

Calculating Customer Lifetime Value Exercises

Task and Introduction to CLV

In this activity you will be completing and checking various customer lifetime value calculations (CLV/CLTV).

But firstly, let's recap what customer lifetime value is and why it matters in marketing...

Customer Lifetime Value (CLV) is a marketing metric that measures the long-term value that a customer brings to a company over the course of their relationship.

That is, CLV tells you how much money a customer is likely to spend on your products throughout their entire relationship with your company and estimates how much profit you will generate from that one customer.

By measuring CLV, as a marketer you can:

- Identify high-value customers
- Know how much to spend on customer acquisition
- Know how much to spend on customer loyalty (retention)
- Measure the overall success of your marketing strategies

As a reminder, here is the CLV formula for a customer:

- $CLV = \text{Profit per year} \times \text{Number of years as a customer (lifetime)} - \text{customer acquisition costs}$

Note: Professional firms would also include a discount rate to calculate net present value of CLV, but we will not be doing that in this task.

Let's work through an example. Let's assume that we own and run a movie cinema.

We have worked out that my using discount coupons distributed locally that it costs us \$50 to acquire a new customer - that's our customer acquisition cost.

We have also worked out that the average come comes to our cinema 10 times per year and, on average, they spend \$25 on the movie ticket and a drink and snacks. But after all our variable and fixed costs, we make \$15 for each customer visit.

That means that each year we make \$150 profit from the average customer. (Note: \$25 revenue less \$10 costs = \$15 profit per visit X 10 visits per year).

We also know that, on average, we have an 80% retention for our customers. That means that year after year, 80% of our customers continue on as customers. That allows us to work out the length of each customer's lifetime for CLV.

We do that by first working out the churn (or loss) rate of our customers - which is 100% less our retention rate of 80% = 20%. This means that we lose 20% of customers per year.

And we can use the churn rate % to tell us how many years our average customer stays by dividing 1/churn rate. In our case that is $1/20\% = 5$ years = customer lifetime.

So let's now put it all together to calculate our CLV.

- $CLV = \text{Profit per year of } \$150 \times \text{Number of years as a customer (lifetime of 5 years) less customer acquisition cost of } \50
- $CLV = \$150 \times 5 \text{ less } \50
- $CLV = \$750 \text{ less } \$50 = \$700$

That means for every customer we acquire, we will make \$700 profit (on average) from them over time.

CLV Calculation Exercises

Now that you have worked through the above example, it's your turn to help with the following CLC calculations. We will start off easy and then get progressively a little harder.

In each scenario we will be using the example of a supermarket chain. All references and numbers used are for the "average" customer.

CLV Scenario 1

A supermarket chain ran a radio and outdoor advertising campaign and they got lots of new customers at an acquisition cost of \$500 per customer.

These customers visited the supermarket 50 times a year. Each customer spends \$150 per visit and the supermarket makes a 5% profit margin on the customer's spend.

The retention rate of the customers is 75%.

What is their CLV?

CLV Scenario 2

A supermarket chain ran a social media campaign and they got 2,000 new customers. The TOTAL cost of the campaign was \$250,000.

These customers visited the supermarket 25 times a year. Each customer spends \$100 per visit and the supermarket makes a 4% profit margin on the customer's spend.

The retention rate of the customers is 60%.

What is their CLV?

CLV Scenario 3

A supermarket chain ran a discount coupon campaign. It cost them \$45,000 to print and distribute the coupons. 750 new customers redeemed the coupons and received a \$40 discount on their first visit (which is part of the customer's acquisition cost).

These customers visited the supermarket 40 times a year and spent \$200 per visit, but this supermarket only makes a 2% profit margin on the customer's spend.

But the retention rate of their customers is 90%.

What is their CLV?

Note: Assume that the profit margin is based on the customer's non-discounted spend, then deduct the discount.

CLV Scenario 4

A supermarket chain ran a multi-media campaign. This included online advertising at a total cost of \$25,000, plus local billboard ads of \$35,000, plus a discount offer for new customers of \$50 each, plus the sponsorship of an influencer of \$15,000.

They were able to generate 300 new customers as a result.

These customers visited the supermarket, on average, 5 times a month and spent \$100 per visit. This supermarket makes a 5% profit margin on the customer's spend.

And to help with retention the store offered a special discount coupon of \$50 per year per customer as well.

The retention rate of their customers is 50%.

What is their CLV?

Note: Assume that the profit margin is based on the customer's non-discounted spend, then deduct the discount.

CLV Scenario 5

This supermarket chain ran a "refer-a-friend" new customer offer, where existing customers entice their family and friends to become customers of the store. This resulted in 100 new customers. Both the existing customer and the new customer received a \$50 one-off discount.

These new customers visited the supermarket, on average, 3 times a month and spent \$75 per visit. This supermarket makes a profit margin of \$4 per \$100 of the customer's spend.

And to help with retention the store offered these new customers a further special discount coupon of \$20 per month as well.

The retention rate of their customers is 2/3rds.

What is their CLV?

Note: Assume that the profit margin is based on the customer's non-discounted spend, then deduct the discount.

CLV Scenario 6

The same supermarket chain as in Scenario 5 keeps running their a "refer-a-friend" new customer offer as above, which results in 100 new customers and both the existing customer and the new customer receive a \$50 one-off discount.

But to help with retention the store decided to NOW offer these new customers a further special discount coupon of \$5 per visit.

As a result, these new customers now visited the supermarket, on average, 3.5 times a month and spent \$90 per visit. This supermarket still makes a profit margin of \$4 per \$100 of the customer's spend.

And their retention rate of their customers increased to 70%.

What is their CLV? Did they improve?

Note: Assume that the profit margin is based on the customer's non-discounted spend, then deduct the discount.

CLV Scenario 7

The same supermarket chain as in Scenarios 5 and 6 keeps with their a "refer-a-friend" new customer offer as above.

But NOW they decided to offer only these new customers a further special discount coupon of \$5 per visit - for the first year only!

As a result, these new customers now visited the supermarket, on average, only 3 times a month but spent \$120 per visit - for the FIRST year.

But in the second year and onward, because they were no longer getting the discount - their behavior became 2.5 times a month spending \$110 per visit.

While the supermarket still made a 4% profit margin of \$4 per \$100 of the customer's spend, their retention rate of these customers fell to 60%.

What is their CLV? Did they improve?

Note: Assume that the profit margin is based on the customer's non-discounted spend, then deduct the discount.