CENTRAL BANK OF EGYPT
Egyptian Banking Institute

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# CURRENT TRENDS

## August 2021

## Customer Lifetime Value( CLV )
## for Banks

MOVING FORWARD WITH CONFIDENCE...

## Background

In today's customer-centered economy, focusing on short-term customers is an outdated business model. Instead, banks must foster every customer relationship to increase retention and customer lifetime value (CLV).

Determining the profit – or loss – potential of each client is essential if the bank is looking to keep the bottom line healthy. Retail banking staff needs to know which types of customers are worth pursuing for long-term value and which ones are likely to switch banks only for lower prices. Understanding the difference between those two types of customers guides the front-line employees, so that they invest their time and resources appropriately – and maximize the customer lifetime value. CLV is about using a customer profitability analysis, deciding pricing and selling products according to a customer's likely future value.

Maximizing customer lifetime value is about focusing the sales efforts on the customers that show the highest potential value over their lifetime and sustaining long-term relationships with clients. Therefore, using inappropriate sales tactics or spending resources pursuing the wrong customers is the direct way to weaken the bottom line.

## Concept

**Customer lifetime value (CLV)** is the worth of a customer over the length of their entire tenure at the bank and is a much more complex calculation than just net profit or total sales. Using customer lifetime value as a metric requires the entire bank to shift its focus from quarterly profits to the long-term health of customer relationships. CLV is the net profit acquired from a customer throughout a company's relationship with them.

**Customer lifetime value (CLV)** is a key marketing metric in the financial sector. This is because banks (and other financial institutions) are holding customers for a long period of time and the customers will go through phases of their relationship – ranging from highly profitable to minor (or even negative) profitability. Banks tend to focus a considerable amount of their marketing efforts on trying to build more profitable relationships with existing customers.

**Essentially direct marketing and relationship marketing efforts are used to:**

- Retain the loyalty of the customer (greater customer lifetime in years)
- Increase the value/profitability of the customer (through up-selling and migration to higher value products).

## Importance

**There are many reasons why CLV is useful:**

- While following a structured approach and implementing CLV into the bank's long-term strategy, a significant competitive advantage will be achieved by selling the most profitable products to the most rewarding customers.

- CLV not only help in tracking the customer profitability, but it also provides an overview on customer acquisition costs. Thus, a thorough customer lifetime value analysis helps make better-informed decisions when it comes to marketing, sales and pricing for new customers.

- High CLV customers are loyal customers, and loyal customers stay with the brand longer and can offer valuable feedback on how to improve the bank's products and services. Once the customers' loyalty is captured, they often become the best brand advocates, singing praises and giving good word-of-mouth referrals and a better reputation. Loyal customers are more likely to try new products or features, which increases their CLV even more.

## Measurement/Calculation

**The customer lifetime value calculation for banking**

The ROI on the investment in the various direct and relationship marketing efforts can be measured quite effectively using a customer lifetime calculation. The easiest way to calculate CLV is to multiply the annual profit gained from a customer by the average length of time of customer retention.

The key inputs into the customer lifetime value (CLV) banking calculation include:
- Average balances of loans and savings on a per customer basis
- Average interest rate margin (as a percentage)
- Average income/revenue per customer generated from non-interest income sources (e.g. fees, commissions, and other sales)
- Costs of providing customer services and access (which would include transaction costs, statement costs, and potentially a provision for infrastructure costs, and so on)

These inputs are used together to determine average annual profit on a per customer basis. This information is then combined with customer retention rates, other costs of retention and up selling, as well as initial customer acquisition costs

# Practices: Customer Life Time Value and Digital Banking

Nowadays, banks look very different due to digital transformation. At the same time, the customers, in their values, expectations and needs are also very different. **Customer lifetime value (CLTV) is one aspect of the customer journey that is being heavily impacted by the rise of digital technologies.** We know that customers are now less focused on a particular brand but on finding the right features and services that work for them. That means they are more likely to switch banks. **One of the prime benefits of moving to digital banking for customers has been that they are free to conduct their financial lives at any time or point in the day**, without requiring anything further than their phone and a password. In account opening, they expect the process to be seamless, without multiple requests for the same information, and completed in a timely manner.
**In a digital world, banks should take into consideration the following to increase CLV:**

- **Facilitating Access:** Being able to access banking services at any time and from anywhere contributes to building customer loyalty. Offering customers new ways of researching and purchasing products also increases the likelihood that they will purchase from the bank and not from another competitor.

- **Segmentation:** Segmentation activities are all now possible as a result of the move to digital. For years customers have been receiving promotional literature or emails that had no concept of who they were as a customer. One can imagine the response to an email urging them to take out car insurance when they did not drive a car.

- **Provide Value Throughout Every Stage of the Customer Journey:** To be in a position to offer appropriate products at relevant times to their customers financial life journey, banks require a genuine understanding of each customer and their financial lives. It is only by understanding the focus, needs and wants of their customers at each stage, will they be able to sell their products and services.

- **Analyzing Data Effectively:** The amount of money that a customer saves, the investments he has, whether he owns or rents a home, how much he spends on petrol each month; all of this information and more is decipherable from bank statements. Banks know virtually everything about customers, but to date, have just not used that data in a particularly effective manner.

With digital tools, it is now realistic to send customers push messages at the appropriate time for products that they genuinely want, and at a price that is right for them. Preparing for different stages of life goes much further than helping young people save and preparing older customers for retirement; but using the customers' data to prepare them for their personal financial future.

Banks should track customers throughout the entire journey, keeping an eye out for relevant patterns and using that data to improve the different stages of the customer journey. For instance, are customers trying to use a product to solve issues? Are they struggling with certain features? Are customers reporting poor experiences? These trends can help banks improve processes.

- **Financial Improvement:** education on how to appropriately manage finances has not been disseminated well to those who need it. Customers are often ignorant of how to maximize savings or investments, how to curtail debt spend or work through a mortgage application. Genuinely understanding customers histories allow banks to equip them with knowledge that will help them manage their finances. Offering this information builds bonds between the customer and the bank, increasing the likelihood that customers will purchase products and services when the need arises.

One example of this was the work carried out Barclays to educate older generations on how to stay safe online, so that they might feel confident about using the web – and manage their account.

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**Headquarters – Nasr City**
22 A, Dr. Anwar El Mofty St., Tiba 2000
P.O.Box: 8164 Nasr City, Cairo, Egypt

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