referral programs
- Customer service plans
- Marketing Communication Programs based on Database (Customer) Segmentation

Why is this so important? Because, for example, if you know that each customer will bring you \$38 profit over a two year period, then you can afford to break even or even lose money on the first sale in order to acquire the customer, since you know that on average you'll make it up later.

Until you identify and understand exactly how much combined profit a client represents to your business for the life of that relationship, you can't begin to know how much time, effort, and, most importantly, expense you can afford to invest to acquire that client in the first place.

Once you know your Customer Lifetime Value, you'll know how much you can afford



to spend -- or lose -- to get that first sale. And that knowledge is priceless. I'm convinced that this one single fact -- the lifetime value of your customer -- is absolutely vital to an intelligent marketing campaign. Without this knowledge, you're shooting in the dark; with this knowledge you'll be willing to take the short term risks necessary to in order to achieve long-term gain.

## Customer LTV is Just One Part of Your Total Marketing Program

Knowing and monitoring your customer LTV is critical, but it's only one part of an effective marketing program. Since 1988, The Mecham Company has been helping business to business marketers get more from their marketing efforts. Call us for a complete picture of how we can help you improve your marketing results.

For Marketing that Increases Your Customer Value . . .

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(509) 922-0535

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