Realizing the precise cost of serving. Can you determine how much is too much?

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THE INTRODUCTION:

The client in question is the subsidiary of one of the world's leading vehicle manufacturing companies. The client's product portfolio includes Motorcycles and Scooters.

THE PROBLEM:

The company has a deeply penetrated PAN India network of ~550 dealers spread across 29 states and union territories. The company's problem statement is three-fold:

1. To gauge accurate costs of serving different customer segments.
2. To identify the profitability earned at varied customer/ geographical segments since, at present, profit earned is at the overall level (standalone entity).
3. To evaluate the performance of the company's marketing efforts through more holistic metrics. This is because the company currently deploys a maximum sales/ marketing workforce in the state/ region where it earns maximum revenues.

THE SOLUTION:

The company strived to develop a meticulously crafted customer profitability system that identifies, measures, analyses and manages the customer profits and its key drivers. Apart from the problems identified above, other reasons for creating this detailed oriented system were:

- **Holding Company's Mandate** - The global corporation wanted to revisit its customer strategy and therefore mandated the company to focus on better customer contact and closer customer relations.
- **To expand global competition horizon** - Companies worldwide are pressured to become more customer-focused and increase stakeholder value.

THE RESULTS:

After rigorous deliberations and continuous collaboration with the client for over three months, our Chandra Wadhwa & Co. team implemented a detailed oriented customer profitability framework. This offered eye-opening insights for the management to perform business operations more productively and efficiently. The framework provided the following salient features:

- Shift from product-centric approach to customer-centric approach.
- Identification of states (geographic factors) as well as the age of the customers (demographic characteristics) as the reporting segments.
- Capture revenue and costs estimates at the transactional level for reporting at customer/market segments as identified above.
- Reorganisation of cost-centres/ profit-centres hierarchies based on the customer/ market segments.

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- The selling and distribution overheads comprise 10% of the total cost, which were assigned to segments following the cause-and-effect principle (approximately 70% of the selling and distribution overheads). These costs include:
    - inventory carrying costs;
    - quality control and inspection costs;
    - customer order processing;
    - order picking and order fulfilment;
    - billing, collection and payment processing costs;
    - accounts receivable and carrying costs;
    - customer service costs;
    - wholesale service and quality assurance costs; and
    - other selling and marketing costs.
- Re-mapping around 20% gross value of the capitalised fixed assets based on the reorganised cost-centres/ profit-centres to help achieve practical and accurate cost assignments.
- Hold employees accountable for customer profitability, including those employed in marketing and other functions.

After implementing the customer profitability framework, our team pointed out that while the company was earning profits at the overall entity level, they were making losses in one of the states where maximum turnover was achieved. This provided an excellent insight to the management about how these state losses were being cross-subsidised from the states earning profits. ***Refer Exhibit 1***

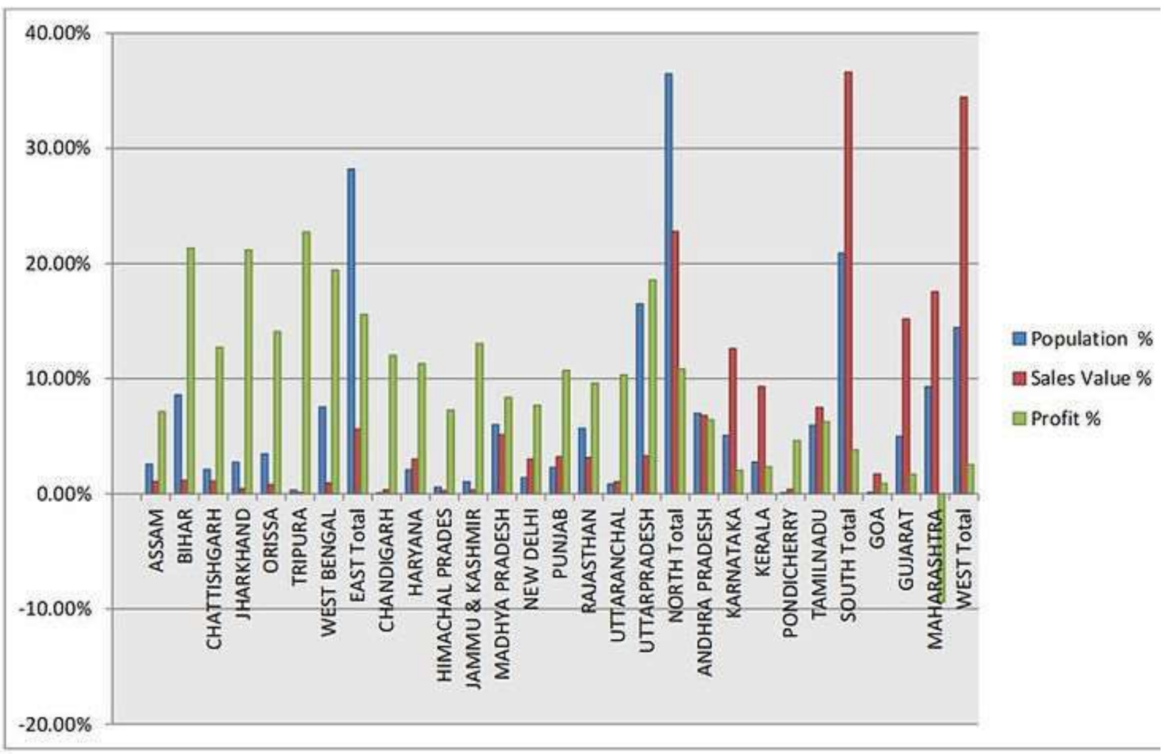

Exhibit 1

Following were the hidden takeaways:

1. Exceptional sales focus
2. Well-targeted marketing
3. Exposed unprofitable and low-value customers

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4. Better quantified customer value proposition
5. Improved conversion from unprofitable customers to profitable customers
6. Superior marketing segmentation, which includes:
    - Demographic
    - Psychographic
    - Behavioural
    - Geographic
    - Firmographic

FREQUENTLY ASKED QUESTIONS:

Q. What is customer profitability in the automobile industry?

A. Customer profitability is a measure of the profit generated by each individual customer of an automobile company. It takes into account the revenue earned from the customer and the cost of servicing the customer, including marketing, sales, and after-sales service expenses.

Q. Why is customer profitability important in the automobile industry?

A. Customer profitability analysis helps automobile companies identify their most profitable customers and segments, as well as the least profitable ones. This information can help companies make better resource allocation, marketing strategy, and pricing decisions. It also enables them to improve customer satisfaction and loyalty by understanding their needs and preferences better.

Q. How is customer profitability calculated in the automobile industry?

A. Customer profitability is calculated by subtracting the cost of servicing the customer from the revenue generated by the customer. The cost of servicing the customer includes all direct and indirect expenses associated with marketing, sales, and after-sales service. It may also include the cost of resolving any customer complaints or issues.

Q. What are the challenges of customer profitability analysis in the automobile industry?

A. Some of the challenges of customer profitability analysis in the automobile industry include:

- Difficulty in allocating costs accurately to individual customers or segments.
- Lack of complete and reliable customer data.
- The complex and lengthy sales cycle of automobiles.
- The need to account for the impact of marketing, branding, and customer service on customer profitability.

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Q. How can automobile companies improve their customer profitability analysis?

A. Automobile companies can improve their customer profitability analysis by:

- Collecting and integrating customer data from different sources, including sales, marketing, and after-sales service.
- Using advanced analytics tools to analyse customer data and identify profitability drivers.
- Developing a standardised methodology for cost allocation across different customer segments.
- Regularly reviewing and updating customer profitability data to reflect changing market conditions and customer needs.
- Involving all relevant stakeholders in the customer profitability analysis process, including sales, marketing, and finance teams.

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