CAPITAL SOLUTIONS

If you don’t do ANYTHING else today, do the following…

1. **Calculate the lifelong value of your average customer**
   This number is a KEY piece of information to decide – amongst other things – how much to spend on acquiring a new customer. All companies, from GM to the corner lemonade stand, profit as well as non-for-profit, have to think about this.
   (Page 2 gives details on how to actually calculate it)

2. **Grow your bottom line, exponentially**
   Single digit Gross Margins are a curse (unless you are selling millions of ‘widgets’ – like Proctor & Gamble - or providing millions of transactions, like eBay). Your bottom line will grow exponentially if you do any of the following (include #7 below):
   a. Consider spending more to acquire new customers (see item #1 above);
   b. Implement clever incentives to keep your customers longer;
   c. Increase your Gross Margin;

3. **Figure out which customers represent 80% of your sales**
   What have you done for them lately? Do you know: what their specific interests are? Wedding anniversary? Childrens’ birthdays? When was the last time you took them to a football/baseball game?

4. **If one or two customers make up more than 60% of your revenue, pretend you lost them today**
   Go into ‘Red Alert’. Drop every other project that is not related to diversifying your customer base…immediately (remember…’today’s laurels are tomorrow’s compost’).

5. **Do not neglect the Internet**
   It has changed forever the way buyers meet sellers; figure out ways to increase the size of your marketplace. Learn to embrace change: take a seminar, hire good talent, become the first one of your colleagues to be out there with a great web site or a new marketing strategy.

6. **Name one breath-taking project you are working on**
   What will it do for your company if you actually do ‘hit it out of the park’? Which brings me to the obvious question…How many hours did you ‘invest’ in the project in the last week? What have you done about it today?

7. **Regularly review your overheads with a very critical eye**
   See what can be outsourced and transformed into a variable cost instead.

CAPITAL SOLUTIONS

How to Calculate the Lifelong Value of a Customer

To calculate the lifelong value of a customer, you need to know 3 variables:

Average 'Stay' of a Client: On *average*, how long do Clients stay with you. Of course, you will have customers that stay longer and others that stay shorter. If you want to make this very scientific, you can take a weighted average. If you want to make it practical, take a very conservative (lower) number of months or years.

Average Gross Margin: Again, you will have customers that allow you a higher gross margin and customers where your sales to them are 'tighter'. Same as above, take an average and err on the side of caution (lower Gross Margin). More importantly, only take the direct costs of producing the item. Example: if you sell a widget at $100 per unit, and your payroll ($30), materials ($15), utilities ($5) and sales commissions ($5) total $55, then your GM is $45 or 45%. Overheads (rent, administration salaries, etc.) typically remain constant no matter what your sales level is.

Sales: How much on average (again, be conservative) does this sample customer buy from you?

Real Life Example

A door knob manufacturer[1]. He has Clients that have been buying from him for 7 years, but with more comparison shopping brought about by the internet, he expects customers to stay with him only for 3 years. Regarding Gross Margin, he has a 35% Gross Margin with most of his customers. His average customer buys from him about $12,000 per year.

The average customer for this manufacturer is worth…

Gross Margin	x	Stay	x	Sales		
35%	x	3 years	x	$12,000	=	$12,600

How important is this information? It is incredibly important!

Say this company gets a quote for a new web site and some exposure. The quote includes $10,000 to produce the site and another $1,000 per month to promote it; total of $22,000 per year (you think "That is incredibly expensive!"). If a very conservative guestimate is that this effort is going to bring 4 new customers per month…should the manufacturer go ahead with the web site project?

Over one year, the manufacturer would get 48 new customers, which over their lifetime will produce $604,800 in new revenue. What is the cost of acquiring these 48 new customers? $22,000. So, should he spend $22,000 to get $604,800? His answer should be…."Of course!"

Note that…

- Without knowing the lifelong value of a customer, it would be impossible to decide whether an acquisition cost (advertising campaign, discounts or the like) is 'too much or too little'. Your "initial reaction" might make you miss out on great opportunities.
- You should regularly review your numbers and adjust them to changing circumstances, market conditions. If in doubt, make them very conservative (lower the Gross Margin, 'stay' and Sales; if anything, this will keep you safer).

[1] If your company is in the 'Services' industry, you will typically have less 'materials' (if any) and more 'payroll' expenses. The basic principles still hold: how much – on average – does a customer 'leave you' in their lifetime, after your pay for direct expenses related to delivering those services (mostly direct payroll).