Measuring customer value? Don't overlook product returns

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When trying to identify "good" customers, managers often ignore those who return products, or might even consider those customers non-ideal, decreasing the resources devoted to them. In the long term, however, satisfactory product return experiences can actually create a valuable long-term customer whose contributions far outweigh the associated costs, according to a new study in the *Journal of Marketing Research*.

"Product returns are no small part of the firm-customer exchange process, currently costing firms about $100 billion annually," write authors J. Andrew Petersen (University of North Carolina) and V. Kumar (Georgia State University). "However, these same returns create long-term value because customers who feel there is little risk in making the wrong purchase keep coming back."

To determine the extent to which product returns could benefit a firm, the authors conducted a large-scale field experiment with 26,000 customers over six months from an online retailer. Customers were divided into five groups: a control group that received no marketing effort whatsoever, several groups that received traditional approaches to product-returning customers, and finally the model group, which factored in both the consumer's positive attitude toward returns, as well as the cost to the company of those returns. The study directed these five marketing strategies toward customers for three months, and then observed the customers for an additional three months.

The results showed that the maximum profit during the field experiment

was achieved, hands down, in the model group. When managers took into consideration not only the cost of the return process but the positive effect of returns on customers, and targeted marketing accordingly, they brought in $1.8 million compared to the control group's $1.22 million. By paying attention to the product returns instead of ignoring them or swallowing them whole as a necessary cost, managers were able to strategize ways to reduce the cost of the return process overall.

"Retailers who do not consider product returns in their measure of customer value (even simply as a cost that needs to be managed) are missing out on profits they could be obtaining by understanding and allocating resources to product-returning customers. Paying attention to these customers pays off," the authors conclude.

More information: J. Andrew Petersen and V. Kumar. "Perceived Risk, Product Returns, and Optimal Resource Allocation: Evidence from a Field Experiment." Forthcoming in the *Journal of Marketing Research*.

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