Fast-track Upturn.

Disrupting customer acquisition for 2020 and beyond

Featuring new consumer research, analysis of Klarna data points and commentary from leading retail futurist Andrew Busby.

Klarna.

Executive summary.

It's no secret that retailers always want to gain and retain more business. In a post-COVID-19 world it will become vital. The paradox is how to do this while keeping Customer Acquisition Costs (CAC) low, lifting Customer Lifetime Value (CLV) and boosting propensity to buy. Finding new ways to do this will be vital for a fast retail recovery.

This paper explains how historic CLV perspectives are holding modern retailers back from realising their full potential. It outlines new models for success including the 'Klarna Effect', what it means and how it can stimulate a re-investment loop that delivers greater ROI for customer-facing marketing strategies.

Why it's a 'must read':

- We explore the challenges retailers face and why they have to think differently about how they measure success.
- Encourage retailers to discover new and better ways to drive acquisition.
- Discuss new engagement approaches for conversion, loyalty and advocacy to boost CLV.

Drawn from insights of 2,000 UK shoppers, we reveal where retailers should be spending money freed from acquisition. Giving them deep market insight to help win revenue, drive 'gain-and-retain' engagement engines and fulfil their growth potential in the next decade and beyond.

Impact of Coronavirus (COVID-19).

Between writing and publishing this report, the world has been rocked by the COVID-19 crisis. All retailers have been affected but undoubtedly physical retailers across every category have been hit the hardest, with long periods of store closure and loss of high-peak seasonal sales.

While no-one knows how long it will take for revenue levels to bounce back post-lock down, we are certain that understanding customers and metrics around sales performance will be crucial on the road to economic recovery.

As retailers re-formulate their strategic roadmaps, establishing more accurate cost models, and crucially identifying new ways to create revenue upturn, will be vital to their regeneration. We hope that this paper can provide some fresh insight on the topic of CLV, helping them to hack sales growth and get back on their feet faster.

Foreword.

Andrew Busby, top 20 global retail influencer, CEO of Retail Reflections and IBM Futurist.

2020 promises to usher in even more demanding and connected consumers. Retailers will have to adopt new, more effective approaches to align brands with their customers. Clinging to obsolete models, based on outdated customer behaviours, will not be enough to keep customer value alive.

It's time for an engagement driven approach.

Traditional methods to establish customer value and cost, rely on sales-first retail models, conceived years before digital and social took hold and are generally based on historical data and traditional marketing campaigns.

Today's consumer has more options than ever before. So, applying traditional metrics to a non-traditional consumer is planning for failure.

Emotional connection is now a more significant driver of sales than price or product. Optimising acquisition costs, allowing brands to better invest in customer engagement and advocacy, are now the most effective ways of tracking a customer's propensity to spend (and in raising it).

The power of partnership.

Where retailers might once have invested heavily in advertisers or affiliates to acquire customers, smart retailers are switching the focus to optimising new strategic partnerships, with service providers that deliver big benefits.

Klarna is one of those providers. With Klarna, retailers can 'hack' the acquisition process, gaining immediate access to pre-engaged and already loyal Klarna consumers, at a significantly lower cost than if they had to go out and acquire new customers. Klarna lowers upfront acquisition costs, which increases total lifetime value by allowing retailers to focus the saved money on nurturing and advocacy.

What's more, the unique combination of convenience, brand appeal and user experience delivered by Klarna significantly boosts engagement, positive sentiment and propensity to spend over time.

Andrew Busby
Founder and CEO of Retail Reflections.

Measuring customer value in an evolving market.

The first step is understanding CAC.

The key to understanding customer profitability is knowing the cost to get them hooked in the first place. For startups, who need to capture audiences and scale up fast, Customer Acquisition Cost (CAC) is often their single most considerable marketing expense. For established retailers, a high CAC often pairs with a high incidence of churn or weak loyalty. If CAC goes unmanaged, it can inhibit growth or result in an unfeasibly long pay-back period (the time the customer needs to be retained before CAC is recovered).

CAC is typically calculated as follows:

$$\text{CAC} = \frac{\text{£ total acquisition spend (per period}^{*}\text{)}}{\text{\# of customers acquired (per period}^{*}\text{)}}$$

**the period will depend on your business, churn rate and sales/investment cycles.*

Establishing Customer Lifetime Value (CLV).

The CLV estimates how much revenue you can hope to realise once you've captured a customer. Traditionally, this is based on typical easy to gather sales metrics, including the Average Order Value (AOV) and purchase frequency. These provide an estimate of the average customer's value to the brand.

$$\text{CLV} = \text{AOV} \times \text{Freq (F)} \times \text{Retention Period (RP)} - \text{CAC}$$

What's wrong with this approach?

While this formula has provided retailers with a simple model to gauge success, the calculation is based on historical data and a stable market, with consistent engagement and results. It's no longer relevant to modern omnichannel and pure-play retailers. Dynamic, fast-paced and constantly evolving markets need a new formula that considers more variability – and which reflects the retailer's ability to influence the consumer emotionally over time, through highly targeted digital, social and CRM-related initiatives.

A future-focused CLV calculation.

Today we must think beyond annual revenue per customer to their 'propensity to spend', taking into account any future growth potential based on the retailer's ability to nurture and engage its customers.

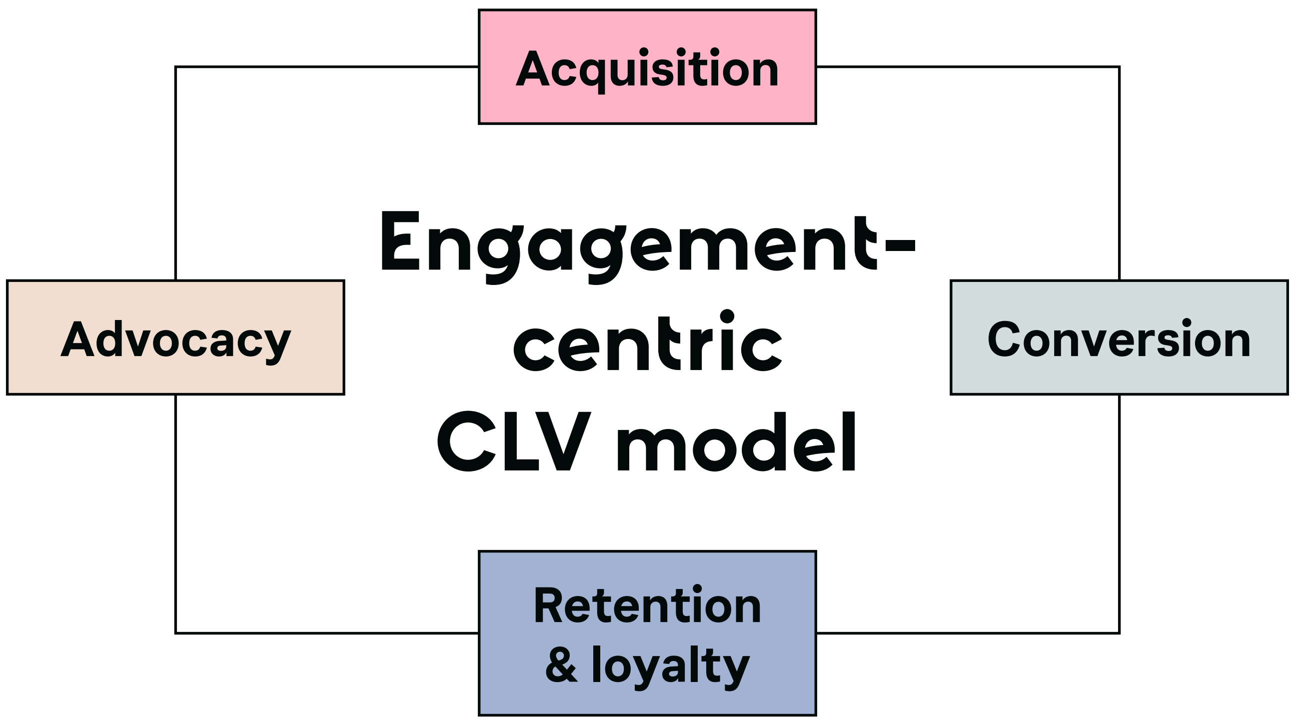
For example:

New CLV = propensity to spend ((AOV x F x RP) + conversion and revenue uplift + advocacy + loyalty) – CAC

Here, propensity to spend is measured by the number of positive customer engagements per annum. At the most basic level, these 'engagements' include volume of transactions, but also incorporate softer metrics such as frequency of engagement with advertising, social media interaction, click throughs and dwell time.

An engagement-centric approach to CLV that covers acquisition, conversion, retention and advocacy.

This new model of CLV is far more aligned with customers' omni-channel journeys and how they are thinking and behaving in 2020. By combining traditional KPIs with new forms of customer intelligence, it encompasses buying behaviour and brand resonance, which gives a far more accurate measurement of their projected future spend.



Hacking CLV & driving growth with Klarna.

What if you could short circuit the process and reach new customers quickly and cost-effectively?

There are lots of stats showing it's cheaper and easier to sell to an existing customer than acquiring a new one. While 20-25% of new customers will buy, that rises to 60-70% for existing customers. The more customers you keep, the faster you can reap the reward and grow.

The Klarna Effect.

Let's take the traditional sales funnel. Imagine your sales hopper automatically filled with millions of customers – all primed to buy, empowered to spend and with no friction points to lock them out.

With no need to spend on acquisition, the money saved can strategically be invested in engaging, nurturing and enticing them to buy more, more often and at a higher value.

With less effort, time and cost, you can plug any leaks, remove churn and ensure more consumers reach the bottom of the sales funnel faster – while spending significantly more with you along the way. Sounds like magic?

We like to call it the **Klarna Effect**, which is based on our observations and data from working with international retailers and brands.

How it works?

With Klarna, 85 million global consumers are already enabled and seeking to spend with our pay later options. They have our app, can use online and in-store and are empowered to buy what they want, when they want.

In the UK, over 7 million consumers have used Klarna's payment options; with an average of 88,000 new consumers added weekly. Two-thirds are using Klarna to purchase across multiple retailers in our network. Meanwhile, retail stats show we're driving millions of referrals and outbound traffic from our owned channels to our retailers per month, as highly engaged consumers actively seek out Klarna retailers via our social channels and shop directory.

Delivering a new formula for success.

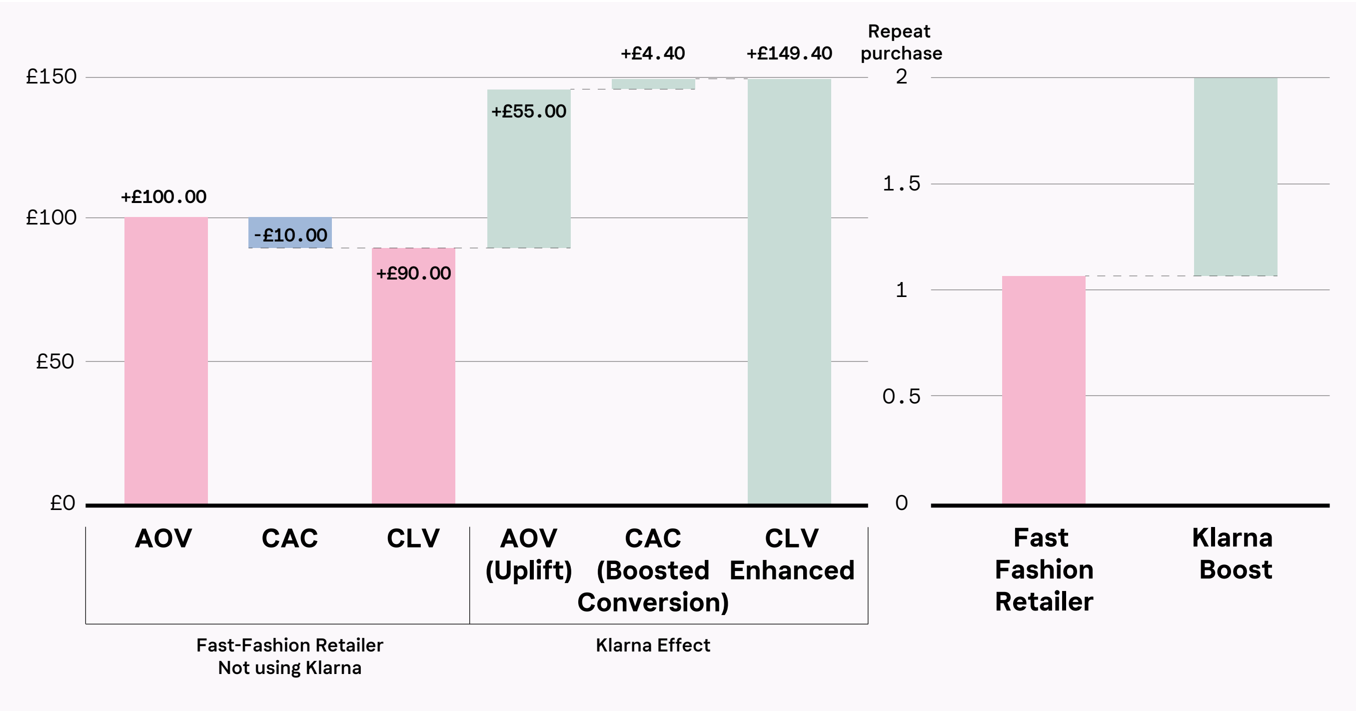
What happens if we import the **Klarna Effect** into our CLV model? What does it mean for our new future-facing value calculation?

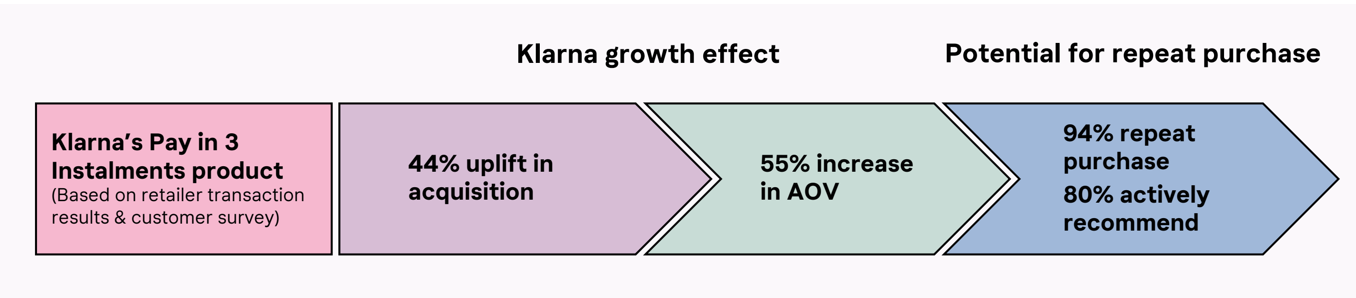
CLV with KE = (Propensity to buy + Klarna value uplift) – (CAC – Klarna conversion uplift)

How does this boost retailer engagement and CLV results?

The following table shows how Klarna and its own marketing 'halo effect' impacts every element of the retailers customer journey, to deliver a significant uplift in CLV for modern retailers, especially for those looking to reduce CAC and make their business more profitable without impacting growth.

So let's look at an example of how:





Let's add some of the figures above into our CLV equation and see what happens:

Imagine a fast-fashion retailer with a current CAC of £10.00 and propensity to buy of £100/customer.

Without Klarna

CLV = £100 – £10 = £90

With the Klarna Effect
(55% AOV uplift and 44% conversion increase)

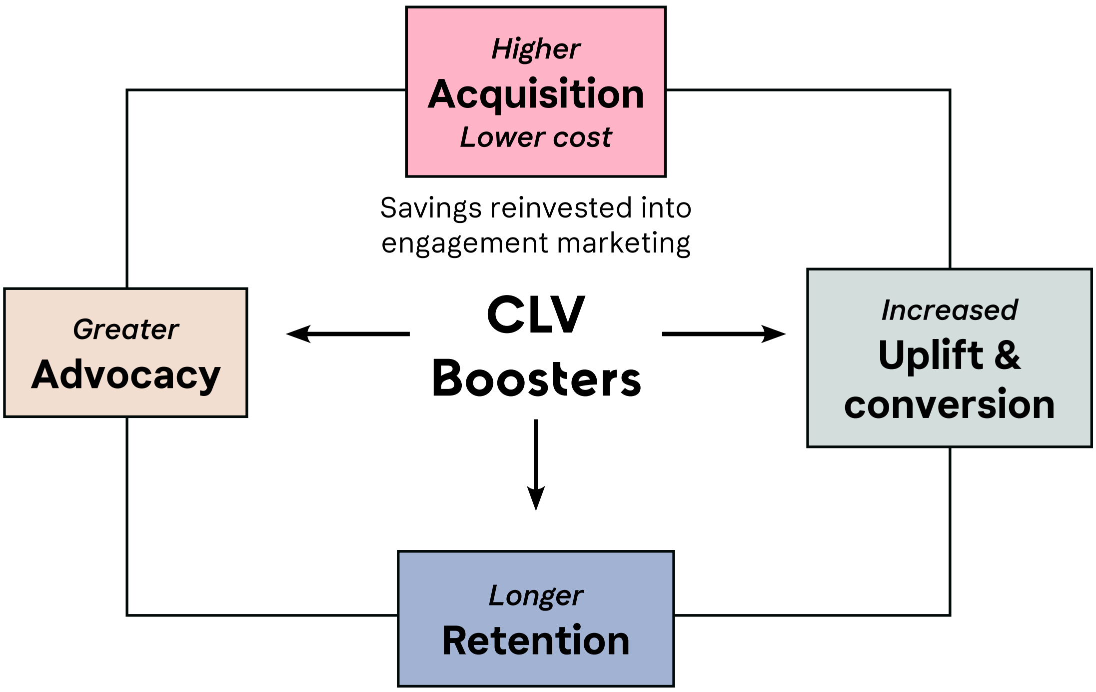
CLV* = £100 + £55 – (£10 – £4.40) = £149.60

	Acquisition	Conversion	Retention & loyalty
The Klarna Effect	*Lowers CAC via:* • Access to pre-engaged Klarna consumers. • Merchant marketing of Klarna availability. • Benefit from Klarna brand awareness through campaigns, experiential and social. • Klarna website, app and shop directory as an entry point, driving referrals to retailers.	*Increased AOV and sale volumes via:* • Empowerment with multiple payment options – pay in 30 days, instalments and financing. • Ability to try before you buy. • Smooth and frictionless UX and checkout. • Online and in-store availability.	*Increases retention and engagement via:* • CSAT > 89%. • One-click repeat purchase. • Curated/co-branded promotion and content across all channels, driving consistency of touchpoints and familiarity. • Post-purchase repayment management and features such as report a return and snooze available in the Klarna app. • 24/7 customer support chat.

Increased propensity to spend

***The Klarna Effect** can also create a growth accelerator for retailers by allowing them to optimise ROI on their own marketing spend.*

By harnessing the CAC saving and reinvesting it into the customer-engagement cycle, spend can be used in new engagement strategies. With no negative impact on customer acquisition levels, this unlocks new resource to drive the AOV, frequency and retention even further, boosting CLV and accelerating growth.



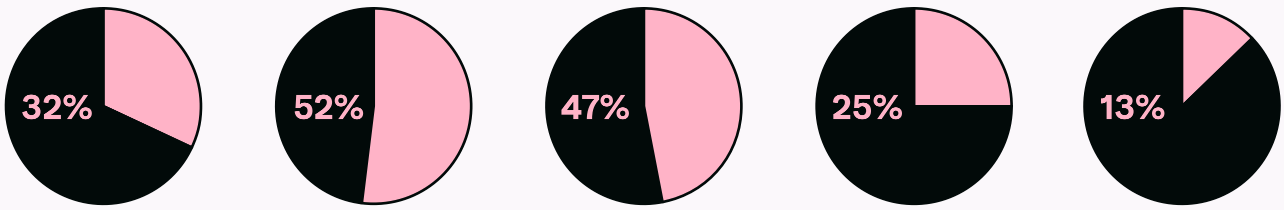
Optimising customer engagement in 2020.

It's clear the right partnership can help you unlock savings in your customer acquisition and engagement chain. How can they utilise their existing budgets to achieve maximum ROI?

1. Acquisition.

Tip #1:

**Today's customers are won and lost online.
Make every digital interaction count.**



Of consumers use a store as a starting point. | Start by using a search engine. | Of shoppers go directly to their favourite brand or retailer's website. | Go to auction sites or second-hand marketplaces. | Turn to social media platforms.

With social media platforms playing a huge role in marketing, retailers should up their investments in digital tactics such as affiliates, SEO and PPC to remain at the forefront of the consumers mind but also to ensure they are easily found.

Tip #2:

**Don't get too close, too soon.
Focus on building an emotional brand connection.**

While personalisation certainly has a place in nurturing existing customers, our research suggests a creative brand campaign can be a more effective way of acquiring new customers. Only **6%** of consumers say personalised marketing would make them consider shopping with a new brand or retailer they haven't bought from before. **Fifty nine percent** are fed up of being targeted with ads for products they've already looked at or purchased online, and **49%** said it irritates them when brands and retailers get personalisation wrong.

33%

Of consumers said **smart or humorous advertising would encourage them to visit a brand or retailer's website** or store, whereas...

39%

Aged 16-34 rank this as the factor most likely to influence them

Tip #3:

Create memorable real-life experiences.

One in ten consumers are drawn to brands for the first time by pop-up shops and real-life experiences; especially for Gen Z where it's double this. To drive footfall to physical stores, brands need to recognise this behavioural change isn't going anywhere. Consumers want to engage in emotional experiences.

35%

Of consumers are likely to shop with a brand or retailer that is **associated with fun experiences**

Thirteen percent are drawn in by the credibility or cool factor of a brand, with Gen Z **22%** are likely to admit to this.

Expert analysis.

"The problem with personalisation today is that it's not really personal. Instead, it's often retrospective, intrusive, irritating or simply out of context. **The amount of content created and targeted at consumers is increasing exponentially, resulting in the development of a 'digital filter'.** We subconsciously block out any content that isn't immediately appealing – meaning traditional marketing methods are becoming less and less effective and brands have to think more creatively about how they engage."

Andrew Busby

Expert analysis.

"**Often, consumer engagement is more effective than direct sales.** The authenticity of pop-ups makes them less imposing than the primary face of the brand and a **combination of curiosity and 'FOMO' attracts footfall where it might not otherwise exist.** Curating experiences that linger in the memory are more important than sales per square foot today, if people are immersed in the brand, the sales will come."

Andrew Busby

Tip #4:

Partnerships that empower your audience.

From Klarna's recent retailer launches, we know that two-thirds of pay later customers are actually existing users who have shopped with other retailers within the Klarna network.

Although not all of these are new, it proves Klarna acts as a driver of acquisition bringing a pre-engaged cohort of shoppers already seeking flexible payment solutions.

No drama, just Klarna.

Klarna's latest out of home ad campaign – 'No drama, just Klarna.' – was designed to show off our brand personality and that of our retailer partners. The campaign ran in Q4 2019 and again in Q1 2020 on billboards and digital channels across the UK and major metros. Klarna retailers – even those not directly involved in the campaign – saw average daily transactions by new users rise by 20% during the campaign period.

2. Conversion.

Tip #1:

Friction causes frustration. Invest in services that empowers and eases the customer.

Price proves to be a sticking point for many people. **Fifty eight percent** of consumers said lower prices would make them consider shopping somewhere they haven't previously bought from. **Thirty five percent** said that promotions and deals would encourage them to make a purchase, while **46%** are encouraged by good value for money. When it comes to conversion, convenience is almost as important as cost.

According to Klarna's consumer research:

28%
Are encouraged to purchase by a good returns policy

26%
Are interested in next or same day delivery options

38%
Likely to shop with a retailer that offers flexible payment options

31%
Likely to shop in-store if flexible payment options are available at the till

Flexible payments are valued most with Millennials **(52%)** and Gen Z **(41%)**.

Expert analysis.

"**Brits love a bargain.** Experience may be a new differentiator, but if the price isn't right consumers are less likely to convert. **Today's 'convenience culture' means ease at every touch point has shifted from 'a nice to have' to an absolute essential.** While there have been qualms about the impact of making returns too easy, serial returners can be the best customers as the flexibility often translates to more purchasing."

Andrew Busby

Flexible payment pays.

UK retailers who offer payment via Klarna's instalments have reported a 55% increase in average order value, with almost half of users saying that they would not have completed the purchase if Klarna was not available.

Tip #2:

Social endorsement is vital.

With so much choice and information overload, people are turning to other users to help them decide what to buy. **Twenty six percent** of consumers said positive reviews encourage them to make a purchase. The most trusted recommendation sources are family and friends **(65%)** and online review sites **(38%)** – although these are followed by retailers and brands themselves **(18%)**. Spending more on your website and webstore's integration with social sites and offering buttons for users to share is an easy way to win.

3. Retention and loyalty.

Tip #1:

Lock in the love.

You cannot be complacent with existing customers, you must remind them why them why they chose you in the first place and more importantly, why they put you above anyone else.

Retention and loyalty are extremely important: **40%** of consumers said they are loyal to a couple of 'loved' brands they shop with whereas, only **3%** say they are completely loyal to retailers and wouldn't shop anywhere else.

Expert analysis.

"**We've entered the age of butterfly consumerism.** Consumers are fickler and more promiscuous than ever before; we are loyal to our family, our close friends, our pets – but not brands. **We are constantly expecting more from stores. The unexpected, the curious, the tempting, the daring** – all are more likely to attract our attention than those who remain static and predictable."

Andrew Busby

Tip #2:

Drive loyalty by great experiences.

Rewards and loyalty schemes are still viewed as an important factor in customer retention, but today's consumers desire experiences – both online and IRL – that go beyond traditional shopping.

35%

Of consumers said an enjoyable in-store experience **would make them more likely to shop again** with a retailer whereas…

30%

Said it would **make them more likely to buy more** from them

Tip #3:

In-store needs improvement.

Nineteen percent of consumers said that additional services being offered in-store would encourage them to buy more from a retailer and shop with them again. This was most pronounced amongst Gen Z **(22%)** and Millennials **(27%)**, saying they would buy more from a retailer that offers additional services. Twice as many Gen Z respondents said they value in-store entertainment, compared to the average across all ages. So, what in-store services would they like to see? Most valued across the board is free wi-fi **(45%)**, followed by food and drink **(39%)**, phone charging stations **(23%)** and in-store entertainment, such as live music or DJs **(15%)**.

Expert analysis.

"**It's all about creating a sensory experience that will evoke an emotional reaction.** As much as **95%** of our purchasing decisions are made at a subconscious level, so it is critical for brands to engage on an emotional level with their customers. **That means giving them services that add value to the in-store or online experience.**"

Andrew Busby

House of Klarna.

We recently created House of Klarna, a unique shopping experience to educate UK consumers on our payment methods and showcase 30 of our amazing retailers. Hosted over three floors, House of Klarna was full of instagrammable moments, unique content and a full schedule of activities running over ten days in Manchester.

4. Advocacy.

Tip #1:

It's not just about selling products. Initiatives that nurture relationships will create an army of brand ambassadors.

60%

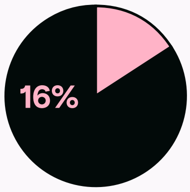
Of consumers said that when they love a brand or retailer, they will tell their friends about it

Expert analysis.

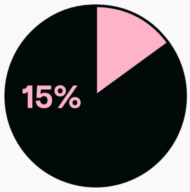
“**The invention of the smartphone created an army of broadcasters,** never shy of sharing thoughts and feelings about brands. **This might not always be positive, but it provides a platform for incredible advocacy** – and this is largely accountable for the rise of the influencer community. It is vital that brands and retailers listen to their customers across all channels, yet many still only do so at a very cursory and aggregated level.”

Andrew Busby

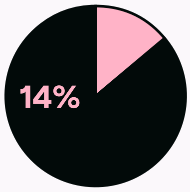
The factors that make consumers most likely to recommend a retailer or leave a positive review:



An enjoyable in-store experience.



A good user experience across all devices and channels.



A good returns process.

Fifteen percent of consumers said that other positive reviews or recommendations will encourage them to leave a positive review or make a recommendation – creating a virtuous circle.

Conclusion: looking ahead.

The traditional model for measuring CLV is fast becoming outdated. With customer behaviour increasingly unpredictable, we need a rethink.

We must look into the future and think in terms of 'propensity to spend'. An approach that recognises the impact of retailers' and their partners' investment – in terms of branding, marketing and customer experience.

CLV and the Klarna Effect.

Specifically looking at the effect of strategic partners, like Klarna, it's clear to see how they can help hack CLV, deliver acquisition and accelerate growth.

We can conclude that as well as differentiating and adding value at the checkout, Klarna shifts the customer conversation from price to convenience and empowerment.

Retailers can benefit from Klarna's own customer base, marketing investment and insights to gain access to millions of potential customers, who already love using Klarna.

Additionally, Klarna's broad appeal can help retailers gain a foothold into new customer segments and demographics, which are currently an untapped opportunity for growth.

Finally, with Klarna to drive traffic on their behalf, retailers reduce their own spend on tactical marketing efforts and can re-distribute it to drive even higher engagement and a closer emotional connection with their existing customers.

Optimising spend.

From the results of the Klarna consumer survey, it's clear that there is an enormous potential for retailers to enhance their sales strategy and the customer UX in areas of acquisition, conversion, loyalty and advocacy, which all impact CLV.

To summarise, retailers should strive to:

- Make digital interactions the best they can be.
- Create emotional, then personal, connections.
- Explore promotional opportunities with partners that resonate.
- Deliver a frictionless UX and experiences that delight.
- Make sharing and advocacy easy.
- Reach out and nurture with compelling communications.
- Build trust by doing the basics well.

Expert conclusion:

“As we move into the next decade, the roaring 20s of retail will be characterised by change and challenge. For forward-thinking retailers who adopt a partnership approach, there will also be huge opportunity to win over the shoppers of tomorrow, grow share of wallet and steal a march on the competition. Disruptors like Klarna have already ripped up the rule book in the relatively short time that they have been operating. In the coming years, the influence of these new players will grow as the boundaries of commerce continue to evolve. Retailers must adapt their approach, seeking out new ways to create customer value and reduce costs, if they’re to survive the seismic shifts the next ten years will bring.”

Andrew Busby

About Klarna.

Klarna, the leading global disruptor of payments and banking and provider of smoooth retail services, was founded in Sweden in 2005. Klarna currently holds a post money valuation of $5.5 billion, which ranks Klarna as the largest private fintech in Europe and one of the largest private fintechs globally. Klarna provides retailers with a flexible range of preferred payment alternatives that enable consumers to easily and securely pay when and how they want everywhere – online and in-store.

Over 205,000 retailers, including ASOS, Peloton, Swoon, Michael Kors, Superdry, Gymshark, Samsung, Topshop, Oliver Bonas and many more, have enabled Klarna’s innovative shopping experience, that stretches beyond the actual transaction and also allows consumers to take control over their personal finances. Klarna has 2,700 employees and is active in 17 countries.

Klarna.com/uk