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Abstract

The scope of this paper is to explore the transaction profitability of frequent and sporadic buyers in the Brazilian e-retailing home appliance market. Concepts in relationship marketing literature stressing the impact of purchasing frequency on customer transaction profitability, as well as recent academic research challenging this approach and pointing out the importance of sporadic clients, are analyzed. This paper uses quantitative evidence drawn from empirical investigation in a digital company to show that greater frequency of purchases does not always lead to greater transaction profitability. Qualitative evidence also drawn from the firm under analysis and regarding its managerial approach, suggests that customer transaction profitability is related to its marketing strategy. Using data triangulation, it can be concluded that the benefits of customer retention in the e-retailing realm would only seem to be interesting for firms truly oriented to their clients. Implications are presented, enabling practitioners and academics to grasp fully the real value of frequent and sporadic clients.

1 Introduction

Traditional marketing literature would seem to indicate that the benefits accrued from long-term relationships between companies and customers are greater than the returns derived from short-term relationships. Conceptual evidence on this theory was collated from several researchers who have addressed the importance of retaining customers for corporate profitability (see, for instance, Reichheld & Sasser, 1990; Reichheld & Teal, 1996; Peppers & Rogers, 1997; Kotler, 1999; Kenny & Marshall, 2000).

Notwithstanding the perceived importance of frequent buyers, recent research has challenged this conventional approach, pointing out that companies often fail to appreciate the true value of their customers, be they frequent or sporadic purchasers. This behavior may lead the firms to make strategic mistakes as well as perpetuate managerial errors, such as high spending for retention of unprofitable customers or failing to perceive the importance of a high-value sporadic consumer (Dowling & Uncles, 1997; Schultz & Hayman, 1999; Reinartz & Kumar, 2000, 2002, 2003).

The correct understanding of how to manage both frequent and sporadic buyers has assumed a truly important dimension, mainly in the e-retailing realm, due to very high client evasion in this arena. Reichheld & Shefter (2000) point out that up to 50% of customers abandon an e-retailing company prior to the third year of their commercial relationship.

The scope of this research is to analyze empirically the transaction profitability derived from sporadic and frequent customers in the e-retailing sector of home appliances. The managerial practice adopted by a digital firm is investigated in order to associate the customer transaction profitability observed with the marketing approach adopted by the company on the Web. The firm analyzed is one of the largest retailing groups in the Brazilian market, serving the major and minor appliance industry, both through conventional channels and via its website. Due to confidentiality issues, the name of the group is omitted from this paper.

This study is divided into six sections. After the introduction, the second section identifies the literature concerning the relationship between customer retention and transaction profitability. The third section appraises the managerial practice related to customer retention and relationships in the e-commerce realm. The fourth section presents the research methodology used to gather and analyze data, the propositions to be tested and some managerial approaches to be investigated. Then, in the fifth section, the propositions are tested statistically, and qualitative evidence of managerial *praxis* is used in order to enable the authors to reach a consensus. Finally, the last section discusses the implications of the authors' findings and presents some of the conclusions drawn.

2 Customer Retention And Transaction Profitability

In relationship marketing literature, several authors have pointed out the beneficial impacts of customer retention on transaction profitability. Kotler (1999) claims that the longer a customer remains with a supplier, the more profitable he becomes. According to him, frequent buyers are more profitable due to four main reasons: a) they purchase more over the course of time; b) the cost of serving a frequent buyer decreases over the course of time; c) satisfied clients usually recommend the supplier favorably to others; and d) frequent customers are less sensitive to price.

Day (1999) suggests that companies achieve higher transaction profitability by building long-term relationships with their customers. Peppers & Rogers (1993) claim that there is only one way a business can guarantee its financial sustainability, namely by cultivating loyal and satisfied customers. These authors argue that the more purchases a customer makes, the higher the mark-up obtained by the firm will be.

Reichheld & Sasser (1990) declare that the loss of a customer can have a higher impact on a company's profitability than other traditional factors associated with a competitive advantage, such as market-share and unit cost. In a later study, Reichheld & Teal (1996) state that businesses with a high rate of customer loss will face a difficult future, with reduced profits, slow growth, if any, and shorter life expectancy.

In marked contrast with the authors quoted, recent research has challenged the traditional methods adopted by most executives for retaining customers as well as the resulting managerial implications involved. Schultz & Hayman (1999) warn that if all the benefits accrued from customer retention claimed by firms were true, loyalty would not be good for their clients, as they would be paying higher prices and advertising the company for free, in addition to receiving worse attention from the firm.

Dowling & Uncles (1997) suggest that customer loyalty is probably a consequence of the industry within which the company operates, as well as the strength of its brand name. According to them, investments in customer retention do not reap the desired benefits for the strategic positioning and brand equity of the company. Moreover, it is quite possible that these investments generate neither a significant rise in the number of frequent customers nor an increase in the company's profitability.

Reinartz & Kumar (2000) found empirical evidence in a catalog-based retailing company in the USA, which ran counter to some traditional concepts regarding customer retention. These authors point out some anomalies in the relationship marketing theory: a) the relationship between customer lifetime and the corresponding company's cumulative profitability was only verified, in a moderate way, in a small percentage of customers; b) the commercial transaction value diminishes during the course of the relationship between a company and its customers; c) as commercial transactions were analyzed individually, frequent customer transactions were less profitable; d) the concept that attendance costs are lower for frequent customers was not supported.

3 Customer Retention And Managerial Praxis

Recent studies, which question the profitability derived from customer retention on the Web, do not investigate the managerial *praxis* associated with the results observed. More specifically, only the quantitative elements were used as a basis for the anomalies noted with respect to the financial behavior of the transaction of frequent clients, which differ from prevailing relationship marketing theory (Reinartz & Kumar, 2000, 2002, 2003).

Marketing and e-commerce literature abounds with innumerable managerial approaches associated with profitable relationships between companies and clients. The section sets out to analyze some of these approaches, in order to pinpoint the qualitative elements to be investigated in the company under analysis.

a) Supply of homogenous or differentiated products

Alba *et al.* (1997) contend that price plays a highly relevant role when products are easily comparable. Consequently, utilization of differentiated products assures greater profitability for the retailer. Concomitantly, Lynch & Ariely (2000) point to empirical evidence showing that price sensitivity is reduced by using differentiated products and increased by the supply of homogenous products.

b) Product dissemination strategy

According to Mitra & Lynch (1996), dissemination of information not related to price favors a decision based on quality, thereby helping the consumer to select the product which best suits her desires and needs. Bakos (1997) adds that greater qualitative information transparency may mitigate the importance of price, thereby affording greater profitability to the electronic retailer.

c) Customizing communications with the client

Conceptual evidence suggests that the use of customized e-mails results in higher profitability for e-retailers (Chen & Sudhir, 2002). This tactic permits the implementation of differentiated offers, exploiting the individual potential of each consumer and respecting areas of interest, periods and frequency of communication.

d) Marketing orientation adopted

According to Day & Montgomery (1999), the more companies change the focus of their marketing approach from products to clients, the more they begin to gain a full insight into the habits and needs of their consumers. Homburg *et al.* (2000) contend that a strategy geared to clients enables the firms to exploit their financial potential in an efficient manner.

e) Customer retention mechanisms

For Schouten & McAlexander (1995), one of the most important tactics for relationships is the creation of consumer communities on the Web, for clients who share the same values and behavior patterns. Brown *et al.* (2002) show empirically how the construction of a solid structure of virtual communities represents an important source of profit in electronic retailing. For their part, Bolton *et al.* (2000) point out that clients involved in loyalty programs underestimate negative evaluations of the company *vis-à-vis* their competitors. Kotha *et al.* (2004) show a positive association between the market value of companies and the existence of relationship services, such as virtual communities and personalization of websites.

4 Research Methodology

In order to gather relevant input to carry out this research, one of the largest retailing groups in Brazil was investigated. The company's database was analyzed quantitatively to assess the transaction profitability derived from sporadic and frequent customers purchasing via the firm's digital channel, namely its website. Besides, qualitative evidence was also collected from interviews with the main professionals involved in marketing and e-commerce in the firm and through analysis of the company's website and e-mail communications with customers.

Due to the characteristics of the products commercialized – major and minor home appliances with a high average purchase price –, this research is based on the premise that customers may only be considered frequent buyers if they make at least one purchase within a 12-month period (see, Santos & Costa, 1997). It should be stressed that these are the same criteria adopted by the firm under analysis to categorize its frequent customers.

The company was selected because it sells a broad range of products throughout the year, without seasonal variations in supply and demand. The analysis includes all customers who made purchases between the day the firm's website went on the air (July 1, 1999) and the day on which the data was extracted from the database (December 31, 2002).

Hence, from a total of 149,062 customers, a sample of 14,906 buyers (10% of the total) was selected at random, of which 10,421 were sporadic consumers and 4,485 were frequent purchasers. The real value of all the monetary amounts involved in this research was calculated using the inflation rate during the 42 months under analysis, i.e. the value of every purchase was discounted using the inflation rate between the date the purchase was made and December 31, 2002.

The customers were divided into two main groups: sporadic and frequent buyers. Each one of them was classified by their average ticket and segmented according to a "Pareto level", as suggested by Roos (cited in Chatzkel 2002, p.111) and Reinartz & Kumar (2000), as presented in Table 1 below.

Table 1: *Customer Segmentation*

Category	Description
Sporadic 20%	Sporadic consumers with the highest 20% average ticket
Sporadic 80%	Other sporadic consumers
Frequent 20%	Frequent customers with the highest 20% average ticket
Frequent 80%	Other frequent customers

From the theoretical background presented in section 2, the paper aims to test the following four propositions quantitatively:

P1: The transaction profit derived from frequent customers increases as they purchase more frequently.

P2: The ticket value of frequent customers increases as they buy more frequently.

P3: Frequent customers purchase more profitable products than sporadic consumers.

P4: Frequent customers purchase more expensive products than sporadic buyers

The statistical tests used to verify whether or not the propositions were viable were based on variance analysis (ANOVA) and bivariate linear regressions of the data collected, developed with a significance level of 5% ($\alpha = 0.05$). This quantitative analysis dealt with the following selected attributes:

a) Customer Purchasing Frequency: number of purchases made by customers;

b) Transaction Profit: profit accrued from purchases made by clients;

c) Ticket Value: value of purchases made by customers.

In addition to this, the following qualitative factors related to the firm's managerial *praxis* (MP), as depicted in section 3 above, were investigated:

MP1: Supply of homogenous or differentiated products

MP2: Product dissemination strategy

MP3: Customizing communications with the client

MP4: Marketing orientation adopted

MP5: Customer retention mechanisms

Finally, data triangulation was used, combining different types of evidence and procedures, increasing the validity of the research and minimizing the conflicts associated with using only either a qualitative or quantitative approach (Patton, 1990).

5 Data Analysis And Findings

5.1 Quantitative Evidence

The researchers in the field study had access to individualized customer transaction profit margins, discounting taxes and cost of capital.

In line with the empirical and theoretical background herein described, this work tested, in quantitative fashion, the four propositions listed above concerning the financial behavior of transactions made by sporadic and frequent customers in the e-retailing realm.

Proposition 1: The transaction profit derived from frequent customers increases as they purchase more frequently.

In order to test this hypothesis, bivariate linear regressions were used to analyze the commercial transaction mark-up as being dependent on the purchasing frequency of each frequent customer. The regressions took the two segments of frequent customers into account (Pareto 20% and 80%). Table 2 summarizes this analysis.

Table 2: *Regressions Of Transaction Profit As A Function Of Purchasing Frequency*

	R^2	Coefficients	Std Error	t Stat	P-value
Frequent 20%	0.74	-6.18	1.38	-4.46	< 0.01
Frequent 80%	0.56	0.34	0.12	2.76	< 0.05

By the regressions it can be seen that the coefficient is negative (-6.18) for the segment of frequent customers with the highest average ticket (Pareto 20%), indicating an inverse relationship between transaction profit and customer purchasing frequency. In the other segment of frequent buyers (Pareto 80%), the coefficient is 0.34, indicating that transaction profit increases moderately as more purchases are made by customers. In other words, this proposition cannot be supported for frequent buyers with the highest average ticket (Pareto 20%).

This finding allows the researchers to challenge the contention that customer retention always enables companies to obtain a premium price, as suggested by relationship marketing theory (Peppers & Rogers, 1993; Reichheld & Teal, 1996; Kotler, 1999; Day, 1999; Brondmo, 2000).

Proposition 2: The ticket value of frequent customers increases as they buy more frequently.

Bivariate linear regressions were used to analyze the ticket value as dependent on the purchase frequency of each frequent client. The regressions took the two segments of frequent customers into account (Pareto 20% and 80%). Table 3 summarizes this analysis.

Table 3: *Regressions Of The Ticket Value As A Function Of Purchasing Frequency*

	R^2	Coefficients	Std Error	t Stat	P-value
Frequent 20%	0.63	-17.86	5.12	-3.48	< 0.05
Frequent 80%	0.51	-0.02	0.01	-2.49	< 0.05

By the regressions it can be seen that the coefficient is negative (-17.86) for the segment of frequent customers with the highest average ticket, indicating an inverse relationship between ticket value and customer purchasing frequency. In the other segment of frequent buyers (Pareto 80%), the coefficient is -0.02, indicating that the ticket value only decreases very slightly as more purchases are made by clients. In other words, this proposition cannot be supported for all frequent customers using the digital sales channel of the company in question.

This finding runs counter to some conceptual evidence from standard relationship marketing theories, which claim that frequent clients are always inclined to buy more expensive products over the course of the relationship (Peppers & Rogers, 1993; Reichheld & Teal, 1996; Kotler, 1999; Day, 1999; Brondmo, 2000).

Proposition 3: Frequent customers purchase more profitable products than sporadic consumers.

For this test, the average transaction mark-up associated with both frequent and sporadic consumers within each segment are compared. The variance analysis is presented in Table 4:

Table 4: *ANOVA - Average Transaction Mark-Up Of Frequent And Sporadic Customers*

	Mark-up of Frequent Customers	Mark-up of Sporadic Customers	F Calc	P-value	F Crit
Pareto 20%	80.34	86.07	0.62	0.43	3.84
Pareto 80%	16.40	14.92	31.61	< 0.01	3.84

The low value of “F Calc” for the segment of buyers with the highest average ticket (Pareto 20%) indicates that the difference between averages is not statistically significant. In the other segment of consumers, the frequent clients present a higher transaction mark-up (R$ 16.40, approximately US$ 5.60) than the respective value associated with the sporadic buyers (R$ 14.92, approximately US$ 5.10). This evidence led the researchers not to support Proposition 3 fully, as the statement that frequent customers buy more profitable products than sporadic purchasers could not be verified for those consumers with the highest ticket value (Pareto 20%).

This shows that it is not true to say that frequent customers always purchase more profitable products than sporadic consumers, as claimed in relationship marketing literature (McKeena, 1993; Reichheld & Teal, 1996; Kotler, 1999; Brondmo, 2000).

Proposition 4: Frequent customers purchase more expensive products than sporadic buyers.

For this test, the average tickets of frequent and sporadic consumers within each segment are compared. The variance analysis is presented in Table 5.

Table 5: *ANOVA - Average Tickets Of Frequent And Sporadic Customers*

	Ticket of Frequent Customers	Ticket of Sporadic Customers	F Calc	P-value	F Crit
Pareto 20%	R$ 375.54	R$ 455.43	34.05	< 0.01	3.84
Pareto 80%	R$ 126.62	R$ 103.71	449.61	< 0.01	3.84

The high value of "F Calc" for all the segments indicates that the difference between averages is significant. In the segment of buyers with the highest ticket (Pareto 20%), sporadic consumers show a higher average transaction value (R$ 455.43, approximately US$ 157.00) than the respective value associated with frequent customers with the highest ticket (R$ 375.54, approximately US$ 129.50). This evidence led the researchers not to support Proposition 4. In other words the statement that frequent customers buy more expensive products than sporadic customers was not established.

This finding challenges traditional marketing literature, which contends that frequent customers always purchase more expensive products than sporadic ones (McKeena, 1993; Reichheld & Teal, 1996; Kotler, 1999; Brondmo, 2000).

5.2 Qualitative Evidence

Qualitative evidence related to the firm's managerial *praxis* (MP) – as depicted in section 3 – is then investigated below, in order to verify whether the firm under analysis complies with the prescriptions of relationship marketing theory.

MP1: Supply of homogenous or differentiated products

In order to investigate this exploratory factor, five products per week showcased on the home page of the electronic store under analysis, were monitored over the course of a 12-week period, thus involving a total of 60 items. To do this, a Brazilian price comparison shopbot site (www.buscape.com.br) and the www.google.com.br search website were consulted to see if the products in question were to be found on, at least, two other e-retailer sites. All the showcased products were indeed located in other electronic retailer sites, pointing to the fact that the company uses the virtual shop front to emphasize products, which are homogenous and easily comparable with those of their competitors

MP2: Emphasis on qualitative information or prices, as a product dissemination strategy

E-mails circulated to clients and the presentation of the products on the website under analysis were evaluated. The home page merely shows photos and information on prices and forms of payment. Upon selecting a product to be purchased, the company displays the conditions for payment in the center of the screen. Analysis of e-mails shows that the retailer only sends information on prices and prevailing conditions of payment in its weekly broadsheets.

MP3: Approach used for transmission of promotional e-mails to clients (personalized or standardized content)

The company does not send personalized e-mails to the clients registered on its distribution lists. In other words, the same e-mail message is circulated to all consumers. The motive alleged by the company is the inherent degree of complexity involved in setting up a system capable of generating customized correspondence, in addition to the high cost of the data transmission services required for sending individualized e-mails

MP4: Marketing orientation (essentially geared to products or clients)

The marketing approach of the company is product-centric. The purchase sector is specifically responsible for defining the portfolio of products to be promoted, taking into consideration the income targets and profit margins established by the board of directors. In other words, the company selects the products to be promoted on the bases of desired billing and profitability targets.

MP5: Customer retention mechanisms

The company does not implement any special relationship mechanisms such as developing virtual communities, issuing loyalty cards or implementing captivation tactics. The firm concentrates exclusively on providing a fast and secure purchasing channel with reliable delivery deadlines.

5.3 Data Triangulation

In order to explore the impact of managerial *praxis* on the transaction profitability associated with frequent and sporadic buyers, Table 6 presents the triangulation of quantitative and qualitative evidence found:

Table 6: *Triangulation Of Quantitative And Qualitative Evidence*

Quantitative Anomalies Observed in the 20% Pareto Client Segment	Managerial *Praxis* (MP) Observed in the Company
P1: The transaction profit derived from frequent customers decreases as they purchase more frequently; P2: The ticket value of frequent customers decreases as they buy more frequently; P3: The difference in average transaction profitability afforded by frequent and sporadic consumers was not statistically significant; P4: Sporadic clients purchase more expensive products than frequent consumers.	MP1: The company uses e-mails and virtual displays to offer homogenous and easily comparable products; MP2: The company emphasizes price, as opposed to qualitative information on its website and in e-mails circulated to clients; MP3: The company does not send personalized e-mails to consumers; MP4: The company is product-centric as opposed to client-centric; MP5: The company does not implement any customer retention mechanisms.

In the analysis of Table 6, the following factors require greater clarification:

MP1/2) The predominance of homogenous products and the emphasis on promoting price, as opposed to providing qualitative information both in e-mail communications and showcasing on virtual shop windows, would seem to contribute to the increase in price sensitivity on the part of frequent clients, making it easier to compare the price of items on offer in relation to those of the competition;

MP3) The transmission of standardized e-mails, in other words the lack of customization, would seem to make it more difficult for the company to exploit the individual potential of each consumer, thereby acquiring greater control over the financial performance of each consumer;

MP4) The strategic orientation of the company as being product-centric as opposed to client-centric would seem to prevent it from gaining a more in-depth insight into its consumers and exploiting their varied needs and requirements;

MP5) The absence of customer retention mechanisms, such as the creation of virtual communities and loyalty programs would appear to make it difficult for the company to take advantage of the benefits of client retention, which is the theory propounded by traditional relationship marketing literature.

6 Conclusions

The quantitative investigation conducted for this work showed up some anomalies in the financial performance of customers of the company under analysis. In the segment of consumers with highest average tickets (Pareto 20%), sporadic clients performed better in transactional terms than frequent customers.

The above result runs counter to the accepted prescriptions of relationship marketing theory – as seen in the theoretical reference work of this paper –, which contends that frequent clients are always associated with more profitable transactions than those related to sporadic clients.

However, cross comparison of qualitative/quantitative evidence suggests that the transactional deterioration of the frequent clients of the company under analysis is associated with managerial practice, which is not in line with the aforementioned theory.

In specific terms, the benefits of Web consumer retention would only seem to be advantageous for digital companies that are client-centric, which can interact with these consumers. Furthermore, the mere fact of using transactional practices, low differentiation between products and the emphasis on promotion of price on the Web would seem to increase sensitivity to price on the part of the consumers, particularly those who make purchases more frequently.

Thus, the methodological strategy chosen for conducting this research, namely an approach using triangulation of qualitative and quantitative evidence (Patton, 1990), proved to be of fundamental importance in obtaining the results given above.

Moreover, it is important to point out that there are some limitations in the methodology used in this study, the first being the premise that frequent customers of small and large home appliances are clients who make at least one purchase within a 12-month period. The lack of literature clearly addressing the concept of how to determine what constitutes a frequent customer within different industries led the authors to use the same criteria adopted by the firm under analysis. The second limitation is the fact that the database has only been compiled recently, i.e. the data refers to the period from July 1999 through December 2002, which might be considered a relatively short period of observation. Furthermore, other customer segmentations than that adopted here could have been taken into consideration, based on the "Pareto level", as explained in the Research Methodology section above.

It might be said that, in terms of the theories of Kuhn (1970), the study did not detect any structural anomalies in relation to the theory of relationship marketing on the Web, since the transactional decline of frequent consumers was seem to be associated with practices which did not conform to the conceptual principles of client retention. Similarly, it is possible to speculate whether some of the discoveries reported in recent publications by Reinartz & Kumar (2000, 2002 & 2003) – attempting to demystify the importance attributed to frequent clients – might not be open to question, in view of the fact that the research strategy utilized in the studies in reference was based exclusively on quantitative methods, without considering, for example, the influence of managerial *praxis*.

Furthermore, some of the recommendations of marketing theory mentioned in the study would seem to require low investment in the digital environment and, consequently, may prove to be valuable for recuperating or maintaining the value of clients over the course of time. In particular, electronic retailers should consider the implementation of virtual communities, the transmission of personalized e-mails, the dissemination of qualitative information about their products and the promotion of differentiated products on the market.

Lastly, the development of qualitative/quantitative metrics for monitoring the financial trajectory of consumers on the Web, allows electronic retailers to identify possible downturns in the financial behavior of their clients and take specific action to remedy these alterations and enhance the inherent mutual benefits of such commercial relationships.

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