EXPLORING THE EFFECTS OF CUSTOMER PORTFOLIO MANAGEMENT

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Abstract
Nowadays turbulent business conditions provoke organizations to develop unique competitive advantages through efficient use of the available limited resources. At the same time companies deal with increasingly informed customers, seeking high added value and better service at reasonable prices. In this context, the need for rethinking traditional marketing activities determines the interest in searching and designing tools, which are able to analyze, evaluate, develop and manage the relationships with the customers. Thus the customer portfolio management (CPM) concept gains popularity. The paper offers a systematic view of the multifaceted nature of customer portfolio management and its effects on the economic performance of the company. The effects are classified into four main areas: cost reduction; relationship improvement; risk optimization and revenue increase. A conceptual model, which can be used as a base for the creation of methodological instruments for measurement and assessment of CPM effects, is proposed.

Key words: *customer portfolios, customer relationship management (CRM)*

JEL Classification: *M30, M31, D21, D46*

I. INTRODUCTION

Nowadays turbulent business conditions provoke organizations to develop unique competitive advantages through efficient use of the available limited resources. At the same time companies face increasingly informed customers, seeking high added value and better service at reasonable prices. In this context, the need for rethinking traditional marketing activities, in order to provide flexible adaptation pathways, is widely accepted. A broadly acknowledged fact is the reconceptualization in the orientation of marketing - from transactions to relationships (Sheth and Parvatiyar, 1995). That is why customer relationship management (CRM) has become one of the main paradigms of modern marketing, a main priority and an important tool for many companies (Kim, Kim et al., 2010). The dynamic development of scientific knowledge and practical solutions in the field determines interest in searching and designing tools, which are able to analyze, evaluate, develop and manage the relationships with the customers. The customer portfolio management (CPM) is one of the major areas of interest within the field of customer relationships. Central to the concept is the idea that customers and relationships are assets, capable of generating value (Bolton, Lemon, et al., 2004). In this sense balancing the customer portfolio is related to the marketing results of the company (Stanimirov, Zhechev et al., 2016), which outlines the need to explore the different possible effects, through which customer portfolio management can improve the economic performance of a company.

The assessment of the value of customers has been studied by many researchers and practitioners since the 1940s. However, the concept of customer portfolios shifts the focus from individual relationships to the whole customer base and has received considerable attention since the 1980s. Over time it has evolved significantly, intertwining with various achievements from the fields of finance; management accounting; applied mathematics; etc. A significant amount of interest in different CPM models has been seen since the 1980s. However, to the best of the author's knowledge, very few publications address the possible effects, resulting from CPM activities. It is assumed that the effective management of customer portfolios and the differentiation of strategically important customers is vital to the success of companies (Kotler et al., 2015), but far too little attention is paid to the rationale and interdependence of the different possible positive effects of customer portfolio management. The topicality of this study stems from the fact that these effects have to be known and classified in order to be successfully measured and managed.

The purpose of this paper is to offer a systematic view of the multifaceted nature of CPM and its effects on the economic performance of the company and in this regard – to offer some recommendations for future research. The remainder of the paper is organized as follows: Section II outlines the theoretical framework of CPM and analyses its nature and scope. The effects of CPM on the economic performance of the companies are summarized and discussed in section III. The recommendations for future research are presented in Section IV. Section V concludes the paper.

II. THEORETICAL FRAMEWORK OF CUSTOMER PORTFOLIO MANAGEMENT (CPM)

The specialized marketing literature fails to offer a coherent definition for the term „customer portfolio". Despite the extensive research in the field, a general definition and a conceptual model of a customer portfolio does not yet exist. Therefore, an attempt to fill this gap may be carried out by analyzing the nature of customer portfolios from several different perspectives. It has been reported that previous studies lack a systematic set of constructs for testing of random and non-random relations in a customer portfolio (Terho & Halinen, 2007, p. 339). A number of authors offer models for customer portfolio management without defining the essence of the concept. A probable explanation for this may be the lack of uniform understanding in determining the economic category "portfolio". Therefore a much more systematic review of the overall theoretical framework in defining the term "customer portfolio" is necessary for identifying and addressing the weaknesses in the existing approaches. It can also serve as a reliable benchmark for further analysis and development of practical solutions in the field.

The analysis of the extant literature suggests several different perspectives on the definition of a customer portfolio. The biggest group of authors defines it as a concept for analyzing the relationships between buyer and seller (Eng, 2004, p. 49). However, differences in terms of the possible scope and aims of the analysis are identified, i.e.: allocating limited resources of the organization (Ford, 1997); analysis of customer profitability (Smith, 2002); and providing long-term profitable relationships with customers (Kotler et al., 1996). Likewise, Storbacka (1977) uses the definition of "powerful analytical tool for the development of marketing strategies". A similar idea is enshrined in the definition proposed by Tikkanen et al: "source of income and knowledge, which facilitates the creation of value for customers and thus develops the company offers" (Tikkanen et al., 2007, p.199). It can be concluded that the existing diversity of objectives testifies to the complex options provided by CPM. It is believed that setting a goal in the definition of the construct is not necessary given the current economic reality, which requires flexible organizations and quick adaptation to the dynamic changes in the environment. Within this group of authors the most recently delivered definition is "a construct for managing relationships with customers as market-based assets" (Nenonen, Storbacka, 2016, p. 147). This view implies that there is a connection between the customer portfolio and the portfolio theory and its relevant capabilities of managing market-based assets. It also does not contradict to the aforementioned assumption for different (in time period, for certain customer group, according to situational factors) objectives for CPM.

Another group of authors see the customer portfolio as a collection of all customers (or customer relationships) of a company. Here comes Eng, who defines the term as "a mixture of all the different relationships between supplier and buyer of a company" (Eng, 2008, p. 570), and adds that its consideration as a part of a network allows building sustainable competitive advantages (ibid ., p. 584). Similarly Stanimirov asserts that the customer portfolio is one of the tools for effective management of customer relationships and proposes the definition "all customers of the company, structured in a certain way" (Stanimirov, 2013, p. 176). A broader perspective is adopted by other authors with the understanding of customer portfolio as "a set of relationships with customers, suppliers, intermediaries and other partners selected, based on certain criteria" (Rebyazina, Smirnova et al. 2013, p. 38). It should be noted that all these definitions do not focus on the presence of several customer portfolios within the customer base of the company, which is argued by other authors (Tarasi et al., 2011; Thakur & Workman, 2016). A possible argument of the need for such assumption may be sought in the turbulent business environment that requires the development of different strategies and tactics for individual products, markets and customers. The new marketing discourse focuses on the lack of universal solutions, because of the difference in goals, values, resources and understanding of individual market participants. In this context, it can be argued that the existence of various customer portfolios within the total customer base of organizations is possible according to the goals set without excluding the possibility, that customer portfolio and customer base perfectly match under certain conditions.

The authors, who introduce the idea that the customer portfolio can be viewed not as a management object, but as a context (Terho & Halinen, 2007, p.338), can be distinguished as a third group. In this sense Reinartz et al (2004) believe that the customer portfolio of a company, including all relationships with its customers, is the context that forms the framework for a variety of strategic decisions in the marketing field. This position refers to the essential differences between the characteristics of different types of exchange relationships with customers, that suggest different challenges in their management into a single customer portfolio.

From the review carried out so far is concluded that the differences in the opinions of the authors about the nature of the customer portfolio stem from the fact that they are focusing on various aspects of the content of the concept. This is to be expected, given the origin and development of the concept, based on research results of the mid-twentieth century, in the following areas:

- *Relationship marketing and customer relationship management*. Relationship marketing can be regarded as a starting point for the development of CRM. Moreover, from this background also arises the concept of customer portfolio that allows optimization of the efforts of managing relationships with customers and thus maximization of the company's profit (Ritter & Andersen, 2014).

- *Business networks theories.* The business networks approach contributes to the development of the customer portfolio concept, representing an understanding of the context in which relationships with customers take place. It should be pointed out that some of the models for customer portfolio management are designed by scholars from this scientific field.
- *Modern portfolio theory.* Here the main subject of interest is solving practical problems of investing capital in various types of assets in uncertain conditions, as though even if the assets are selected individually, the balance between risk and return of the entire portfolio of assets is desired. This idea corresponds with the idea of the customer portfolio, which like the financial portfolio is formed through selection between different market assets (i.e. customers), which are characterized by different levels of risk and return (Tarasi et al., 2011, p.1). Another similarity between the customer and the financial portfolio is that the allocation of resources among different assets can improve the performance of the company.
- *Resource based management.* Companies, that optimally manage their resources, are expected to have a strong competitive advantage (Hunt, Morgan, 1997). As far as customer relationships are determined as a relational resource of strategic importance (Hunt, Morgan, 1995), the customer portfolio gains popularity because of the opportunities it provides for efficient allocation of scarce resources.
- *Value based management*. It determines the interest in conceptualizing, measuring and managing the value of the relationships between seller and buyer, which contributes to the development of the customer portfolio concept.

It can be concluded that these areas form the theoretical framework of the customer portfolio concept (Fig. 1). This view does not claim to be exhaustive and axiomatic, but it attempts to account for the interconnectedness amongst the presented areas on the one side, and on the other – to their complex nature and evolution, projected in the field of intersection of many other concepts and theories.

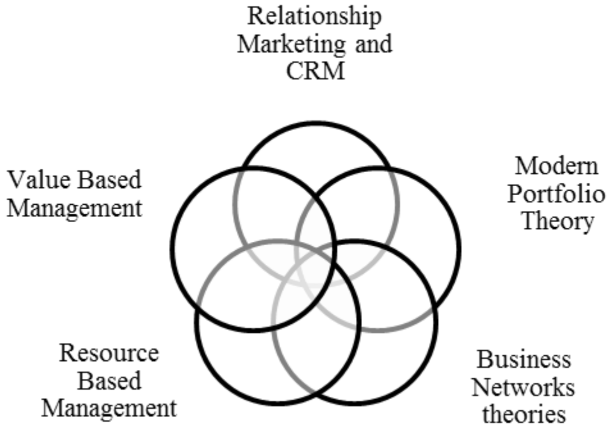

Figure 1 - Theoretical framework of the customer portfolio concept

In view of what has been discussed so far, it may be supposed that managing customer portfolios also has a multifaceted nature, which results in a variety of opinions about its definition. Some authors focus on the process nature of the management of customer portfolios, stating that this dynamic process creates value by balancing current relationships with customers of the company" (Johnson & Selnes, 2004). This view is shared by Rajagopal & Sanches (2005, p.314), who add that it is a "multi-level process that encompasses understanding the customer portfolio, developing a plan, managing implementation of the plan and evaluation thereof". Other authors have similar understanding of the stages of the process, but they arrange them as follows: (1) analysis of the value of the company's customers; (2) allocation of resources among different customers or customer groups in order to create a balanced customer structure (Terho & Halinen, 2007). It is assumed that the key priority in the management of customer portfolios should be identifying the characteristics of different customers within the customer base of the company (Terho, 2009).

Other authors present an extended understanding of the management of customer portfolios by including the importance of the process not only for the present value of customers, but also the future. For example, some define it as "the classification of customers or customer segments according to their current and future value" (Rajagopal & Sanchez, 2005). In this sense is the broader definition of Terho & Halinen (2007, p. 721), according to which the analysis of client portfolios is, "an activity by which a company analyzes the current and future value of its customers for developing a balanced customer structure through effective resource allocation to different customers or customer groups". It should be noted that this definition is based on a review of theoretical models for customer portfolio management, which raises questions about its accuracy towards corporate practices. A subsequent study of Terho confirms the differences between theory and practice, and suggests the following operational definition of CPM: “the company’s activities in analyzing its portfolio of customers pertaining to their role in providing current and future value for the focal company, and its responsiveness to the analysis conducted” (Terho, 2009, p.382).

However, there is an inconsistency with some of the definitions. For example, Möller and Halinen (1999) explain CPM as, "management of different types of customers who require different management approaches to ensure profitability," but did not distinguish the concept of managing relationships with customers at all. Other authors have launched the idea that this is "methodological resource allocation and implementation of marketing strategies for retaining and developing the most valuable customers of the company" (Thakur & Workman, 2016). A serious weakness with this definition, however, is that it sounds similar to the concept of "key account management".

The results from the presented literature review reveal the following characteristics of the process of customer portfolio management:

Firstly, it is a continuous and non-stationary process that is associated with the processing and analysis of information for the customers and the environment in order to take adequate situational decisions.

Secondly, the management of customer portfolios can be done for different purposes, which determines various options for structuring the stages of the process, the selection of appropriate tools and the developed strategies.

Thirdly, CPM is an internal activity with a focus inside and outside the company, because it requires taking into consideration internal objectives, resources and limitations, as well as the influence of the external environment.

Fourthly, the activities of CPM can be performed at different levels of governance and affect not only the marketing results of the organizations, but are associated with other functional areas. That is why it is required to achieve integration of the CPM activities into the overall value chain in the company.

III. CUSTOMER PORTFOLIO MANAGEMENT IMPACT ON ORGANIZATIONAL PERFORMANCE

The brief theoretical overview of the nature and scope of customer portfolios presented thus far allows us to make the assumption that each business organization has its own portfolio of customers, whether it manages it consciously or not. The role and importance of the customer portfolios has attracted scientists’ attention since the 1980s as a logical reflection of a number of new strategic concepts, demonstrating the triumph of customer-centric marketing. Cross-selling, up-selling, as well as various tools for customer engagement (club concepts; bonus programs; customer magazines; differentiated service, etc.) and integrated multichannel distribution become popular around this time. All this requires companies - which are seriously compromised by the severe economic, financial and debt crisis and the ensuing regulatory reforms - to implement "new interpretations" of their policy on managing relationships with customers and in particular to focus on the opportunities for managing customer portfolios.

Reasons and motives for purposeful customer portfolio management may be sought in the opportunities they provide for businesses. The desired effects of their optimal management can summarized as follows:

Firstly, a number of authors share the view of the company's customers as an essential intangible asset, capable of generating value and achieving profitability (Rappaport, 1998; Hogan et al., 2002; Gupta, Lehmann & Stuart, 2004; Gruca, Rego, 2005). This understanding justifies the relationship between the customer portfolio and the shareholder value of the company (Payne, Frow, 2005; Golec, Gupta, 2014). It should be pointed out that shareholder value maximization is often defined as a leading goal for the companies. Later this concept was further improved and stakeholder value maximization became one of the key fundamental components of the development of the principles of corporate governance (Dankova, 2006) and sustainable development (Steurer et al., 2005). Keeping in mind the relevance of these concepts, it should be emphasized that CPM is a prerequisite for the successful functioning of the overall architecture for managing relationships with customers, which in turn can help in achieving the main strategic goals of the organization, including the creation of added value for various stakeholders and ensuring the sustainable development of the organization.

Secondly, CPM ensures a balance in the allocation of limited resources (financial, human, time, technology, etc.). Provision of information necessary for CPM creates prerequisites for greater accountability and opportunities for identifying trends, which leads to more responsibility in spending costs for relationships management. Several studies highlight the pertinent role of the focus on analytically-based decisions, resulting in balance and efficiency in the allocation of scarce resources of the organization by individual customers and marketing tools, which in turn positively influences the economic performance of the company (Kumar, Shah, 2009; Verhoef, Lemon, 2013).

Thirdly, there is evidence that formal systems and models for identifying and managing relationships with customers with high potential for development, including the use of a CPM model, are able to improve the economic performance of companies, because of their influence on income and expenses (Becker, Greve et al., 2009; Verhoef, Lemon, 2013). It is believed that the management of marketing activities and its "tuning" according to the specific characteristics of customers affects the level and volatility of the expected cash flow of the company (Shah, Kumar et al, 2016). On the other hand cash flows are among the fundamental determinants of firm performance in business valuation (Dechow, 1994), as ceteris paribus an increase in the value of cash flow positively influences the value of the company (Vuolteenaho, 2002; Fernández, 2007), and an increase in their volatility – negatively influences the value. (Froot, Scharfstein et al., 1993; Zhang, 2006).

Fourthly, CPM allows the identification of the most prospective relationships and the differentiation of key customers. A number of marketing studies provide application of the Pareto 80/20 rule, which adapted in terms of customers of an organization suggests that approximately 20% of customers contribute to 80% of the revenues of the organization and vice versa. Given the increasingly competitive environment and the limited resources that companies have today, it can therefore be assumed that treating relationships with different customers equally is not rational. Here, it should be noted that some authors suggest that companies need to "tailor" their value offer according to customer's key attributes (risk, return, loyalty, share of wallet, CLTV, etc.) and their compatibility with the selected goals of the company (Friend & Johnson, 2014). These findings raise intriguing questions regarding the possible effects of CPM activities on the characteristics of the customers.

Fifthly, CPM assists the companies in establishing priorities for developing their client base (Brennan, Canning et al, 2010). This can be seen as a prerequisite for taking appropriate decisions in managing customer relationships at strategic and operational levels. Hence, it could conceivably be hypothesized that CPM helps the company to develop its relationships with key customers with greater confidence.

Sixthly, the presence of many actors in the same customer portfolio is a precondition for the emergence of conflicts between their individual business goals and interests. It is widely believed that marketing exchanges are usually characterized by information asymmetry (Mishra, Heide, et al., 1998). Therefore, the willingness of each company to increase and maintain their competitive advantage over other market players leads to a need to coordinate the interests of all participants in its customer base. An implication of this is the need for intentional CPM activities.

Some of the issues emerging from the aforementioned motives relate to the substantial contribution of CPM for the economic performance of the companies. The key aspects of this contribution can be listed as follows: costs reduction, relationship improvement, risk optimization, revenue increase. They are illustrated in Fig. 2.

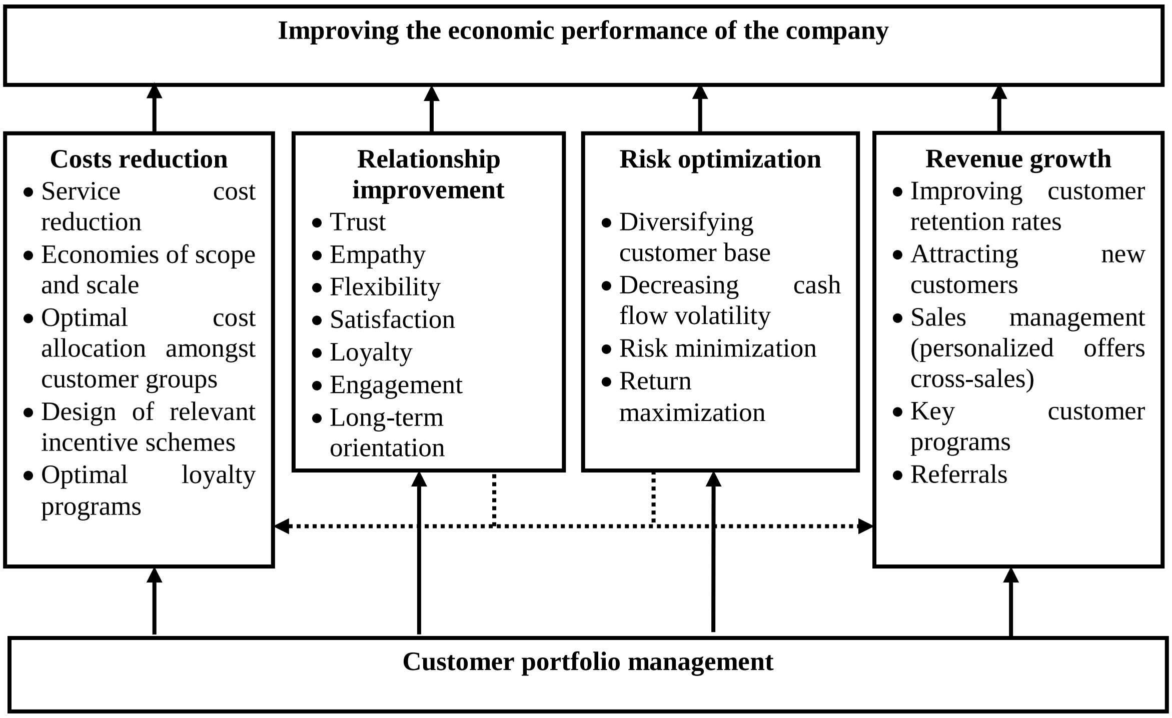

Figure 2 - Possible effects of customer portfolio management

The conceptual model is constructed on the basis of a review of extant specialized literature that provides theoretical or empirical evidence for the illustrated relations. The presented dotted links suggest the possibility, that improving relations and risk management may in turn influence the revenue and expenditures of the organization, and thus may impact on its economic performance and the created value. The simultaneous manifestation of all illustrated effects is not mandatory. It is a function of determinants such as: vision; mission; values of the organization; targets; situational factors; used tools for managing customer portfolios; and engagement of the staff in CPM processes, etc. In this context, although the role and importance of CPM, as well as its potential to create value in different ways, it should not be seen as a strategic imperative for any company - it is neither an universal tool for maximizing the revenue base, nor a "springboard" able to expand and strengthen customer relationships. In this sense the endeavor to build closer relationships with customers in every possible way could prove to be ineffective. The focus on the "the forest, not the trees" implies the possibility of an "unattractive" (at some point, but promising in the future) customer (or customer segment) to have a positive impact on the performance of the company in the long term (Johnson & Selnes, 2005). It can therefore be assumed that every company has to assess the economic efficiency of taking any CPM activity, which is associated with the use of certain resources.

IV. LIMITATIONS AND DIRECTIONS FOR FUTURE RESEARCH

In this study, a conceptual model of the possible effects of customer portfolio management is developed, but not empirically tested. The proposed model can be used as a base for the creation of methodological instruments for the measurement and assessment of the effects of CPM. Hence, future research might be performed to empirically test and measure the impact of CPM on the economic performance of companies.

Future studies can be carried to explore the factors that influence the successful deployment of CPM models. It is known that “the success of CRM projects is not unconditional” (Stanimirov, Zhechev et al., 2016, p.10). There is evidence that between 30% and 80% of the CRM initiatives do not achieve the predetermined goals (Nelson, 2002). Different authors address the possible reasons for these failures (Foss, Stone et al., 2008; Almotairi, 2009). In that sense the research of the CRM success factors is not a new topic for the scientists and there are different frameworks proposed (Alamgir & Shamsuddoha, 2015). However, extant literature does not provide evidence for specific CPM success factors, even though there are a lot of critiques towards the different custom portfolio management models available (Gelderman, Van Weele, 2005).

Moreover, further research regarding the importance of the customer type would be of great help in managing customer relationships. There are questions to be asked: Are there “best” type customers (or best combination of customers), that determine the achievement of all of the aforementioned positive effects? Should we focus only on the customers, who are the most loyal (and/or profitable, satisfied, flexible, etc)? There are a number of authors, considering these issues and attempting to answer them in their research studies. However, today their answers sound inconsistent and definitely involve certain contingencies and restrictions. For example it is widely acknowledged that acquiring a new customer is more expensive than retaining an existing one (Bitran & Mondschein, 1997) and in this sense focus on current customers (especially those with increasing in time profitability) is the preferred strategy (Morgan & Hunt , 1994; Palmer, 1995; Reichheld & Teal, 1996). It is known that “having enough loyal customers mean a financially stable company that receives higher profits, growing sales and is superior to the competition” (Isoraite, 2016). At the same time, there is evidence, that transaction-oriented disloyal customers can represent a profitable segment (Reinartz & Kumar, 2000). In addition it turns out, that loyal customers are not always the most profitable segment (Tien, 2014). It is confirmed that there is a heterogeneous distribution of the profit of companies from different clients (Niraj, Gupta & Narasimhan, 2001). This testifies to the role and functions of different types of customers for companies in the long run (Walter , Ritter et al., 2001). It is believed that the formulation of unambiguous answers to the questions above is a too ambitious a task. The diversity of viewpoints in the literature gives us grounds to assume that organizations should not focus only on the development of relationships with a group of clients, but to seek balance in managing the "amalgam" of all of its customers - from transaction-oriented to strategic partners. That is why issues of customer characteristics (incl. company size; industry and organizational structures; etc.) can be used as important contextual variables in order to measure their impact on the positive effects of CPM activities.

V. CONCLUSION

The understanding of customers as strategic resources capable of generating value that can be measured, managed and maximized is leading for the development of the customer portfolio concept. Over time, the evolution of the multifaceted nature of customer portfolio management has pushed research as well as practice towards the exploration of new opportunities for effective management of customer relationships. The interdisciplinary theoretical foundation of the concept of CPM, which is discussed, summarized and clarified in the paper, determines the variety of opportunities that it provides for organizations, as well as the diversity of tools that can be used. That is why in the last thirty years customer portfolio models have seen an increase in popularity and areas of application. This can be attributed to the possible positive effects, which are expected from intentional CPM activities. The present study was designed to determine these possible effects. The paper confirms the previous findings about CPM's role and its importance for the company performance and suggests that the CPM effects can be summarized into four main groups: cost reduction; relationship improvement; risk optimization; revenue increase. It is believed that some of them are interconnected and all of them have the potential to impact positively on the performance of organizations and the created value. This is also the rationale for the need to take deliberate and "tailored" measures for customer portfolio management.

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