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Development of the Customer Marketing™ Method: an application of Analytical CRM

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Abstract

Analytical CRM involves acquiring and updating knowledge about customer needs, motivation and behaviour and requires a structured method to be implemented in a multidimensional database. The presentation describes The Customer Marketing™ Method - CM in short - and the CM application within the Customer Focus Suite of SPSS Showcase - CFS in short -, in the analytical CRM environment. CM, originated by Jay Curry[1] and others and implemented by Sergio Meacci[1] and others (see references), covers all topics of the marketing and sales process: customer focus and its impact on company profile, understanding customer expectations and requirements, measuring and monitoring customer performance. CM measures customer satisfaction and loyalty and customer performance within a defined process of marketing techniques for customer value segmentation and definition of marketing actions/plans for existing vs new customers through an appropriate mix of acquisition and retention cycles.

Customer behaviour is measured using pyramids - historical, actual and planned – and the related migration matrixes that monitor the movement of the customers among the value categories. The 10 steps approach to measure Customer Value within the CFS of SPSS will be described by choosing value measurement metric and sorting customer list; by defining customer categories and boundaries; by managing potential revenue growth and by defining the appropriate marketing actions/plans, allocating marketing expenses and resources and measuring the related actual performance vs the expected ones.

1 Customer Marketing Method-CM

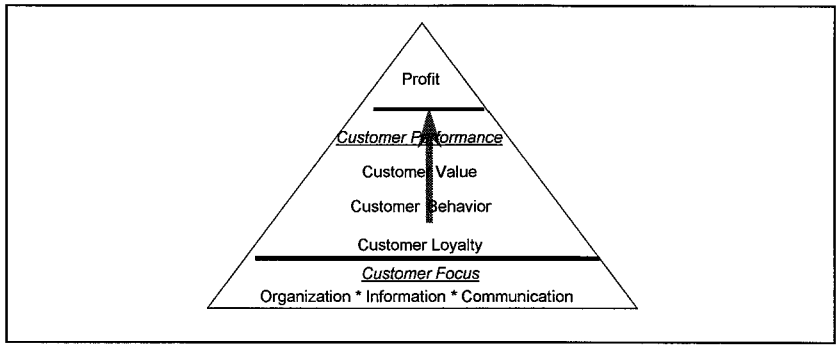
The organisation has to be structured around the customer, communicate efficiently and effectively with its customers and prospects. That's why the process starts from the enhancement of the customer focus areas, then improving

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the customer performance-value, behaviour and loyalty–and company profitability.

The solution offered enables to measure performance and profitability and to manage the action plans that are aimed to reach the improvement goals, providing the appropriate metrics to be measured and monitored.

Table 1 The simple promise of customer marketing



A key tool of the CM is the Customer Pyramid. The pyramid is created by using series of business rules to segment customers into active versus inactive customers and within the active segment, between value categories such as top, big, medium and small. Segmenting active from inactive customers, involves selecting a timeframe during which a customer is expected to make a purchase. For example, some businesses might expect customers to make weekly or monthly purchases, whereas other businesses might expect a customer to make at least one purchase each year to be considered an active customer. Within the active customer group, customers are further segmented into value categories.

This involves 2 steps:

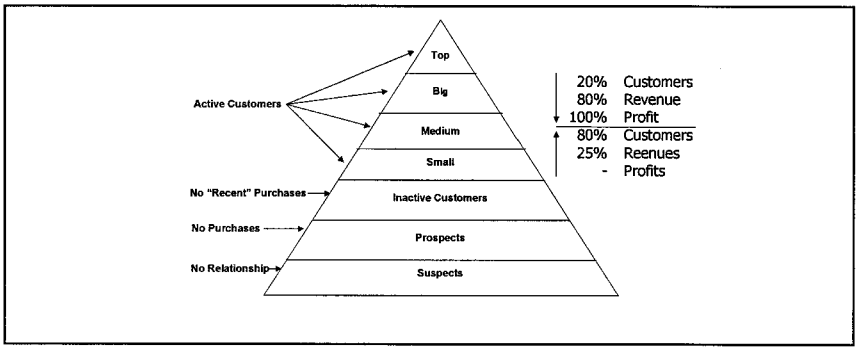
First, a customer valuation method must be selected; this should be a measurable customer behaviour metric that the company can influence. For example, airlines might select the # of miles flown or a hotel chain might select the # of stays at their properties. But for many organisations, the amount of money spent by the customer on its products and services, (revenue), is the most meaningful customer value measure.

Once the customer value metric has been selected and the active customers have been sorted from the highest to the lowest value, then the boundaries must be defined that will segment customers into the various categories. Establishing these boundaries is critical to being able to measure meaningful customer behaviour movements. The creation of the top, big, medium and small value categories and the tracking of the movement of customers up and down within these categories is what begins to provide meaningful customer behaviour metrics.

In this presentation revenue will be used to measure customer value.

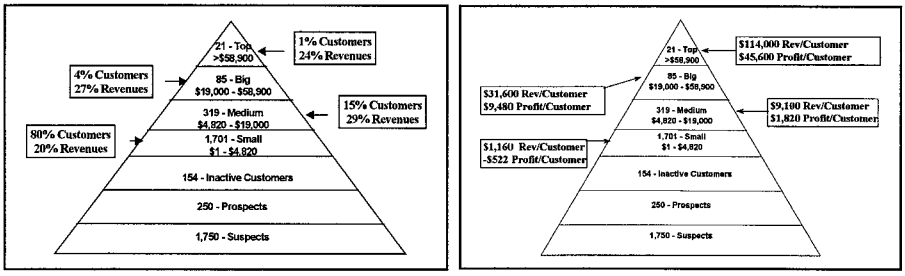
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Table 2 Using the customer pyramid for value segmentation



Once the customer pyramid is created, it easily appears that not all customers are the same. Some are much more valuable then others. In fact, in the example in table 2, the 80-20 rule applies; 20% of the customers are generating 80% of the revenues.

Table 3 What % of the customers deliver what % of revenues? and what % of the profits?



Once all marketing, selling and other company expenses are allocated to each customer within each value category, some customers appear much more profitable then others and much easier and less costly to sell more to existing customers then acquiring new ones. When the business matures, it becomes imperative for profit maximization to ensure that the revenue mix from existing versus new customers makes sense, because more attention (and money) is often spent on non-customers. Many mature companies find that although existing customers may be generating 80% or more of their revenues that a disproportionate amount of money and attention is being focused on non-customers.

Given the percentage of revenues expected from the existing customers, it is important to measure the result of the allocation of the limited marketing and sales resources between cross and up selling existing customers versus new customer acquisition efforts.

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As in any business, there are only 2 ways to increase profits: reduce expenses, or increase revenues. The starting point to increasing revenues is to isolate small and medium customers that have a high growth potential. In B2B business these are typically large companies that are currently doing only a small amount of business with us. In fact they may be potential top customer in competitor's planned pyramid. Once isolated, these are the accounts that require to focus the energies on. The system has to provide the % small and medium customers candidates for moving up.

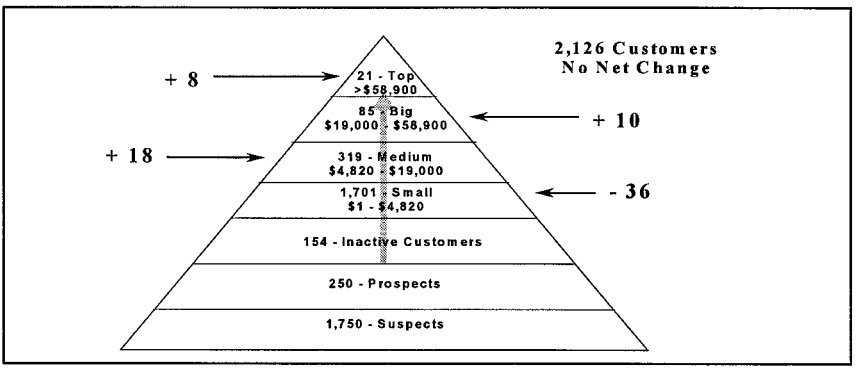
Of course ultimately it is necessary to find out what customers think about the company they behave. Customer behaviour can be measured over any meaningful timeframe by examining their migration from one customer value category to another.

CM supports a rich assortment of customer performance metrics and it will make CRM understandable to everyone in the company, from the mailroom to the boardroom. It is a clearly defined CRM process, tested, validated and proven in the real world because it focuses on--and achieves--results that speak to management: operational profit and ROI. It uses a "Customer Team" approach that involves and empowers all employees with customer contact. Definitely it equips middle managers to handle CRM implementation issues, with a special emphasis on "change management".

The CM Migration Matrix, the core tool of the CM, monitors the movement of the customers among the value categories.

Even a small upward migration of customer value can make a big difference to the bottom line.

Table 4 The Bottom Line – a small net upwards migration can deliver a big improvement in profits



In this example, there was no net change in the total number of customers. But a plan was put in place to migrate some small customers up and to replace others with new more valuable accounts. At the end of the year, the company ended up with 36 fewer small customers, 18 more medium, 10 more big and 8 more top. Revenue was increased by more then a $1 million dollars and bottom line profits increased by more then $500,000.

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2 SPSS Showcase Customer Focus Suite

The ten steps of CM within the CFS, are now described (see references Jim Berkowitz[5], SPSS, 2001).

The first step is to choose a value measurement (like revenue) and to use the Customer Focus Suite (CFS) to sort the customers list from the highest to the lowest value.

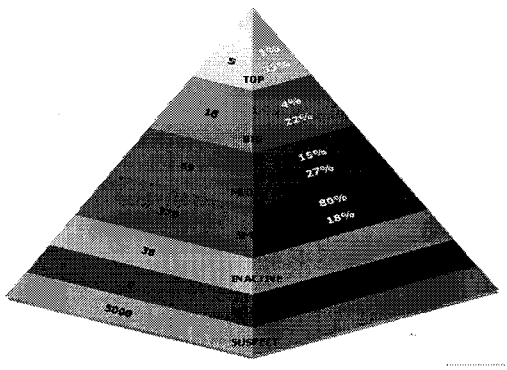
The second step is to use CFS to set the customer value category boundaries that will define how many and which specific customers will fall into each category.

As part of this process, CFS will automatically assign a value category (top, big, medium, small, inactive, etc.) to each customer for each period that a pyramid is created (Weekly, Monthly, Quarterly or Annually).

Table 5 Measure customer value: Step 1, 2 and 3

Step #1 - Choose your value measurement metric & sort your customer list

Step #2 - Define your Customer Value Categories



Step # 3 - Review the reasonableness of the value categories & rank boundaries

	# Total	% of Pyramid	Revenue	Rev Per Customer	Rev % of All	Average Sale
All Ranks	118	100%	$2,654,978	$22,500	100%	$11,696
Top	3	3%	$1,158,671	$386,224	44%	$50,377
Big	7	8%	$932,557	$133,222	35%	$19,032
Medium	22	24%	$375,287	$17,059	14%	$5,686
Small	61	66%	$188,463	$3,090	7%	$2,118

	Top	Big	Medium	Small
Rank Boundaries	$313,500	$50,506	$8,356	$1

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In this example, 7 customers representing 8% of all customers fall into the big category. The average sale to a big customer was approximately $133,000 and the revenue generated from big customers represented 35% of all company revenues. Finally, in order to become big customer $50,506 of revenue needs to be generated from an account and to migrate up from big to top will require a minimum of $313,500 in revenue.

The CFS will automatically maintain most valuable customer analytics by industry, sales region or individual sales executive.

Each sale region and sales executive will have a better understanding of who their most valuable customer are. How often and how much they are buying. How long has it been since their last order. And whether or not they are they are growing in value.

In addition, understanding how customer value is being distributed throughout the company's sales regions and sales organization will allow marketing to more effectively support the company's selling efforts by conducting new customer acquisition versus customer growth campaigns where they are most needed.

Table 6 Customer value insights

Who are your most valuable customers?

	Customer Rank	Revenue	# Transactions	Average Sale	Days Since Txn	Last Year Customer Rank
KAO SPECIALTIES AMERICAS (125116327)	1	$1,437,659	26	$55,295	48	9
MIDLAND STEEL WAREHOUSE CORP (4003596)	2	$1,325,675	22	$60,258	32	3
CHART HOUSE ENTERPRISES INC (200080208)	3	$1,108,272	43	$25,774	88	4
AERO OIL CO (400778510)	4	$976,097	29	$33,659	48	5
FIRST FEDERAL SAVINGS & LOAN (141095414)	5	$867,598	43	$20,177	36	6
JUSTICE GOLF CAR CO (158726182)	6	$820,169	35	$23,433	1	30
MILO PETERSON FORD (148236318)	7	$799,829	32	$24,995	72	24
SWAGELOK VALVES (407681618)	8	$670,509	35	$19,157	64	10

How is value being apportioned among your sales organization?

Success to a B2B company means much more then how many new customers it can acquire. It very much depends on how successfully it can grow its current customer accounts.

In order to determine the potential growth that current customers have, the CFS includes the tools needed to create a "top-down" revenue growth plan by inputting estimated spending by industry and company size and customer share increases. These estimates are used by the system to automatically calculate a revenue growth amount for each and every customer. The example shown here displays an overall upward migration of 9 small customers; 6 to medium and 3 to big and a projected increase in revenue of $3.2 million.

After management has completed its "top-down" revenue plan, this information is passed on to each Rep for review. Based on the Reps review of management's plan and their knowledge of each account, they can input a

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targeted revenue amount for each customer. As a final step, the amount of new customer acquisition revenue that will be needed in order to arrive at the desired plan total can be added to the plan details.

Management can then compare their plan against the plan developed by the sales team and a final consensus plan can be agreed upon and "locked in."

Table 7 Project value for a future time period: Step 4 and 5

Step # 4 – Management projects the potential revenue growth from existing customers....

- **B2Bs can use industry spend & share growth estimates**
- **B2Cs can use up & cross-sell data mining models**

	Plan Total	Actual Total	Actual Var Total	Plan Revenue	Actual Revenue	Actual Var Revenue	Plan Share
All Ranks	113	113	0	$20,845,985	$17,640,714	$3,205,271	72%
Top	9	9	0	$9,639,660	$8,665,678	$973,982	90%
Big	22	19	3	$7,606,626	$5,592,029	$2,014,597	64%
Medium	33	27	6	$2,873,696	$2,608,701	$264,995	69%
Small	40	49	-9	$726,003	$774,306	-$48,303	33%

Projected Value Category Changes

Projected Value Growth

Step # 5 – The Account Executives (Reps) complete a Revenue Goal Plan

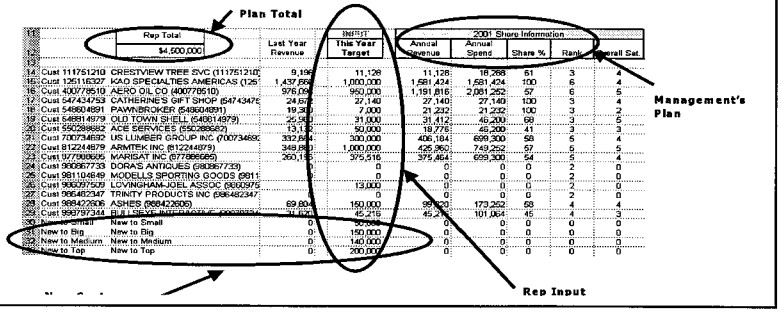
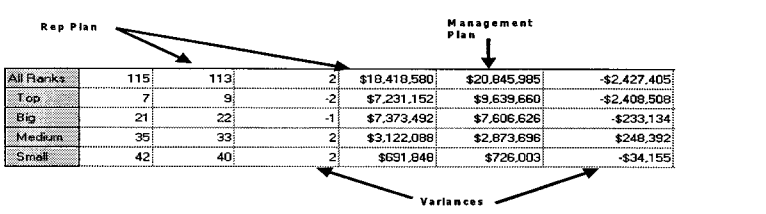


Table 8 Project value for a future time period: Step 6

Step # 6 – The Plans are compared, consensus is reached and the revenue plan is "locked in."



All Ranks	115	113	2	$18,418,580	$20,845,985	-$2,427,405
Top	7	9	-2	$7,231,152	$9,639,660	-$2,408,508
Big	21	22	-1	$7,373,492	$7,606,626	-$233,134
Medium	35	33	2	$3,122,088	$2,873,696	$248,392
Small	42	40	2	$691,848	$726,003	-$34,155

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Once the projected revenue amounts by customer have been derived, the most growable accounts can be measured and monitored by sales Rep and or by industry.

Table 9 Most growable customers insight

	Share	Revenue Growth	Revenue	Last Year Revenue
AERO OIL CO (400778510)	57%	$215,717	$1,191,814	$976,097
MIDLAND STEEL WAREHOUSE CORP (400396)	100%	$145,824	$1,471,499	$1,325,675
KAO SPECIALTIES AMERICAS (125116327)	100%	$143,766	$1,581,425	$1,437,659
O & W GLASS (804091726)	57%	$130,276	$424,352	$294,076
SILVERSTONE INC (980390687)	44%	$129,543	$235,726	$106,183
COMMUNITY NATIONAL BANK (712156595)	55%	$115,592	$401,711	$286,119
MARISAT INC (877988685)	54%	$115,26[illegible]	$375,463	$260,199

Who are your most growable customers?

In addition, using the system's Customer-based Accounting spreadsheet, company expenses are allocated to each customer value category and the overall profitability of each customer is automatically calculated.

Table 10 Customer profitability: Step 7

Step # 7 – Allocate expenses to each Customer Value Category

	Total	Top	Big	Medium	Small	Inactive	Prospects	Check
Others	21						0	21
Customers	997	10	39	149	799			
Revenues	27,302,196	5,214,489	6,879,427	8,217,513	6,990,675			27,302,196
Costs of Product	21,841,685	4,171,591	5,503,542	6,163,136	6,003,416			23,841,685
Margin	5,460,421	1,042,898	1,375,885	2,054,379	987,259			3,460,421
Margin %	20%	20%	20%	25%	14%			13%
General Overheads	1,050,000	21,000	84,000	168,000	651,000	105,000	21,000	1,050,000
General Overheads %	100%	2%	8%	16%	62%	10%	2%	100%
Sales Costs	1,275,000	12,750	51,000	191,250	828,750	63,750	127,500	1,275,000
Sales Costs %	100%	1%	4%	15%	65%	5%	10%	100%
Marketing Costs	1,050,000	10,500	42,000	157,500	682,500	52,500	105,000	1,050,000
Marketing Costs %	100%	1%	4%	15%	65%	5%	10%	100%
M&S Overheads	185,000	1,850	7,400	27,750	120,250	9,250	18,500	185,000
M&S Overheads %	100%	1%	4%	15%	65%	5%	10%	100%
Total M&S Costs	2,510,000	25,100	100,400	376,500	1,631,500	125,500	251,000	2,510,000
Total M&S Costs %	100%	1%	4%	15%	65%	5%	10%	100%

Cost Allocations

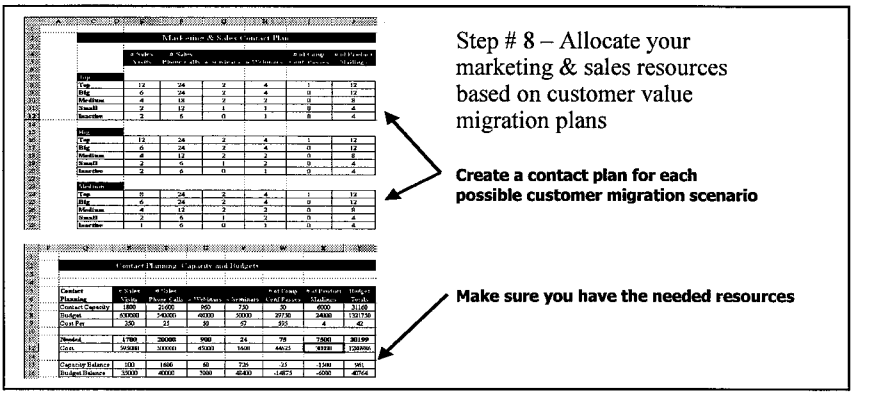
Many companies have found it useful to track interactions with their customers through an Operational CRM database. But knowing the "who" and "when" of customer contact is not nearly as valuable as being able to monitor whether a company's limited resources are being allocated to the "right" customers.

To make sure this happens, the CFS will allow you to design a marketing and sales plan that allocates resources based on the specific migration plan developed for each of your customers. For example, more on-site sales visits may be planned for your most valuable and growable customers, while small customers with minimal projected growth may receive only phone contacts or direct-mailings.

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Using the CFS's Contact Planning functionality resource capacities can be determined, plans can be designed for each possible migration scenario and every active customer can be assigned a contact plan that supports their migration plan.

Table 11 Contact planning: Step 8

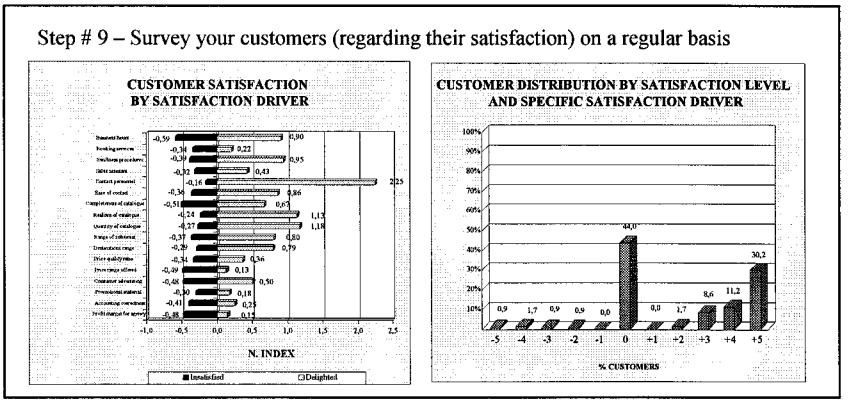


Is there a relationship between customer behaviour and customer satisfaction? Most executives would intuitively say yes. The CFS will provide the analytics necessary to understand exactly how these two key customer performance metric areas relate.

Measuring and monitoring customer satisfaction must be at the core of any initiatives designed to retain and grow customers. The CFS can capture customer satisfaction ratings throughout the year and satisfaction can be monitored by sales region, sales rep and industry.

Customer satisfaction initiatives with customer-specific programs enhance the efforts that will maximise customer loyalty and growth.

Table 12 Customer satisfaction survey: Step 9



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The CFS delivers the tools missing from virtually every other Analytic CRM solution available today: tools for measuring and monitoring customer behaviour.

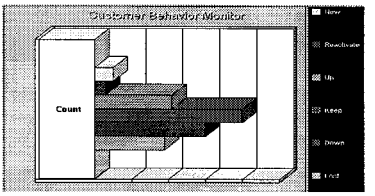
Whereas the focus of the customer pyramid lies in understanding potential and actual customer value at various points in time, the customer behaviour monitor focuses on understanding and comparing anticipated versus actual customer migration "up" or "down" within your value categories over time.

Table 13 Customer behaviour: Step 10

Step # 10 – Monitor the performance of your customers

	Count	Revenue Value
Total New	8	$4,388
New	5	$1,521
Reactivate	3	$2,867
Total Retained	91	-$468,302
Up	21	$283,173
Keep	40	$451,851
Down	30	-$1,203,326
Total Lost	19	-$1,293,301
Migration Summary	118	-$1,755,214

From Period to Period
track your actual customer performance versus your plans



And the customer migration matrix provides a detailed understanding of how customers behaviour is effecting company revenues.

Table 14 Customer migration

Prior Period Actual: 2000 Actual — 2000 Actual vs. 1999 Actual

Customer-based Business Planning: "What if?" Scenarios

Customer Pyramid	*# Customers*	*Ave. Rev $s*	*Top*	*Big*	*Medium*	*Small*	*Inactive*	*Prospects*
Top	9	962,853	7	2	0	0	0	
Big	19	294,317	1	16	2	0	0	
Medium	27	96,619	2	3	18	4	2	
Small	49	15,802	1	2	5	41	0	
Inactive	9	0	0	0	3	4	2	
Prospects	5	0	0	0	0	0		5
Last Year Active Customers	*104*		11	23	28	49		
Last Year Other	*14*						4	5

Plan Results

	Total	Top	Big	Medium	Small
Revenue Projection	20,840,308	10,591,384	6,769,298	2,703,320	774,306
Change - Absolute					
Difference/Customers	7	1	4	1	0
Difference Revenue	3,199,594	1,925,706	1,177,269	96,619	0
Difference Revenue on Share	3,612,251	2,142,147	1,383,023	87,082	0
Change - %					
Difference/Customers	7%	22%	21%	4%	0%

From Period to Period you'll be able to monitor customer value migration & its effect on revenue

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