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[Headline]

Selecting the Right Customers

[Subhead]

The  second in a series of white papers
on the topic of
"Managing Customer Value"

[Inside front: Overview, acknowledgements - pg. 2]

[Subhead] *About This White Paper*

This is the second in a series of [six] white papers that provide an overview of the customer value management process. The topics covered in this series include:

- #1: Learning who your customers are and what they value
- #2: *Selecting customers carefully and increasing their value* (this white paper)
- #3: Designing products & services that deliver the desired value
- #4: Designing effective sales & service channels
- #5: Recruiting & training employees to deliver & increase customer value
- #6: Building customer retention through the constant refinement of the value proposition

Executive Summary

In business, there are really only three ways for an organization to grow:

- Get customers
- Keep customers
- Grow customers

The previous white paper stressed the importance of knowing your customers through-and-through. This white paper assumes that you now know what your best customers look like, and sets out to help you find more just like them. Once acquired, these new customers must then be cultivated to reach their full potential. Thus, this white paper will focus on how to *get* and *grow* new customers.

There are four basic steps to finding and growing good customers:

- #1: Identify your market potential
- #2: Develop the initial offer
- #3: Cultivate customers with cross sell and upsell
- #4: Plan and manage your campaign

By following these steps and applying the principles of Convergent Marketing, you should be able to slowly transform these newly acquired customers into “clones” of your current best customers. The task then becomes one of building customer loyalty through service and relevant product or service offerings; these topics will be discussed more fully in later white papers.

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Introduction

Many organizations are preoccupied with acquiring new customers, *any* new customers. This may sound like a worthwhile goal, but it is only a partial statement of a more important goal. Long-term, organizations will be better served by carefully recruiting the *right* new customers and then cultivating them so they grow into “clones” of your current day best customers.

The previous white paper focused on learning who your customers are, through the use of profiling, segmentation, data mining and statistical modeling. These methods — along with a powerful marketing database — are the essential tools for understanding the needs and behavior of your customers. They also provide the objective criteria for measuring and rating the value of your customers.

One of the first things you'll learn from analyzing your customer database is that some customers are more valuable than others, and that there are many levels and types of "best customers." You'll also learn that some customers actually cost you money and should be weeded out if they can't be made profitable. The profiles of these different customer segments are exactly the kind of information you need to select the right new customers.

You must select your new customers carefully — you want them to resemble your best existing customers. This is because customer acquisition typically costs you money in the early stages (see Graph #1). Your marketing efforts should therefore focus on acquiring customers with significant long-term growth potential — these are the right customers.

[Graphic: Marketing Management graph of 8-year acquisition costs.]

Acquiring the right customers is best accomplished by a process known as *Convergent Marketing*. This process is based on six principles that can help companies shift focus from a traditional product-centric approach to a more effective customer-centric approach.

The six basic principles of Convergent Marketing are:

- Learning who your customers are and what they value
- Selecting customers carefully and increasing their value
- Designing products & services that deliver the desired value
- Designing effective sales & service channels
- Recruiting & training employees to deliver & increase customer value
- Building customer retention through the constant refinement of the value

proposition

This white paper examines principle #2 in depth. For a more thorough discussion of Convergent Marketing, please read white paper #1.

In Convergent Marketing, selecting the right customers is a four-step process:

- #1: Identify your market potential
- #2: Develop the initial offer
- #3: Cultivate customers with cross sell and upsell
- #4: Plan and manage your campaign

Let's examine these steps one-by-one.

Step #1: Identify Your Market Potential

Let's assume that you've already built your marketing database and have come to thoroughly understand your customers by using profiling, segmentation, data mining and statistical modeling (as described in white paper #1). In other words, you know what your best customers look like.

Armed with this information, you're now ready to acquire new customers who look just like your current best customers — in fact, they're sometimes referred to as “look-alikes” or “clones.”

First, you'll examine the marketplace and identify the areas of greatest opportunity — the areas of low penetration. Your marketing will be more effective when you find look-alikes in areas with above-average growth potential.

GIS tools can be very valuable at this stage. Geographic Information Systems (GIS) can visually correlate marketing or census data with graphical maps; this allows the marketing team to view their data in map formats, not just as tables of numbers. The human mind can grasp information more quickly when it's presented in this sort of graphical format.

GIS maps are excellent for finding pockets of prospects, by correlating and displaying relevant marketing factors. This is done by matching the demographics of your best customers to the census statistics of the market. You can quickly and easily identify the areas where there are large numbers of best customer look-alikes (high potential) but very few customers (low penetration).

Now you're ready to build your prospect list. Use the results of your marketplace analysis to specify the geographic areas to target and the demographic and psychographic profile of the prospects you want to reach. Your list vendor will help find names that match your profiles in the target areas.

Although it's rare that specific purchase histories are available from list vendors, sometimes they can use survey information to match general buying behavior, or can compile several lists of related buying behavior. For example, if you know that your best customers use the PC banking feature of your software, you may be able to develop a good prospect list by correlating your profile data to subscribers of PC Magazine.

[Graphic: GIS map showing color-coded market segments.]

[Caption: "Humans are better at detecting patterns when the data is presented graphically, as in this market penetration map."]

Step #2: Develop the Initial Offer

Because you've just selected prospects that closely resemble your best customers, you can draw some fairly informed conclusions about what these prospects will respond to. Use the results of your best customer profiling and segmentation (discussed in white paper #1) to develop the initial offers to your prospects.

First, add your prospects to your database. Group them with the similar segments of your customer base. You won't have all the information that was used to segment the customers (such as actual purchase behavior), but you should have enough information to place them in the appropriate segments.

Then, on a segment-by-segment basis, look at the product affinity and purchase patterns of your most profitable long-term customers. Purchase *sequence* and *frequency* are often the most useful data to track. Make sure that your marketing database has all the fields necessary to capture this key information.

By segment, which products or product categories did the best customers typically buy first? Second? Third? How much time elapsed, on average, between their first and second purchase? These factors will vary from segment to segment, so don't assume that what works with one group of best customers will work with other customer segments — or with your prospects.

Use this product affinity information to identify the most appropriate products or services for your initial prospect offering. You might choose to offer the typical first and second product purchases together (perhaps as a bundle), to make the

prospect profitable even more quickly.

Testing and analysis should be an ongoing process. When you're reviewing what best customers did in the past, compare it to the actions of more recently-acquired best customers. Do they still behave the same? Or are there new affinity trends emerging? Motivations change with time and circumstance. That's why a powerful marketing database is so essential — you need to capture and maintain a wide range of information if you are truly to know your customers, both present and future.

Step #4: Cultivating Customers with Upsell and Cross Sell

Your job is not done when the campaign ends. You need to know more about those newly-acquired look-alikes that are now customers. After all, your goal is to create a long-term, ever more satisfying relationship with customers. In short, you want to cultivate your customers and realize their full potential.

Customers 'grow' through a combination of *upsell* and *cross sell*. Again, examine what has worked in the past with your best customers and apply that to your newest customers. Use the profiling techniques discussed in white paper #1 to enhance your knowledge of new customers. Pay special attention to:

- Demographics (usually purchased and appended)
- Location (ZIP code or GIS-based)
- Lifestyle or lifestage (if available)
- Buying behavior
- Revenue
- Tenure

Code your customer records with all the key factors. Always look for the factors that separate the segments; for example, compare frequent high-dollar purchasers to infrequent low-dollar purchasers... what are the underlying differences between them?

As you can see, Convergent Marketing is a process of constant re-discovery of the customer. By recognizing that your customers are a dynamic, ever-changing population, you can grow your customers by selling them new product categories (cross sell) or by increasing their billings for existing categories (upsell). However, your marketing database must be up to the task...

Again, use your segment-by-segment analyses of product affinity and purchase patterns to identify what to offer, and when. Always try to anticipate the effect of the offering on the customer's profitability. For example, would it be wise to offer a home equity loan to a customer who typically carries high credit card balances with your bank... ?

To keep up with your ever-changing customer base, you need to program your e marketing database with event-triggered activities. For example, define action steps that should be triggered by such events as:

- *New Customer Groupings* — for example, when a single person becomes a married person, they become a 'household' grouping. Change your approach strategies to recognize and appeal to this new grouping.
- *Expiring Contracts* — anticipate what your customer will do towards the end of the contract and contact them in advance with a pre-emptive offer.
- *Best Customer Recognition* — as a customer's purchases increase, acknowledge and reward their status in an appropriate manner. 'Preferred customer'

discounts are a common example of this recognition, but be cautious of this practice — indiscriminate discounting can quickly turn a best customer into an unprofitable customer. A better approach may be to provide best customers with express service (if cost-effective), combined with occasional thank-you letters or acknowledgements.

- *Cultivating Channel Behavior* — recognize and encourage the use of the desired service channel. For example, promoting low cost customer support options like Internet sites or automated phone systems may reduce the workload on the more expensive option of letting customers talk one-on-one with a service representative.
- *Customer Activation* — take action to motivate customers to use an existing (but underutilized) service or product. For example, offering incentives to customers who have received, but never used, their credit card.
- *Add-on Sales* — expand the customer's use of a basic service or product. For example, offer them incentives to add voice mail to their basic phone service.

All of these are examples of increasing the long-term value of your customers through upsell and cross sell. By tracking the results of these efforts, you can evaluate your strategies and modify your campaigns to make them more relevant and effective. This results in more profit for you and greater satisfaction for the customer.

[Sidebar A - see sidebar section at the end of this document]

Step #5: Manage Your Campaign

The essential tool in Convergent Marketing is, as always, your marketing database.

It must be capable of handling and tracking every aspect of your campaigns, for both prospects and existing customers. Make sure that you've defined and created all the records and fields needed to capture data and analyze the results. Without all the data, you're just guessing.

Track *all* promotions and thoroughly document them in promotion history fields. *Response* is key when evaluating your promotions, so be meticulous in capturing the data. Include such campaign details as promotion name, mailing date, mail cell, offer made, creative type, mailing cost, telemarketing followup activities and, of course, the prospect or customer responses.

Relevance Sells

Prove that you know your customers — always approach them in a personal and relevant manner. For example, based on your segmentation strategies, develop mailing or telemarketing list formats that include key information:

- Mailings: Use mail merge to include key demographic or buying history information that personalizes the mailing and strengthens your message.
- Telemarketing: Give telemarketers the key demographic and buying history information needed to confirm the relevance and appeal of your offer. And remember: the more “user friendly” the information given to the telemarketers, the more effective they can be in making their pitch.

By making your approaches meaningful to the customer, you can significantly increase their loyalty and long-term profitability.

Tracking & Measuring Performance

If it's worth doing, it's worth tracking. Know in advance what sort of reports you'll need and the data you'll want in your analyses. Structure your database to deliver all necessary information.

If it's worth tracking, it's worth acting on. Define your goals and milestones in advance. Be objective and quantified. And commit to regular followup; you don't want to lose sight of the information needed for decision-making.

Keep on tracking. Don't stop tracking when the offer expires; continue for at least two more months. And don't just focus on the products or services you featured in your offers — it's also important to know what was purchased *instead of*, or *in addition to*, the featured items. You always want to know what brings customers through the door...

Become a student of history. Tracking each campaign is important, but learning from your overall campaign history is essential. Take tracking to the next level — in most industries, you'll need three or more years of campaign history in order to evaluate your long-term results. For each customer or segment, analyze purchase frequency and compare it to your promotional frequency. Many organizations find they can decrease promotional frequency without hurting customer purchase frequency. Finding the optimum frequency will stretch your marketing dollars, but you'll never determine that optimum value by just evaluating one campaign at a time.

Finally, use your most up-to-date customer information as your guide. You'll constantly discover new facets to your current customers and you'll be increasingly successful in finding more just like them.

Conclusion

The best way to grow your business is to clone your best customers. Use the power of your marketing database to discover what your best customers have in common, then go out and target look-alikes as your prospects. Segment your prospects and match them to the customer segments they most closely resemble. Then, send each prospect segment the same kind of offer that worked best with the corresponding customer segment. Learn from the feedback and modify your plans accordingly.

The job's not over when a look-alike becomes a customer — now you need to track and analyze their subsequent purchases and expand your understanding of them. Tailor your message and guide them into a long-term relationship with your organization. They'll reward you with their loyalty and ever-increasing purchases.

The next white paper in this series — white paper #3 — will discuss how to optimize the appeal of your product and service offerings.

‘Practical Applications’ SIDEBAR TEXT

[These would be on the same page as the topic they discuss.]

[Sidebar A]

GIS MAPPING

In the Real World

The Scenario:

A bank wants to sponsor a series of local financial seminars as a way of attracting more high-end customers. To maximize attendance, the bank wants to offer these free evening seminars at a location close to its best prospects. How can the bank decide on the best seminar location?

The Solution:

The bank uses its AnalytiX system in conjunction with GIS mapping software to determine the neighborhood with the greatest market potential. They use AnalytiX to define their best current customers, using its detailed profitability analysis and customer profiling information. Then, the bank uses GIS mapping software to locate these customers on a regional map. They set the GIS map to display locations on the *tract* level, rather than on a ZIP level. They can then easily see where their best customers are concentrated.

Next, the bank uses its GIS software to purchase census-level demographics. By comparing this information with the profiles of their best current customers, the

bank can estimate their market penetration on a tract-by-tract basis. For example, one tract may have 500 matching profiles, but 400 of them are already bank customers; this is an 80% penetration level. However, another tract also shows many matching profiles, but the penetration rate is only 20%. The bank decides to offer its seminars in this low-penetration tract, as it has more sales potential. They buy a list of families in this tract that match their best customer profile and launch a very successful series of seminars. The following year, they expand the seminar program by offering it in other low-penetration, high-potential tracts.

[Sidebar C]

TARGETING YOUR OFFERS

In the Real World

The Scenario:

A mail order video club wants to boost its 4th Quarter sales with a big promotion, but they're not sure which segment to target or what offer to use. How can they determine which prospects they should go after, and with what offer?

The Solution:

The video club uses the detailed profile and purchase history information in their AnalytiX system to determine that families with 3 or more children are the most frequent buyers, and very profitable. The club then uses AnalytiX to create sub-segments of this group and looks for correlations in the promotion history. They discover that the family segment responds best to offers of "2-for1" as opposed to "50% off" or "buy-one, get-one-free," even though these are all just different

forms of the same discount.

The video club uses their detailed family profile information to buy a list of ‘look-alike’ households that are also non-customers. They mail an offer of “2-for1” to these names and get a very strong response — 21% higher than the rate for their general customer population. The 4th Quarter exceeds all projections and the manager who purchased the AnalytiX system is promoted and given a big bonus.

[Sidebar **D**]

UPSELL & CROSS SELL

In the Real World

The Scenario:

A cellular phone service provider wants to generate more after-the-sale revenue, but doesn’t know which additional services to offer, or when.

The Solution:

Using data from their AnalytiX system, the cellular service provider does a detailed purchase cycle analysis on its customer segments. They pay special attention to purchase *sequence* and the *interval* between purchases. They discover that the best customers in segments A and C typically add voicemail about 5.5 months after starting phone service. Segments B and D typically add voicemail and call forwarding after 7 months of service.

The cellular service provider then codes these segments in their AnalytiX system, marking them for different promotions: Segments A and C will receive an

promotional offer on voicemail at 4 months, while Segments B and D will get a “special bundle price” on voicemail and call forwarding at 5.5 months. The AnalytiX system automatically generates mailing labels at the appropriate time for each customer and segment — the right offer at the right time. The result: overall profitability for these segments increases, due to more customers adding more services (cross sell) or broadening the terms of their basic service (upsell).

[Sidebar E]

CAMPAIGN MANAGEMENT

In the Real World

The Scenario:

A car manufacturer wants a greater understanding of its customer base and how to market more effectively to its many different buyer types. The company’s data warehouse contains ample data — much of it irrelevant to marketing — but doesn’t seem to have the ability to “slice-and-dice” the information into a clear picture of their diverse customer base. With thousands of new customers every year, how can they learn more about their customers and prospects and improve their marketing?

The Solution:

The car manufacturer creates a true marketing database by importing its customer information into AnalytiX. They structure the new system with marketing-related fields lacking in the corporate data warehouse: promotion names, mail date, the offer(s) and creative(s) used, the customer segment/cell category, and various cost-tracking fields.

Now that they can capture this key marketing information, they begin to track the purchase patterns of their best customers, looking for correlations between segments and the promotions used. As a result, they begin mailing different promotions, using different creative, to different segments. No more “one-size-fits-all” mailings — they now have the mechanism to manage very complex campaigns and tailor their message to their very different audiences.

For example, first-time buyers in their ‘20s may receive a “no downpayment” offer in a flashy envelope showing cars against a backdrop of surfboarders, in-line skaters, etc. Retired people in their ‘60s, on the other hand, receive a more subdued mailing that stresses “reliability” and “safety,” not affordability.

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