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The CLV Revolution

The CLV Revolution: Transform your eCommerce with
Customer Value Optimization/Valentin Radu
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CHAPTER 1

The Path You're Following Is Incomplete

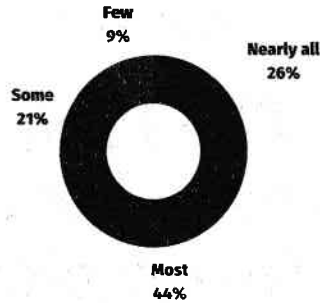


There are tons of books stating that a company's main source of growth comes from the decisions its leaders make. However, according to research by S&P Global, only 26 percent of companies state that nearly all of their decisions are data-driven.¹ If both of these statements are true, then where are nearly three-quarters of leaders getting their information, if not from data?

¹ Aslett, Matt: "Delivering Value from Data." 451 Research. <https://www.spglobal.com/marketintelligence/en/documents/sp-global-delivering-value-from-data.pdf>.

EXTENT OF DATA-DRIVEN DECISION-MAKING

To what extent would you say strategic decisions at your organization are currently 'data-driven'?



Source: 451 Research's Voice of the Enterprise Data & analytics 2H 2021 S&P Global Market Intelligence

Here is one reason why this is happening. Although most executives understand different ways growth happens and even have data to support their understanding, they can't always convey this important message across their organizations. These leaders get stuck trying to convince everyone else that these things matter. Like everything in business, to gain institutional adoption, you must have critical mass.

Leaders must act as agents of change in order to get other executives on board. Then, they must champion this message across all levels of the organization until enough people understand the rationale and buy-in to support their efforts.

Here is some bad news: Even when the CEO is the agent of change behind an initiative, if the rest of the organization does not align with the decision, adoption will be lacking, and the change will fail to take root.

For something to go from being one person's conviction and become a company-wide mandate, you must have facts, data, and a strong business case that shows why it matters.

Perhaps you find yourself in a similar situation. You are fighting organizational inertia, stuck in the land of chaotic reporting, conflicting KPIs, frustration, and painfully slow progress. It's time to get you out of that mess.

The Change is Already at Your Fingertips

Only a handful of traditional retailers have updated their thinking to leverage the new goldmine that is right at their disposal—customer behavior data. Their unwillingness or inability to change keeps them trapped in an old model that slows innovation, prevents agility, and makes it difficult to pivot toward new profitability. In order to change, they must adopt new ways to understand their customers and redefine their organizational understanding of what success really means.

The true path to discovering these new vistas begins with optimizing the customer journey. When companies do so, it's like hopping on a secret highway that bypasses traffic and gets them to their destination faster than they ever expected.

How Do You Measure Profits?

The simple e-commerce equation that most people use for profits reads like this:

$$\text{Profits} = \text{Revenue} - \text{Costs}$$

This equation is too simple to be actionable. Throughout chapter 1, I will unpack the variables (root causes) and fill in the gaps. In the process, I will take a much deeper look at the numbers that actually drive e-commerce revenue and success. First, let's talk about your business.

When things are going well, it can be difficult to pause, peel back layers of data, or spend extra time talking with customers. I know this from experience, especially after seventeen jobs and four businesses. In my early e-commerce days, when I was struggling to break even on my acquisition ad spend, I needed to pull my head out of the weeds and actually go talk with customers. Short of that, I needed to at least learn to put my ear to the data, so I could hear what it was saying. That's when I realized that a lot of what I was doing was wrong.

Whether you are a business owner or an e-commerce professional supporting someone else's business, take this to heart: Your business journey is tied to the journeys of your customers more than you realize. In fact, your business success is more about them than it is about you.

In e-commerce, there is always work to do and plenty of new things to learn. Perhaps you have found the key to actually driving traffic to your website. If so, congratulations. We should all be aiming as high as possible in our businesses. However, if you're aiming for the moon and you're off by even a fraction of a degree, you will miss your mark. Maybe that's why many of us never reach it.

Today's major digital networks and performance agencies have a vested interest. They know that the principles of Customer Value Optimization work in their favor. The more your company spends on ads, the higher your Customer Lifetime Value will be for them since you are their customer. Plus, many performance marketing agencies base their charges on how much you spend, not on how much you gain from the media you buy. This gives them a predictable revenue stream—something retailers do not have. They throw up a loud signal that reads exactly the same as the simple profits equation

I shared above: profits = revenue - costs. Then, they equate this signal with another key message that works to their benefit:

Ads = Revenue & Revenue = Growth

Quite convenient for them, right? Their message to you is clear: If you want to continue to grow your company and become more profitable, you must spend even more money on ads. Why? Because of the following cycle of equations:

ads = eyeballs

eyeballs = visitors

visitors = shoppers

shoppers = revenue

What a tricky cycle we're tumbling around in. They have us believe that as long as we chase after revenue, things will be just fine. Even the metric they use to show us we're successful is all about revenue. It's known as ROAS: Return On Ad Spend. In my opinion, this metric is stupid. For one, attribution is unreliable. Plus, they also measure return by how much revenue you generate.

What happened to profits? Shouldn't we be aiming for profits? In the end, ads ≠ profit, not every time, at least. Still, these conglomerates continue to simplify and amplify their message over and over. But you're smarter than that. You know that even when something plays on repeat over and over, that doesn't mean it's right. Unfortunately, not everyone is that smart.

When enough people believe in the same illusion, it becomes a reality that creates grim scenarios for companies that

disregard the real e-commerce growth formula that I'm going to share with you.

Sadly, far too many marketing managers continue to blindly adopt ROAS as the go-to North Star metric. Doing so changes their behavior. It's no longer about making a company profitable or caring about what happens downstream with customers' happiness. Instead, they focus on multiplying their ROAS many times over. They let the number lead the way and leave people out of the equation. In the process, these marketing managers become spending managers.

Adopting a New Way of Thinking About Revenue

In what other areas of your life do you feel there is only one way to do something? Even if you can name a few places where you take finite, absolute positions, my larger point is that business is different from life. In business, the moment you decide that there is only one way to do anything, you have worked yourself into a trap.

Very few things in business work in an absolute way. If you are of the mind that the only way forward for your business is through acquisition marketing alone, especially because that is what the dominant media players are telling you, then now is the time to rethink your position.

Let me repeat something I wrote in the introduction: I am not trying to talk you out of acquisition marketing because it is a key part of business growth and success. Instead, I'm trying to help you enhance your approach in a way that helps you market yourself smarter and in a more targeted fashion, so you can connect with customers who will stay with you for the long haul.

There are many ways to achieve business success, but none is more important than Customer Lifetime Value. There are many dots to connect as you shift your focus toward putting CLV to work for you. Along the way, you will begin to see the link between growing your e-commerce and understanding what customers value.

If you continue to do what everyone else is doing or what major media companies like Google and Meta want you to do, you will continue to swim upstream in a crowded marketplace. You owe it to yourself to do experiments, take calculated risks, and explore other ways to achieve business growth.

During the early days of my own e-commerce journey, the relationship between the customer acquisition cost and Customer Lifetime Value was blurry. It wasn't until my fifth year of being an e-commerce entrepreneur that I finally started to understand things to the point where I could put CLV to use for my own business and eventually for others.

What I realized was quite simple on paper: I was spending too much to acquire customers who were either never going to buy again or were only going to buy sporadically over the next few months before disappearing forever.

E-commerce is much more than an acquisition game and also much more than a conversion game. It's also a retention game with everything to do with customer lifetime value. And it's a game that begins and ends with Customer Value Optimization.

Changing the Growth Equation

(TL;DR: If you're not interested in going too deep into data explanations, I've summed this up for you. You can skip to chapter 2, where I talk about how to improve it.

- You must move away from simple financial figures that show only the past and adopt customer-centric measures like Customer Lifetime Value and Customer Acquisition Costs.
- Without those, you're shooting in the dark, and you will not know who to target, why, and how much to spend to acquire those customers.

Now, if you're a data geek, please continue to read!

To have a healthy business, you need profits. From a very simple perspective, the profit equation I shared earlier makes a lot of sense:

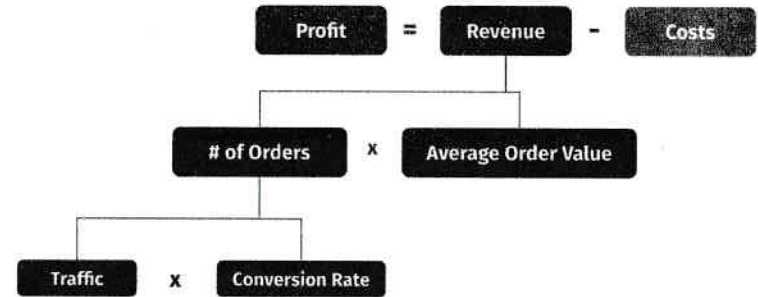
WE ALL KNOW THIS, RIGHT?

$$\text{Profit} = \text{Revenue} - \text{Costs}$$

It's so clean it's almost beautiful. You take your revenue and subtract costs, end of the story. However, to actually move the needle, you need to analyze things in greater depth. You have to understand which factors matter most because the e-commerce game is much more complex than any simple equation will have you believe.

What you'll find, and what this book presents, is that this equation is far from absolute. It's a starting place that points the way forward. Here's a better example of leaning into when it comes to an e-commerce business model:

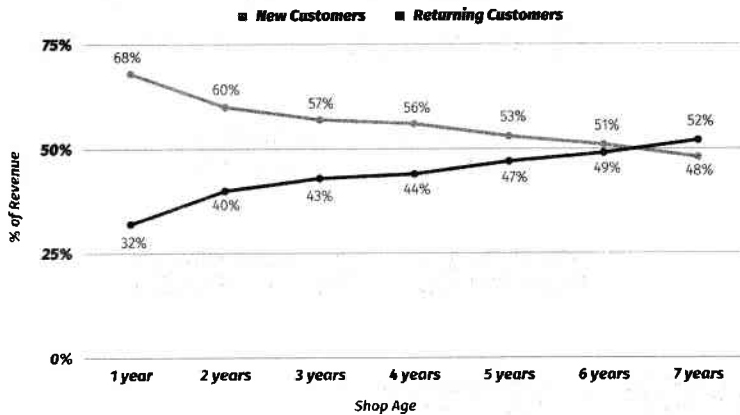
IN ECOMMERCE, THIS IS THE COMMON UNDERSTANDING



Orders don't just happen out of the blue, right? Actual humans make decisions based on behaviors, desires, needs, etc. New customers choose companies while existing customers return to buy again and again. Depending on the vertical and the maturity of a company, returning customers can generate up to 90 percent of the total revenue.

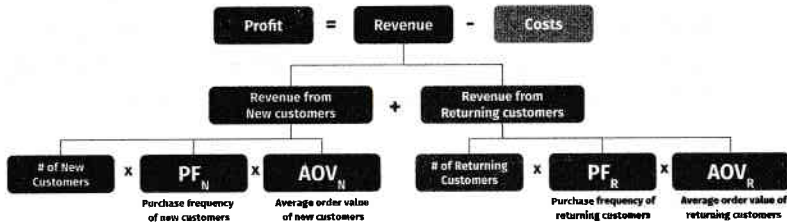
Here is a picture of aggregated data from my company's benchmarked data, including two thousand e-commerce companies. It shows how the revenue from returning customers grows in importance as a company matures.

Lifetime Revenue from New and Returning Customers by Shop Age



As you can see, the revenue that an e-commerce company generates relies on two streams of revenue: one from new customers and the other from returning ones.

WE NEED A CUSTOMER-CENTRIC PERSPECTIVE TO EVALUATE THE PERFORMANCE



Customer generation comes from a handful of dominant numbers, including the following:

- Traffic
- Average order value (AOV)

- The conversion rate
- Purchase Frequency
- Repeat Purchase Rate

Unpacking the Components of CLV

Before we go too far forward into the land of CLV, I want to unpack some of the less-commonly known terms and components for you. Each of these plays a role in measuring and improving CLV.

Purchase Frequency (PF)

PF represents the number of orders per customer. This number should always be higher than one, as any customer is placing at least one order, and orders are calculated once they are shipped, not just placed.



Number of orders

PF

=

Purchase Frequency



Number of customers

For context, here are some benchmarks with the average lifetime PF by a sample of verticals, which I've borrowed from Omniconvert's data team:

- Food and Drinks: 3.52
- Toys & Hobbies: 2.24