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By considering the lifetime value of the customer relationship, progressive banks are re-focusing the cross-sell viewfinder on priority customer needs.

Rx for Cross-Sell: Customer Lifetime Value

BY SHERIEF MELEIS

Retail banks are facing a revenue drought, with slack loan demand, a flat rate environment and dwindling fee revenues in the face of new laws and regulations. Often, the best hope for growth is to serve established customers more fully – essentially a person-by-person campaign to gain "share of wallet."

For winners in this quest, the opportunities are enormous. Today's customer relationship "depth gauge" remains stubbornly lodged at less than 20% at most banks. In other words, for any given individual or household served by the institution, typically more than 80% of the financial services needs are met by competitors. Changing this ratio by even a small amount across the customer base can have a huge financial upside.

One challenge, however, is a widespread shortage of insight about the economics of customer relationships. Currently, for example, many retail banks are intent on re-tooling the checking business following the governmental crackdown on overdraft and debit card fees. But this tight product focus tends to ignore the bigger picture of customer needs, and the lifetime economic potential of meeting them.

It is within this context that progressive banks are expanding the cross-sell viewfinder. Instead of just looking at the current-year profit potential of individual products, they are considering the full span of the customer relationship, from beginning to end. What are the top items of mutual benefit to the customer and the bank?

As an example of how customer lifetime value (CLV) makes a difference in decision-making, consider all of the recent controversy surrounding the checking account. There's a widespread effort to "repair" free checking by attaching monthly service fees, to ease the profit drain from lost overdraft fee revenue. This approach can be short-sighted, however, in cases where free checking succeeds in attracting robust accounts with high cross-sell potential. With a potential CLV of between $3,000 and $5,000, for

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example, high-value customers will more than reward the bank for providing free checking as they use additional banking products.

To capitalize on such insights, it is helpful to begin with a three-step plan. This includes 1) recognizing the “hidden value” in deep customer relationships; 2) sorting through the maze of customer behaviors and product possibilities to find the select combinations with the highest CLV potential; and 3) setting marketing, product and sales priorities that will energize cross-sell and relationship expansion in the field.

Hidden value. The value of cross-sell often is evaluated product-by-product, when in fact the benefits go much further. In-depth customers tend to stay with the bank longer; make greater use of their products; and tend to pose a lower risk of default. In many cases, price sensitivity falls as the focus turns to rewards, recognition and service. Also, cross-sell can make far more effective use of staff and corporate resources, compared with a product-by-product effort. It is important to recognize these factors in considering the value of deeper customer relationships.

Customer analytics. To identify priority cross-sell opportunities, the bank needs to be able to sort through a large set of possible product combinations and offer sequences, and arrive at a select list of offers that will provide the highest mutual benefit to the customer and the bank. In one instance, for example, the retail banking division of a major bank initially evaluated more than 200 cross-sell possibilities, eventually narrowing down the consideration set to somewhere between 12 and 15 possibilities that would capture the lion’s share of the opportunity.

The importance of this exercise is underscored by the current retail banking emphasis on promoting home equity loans to the “best customers.” This likely will be ineffective for customers who are valuable on the basis of money market deposit balances, however, given that they already are liquid and probably don’t need additional interim credit. CLV analysis helps to uncover these critical nuances.

Marketing, products and sales. The success of CLV- guided cross-sell initiatives largely will hinge on targeted marketing – matching the right offers with the right groups of targeted customers. There are also implications for product packaging and relationship pricing. Then within the branch network and call centers, the retail bank will need to supply timely sales leads, review sales processes and reconsider performance goals and incentives for front-line staff.

In following through on these three steps, various kinds of preparation will be needed inside the bank. The marketing team will need to develop robust models that will accurately measure the total lifetime value of every customer. Individual product teams will need to collaborate with distribution in rolling out centrally-designed cross-sell propositions that branch and call center reps can sell within a relationship context.

Meanwhile, executive management will need to resolve simmering issues with performance measurement, given the persistent bank emphasis on splintered metrics centered on individual products. Executives also will need to promote cooperation among the product, distribution and marketing teams so that the bank can proceed in a focused way that unlocks opportunity with a minimum of strife and wasted effort.

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