

ABSTRACT

Loyalty Myth #37:

Long Term Customers Purchase More

*In this excerpt from their book **Loyalty Myths**, the authors argue that there are many business sectors where this myth is, well, nonsense.*

The idea that long-term customers purchase more is a core tenet of the customer retention movement. The notion is, that like a fine cabernet, customers improve with age. Thought leaders such as Frederick Reichheld have marked this idea in executives' minds indelibly: "Across a wide range of businesses, customers generate increasing profits each year they stay with a company. Why? Return customers tend to buy more from a company over time."

This myth should be examined from two perspectives. One deals with the purchasing power of individual consumers over their temporal lifetimes. The other is a share of requirements explanation, which plays particularly well within an industrial, business-to-business context. (Share of requirements, share of spending, and share of wallet are all measures of the share of a customer's spending that a particular brand or marketer receives.)

The myth seductively dovetails with our basic understanding of the economics of individuals: earnings generally increase with age (until retirement, at least). Therefore, it would appear to make perfect sense that because wealth tends to increase with age, customers should buy more from a company over time.

Loyalty Myth #37 De-bunked!

Looking purely at individual economics with regard to this myth, however, consumption is probably a more important variable to examine. Although consumption of all goods and services does tend to increase with age, it is at a much less steep increase than that of earnings. And consumption is dispersed throughout all products and services purchased.

At the micro-level, it is highly unlikely consumers purchase more of a product or service over time. Most of us return regularly to our grocery stores, our telephone companies, our Internet service providers, our shoe stores, etc. Did we buy more food, telephone time, ISP services, or shoes simply because we returned? Obviously not. Need was the driving factor and controls our rate of consumption. There are many business sectors where this myth is nonsense.

Firms' customer bases are composed of a mix of customers who vary in the costs to retain them and their contribution to profits. We classify customers into three basic types by their profitability:

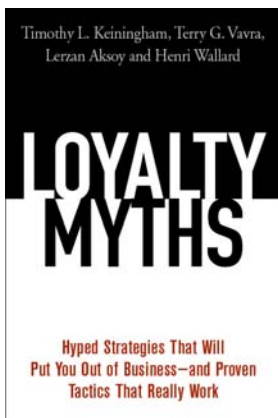
- 1) **Desired Customers:** those who generate substantial profits;
- 2) **Break-even Customers:** those who contribute a minimally acceptable rate of return (but can help businesses achieve a "critical mass"); and
- 3) **Costly Customers:** those who require such extensive servicing that they end up costing substantially more than they contribute to operating profits.

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For most businesses, a simple point-in-time analysis of all customers would reveal that “Desired Customers” (that is, those that are profitable) would generally be customers with longer tenures with a company. But, the longer tenure of desired customers is explained primarily because their counterparts, “Costly Customers” (e.g., unprofitable customers), are more likely to frequently switch vendors, thereby shortening their tenure. Therefore, the apparent higher value of customers with longer tenures is really an artifact. Desired Customers spend more from the beginning—their desirability did not improve over time.

In *Loyalty Myths*, business strategists and renowned authors Keiningham, Vavra, Aksoy, and Wallard reveal the ugly truth about customer loyalty: almost everything we have been told about it is wrong. Following the conventional wisdom that has been propagated about customer loyalty has, at best, led to misallocated resources; at worst, it is a recipe for financial disaster.

The pursuit of customer loyalty can be a highly profitable strategy, but not by following the myths that have developed. Our current knowledge of customer loyalty has advanced to the point of being able to identify the flaws in the conventional positions – the myths. More importantly, we can now establish and prove “loyalty truths” that we’ve associated with profitable customer loyalty strategies.



Praise for *Loyalty Myths*

by Keiningham, Vavra, Aksoy, and Wallard

“The book is a constant intellectual jolt as you realize that what you accepted as a truism is in fact quite shaky if not totally wrong ... overall it's an easy and pleasurable book to read, assuming your company hasn't made million-dollar investments based on the myths.”

Harvey Schachter
Globe and Mail (Toronto, Canada)

The Globe and Mail ranked *Loyalty Myths* Number 4 in its rankings of the best business books of the year.