

Drilling Down

Turning Customer Data into Profits with a Spreadsheet

Note: This is a shortened version of the Drilling Down book. The last 2/3 of the book have been eliminated and the customer profiling software application is not included as it is with the full PDF or hardcopy book. To order the complete book with customer scoring application, visit my page at Booklocker:

<http://www.booklocker.com/p/books/224.html?s=PDF>

**Drilling Down
Turning Customer Data into Profits with a Spreadsheet**

Third Edition

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Drilling Down

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with a Spreadsheet**

Jim Novo

Acknowledgements

Without the support and input of my wife Barbara, you would not be reading this book, and there would be no Drilling Down software. 'Nuff said.

I'd also like to thank Alex Romanov and Wade Downs, two friends from Home Shopping Network who helped to develop these techniques and along with my wife, forced me to massage my ramblings on these topics into a book the average person can read and understand.

Thanks to Richard Hoy and Angela Hoy, for starting this whole book thing in the first place and making it come true through Booklocker. Visit them at <http://www.booklocker.com>.

Bud Paxson and Roy Speer, the founders of the Home Shopping Network, deserve more credit than they have ever received for pioneering 24 x 7 interactive retailing, business operations, and customer service. Despite the limitations of technology at the time, they provided customers real-time interaction, community, and the first taste of being "in charge," all in one service. Thanks to them for believing our small group could find profitable marketing and customer service answers for the new interactive world, and for also seeing past our failures to the future.

And thanks to my Mom and Dad, for helping to shape my life.

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Preface

Drowning in data but have no information? Confused by ROI, LTV, RFM and all the rest of the alphabet soup involved in using customer data to increase profits? You know you should be “Drilling Down” and creating “customer profiles,” but how is it done? Drill how deep, and look for what?

Drilling Down pulls back the curtain on the “how” of Data-Driven marketing and service concepts, the enabling knowledge behind CRM, database marketing, frequency marketing, loyalty marketing, relationship marketing, 1-to-1 marketing, permission marketing, and so forth. Learn the basic techniques of Data-Driven marketing / service and you will know how to use your data to attack any of these approaches, while customizing them for your business.

You will learn the hands-on fundamentals of teasing out and evolving the essentials of highly profitable marketing and service programs using customer data, without using fancy hardware or software. Do it yourself with a spreadsheet! Drilling Down is not another “consultant fluff book,” where the promise to deliver actionable ideas is not kept. You will get the whole “how do I actually do it” story in this book.

The book puts forth an easy to follow real world framework for designing your own marketing and service programs using customer data. The core ideas are based on a process and techniques proven under circumstances where there was no previous history to follow for guidance, and require no specialized skills other than knowledge of your business. This framework allows those with little customer data experience to create a structure for marketing and service decision-making. Instead of going about business in a haphazard way, always wondering, “**Who** should I pay attention to? **When** should I pay attention to them? **How** should I design the program?” the reader will be able to make these marketing and service decisions based on the customer data they have on hand.

If you work in a larger company trying to figure out the mysteries of CRM (to CRM, or not – that is the question) following the Drilling Down method “pre-CRM” will allow you to uncover the potential benefits and ROI traps in your customer data **before installing CRM**. Learn how your customer base responds to database marketing and service techniques and use this experience to evaluate the features of analytical - marketing CRM packages and their potential ROI. Drilling Down explains why Data-Driven marketing and service programs work, and shows you how to develop them step-by-step. You can learn at your own pace and implement simple techniques right away, then graduate to increasingly

complex approaches as you experience the results. To top it all off, the book provides descriptions of advanced testing ideas discovered only through years of research in database marketing and customer behavior, with a special focus on interactive customers and their special quirks.

Introduction

I spend a lot of time in marketing and CRM-oriented discussion lists. If you do, you probably also sense the incredible frustration of people who keep asking about using their customer data to retain customers and increase profits. Everybody knows they should be doing it, but can't find out **how** to do it.

Consultants and agencies make this process sound like some kind of "black magic," something you can't possibly do yourself. I disagree. I think the average business owner can do a perfectly decent job analyzing customer data and use this knowledge to develop campaigns and programs that increase sales while reducing marketing costs. That is why I wrote the book.

This book is about the down-and-dirty, nitty-gritty art of taking data generated by your customers and making sense of it, getting it to speak to you; it's about creating insight into what types of marketing or general business actions you can take to make your business more profitable.

We'll be talking about "action-oriented" ideas you can generate on your own to drive sales and profits, ideas that will reveal themselves by analyzing your own customer data, using only a spreadsheet. Of course, you don't have to use a spreadsheet, and just by following the business rules, any average programmer can create all the analytics and reports you need in any standard database.

We have all heard how important it is to collect customer data, to "know" your customer. What I don't hear much about is what exactly you DO with all that data once you have collected it. How is it used? What exactly is Drilling Down into the data supposed to tell me, and what am I looking for when I get there? For that matter, what data should I be collecting and how will I use it when I have it? And can it be done without breaking the bank? The answer to the last question is yes, and the rest of the questions are answered in this book. The following outlines what you will learn and be able to do after reading the Drilling Down book:

What data is important to collect about a customer and what data is not

How to create action oriented customer profiles with an Excel spreadsheet and use these profiles to create marketing and service programs that retain and increase the value of customers.

How to use these profiles to define the future value of your customers and measure the general health of your business, now and in the future

How to use these profiles to encourage customers to do what you want them to

How to increase your profits while decreasing your marketing and service costs

How to design high ROI (Return on Investment) marketing / service programs

How to predict when a customer is about to defect and leave you

How to blow away investors with accurate predictions of the future profitability of your business

Before we get going, let me make some suggestions. Take it easy. Read the book slowly. Make sure you understand each section before you move on to the next, because each section builds on the concepts of the previous section. Important concepts are in **boldface** type. There are plenty of examples provided; please take the time to understand them.

Once you internalize these concepts, you won't believe how profitable your marketing and service programs will be when you do some Drilling Down. This book covers five decades worth of Data-Driven thinking, detailing valuable techniques from the beginnings of catalog marketing up through state-of-the-art techniques used in interactive CRM. It's a lot of serious material and no fluff; so take your time reading it. And if you like the book, tell your friends about it.

Jim Novo

About Jim Novo

Jim Novo is an interactive customer valuation, retention, loyalty, and defection expert with close to 20 years of experience generating exceptional returns on marketing program investments. His professional career has been focused on introducing Data-Driven marketing to new industries. In the 80's, cable television was the target and his groundbreaking programs were widely copied throughout the industry. In the 90's, Jim revolutionized the TV Shopping industry by focusing resources on the customer instead of the products. And for the 00's, the Internet lies squarely in Jim's sights.

At The Home Shopping Network, Jim Novo witnessed the entire business cycle of a hyper-growth interactive retailer. After the land-grab customer acquisition phase, he directed the critical transition to customer retention and credit marketing activities across the television, catalog, and Internet divisions. As Vice President of Programming & Marketing during the slowdown to the mature phase, Jim handled the integration of customer communications and marketing across all the distribution channels, creating a "cradle-to-grave" customer path from Television to Internet to Catalog.

These early interactive lessons are proving valuable to understanding visitor and customer behavior on the web. Jim is recognized for developing the "Friction Model" of behavioral targeting to explain how interactivity and increasing levels of customer control in a business relationship affect customer behavior tracking and measurement, the design of customer retention programs, and the management of "potential customer value" – the future stream of profits expected to flow from a customer.

Jim is an MBA Graduate of Babson College, a school known for a focus on entrepreneurial activity. He majored in Economics and Psychology as an undergraduate at Dartmouth College. Jim is currently working with software and marketing companies to improve their products and practices in database marketing and on the Internet.

You can schedule workshops, seminars, and speaking engagements based on the techniques and methodology described in this book. Jim will teach your marketing and / or IT staff the Drilling Down method using your own data - see <http://www.jimnovo.com/Customer-Consulting.htm> for more information.

Chapter 1

Jonesin' for Some ROI

It was a day just like any other day. The Customer Retention Clinic was open, yours truly at the helm. Both offline and online marketers trudged through, with the same old issues. One is drowning in data. The other has reports that provide no actionable information. Still others have fancy models and profiles, but don't know how to use them to increase the profitability of the company.

I became aware of a fresh-faced marketer, waiting eagerly in line. Something seemed different about this one. Untouched by CRM. Never been to a Business Intelligence demo. Ignores every e-mail plea to attend "educational" webcasts.

"Your question?" I ask.

"Jim, how can I tell if a customer is still a customer?" was the reply.

I stood there, floored by the question. I knew this marketer was special. How elegant, I thought: the summation of 20 years of my work in a single question. Nobody had ever asked it before. They always want to know about the money, you know - how can I make more money, show me the tricks. Addicted to ROI. They start off innocently enough, probably with a spreadsheet. Then maybe a simple model or two. Before you know it they're into data mining. But they don't make any money for the company. Devastating.

Then they show up at my Customer Retention Clinic, looking for the magic bullet, the secret to ROI. But not this one. No, this one was special.

"Why do you want to know?" I asked.

"Because I want to calculate our customer retention rate and track it over time" was the answer.

"You can't put a retention rate in the bank, you know" was my cynical answer. "What you really need is a formal, widely accepted definition of when a customer is no longer a customer in your company. Then you will be able to get at your precious retention rate."

Silence from the fresh-faced one. Then:

"In customer service, they say only 10% of customers complain and tell us they will stop doing business with the company. They say this means customer satisfaction is 90%. Does that mean customer retention is 90% too?"

Well, it's all well and good to be fresh-faced, but now we're getting into naive. Still, I think, maybe there is something here, something worth saving for the future of customer marketing.

"Are you saying the only defected customers are ones you have documented?" I sneer. "Ones who told you they will never do business with you again? Look, to me, a customer is a person or company you sell stuff to, who pays you for a product or service. You have identified 10% who are not going to buy from you anymore; they are definitely defected customers."

"But the word 'customer' implies some kind of 'future activity,' doesn't it? I mean, if you know they will never buy from you again - as in the above complaint example - you don't call them customers, so the opposite must be true: to be a customer, there must be expectation they will buy again. If you know they will not buy again, they're former customers, correct?"

"So the definition of a customer would be someone who:

1. Purchased from you in the past, and
2. Is expected to purchase in the future."

"Just because somebody bought from you in the past and did not tell you they hate your guts now does not mean they are still a customer. A customer is somebody you expect to transact with you in the future; otherwise they are a former customer, by definition."

Not a bad sermon, I think.

"Wait a minute," says fresh-face, "what about customers who purchased in the past that we have no expectations for? We don't have any idea whether they are likely to buy or not, there is no 'expectation.' What about them?"

Oh, so fresh-face is going to play tough with me, I think. Probably an MBA. Wait a minute; I'm an MBA. Is it getting hot in here?!

"Listen, you know the answer to that question, don't you? Because you don't know crap about the people you sell to and their likelihood to buy, you simply

call them all "customers." You have no more reason to call them customers than to call them former customers, but of course, you "default" to calling them all customers. They didn't call up and tell you they are not customers, so they are, right? Is that what you are saying?" It is hot in here...phew.

I go on. "What if they didn't tell you they hated your guts, but they told 10 other people they would never buy from you? Are they still a customer? Do you know how many there are? How many have had a bad product or service experience and never said anything? Is it 10%, 20%, 40% of your customers?"

No reply. Floor staring from the face-man. I have caused hurt feelings. But I have got to move on, there are all these people waiting for their magic bullet, people who need a customer marketing fix, they're jonesin' for some ROI...

"Look, I'm sorry" I say half-heartedly. "Let's come at this from a different direction that will perhaps be more helpful. Let's take all the customers who you think are customers, and ask just one question - when was the last time you had contact with these people?"

"For example, the last time you had any contact with a customer was 3 years ago. Are they still a customer? With no activity for 3 years?"

"Maybe" says fresh-face.

"OK, fine. What about if the last contact with the customer was 5 years ago? Is this person or business still a customer?"

"Maybe" is the reply.

"10 years ago?" I ask, sweating.

"Maybe."

That worked like gangbusters, I think. No wonder nobody knows how to sell more to current customers while reducing costs. All customers are customers for life - unless they tell you they aren't anymore. Sometimes it seems as if today's marketing people have no sense of reality. They are thinking every person or business that ever transacted with them is still a customer!

"All right, one more try," I say impatiently.

"Take two customers – the last contact with one was 10 years ago, the last contact with the other was 2 years ago. Would you be willing to go out on a limb and say the "customer" you last had contact with 2 years ago is more likely to still be a customer than the customer you last had contact with 10 years ago?"

"Yes," says the face.

"Finally," I gasp. "And if the customer you last had contact with 2 years ago is more likely to still be a customer than the customer you last had contact with 10 years ago, is the customer you last had contact with 2 years ago more likely to purchase good or services from you today than the customer you last had contact with 10 years ago?"

"Sure."

"More likely to purchase goods or services now, and in the future, from you?" I wheeze expectantly.

"Yes" is the reply.

"So, let me get this straight - when comparing two customers, the customer you have had contact with more recently is more likely to purchase, relative to the other customer?"

"I would think so" is the answer.

"What???" I gurgle, starting to lose my balance, eyes becoming glassy...

"I mean yes, Jim..."

"Then, if I was to define a customer as someone who:

1. Purchased from you in the past, and
2. Is expected to purchase in the future,

you would say the customer you last had contact with 2 years ago was more likely to still be a customer than the customer you last had contact with 10 years ago? Would you say that?" I ask breathlessly.

"Yes!" the face shouts triumphantly. "I get it!"

"So for any two "customers," the one you had contact with more recently, relative to the other, is more likely to still be a customer and keep purchasing goods or services from you, now and in the future?"

"Yes!!!" fresh-face screams.

"So as a marketing genius, you would then go out and treat these two customers exactly the same, spend the same amount of money marketing to them and servicing them, even though one is more likely to still be a customer and purchase than the other?" I scream back.

The trap was set.

"Yes!!!" face blurts out. "That's what we do! We spend the same amount of money and resources on every "customer," regardless of their likelihood to still even be a customer!"

"I know, your company and most other companies out there. The question is **why do you do this**, when it is so darn easy to tell which customers are more likely to purchase goods or services relative to the others?"

And that, Dear Driller, is what this book is about. You are going to learn some very simple techniques for tracking which customers are more likely to purchase goods or services from you, and then you will learn precisely what to do with this information to increase your sales while cutting your marketing costs.

Because I don't want to see you down at the Clinic, the line is too long already.

First, we're going to talk a little bit about customer models – what they are and are not. Then we'll put a little background in place so you understand the basic objectives and strategy behind High ROI customer data-driven marketing. Next, we'll take a look at the simplest model of all – Latency – because it is the most intuitive model and often the easiest to implement for those just getting started with customer behavior models. Then it's on to the Recency and RFM models. Often used in tandem with the Latency model, Recency and RFM are "smarter" than the Latency model but a bit less intuitive.

And finally, we'll jump into the whole Customer LifeCycle marketing methodology and show you how to use what you will know about simple customer models to really drive the profitability of your customer marketing /

retention / CRM programs. By understanding what the customer is likely to do even before they do it, you can use your modeling intelligence to craft the most profitable customer marketing programs you probably have ever been a witness to. The Customer LifeCycle is the key to the fabled “right message, to the right people, at the right time” marketing kingdom.

By the end of this book, you should be able to very clearly answer some basic marketing and service questions about your customer base. Questions you no doubt have asked many times yourself, such as the following:

Who do I provide marketing or service programs to? When? How often?

Should I contact some customers more often than others? (Yes, you definitely should.)

How much and what kind of incentives should I provide to get a customer to do something I want them to? Can I predict which customers will be responsive to the program? (Yes, you can)

How can I tell when I’m losing a customer or when service has failed?

How can I put a value on my different customers and the business as a whole now, and project this value into the future?

Is my business strong and healthy, or becoming weaker?

What can I expect in future sales from my existing customers?

So what do you say, fellow Driller? Ready to cut that line at the Clinic?

Chapter 2

Customer Profile or Customer Model?

Many people think using your customer data for marketing efforts is about creating a customer “profile.” It’s a hot topic. Everybody wants to do it. But what is a customer profile? Here are 2 kinds of customer profiles:

Customer is married, has children, lives in an upscale neighborhood, and reads Time magazine

Customer visited the web site or business every day for 2 months, but has not visited at all in the past 2 weeks

The first profile is demographic, a set of characteristics. The second profile is behavior-based, involving what the customer is actually doing. **It’s about customer activity.**

Which seems more important to you?

They’re both important in their own ways. For someone selling advertising, or deciding on content for a website, the first profile could be important, because it defines the market for ad sales and provides clues to editorial direction. These are important considerations in attracting customers and generating revenue in the first stages of an online project.

The second profile is about action, behavior, and for anybody concerned about what his or her customers are **doing**, is more important than the first. Will they visit again? Will they buy again? These are the questions answered by looking at behavior. Customer behavior is a much stronger predictor of your future relationship with a customer than demographic information ever will be. You have to look at the data, the record of their behavior, and it will tell you things. It will tell you “I’m not satisfied.” It will tell you “I want to buy more, give me a push.” It will tell you “I think your service is awful.”

I’d argue the second type of profile is more important longer term, because if the customer stops buying from or visiting the site, you’re not going to have much of a chance to serve up the customized pages or ads based on any “profile” given to you. You could customize the heck out of the site based on demographics or self-reported survey data but customers would never see the

results if they never come back. So for the long haul, if you had to choose the more important profile, the profile based on action and behavior would be more critical to you than a demographic one. **Customer behavior profiling is critical to a company interested in selling more to existing customers.**

Marketers who use data often talk about “customer modeling,” instead of customer profiling. Modeling is kind of like profiling, but it is action oriented. Models are not about a static state, like “Customer is 50 years old.” Models are about action over time, like “If this customer does not make a purchase in the next 30 days, they are unlikely to come back and make any further purchases.”

It sounds so mystical, and it is. To see a mathematical model predict customer behavior is astonishing, to say the least. The model says, “Do this to these people and they will likely do this.” The marketer or service provider goes out and does what the model says, and like magic, a good bunch of the customers do exactly what the model said they would. It works like a charm – usually.

Building heavy-duty models is expensive, because it requires an awesome amount of talent and experience. There are many mathematical techniques used to build models, each with their own pitfalls and gotchas. Success depends a lot on the type of business, the kinds of data available, and the experience of the modeler / analyst in building models for a particular business.

What is a model? Simply, it looks at customers who are engaging in a certain behavior and tries to find a commonality in them. The marketer might say to the modeler, “Here’s a list of our very best customers, and here’s a list of our former best customers. Is there any behavioral signal a best customer gives before they stop being a customer? What does the data say to you?”

So here’s what’s in it for you, what this book is about. You can do your own models, based on the decades of experience Data-Driven marketers and service providers have already invested. And while they won’t be as good as the heavy-duty models done by Ph.D. analysts, they’ll be pretty darn good. Plus, they will help you increase profits while cutting marketing and service costs. This book will show you how to do it, with just a spreadsheet. Ph.D. not required.

By the way, once you figure out your behavioral models, you can use them **in combination with demographics and characteristics** to produce an even richer picture of the customer. But the behavior comes first, because it is behavior you want to influence. Knowing the following about a customer is not very **actionable**; there is not much you can **do** with this information:

Customer is married, has children, lives in an upscale neighborhood, and reads Time magazine

But if you add behavior to this demographic profile:

Customers who are married, have children, live in upscale neighborhoods, and read Time magazine appear to be disappointed with our site, because a high proportion of them haven't visited the site in the last 30 days

you can start deciding what (if anything) you want to do about it, because you know these customers are engaging in a specific behavior.

The combination of behavior and demographics can be very powerful indeed. But without the behavior, demographic characteristics don't tell you much. You will learn how to use both in building your models. First we'll talk about customer behavior, and then add customer demographics later on.

Chapter 3

Data-Driven Marketing and Service Drivers

I came up with the phrase “Data-Driven” because I needed one name for the process happening in the background of all the marketing and business optimization approaches where customer data is used. As soon as you say “Relationship Marketing” or “Loyalty Marketing” or “1-to-1 Marketing” or “Permission Marketing” or “CRM,” all kinds of extra ideas creep in, obscuring what’s really going on in the background of all these concepts.

These approaches differ in how they are positioned to the customer, and how they are communicated. But back in the pits where the data analysts are, where customer profiling and modeling take place, they’re much the same.

Data-Driven marketers and service providers generally have two objectives with customer value management, which is what the above approaches are all about:

1. Hold on to the most valuable customers
2. Try to make less valuable customers more valuable

So whether it’s relationship marketing, a loyalty program, permission based, or 1-to-1, you still have to accomplish these goals, and to do it, you have to create marketing or service programs and execute them. This means you have to know the value of your customers and their likelihood to respond to a program, whether the program is customized based on books already purchased, uses loyalty points, or is service-oriented.

The marketing and service programs named above are all “wrappers” around what is really going on — you want the customer to do something, or perhaps not do something. This means you have to reach out to the customer and communicate your marketing and service programs. When you’re going to execute the communication, you need answers to 3 questions — WHAT will you say, WHO will you say it to, and WHEN will you say it. It doesn’t matter what you call your program, what “wrapper” you put it in for the customer — you always have to answer these 3 questions (and maybe a few more).

In addition, you probably care about how much you spend on these marketing and service programs. Ideally, instead of blasting out expensive stuff to every

customer, you would want to spend money on the customers most likely to do whatever you want them to, and not waste money on those who are not.

You want customers to do something, to take action. You want them to visit your website, make a purchase, sign up for a newsletter, add new services. And once they do it for the first time, you usually want them to do it again, especially since you probably paid big money to get them to do this “something” the first time. You don’t want to pay big money the second time. The data can tell you how to accomplish this, no matter what kind of front-end marketing or service program you are running or how you “wrap it up” and present it to the customer. As long as you have the data, you can interpret it for clues as to what steps to take next, and how to save precious marketing dollars in the process.

When you understand the fundamental ideas behind Data-Driven Marketing and Business Optimization, you will understand how to execute all of these customer retention-oriented programs, no matter what they are called. Here are the four primary ideas driving all of these programs:

1. **Past and Current customer behavior are the best predictors of Future customer behavior.** Think about it. Any entity you can define as a customer – external, internal, distributors, manufacturers, suppliers – they all pursue certain routines, and changes in these routines often indicate an opportunity or challenge is ahead in your relationship with them. When it comes to action-oriented activities like interacting with a web site, this concept really takes on a very important role. You can predict future behavior based on an understanding of past behavior, and use this knowledge to improve marketing or service programs.

We are talking about actual behavior here, not implied behavior. Being a 35-year-old woman is not a behavior; it’s a demographic characteristic. Take these two groups of potential buyers who surf around the ‘Net:

People who are a perfect demographic match for your business,
but have never made a purchase / subscribed to a service online

People who are outside the core demographics for your business,
but have repeatedly purchased / subscribed to a service online

If you sent a 20% off promotion to each group, asking them to visit and make a first purchase, response would be higher from the buyers (second bullet above) than the demographically targeted group (first bullet above). This effect has been demonstrated for years with many different Data-

Driven programs. **It works because actual behavior is better at predicting future behavior than demographic characteristics are.**

2. **Customers want to win at the customer game.** They like to feel they are in control and smart about choices they make, and they like to feel good about their behavior. Marketers and service providers take advantage of this attitude by offering programs and communications of various kinds to get customers to engage in a certain behavior and feel good about doing it. Customers like to “win” through these programs, whether they are consumer customers taking a discount, B2B customers getting enhanced attention or service, distributors receiving volume-based perks, or manufacturers partnering on supply chain issues. Communication programs encourage behavior. If you want your customers to do something, you have to do something for them, and if it’s something that makes them feel good (like they are winning the customer game) then they’re more likely to do it.
3. **Data-Driven programs are about allocating resources.** All businesses have limited resources, even the dot-coms (eventually). When you spend \$1.00 on a program, you are looking to make back more than \$1.00 in **PROFIT** (not sales). If you can’t make back \$1.00, the dollar is not worth spending. Given multiple places to spend the program dollar, if you can get back \$2.00 in one place and only \$.50 in another, wouldn’t you rather spend it where you get \$2.00 back? This approach is called **Return on Investment, or ROI, and is the reason why you want to do Data-Driven programs in the first place.** Data-Driven marketing and service programs are among the very few allowing you to accurately measure ROI.

It’s about knowing you will make a \$2.00 for every \$1.00 you spend. If you know this for sure, wouldn’t it be foolish not to spend every \$1.00 you had in the budget to get \$2.00 back? If you always migrate and reallocate program dollars towards higher ROI efforts, profits will grow even as the program budget stays flat. This idea is at the center of ROI thinking — reallocating capital with low return to higher return projects or programs, generating higher profits in the process.

ROI is often a difficult concept to understand because there are so many people using ROI in the wrong context and measuring it incorrectly. You will learn the correct way to calculate and use ROI later on in the book. If you have a financial background, you probably know that what people nowadays call ROI is really ROME (Return On Marketing Expense), but I’ll use ROI to keep things from getting too confusing.

4. **Action – Reaction – Feedback – Repeat. Data-Driven marketing and service programs are driven by creating continuous communications and interactions between the business and the customer, and analyzing these interactions for challenges or opportunities.** Marketing and service programs are conversations, as the ClueTrain Manifesto (www.cluetrain.com) and Permission Marketing (www.permission.com) have pointed out (if you have not read these books, do so, they are not just dot-bomb fantasies). At a high level, service is just another form of marketing – and an extremely important one. Marketing and service provision using customer data is a highly evolved and valuable conversation, but it has to be back and forth between the program operator and the customer, and you have to L-I-S-T-E-N to what customers are saying through their actions and data these actions create.

That’s why I will sometimes talk about the data “speaking to you.” The data is, in effect, speaking for the customer, telling you by its very existence (or non-existence) that there has been an action (or not) that is waiting for a reaction. **An action or inaction is a raising of the hand by the customer, and the Data-Driven marketer or service provider not only sees the raised hand, but also reacts to it, then looks for the hand to be raised again by the customer.**

For example, if a customer visits your web site every day and then just stops, something has happened. They are unhappy with the content or service, or they have found an alternative source. Or perhaps they’re just plain not interested in you anymore. This inaction on their part is the raising of the hand, the flag telling you something has happened to change the way this customer thinks about your site. You should react to this and then look for feedback from the customer. If you improve the content, e-mail them a notice, and the customer starts visiting again, the feedback has been given. The cycle is complete until the next time the data indicates a change in behavior, and you need to react to the change.

Let’s say this same customer then makes a first purchase. This is an enormously important piece of data, because it indicates a very significant change in behavior. You have a new relationship now, a deeper one. You should react and look for feedback. You send a welcome message, thank the customer for the trust they have displayed in your site, and provide a 2nd purchase discount. Then you await feedback from the customer, in the form of a second purchase, or increased visits. Perhaps you get negative

feedback, a return of the first purchase. React to this new feedback and repeat the process over again.

The Data-Driven model of marketing / service provision is 2-way, as opposed to the 1-way approach of media advertising or “data-blind” service. It is give and take, an exchange, a communication process. Using a lot of customer communications can be costly in the offline world. But communication costs are generally low on the Internet, so the Data-Driven model is ideally suited for use there. That’s not to say this model doesn’t work offline; the initial development and implementation of ideas has been happening in the offline world for decades.

How is this exchange accomplished? Can the data really “speak”? It can and does, but you need to know its language and learn how to listen. It’s not very hard, and I’m going to teach you how to do it. But first we’re going to run through an overview of how these four driving forces of data-driven marketing are turned into actionable campaigns and programs that will drive your sales higher while cutting marketing expenses.

Chapter 4

Customer Marketing Basics

No question about it, the constant drumbeat of the CRM machine over the past several years has confused the heck out of people. I've been doing this stuff for almost 20 years now, and I can tell you it is not as difficult as it is often portrayed. Sure, you can make it very, very complicated if you want to. But if you don't start with the basics, you're going to end up wasting a ton of money.

Let's start simple, shall we?

In this chapter I'm going to explain in a general sense how High ROI Customer Marketing campaigns and programs are developed and implemented, and in particular, address some of the misconceptions people have regarding customer value-based and relationship marketing techniques. Much of what is now called "CRM" from a marketing perspective is based on these fundamental ideas. Remember, CRM is an approach to managing a business, not a technology. You do not need to live on the bleeding edge of technology to take advantage of a customer-based management philosophy.

Generally, CRM / Relationship Marketing / Database Marketing attempts to define customer behavior and then looks for variances in behavior. When you hear people talk about "predictive modeling" or looking for "patterns" using data mining, they are essentially taking a behavioral approach using the latest tools. Once you know how "normal" customers behave, you can do two things with your business approach:

Formally document "normal" customer behavior and internalize it systemically, leveraging what you know to improve business functionality and profitability.

Set up early warning systems, triggering events, or "trip wires" to alert you to customer behavior outside the norm. This variance in behavior generally signals an opportunity to take action with the customer and increase their value - online or offline.

What is most important to measure in CRM is change. People spend way too much time worrying about "absolute" numbers, like LifeTime Value – the cumulative value of the customer now and in the future. What they should

really be looking at is "relative" numbers - change over time. It's not nearly as important to know the absolute or exact value of a customer as it is to know whether this value is rising or falling over time. Customer behavior also changes over time, and these changes in behavior typically precede a change in customer value. That means if you track these changes in behavior, you can forecast a change in value, and if you can forecast a change in value, you can get your campaign or program out there and do something about it. This is the core idea behind Relationship Marketing, and these changes in customer behavior and value over time are called the Customer LifeCycle. Knowing and understanding the Customer LifeCycle is the most powerful marketing tool there is; you will learn how to track the customer LifeCycle and use it to increase the ROI of your customer marketing later in the book.

Segments of customers tend to follow similar behavioral patterns, and when any single customer deviates from the norm, this can be a sign of trouble (or opportunity) ahead. For example, if the average new cellular customer first calls customer service 60 days after they start, and an individual customer calls customer service 5 days after they start, this customer is exhibiting behavior far outside the norm. Is there a potential problem, or opportunity? Does the customer having difficulty understanding how to use advanced services on the phone? Or is the customer happily inquiring about adding on more services? In either case, there is an opportunity to increase the value of the customer, if you have the ability to recognize the opportunity and react to it in a timely way.

Understand, there is no "average customer," and a business will have many different customer groups, each exhibiting their own kind of "normal" behavior. The tools available to identify and differentiate customer segments using behavioral metrics are discussed at length in this book. For example, the type of media or offer used to attract the customer can have a dramatic effect on long-term behavior, and customers who come into the business on the same media and offer at the same time will tend to behave in similar ways over time.

In the cell phone case above, number of days from sign-up to the customer service call serves as the "trip wire," and detects a raising of the hand by the customer, which should say to the marketer, "I'm different. Pay attention to me." It is then up to the marketing behaviorist to determine the next course of action. Trip wire metrics like these provide the framework for setting up the capability to recognize the opportunity for increasing customer value.

This raising of the hand by customers, and the reaction by marketers, is the feedback loop at the center of Relationship or LifeCycle-based Marketing. It's a

repeating Action - Reaction - Feedback cycle. The customer raises the hand, the marketer Reacts. The customer provides Feedback through Action — perhaps they cancel service, or perhaps they add service. The marketer reacts to this Action, perhaps with a win-back campaign, or with a thank you note. It's a constant (and mostly non-verbal) conversation, an ongoing relationship with the customer requiring interaction to sustain itself. It is not a relationship in the "buddy-buddy" sense. Customers don't want to be friends with a company, they want the company to be responsive to their needs — even if they never come out and state them openly to the company.

This relationship continues to cycle over and over as long as there is value in the relationship for both the customer and the marketer. If the customer takes an Action and there is no Reaction from the marketer, value begins to disappear for the customer, and they may defect. When value disappears for the marketer (the customer stops taking Action / providing Feedback), marketers should stop spending incremental money on the customer.

Notice I did not say "fire the customer" or any of the related drivel thrown around in some of the CRM venues. All customers deserve (and pay for) a certain level of support. The real question is this: for each **incremental**, or additional dollar spent on marketing to the customer, is there a Return On the Investment? If I have the ability to choose between spending \$1 on a customer returning \$.50, and \$1.00 on another customer returning \$2.00, I would be nuts not to choose the customer returning \$2.00. I have not "fired" the customer returning only \$.50; I have just **chosen not to spend incremental money** doing any special marketing or service programs with them.

Do you see the difference?

In fact, much of the profitability typical of High ROI Customer Marketing techniques comes from knowing who **not to spend on**. Most of the decreased profitability in any marketing program is a result of over-spending on unsuitable targets with lowered returns. But because marketers tend to look at results in the aggregate, or they are looking at demographically-based segments to measure a behaviorally-based outcome like purchases, they miss important details. For example, certain segments in the campaign or program may return \$5.00 for each \$1.00 spent while others may lose \$5.00 for every \$1.00 spent, even though the campaign as a whole may return \$2.00 for each \$1 spent.

When you are trying to encourage a customer to buy something, you are looking for a behavior to occur. To measure the results of such a marketing campaign using only demographic segmentation without any behavior-based metrics is

misleading at best, and lazy otherwise. If you are trying to create behavior, use behavior as your measurement yardstick to define success.

Why is all of this important to understand?

Customers who are in the process of changing their behavior - either accelerating their relationship with you, or terminating their relationship with you - are the highest potential ROI customers from a marketing perspective. They represent the opportunity to use leverage, to make the highest possible impact with your marketing dollar. You may make some money marketing to customers who are just cruising along the LifeCycle, acting like an "average customer." But when you can predict the likelihood of an average customer to turn into a best customer, and you successfully encourage this behavior, or you can reverse a customer defection before it happens, then there are tremendously profitable longer-term implications for the bottom line. You will discover these opportunities by understanding behavior and setting up trip wires to alert you to deviations from normal behavior by a customer.

What about all the rest of the customers, those who are not either accelerating or terminating the relationship? Leave 'em alone. Whatever background marketing you are doing (advertising, branding, service campaigns, etc.) is serving them just fine. **High ROI Data-Driven marketing techniques are best used (and create the highest returns) when they are used to surgically strike at a trend in behavior, not when customers are comfortably plodding along.** However, there are not nearly as many comfortable plodders as you think; in fact, from 40% to 60% of your customer base is either in the process of accelerating or terminating their relationship with you right now. So the real question is this: how do you find out who these customers are, and how do you take advantage of the situation?

Latency, Recency, and all the other customer behavior metrics described in the Drilling Down book are simply tools for recognizing the opportunity to take an Action in Reaction to the customer raising their hand. If you don't have some kind of system to recognize customers in the process of changing their behavior, you will miss out on most of the highest ROI customer marketing opportunities you have. And don't count on the customer to e-mail or call you when they're thinking of changing their behavior - we both know that is not typically going to happen. A more likely scenario: they will just stop taking Action and providing Feedback. And by then, it's too late for you to do anything profitable about it. Set up your trip wires and predict the behavior, folks. It's the only way to sense when an average customer is ready to become a best customer. And reacting to

a customer defection after the fact with a “win-back” campaign is a truly sub-optimal way to “manage” a relationship.

For example, a win-back program is triggered when the customer defects. Have you switched long distance or cellular providers lately? Did you get inundated with win-back calls begging you to reconsider? “Jim, we just wanted you to know we have lowered our rates.” Yeah, well, thanks for telling me after overcharging me for the past six months! But could they have known I was about to switch by looking at my behavior?

Sure. If they had looked at the calling patterns of previously defected customers like me, they would have seen a common thread in the behavior. These patterns create the “trip wires” for initiating high ROI marketing campaigns before the defection. The proper profit maximizing approach is to wait until I **look like I'm going to defect**, and then call me and offer a lower rate **before** I defect. I would humbly submit marketing to the customer after they defect is a sub-optimal approach; the decision has already been made. If you can market to them when they appear likely to defect, you optimize your marketing resources by not applying them too soon or too late in the Customer LifeCycle.

Based on a national survey, 50% of marketing managers do not know their customer defection rate, and the other 50% underestimate the true defection rate. After reading this shocking statistic, I figured it was time write the book on using Customer LifeCycles to both track customer defection and define high ROI opportunities to retain customers before they defect. If you understand the Customer LifeCycle, you can predict the primary defection points and react to them before customers leave you. This is the highest ROI marketing you can possibly do; it's much cheaper than “win-back” (after the customer defects, response is much lower) and preserves the investment and profits you have in the customer already.

Chapter 5

Customer Marketing Strategy: The Friction Model

You have probably heard or read references to the “portfolio” approach to managing customers and their value. I think it’s a sound idea and one I have used over the years because it’s generally quite easy to understand in theory, though the actual implementation is always left for you to figure out on your own. So we’re going to take a look at this portfolio approach for managing customers and I am going to supply you with the implementation tools you need to actually make it work. This is an important chapter, because understanding these concepts will provide you with the very foundation needed for developing all of your Data-Driven marketing campaigns and programs.

The general idea behind the portfolio approach to customer value management is this: your customer base is a business asset. Businesses can have lots of different assets, for example, real estate holdings, buildings, inventory, and common stock, along with other financial instruments. Each of these assets has a value to the business. This collection of assets is an “asset portfolio,” just as you may hold your own personal portfolio of stocks.

The assets in a portfolio have a current value, which is what they can be sold for today. As we know, there can be changes in the current value of an asset portfolio over time, as what you can sell assets for changes almost daily. Assets also have an “expected” or future value, which can be rising or falling as well, depending on the market for an asset and the type of asset it is. For example, real estate generally appreciates in value over time, but machinery generally declines in value over time. This means at any point in time, an asset has a current as well as a potential or future value.

The customer base can be viewed as such an asset as well, and in fact, each customer has a current and a potential value. The current value is whatever the customer has created in value for the business as of today. Current value could be the cumulative profits for the customer since they became a customer, or the cumulative advertising value of all the visits made to a web site since the first one. Potential value is the future stream of profits expected from the customer as long as they continue to be a customer. If the customer terminates the business relationship, the potential value of the customer drops to near zero; this is the end of the customer LifeCycle, the defection by the customer. The sum of

Current Value and Potential Value is equal to the LifeTime Value of the customer; it's the Total Value contributed by the customer to your business.

If customers in your customer portfolio have both current and potential value, then you can set up a 2 X 2 chart describing the value of your customer base in terms of current plus potential value (LifeTime Value), shown below.

Current Value ↑	Low Potential Value, High Current Value Grow These Customers	High Potential Value, High Current Value Keep These Customers
	Low Potential Value, Low Current Value Should You Spend Money Here?	High Potential Value, Low Current Value Grow These Customers
Potential Value →		

Figure 1: The Customer Value Portfolio

Customers having both high current value and high potential value (upper right corner of chart) are the “rocket fuel” customers; these are the 10% - 20% of your customers generating 80% - 90% of your profits. You very much want to keep these customers and should be paying special attention to keeping them happy; these are your best buyers, heaviest visitors, and so forth.

In the lower left corner of the chart, you have the opposite situation; these customers have low current and low potential value. This group probably includes most of your 1X buyers, accidental visitors to the web site, and so on. For the most part, though it's nice to have these customers and they perhaps contribute to paying overhead costs, you probably should not go out of your way to spend a lot of resources trying to grow their potential. In fact, this group likely contains every customer you have **already** spent too much money marketing to – those that never respond. This is also the group customer “win back” programs often focus on.

The upper left and lower right corners of the chart hold customers with a mix of current and potential values. In the upper left, you have high current, low potential value customers. This area is populated mostly by defecting best customers – they were best customers at one time (by current value) but for whatever reason have slowed their profit-generating activity with you and are probably destined to fall into the lower left corner of the chart by defecting. If you're smart, you'll come up with programs that drag them back across to the upper right corner. Customer retention programs should be focused on this group, but more often than not, are not really focused on any group in particular, and that is why they have a high failure rate.

In the lower right corner, you have customers with high potential value and low current value. Who are these people? It's likely they are fairly new customers who have not had a chance to create a lot of value for you yet, but are **expected** to create value in the future. If they do, they will rise into the upper right hand corner of the chart and become “rocket fuel” customers. If they don't, they will fall back across the chart into the lower left corner and contribute very little. Customers in this corner should be the targets of programs designed to increase customer value, though as with the retention programs mentioned above, these “grow the customer” programs are often not focused on this specific group and tend to actually lose a lot more money than they make.

That's the portfolio approach to managing customers and their value, or at least my definition of it. There are others, which for the most part use lifestyle or demographic metrics to allocate the customers. But we're on to that charade, right? Demographics tell you nothing about the current or potential value of the customer, and if you're in a real business, what you care about is the money. For this reason, my approach uses actual spending or value-generating behavior to allocate customers into the quadrants of the customer portfolio.

You say, “Yea, but wait a minute Jim, you're pulling a fast one here. I get how current value is derived, I mean, it's the actual transactional value of the customer – sales, visits, whatever behavior is monetized by the business. But how do you do this “potential value” allocation, how do you measure potential value? I guess future behavior will create value in the future, but how do I measure behavior that has not happened yet? What kind of behavior indicates the potential value of the customer? I was with you until now, but ...”

Relax. Can you take the pebble from my hand, grasshopper? When you can take the pebble from my hand, it will be time for you to leave...

If you didn't get the reference above, you're not up on your 70's TV shows. Try a web search on "pebble grasshopper Kung Fu" if you really need to know.

You are right. This whole potential value measurement issue is, of course, the big problem embedded in the preaching you hear on LifeTime Value, CRM, and these portfolio models of customer value. How do you deal with this whole "potential value" question, how do you actually measure it and act on it?

Well, fellow Driller, would it surprise you to learn that the specific answers to those questions are what the rest of this book is about? I'm not going to give you a conference lecture about all these wonderful things you should be doing with customer value management and then not tell you how to actually do them. Oh no. You will find out exactly how to measure potential value, and as a bonus, you will be surprised how easy it is. In fact, there are specific metrics for potential value and you will learn what they are and exactly how to use them.

Recall this passage from the previous chapter:

It's not nearly as important to know the absolute or exact value of a customer as it is to know whether this value is rising or falling over time. Customer behavior also changes over time, and these changes in behavior typically precede a change in customer value. That means if you track these changes in behavior, you can forecast a change in value, and if you can forecast a change in value, you can get your campaign or program out there and do something about it. This is the core idea behind Relationship Marketing, and these changes in customer behavior and value over time are called the Customer LifeCycle.

So the following may not surprise you: there are LifeCycle Metrics you can use to forecast future changes in value **by tracking behavior in the present**. Pretty handy, huh? And just in time, it seemed like you were getting kind of unruly...

These LifeCycle metrics are where the idea of Friction comes into play. They measure Friction so that you can track and manage it. And if you can track and manage Friction, you can actually put the concept of the customer portfolio management from above into action.

Friction is really about the likelihood a customer will continue to do business with you. The actual causes of friction are created on the business side, and manifest themselves on the customer side as impatience, frustration, and lack of loyalty. Customers encounter varying degrees of this friction in their business relationships, and become more or less likely to do business with you as this

friction changes. They already have low tolerance for poor customer service, processes that don't work as they should, pricing that changes unexpectedly or is confusing, interfaces that make it difficult to accomplish tasks, communications that are sloppy, not delivered in a timely way, or irrelevant. All of these friction points tend to create increasing levels of frustration and ill will, which over time mutate into dissatisfaction and defection. Friction accumulates to the point the customer simply decides to start seeking alternatives, and once alternatives are found, the customer terminates the prior business relationship.

Now, none of this may sound new to you, but here is something that is new. **The friction effect is especially true and is more pronounced as “customer control” of the business relationship increases.** Customers are demanding and taking more control of business relationships themselves, as is true with web retail, or have been forced to take control, as with the practice of pushing customers to serve themselves through the web or a telephone interface. **As the ability for the customer to exert control in the business relationship increases, customers become less and less tolerant of friction.**

And, as friction rises, the customer becomes less and less likely to do business with you in the future. If a customer is becoming less and less likely to do business with you, the value you could realize from the business relationship with the customer in the future has to be falling.

In other words:

Rising friction = falling potential value; falling friction = rising potential value

So, if you can measure friction, you can measure potential value. And measuring friction is exactly what LifeCycle Metrics do. By measuring friction, these metrics also measure the likelihood of a customer to do business with you in the future, and so also measure the potential value of the customer. Visitors and customers will “signal” their friction levels through their own behavior; LifeCycle Metrics organize and codify this behavioral data for you, and allow you to create reports and trip wires that flag increasing or decreasing friction.

And how do you reduce friction? By applying the **grease**, my fellow Driller – your innovative selling and service campaigns are the grease that will hopefully reduce friction and increase the potential value of the customer. Fortunately, you will have your LifeCycle Metrics to tell you precisely who needs the grease, when it should be applied, and even when it should be applied a second time. Your potential value metrics will also tell you when your relationship with the

customer has already “seized up” and it’s too late for the grease. You only have so much grease and the grease is expensive, so you want to apply it only when and where you think it is likely you can reduce friction and prevent the relationship from seizing up.

By the way, customers are not the only folks who experience friction, people **trying to become customers** experience it also. An easy way to measure this want-to-be-a-customer friction is to look at the visitor conversion rate on your web site. Navigational design and layout determine “physical” friction and copy elements determine “emotional” friction. Design and layout testing will reduce physical friction; persuasive copywriting will reduce emotional friction. Success at reducing want-to-be-a-customer friction is measured by an increased visitor conversion rate.

But back to customers. With our first LifeCycle Metrics, Latency and Recency, we’re going to be looking at the tracking of **potential value** only, and how you can use changes in potential value to trigger High ROI Customer Marketing campaigns or programs. After the Latency and Recency metrics we will cover the RFM model, which uses both Current Value and Potential Value metrics to really juice up your results and drive even higher profits to the bottom line.

Latency Metric Toolkit

Chapter 6 Trip Wire Marketing

An easy to implement and proven powerful potential value LifeCycle Metric is called Latency. Latency refers to the average time between customer activity events, for example, making a purchase, calling the help desk, or visiting a web site. All you have to do is calculate the average time elapsed (Latency) between the two events, and use this metric as a guide for anti-defection campaigns. Many small business people naturally use Latency in an intuitive way, for example: "Gee, it has been a while since Mary Lou had her hair styled." What the stylist really means is this: Mary Lou is taking longer than the average customer to schedule a "refresh" on her hair. In database marketing terms, her Latency is exceeding the norm. So the stylist calls Mary Lou and finds either a customer who appreciates the reminder or a customer who has defected to another salon. The longer the stylist waits to contact Mary Lou after the average Latency trip wire has triggered, the more likely it is she has already defected, and the **lower her potential value** is to the salon.

In database marketing, we don't rely on "remembering" the habits of thousands of customers; we measure the behavior and react based on these measurements. When you see a particular customer's behavior diverge from the average customer behavior you have calculated above, you get a trip wire event. Since the calculation of Latency is very simple, and the diverging behavior is easy to spot, this type of anti-defection campaign is an ideal candidate for "lights-out" or automated rules-based customer retention campaigns.

As an example, let's take purchase behavior in a retail scenario. If you examine your customers and find the average time between the second and third purchase is 2 months, you have found "third purchase Latency." Any customer who goes more than 2 months after the second purchase without making a third purchase is diverging from the norm, and a likely defection candidate. It's simple logic. If the average customer makes a third purchase within 2 months of the second purchase, and a particular customer breaks this pattern, they are not acting like the average customer. Something about the relationship with this customer has changed; **friction is rising**. This particular customer's LifeCycle has become

out of synch with the average customer LifeCycle, and this condition is a trip wire for a High ROI Customer Marketing event.

On average, if you divert marketing resources away from customers who have made a 3rd purchase within 2 months after the second purchase, and apply these resources to customers who are "crossing over" the 2 month LifeCycle trip wire without making a third purchase, you will end up spending less money and generating higher profits for any given marketing budget. You are applying your limited resources (**the grease**) right at the time in the LifeCycle when they create the most powerful impact – at the point of likely customer defection.

Now, will all these customers respond? No, of course not. But the ones that do generally become active, loyal customers again, and those that don't may not be good customers in the future. The behavior of the rest of your customers tells you so. These non-responding customers may not be worth spending money on to "win-back," and in fact, will have much lower response rates to a win-back campaign. They have already demonstrated their lack of interest with their behavior, and you could be better off financially by just letting them go and focusing on more responsive, more profitable customers.

The above example is a relatively crude approach to Latency. As you might expect, different customer segments will have different Latency characteristics, and the more you fine-tune a Latency campaign, the more profitable it will become. For example, let's say you execute the Latency campaign described above, and succeed in retaining 30% of the defecting customers, making a tidy profit. But you really have two major product lines, software and hardware, each 50% of sales. Could 3rd purchase Latency be different when comparing software with hardware customers? You betcha. On further analysis, you find 3rd purchase Latency for software is really one month, and for hardware it's three months. The average 3rd purchase Latency of all customers is 2 months, but the Latency by product line is specific to each line. So you bust the two groups apart, and run separate Latency-based campaigns, one for each product line.

In your original third purchase Latency campaign, you promoted to customers who did not make a third purchase within 2 months of the second purchase. This means you were "late" for software (because the average Latency is really 1 month) and early for hardware (because the average Latency is really 3 months). When you realign the timing based on the line of merchandise, you find instead of retaining 30% of customers, you retain 50% of the customers, because you have synched-up the marketing effort with the true customer LifeCycle.

And that, folks, is what LifeCycle-based marketing is all about - using your own customer's behavior to telegraph to you the most important (and profitable) time to market to them. The customer, through their behavior, raises a hand and asks you to take action. If you synch up your marketing efforts with the natural customer LifeCycle, you can't help but being more successful.

What if you were to look at an entire series of Latencies? The average number of days between the first and second purchases, the average number of days between the second and third purchases, third and fourth, fourth and fifth, etc. You don't have to use purchases; you could use contacts with customer service, visits to a web site, any behavior important to your business. What would that look like, and more importantly, what can it do for you?

It would look like a snapshot of the customer LifeCycle. And what it can do for you is start you on the path to predicting customer behavior and increasing the value of your customer base. Any type of event can be used – purchases, downloads, site visits – but the event must be one that repeats or be a series of events with an established “action sequence,” like many B2B sales processes.

Let's say you look at average behavior across all customers, and end up with a "Latency Sequence" that looks something like following:

Time between 1st - 2nd event: 90 days
 Time between 2nd - 3rd event: 60 days
 Time between 3rd - 4th event: 30 days
 Time between 4th - 5th event: 60 days
 Time between 5th - 6th event: 90 days
 Time between 6th - 7th event: 120 days
 Time between 7th - 8th event: 150 days

What does this pattern say to you? Think about it.

I'll tell you what it says to me. First, as you probably realized, you are now starting to see something that looks like a "cycle," as in LifeCycle of the customer. It's a series of events you can graph with a line and make charts of. If you can measure it, you can try to affect it in a positive way, and determine the results of your efforts. Second, you now have a series of seven "trip wires" you can use as described above to more finely sift and screen behavior looking for deviations from the norm. If the average number of days between events for any single customer starts to exceed the average for all customers, a trip wire call for action is triggered on that customer. And third, somewhere around the 4th event,

something significant happens to change customer behavior in a very noticeable way. The customer accelerates into the 4th event (the time between events gets shorter and shorter), and then begins to decelerate in terms of behavior (the time between events gets longer and longer). Depending on your business, this may be positive or negative.

How to use this information?

Regarding the Lifecycle and the trip wires, you could have a series of seven actions ready to take at any point in this LifeCycle where the customer deviates from average behavior. As long as the customer stays on track, save the money and take no action. But as soon as the customer misses or "rolls over" past one of these LifeCycle milestones, you know to pull the trigger on your action. If you follow this model, you will end up maximizing every cent of your budget and driving higher profits, because **you don't spend unless you have to, and when you spend, it creates maximum impact**. This is the recipe for High ROI customer management and marketing. Act only when you have to and always at the point of maximum impact.

Regarding the behavior change, if I was a retailer, this looks negative since the "ramp" in buying behavior reversed and went in the other direction. If I was running a pure service center, this may be a very desirable pattern; perhaps meaning the customer has "learned" the product and no longer needs as much service. It could be negative though, since opportunities to up-sell or cross-sell the customer are decreasing over time. It depends on your business. The important thing to recognize is this: there was a change in behavior, and you should try and determine how you might affect this change in a positive way. Reversals in the direction of a behavior like this are almost always significant turning points in the relationship with the customer.

Human behavior dynamics often take on seemingly "physical" properties. Inertia is one such property - an object in motion tends to remain in motion unless acted on by an outside force. This reversal in the direction of the customer "momentum" after the 4th event indicates there is something about your business - a process (or lack of a process), a product (or lack of a product), something - which causes the average customer to "slow down" and reverse their contact momentum. This reversal of momentum, fellow Driller, is evidence of **a change in friction**. Changes in friction can be positive or negative, depending on what activity you are measuring and the nature of your business and relationship with the customer.

In most business cases, more activity is better; you want more sales, more visits, more downloads, etc. In this business case, customers demonstrating a slowing in the rate of their activity means **friction is rising**; you need to find out why and do something about it. In some cases, primarily in service-oriented settings, less activity is better (think trouble calls). Under these circumstances, slowing activity can be viewed positively (through the eyes of the customer and business, fewer trouble calls is good) and this **means friction is falling**.

Let me say this another way to make sure you have the point: rising friction is always bad for the customer and the business because it indicates the likelihood to continue the relationship and potential value are both decreasing; falling friction is always good for the customer and the business because it indicates the likelihood to continue the relationship and potential value are both increasing. Whether a **particular behavior** is indicative of rising or falling friction depends on the business situation, as demonstrated with the Latency case above.

The slowdown in activity at the 4th event indicates rising friction if you are a retailer; it may indicate falling friction if you are Help Desk and you actually help your users. On the other hand, if you know your Help Desk users are generally a frustrated bunch, a slowing of activity at the 4th event perhaps means they are simply giving up and friction is rising. Frequently in a service center or Help Desk environment, the “reason codes” for contacts help you understand whether a certain behavior indicates rising or falling friction; you might want to run your Latency calculations not on all calls, but just for specific reason codes to gain more insight. And if you are not collecting reason codes for each call, what are you waiting for? That piece of data is important!

If I am profiling retail activity, this Latency sequence looks negative, a slowing rate of purchase indicates an increase in friction. If I had very limited resources, given the seven possible promotional opportunities listed above, but looking for the **absolutely highest ROI on a single promotional event**, I would send a promotion to the customer immediately after the 4th purchase - and no sooner. I don't want to spend money on a promotion or by reducing my margin if I don't have to, so as long as the customer is accelerating, there is no reason to spend any money. But I would really like the ramp to continue past the 4th purchase, and any way I can bring that 5th purchase in closer to the 4th is going to affect my bottom line, and perhaps lengthen the ramp into the 5th or 6th purchase and beyond. If I had more money to spend on promotions, I would test each of the seven trip wire opportunities, and pursue only those with the highest ROI, probably using a separate and unique discount approach for each of the seven trip wire opportunities.

If I am profiling contacts in a service center, this behavior might be a good or bad thing, depending on the circumstances. If this pattern of slowing contacts indicates frustration on the part of the customer, as in the retail example, friction is rising and I want to act on the problem. If I up-sell and cross-sell, I would look to weight more of this activity early in the process knowing I am not going to get as many chances as the customer becomes less likely to call.

However, on a help desk, slowing of contact behavior could mean the customer no longer needs as much help. If this is the case, what I am observing in the behavior is actually a reduction in friction. The fact it takes 4 calls to educate the customer in the first place might not be acceptable, and I would look for ways to decrease the length of time it takes, reducing friction earlier in the cycle.

Success in any of the cases above creates incremental value with very little expense; you're not necessarily changing what you do, just when you do it — to match more closely with the customer LifeCycle. The point of profiling the behavior is to discover the most profitable time is to act.

Of course, you can begin to subdivide the customer base, just as we did in the hardware / software example above. The Latency Sequence may look quite different for hardware buyers relative to software buyers, and it will certainly be different by the type of campaign you used to attract the customer in the first place. Once you are able to compare and contrast different customer LifeCycles by product, campaign, customer source, or by any other data point meaningful to your business, you will begin to paint a more complete picture of what parameters positively or negatively affect customer behavior. Once you understand the behavior, you can learn to profit from it.

Chapter 7

The Hair Salon Example

There are three main phases to a successful High ROI Customer Marketing program: **Measure, Manage, and Maximize**. We'll tackle each of these components one at a time in this example.

Two hair salons operate in the same town, Salon A and Salon B. Both are equally competent one-person operations and charge similar prices for similar services and products. And both salons practice CRM.

There is a difference though - Salon A does not use customer data to track and manage the CRM effort, but Salon B does. Salon B's CRM toolset consists of a paper appointment book and a PC with a spreadsheet program. Salon A has only a paper appointment book, and doesn't really track anything.

One day the owner of Salon A is thinking:

Where has Mary Lou been? She's a high value customer who comes in to get the whole job done - hair, nails, massage, the works. Seems to me she hasn't been in the Salon for a while. She's tardy in scheduling her session. I should call her and find out when she is coming in.

The owner of Salon A is practicing CRM. High value customers have been identified, and a change in the behavior of one of these customers has been detected. This situation has been evaluated, and an action to take has been decided on.

But the owner of Salon A is very busy that day, and forgets to call Mary Lou. What's more, the owner has no system for classifying the fact Mary Lou has not been in "for a while." How long is a while? Part of why the owner forgets to call Mary Lou is there is no real urgency; she's just "tardy." But how tardy is tardy? When should the call be made? If there were a rule about "tardy," perhaps there would be more urgency to make the call. But there isn't, so it may seem like a waste of time. The owner thinks later on:

She'll come in sometime soon. I'm too tired to make the call tonight.

As we sit here gazing into Salon A, some other thoughts probably come to mind. How many Mary Lou customers are there? And how "tardy" will they get before the owner calls them? When you are making money cutting hair all day, it's probably hard to face calling Mary Lou customers, right? Time spent on the phone calling customers or sending them postcards is time not spent cutting hair, and the owner of Salon A can't afford to not cut hair. If the owner had only the time or energy to call just three Mary Lou customers, which three would it be?

If the owner has to give up time cutting hair to make calls, these calls better result in more business than was lost by not cutting hair to make calls. This potentially negative outcome is called "opportunity cost." If resources are allocated away from an income producing activity towards another activity, you better make sure these resources create more value than they did before re-allocation. If they do not, an opportunity cost has been created. The two fundamental rules of High ROI Customer Marketing are designed to avoid these opportunity costs:

1. Don't spend until you have to, and
2. When you spend, spend at the point of maximum impact

Over at Salon B, the owner has been thinking along the same lines as the owner of Salon A, about a High Value, tardy customer named Angela. The owner is cleaning up for the night, and thinks:

How many Angela customers do I have? If I keep forgetting to call my Angela customers, I may eventually lose them. But they always come back. Or do they? I'm going to start **Measuring** Angela customers. I'm going to start tracking "tardy" customers and find out exactly what this issue is about. If it's a real issue, I'll worry about it then. If it's not an issue, I can forget about it once and for all, and spend my time cutting hair.

So the owner of Salon B sits down with the paper appointment book, looks through the customer names, and enters all the "High Value" customer names into the spreadsheet, one to a line. The owner reasons the choice to track high value customers in this way:

If there is anything to this "tardy Angela" customer thing, I get hurt the most financially by losing High Value customers. If it's ever going to be worth spending time on this instead of cutting hair, then it will be most worth it to spend the time marketing to high value customers. If it's not worth it for them, it won't be worth it for any customers and I can forget all about the whole thing.

Once the high value customers are entered into a spreadsheet (about 50% of the customers are considered high value), the owner of Salon B then enters all the appointment dates for each high value customer into the columns of the spreadsheet, next to each name. To keep this project manageable, the owner decides to enter only appointments for High Value customers for the past 6 months. The owner also creates columns to subtract the dates from each other for each customer and find the average number of days between visits for each customer. The spreadsheet (nothing special, off the shelf software) is smart enough to know these entries are dates and is able to easily subtract them and convert the result into days, so all these calculations are easy and take less than an hour to create.

The owner of Salon B is then astonished to discover these facts about customers: About 30% of high value customers have not had an appointment in 6 months. Since 50% of all customers are high value, this means $30\% \text{ of } 50\% = 15\%$ of all customers are already defected best customers. The average number of days between appointments is very similar across all the high value customers. It is, however, not the 30 days the owner expected, but 40 days.

The owner then assumes a high value, supposedly loyal customer who has not been to the salon in over 6 months is a lost customer - at least for the near future. The owner then calculates the value of the lost business for the 6-month period by multiplying the number of customers lost by the average sale of \$150 per trip at 40 days between trips. Needless to say, the resulting number is a very large, representing many days of total sales for Salon B:

Total Customers	200
Defected Best Customers @ 15 % of Total	30
Number Trips in 6 months @ 40 days between trips	4.5
Revenue per Trip	\$150
Lost Revenue: Defected Best Customers (4.5 x 30 x \$150)	\$20,250

Figure 2: Lost Revenue from Defecting Customers

The owner of Salon B then thinks:

I must be crazy for not looking at this before. I would make more money by not cutting hair for a couple of hours a week if I could get back even one of these

high value customers. I'm going to do something about this right away - before I lose even more high value customers. Now that I have **Measured** this effect and know how much money it is costing me to not address the tardy Angela customers, I need to **Manage** the process somehow. How can I set up some kind of "system" that will help me figure out what to do with this data I have discovered? How can I turn the data into an action plan?

Over at Salon A, the owner knows the names of best customers who "have not been in for a while." But this owner has no system, no way to measure what the dynamics of the situation are. How long is "a while"? But at Salon B, the owner knows the average time between best customer visits is 40 days, and there are customers in this group who have not had an appointment in over 6 months. How can the owner get this business back? The owner thinks:

I'll just mail all these best customers who have not had an appointment in over 6 months a postcard offering them a discount. The postcards will say, "Since you are a best customer, you are entitled to a 15% discount if you come in for a visit within the next two weeks." They will come in and I will start a new relationship with them, and find out why they have not been in. The owner of Salon B prepares the targeted postcards, mails them out, and awaits appointments from these customers

The appointments never come.

A bunch of the postcards come back as "undeliverable," and the owner gets several phone calls from customers saying "I now go to Salon A, take me off your mailing list." Undaunted, the owner of Salon B reasons:

Clearly there is something wrong with this approach. Best customers who have not had an appointment for 6 months must already be "defected" customers. They obviously do not want to come back to me, and feel the relationship is broken already. They have moved on and established new relationships. I will try a new approach with the postcards, and will use the same offer. But this time, I will mail the postcards out as soon as the best customer has not been in for over 40 days. Since the average best customer comes in every 40 days, a best customer who fails to do so is not acting like a best customer. So each week I will use my spreadsheet to identify best customers who have not been in for 40 days, mail the discount postcard out to them, and track the results.

After a month of mailing the postcards to best customers who had not had an appointment in over 40 days, the owner of Salon B sat down to analyze

the program. Of all the best customers mailed to, 1/3 had made new appointments, and 2/3 had not. But even with the discount, the additional profits from these customers paid for the postcard mailing many times over. High value Customer defection was being **Managed** by the program.

Despite this success, two things bothered the owner of Salon B. The first was what customers who responded said when making their discounted appointments. The second was the 2/3 of best customers who did not respond.

The owner thinks:

Half the customers who responded said to me, "I'm so glad you mailed me a discount, I was planning on making an appointment in the next week and would have made one anyway, so it was great to get the discount." So I gave up margin and profits I did not need to give up. And how is it possible that so many of my best customers never responded to my offer? I wonder if there is a way to address these two issues? If I could reduce the number of "would have come in anyway" customers who got a discount, and get more customers to respond overall, I would be really making a ton of money on my best customer retention postcard program. I have **Measured** my best customer defection, and am **Managing** it with this program. I wonder if there is a way to **Maximize**, to make it even more profitable?

Well, fellow Driller, have you got an idea? You know Customer Retention is all about this process: Action - Reaction - Feedback - Repeat. The owner of Salon B has taken an action, and there has been a Reaction. How should the owner go about analyzing the Feedback? The owner of Salon B then has an idea:

What about this group of customers who said "they would have scheduled anyway without the postcard." Are they similar in any way? If there is a common reaction to the postcard among these customers, perhaps there is a commonality in the behavior or backgrounds of the customers. If I can find the key linking these customers together, perhaps I can understand why this is happening with them.

The owner of salon B goes back to the CRM software (a paper appointment book and the customer spreadsheet). The owner has entered "response date" in a spreadsheet column for each customer who responded to the postcard and any comments. The owner sorts the customers by the responders and looks at those customers who said, "would have scheduled anyway without a postcard." For

each customer who responded and said this, the owner looks the customer up in the appointment book to find more details.

"Long hair cuts!!!!" the owner exclaims. "They all have long hair cuts!" which the owner immediately realizes is the problem with the discount postcard mailing program. The owner thinks:

Best customers with long hair styles can come in much less often than every 40 days, even through the average of all best customers is a cut every 40 days. So customers with long cuts are getting the postcard too early - they're not really "defected," and schedule a planned appointment with a discount I did not have to offer. They should get a postcard possibly at 60 days, or even 90 days or longer after their last appointment. Since I have a lot of customers with long cuts, most are getting the postcard too early for the cut. This explains the low overall response rate. Best customers with short cuts however, are probably getting the postcard too late. By the time I get them in the mail and they reach the customers with short cuts, it could be too late, they may have already gone elsewhere for their short hair cut.

The owner of Salon B resolves to recalculate the average days between appointments separately for best customers with long cuts and best customers with short cuts. The owner divides the customer base in two - by length of cut, and finds the average time between trips of long cut customers is actually 75 days, and for short cut customers is actually 20 days. Rethinking the retention campaign, the owner resolves to track each group individually, and to do two types of mailings each week - one to long cut customers over 75 days since last visit, and one to short cut customers over 20 days since the last visit.

Using the advanced CRM system (a spreadsheet program with one customer per row), the owner creates a column for acceptable number of days since last visit - 75 days for long cut customers and 20 days for or short cut customers. Using the date of last appointment, the owner creates a simple equation that uses today's date and last appointment date to calculate days since last visit, and to subtract this number from the number in the "acceptable" column.

The salon owner thinks:

I have created a "trip wire" system for the best customer retention postcard program. When the number in this column approaches zero or goes negative for a customer, it is time to mail the discount "where have you been" postcard. Since each customer has an acceptable number of days since last visit based on

hair cut length, the timing of the mailings should more closely reflect whether or not the customer has actually defected.

The salon owner tests the new campaign - and it works. Not only does the owner get many fewer customers saying "thanks for the discount, would have been in anyway," the response rate among targeted best customers increases by 30%. The program now is maximized for this level of detail - it makes even more money than it did before, and retains more customers while decreasing the cost of discounts given away. A beautiful thing, the owner thinks. But then another Eureka moment comes to the owner of Salon B:

If I use this system there is another benefit - I should be able to actually forecast what my volume should be months in advance based on customers likely to schedule an appointment. If I see a week coming up where visit volume looks to be low, I can promote to some customers and fill up empty slots, maybe give them a discount for scheduling on a specific day when my traffic is light. That way the customer is happy because they get a special one-time discount, and I am happy because I am maximizing my revenue per day by filling up light traffic days with happy customers!

Just then, the owner of Salon B hears someone walk in the door. A voice calls out, "Can we schedule appointments?" The owner recognizes the voice - it belongs to lost best customer Angela, the one who started this whole project by being tardy in scheduling an appointment. Angela is the reason the owner of Salon B first asked the question, "How many tardy best customers do I have?" But what does she mean "we"?

As the owner of Salon B comes around the corner, Angela smiles and says, "This is my friend Mary Lou. She was going to Salon A, but is dissatisfied with the results she is getting. She would like to try Salon B. And I need a cut too! I tried growing my hair out long, but I decided I like it better short."

The owner of Salon B thinks: I can't predict everything, but my new system is sure better than not predicting anything at all!

Chapter 8

The B2B Software Example

A B2B software company has an appealing pitch to business - their software makes a company more efficient and saves more money for the company than

the software costs. The software is modular, with a base application and additional add-ons that are specific to certain business challenges. The selling strategy is to under-price the base application to get market penetration and then make a higher margin on the add-ons. The add-ons drive the profitability of the business, as does the installation and customization of these add-ons.

The company has been quite successful with this selling strategy. But lately the CFO has noticed sales of the base application have risen, but revenue from add-ons has not risen in the same proportion. In other words, the company is further penetrating the market and gaining new customers but getting less revenue from each customer. The CFO thinks:

I can't understand this. Sales of the base application are rising according to plan but overall company revenue is not growing at the same rate. The only thing I can think of that would create this particular situation is fewer basic application customers are buying add-ons. How can I figure out why this is happening?

The CFO calls the heads of business development and marketing to ask about the situation. They both report they are aware of slowing add-on unit sales per customer, but cannot attribute it this to anything specific. The company is simply penetrating the overall market more deeply they say, and as we penetrate further and further, add-on sales seem to have slowed.

The CFO is not particularly satisfied with this answer, and thinks:

If it shows up in my financial statements, it has to be measurable. I'm just seeing this from too high a view. All the sales of the different base applications and add-ons roll up to total sales, so the data I need to better understand this must exist somewhere. The CFO picks up the phone to call the CIO, and then hesitates. The IT people are going to want to know specifically what I am looking for, the CFO thinks. Do I really know?

What is needed here, fellow Drillers, is quantification, some framework for analyzing the situation. What is the real question to be answered here? The CFO knows IT has limited resources to apply to this kind of ad hoc work - if the request just generates information that leads to another question, then time and resources are wasted.

The CFO could ask for monthly product sales percentage by type over the past year. In a lot of ways, this information would simply confirm what the CFO already knows - sales of add-ons have gone soft. But does it answer the core

question of **why** they have gone soft? It does not, and that is the real question at hand. Since customers have different LifeCycles, any monthly sales data will contain customers in various stages of being likely to buy an add-on. So raw monthly financial data - the kind the CFO is used to working with - is not going to answer the "real" question. The CFO thinks:

Customers buy the base package and once they get it integrated and tuned up they start to buy the add-ons. During any one-month period, we have customers who just bought the base package, customers who are in different stages of integration, and customers who are buying add-ons. What I really need to know then is this: what is the average number of weeks between the purchase of add-ons, this year versus last year? If this number of weeks is rising, that is where the softness in add-on sales is coming from - customers are simply taking longer to make the purchase decision. If this number of weeks is constant or falling, then something else must be going on.

With a definition of the question at hand, the CFO picks up the phone and calls the CIO. The CFO gets the report on the average number of weeks between the purchases of add-ons. The information looks like this:

Last Year	This Year
8.6 weeks	8.9 weeks

Figure 3: Average Weeks between Add-on Purchases

So it **is** taking longer for them to purchase, the CFO thinks, and darn it, now I have another question. The IT people are going to have me for breakfast for not thinking this all the way through the first time! I got the information I asked for, but this information is not actionable, I can't **do** anything with it. There is not enough detail in the information to act.

Fellow Drillers, when you are plumbing the depths of your data, try to think of what you will do with the information you are asking for. Imagine getting back your results, and taking an action based on those results. If you can't imagine the action you would take knowing the information, you are not asking the right question yet. The CFO thinks:

Our add-on modules have different prices and different levels of difficulty involved in their integration. And they are usually installed in a particular sequence. So what I really should have asked for is the average number of weeks between the purchase of add-ons **by add-on** - the time between base purchase and the first add-on, the time between the first add-on and the second,

and so forth. Maybe there are problems with installing one of the add-ons due to changes in the next generation of operating systems, for example, and this is slowing the installation of a particular add-on down. If I can get the average number of weeks between add-on purchases by add-on, I can act on it, because I will know which particular add-on is causing the slowdown.

The CFO reluctantly picks up the phone to call the CIO. At least this time, the CFO thinks, I have thought the question out all the way through, and I know what action I can take with the information once I get it. Shortly after a slightly heated exchange involving resource allocation, budgets, and a hiring freeze in IT with the CIO, the CFO gets this report:

	Last Year	This Year
Base app to 1st add-on	12.3 weeks	12.1 weeks
1st add-on to 2nd add-on	10.5 weeks	10.2 weeks
2nd add-on to 3rd add-on	8.7 weeks	8.9 weeks
3rd add-on to 4th add-on	6.1 weeks	6.7 weeks
4th add-on to 5th add-on	5.2 weeks	6.5 weeks
Average Time Between Add-Ons	8.6 weeks	8.9 weeks

Figure 4: Average Weeks between Add-On Purchases by Add-On

Fellow Drillers, it would be nice if the pattern were a bit more clear, yes? It appears customers are ordering their first and second add-ons more rapidly than last year, but as they get to the third, forth, and fifth add-ons, they are ordering more slowly than last year. What could this possibly mean? The CFO thinks:

Well, I answered my question, but I've got another. The reason why add-on sales appear soft is a longer purchase cycle for the average add-on, and the reason this is happening is the later add-ons are taking much longer to be purchased than they were last year, even though the first add-ons seem to be cycling much more quickly. What does that mean? I promised the CIO I would be able to act on this information, and I simply do not know how.

Fearing another phone call right away to the CIO, the CFO thinks:

What I have here is change. There has been a significant change in the way this business works for some reason. Change doesn't happen in a vacuum though; something must have caused these changes to happen, a significant event now being reflected by these average weeks between add-on purchase numbers.

What could it be?

The CFO remembers the heads of business development and marketing saying the company was "penetrating the overall market more deeply, and as we penetrate further and further, add-on sales seem to have slowed." Was this the change the CFO was looking for? What did it really mean, in terms of how the business may have changed?

Getting the heads of business development and marketing on the phone again, the CFO asks if this market penetration situation had created any changes in the way the company does business. The CFO hears for the first time about a new trade campaign and a new sales person hired to address a particular market segment. This is most assuredly the change the CFO has been looking for!

Gingerly, most humbly, the CFO calls the CIO once again. This time, the CFO wants to see average number of weeks between add-on installs by add-on **by salesperson**. After a promise to review the hiring freeze is extracted from the CFO, the CIO delivers the following report:

	Last Year	This Year	Sales 1	Sales 2	Sales 3	Sales 4
Base app to 1st add-on	12.3	12.1	12.3	12.3	12.3	11.6
1st add-on to 2nd add-on	10.5	10.2	10.5	10.5	10.5	9.4
2nd add-on to 3rd add-on	8.7	8.9	8.7	8.7	8.7	9.3
3rd add-on to 4th add-on	6.1	6.7	6.1	6.1	6.1	8.3
4th add-on to 5th add-on	5.2	6.5	5.2	5.2	5.2	10.2
Avg. Time Between Add-Ons	8.6	8.9	8.6	8.6	8.6	9.8

Figure 5: Average Weeks between Add-On Purchases by Add-On by Salesperson

And there it is.

Clients of Salesperson # 1, # 2, and # 3 are purchasing add-ons at the same rate they did last year. The clients of the new salesperson # 4 are purchasing in a dramatically different pattern, with much shorter purchase cycles in the beginning and much longer cycle purchases later on. Literally, the LifeCycle of the customers in this market segment are different from the LifeCycles of the average customer from previous years, and dramatically so.

It takes these customers on average 14% longer to purchase any add-on - 9.8 weeks versus 8.6, or 1.2 weeks. Over the entire purchase LifeCycle of the add-ons, this increases the purchase cycle by 4.8 weeks (1.2 x 4). If this new segment is doing a lot of dollar volume compared with the old segments, this could significantly affect sales and make add-on purchases look soft - even though they are in fact getting purchased!

At this moment, the head of business development appears in the door with another person who turns out to be new Salesperson 4. The CFO looks up and the head of biz dev, somewhat sheepishly, introduces the new salesperson.

"Glad to meet you," the CFO says. "By the way, can you tell me something? Do the customers in your new segment purchase and install our add-ons in the order we suggest in our operations manuals?"

"No, they don't" said Salesperson # 4. They install them in a different order, because they are having some difficulty installing a couple of the add-ons, and usually delay those to the end of the purchase cycle when they have more experience with the applications. Is there something we can do about that?"

The CFO just smiles, and thinks:

Looks like I just found the money to pay for unfreezing some hiring in IT.

"I think so," the CFO tells new Salesperson #4, calculating the improvement in cash flow on the fly if these add-ons were installed faster. "I really do think so."

Chapter 9

Turning Latency Data into Profits

Customer LifeCycles are a reality: there is going to be a LifeCycle and you will not be able to stop it. You probably don't know about LifeCycles because you have not measured them. You don't even hear many pundits talking about them. This is most amusing given all the jaw flapping and tongue wagging about LifeTime Value; if you don't understand the customer LifeCycle, how would you ever know when the "LifeTime" was over to measure value? The plain fact is people have it backwards; LifeTime Value is the last thing you want to try to wrestle with when just starting out with customer relationship and value management. You start with the LifeCycle, and only after fully playing out that card, do you move on to the idea of LifeTime Value. You do not have to mess around with calculating absolute customer LifeTime Value to be successful using data-driven marketing. Only after you have nailed down the basics of data-driven marketing do you need to go there; you will learn all about Lifetime Value later on in this book. What you need to understand first is the customer LifeCycle, and how to use knowledge of it to your advantage.

Customers are not just customers one day and then not the next day; there is a process to customer defection, and the smart data-driven marketer creates High ROI Customer Marketing programs by taking advantage of understanding the complete customer defection process.

There are two ways you can increase the value of customers:

Extend the customer LifeCycle, leaving more time for the customer to increase in value, by increasing the time the customer takes to defect.

Increase the value of the customer within the existing LifeCycle. The customer still defects pretty much on schedule, but you have done everything you can to increase their value before the defection.

The first approach usually requires some pretty sophisticated tools and can be expensive; loyalty programs are a classic example of extending the LifeCycle. Not for the faint of heart financially and organizationally, loyalty programs also do not work well for every type of business. But they do work and can be extremely profitable if they are designed and executed correctly. If you are

interested in how this type of loyalty program is constructed, visit my website at <http://www.jimnovo.com/download.htm> and download the loyalty case study.

The second approach to increasing customer value above is easier to execute, and for many companies, is the right way to go. It involves what I would call a customer retention or anti-defection program as opposed to a loyalty program, and this is how you go about setting it up.

Recall this table from the Latency Toolkit chapter titled "Trip Wire Marketing":

Time between 1st - 2nd event:	90 days
Time between 2nd - 3rd event:	60 days
Time between 3rd - 4th event:	30 days
Time between 4th - 5th event:	60 days
Time between 5th - 6th event:	90 days
Time between 6th - 7th event:	120 days
Time between 7th - 8th event:	150 days

The first place I would look to address the above customer LifeCycle is the fourth event. Why? This event looks to be the one that is "low hanging fruit," since the average customer is accelerating into it, meaning the response rates should be quite high. In other words, we are taking advantage of the natural behavior customers have demonstrated, rather than trying to force them to do something out of the ordinary.

For the average customer, this fourth event happens at 180 days after the first event. How do I know? Just sum the first 3 lines of the table above: 90 days + 60 days + 30 days = 180 days. Any customer who is 180 days old and has not yet made a 4th purchase, a 4th visit to the web site - whatever the event is you are tracking - is acting outside the behavior of the average customer and is a prime candidate for an earlier than normal defection. This is where you focus your efforts. You set up this fourth event as the "trip wire" - if the customer doesn't trip the wire by engaging in the 4th event by day 180, you take action and try to affect this behavior. If you can save just a small percentage of defecting customers, the ROI can be very high, because these customers represent "found profits" which would not have existed without your efforts. And yes, you can measure these found profits - I am going to show you how to do this below.

This may not be the highest short-term ROI promotion we can do, but in terms of reducing customer defection and extending the LifeCycle, it is probably the

highest long-term ROI promotion we can do, because we are helping “slow customers” accelerate into that 4th purchase. We have a reasonable expectation, based on looking at average customer behavior, that a certain percentage of customers will do this and continue on into the 5th and 6th events. We are choosing a specific group of customers at a specific time in their LifeCycle to promote to, a group with the highest likelihood of success.

Why concentrate on these defecting customers? The **two fundamental rules of High ROI Customer Marketing**:

1. Don't spend until you have to, and
2. When you spend, spend at the point of maximum impact

You don't have to spend on customers who make the fourth purchase or visit within 180 days, because they are acting like "average" customers. Why spend on them if everything there is OK and they are behaving normally? You want to concentrate your spending where it will have maximum impact - on the customers who "roll over" the 180-day barrier without engaging in "average" behavior. These customers are the most likely candidates for a complete defection, and by focusing your resources laser-like on these people, you can spend more per customer and really have some impact.

Put another way, let's say you have a customer retention budget of \$20,000 and you have 20,000 customers. You currently spend \$1 per customer each year sending all your customers the same lame retention stuff - statement stuffers that say you care and so forth. But if you could tell which 5,000 customers were the most likely to defect, and only spent on them at the point of maximum impact - when the defection was taking place - you could spend \$4 per customer trying to stop or slow the defection with the same budget, have a much higher success rate, and actually realize the "found profits" I spoke of earlier. Make sense?

How To Execute a Latency-based Promotion

We'll use a retail example because the numbers are easiest to understand and convey. But the same thought process is valid for any kind of business.

1. Determine the timing of your promotion. You normally want to take action as close to the "trip wire" event as is reasonable and practical, taking into consideration the cost. If you have a ton of customers, there may be enough customers rolling over the "180-day with no 4th purchase" barrier to execute your promotion every week; if not, then

gather up enough customers to execute efficiently. Some may be anywhere from 180 - 210 days old with no 4th purchase. That's fine; but don't let them get more than 30 days past the trip wire without taking action.

2. Create the offer. In a retailing business, this could be as simple as a discount of some kind. You could sub-divide the 180 day old / no 4th purchase customers into "best" and "other," creating a VIP service offer to best customers and a discount offer to other customers.
3. Prepare the list. Select all your 180 day / no 4th purchase customers, and then randomly select 10% of them to not contact. This is called your control group. People will tell you to only use 2% or 3% as control, and statistically they **could** be right about this. But the first time out of the box, I like to go with 10%, for two reasons:
 - a. It's a "no argument" control group size. If your effort works and you can prove it, there won't be chattering from the sidelines about the possibility of a "defective" control group.
 - b. Why spend more than you have to the first time? By taking a large control, you reduce the number of people you are spending on to execute your promotion.

If you created the two groups "best" and "other," you need to take a 10% random sample of each. The other 90% of a group is called the test group; they are the ones who will receive the promotion by direct mail, e-mail, or other means. The creation of proper control groups is absolutely essential to measuring the "found profits" referred to above. If this step has you puzzled, you will read more details on creating control groups and random samples later on in the Advanced Toolkit chapter titled "Predicting Campaign ROI: Set Up" or see <http://www.jimnovo.com/Random-Sample.htm> for more.

4. Now you have two lists of people, control and test. Set up your tracking capability, which at minimum is the ability to run a report every 30 days that reveals the sales of each group starting from the beginning of the promotion, which is when you execute the e-mail, snail mail, or other communication of your offer to the test group. The metric you are interested in here is revenue per customer, so you would

take the total sales of each group from the time the promotion is delivered and divide by the number of customers in the group, for both control and test groups.

5. Deliver your promotion to the test group.
6. Monitor the revenue activity of test and control groups. Run a sales report weekly or every 30 days, and look for divergence in the revenue per customer. The customers in the test group should be registering a higher sales per customer level (you hope). Keep running the report until the increase in revenue between test and control remains stable or begins to fall. When this happens, the LifeCycle of the promotion is over (promotions have LifeCycles too!). Let's say this takes 90 days, so 90 days after the event, you have a revenue per customer number for activity during the promotion, for both the control and test groups.
7. Calculate ROI. I'll use some plug numbers as an example. The idea here is to compare the revenue behavior of the test group with the control group, and determine how much additional revenue occurred because of your promotion. Since the control group experienced no promotion, any difference in revenue between test and control can logically be attributed to the promotion. We then take out costs, and see if we added value to the customer LifeCycle - in more mercenary terms, did we make money or not?

	Control	Test
90 day Revenue per Customer	\$100	\$110
Gross Margin @ 30%	\$30	\$33
Additional Margin Due to Promo		\$3
Per Customer Cost of Promo		\$.50
Additional Gross Margin per Customer		\$2.50

Figure 6: 180 Day / No 4th Purchase Promotion

Here's the key to the above. The people in control generated \$30 in Gross Margin per customer over 90 days; the people in test generated \$33 per customer. So \$3 in additional Gross margin per customer was created because of your promotion, since the two groups are the same in all other ways (if control was truly a random sample).

This \$3 nets down to \$2.50 because the cost of doing the promotion was \$.50 per customer. Note: Nowhere in here are we talking about response rates. Response Rate doesn't matter in the measurement of profitability (it matters a lot in other cases); what matters is actual buying behavior. When you use control groups, you pick up buying behavior you never could have measured by just looking at response rates.

Now, the Per Customer Cost of Event is usually where you get into some arguments. If the event included a discount, the per customer cost of this discount must be included in the calculation:

Discount	\$5
Number Used	500
Total Discount	\$2,500
Number of Customers	5,000
Per Customer Discount	\$.50
Gross Margin / Customer from Above	\$2.50
Gross Margin / Customer - Discount	\$2.00

Figure 7: Calculating the Promotional Discount

Also, in the strictest sense, there is probably additional overhead attributable to the additional revenue: the cost to take a call and ship the box, the cost of additional salespeople needed to cover the promotion, and so on.

Cost of sales people for Promo	\$2,000
Number of Customers in Promo	5,000
Per Customer Cost of Salespeople	\$.40
Gross Profit per Customer from Above	\$2.00
Net per Customer Value - Sales Cost	\$1.60

Figure 8: Calculating the Promotional Overhead

These costs would not exist if you had not executed your promotion, so they should be included in the calculation to the extent you can calculate these additional overhead costs. In Figure 8 on previous page, we calculate the overhead costs of the additional salespeople to get the cost per customer after Discounts and Overhead.

This \$1.60 is profit after all expenses have been paid back. You have added \$1.60 in value to the LifeCycle (and LifeTime Value) of the average customer in the promotion. To get to ROI, we need to look at what the promo cost, and compare this to the value we generated; this is the definition of ROI. How much did we invest, and how much did we get back? We know what we got back \$1.60 per customer Net of all costs, so we need to calculate total costs:

(Data from tables above)

Per Customer Cost of Promotion	\$.50
Per Customer Discount	\$.50
Per Customer Cost of Salespeople	\$.40
Per Customer Total Cost	\$1.40
"All Expenses In" 90-Day ROI	114%

Figure 9: Calculating the Total Costs and ROI

Note: $\$1.60 / \$1.40 = 114\%$

You spent \$1.40 and you generated \$1.60 after all costs. It's a 90-Day ROI because the additional revenue generated was measured over a 90-Day period. A 114% return is not something the CFO is going to be against, trust me. In fact, you could make the argument that since ROI in financial circles is usually measured on an annual basis, and this is a 90-day ROI, the real ROI here is 4x the 90-day ROI, or 456% on an "annualized basis."

These are the found profits you have generated from your effort. By comparing the test group with the control group, you have proven these profits would not exist without your 180-day trip wire promotion. A smaller percentage of customers in the test group defected when compared with the control group; at least some portion of test made a purchase, and some kept right on buying for at least 90 days. These are found profits that would not have existed without your effort. You have proven the 180 day / no 4th purchase trip wire promotion added value to the customer LifeCycle, a total of \$1.60 per customer x 5000 customers = \$8000 to be specific, and you did this without costing the company a single dime, since you paid back all your costs with profit from the promotion, and still had \$8000 left over to put in the bank.

I can hear you now. C'mon Jim, looks good on paper, but 485% annualized ROI? An \$8000 profit on a promotion that with every cost imaginable thrown in costs \$7000? How is that remotely possible?

Folks, it's not just "possible," this kind of return is **normal** in LifeCycle-based promotions. Remember the two rules of High ROI Customer Marketing:

1. Don't spend until you have to, and
2. When you spend, spend at the point of maximum impact

By focusing your resources squarely on the problem, each dollar you spend works much harder. By waiting for the trip wire you narrowed the population you were promoting to, weeding out people you would normally waste money on. And by acting when the wire was tripped, you spent at the point of maximum impact.

Here is why this type of promotion makes so much money. It's anti-defection. You literally kept customers from leaving the company, and the control group proves this. The people you did not promote to in the control continued to slip away, while some portion of folks in the test group were stopped and their behavior reversed. This is where the huge returns come from - it's the relative spending disparity between the groups that creates the "found profits," which would have slipped away had you not done the promotion. It's a "tipping point" kind of idea - if you can be in the right place at the right time with the right catalyst, it doesn't take much change to create a big impact on the scene.

This promotion was not designed to extend the customer LifeCycle, but to add value to the LifeCycle. Did it in fact actually extend the LifeCycle, and how would you measure this effect? All the customers in both the test (received promotion) and control (did not receive promotion) groups were 3x buyers who failed to make a 4th purchase by 180 days after their first purchase. This was the Latency "trip wire" selected to trigger the promotion.

So let's look at tracking these two groups for another 90 days, and look at continuing purchase activity using what I call the Hurdle Rate method. A Hurdle Rate is simply the percentage of customers in a group who have "at least" a certain amount of activity. You define the behavior hurdle they have to reach, and measure the percentage of customers who have achieved this "threshold" (rate). If you track these percentages over time, you can use them to compare the actual and potential value of customer groups as a whole.

At the point of the promotion, 0% of both groups had made a 4th purchase. Recall we measured the profitability of the promotion over a 90-day period after we sent it to the test and control customer groups.

To track the Hurdle Rates for each group, we ask, "What percent had made at least 1 more purchase at 30 days, at 60 days, and at 90 days after the 90-day promotion was over, in both the test and control groups?" We know some percentage of both groups made a purchase during the promotion, because there were revenues generated in both groups. We made a profit in the first 90 days because the revenues were much higher for the test than control group. So at the beginning of this "post promotion" tracking, we see 1% of control and 3% of test have made 4 or more purchases. For the following 90 days after the promotion was over, data might look like this:

% 4 or more purchases	Control	Test
End of 90-day Promotion	1%	3%
30 Days After Promotion End	1%	5%
60 Days After Promotion End	2%	8%
90 Days After Promotion End	2%	10%

Figure 10: Percent Purchasing After Promotion End

Realize this: we have already made money on this promotion, a 114% ROI. We have already added value to the LifeCycle, increasing LifeTime Value - no matter how long a "LifeTime" is (does it really matter, as long as you are making increased profits?)

But as you can see from the chart above, we also extended the LifeCycle itself, because the percentage of customers exceeding the "4 or greater Hurdle" in the test group is far higher than the percentage of customers over the same Hurdle in control, and it appears to be growing over time.

There is a group of customers in the test group who just keep on keeping on - and this percentage (10% at 90 days after Promotion End) is much higher than both the initial group who responded to the promotion and made a 4th purchase (3%) and the test group. What's going on with that?

It's called the Halo Effect. It represents customer activity stimulated by the promotion not occurring within the promotional period. Now, we don't know exactly where it's coming from, and we can't show any measure of profit from it (we defined our promotion period as 90 days), but it is clearly there, plain as the nose on your face. Recall when describing the original promotion, I stated, "Response Rate doesn't matter in the measurement of profitability (it matters a

lot in other cases). When you use control groups, you pick up buying behavior you never could have measured by just looking at response.”

This "buying behavior you never could have measured" is the Halo Effect, working its magic during the promotion. People you have no way to track will respond to the promotion. They want to make a purchase but forget the coupon, for example. So they go ahead and make the purchase anyway - because the promotion "woke them up" to a need for something you sell.

After the promotion is over, the same thing continues. It's the Halo Effect again, working after the promotion. For example, people think about participating in the promotion but wait too long. They've missed it. But they're now in a new state of awareness about your company because of the promotion, and as a result, are more likely to make a purchase given any random positive stimulus. Perhaps some product appears on a TV show. Maybe a competitor promoted a product to them, the customer remembers you sell it also, and prefers your store. It doesn't really matter. Fact is fact, and because of your promotion, you extended the customer LifeCycle. You created a situation where people became more likely to purchase from your company in the future.

Not bad for a beginner. In the first 90 days, your promotion created present value - real bottom line, measurable ROI - adding Value to the customer LifeCycle (LifeTime Value). In the 2nd 90 days, your promotion created future value - accelerated repeat purchase rates - by extending the LifeCycle. CFO sings your praises! At last, somebody who can prove they are making more money than they are spending with marketing!

There is an important lesson here: you will never know how much money promotions really make without using control groups.

Note: This is a shortened version of the Drilling Down book. The last 2/3 of the book have been eliminated and the customer profiling software application is not included as it is with the full PDF or hardcopy book. To order the complete book with customer scoring application, visit my page at Booklocker:

<http://www.booklocker.com/jimnovo>

**Chapters Missing from this Version
of the Drilling Down Book:**

The following are descriptions of the remaining chapters in the full PDF and hardcopy editions of the Drilling Down book:

REGENCY METRIC TOOLKIT

Chapter 10 PREDICTIVE MARKETING

Chapter 11 THE AD SPENDING EXAMPLE

Chapter 12 TURNING REGENCY DATA INTO PROFITS

Chapter 13 THE ONLINE RETAIL EXAMPLE

Recency is just a bit more complex than Latency, because it involves ranking customers against each other versus creating a simple "trip wire" for all of your customers. The Recency approach creates a more finely tuned model, allowing you to segment and target customers with more accuracy and drive profits even higher than you can with Latency.

The Recency Toolkit builds on your knowledge of Latency and shows you how in some cases, using Latency and Recency together generates the highest increase in profits.

Recency is particularly effective in maximizing the margins of promotional programs, often making it the preferred model for retail oriented businesses, ad-supported web sites, and other businesses lacking "built-in reasons" for repeated customer activity over time.

RFM SCORING TOOLKIT

CHAPTER 14 - PREDICTIVE MARKETING

CHAPTER 15 - A TWEAK FOR INTERACTIVE CUSTOMERS

CHAPTER 16 - NO CUSTOMER DATABASE? HOW TO SET UP A SPREADSHEET TO SCORE CUSTOMERS

CHAPTER 17 - HOW TO SCORE YOUR CUSTOMERS

CHAPTER 18 - THE COMMERCE AND CONTENT EXAMPLES: TURNING SCORING DATA INTO PROFITS

CHAPTER 19 – CASE STUDY: NON-PROFIT SCORES 192% INCREASE IN ROI USING RFM MODEL

Predictive marketing is proactive, meaning you predict the likelihood of future events based on customer models, where each customer is given a "score." These scores rank customers against each other for likelihood to respond, to defect from your business, to become a high value customer, and so forth.

Don't get nervous about the word "model"; it's not some kind of black box thing you can't understand. If you can use a spreadsheet (or write some simple code), you can create these customer scores using a model called RFM.

Why are scores important? Three reasons:

RFM Scores tell you which customers are drifting away, getting ready to leave you, and determine whether it will be profitable for you to act to try and keep the customer

RFM Scores tell you what best customers like and don't like

RFM Scores tell you how to make more money by allocating resources where you will drive the most profitable activity

More Details On RFM:

<http://www.jimnovo.com/RFM-tour.htm>

ADVANCED DATA-DRIVEN MARKETING TOOLKIT

In Chapter 18, you learn how to use customer scores in the "snapshot" mode of traditional RF(M) scoring to dramatically boost response rates and compare the value of customer groups. But that approach just barely scratches the surface. Now that you have the scores, you can use them to drive very High ROI Customer Marketing Programs and Business Process Redesigns.

To generate maximum ROI, you don't just want to react to customer behavior; you want to predict it. You can even predict campaign ROI before a campaign is executed!

CHAPTER 20 USING CUSTOMER CHARACTERISTICS AND MULTIPLE SCORES

Now we go into "advanced snapshot mode". Customers can have scores for different behaviors (purchases and page views, for example) and using these scores in combination improves the predictability and profitability of campaigns. Additionally, you find out how to add other information you have (from surveys, for example) to start understanding which types of customers have high future value. You can profile customers for likelihood to respond and relative future value by any characteristic in your database - purchase categories, favorite pets, which magazines they read, ad source, anything - and determine the types of customers that are most profitable to you. Then you can reallocate your budgets and go get more like them!

CHAPTER 21 CUSTOMER LIFECYCLES: TRACKING SCORES OVER TIME

Picking up after the powerful "static" or snapshot future customer value profiling of RF(M) scoring, this chapter moves into the even more powerful "dynamic" customer scoring – the "snapshot" turns into a "movie". Customers change over time and so does their future value. By tracking customer LifeCycles, marketers can predict the "trigger points" in the customer relationship where the very highest ROI marketing takes place — customer anti-defection campaigns. If you can predict the defection, you take action before it takes place, and get a much higher response than in win-back campaigns, where the customer has already defected. You can react to the defection with win-back, or predict the defection by tracking customer LifeCycles – your choice.

CHAPTER 22 CUSTOMER SCORING GRIDS: HIGH PERFORMANCE LIFECYCLE-BASED TRACKING

Not good enough for you? How about combining the Hurdle Rate techniques from the first section of the book with tracking the customer LifeCycle – the "advanced movie" mode? The result is Customer Scoring Grids, a visual map of customer retention and defection you can use as the "master plan" for managing your entire customer marketing efforts. Spot high ROI customer groups coming up the value chain, and plan ahead for multi-step defection campaigns with accurate counts of customers in the various stages of defection. This tool was invented by Jim and has been used to manage the retention effort against massive multi-million customer databases. You have to know where customers

are and where they're headed in the LifeCycle to make 200% and 300% ROI's in customer marketing. The Customer Scoring Grid is your master battle plan.

CHAPTER 23 STRAIGHT TALK ON LIFETIME VALUE

The promised land of LifeTime Value. If you could only tell what a customer was worth in the future, you would know how much you could spend on them and still make a profit. But how do you know what a LifeTime is? That's easy – you already figured out the LifeCycle, remember? You can now predict when a customer will defect, and if you know that, you know the LifeCycle (and Lifetime Value) are coming to an end. But the concept of LifeTime value is more than the LifeCycle, and in this chapter you will learn the ins and outs of calculating it, along with suggestions for integrating the concept into the rest of the corporate framework (if you have one, that is).

CHAPTER 24 LTV, I'D LIKE TO INTRODUCE YOU TO THE CFO

When profits, security prices, compensation, and budgeting are all tied to the income statement and balance sheet, then how would you expect a firm to embrace the idea of a customer Lifetime? Where is the incentive? What value will implementing the use of Lifetime Value measurement bring to the firm? If you don't have a way to reconcile the notion of LTV with the internal financial yardsticks of the firm, it is not likely you will find a lot of support for managing based on customer value measurements. Who would care?

This chapter provides specific direction on talking with financial types about LifeTime and value and provides examples of reconciling LTV with financial reporting, including how to take a typical quarterly report and recast it in terms of the LifeTime Value approach.

CHAPTER 25 FELLOW DRILLERS AT WORK: READER QUESTIONS ANSWERED

Definitions and Background Information
Customer Loyalty and Retention
Customer Segmentation and LifeTime Value
Professional Services
Ad-Supported Content / Subscription Models
Online / Offline Retailing and Catalogs
Distribution / Operations / Channel Management

The ROI of Online Branding Efforts

Jim invites owners of the book to e-mail specific questions on using the customer models and techniques in Drilling Down. These questions have been organized into the functional categories above, and cover a wide range of industries such as publishing, facilities management, hospitality, education, call centers, professional services, manufacturing, telecommunications, retail, travel, banking & finance, enterprise software, automobiles, conference management, casino, and utilities.

PREDICTING CAMPAIGN ROI

CHAPTER 26 PREDICTING CAMPAIGN ROI: SET UP

This chapter picks up after LifeCycles and Lifetime Value, demonstrating step by step how to set up the controlled test needed to determine the financial value of an RF score. After this test, you will be able to predict the profitability of a promotion before you even send it out! Includes instructions detailing the creation of control groups and random sampling methods.

CHAPTER 27 PREDICTING CAMPAIGN ROI: THE MODEL

In this chapter, you learn how to create ROI models with RF Scores, and learn one of the most important fundamental concepts in the Drilling Down method – how to control the issue of top-line sales versus bottom-line profits in a promotion. In an RF scored promotion, you can literally choose to maximum top-line sales at a reduced profit, or drive maximum bottom line profit in exchange for lower top-line sales – or any mix in between. The financial models show you how.

CHAPTER 28 PREDICTING CAMPAIGN ROI: FINE TUNING

Flexibility is the name of the game in the Drilling Down Method, and this chapter introduces modifications to the basic financial model from Chapter 13, allowing further financial flexibility in targeting customers by RF scores. See an impossible, money loser of a campaign turn into a winner right before your eyes using RF scores and the advanced ROI model.

**CHAPTER 29 COSTS YOU DON'T KNOW ABOUT:
MEASURING TRUE ROI IN BEST CUSTOMER PROMOTIONS**

Bet you think high response rates are always good, right? Wrong! Not when you are spending money to promote to customers who would have bought anyway without a promotion. These not needed (and not wanted) expenses are called subsidy costs, and when you plan promotions correctly using RF scores, you can eliminate most of them, creating much higher ROI campaigns. This chapter talks about where subsidy costs come from, how to measure them, and how to get rid of them in your promotions. Learn how to measure the profits generated by customers who don't use your campaign tracking device, and the profitability of customer campaigns with no response tracking device at all - a "must have" for service-oriented initiatives like thank you programs and VIP benefits.

**CHAPTER 30 SOME FINAL THOUGHTS: SEASONALITY, CRM,
BEHAVIORAL INERTIA, DATA-DRIVEN PROGRAM OUTLINES**

This section also contains additional information applicable in special situations such as seasonal effects on modeling, tweaking your timing on campaigns, and modeling for rules-based CRM. Also provided is an overview of and comparison between the different mainstream data-driven marketing program approaches - Database Marketing, Frequency Marketing, Relationship Marketing, Loyalty Marketing, Permission Marketing, and One-to-One Marketing.

To order the complete book with customer scoring application, visit my page at Booklocker:

<http://www.booklocker.com/p/books/224.html?s=PDF>