Overview of the Relationship Between the Seller's Profit, and the Costs of Creating Customer Value

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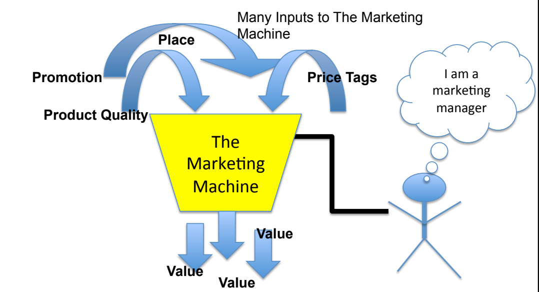
Learning objectives

- 1) first premise: increasing customer value increases customer demand and sales revenue at a diminishing rate
- 2) second premise: increasing customer value increases the cost to the seller and costs can increase at an exponential rate
- 3) identify two types of costs (Fixed and Variable)
- 4) the relationship between seller's investment in customer value and seller's profit is a quadratic
- 5) identify two types of ingredients in the marketing mix

Marketing Machine: 4 P's as Inputs

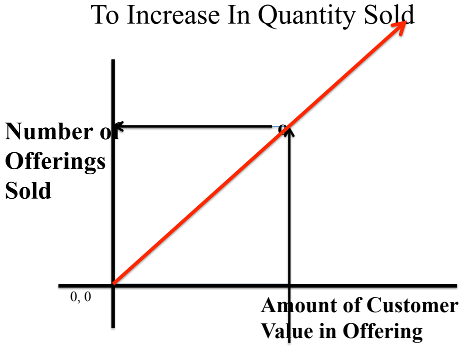


The Marketing Machine Creates Customer Value

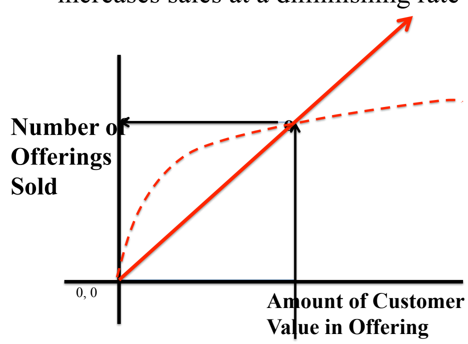
Basic Premise of Marketing

- Increase The Amount of Customer value in the Seller's Offering then
- You Increase the number of offerings that will be purchased

Increase Amount of Customer Value To Increase In Quantity Sold



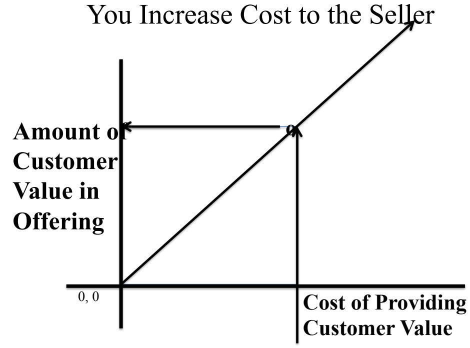
increases sales at a diminishing rate



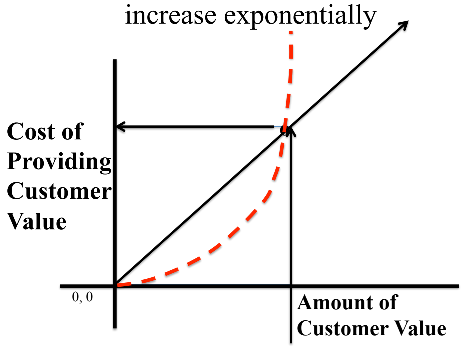
Basic Nature of Costs

- To Increase the amount of Customer value in an Offering
- the Seller spends more money on providing
- More Product and Service Quality
- More Convenient Places and Times for Transaction
- More Information about the offering in his Promotion efforts

Increase Amount of Customer Value You Increase Cost to the Seller



Costs to Increase Customer Value can increase exponentially



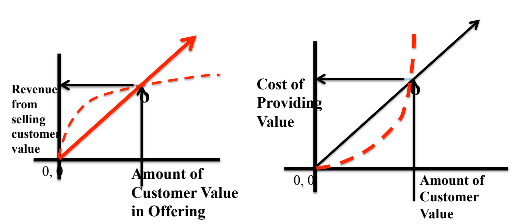
There are **TWO** Types

- Of marketing **COSTS**
- 1) Seller's Investments: those costs that make a direct, traceable and immediate contribution to amount of value the customer finds in the seller's offering
- 2) Seller's Overheads: those costs which provide the managers, the market research, the product development, and other overheads that do not make a direct, traceable and immediate contribution to the offering but are necessary for the marketing process to function

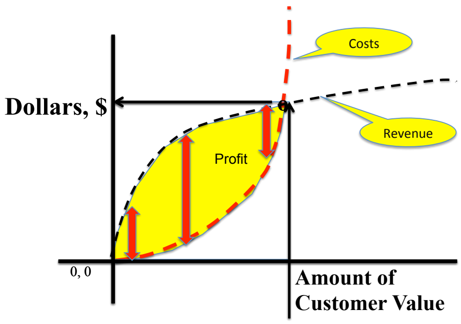
Basic Nature of Profit and Customer Value

- When you first increase customer value in the offering, the increase in sales revenues offsets the additional costs, and profits increase
- As you continue to increase the amount of customer value the amount of profit reaches a maximum and then decreases

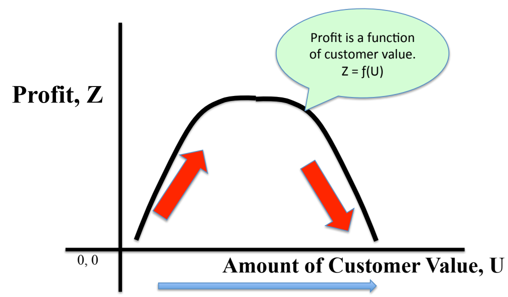
Revenue – Costs = Profit



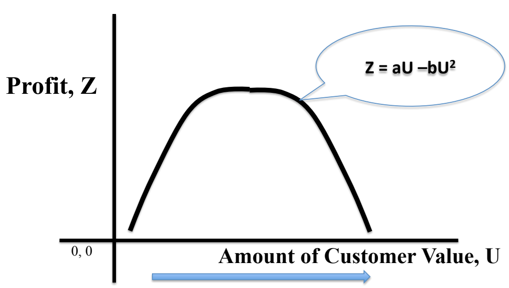
Profit = Revenue - Costs



Profits increase and then decrease as the Customer Value increases



Quadratic relationship between Customer Value, U and Seller's Profit, Z



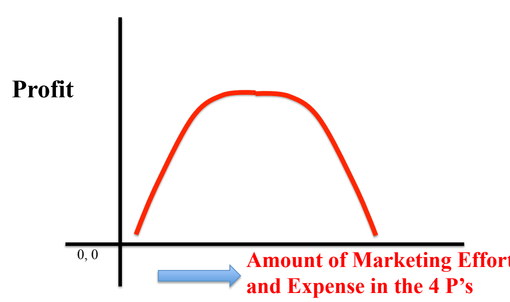
When we know

- The relationship between two marketing variables (e.g., profit and value) then
- 1) we can explain how the change in one variable changes the size of the second variable
- 2) we can forecast the size of one variable given a proposed change in the size of the other

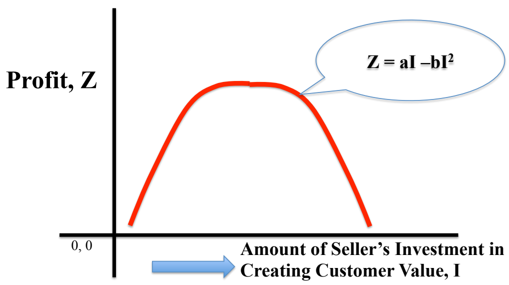
Customer Value

- Is difficult to measure on a day to day basis
- Normally Marketing managers want to measure the relationships between **Profit** and the **Cost** of providing customer value in a more direct and objective way
- Use the **cost** of providing **P**roduct quality, **P**romotional information, convenient **P**lace and time of transaction **as a surrogate measure of value**

Cost of providing Customer value is a measure of the amount of value in the offering



The costs of putting customer value into the offering are called Marketing ‘**Investments**’



Three Current Debates

- 1) Which Marketing Expenses be considered and treated as marketing ‘INVESTMENTS’?
- 2) Can the profits being returned on marketing expenses be called a ‘Return on Investment’ or ROI?
- 3) Do all 4 P’s of the marketing mix contribute to the customer value value to the seller’s offering?

Two Types of Ingredients in Marketing Mix

- 1) Ingredients of the 4P’s with a direct and positive impact on customer value and the quantity sold (expenses that create customer value)
- 2) Elements of the 4P’s with an inverse or negative relationship with customer value and reduce customer demand and quantity sold (larger Price Tags, poor service, costs of acquisition)

Positive Contributions to Customer Value

- 1) Ingredients from the 4P’s with a direct and positive impact on customer demand and quantity sold
- **P**roduct and Service Quality
- Convenience of **P**lace, time, nature of transaction process
- Informational Value of **P**romotional Effort

Reductions to Customer Value

- Elements of the 4P’s with an inverse relationship with customer value which reduce customer demand and quantity sold
- Costs of Acquiring the Benefits Sought
- Size of **P**rice Tag
- Credit Card, Interest and Terms of sale
- Assembly, Recycling, Pick up and Delivery
- Learning curve to operate

Any Questions

- 1) how increasing customer value can increases customer demand at a diminishing rate
- 2) how increasing customer value increases the cost to the seller and can increase at an exponential rate
- 3) the two types of costs (Investment and overheads)
- 4) the relationship between customer value and seller’s profit is a quadratic
- 5) There is an optimal level of customer value which the seller puts into the offering that maximizes profit
- 6) the positive and negative ingredients of the four P’s in the marketing mix