What is Customer Profitability Analysis?

Worksheet

Customer profitability = Revenue from a customer Cost to serve that customer, revealing which customers actually create value versus which ones destroy it.

Questions

1. What is the formula for customer profitability?

A) Revenue Cost to serve
B) Revenue Cost to serve
C) Revenue Cost to serve
D) Cost to serve Revenue

2. A customer with $100,000 revenue and $110,000 cost to serve is

A) Highly profitable
B) Break-even
C) Unprofitable
D) Impossible to determine

3. Which of these is part of 'cost to serve'?

A) Only the cost of goods sold
B) Support calls, rush shipping, and discounts given
C) The company's total marketing budget
D) Shareholder dividends

4. Why do companies perform customer profitability analysis?

A) To calculate corporate tax
B) To identify which customers to retain, reprice, or drop
C) To set employee salaries
D) To value inventory

5. Customer A generates $120,000 in revenue but requires $95,000 in service costs (support, discounts, delivery). Find customer profit.

6. Customer B generates $80,000 in revenue but demands rush shipping and heavy support, costing $88,000 to serve. Find customer profit.

7. A company has 3 customers with profits of $25,000, $8,000 and $12,000. Find total customer profit and identify the least profitable.

8. Define: What is the customer profitability formula?

9. Define: What counts as 'cost to serve'?

10. Define: What is a 'whale curve' in this context?

Answer Key

1. B) Revenue Cost to serve - Customer profit is revenue minus the true cost of serving that customer.

2. C) Unprofitable - 100,000 110,000 = $10,000, an unprofitable customer.

3. B) Support calls, rush shipping, and discounts given - Cost to serve includes all customer-specific service costs beyond just product cost.

4. B) To identify which customers to retain, reprice, or drop - It reveals which customers truly create value so a company can focus resources accordingly.

5. Customer Profit = Revenue Cost to Serve = 120,000 95,000 = $25,000 profit

6. Customer Profit = Revenue Cost to Serve = 80,000 88,000 = $8,000 (unprofitable customer)

7. Total = 25,000 + (8,000) + 12,000 = $29,000 Least profitable = Customer B ($8,000), a candidate for repricing or dropping

8. Customer Profit = Revenue from customer Cost to serve that customer.

9. All costs tied to a customer: order processing, discounts, returns, support calls, custom delivery, etc. - not just cost of goods sold.

10. A chart ranking customers by cumulative profit, often showing the most profitable 20% generate far more than 100% of total profit, offset by unprofitable customers.