

## What Have You Done For Your Most Profitable Customers Lately?

By Nora Laughton

With Vendor Specific Objective Evidence (VSOE) and revenue recognition rules taking some of the fun out of negotiating both license and maintenance for normally zealous sales people, high tech companies are having to spend more time analyzing both where their profits are really coming from, and what the real cost is of “servicing” each type of customer. We all know that it costs five to seven times more to acquire a new customer than it does to keep or service an existing one. Since for most software companies, 60-80% of their total revenue (license, services and maintenance combined) is being generated from their existing install base, it is reasonable that selling to existing customers generates more profit than cultivating a net new customer.

Many companies don't know who their most profitable customers are, and neither do they have a strategy to keep them. Perhaps as important, how many companies actually profile those customers so they can develop strategies to attract more customers that match that profile?

*How do you know you have the right customer strategy?* First, segment your customer base by total spend. How many customers represent the top 1% of payers, top 10%, top 15% and 20%? You need to know how many large, medium and small customers you have.

Then, develop a sales and marketing strategy by segment that maximizes revenue and retention within that segment. In most software companies the top 20% of customers generate about 80% of the revenue. For these customers, you'd likely take a more proactive approach with an emphasis on retaining and growing them. An example of the type of service you might provide higher-paying customers is a designated account manager—someone they can call for any reason, such as escalation of an existing issue, to order more product, or discuss a migration. This type of established relationship can help you reach trusted partner status with your customer and enables you to keep up to date on their business plans and needs.

Within the other 80% that generate 20% of the revenue, you'll find a mixed bag consisting of low-paying customers that cost more to deliver service to than they pay (you'll certainly want to address that), customers who just cover their costs, and middle-paying customers that, with the right strategies and services, will grow over time into larger customers.

It takes time to determine who the most profitable customers are, but it does pay to spend the time to determine exactly how much services cost to deliver, and just exactly which

customers are using those services. You might be surprised at what you discover. Some of our customers have changed the services they offer .... Once they know how much they actually cost to deliver and who is using them. Look for trends in your customer base. If your most profitable customers are all in a particular industry or are a specific size, use that information to develop your retention strategies and future sales and marketing strategies.

Once your services initiatives are in place, you'll need to create the proper organization to support and deliver on them. First, develop a cost-effective model that supports your service strategies. Some of our customers establish a threshold of dollars that a customer must pay in maintenance before they will have access to different levels of service.

Establish clear lines of responsibility and accountability, and ensure that there are defined lines of communication and escalation where applicable. Goals should be measurable and reachable. Layers of administration can hinder service delivery levels—the simpler the better.

Lastly, develop a compensation model that will drive the kind of behavior that you want from the organization. The best strategies will achieve nothing if compensation spurs different behavior. Effectively, regardless of how important you *tell* your sales people maintenance is, they are really not going to *hear* you unless there is compensation tied to it.

Companies that apply the right strategies to the different segments of their customer bases find that their retention rates are more stable than companies that simply throw additional services at customers when they are unhappy. A well thought out strategy can help you determine who your most profitable customers are and how to treat them so that they will want to stay your customers. What have you done for *your* most profitable customers lately?