Retail Profitability principles Mark 2

In the second of the Retail Rules series, Norrelle Goldring from GfK discusses customer lifetime value and product/price mix.

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In the previous article on our 'Retail Rules' series, we discussed two of four retail profitability measures, being GMROI (gross margin return on inventory) and sales/rent ratio. Here we're going to outline two more: customer lifetime value, and product/price mix.Gross margin return on inventory (GMROI): sales gained from money spent on inventory. Linked to velocity.

1. CUSTOMER LIFETIME VALUE

Understanding who your current customers are, what they are worth to you over the long term and how you can leverage this.

Shoppers are creatures of habit, and have a repertoire of stores for most categories. Often that repertoire is driven by the store that is closest to home, closest to work or on the way between the two (supermarkets, convenience stores and bottleshops are all examples of this). Stores with non-FMCG categories that have longer replacement cycles, such as appliances, still work on catchment area. That is, they are based out of a shopping centre or homemaker centre which, depending on size and retail offering, may have a shopper catchment area of up to 20km where shoppers will come from up to 20km from their homes.

All of this means that you are likely to have a combination of regular customers, infrequent customers, and some one-off customers. The regular and infrequent ones are the ones who are the biggest opportunity – for regular customers potentially increasing spend and possibly frequency, and the infrequent ones is about increasing frequency.

The frequency of visit combined with spend per visit (transaction), over their lifetime, is what is meant by customer lifetime value. If you're a convenience store a shopper may only spend $4 with you on a drink once or twice a week, but if they do that every week for a year then they're worth at least $200 in revenue to you over the course of that one year alone. Same with bottleshops. On average bottleshop buyers buy once to twice a week from the same store. Say they spend $20 per trip or $40/week. That's $2000 for one year. In appliances it's a sale across multiple categories. A shopper may be renovating a room, or their house, or moving house, or replacing multiple individual items across categories but at any rate theoretically they would be in the appliance store a couple of times a year.

It's easier and cheaper to get more sales out of your current customers than it is to find new ones and rely on passing foot traffic. This is why establishing a customer database and keeping a record of customer

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transactions – who they are and what they buy - is crucial, even for petrol and convenience, so you can market to them directly (typically via email or mobile).

2. PRODUCT/PRICE MIX

Getting maximum transaction value from your range.

Having the right product and price mix relates directly to who your shoppers are, and further who your most valuable shoppers are (this relates to Customer Lifetime Value, above). Whilst you need to appeal to a broad mix of customers, your range needs to skew to the products your most regular customers buy. This is related to GMROI – product margin x stock turn.

In some channels covering the range and price mix is presented as a 'good, better, best' or 'value, mainstream, premium' scenario. The trick then is your overall pricing strategy. It's not necessarily about being perceived to be cheapest versus competitors. As mentioned above, many of your shoppers will be repeat purchasers who choose you because of your location and your range. What they're looking for is perception of value, not just absolute cheapest price. And for some consumption and purchase occasions, particularly in liquor, it can be about more premium products with higher spend. Value perceptions come from a combination of convenience, range quality, customer service, instore experience and a number of other factors.

Different categories play different roles and thus require different pricing strategies. Pricing is a big topic with a number of strategies but the point here is to understand who is buying what types of products, what type of role each category plays (traffic, volume, profit/premiumise, impulse/incremental add-on etc) and therefore what your product mix and price strategy needs to be per category.

Next time we'll move on to the five retail growth objectives of traffic, penetration, AWOP, spend and frequency.

ABOUT NORRELLE GOLDRING & GFK

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