

# Keep or fire? Cost of customer abandonment and optimal abandonment decisions

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## **Abstract**

Keeping unprofitable customers is costly, yet abandoning them can lead to bad word of mouth, which is also costly. Firms are typically operating in the dark, as they are uncertain about how profitable customers will be in the long run. We present an analytical model for optimal customer abandonment decisions; it incorporates the cost to abandon customers and two-sided abandonment: Firms have an option to abandon customers, yet customers also have an option to abandon the firm if they drop out. We show that a myopic firm may wrongly abandon profitable customers, because the firm ignores that currently unprofitable customers may turn out to be profitable in the long run, and if not, the firm has the option to abandon them later. On the other hand, a myopic firm may also wrongly serve unprofitable customers, because it focuses too much on avoiding the immediate cost to abandon. We use comparative statics to relate the optimal serving versus abandonment decisions to structural parameters.

**Keywords:** *Customer abandonment; Cost of abandonment; Analytical model*

**Track:** Methods, Modelling & Marketing Analytics