

Customer Insight & Marketing Decision Sciences

Information-Based Target Marketing & Customer Relationship Management

By Mark Van Clieaf

The new era of marketing offers the ability to sharpen insight into customers through the application of marketing decision sciences to transactional customer data. Datamining for marketing purposes had its early history in transaction-based industries like financial services, telecom, retail, catalogue, and hospitality where for many years there have been volumes of customer data, and various levels of competence in mining this data for marketing and credit risk decision making.

With the internet as a catalyst many of the old business models and their approaches to marketing, branding and customers are being reinvented. Now customer data from web page views to purchase and customer service data can be tracked on the internet for such industries as packaged goods, pharmaceutical, and automotive. In some cases new web-based business models are evolving with transactional customer information at their core. This includes both business to consumer and business to business sectors. Marketing initiatives can now be tracked in real time interactions with customers through web and call center channels.

Thus the 4 P's of marketing (product, price, promotion and place) are also being re-defined as the killer B's (branding, bonding, bundling, billing) for a digital world. Branding becomes a complete customer experience (branding system) that is intentionally designed and integrated at each customer touch point (bonding), provides for a customizing and deepening of the customer relationship (bundling of multiple product offers), and reflects relationship based pricing payment and bill presentment options (billing).

Marketing decision sciences have played a role in each of "three waves" of becoming customer centric over the last 15 years. First came the loyalty / frequency wave. This started with many of the continuity clubs (books, music), airlines and catalogue companies. Initially good information-based marketing differentiated customers based on simple RFM metrics (recency, frequency, monetary value). Many loyalty programs were developed to attempt to recognize, differentiate and reward tiers of better customers.

The second wave, customer value optimization, aimed for more precise matching of product to customer, with some level of tailoring products and services to smaller niches of customer segments. Many of the second wave companies, such as Lands End, LL Bean, Limited, Sears, Capital One, Providian, Amex, Norwest Bank, First Union Bank, Chase Manhattan, Transamerica, GE Capital, applied sophisticated marketing decision sciences to target and tailor product offerings through telemarketing, DRTV and direct mail channels. Some examples of this will follow.

Where the first and second waves were essentially about products in search of customers, the third wave starts with customers and what can be done to meet their needs with products and services, whether individually or bundled. The third wave has seen a select few companies begin to use marketing decision sciences to create a single customer view across multiple product categories or lines of business. This customer view also includes the duration of the relationship beyond the 1-year profit and loss statement and the financial implications for optimizing pricing and marketing spend over multiple years. This single view allows for the creation of new bundled value propositions. Wachovia Bank, Royal Bank, US West, Centurytel, Charles Schwabb, Federal Express, Neiman Marcus are just a few companies who are riding this third wave of truly becoming customer centric.

We will briefly address the use of marketing decision sciences from the following perspectives: strategic (shifting the customer portfolio make-up and profitability over multiple years) versus tactical (campaign tailoring & targeting); using customer information to create new value propositions, campaign planning and targeting; using decision sciences in closed loop marketing processes; recognizing the difference between an information driven product strategy and a customer strategy; key metrics to drive a customer or CRM strategy. This is based on our experience in assisting companies in both the design of new roles and the recruitment of key executives in marketing, database marketing, interactive marketing and analytical modeling across North America.

The Strategic Use of Customer Information

The starting point for the strategic use of customer information is in creating a customer scorecard across the customer portfolio. This scorecard creates a macro level segmentation based on customer segments driven primarily by tiers of customer profitability and product / service usage. Thus a distribution of customers by product usage and profit tiers (high, medium, low or even deciles) highlights such macro level drivers as what percentage of customers and the products they use are driving what patterns of revenue, EBITDA, Operating Earnings or Free Cashflow. This is the intersection of customer, product and finance from a future marketing investment and return perspective.

In many industries, such as financial service and telecom, there is a very skewed distribution across the total customer portfolio, e.g. 20 % of the customers contributing 80 - 150 % of profit contribution. In some industries because a certain percentage of customers are unprofitable (i.e. banking , telecom) another group of customers can actually contribute more than 100 % to overall profitability. When current profit contribution and an analysis of some type of future profit potential is established, then a profit opportunity gap can be identified for the existing customer portfolio.

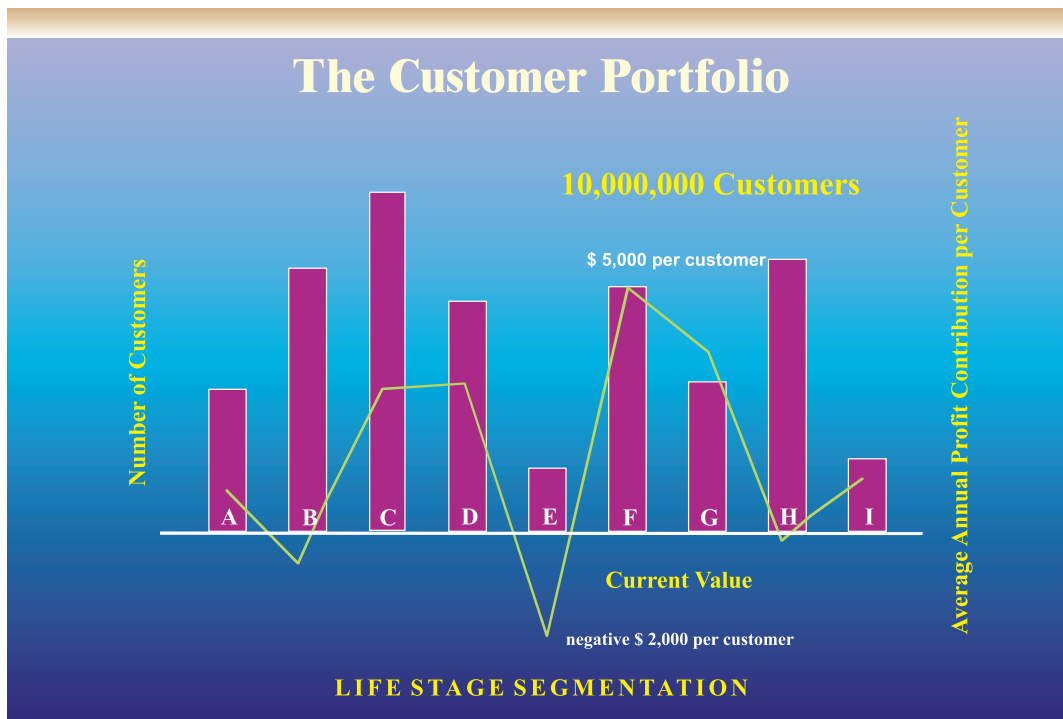
This type of strategic customer analysis can start to provide direction on where to make marketing investments to optimize marketing spending based on a positive net present value (NPV) or life-time value at the contribution margin or operating profit level (see figure 1).

Customer Value Proposition Development

Datamining of customer information may identify a number of new marketing opportunities. This could include a new way to bundle and price an individual product based on the actual volume and frequency of purchase, like cellular telephone packages.

The majority of companies are still campaign / product versus customer centric. They are using datamining for targeting existing products and services to certain customer segments, but spend little time using the customer data to drive the development of new value propositions based on patterns of the way micro-segments of customer are actually buying. A bad lead can't be turned into a good lead if the fundamental value proposition for that customer does not meet their needs.

A bundled value proposition that includes the packaging of a number of products and services together may be uncovered. As an example, Schwab and Fidelity are broad-based US financial service companies that have identified opportunities to package solutions for investment management, financial planning, securities brokerage and credit card access across multiple channels including retail, telephone and web channels. It must be recognized that even bundling opportunities identified through datamining of actual past behavior are not static bundles, and represent the sequencing of product usage pattern of the customer over time that could change due to lifestage / lifestyle and other variables.



In the future, more and more marketers will be involved in working with datamining teams to develop the decision rules and analytical models that will create service packaging and pricing options, and allow customers to create their own custom packages of services that are self serve through the internet and other channels.

Figure 1

Campaign Planning & Targeting

Marketing decision sciences is at the heart of effective campaign planning & targeting in an information age. Many organizations apply an integrated analytic framework that brings together response modeling, financial modeling and credit risk modeling. This type of integrated analytic strategy helps the marketer to target offers and messaging to customers based not only on customer response, but also on the predicted revenue or profit in a 1 to 3 year period (after acquisition costs) and on the risk profile of getting paid. In some cases 100 cells of unique target segments may be created for target marketing purposes based on a multi-dimensional analytic framework. To the dismay of some marketers who would like to contact as many prospective or current customers as possible, cut off scores based on an overall NPV of a customer will determine how deep into a customer file targeting can profitably be done. A marketer can target more customers beyond the cut off score, but must recognize that the forecasted revenue and NPV will no longer be positive or profitable (after acquisition costs and credit risk).

Beyond the targeting models and micro-segmentation is the application of test and control strategies that meet some level of statistical validity. The key to Information-Based marketing is developing a hypothesis about a customer group from which to test a broad range of value propositions, pricing, messaging options. The creation of this type of test and learn strategy with campaign feedback loops, from days to weeks, is core to marketing in the 21st century.

Ensuring that the marketing process has a back-end campaign analysis of the response, purchase patterns and on going profiling of both responders and non-responders is key. A repeated non-response can tell you as much about the customer as a response can. Tracking this type of ongoing campaign response history information is equally critical. One credit card company undertakes over 10,000 tests through hundreds of campaigns a year of which only 1,000 may be successful, but the learning from the other 9,000 is equally important.

Turning complex modeling algorithms into targeting codes which can score a file and then be used to drive campaigns is where the rubber meets the road for target marketing. Marketers should be aware that the application of model tracking reports are key to ensure that the basis upon which the analytics were originally developed (including overall customer file distributions) matches up closely to the file distribution when the complete customer file is scored using the models for campaign targeting. If there is

a discrepancy then the list pulled will probably not deliver the projected financial results and campaign ROI. In a closed loop marketing system the initial analytic validation process and customer file distribution, the distribution of the completed scored file prior to campaign, and the back-end results analysis should ideally mirror each other. The consistency of model results at each stage of the model development and application process is required to provide the marketer with a confidence level in using the decision sciences to make marketing decisions. Thus customer data is turned into information, information is turned into customer knowledge and insight, and customer knowledge is applied to create profitable customer relationships.

Implementing Real time Closed Loop Marketing Processes (it's not just the models)

Some companies build an extensive array of both strategic and / or tactical models that either never get implemented or do not positively impact the business. The disconnect between the models and implementation is the failure of the analytic team to educate the marketers about how to use this new customer information to make better marketing decisions.

The second disconnect is the need to re-design the marketing processes into a closed looped marketing system that incorporates numerous analytical models and business decision rules. This system includes customer portfolio scorecards and segmentation; hypothesis generation about customer segments; value proposition creation; offer test and control strategy development; file scoring and target list generation; campaign execution across multiple channels; and finally back-end campaign analysis, and customer portfolio re-scoring.

A growing number of companies have built extensive customer data warehouses and developed impressive analytic models, but undertake no test and control or no back-end analysis. Companies that have not designed marketing processes that include test and control and back-end campaign analysis processes are missing the real opportunity for Information-Based marketing. The real learning about the customer is in creating closed loop marketing processes. Even a non-response is valuable customer information that needs to be tracked and recorded in a customer database.

Increasingly companies are creating process ownership for customer acquisition / activation, customer development (cross-sell/ upsell/ bundle), customer retention / win-back. The re-design of these marketing processes includes business decision rules for inbound and outbound customer contact by each channel (retail, direct mail, call center,

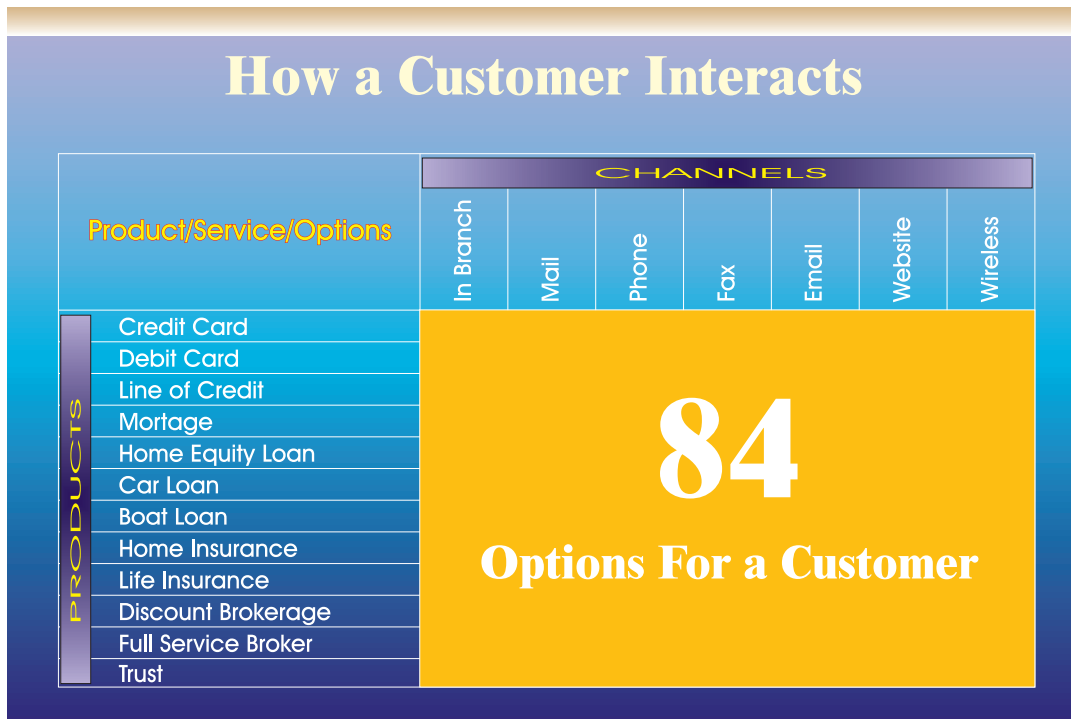


Figure 2

web), and the level of value proposition personalization.

In some cases inbound customer care marketing processes are being designed to allow customers to self-select their preferred bundle of products, services, and channels (see figure 2). Behind this self-selection model is an extensive set of business decision rules, analytic models and pricing tables used to customize and determine the pricing and channel delivery for such packages. The total customer experience is being engineered, with the level of personalization dependent on these marketing decision rules and analytical models. The design of dynamic websites incorporates the integration of customer segmentation modeling and marketing decision rules into a navigation architecture that creates the total interactive customer experience.

It must be recognized that these marketing processes, analytical models and business rules cannot just be completely automated as many would like to think. At one major credit card company there is a group of 40 individuals who personally review customers who have been turned down for a credit card based on the credit risk models. It is estimated that this group approves 10 to 15 % of these customers and the financial impact is an additional \$ 50 to \$100 million in revenue from customers at the edge of acceptable credit worthiness. Each of these customer situations is unique and requires a level of human judgement to make a final decision. Thus processes have been designed to manage customers for whom all possibilities could not

be effectively built into analytic models and technology-enabled decision engines. These are marketing decision support systems not marketing decision making systems.

Increasingly, marketers are designing inbound marketing processes, which will include workflows and customer routing from various channels (web & customer care center). Key to this real time marketing will be the development of business decision rules and decision engines that support the branded customer experience for a certain segment of cus-

tomers and will optimize marketing investments based on customer life-time-value.

No longer are site visits and click-throughs from internet channels acceptable measures, because they don't necessarily lead to short or even mid-term profitability. Thus the future role of marketing decision sciences will be in creating an integrated capability working closely with the core marketing team in designing customer experiences (on-line & off-line) and related processes (acquisition, development, win-back) which are optimized to meeting customers needs, channels preferences, customer value, and inbound / outbound customer contact strategy.

Information Driven Product Strategies

In a mass marketing world the value proposition / product benefit is static, and marketers try to market a product to as many people as possible. In a target marketing world, decision sciences plays a pivotal role in identifying those customers that best match up to the defined product benefit.

One of the best examples of this is in the credit card business, at such well known companies such as Capital One, Providian, American Express and others. These companies are effectively integrating descriptive modeling (segmentation through a broad range of clustering techniques), predictive modeling (using applied statistics to predict probabilities of response, activation and usage), credit risk

modeling (to predict current / future credit worthiness and probability of payment problems), and finally financial modeling (forecast revenue / margin / profit in an annual and 3 to 5 year life-time value measure).

This integration creates a complex three dimensional response, revenue/profit and risk matrix from which to segment customers, determine risk based product offers, and set cut-off points in the prospective customer universe below which investing marketing money (cost per acquisition) will have a break even to negative payback over a multiple year time period.

This integrated targeting framework (response/profit/risk) has been missing in many of the Dot.com start-ups and so their cost / acquisition is high relative to future forecasted revenues / cashflows at the individual customer level. The failure to turn these customers into future cashflows at a positive margin or profit level is one reason why the capital markets recently had a 30 % downward correction, reflecting the perceived lack of future profitability of these business models, and the customer portfolios that have been acquired.

Thus many product driven companies, from credit card, insurance, and retail banking, to telecom, catalogue, travel are all applying marketing decision sciences to target and tailor campaigns and optimize marketing spending.

Key Metrics to Drive a Customer Strategy

To truly drive a customer-centric strategy across multiple product or lines of business there are four core principles of marketing decision sciences and customer measurement being applied by the better practice companies. These are assessing the

- Depth & Breadth of the Customer Relationship
- Duration of the Customer Relationship / Attrition Risk of Customer
- Profitability of the Total Customer Relationship
- Current / Future Potential of the Total Customer Relationship

Measuring these drivers of the customer relationship is critical, including whether the total customer portfolio is trending positive, neutral or negative, by customer segment over time (monthly, quarterly, yearly). This provides the top marketing executive, CFO and CEO a “dashboard” of customer measurement from which to make sound marketing and organizational decisions that will provide a measurable ROI on dollars invested.

The use of depth and breadth of customer measures will allow a scoring of current status with the customer including their current annual spend in dollars for each product and service (depth) and how many of your products / services they currently use (breadth). Another breadth measure is the channel preference by customer. In some industries there could be five or more preferred customer contact channels. This will provide strategic marketing direction for up-sell and cross-sell strategies by preferred channels that will increase the NPV of the customer.

The depth and breadth of customer information will allow for the development of a segmentation strategy based on real usage, regardless of age, income and other geo-demographic and psychographic data that has been traditionally been used in customer segmentation studies. Past history has shown what customers appear to be from a psychographic or geodemographic perspective and what they say they will buy, versus what they actually do in many cases are quite different. As the CEO of Providian is often quoted saying “ I don’t care what the customer says, I care what they actually do”.

The duration of the relationship is important customer information because it assists marketers in better understanding where they are in the customer relationship (just started, just left you or somewhere in between). For recurring revenue businesses especially like telecom, financial services, and continuity clubs, forecasting future revenues and cashflows depends on predicting the duration of the relationship by customer segment. Another way to look at customer duration is the risk of customer attrition at different times in the relationship. While many organizations have built attrition models based on products, few have built attrition models based on the vulnerability of the total customer relationship.

Financial modeling will identify the relationship between current product profitability and current customer profitability. Customers can then be segmented based on similar current product usage, and each customer segment can then be analyzed based on total revenue, margin and total profit contribution at an individual customer level.

This type of financial analysis for one bank showed that 40 % of their products were not profitable, and that 30 % of these products were of little interest (individually or in a bundle) to the top tiers of their most profitable customers. This bank subsequently ceased to offer these products to their customers. The bank increased its equity value of the enterprise over the following four years by a factor of four times as a result of better customer management.

Other financial / customer modeling includes current and future potential (revenue / profit) based on the lifestage of the customer and their forecasted life-time-value (LTV). This can help differentiate customers which may look the same today, but where increased investment could provide a return in the future. The challenge in forecasting LTV is in developing a set of assumptions about the duration of the customer relationship and purchase patterns over time that are robust enough to have credibility with both the marketing and finance disciplines.

Another way to look at customer potential is the customer share-of-wallet. A customer may look unprofitable, but this could be due to low current share of wallet. Thus, to optimize marketing investments, customer information on their spending patterns or profile outside your organization is required. A number of companies are using both survey and appended third party data to create actual or proxy estimates for share-of-wallet.

The integration of these four principles of customer relationship management (depth and breadth, duration / attrition, profitability, potential) is providing leading companies a scorecard of customer measurement from which to create profitable customer relationships.

Marketing Decision Sciences Comes of Age

Developing customer insight based on real transactional behavior at an individual customer level is a significant shift from mass marketing. But this is not to say that traditional consumer research techniques developed for a mass marketing world are no longer of value. The future is here today as leading companies integrate both datamining and traditional consumer research into a more insightful understanding of the customer.

Traditional qualitative and quantitative consumer research provides a good understanding of consumer attitudes and interest, which helps to uncover the underlying answers to the “why” of their behavior. The problem with these traditional techniques and attitudinal segmentations is that because they are based on a statistical sample as a proxy for customer segments, that usually are not actionable through addressable direct media like e-mail, direct mail, or call center.

Surprisingly, many market researchers have resisted appending actual results from surveys (customer profiling) and focus groups to an individual customer file due to concerns of privacy. Yet companies like USAA survey every customer on some 100 plus dimensions every 2 years and directly append this to the individual customer file.

While privacy will continue to be an issue, companies that use this customer information to provide relevant products and services to meet customer needs will be seen positively by the consumer.

One international credit card company held focus groups with a segment of their most profitable customers. The focus group participants were selected based on their actual consumer behavior from the customer database. All had a minimum level of balances on their card and revolved monthly. The focus group facilitator was NOT told the participants revolved. Most of the focus group participants denied they revolved on their credit card, but provided insight into their attitude towards debt, use of credit cards, lifestyle, and meaningful communications strategy. The marketer thus had a unique insight into what the consumer actually did and why, from which to better target existing products and develop new products and communications strategies relevant to this niche of customers.

A new emerging customer management capability is evident in a service provided by a company called Recipio. Their patented insight engine allows customers to provide internet or ITV enabled feedback on their interests and preferences, on a low cost, fast cycle time basis. This customer input can drive ideation meetings, based on open-ended customer feedback (unlike traditional closed-ended surveys), and these ideas can be quickly be incorporated into new value propositions that can be then targeted through outbound campaigns back to the individuals that provide the ideas in the first place on a one-to-one basis. This is the ultimate in true CRM. General Motors is using this on their internet showroom, where customers get to design their dream car. Thus GM has a 365 day a year capability to listen to their customer on a large scale, and provide targeted relevant offers based on new customer insight, on a true one-to-one basis.

The new era of information based marketing is here. We now have enabling marketing technologies, processes and tools to provide a level of precision in meeting customer needs at a micro-segment or individual customer level never seen before. The development of products, services and customer communications that can be profitably mass-customized to niches of customer segments is dependent on the effective use and re-design of marketing processes, business decision rules, and analytical models that optimize the match between individual customers, products, channels and the creation of shareholder value.

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He has led a number of highly regarded benchmarking studies on the [Future of Direct and Interactive Marketing](#) and the [Three Waves of Customer Centric](#). See www.mvcinternational.com

Mark has a broad range of line and consulting experience. He began his early career in account executive roles in the marketing communications, direct response and advertising industry. He later became Director of Sales for a rapidly growing marketing communications company and Director, New Business Development for a major advertising agency. He brings over 15 years of experience in providing counsel in job / organization design and executive resourcing strategy, recruitment, and leadership development to senior management in a broad range of organizations across North America, Asia, and the Middle East. This included four years with Price Waterhouse in their strategy and executive search consulting practices

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