Opportunities for Action in Consumer Markets

Sizing Up the Heavy Spender

The Boston Consulting Group

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There are as many ways to segment the consumer market as there are consumers, and drilling down to segments of one can produce significant insights. But with intense pressure from low-cost competitors, escalating product variety, multiple channels, and increasingly demanding customers, most retailers are looking for quick and direct infusions to their bottom line. In this case, they don't have to look further than their best customers.

In scores of categories, the top 30 percent of customers generate from 50 to 80 percent of the revenues—and an even greater portion of the profits. (See Exhibit 1.) Many companies that serve consumers are beginning to act on this insight by focusing on their heavy spenders. Last year, Best Buy identified five segments of heavy spenders and designated specific stores in its chain to target one or more of them. The Home Depot's recent upgrading of its kitchen-remodeling centers was a direct appeal to its most profitable customers. Some financial-services companies are starting to conduct customer profit-and-loss calculations, and one telecommunications company now measures the current and potential value of its customers in order to focus on heavy spenders.

Of course, identifying the heavy spenders who produce most of a category's revenue is only half the job. The real competitive advantage comes with understanding how those customers differ from average spenders. Why do they choose certain products and retailers over others? What factors close the sale? Only by answering such questions will a retailer be able to develop a merchandising and promotional strategy that attracts heavy spenders and encourages them to spend more.

Focusing on heavy spenders can be as beneficial for general merchandisers as it is for category specialists. A recent survey of consumers who shopped across 12 different product categories, conducted by The Boston Consulting Group, yielded some powerful insights. Although the results were similar across categories—heavy spenders contributed between 60 and

Exhibit 1. For Most Retailers, a Small Group of Customers Generate More than Half the Sales

SOURCE: BCG analysis.

90 percent of sales—we found some interesting differences as well. Categories with high consumer involvement—those in which products come in a range of prices and offer buyers the opportunity to trade up (such as large consumer durables and formal apparel)—attract a higher concentration of heavy spenders than low-involvement categories (such as casual apparel and housewares).

Even more interesting, differences in the spending habits of heavy and light spenders also varied across categories. We found that heavy spenders in high-involvement categories spend an average of ten times more per year than light spenders, whereas those in low-involvement categories spend an average of only five times more. Such differences suggest how important it is to capture the high-value group—for its potential as well as its current spending. As people's lives change, so do their spending habits. Focusing on the most likely *potential* heavy spenders—those on the cusp between the low- and high-spending groups—could double the value of those customers to a business.

Heavy Spending Across Channels

Today's big spenders are likely to shop in more than one channel, so targeting them is particularly important for multichannel retailers. By deepening and expanding their relationships with high-spending customers, retailers can justify the additional cost of operating through multiple channels. Such an approach will allow them to gain a higher share of wallet from their existing customer base, as well as win over profitable new customers from competitors unable to satisfy their multichannel needs. In addition, retailers that want to extend their footprint—but find real estate prices too high and opening new stores too risky—will discover that the Internet is ideal for targeting heavy spenders quickly. For example, women who spend more than $1,000 a year on cosmetics like to replenish their supplies online. But there are very few multichannel cosmetics retailers—so far. Rather than thinking of the Internet as an independent channel or a standalone business, retailers should treat it as an integral component of a new business model whose goal is to attract the most profitable customers and build deeper relationships with them.

Developing a compelling multichannel offering for heavy spenders will require retailers to look beyond traditional sources of information—such as loyalty clubs and credit card data—and figure out how consumers behave in various categories and across retailers and channels. It's a daunting prospect, because most retailers don't track even their own customers across channels—let alone those of their competitors. But the idea of segmenting customers according to their value and activity is not new. Mail-order retailers call it RFM—recency, frequency, and monetary value. This is a straightforward, data-driven formula that lets them segment their customer base and focus on the high rollers. Retailers that monitor RFM as catalogers do will greatly increase their odds of survival.

To assess the value of tracking customer spending across channels and competitors, BCG considered the book business, one of the maturest of the multichannel categories. We identified five segments of book buyers on the basis of how recently they had purchased books, how frequently they had done so over the most recent year, and how much they had spent. It was no surprise that the top two segments drove most of the sales and profitability.

We uncovered important data on channel preference and usage as well. For example, an overwhelming 70 percent of book buyers in the top segments of our survey were multichannel purchasers, spending a full 37 percent of their category dollars online. However, their purchasing behavior online didn't always match their behavior offline. They cited superior product availability and selection as their main reason for shopping online. Indeed, they often made online purchases following a store visit, and they used the online channel to locate hard-to-find titles. (This is why a store retailer should direct its customers to its Web site whenever it can't fulfill a request.) Book lovers also said that price discounts influence them less online than at a brick-and-mortar store. Understanding such factors will help online retailers develop the right marketing programs for heavy spenders.

Understanding Heavy Spenders

A retailer's goal should be to design an offering that will increase its share of wallet of high-value customers. To do that, it needs to understand its customers' attitudes toward shopping and how they shape behavior. For example, we found that heavy spenders in many categories were *twice* as likely to window-shop every month for products in those categories. We also found that heavy spenders often shopped in adjacent categories. To better understand the factors that influence shopping behavior, we asked consumers to tell us what is most important to them when they are shopping for products in the 12 categories studied. The heavy spenders in one category, for instance, like having a wide selection of high-quality brands with the latest features and are less interested in price. We then asked them to rate our client and its competitors across those dimensions. The insights we gleaned from this exercise—as well as from other competitive assessment tools, such as assortment and square-footage reviews—helped us develop a focused category-by-category plan for capturing the highest-value customers.

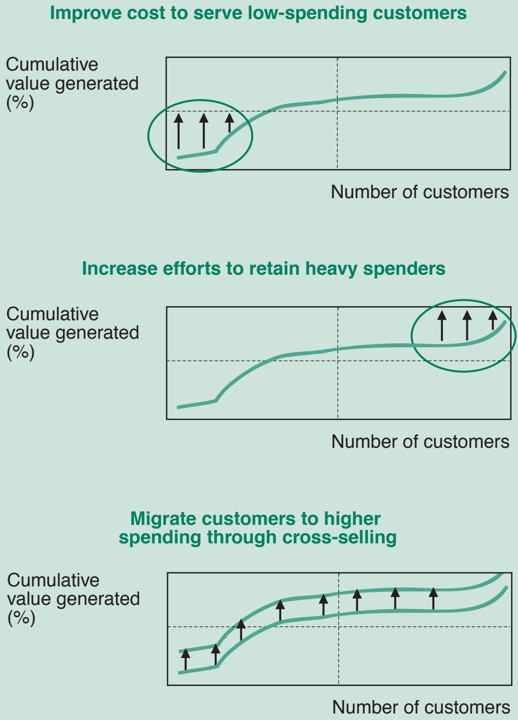
Similarly, in our study of the book business, we found that nearly one-third of the top purchasers of books visit a bookstore at least once a week, shopping for an average of 45 minutes—about 20 percent longer than consumers in the other segments studied. Obviously, these book lovers are unlikely to be book club members, preferring instead to select their own titles. By capitalizing on such information, retailers can tailor their brand positioning, promotions, merchandising, and store environment to entice and satisfy their best customers.

You Can't Be All Things to All People

If you were to construct an economic model of your customers and segment them on the basis of frequency of purchases, average margin, and loyalty, you would find that many of them just aren't worth keeping. For instance, frequent diners at midprice restaurants offer ten times more return than "special night out" visitors do. The value of cosmetics customers loyal to one brand is more than 15 times the value of infrequent purchasers. And a telecommunications company determined that, in addition to retaining more of its heavy spenders and persuading them to buy more through cross-selling, it could save tens of millions of dollars by reducing the cost of serving its lowest-spending (and lowest-value) customers. Of course, that doesn't mean you shouldn't convert occasional customers into frequent and valued ones. (See Exhibit 2.)

To increase your share of your heavy spenders' purchases, as well as your share of heavy spenders, the first step is to discover why your best customers

Exhibit 2. Businesses Have Three Options for Economic Improvement



SOURCE: BCG analysis.

choose you. Chances are that the customers who spend the most at your stores have been doing so primarily because they appreciate your products and trust your company. They feel that they mean more to you than just a sale, and they reward you with their loyalty. To encourage them to buy more, more often, you need to focus on broadening and deepening your product and service offering. That means looking beyond the purchase transaction to your customers' experience of your total brand. And it means thinking differently about the points where you connect with customers. For example, your internal operations may be organized around marketing, sales, and after-sales service. But to your customers, it's a single experience—from learning about the product to shopping for it, buying it, and having it delivered to getting it repaired: a single experience that has your brand's name all over it.

Heavy spenders can be your most valuable assets, both today and in the future. Develop specific messages for them, create tiered levels of service, and lock in the heavy spenders with the best you can offer to maximize their value. Cultivate them or lose them.

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