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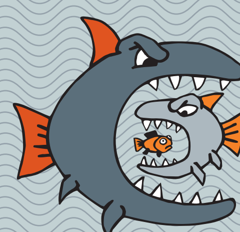
# GfK Marketing Intelligence Review



GfK Association

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*Vol. 2, No. 1, May 2010*

# EDITORIAL

Precisely when the most severe and longest economic crisis of the postwar era will end is not yet foreseeable at this stage. However, what we can say with certainty is that marketing and its marketing intelligence systems will emerge from it differently.

One of the initial major changes is the result of the ethical disappointment experienced by many citizens and consumers in previous years. Confidence in the financial sector is at an all-time low. Excessive bonuses discredit the whole class of managers as greedy egotists. The growing polarization of society encourages envy and resentment, and the slow response to climate change issues by most companies now favors those who have chosen not to stonewall the subject and are committed to an offensive approach. In consequence of this, fairness and social considerations are becoming increasingly important decision-making criteria in marketing.

Our third issue of GfK Marketing Intelligence Review (MIR) examines this problem area in the article by Ty Henderson and Neeraj Arora (''Doing well while doing good. Linking a social cause to product promotions: Why it Works and How to Make it More Effective'').

In three experiments, the authors document that linking promotions to social matters can be very effective. They demonstrate in a very practice-oriented way, that ''embedded promotions'' outbalance classic forms of price promotions.

A second change results from the raised level of cost consciousness caused by the crisis and places a stronger focus on customers with higher value. To a growing degree, this is displacing what we Germans call ''the watering-can principle,'' whereby an even-handed approach is adopted towards all customers. Christian Homburg, Dirk Totzek, and Mathias Droll (''All customers are equal, but some are more equal. Should Firms Prioritize Their Customers?'') verify if prioritizing some customers actually offsets the risks and drawbacks of such an approach. In a comprehensive study, they confirm that such a strategy is more effective if implemented well and highlight six key levers for implementation. Some of these are closely related to Marketing Intelligence, such as the ability to assess customer profitability, to collect and interpret customer information and to align customer-specific processes.

The study by Thorsten Wiesel, Bernd Skiera and Julian Villanueva (''My customers are better than yours! On Reporting Customer Equity'') follows up on this topic. The authors present a new reporting system for the present and future customer value and demonstrate its application within an internet company. The system not only helps in strategic questions and sales control but also in documenting marketing success according to financial standards. In this way, the system can contribute to improving the image of marketing at the highest level and to revealing the importance of strategic customer management to shareholders. It is also possible that it can help to overcome the traditional short term perspective of financial analyses in favor of reporting directed at longer term market success.

The rapid development of online technology in the past two years has caused a reorientation in corporate communications. Many companies have broken new ground to accommodate the new media behavior of consumers and to communicate more cost-efficiently.

Word of mouth is one of the most interesting tools within the new range of options. In their study, Michael Trusov, Randolph E. Bucklin and Koen Pauwels (''Do you want to be my ''friend''? Monetary Value of Word-of-Mouth Marketing in Online Communities'') investigate if and to what extent new customer contacts initiated by customers are more efficient in expanding the customer base than traditional promotions. They track the direct effects as well as the indirect impact on customer value arising from expected follow-up recommendations of new customers and their specific life cycle. Indeed, word of mouth proved to be superior to traditional campaigns in this case. The study is also insightful from a methodological point of view. It shows the thoughtful planning involved for demonstrating the effects of marketing campaigns.

Accountability is also crucial for the standing of marketing departments within organizations. Peter C. Verhoef and Peter S.H. Leeflang show this effect in a series of studies conducted in the Netherlands (''Getting marketing back into the boardroom: The Influence of the Marketing Department in Companies Today''). Other important elements are innovativeness and the ability to connect well with customers. Further, the study reveals some interesting descriptive reports on the status of marketing. Compared to 1999, the influence of marketing has risen in the sphere of advertising or customer management, but declined in product development, strategy formation, decisions on expansion into new markets or the selection of business partners. The loss of impact of the marketing department is particularly high in terms of pricing and distribution, both of which are increasingly dominated by sales departments. Generally speaking, marketing is considered to be of moderate influence only. However, marketing mangers themselves tend to overestimate their impact, compared to how their influence is assessed by managers of other functions.

Such misperceptions are not only dangerous for the managers themselves, but also for their companies. Consequently, Marketing Intelligence has to ensure that managers really do ask the right questions, adopt the perspectives which are relevant for corporate policy and provide meaningful answers for central managerial questions during and in the wake of the economic crisis.

I am confident that the articles in our present issue will be helpful in this respect. Beyond this, the studies prove that the contribution made by marketing science helps to answer important and prevailing questions associated with marketing policy.

I hope all our readers come to the same conclusion after reading this journal. Relevance is the most important selection criterion for our articles. In an ongoing process, we screen a huge number of academic marketing publications. Out of 100 articles scrutinized, only 10 are short-listed and only 3 make it into our publication. Please judge for yourself, if the effort is worth it: we certainly think so!

Nuremberg, March 2010

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*Editor-in-Chief*

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# EDITORIAL BOARD

{ New Insights }

# Doing well while doing good
# LINKING A SOCIAL CAUSE TO PRODUCT PROMOTIONS: WHY IT WORKS AND HOW TO MAKE IT MORE EFFECTIVE

*Ty Henderson and Neeraj Arora*

An increasing number of brands in the marketplace are being linked to social causes. Such enhancements are called embedded premiums (EP) and can be quite effective as a sales promotion strategy. Across three experiments, using a nationwide internet panel, we find that (i) at low denominations EP is more effective than an equivalent price discount, (ii) EP benefits an unknown brand more than a known brand, (iii) an identifiable segment of individuals prefer the "other" over "self," suggesting possible EP optimization and segmentation strategies, (iv) a customization strategy is shown to be more effective than a coverage strategy. These findings have broad implications for brand managers in regard to resource allocation and EP program ROI.

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This completely revised article is based on: *Neeraj Arora and Ty Henderson (2007):* "Embedded Premium Promotion: Why it Works and How to Make it More Effective," Marketing Science, Vol. 26, Number 4, pp. 514 – 531.

**Social Causes as a New Promotion Strategy for Consumer Goods**

An increasing number of brands in the marketplace are being linked to social causes. Consumer packaged good brands such as Yoplait and Cheerios, retailers such as Target, and service firms such as Working Assets have associations with a variety of social causes such as children's education (http://www.boxtops4education.com, http://www.target.com/tcoe) and breast cancer research (http://www.yoplait.com/slsl). While such examples of "doing well while doing good" are increasingly common, the effect of such associations on consumer choice behavior is not well understood. We refer to them as embedded premiums (EP) and define the term as an enhancement that involves a social cause added on to a product or service. In the Cheerios example above, Box Tops for Education is the enhancement we call the embedded premium. For Yoplait, EP is the association with the Susan G. Komen Breast Cancer Foundation.

While most managers may believe the idea of associating a cause with a brand to be sound business practice, we do not quite know why they work, how individuals differentially react to their presence, how effective they are relative to regular price promotions, and how they can be optimized. Like traditional forms of promotion, an EP provides an additional incentive to consumers, yet it remains unclear how this new form of sales promotion compares with existing price promotion strategies such as rebates and coupons that reward the consumer (self), and not the cause (other). This fundamental tension between concern for the "self" and the "other" is at the core of EP effectiveness. Careful understanding of such self-other tradeoffs that consumers make is important to brand managers because of their implications for brand building, return on investment and long term sustainability of any EP program. In an era of increasing marketing accountability, EP promotions must be a legitimate tactical weapon in the brand manager's strategic promotion arsenal rather than a "feel good" gimmick.

### Are Social Causes Really Effective?

There are five important business questions as they relate to an EP program. These include:

1) Does EP enhance market share? And if yes, what motivates consumers to choose products with an embedded premium?
2) How sensitive are consumers to EP promotion depth?
3) Which is more effective: an EP or an equivalent price promotion?
4) Do well known brands benefit more from an EP association when contrasted with relatively unknown brands?
5) How big is the market segment that cares more about "the other" than "the self" and can this group be targeted?
6) Are there EP program strategies that can enhance effectiveness?

To answer these questions the authors employed three experiments using over 2,100 web panelists spread all over the U.S. The experiments involve two separate contexts — bottled water and credit cards.

### Key Findings

Here is an executive summary of our key findings: Across studies EP is a unique and effective form of promotion whose effect is heterogeneous across people. Interpersonal differences in EP attractiveness vary by cause affinity and personal attributions, and EP sensitivity is invariant to promotion depth (e.g. 15¢ vs. 30¢ vs. 45¢). At small denominations we find that an EP is more effective than traditional forms of promotion such as a discount or a rebate. Interesting differences emerge when EP effectiveness is compared between unknown and known brands — we find a stronger effect for an unknown brand with an EP than for a known brand, as positive EP associations enhance quality perceptions for the unknown brand. We demonstrate that EP effectiveness could be improved via a customization strategy where consumers are allowed to select their preferred cause, but find evidence against a coverage strategy — bundled EP's have a dilution effect. The self-other gap, a measure of concern for oneself versus a social cause, is heterogeneous across respondents, with almost 20% of individuals exhibiting "selfless" preferences. We find that the self-other gap is related to a variety of behavioral, attitudinal and demographic markers, suggesting the feasibility of segmenting the marketplace based on EP effectiveness.

### Getting into the Minds of the Buyer

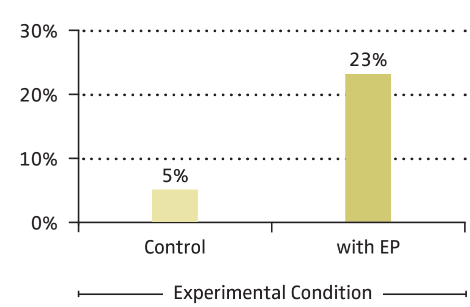
In a first study 131 participants completed an on-line bottled water product evaluation experiment.

The key independent variable in the study was the presence or absence of EP — a donation to the American Red Cross. There were three treatment conditions, which varied only by the amount of the promised donation to the Red Cross: 15¢, 30¢ and 45¢. We also included a control condition, resulting in a total of four conditions. Individuals assigned to the control group were provided product descriptions for three brands of bottled water (two known brands Evian and Dasani, and a fictitious brand Amphora). Individuals in the treatment conditions viewed the same product descriptions for the same three brands with the exception that Amphora, the unknown brand, featured an EP as shown in Figure 1.

### Does EP Work and How?

The answer in our experimental setting is an unequivocal yes. In the control condition Amphora received only 5% choice share, but when Amphora promised a donation to the Red Cross in the treatment condition, choice share jumped to 23% ($p < .05$).

FIGURE 2:
Choice Share
All brands priced at $1.25




Interestingly, quality perceptions for the Amphora brand are significantly higher when the brand has an EP association (3.14 vs. 3.69, $p < .05$). We also find that the EP effect does not vary by depth: the effects in the three 15¢, 30¢ or 45¢ treatment conditions are identical. The mere presence of an EP, rather than its magnitude,

*Figure 1:*
EXPERIMENTAL SETTING


DASANI
(well-known)

- Purified water enhanced with minerals for a pure, fresh taste
- Confidently cool, vitally refreshing, abundantly available, and invigoratingly blue
- ***Enjoy it at home, at the gym, and in between***

AMPHORA
(ficticious)

- Natural spring water with a unique range of nuances and tastes
- Pristine, naturally healthy, purely spontaneous, and refreshingly clean
- ***15¢ of each purchase donated to the American Red Cross***

EVIAN
(well-known)

- Untouched by man, bottled right at the source
- Perfectly pure, unsurpassed quality, a water of distinction you can trust
- ***Unlock your potential, refresh yourself, water is vital for life***

appears to be sufficient to impact consumer choice. The depth invariant effect of an EP is good news for a brand manager because of its ROI implications.

» The mere presence of an EP, rather than its magnitude, appears to be sufficient to impact customer choice. «

**What Motivates Buyers to Engage with EP Products?**

Using open-ended questions, we uncovered five types of individual motivation toward EP, and EP effectiveness is different across these groups (Refer to Table 1).

The variety of motivations toward EP reveals a unique aspect of EP that stands in contrast to traditional forms of price promotion. Contrary to a price cut, which invokes a uniform price-focus among consumers, EP conjures a menu of personal motivations with differential outcomes on effectiveness. In some circumstances, the EP serves as an aid to decision making to tip the scale in favor of the promoted product for an otherwise indifferent consumer. In other cases, it facilitates the accomplishment of interconnected personal strivings, which can include helping the charitable organization.

**Why Should I, the Brand Manager, Care? (Study 2)**

The experimental design in the second study (n = 1,650) had the following factors, each at two levels: Brand (Unknown, Known), Promotion pay-off destination (Self, Other) and Effort (No effort, Some effort). In all there were 2×2×2 treatment conditions and one control group resulting in a total of nine conditions. The basic study design and context was identical to Study 1 and the depth of payback was set at 15¢.

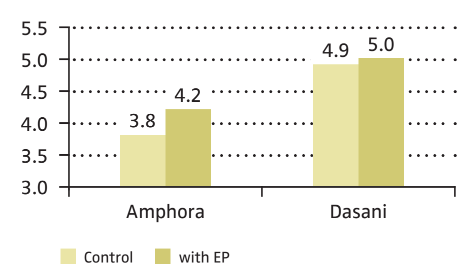
**Juxtaposing Traditional Promotions with EP**

The second experiment shows that promotion pay-off destination matters. A small discount or rebate appears to have lower incremental value to respondents than an equivalent EP. This is somewhat surprising. We believe that at small denominations, such as fifteen cents, the incremental utility associated with a discount or rebate may be quite low. Most price promotions are much deeper than the manipulation used in this study, thus respondents may have a reference depth for price cuts that must be met for the promotion to have an effect. However, the moral satisfaction "purchased" with the EP may be high because the incremental utility is linked to the warm glow of contributing and not to the amount of the contribution per se.

**Known versus Unknown Brand EP Effectiveness:**

Unknown brand benefits more from an EP association than a known brand. Across all measures, the effect size and percent gain because of an EP is higher for the unknown brand than the known brand. Although the known brand does benefit from an EP association, what is different is that the EP association also enhances the unknown brand's quality perceptions, while the EP association has no effect on known brand quality perceptions (See Figure 3).

FIGURE 3:
Quality Perceptions




This may be occurring because respondents are likely to have strong prior beliefs about the perceived quality of an existing brand. An unknown brand, on the other hand, is like a clean slate and any positive "tag" that gets attached to an individual's otherwise neutral brand schema is therefore likely to enhance perceived quality. In general, the cause association may be playing the important role of legitimizing an otherwise obscure brand, resulting in higher overall gains for an unknown brand relative to a known brand.

**TABLE 1:**
Individual EP Motivations

| MOTIVATION | PERCENT OF SAMPLE | EXEMPLAR | CHOICE SHARE |
|---|---|---|---|
| Feel Good | 11% | It would make me feel good about myself. | 22% |
| Product Assurance | 9% | I might be indifferent on which brand I choose, but if I know that my choice could help a charitable organization it would make up my mind for me. | 43% * |
| Facilitation | 37% | Because I would be receiving what I needed while simultaneously helping those less fortunate. | 21% |
| Help Others | 29% | Because it would benefit a worthy cause. | 30% * |
| Activism | 13% | Because my money is going to other places than just the big wigs pockets. | 20% |
| Control Group | | | 5% |

* The difference between motivation group and control is significant ($p < .05$)

### EP, Brand Loyalty and Price Sensitivity:

Gains because of EP are highest among respondents with low loyalty to Dasani. EP effectiveness therefore appears to be tied to the presence and the size of the ''non-loyal'' group. For a known brand if such a group exists, and is substantial in size, EP effectiveness is likely to be higher. This finding is consistent with the empirical generalization that the majority of gains from a sales promotion come from brand switching. Importantly, there is evidence for a link between EP and price sensitivity. The data suggests that presence of an EP makes respondents less price sensitive and more willing to choose the brand when it is premium priced. This is an interesting finding because it points to the distinction between EP and traditional price promotions. Whereas price promotions are known to make individuals more price sensitive, EP has the opposite effect.

### Building a Better EP Mousetrap (Study 3)

Because cause affinity is well known to be a driver of EP effectiveness, two alternative strategies to enhance the EP effect were considered: coverage and customization.
Coverage: Unlike price promotion where the underlying discriminator across consumers is price sensitivity, a unique aspect of an EP is that it could potentially contain multiple social causes. We refer to the EP strategy to offer multiple social causes as coverage. Consider, for example, two causes C1 and C2 where each may be attractive to different individuals. A coverage strategy suggests that inclusion of both C1 and C2 in an EP promotion offer, compared to the case when either C1 or C2 is included, should result in increased EP effectiveness. More individuals are likely to purchase an alternative that has multiple causes as an EP compared to an alternative that has only one cause as an EP. Working Assets (www.workingassets.com) provides a good example of this.

***Customization:*** Another method to increase EP effectiveness is customization. Because it permits consumers to select into the cause for which they have the highest affinity, and higher affinity is likely to result in an enhanced EP effect, customization is expected to increase EP effectiveness.

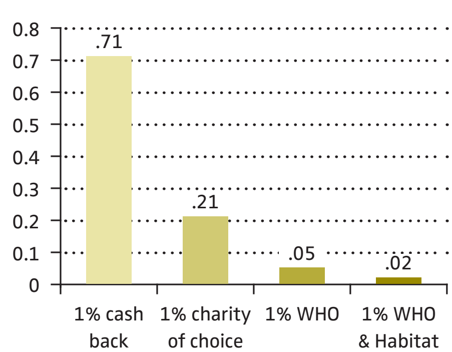
Study 3 uses a different context (credit card) and design than the previous two studies. Respondents were asked to indicate their charity preference for a credit card offer with an EP option. Specifically, they were asked, ''If evaluating a credit card offer with a charitable donation option that lets you decide who receives your money, which one of these five organizations would you choose to support:

American Cancer Society, World Health Organization, Habitat for Humanity, SchoolWise (for local schools), or National Wildlife Federation." They then completed a choice based conjoint task of potential credit card offerings that varied on four attributes: brand, interest rate, payback percentage, and the focal attribute, payback destination. Conjoint analysis is a popular technique among market researchers because it provides a direct measure of consumer preference and relative importance of each product feature included in the study.

In this study, three of the four levels of the payback destination attribute had an EP component. The first level, donation to a single pre-determined charity (the World Health Organization), was included as the baseline EP case. The second level, a joint donation to two fixed charities (the World Health Organization and Habitat for Humanity), was included to test coverage. The third level, a charity of the respondent's choice, was included to test for customization. The fourth level for the payback destination attribute, namely cash-back, was included to compare the differential effect of "self" versus "other" pay-off destination in a tradeoff scenario.

To visualize our results a hypothetical market situation was created where each respondent in our data is assumed to evaluate four credit cards that are identical in every respect (Capital One card, 12.9% APR and 1% payback), except for the payback destination options of cash, WHO, WHO + Habitat for Humanity, or the cause chosen by the individual. The results from the conjoint experiment were used to compute a choice probability for each one of the four available credit card offers. The results are shown below.

FIGURE 4:
Median Choice Probabilities




Not surprisingly, the median choice probability for the credit card with a cash back option is higher than other credit card options with an EP (.71 vs. .21, .05, .02). The median choice probability for the 1% WHO card is higher than 1% WHO + Habitat card (.05 vs. .02) — which is a pattern opposite to the coverage argument. The median choice probability for the 1% WHO card is lower than 1% choose card (.05 vs. .21), which supports the customization argument. These results demonstrate that EP effectiveness could be improved via a customization strategy. There is evidence against a coverage strategy wherein a bundled EP strategy was shown to have a dilution effect.

### Key Findings

> *EP is very effective to increase sales*
> *EP support for unknown brands is stronger*
> *Small denominations work well*
> *Customization enhances effectiveness*
> *20% choose EP over savings for themselves*

The results show that 81% of the respondents prefer the self (i.e. cash back) over the other (i.e. a cause). The remaining 19% of respondents would choose other over self. The self-other gap is higher (meaning an individual wants the cash for themselves) for respondents who have a card that earns cash rewards, charge more money to credit cards, are female, and have a college degree. Individuals also tend to get more "selfish" as payback levels increase. Because the self-other gap is related to a variety of behavioral, attitudinal, and demographic variables it may be possible to segment the marketplace based on EP effectiveness and certain groups of individuals are more likely to be effective targets for an EP program.

### Takeaways

The most basic takeaway from this research is that EP is a promotion strategy that works. Consumers are differentially responsive to its effect based on personal motivations, dispositions, cause affinity, and characteristics of the connected brand. EP can be an effective lever to not only increase sales, but also alter perceptions toward the brand. For brand managers looking for ways to create a point of differentiation for a lesser known brand, embedded premiums present a useful tactical option. Across studies there are two "self" vs. "other" results

» The conclusion is that EP is much more than a promotion strategy, because not only can it sell more products, it can also help the brand, the consumer and society. «


with important substantive implications. First, at low promotional levels an EP is more effective than traditional price promotions. The implication for brand managers is that EP promotions may be cost-effective alternatives to couponing or discounting. Whereas a price cut or coupon must be sufficiently deep to produce a response, a small EP can generate incremental consumer utility because there are significant non-economic drivers of this effect such as an informational component and warm glow. Second, although when framed as a substantively meaningful quantity (percentage of annual credit card charges) in a trade-off setting "self" trumps "other," there are some individuals who would still choose an EP over cash in their pocket. This substantial and demographically measurable market segment is a potentially attractive target for EP-style promotions and focused message strategies.

The conclusion is that EP is much more than a promotion strategy, because not only can it sell more product; but it can also help the brand, the consumer and society. Rather than operating primarily on one dimension, EP invokes a host of associations, both social and personal, that act as levers on consumer choice behavior. This unique win-win-win situation merits ongoing inquiry because of its strategic, public, and behavioral importance. Companies should embrace EP as an opportunity to link public interest to the private performance of the firm, not out of a sense of obligation but, because it is a sophisticated promotional tool at the brand manager's disposal. •

## FURTHER READING

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KEYWORDS:

Cause Related Marketing, Product Promotion, Price Promotion, Embedded Promotion

*{New Strategies}*

# Customer Prioritization


*/// Positive effect on profits compared to equal treatment*

# All customers are equal, but some are more equal
# SHOULD FIRMS PRIORITIZE THEIR CUSTOMERS?

*Christian Homburg, Dirk Totzek and Mathias Droll*

Focusing marketing efforts on the most valuable customers so as to increase company profits is not as straightforward as it seems. There is a downside to customer prioritization such as negative reaction from low priority customers. Taking this into account we still show that prioritizing customers does lead to higher profitability and more return on sales. There are two reasons for this. Firstly, it has a positive effect on the key characteristics of a firm's relationship with its elite customers while not affecting the lower level. Secondly, it reduces sales and marketing costs. Customer prioritization is more effective and efficient than equal treatment. We also show that firms can rely on six key levers relating to a company's organizational structure and processes, enabling proper implementation of customer prioritization.

### Should Some Customers be "More Equal" than Others?

The relevant question for almost all businesses is: should firms clearly set priorities among their customers and treat their best customers preferentially or should they treat all customers fairly equally?

At first sight, managers should try to treat all customers as well as possible. This should lead to the maximum return a firm can expect from its customer base. The major problem here is that firms do not usually have the resources for this. In highly competitive industries many firms compete for the same customers and as a result customers substantially increase their bargaining power, particularly in business-to-business markets. Therefore many firms actually suffer from a decreasing return on investment in customer acquisition and retention activities. Thus, in practice, firms cannot treat all customers as well as they would like to do because they simply cannot afford it.

Against this background, firms have to concentrate their marketing efforts on particular customers, thus creating prioritization. Logically speaking, firms should focus their efforts on their best customers. Customer prioritization implies that selected customers receive clearly different and preferential treatment to others in terms of marketing instruments. Firms should do so as their marketing efforts should become more effective and efficient when concentrating on their best customers. ***Marketing effectiveness*** should increase as the needs of the most important customers are better served consequently leading to more business with them. ***Marketing efficiency*** should also increase as marketing resources are concentrated on key customers.

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This article is an adapted version of: *Homburg, Ch.; Droll, M.; Totzek, D. (2008):* "Customer Prioritization: Does It Pay Off, and How Should It Be Implemented?," Journal of Marketing, 72 (5), pp. 110 – 130, and is published with the permission of the American Marketing Association.

*{Box 1}*

## THE RESEARCH APPROACH

We conducted a large-scale survey study. We sent out questionnaires to about 2,000 companies of different sizes and from industries in both business-to-consumer and business-to-business markets. The questionnaires included measures of the variables highlighted in Figure 1 and Figure 3, assessed on commonly used rating-scales (for example, the customer prioritization checklist as shown in Table 1).

We made follow-up telephone calls four weeks after sending out the questionnaires. As a result, we finally obtained responses from 310 business units or firms (if no specialization in different business units existed). The industries represented the most in our final sample are: financial services (16%), utilities (13%), pharmaceuticals (11%), machinery (11%), transport (10%), IT/telecommunications (10%) and chemicals (8%). The vast majority of our respondents are senior level managers, i.e., managing directors/CEOs (31%) or the heads of corresponding marketing or sales departments (52%).

We also conducted more than 250 telephone interviews with customers of a subset of the participating firms in order to validate the managers' responses with regard to customer reactions to customer prioritization. Depending on availability, we also drew on secondary financial data provided by commercial databases to validate managers' assessments of their firm's financial performance. We found that both customer responses and financial performance data were very similar to the managers' assessments, underlining that our findings are valid.

In order to test the supposed effect of customer prioritization on a firm's top-tier and bottom-tier customers, and ultimately on the performance outcome as depicted in Figure 1, we used structural equation modeling (the LISREL software package). This allows for simultaneous investigation of all effects as depicted in Figure 1, notably the effects of customer prioritization on a firm's top-tier and bottom-tier customers' satisfaction, loyalty, and share of wallet.

In order to identify the key levers for implementation, we relied on multi-group structural equation modeling using LISREL. More specifically, we compared how a firm's intent to prioritize customers relates to actual customer prioritization. This depends on whether the firm has a relatively low or relatively high score with respect to the corresponding pre-requisites (see Figure 3). We discovered that the intention to prioritize customers had a significantly greater effect on actual customer prioritization when firms´ scores were high on the corresponding levers for implementation than when firms had low scores concerning the six key levers.

### The Dark Side of Focusing on Your Top Customers

Arguing for prioritizing customers is obviously appealing, however this also implies that firms should stop doing business with less profitable customers. At rock-bottom, firms have to provide their lower level customers with much less quality. What about ticket vending machines, services for "economy customers," and how do you feel when you are put on hold by telephone hotlines while the charges mount up?

Firstly, the problem of focusing on top customers is that the number of "economy customers" is usually much higher than this. In many firms, the bottom tier makes up 80% of the customer base so much of the lower priority customer base is unhappy when services are cut. As a result, such "pariah" customers may tell other customers or potentially new ones that they have been poorly treated. In the end, many of these customers leave and company sales and profits are affected considerably.

Secondly, focusing on a limited number of customers who receive preferential treatment does neglect economies of scale when offering the same product or service to all customers. Customer prioritization implies that firms create differentiated offers for different tiers of their customer base. This leads to a high level of complexity along the value chain and inevitably, results in higher costs.

Thirdly, a balanced portfolio of top-tier and bottom-tier customers may well be important in order to reduce dependence on a very small number of top customers. When a minimal number of customers accounts for a huge portion of sales, firms then risk losing one of them which may be very unhealthy. For example, the two leading aircraft constructors, EADS and Boeing are indeed competing fiercely for a single deal worth up to 40 billion US$ for the new USAF refueling tanker. On the other hand, bottom-tier customers may provide small, yet very steady cash flow leading to predictable sales and profits. Thus, by having a balanced portfolio of top-tier and bottom-tier customers, firms can hedge the risk of certain top-tier customer relationships against a solid basis of small, ongoing returns.

These arguments show that customer prioritization does not automatically lead to higher company profits when taking into account its drawbacks. Thus, answering our initial question is not as simple as it seems and therefore needs explaining. Managers have to know how customers of different importance react to customer prioritization in order to assess its effects on a firm's customer portfolio. Furthermore, knowing if and how this affects firm profits will help managers to make a healthy decision whether to prioritize customers or to treat them all equally.

### Does Customer Prioritization Ultimately Pay Off?

In order to address the fundamental question of whether firms should prioritize customers, we had to consider the effects of customer prioritization on a firm's relationship with ***both*** important and less important customers. We also took a close look at the effect of customer prioritization on marketing efficiency. To provide comprehensive answers, we drew on a large-scale company sample consisting of more than 300 business units of different sizes and from various industries. The study was supported by the Institute for Market-Oriented Management at the University of Mannheim (Germany). Details on our sample and methodological procedure are provided in the box highlighting our research approach (Box 1).

Before addressing the performance outcome of customer prioritization, we started to assess customer prioritization itself. More specifically, we asked the firms participating in our study about how far they engaged in customer prioritization. In particular, we assessed the degree to which customers were treated differently with respect to key marketing instruments relating to their importance to the firm. As a result, a high level of customer prioritization became apparent when top-tier customers received a clearly different and preferential treatment. We considered customer prioritization in terms of five key marketing instruments: product, price,

TABLE 1:
Customer Prioritization Checklist

| To what extent do you differentiate between your customers / customer segments concerning the following aspects? | To a large extent (100) | (75) | Somewhat (50) | (25) | Not at all (0) |
|---|---|---|---|---|---|
| **Customer Prioritization in Product** | | | | | |
| • *Offer of particular goods / services* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Offer of individualized goods / services* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Offer of additional services* | ☐ | ☐ | ☐ | ☐ | ☐ |
| **Customer Prioritization in Price** | | | | | |
| • *Price level* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Price conditions (e.g., rebates, discounts)* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Flexibility of payment targets* | ☐ | ☐ | ☐ | ☐ | ☐ |
| **Customer Prioritization in Sales** | | | | | |
| • *Distribution model (e.g., direct vs. indirect, cross-functional teams for serving customers)* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Quality of the sales personnel* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Frequency of contacts initiated by the sales force* | ☐ | ☐ | ☐ | ☐ | ☐ |
| **Customer Prioritization in Communication** | | | | | |
| • *Quality of information given to the customers* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Timing of information transfer* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Costs of communication efforts* | ☐ | ☐ | ☐ | ☐ | ☐ |
| **Customer Prioritization in Processes** | | | | | |
| • *Rapidity of processes* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Flexibility of processes* | ☐ | ☐ | ☐ | ☐ | ☐ |
| • *Transparency of processes* | ☐ | ☐ | ☐ | ☐ | ☐ |

sales, communication, and processes. The lowest possible level of prioritization was given when all customers were treated equally regarding all these instruments. We developed a checklist for customer prioritization consisting of 15 items (see Table 1). Readers can use this checklist in order to assess the extent to which customer prioritization is present in their company.

We then registered how customer prioritization affects the characteristics of a firm's relationship with both its current top-tier and bottom-tier customers. The top tier contains the most important (i.e. valuable) customers to the firm, whereas the bottom tier obviously contains the least important customers. For both customer tiers, we evaluated the effect of customer prioritization on three important characteristics of a customer relationship: customer satisfaction, loyalty, and share of wallet, which is the share of category purchases a customer conducts with the firm. Firms indicated the average satisfaction, loyalty and share of wallet for customers belonging to each respective tier.

We recorded the performance outcome of customer prioritization on the overall level of the customer portfolio by the average sales per customer and the average customer profitability. To capture the effect of customer prioritization on marketing efficiency, we set the firm's marketing and sales costs off against sales. To record financial performance, we assessed the firm's return on sales (see Figure 1).

To put it in a nutshell: our analyses show that customer prioritization indeed pays off. Our findings show that customer prioritization has a positive effect on company profits compared to equal treatment using two mechanisms: first of all customer prioritization has a different effect on important customer relationship characteristics (customer satisfaction, customer loyalty, and share of wallet) when comparing top- to bottom-tier customers. While prioritizing customers leads to a higher satisfaction, loyalty, and share of wallet for top-tier customers, there is no negative effect on a firm's relationship with its bottom-tier customers. This mechanism causes customer prioritization to lead to higher sales per customer thus increasing marketing effectiveness.

Furthermore, customer prioritization increases average customer profitability as the former reduces marketing and sales costs in relation to sales. This enhances the efficiency of the marketing and sales effort and leads to higher average customer profitability.

Finally, our results show that firms which prioritize their customers ultimately have a higher return on sales than firms who treat all their customers equally. This allows for a simultaneous increase in financial returns through operational efficiency as well as through revenue enhancement. Figure 1 highlights how customer prioritization affects a firm's relationship with top-tier and bottom-tier customers and ultimately how a company performs.

To summarize, our analyses indicate that customer prioritization implies a higher return on sales as average customer profitability is increased: firstly, by indirectly increasing average sales per customer through increasing top-tier customers' satisfaction, loyalty and share of wallet and: secondly, by decreasing marketing and sales costs. Thus firms that prioritize customers are able to lever key performance indicators compared to their major competitors. Customer prioritization affects sales, profitability, and return on sales quite considerably. Our company sample in Figure 2 highlights that firms which prioritize customers to a high extent are market leaders in their industries with respect to these performance indicators.

» Managers have to know how customers of different importance react to customer prioritization in order to assess its effects on a firm's customer portfolio. «

### How Should Customer Prioritization be Implemented?

Our rationale is that firms should prioritize their customers on a broad empirical basis. However, our analyses also reveal another very intriguing result: about 80% of the firms participating in our study indicated that they intended to prioritize their customers to a high extent.

FIGURE 1:
How customer prioritization affects a firm's relationships with top-tier and bottom-tier customers and firm performance

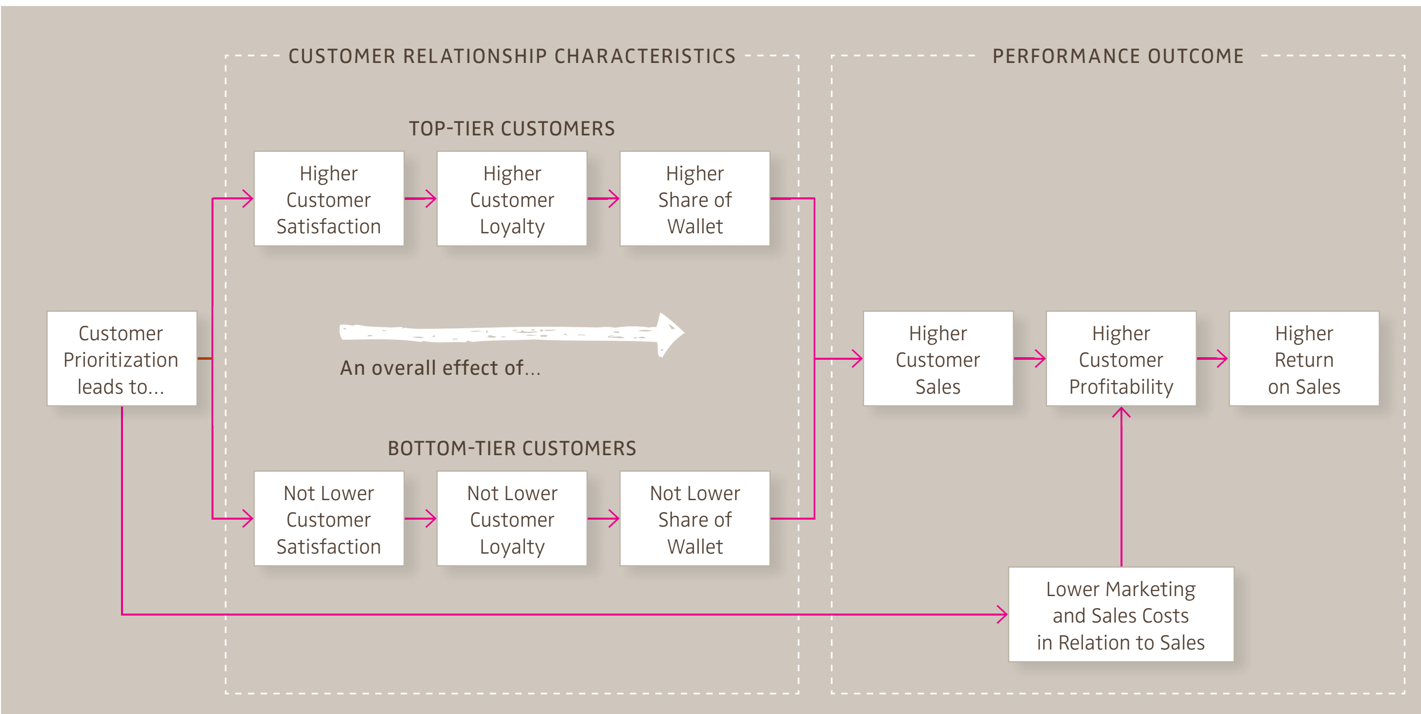
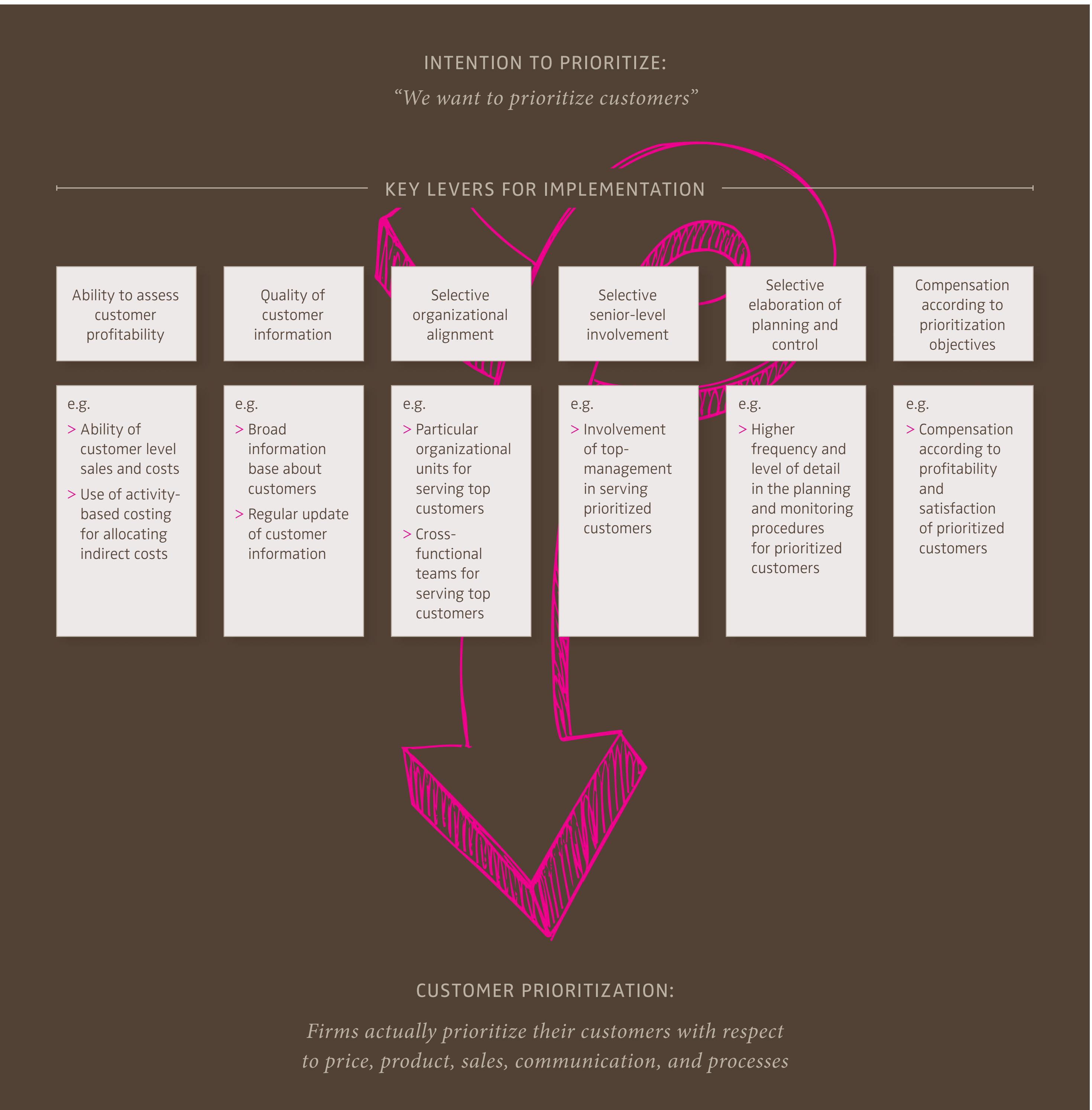



FIGURE 2:
How customer prioritization increases firm performance relative to the competitive landscape

*Figure 3:*
SIX KEY LEVERS TO ASSURE CUSTOMER PRIORITIZATION IN YOUR COMPANY



In contrast, when examining the firms' answers to our prioritization checklist (see Table 1), less than 40% indicated that they actually did prioritize to a high degree.

Many firms intend to prioritize among their customers, but give way at the implementation stage. In other words, although customer prioritization is strongly present in a firm's marketing strategy, this may not correspond to the actual allocation of resources and the use of marketing instruments in daily business. We therefore identified crucial leverages managers need to consider in order make a prioritization strategy really work.

We found that a firm's intention to prioritize customers does in fact lead to real customer prioritization when important internal prerequisites are met. These leverages are the firm's ability to assess customer profitability, the quality of customer-related information, selective organizational alignment, selective senior-level involvement, selective elaboration of planning and control and employees´ compensation in customer care according to prioritization goals. Figure 3 highlights the six key levers for customer prioritization as well as explanatory details.

Firstly, a firm's ability to assess profitability at customer level and the quality of customer-related information is crucial to prioritize customers properly in daily business. This is important as employees concerned with prioritizing in customer care have to be provided with the necessary information. Notably, sales and cost information for each customer account are crucial for understanding which customers should receive preferential treatment. Besides, firms need this customer-level information to be able to assess the profit impact of particular marketing initiatives. Our results also show that this information has to be up-to-date and that firms should not solely focus on "hard data" but should also consider qualitative customer information (e.g., information on referrals or complaints).

In addition, organization alignment is important in order to achieve properly implemented customer prioritization. In particular, our results imply that firms should install customer-responsive structures and internal processes depending on the customer's importance. Specifically, firms should create particular units that are solely responsible for looking after key accounts. By the same token, these units should include personnel from different backgrounds (e.g., marketing and R&D) as cross-functional teams are better equipped to deal with the complex needs of key customers.

Senior-level management has to engage in customer prioritization as well. Senior-level involvement is an important signal for all employees in customer care and for the customers that they receive special treatment. In particular, senior-level management should actively participate in dealing with these key accounts.

Firms also have to install adequate planning and monitoring procedures. These should address key prioritization goals as well as the corresponding resource allocations for specific customer tiers. Our analyses show that, in line with selective organizational alignment, planning and monitoring, procedures should also be differentiated according to the customer's importance. Planning and monitoring procedures should be more specific, followed more rigorously and updated more regularly for top-tier than for bottom-tier customers. In particular, more frequent, detailed planning and monitoring for high-priority customers leads to more specific and

» Many firms intend to prioritize among their customers, but give way at the implementation stage. «


accurate plans for these customers. Furthermore, monitoring procedures should be more rigorous for top customers. Relatively small deviations from expected sales or customer satisfaction scores should instigate an investigation of the circumstances that lead to this deviation.

Finally, firms can support customer prioritization by setting the right incentives. They should compensate their employees in customer care based on key performance metrics evaluating relationships with high-priority customers. In particular, compensation based on criteria such as customer satisfaction or sales volumes of high-priority customers will encourage sales people to provide higher value for top-tier customers.

» Firms can support customer prioritization by setting the right incentives. «

**Key Implications for Customer Relationship Management**

Our initial question was whether firms should prioritize customers. Our analyses lead to one major implication: firms should strive for customer prioritization simply because it pays off. Customer prioritization increases a firm's average sales per customer account. Managers can rely on this sales-enhancing effect as customer prioritization improves relationships with top-tier customers whereas bottom-tier customers do not suffer. Therefore, customer prioritization allows the development of important relationships that ultimately drive sales and profitability. In addition, customer prioritization drives customer profitability by reducing marketing and sales costs. In this way managers can simultaneously enhance the efficiency of their customer relationship management efforts and increase sales by prioritizing customers.

However, the will to prioritize customers itself does not necessarily mean that this will be properly implemented. Firms are facing a considerable implementation gap today. Customer prioritization first requires proper information systems which provide profitability information on a customer-account level. These have to be up-to-date and should provide key customer-related information. Managers should also align their organization selectively as well as monitoring their customer tiers. Firms should support prioritization efforts by aligning their organizational structure, for example, by creating customer-responsive units for the most valuable customer accounts. Furthermore, preferential treatment of key customers is a task for top management. Upper management should be largely involved in customer relationship management for key customers. Finally, firms have to set the right incentives for their employees in customer care in order to facilitate customer prioritization. Thus, firms have to support customer prioritization by substantially aligning their organization to this end. •

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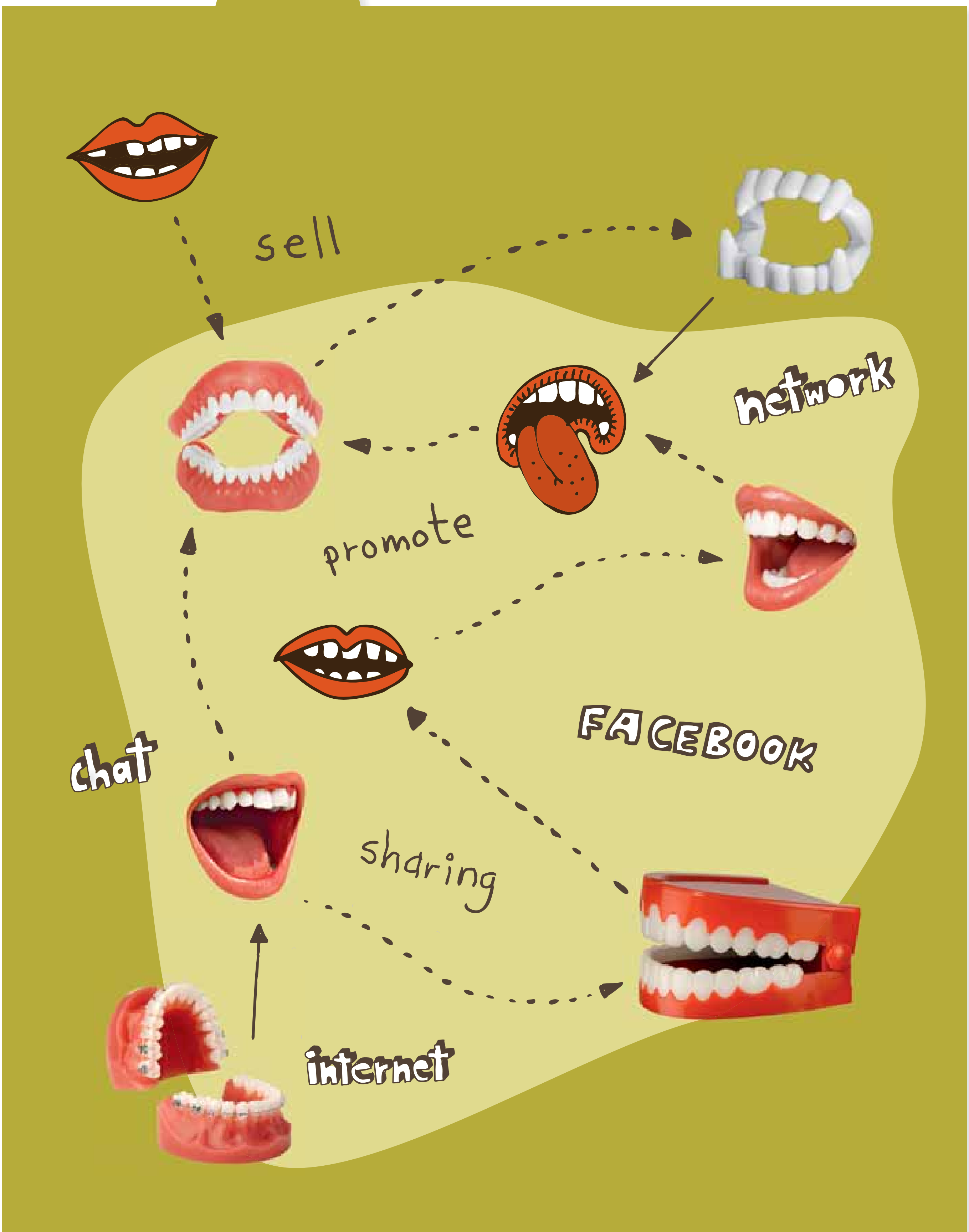
KEYWORDS:

Customer Relationship Management, CRM, Sales Management, Profit Management

{New Strategies}



# Do you want to be my "friend"? MONETARY VALUE OF WORD-OF-MOUTH MARKETING IN ONLINE COMMUNITIES

*Michael Trusov, Randolph E. Bucklin and Koen Pauwels*

How large and lasting are the effects of word-of-mouth (WOM) referrals versus paid marketing? What is the $ / € worth of a WOM-referral to an Internet social networking site? This study finds that word-of-mouth referrals have substantially longer carryover effects than traditional marketing actions. The long-run elasticity of WOM on site signups is 0.53; about 20 times higher than that of marketing events, and 30 times that of media appearances. Based on revenue from advertising impressions served to a new member of the site, the monetary value of a WOM referral is about $0.75 per year. By sending out 10 referrals, each network member thus brings in $7.50 to the firm; which represents the maximum reward the firm could consider to incentivize word-of-mouth referrals. Managers can use this approach and findings to benchmark metrics for both WOM and traditional marketing, to test changes in online WOM referral content, and to decide on the appropriate size of financial incentives to stimulate WOM.

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**Word-of-Mouth: The Most Effective, yet Least Understood Marketing Strategy?**

Word-of-mouth (WOM) marketing has recently attracted a great deal of managerial attention. WOM is more and more touted as a viable alternative to traditional marketing communication tools. One calls it "the world's most effective, yet least understood marketing strategy." Marketers are particularly interested in better understanding word-of-mouth as traditional forms of communication may be losing effectiveness. For example, one survey showed consumer attitudes toward advertising plummeting between September 2002 and June 2004. Other survey results show that 40% fewer respondents agree that ads are a good way to learn about new products, 59% fewer say they buy products because of their ads, and 49% fewer find ads entertaining.

WOM communication strategies are appealing because they combine the prospect of overcoming consumer resistance with significantly lower costs and fast delivery — especially through technology such as the Internet. Indeed, the Internet provides numerous venues for consumers to share their views, preferences, or experiences with others as well as opportunities for firms to take advantage of WOM marketing. In the words of commentator Whitman: "Instead of tossing away millions of dollars on Superbowl ads, fledging dot-com companies are trying to catch attention through much cheaper marketing strategies such as blogging and word-of-mouth campaigns." Thus, it is vital to managers to understand whether word-of-mouth is truly effective on the Internet and, if so, how its impact compares to traditional marketing activities.

Unfortunately, empirical evidence remains limited regarding just how effective WOM marketing is in attracting customers over time. Managers who need to allocate firm resources require better measures for the monetary effects of both WOM ***and*** traditional marketing. A second benefit of such measures is allowing managers to benchmark different WOM/referral content options. Finally, a growing practice in both offline and online markets is to offer financial incentives to existing customers to provide WOM referrals (e.g., Netflix has incented current subscribers to recruit new ones). The key question is how much to pay for such WOM referral. To decide on the maximum amount to pay for such WOM referral, managers need to quantify how much additional revenue it brings to the firm.

Quantifying the full effects of WOM referrals and marketing requires us to account for the interplay of these communication mechanisms. Managers and researchers alike realize that WOM not only influences new customer acquisition but is itself affected by the number of new customers. Likewise, traditional marketing activities may stimulate WOM; they should be credited for this indirect effect as well as the direct effect they may have on customer acquisition. Also, all these communication mechanisms may have permanent effects on customer acquisition. For instance, WOM may be passed along beyond its originally intended audience and thus increase the site's potential to recruit signups in the future. Network externalities can also imply that signup gains today may translate into higher signup gains tomorrow, even in the absence of marketing actions. In the presence of all these effects, separating out the monetary value of word-of-mouth requires excellent longitudinal data, which are provided in the context of Internet social networking sites.

**Do You Want to be my "Friend"?**

Social networking sites have become extremely popular, with the majority of US Internet users visiting at least one of the top 15 social networking sites. About 50 social networking websites each have more than one million registered users and several dozen smaller, though significant, sites cater to specific niches. As of June 2009, the largest online social networking site, Facebook.com, boasts 122 million unique visitors per month.

» Instead of tossing away millions of dollars on Superbowl ads, fledging dot-com companies are trying to catch attention through much cheaper marketing strategies such as blogging and word-of-mouth campaigns. «

Social networking sites allow a user to build and maintain a network of friends for social or professional interaction. The core of a social networking site consists of personalized user profiles. Individual profiles are usually a combination of users' images (or avatars), list of interests, music, books, movies preferences, and links to affiliated profiles ("friends"). Different sites impose different levels of privacy in terms of what information is revealed through profile pages to non-affiliated visitors and how far "strangers" vs. "friends" can traverse through the network of a profile's friends. Profile holders acquire new "friends" by browsing and searching through the site and sending requests to be added as a friend.

Typically, sites facilitate referrals by offering users a convenient interface for sending invitations to non-members to join. Figure 1 shows how a popular social networking site, Facebook.com, implements the referral process.

The social network setting offers an appealing context in which to study word-of-mouth. The sites provide easy-to-use tools for current users to invite others to join the network. The electronic recording of these outbound referrals opens a new window into the effects of WOM, giving us an unobtrusive trace of this often hard-to-study activity. When combined with data that also tracks new member signups, it becomes possible to model the dynamic relationship between this form of word-of-mouth and the addition of new members to the social networking site. These members are, in a real sense, also "customers" of the social networking site, as their exposure to advertising while using the site produces revenue for the firm.

**What Drives the Growth of Your Site?**

Figure 2 displays the daily signups (new members) for a social networking site from February 1 to October 16, 2005. Besides the seasonal patterns of day of the week and holidays, the graph clearly shows the growth in customer acquisition.

The key question for management is: to what is this growth attributable? The interplay of several forces drives a growth process of a typical social networking site. On the firm's end these are traditional marketing activities like advertising, event marketing (directly paid for by the social networking site) and media appearances (induced by PR), while on the consumers' end it is primarily word-of-mouth (WOM) referrals. As visualized in Figure 3, WOM referrals lead to new signups and (following the reverse arrow) new signups lead to more WOM referrals, and therefore indirectly to more new

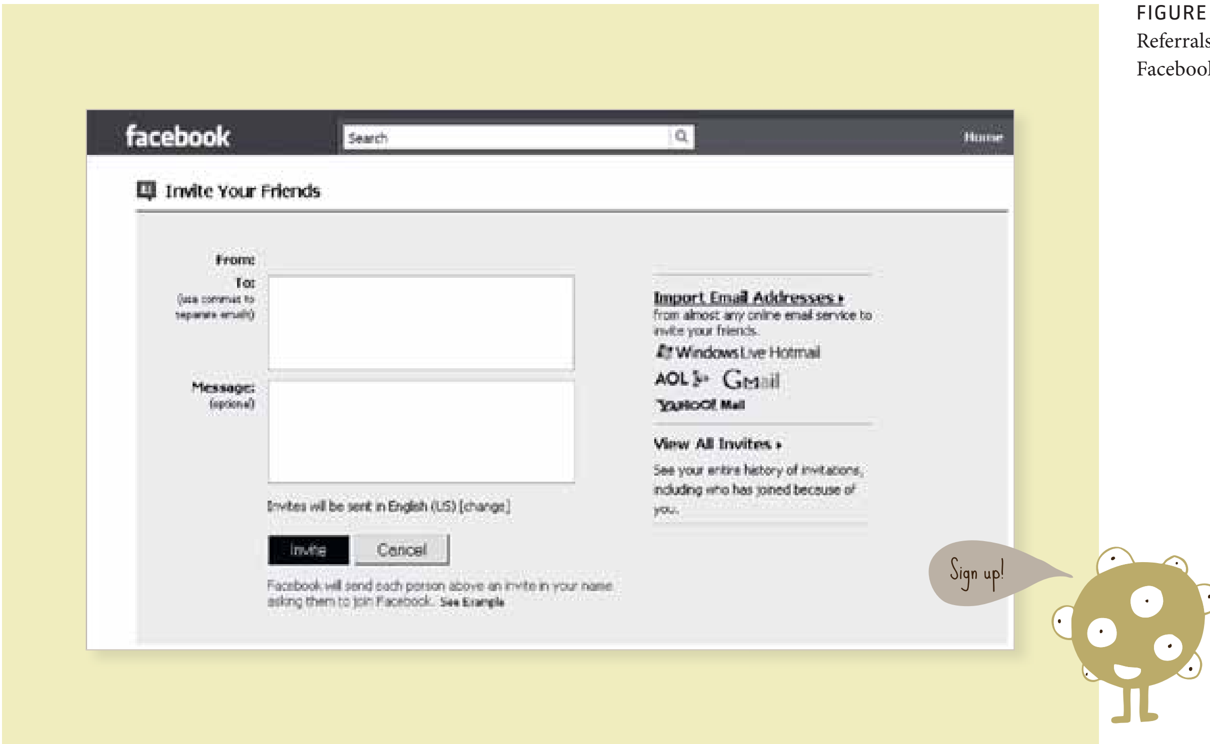
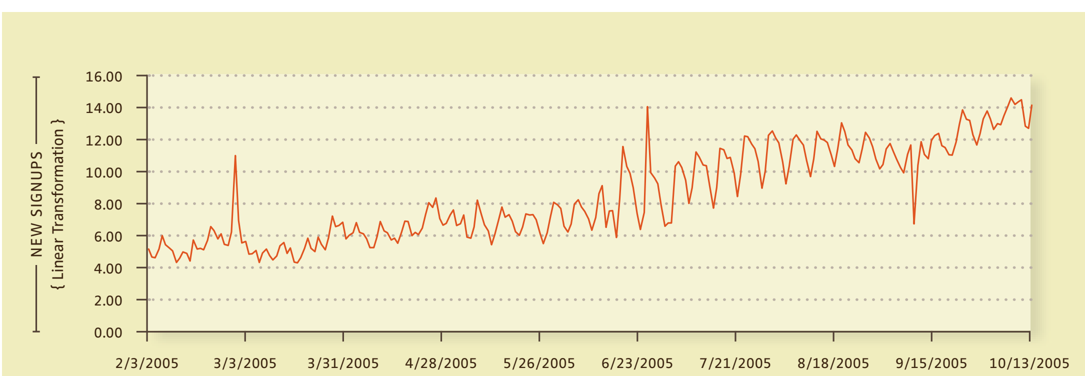



FIGURE 1:
Referrals Process at Facebook.com




* The Y-axis values shown in the figure reflect a linear transformation used to disguise the identity of the source.

FIGURE 2:
The Growth of a Social Networking Site

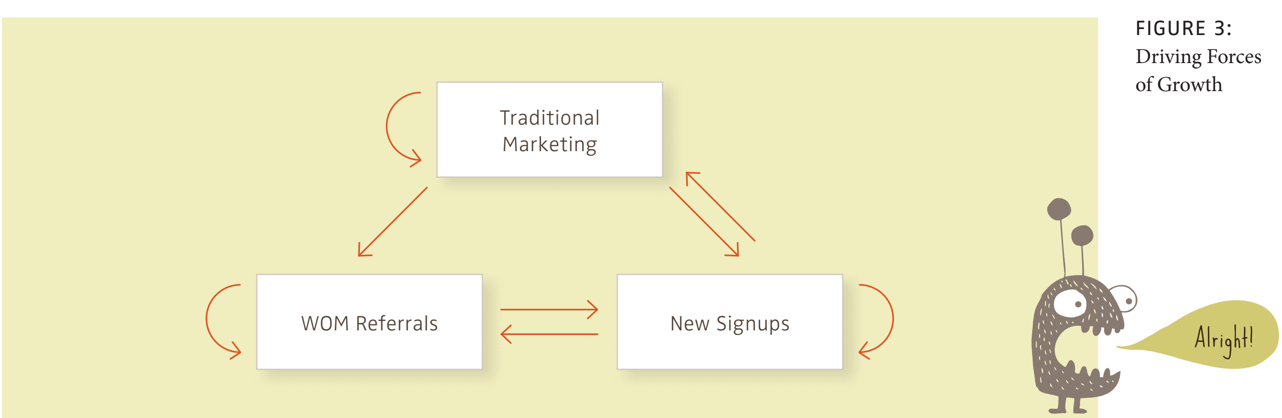
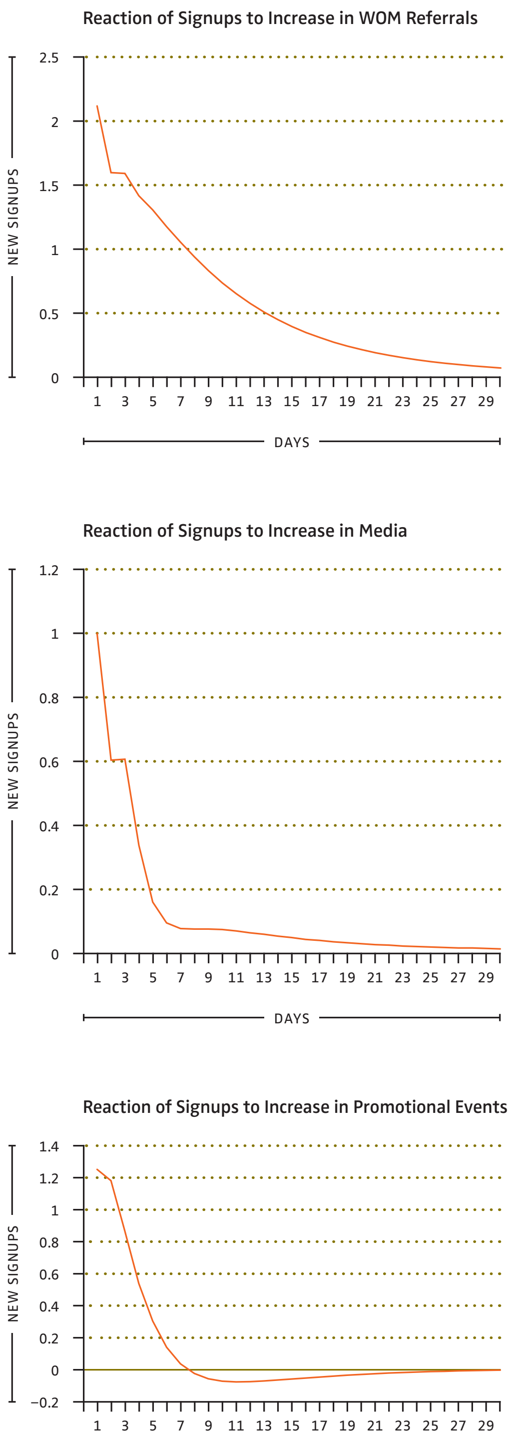



FIGURE 3:
Driving Forces of Growth

FIGURE 4:
Response of Signups to Increase in Referrals, Media and Promotional Events




signups. A similar pattern of influence is observed for new signups and traditional marketing activity — traditional marketing stimulates WOM referrals, leading to another indirect effect on new signups. Lagged effects of traditional marketing, new signups, and WOM referrals are also included in the model (as indicated by the curved arrows).

A proper statistical analysis which accounts for these interactions allows us to quantify the impact each of the individual drivers has on all other components in the system (for details, see Trusov/Bucklin/Pauwels 2009). Of particular interest to site management is the short-run and long-run effects of WOM and traditional marketing actions on new customer acquisition.

### Short-term and Long-Term Effects for WOM and Traditional Marketing Actions

Based on the model estimates, Figure 4 plots the effect of WOM referrals, media, and events on new signups over time.

The top panel in Figure 4 shows that the effect of the one-time increase in WOM lasts for about three weeks. In contrast, the effects of media and events disappear within just a few days (middle and bottom panels of Figure 4). Promotional events even experience a "post-promotion dip" indicated by the (small) negative values for effects beyond 8 days. In other words, new members that would have signed up later, are encouraged by the promotional event to sign up now. Compared to traditional marketing activities, the WOM referrals induce both a larger short-term response as well as a substantially longer carryover effect.

As to the size of the effects, Figure 5 presents the estimated elasticity (i.e., percentage change in new signups to percentage change in a corresponding marketing driver) for WOM, events, and media. For managers interested in the timing of returns, we distinguish the elasticity at 1 day, 3 days, 7 days and long-run (summing up all effects over time).

The immediate (1 day) elasticity of WOM (0.068) is 8.5 times higher than that of traditional marketing actions (0.008). Moreover, this discrepancy grows over time. Indeed, the long-run elasticity indicates that WOM-referrals are akin to the "gift that keeps on giving," especially when compared to the performance of traditional marketing activities. Figure 5 shows that the long-run elasticity of WOM referrals (0.53) is about 20 times higher than the elasticity for marketing events (0.53 vs. 0.026) and 30 times higher than the elasticity for media appear-

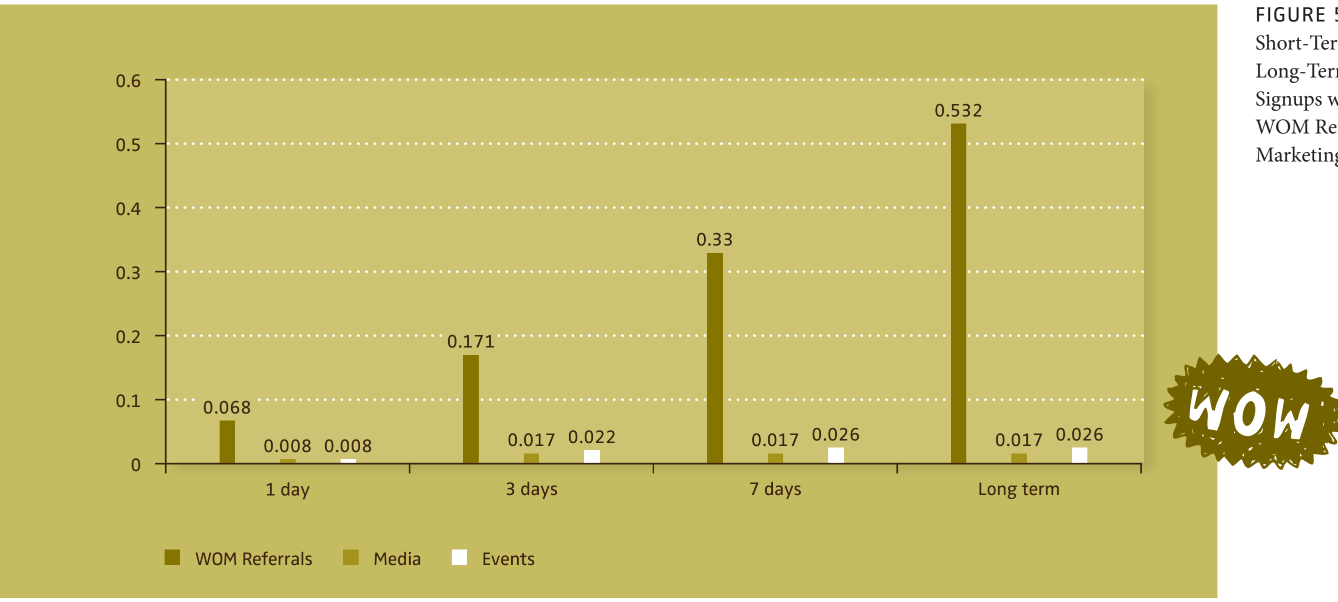



FIGURE 5:
Short-Term Versus Long-Term Elasticity of Signups with Respect to WOM Referrals and Marketing Activities

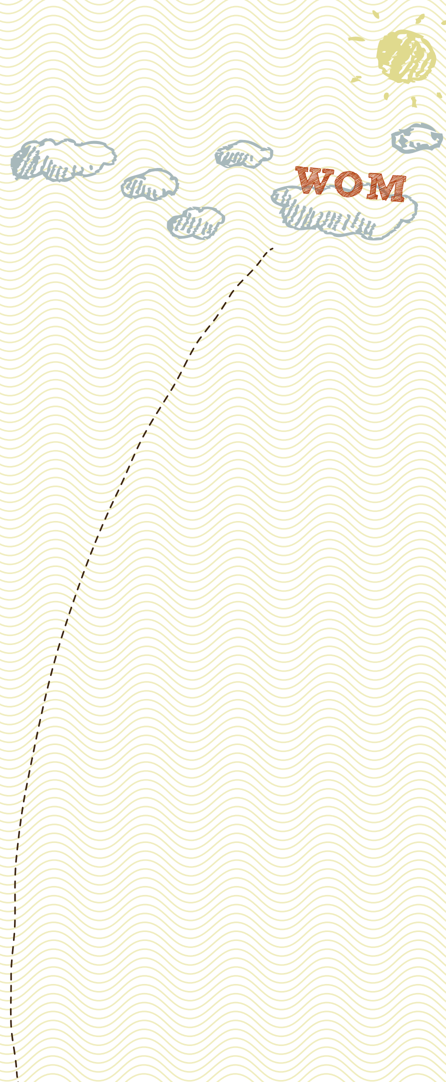
ances (0.53 vs. 0.017). The estimated WOM elasticity of 0.53 substantially exceeds the range of values for advertising elasticities reported in the literature. This supports the notion that WOM may be among the most effective of marketing communication strategies. But of course the effectiveness of different marketing instruments is company specific — point elasticity comparisons do depend on a "base" level of these instruments. Therefore our findings should not be taken as generalization. On the other hand, in this paper we are dealing with a major social networking site, and therefore the scale of a membership base, media coverage and promotion events are representative for the industry leader.

### Monetary Value of WOM Referrals

To calculate the monetary value of WOM, managers also need to know how much revenue each new member (signup) brings in for the firm. For the typically free social networking site, a new member brings in revenues due to future banner ad exposures. In the absence of firm-specific data, managers can use industry averages for cost per thousand impressions (CPM) and number of impressions per user / day while making assumptions regarding a customer's projected lifetime with the firm. For CPM, we obtained price quotes from several social networking sites and concluded that about 40 cents is reasonable. For impressions, the average number of pages viewed on a community site by a unique visitor per month is about 130. Assuming the average page carries two to three ads, we calculate that the average user contributes approximately 13 cents per month or approximately $1.50 a year. From our elasticity estimates, we know that 10 WOM-referrals bring in roughly an estimated 5 new site members over the course of 3 weeks. This suggests that each outbound referral is worth about 75 cents per year. By sending out 10 referrals, each network member could bring in about $7.50 to the firm.

Two important caveats apply to this number. First, it is based on banner ad exposure. Other online advertising models such as pay per click (PPC), pay per lead (PPL), and pay per sale (PPS) could be analyzed by substituting appropriate conversion rates. Second, when a company

» ...the effect of the one-time increase in WOM lasts for about three weeks. In contrast, the effects of media and events disappear within just a few days. «




» The elasticity for WOM is about 20 times higher than for marketing events, and 30 times that of media appearances. «

stimulates WOM activity with financial incentives, it is no longer "organic" word-of-mouth. Indeed, one might term it "fertilized" word-of-mouth. We do not know whether fertilized word-of-mouth would produce the same elasticity as the organic word-of-mouth observed in our data. If the paid nature of WOM activity is known to prospective members, fertilized word-of-mouth may be substantially less effective than organic word-of-mouth. In this respect, the monetary value calculations represent an upper bound of the money that could be generated by stimulating word-of-mouth. The key implication is that, if the firm cannot effectively generate additional referrals at less than 75 cents each, it should not pursue firm-stimulated WOM programs.

**What Have We Learned and What Do We Still Need to Learn?**

In today's connected world, managers face many options to stimulate growth, including word-of-mouth referrals. Effective allocation of firm requires benchmarking of the monetary value of word-of-mouth referrals, in the context of other growth drivers and of complex feedback loops among WOM, marketing activity, and customer acquisition. Analysis for an online social networking site revealed that WOM referrals have a very strong impact on new customer acquisition. The long-run elasticity of signups with respect to WOM is estimated to be 0.53 (substantially larger than the average advertising elasticities reported in the literature). The elasticity for WOM is about 20 times higher than for marketing events, and 30 times that of media appearances. Thus, the outlined approach offers managers a tool to improve the metrics they use for assessing the effectiveness of traditional marketing when WOM effects are present.

Based on revenue from advertising impressions served to a new member of the site, the monetary value of a WOM referral is about 75 cents per year. Managers can use this approach to test changes in online WOM referral content, and to decide on the appropriate size of financial incentives to stimulate WOM.

Not all managerial questions could be addressed by the current data. First, it did not contain information on competing sites, and therefore did not allow an analysis of the effects of competitive WOM-referrals and marketing activity. Second, the data tracks new signups and WOM at the aggregate level. Site members attracted in different ways (i.e. through WOM, events or media appearances) could differ in visit frequency and pages viewed, and thus yield different revenue benefits to the site. The lack of such individual-level data did not allow us to make this distinction in our revenue calculations. Third, the collaborating social networking site already had a well established brand among many online communities. Because social networking sites start out with a crucial mix of user-generated content and WOM of founders to friends, WOM may be even more important for small sites, which also typically do not have the funds for paid marketing events nor get much media attention.

Application of our approach to other settings will also reveal whether the "dominance of WOM" for a particular social networking site extends to other firms and industries. This may well be the case, as a review of 23 service categories reported that WOM had greater reported impact on brand choice than advertising or personal search.

In conclusion, this study has shed new light on "the world's most effective, yet least understood marketing strategy," providing the empirical evidence that word-of-mouth communication is a critical factor for firms seeking to acquire new customers and that WOM can have larger and longer-lasting effects than traditional marketing activity. •

KEYWORDS:

WOM, Word-of-Mouth, Referrals, Communication Strategy, Winning New Customers, Internet, Social Networks

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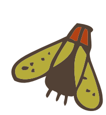

{New Theories}

# Getting marketing back into the boardroom: THE INFLUENCE OF THE MARKETING DEPARTMENT IN COMPANIES TODAY

*Peter C. Verhoef and Peter S.H. Leeflang*

What influence do marketing departments have in companies today? Which factors determine this influence? These are the issues discussed in the present article. Empirical evidence based on data from companies in the Netherlands demonstrates that accountability, innovativeness and customer connections are the three major drivers of influence. The need for a strong marketing department within companies is also discussed, supported by empirical data.

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**The Status of Marketing**

In the past three decades, marketing academics and practitioners have raised concerns over the declining influence of marketing in corporate life.

An anthology of the status of marketing in today's organizations reveals that marketing is in deep trouble. On the basis of existing discussions and publications, we might conclude that "marketing died, was declared impotent or most likely just became irrelevant to many senior managers." It is even maintained that "misguided marketing strategies have destroyed more shareholder value, and probably more careers, than shoddy accounting or shady fiscal practices have." This assertion is confirmed by ex-chief of LEGO, Christian Majgaard, who believes that marketing has lost its strategic role and that few marketers remain involved in rolling out strategies. Instead, most are engaged in more tactical decisions, particularly advertising, sales support, and public relations. These developments have important consequences:

- The marketing function drops down in the corporate hierarchy.
- Marketing and management issues receive less attention in the boardroom.
- Marketing is perceived as a cost, not as an investment.
- Marketers are being marginalized, in the sense that many strategically important aspects of marketing move to other functions in the organization.
- The synergies that result from mixing marketing decisions disappear.
- The roles of general managers, CFOs, and "other penny pinchers and number crunchers" become more important than the role of CMOs.
- Most CMOs are in the hot seat, with tenures averaging 22.9 months.

Many statements on the role of marketing in modern companies, however, remain anecdotal or journalistic and lack an empirical basis. In this article we offer empirically based statements about this topic, supported by empirical data from the Netherlands (see Box 1 on page 38). Based on this study, we determine (1) the influence of marketing in companies today, (2) the determinants of the marketing department's influence, and (3) the impact of weakened marketing departments on business performance.

### Framework for Marketing's Influence within the Company

Marketing departments should have a strong role within the company, as it will improve business performance. Figure 1 shows how companies can improve MD influence through the improvement of capabilities of the marketing department and how this subsequently affects business performance. There are two ways in which MDs can influence performance. Either directly, where the benefits of a strong marketing function flow immediately into improved business performance, or indirectly, where a strong marketing function increases marketing orientation. In the latter case, it is market orientation, not just the power of the marketing function, which increases performance.

» There are two ways in which MDs can influence performance. Either directly, where the benefits of a strong marketing function flow immediately into improved business performance, or indirectly, where a strong marketing function increases marketing orientation. «

### Declining Influence of Marketing Departments

Marketing departments should have a strong influence within companies. However, this is not reflected in the empirical data collected in the Netherlands. The average scores for each of our measures in the total sample and per function are reported in Table 1. The average perceived influence is 3.69, and there is no significant difference between respondents from a marketing function and respondents from other functions (i.e., finance and general management). This average score suggests a moderate influence. Top management respect is significantly higher, with an average score of 5.12. Remarkably, finance executives believe the marketing function receives significantly more respect from the board than is the case with marketing executives (not shown in Table 1). The average importance of marketing across different decisions is 36.81. For marketing decisions, this score is significantly higher, with a value of 43.00, whereas for other decisions, it is significantly lower at 27.24. Marketing executives tend to score the decision influence higher than other executives. The average influence per decision per department is shown in Table 2. The marketing department is most influential in marketing decisions pertaining to advertising, customer satisfaction measurement and management, segmentation, targeting, positioning and relationship/loyalty programs. The sales department is far more influential in customer service, pricing, and distribution decisions. The influential scores for these decisions are markedly lower than those reported in a study in 1999 on the influence of marketing in German and US companies. Marketing has a relatively strong influence in the formulation of the business strategy, though for the other decisions, marketing seems to have only a moderate influence, with scores of 30 and 26 and usually ranking second. The marketing scores are again lower than those reported in the 1999 study.

### The Importance of Marketing Department Capabilities

Marketing department capabilities are essential for improving the influence of the marketing department. There are three key capabilities:

> accountability
> innovativeness
> customer connection

Beyond these three key capabilities, integration, in particular with the finance department, also plays a role.

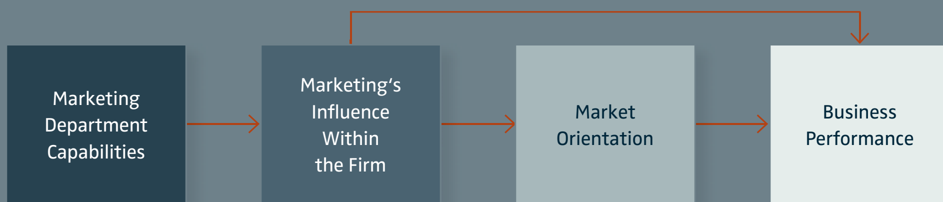



FIGURE 1:
From Marketing Capabilities to Business Performance

TABLE 1:
Averages of marketing department's influence measures

| Influence Measure | Average Score |
|---|---|
| Influence perception (1 = low, 7 = high) | 3.7 |
| Top management respect (1 = low, 7 = high) | 5.1 |
| Decision influence total (0 = low, 100 = high) | 36.8 |
| Decision influence: marketing decisions (0 = low, 100 = high) | 43.0 |
| Decision influence: other decisions (0 = low, 100 = high) | 27.2 |

TABLE 2:
Decision influence across departments and functions

| | Marketing | Sales | R&D | Finance | Marketing Score 1999 (Study executed by Homburg and colleagues) |
|---|---|---|---|---|---|
| MARKETING DECISIONS | | | | | |
| Advertising | 69 | 23 | 4 | 3 | 65 |
| Customer satisfaction measurement and improvement | 57 | 30 | 12 | 2 | 44 |
| Segmentation, targeting, and positioning | 55 | 33 | 8 | 5 | N/A* |
| Relationship- and loyalty programs | 51 | 35 | 6 | 8 | N/A |
| Customer service | 28 | 51 | 18 | 3 | 31 |
| Pricing | 20 | 48 | 13 | 18 | 30 |
| Distribution | 18 | 45 | 24 | 13 | 34 |
| OTHER DECISIONS | | | | | |
| Strategy | 34 | 32 | 16 | 18 | 38 |
| Product development | 30 | 25 | 39 | 7 | 32 |
| Expansion to foreign markets | 26 | 33 | 4 | 28 | 39 |
| Choice of a business partner | 26 | 33 | 13 | 23 | 33 |
| Investments in IT (e.g., ERP, CRM, Internet) | 26 | 16 | 15 | 42 | N/A |

(n = 213) (Allocation of 100 points over 4 departments)
* Not available in 1999 study.

{*Box 1*}

## DESCRIPTION OF STUDY ON MD INFLUENCE

Marketing department's (MD) influence within the company is measured using three variables:

> the perceived importance of the MD
> top management respect of the MD
> decision influence of the MD on marketing and other decisions

Perceived marketing influence is measured with an attitude-based scale. One example indicates "The activities of the marketing department are considered as more important than other activities." Top management respect focuses on the perceived respect for the marketing department among the top management and board of the company. Top management respect is measured using different scales such as: "Top management acknowledges the strategic importance of the marketing department." The variable decision influence is measured by asking each respondent to divide 100 points among four departments (marketing, sales, finance, R&D/production) for seven marketing decisions (i.e., pricing, advertising, segmentation, targeting, and positioning, customer satisfaction measurement and management, customer service, relationship and loyalty programs, distribution) and five non-marketing decisions (i.e. general business strategy, IT-investments, partner choice, new product development, expansion to foreign markets). Influential departments should gain more points.

Data are obtained from a written survey of 2,500 companies in the Netherlands with a minimum of 250 employees and at least one subsidiary. In total, 296 respondents participated in the survey. The companies in our sample mainly operate in B2B markets, with a 3.07 average score on a 10-point scale (1 = sales generated exclusively from B2B, 10 = sales generated exclusively from B2C). In line with recent trends in Western economies, the companies primary focus is on services, with an average score of 5.85 on a 10-point scale (1 = sales generated exclusively from goods, 10 = sales generated exclusively from services). The sample companies are active in a variety of industries (e.g., retail, tourism, business services and construction). Approximately 20% employ more than 1,000 full-time members of staff. For only 8% of the included companies, the primary background of the CEO is marketing and for 36.8%, marketing is represented in the board. Finally, for 19% of the companies surveyed, marketing is a line function, whereas for 51%, it is a staff function.

Similar studies have been carried out using data from the USA, Germany, United Kingdom, Australia, Israel and Sweden.

### Accountability

In many companies, marketers have a difficult time justifying their expenditures in terms of direct return on investment. In other words, the inability to account for marketing's contribution has undermined its standing within the company. McGovern and colleagues state that "the [marketing] field is chock-a-block with creative thinkers, yet it's short on people who lean toward an analytic, left-brain approach to the discipline." Two aspects are relevant in this respect. First, many marketers do not measure the effect of their actions, because they are unable or unwilling to do so, or because they do not use the appropriate metrics and/or methods. As a consequence, many advertisements have no effect on sales, sales promotions have no persistent influence on sales at either the brand or the category sales level, and new products suffer low success rates. Not surprisingly, CEOs cannot obtain clear, compelling answers about the impact of marketing. Marketing productivity could increase if managers were able to measure it. Recent calls for more attention to be focused on accountability, marketing metrics, and dashboard marketing may be helpful. In this respect, Farris and colleagues have written an excellent monograph in which they discuss the 50+ metrics that every executive should master. Second, there is still a lack of appropriate specifications of metrics, especially metrics that measure long-term or persistent effects. Many managers do not know what to measure and how to interpret the results. So, for example, a manager might collect customer satisfaction scores and customer retention rates, but if he or she cannot explain these scores (in relation to marketing activities), the data are not very useful. Accountability also involves the determination of the effects of marketing activities on the value of the company.

### Innovativeness

Innovativeness is one of the most important business drivers. Marketing might play an essential role in the innovativeness of firms, in that it could initiate new innovations or translate customer needs into the pipeline of innovations. The innovative nature of the marketing department can be regarded as the degree to which marketing contributes to the development of new products within the company. We know, however, that CEO's are often disappointed by the level of innovation in their business, for which they hold marketers at least partially accountable.

#### Customer Connection

The customer connecting role of the marketing department concerns the extent to which the marketing department is able to translate customer needs into customer solutions that fit customer needs, and the extent to which it demonstrates the criticality of external customers and their needs to other organizational functions. In practicing this connecting role, the marketing function should emphasize the customer vantage point. The marketing department's ability to connect with the customer increases its influence within the company. The relationship between customer-connecting capabilities and the marketing department's influence is not without controversy. Primarily, it is not clear who is responsible for the company's relationships with its customers. Many executives mention that the customer must be a shared responsibility throughout the organization, but none mention the marketing department as solely responsible. However, paradoxically, the deeper the marketing concept is embedded within an organization and becomes the declining theme for shaping competitive strategies, the more likely the role of marketing is diminished. Consequently, as more functions connect to the customer, marketing becomes less relevant.

#### Integration / Cooperation

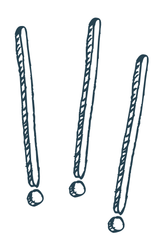
Clashes between marketing and other departments are relatively common and are considered one of the causes of the decline of marketing within the company. One solution is to create cross-functional cooperation in teams, which is generally considered beneficial to the company, a fact acknowledged by multiple organizations (i.e. Unilever, Procter & Gamble). The effect of cooperations with other departments on marketing influence is less clear. On the one hand, more cooperation could increase influence, because it prevents marketing from becoming a separate entity (or silo) without influence within the organization and prompts it to promote its plans within the company. On the other hand, more cooperation may cause the loss of sovereignty in marketing decisions and create further dispersion of the marketing department's responsibilities, with a concomitant loss of influence. Empirical evidence reveals that integration with other departments weakens the marketing department. This especially holds true for strong cooperation with finance.

#### Average Performance on Capabilities

Marketing departments score particularly poorly on innovativeness, and also do not excel in accountability (see Figure 2). However, they seem to be well connected to customers. Therefore, in the main, marketing departments should improve their innovativeness and accountability.

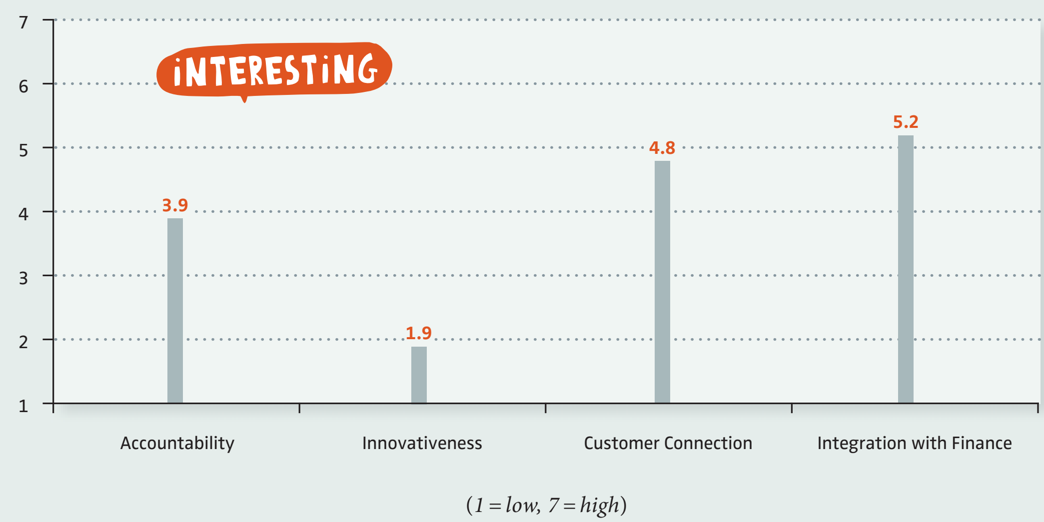
#### The Need for a Strong Marketing Department

One important question is whether companies actually require strong marketing departments. Both in practice and in the literature, pledges have been made that a strong marketing department is not necessary, as long as the company as a whole has a strong market oriented culture: ***marketing is everywhere!*** This would imply the absence of a direct link between marketing department influence and business performance.



» Empirical evidence shows that companies with strong marketing departments record a higher performance. It follows that these results confirm the need for strong marketing departments within companies! «

FIGURE 2:
Average Scores for Important Marketing Department Capabilities




Empirical evidence shows that companies with strong marketing departments record a higher performance. In five (Germany, UK, USA, Australia and Israel) of the seven countries studied, a positive relationship between the influence of the marketing department and both market orientation and business performance is evident. It follows that these results confirm the need for strong marketing departments within companies! It is, however, possible that there is no direct link between the influence of the marketing department and business performance. This is particularly true for companies in the Netherlands and Sweden. Therefore, in these companies, a strong marketing department only increases business performance by its impact on market orientation!

### The Status of Marketing

What is the influence of the marketing department in companies today? Empirical results indicate that the actual decision influence of marketing departments is limited to advertising, relationship management (including satisfaction measurement and improvement) as well as segmentation, targeting, and positioning. Decision areas such as pricing and distribution that were originally dominated by marketing, at least according to most marketing textbooks, are now covered by other departments, in particular, sales and finance. Overall, empirical findings support claims in the popular and scientific press that marketing is losing ground within corporate life.

These negative findings are disturbing, since companies with strong marketing departments tend to perform better, due to a stronger market orientation and the direct effect of the influence of the marketing department on performance. Consequently, we believe that companies should give the marketing department more power. This is actually confirmed by experiences at General Electric, where the marketing function is currently being paid more attention in the wake of deteriorating market performance in a period without a strong marketing focus.

### Regaining Influence

How can marketing regain its strategic role in companies? Based on empirical outcomes, the following general solutions are suggested:

> ***Marketing departments should become more accountable for the link between marketing actions and policies and financial results.***

> ***Marketing departments should become more innovative by increasing their share in new product/service concepts, which implies a greater contribution of marketing to organic growth.***

> ***Marketing departments should improve their connection with the customer.***

To achieve greater accountability, marketers should develop capabilities in analytics, finance and cost accounting.

Marketing departments require a financial behavioral change, with marketing plans including a financial section that features the planned financial consequences (i.e. pre-ROI) of their marketing actions. Marketing departments should also embrace more testing. In evaluation reports, they should report ROI along with other performance metrics of marketing plans and marketing campaigns carried out.

To increase the innovativeness of the marketing department, marketing people might capitalize on their market and customer knowledge to develop successful new product and service concepts. They could build on new trends, such as customer co-development and customer solutions. At the same time, marketers should be trained in techniques such as lateral thinking, to transform customers' desires and needs into explicit product ideas. To improve customer connections a deeper knowledge of customer needs is required. This may arise from good marketing research. It may, however, also be increased by closer connections with customers and through customer engagement. Also, quantitative knowledge could be enriched with qualitative insights.

To summarize, marketers should deserve more influence within companies. At the same time, they should improve their capabilities and generate more respect within the company. This will be an important challenge for today's marketing function. •

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KEYWORDS:

Marketing Function, Cooperation, Market Orientation, Marketing Capabilities, Business Performance

{New Methods}

/// Short-term profit and long-term value need to be balanced

# My customers are better than yours!
# ON REPORTING CUSTOMER EQUITY

*Thorsten Wiesel, Bernd Skiera and Julian Villanueva*

Managers and investors need information about the performance and future prospects of a firm. If information is relevant in steering a business, it is also relevant for its investors' investment decisions. Recent initiatives demand information that supplements and complements a firm's financial statements to bridge the gap between financial statement capabilities and financial reporting objectives. Firms that aim to increase the value of their customer base should manage their business by future-oriented customer metrics. They should also report this information externally because it aligns customer management with corporate goals and investors' perspectives. The authors propose a means to report customer equity that enables monitoring firms' performance with respect to their customer assets. Furthermore, they develop a specific model for Netflix and apply it to quarterly reports that cover more than six years.

### Deficiencies of Traditional Financial Reporting

Nowadays, managers and investors are confronted with an overload of information. This mass of information has to support managers running their company and investors in making investment decisions. Although gathering company information is very time consuming, structuring the available information in such a way that it provides value for the company and its investors may prove to be even more difficult. In general, if information is important for managing the business, it must be just as important to investors who want to assess performance and future prospects. Numerous metrics evaluating managers´ performance tend to reflect past performance rather than future performance. As such, they provide limited guidance for long-term oriented management. Current financial statements alone do not provide sufficient information to help investors assess the amounts, timing, and uncertainty of prospective cash receipts. Consider, for example, the profitability analysis in Figure 1 that was done for two consecutive periods evaluating a manager´s performance in a company with contractual relationships, such as a bank, a telecommunications provider and an online retailer. The results clearly indicate that the manager has done an excellent job: all metrics increased substantially and profit rose by more than 30%. So why bother?

The problem is that these profitability metrics are short-term oriented. They mirror this year's results, but do not outline what is likely to happen in the coming years. What is worse, they might even provide incentives for short-term oriented management like reducing advertising spending in order to improve profitability at the expense of diminishing consumers´ awareness and their intention to buy in the future. How can such behavior be avoided?

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We recommend reporting customer equity on an internal and external basis. Customer equity measures the long-term value of a firm's current customer base, which is the discounted profit that a firm will make with their current customers — now and in the future. This idea is illustrated by including the number of acquired and lost customers in our profitability analysis example (see Table 1). This enables the churn rates to be calculated by dividing the number of lost customers by the average number of customers in the given period. The latter is simply the average number of customers at the beginning and end of the respective period. This churn rate increased dramatically by 86.37%. If we consider the first eight rows of Table 1, evaluating whether management has done a good job is quite difficult. Some metric changes are positive, whereas others are negative, yet the overall effect remains unclear.

» Customer equity measures the long-term value of a firm's customer base, which is the discounted profit that a firm will make with their customers — now and in the future. «

Using the available information to estimate an easily applicable model of customer lifetime value (CLV), the present value of all current and future customer profits shows that CLV diminished by 15.89%. Customer equity, here defined as CLV multiplied by the number of customers, also decreased by 7.87% (–$4,602.54). Hence, it would appear this manager has increased the profit margin at the expense of the retention rate. In terms of short-term profit — that is a wise decision, but not in terms of the long-term success of the firm. Instead of congratulating the manager for increasing the current period's profitability by 31.43%, we should ask why he has destroyed so much long-term value.

Enlarging on this example, we would like to stress the importance of tracking future-oriented customer metrics and reporting customer equity internally as well as externally. Customer equity allows for better company management and value creation, but it also tackles the increasing demand for additional information that facilitates investors' decision making. Thereby, we focus particularly on firms with contractual relationships (e.g., Internet service providers, financial service providers, telecommunication firms, energy suppliers, pay-TV broadcasters, online movie rental services), which can easily determine the number of existing and lost customers at a particular point in time.

### Customer Equity Reporting

In general, customer equity reporting should comprise two main elements: the ***Customer Equity Statement*** and the ***Customer Equity Flow Statement.*** The Customer Equity Statement reports customer equity (i.e., the customer base value) and its components in a single, clear display thus revealing the value of the existing customer base. The ***Customer Equity Flow Statement*** describes changes in customer equity and its components between two points in time and reports the influence of any changes in customer metrics on customer equity.

For the specific purpose of reporting, we define customer equity as the sum of the CLVs (after marketing expenditure) of all of the firm's current customers in period 1. CLVs before marketing expenditure result from several customer metrics, such as profit per customer and the duration of a customer's relationship with

*Figure 1:*

## PROFITABILITY ANALYSIS

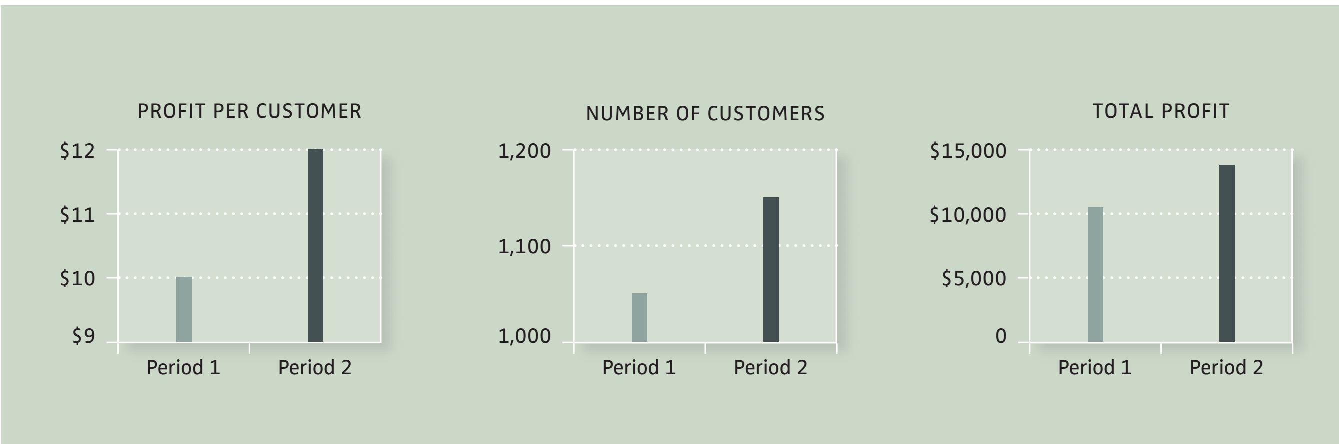


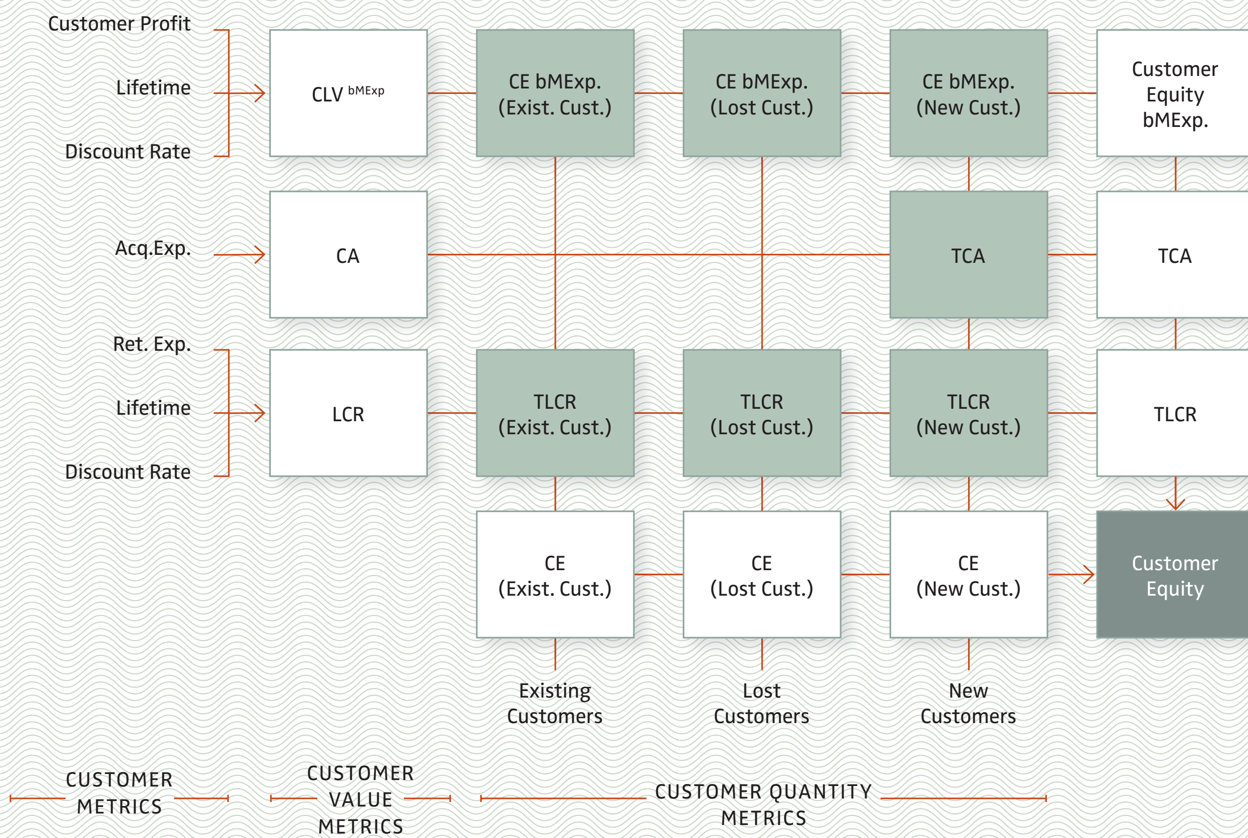

*Table 1:*

## CUSTOMER EQUITY ANALYSIS

| | Period 1 | Period 2 | Change (in %) |
|---|---|---|---|
| Profit per customer (in $) | 10.00 | 12.00 | 20.00 |
| Total profit (in $) | 10,500 | 13,800 | 31.43 |
| Total number of customers, in 1,000 (beginning of period) | 1,000 | 1,050 | 5.00 |
| Total number of customers, in 1,000 (ending of period) | 1,050 | 1,150 | 9.52 |
| Number of acquired customers, in 1,000 (during the period) | 150 | 300 | 100.00 |
| Number of lost customers, in 1,000 (during the period) | 100 | 200 | 100.00 |
| Churn rate (in %) | 9.76 | 18.19 | 86.37 |
| Retention rate (in %) | 90.24 | 81.81 | – 9.34 |
| Customer lifetime value (in $) | 55.67 | 46.83 | – 15.89 |
| Customer equity (in K$) | 58,451 | 53,848 | – 7.87 |
| Change in customer equity (in K$) | | – 4,602 | |

*Figure 2:*

CUSTOMER EQUITY BREAKDOWN




Acq. Exp.: Acquisition Expenditure, CE: Customer Equity, $CLV^{bMExp}$: Customer Lifetime Value before Marketing Expenditure, CA: Acquisition Expenditure, LCR: Lifetime Retention Expenditure, MExp.: Marketing Expenditure, TCA: Lifetime Acquisition Expenditure, TLCR: Total Lifetime Retention Expenditure

the company known as customer lifetime. To retain or acquire customers, a firm must invest money; the measures of retention and acquisition costs per customer reflect those investments. Combining customer metrics with an appropriate discount rate provides a calculation of the present value of all profits of a customer (CLV before marketing expenditure) and the present value of all costs necessary for retaining a customer (lifetime retention expenditure). These metrics are labeled as customer value metrics because they determine the value of a particular customer. Altogether, they determine each customer's CLV after marketing expenditure. For simplicity´s sake, we do not distinguish between different segments of customers in this paper, but the requirements for doing so are fairly straightforward.

The number of customers at the end of a period equals the number of customers at the beginning of a period plus the number of customers acquired minus the number of customers lost. To understand these customer movements, we use the number of existing customers (at the beginning of a period) and the number of new and lost customers (during a period) as customer quantity metrics. Multiplying the CLV of an average customer before marketing expenditure by the number of existing, new, or lost customers provides the corresponding value of existing, new, or lost customers before marketing expenditure. A similar calculation for acquisition and retention expenditures is equally valid. These various combinations of customer value and quantity metrics provide several different components of customer equity. As illustrated in Figure 2, customer equity can be broken down according to the various kinds of customers (existing, new, or lost) or the value components, which is the net present value of customer cash flows, retention expenditure, and acquisition expenditure.

**Application: The Netflix Case**

**Objectives**

Our reporting technique is applied to Netflix.com. Netflix.com's principal activity is to provide online movie rental services through access to more than 55,000 movies, television, and other entertainment titles. The standard subscription plan gives customers up to three titles at the same time with no due dates, late fees, or shipping charges. Shipping and receiving centers throughout the United States deliver the DVDs through the U.S. Postal Service free of charge to customers. We use publicly available, quarterly data from annual reports, 10-K and 10-Q statements, and other company reports from September 2001 – September 2006. The data for each quarter include the number of customers, average monthly churn rate, gross subscriber additions, subscription revenue, subscription costs of revenue, operating expenses (without marketing expenditure), acquisition cost per customer and marketing expenditure.

This information enables us to calculate the necessary customer metrics (see Table 2). The company provides no information about its discount rate, so we chose an annual discount rate of 10% (the quarterly discount rate amounts to 2.41%).

We use Figure 3 to illustrate the value and changes of customer metrics over a certain period of time. On the positive side, Netflix.com increased its number of customers and its retention rate, as well as the profit per customer in 2006 after suffering a drop in 2005. However, its acquisition expenditures increased. Therefore, these measures do not provide a clear picture of the overall value of the customer base.

We select a tight-fisted, easily applicable CLV specification. Based on this formulation, Figure 4 depicts Netflix.com's Customer Equity Statement for Q3 2006. Customer equity yields \$358.56 million in Q3 2006, according to the customer equity without marketing expenditure for existing customers (\$381.54 million), lost customers (–\$60.30 million), new customers (\$96.69 million), and total lifetime acquisition expenditure ( \$59.37 million). Because all Netflix.com´s marketing expenditure is for acquiring new customers, the total lifetime retention expenditure is always zero. We also show the breakdown according to groups of new, lost and existing customers in Figure 4.

» Customer equity reporting matches financial reporting criteria. It enables investors, creditors, and other ''consumers'' of financial reports to clearly understand the firm's capability to generate shareholder value. «

The Customer Equity Statement monitors customer equity over a given period of time. Therefore, it provides information about the value of the customer base and its components as well as an illustrative overview of customer metrics. However, it does not indicate the sources of change in customer equity over a certain period of time. It would enhance any analysis by giving insights into how much the value of the customer base has changed due to whichever metric. More detailed statements about the firm's customer management activities appear in the Customer Equity Flow Statement.

**Netflix.com's Customer Equity Flow Statement**

Following on from Figure 4, we develop Figure 5 to depict Netflix.com's total change in customer equity, its components and its customer metrics in Q2–Q3 2006. Customer equity changed by \$48.10 million, which reflects a shift in customer equity before marketing expenditure of \$60.44 million and a change in total lifetime acquisition expenditure of –\$12.34 million (i.e., total lifetime acquisition expenditure increase). The change in customer equity before marketing expenditure comprises three components: change in customer equity before marketing expenditure of existing customers (\$45.01 million), lost customers (–\$7.26 million) and new customers (\$22.69 million).

*Table 2:*

## CALCULATION OF CUSTOMER METRICS

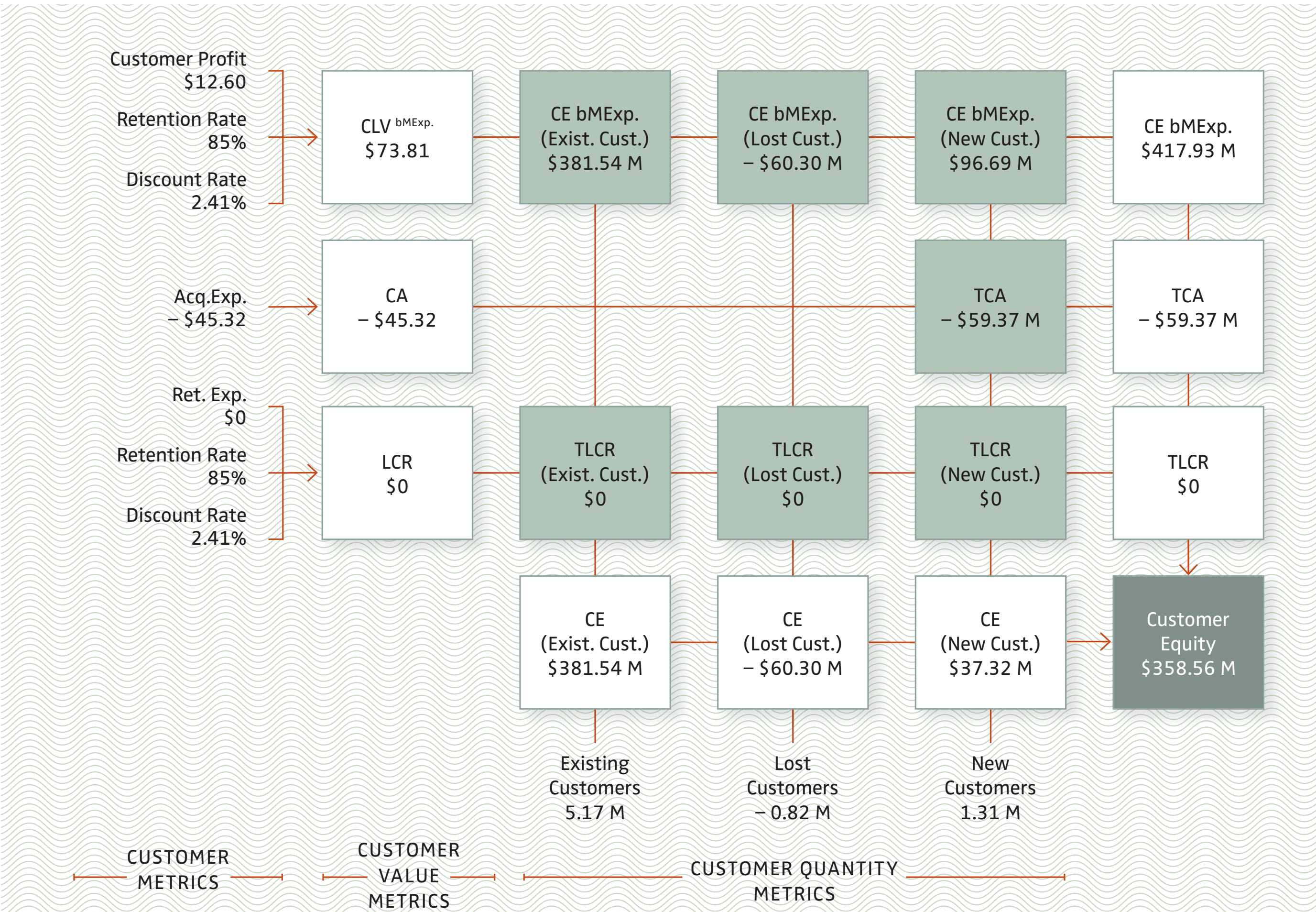
| | Calculation Method or Data Source | Q4 2005 | Q1 2006 | Q2 2006 | Q3 2006 |
|---|---|---|---|---|---|
| **Number of customers (in thousands)** | Reported number of customers per quarter (source: financial statements) | 4,179 | 4,866 | 5,169 | 5,662 |
| **Number of new customers (in thousands)** | Reported number of gross subscribers additions (source: financial statements) | 1,156 | 1,377 | 1,070 | 1,310 |
| **Number of lost customers (in thousands)** | Difference in number of customers between the current and the previous quarter + number of gross additions in the current quarter | 569 | 690 | 767 | 817 |
| **Quarterly profit per customer (in $)** | (Subscription revenue – subscription cost of revenue – operating expenses without marketing) / number of customers | 9.97 | 10.84 | 11.87 | 12.60 |
| **Retention rate** | 1 – (number of lost customers during quarter / [number of customers at the beginning of quarter + number of customers at the end of quarter] / 2) | 0.83 | 0.84 | 0.85 | 0.85 |
| **Retention expenditure per customer (in $)** | (Reported marketing expenditure – reported acquisition cost per customer × number of new customers) / (number of customers – number of new customers) | 0.00 | 0.00 | 0.00 | 0.00 |
| **Acquisition expenditure per customer (in $)** | Reported acquisition cost per customer (source: financial statements) | 38.08 | 38.47 | 43.95 | 45.32 |

*Figure 3:*

DEVELOPMENT OF CUSTOMER METRICS OVER A CERTAIN PERIOD OF TIME

*Figure 4:*

NETFLIX.COM'S CUSTOMER EQUITY STATEMENT (Q3 2006)



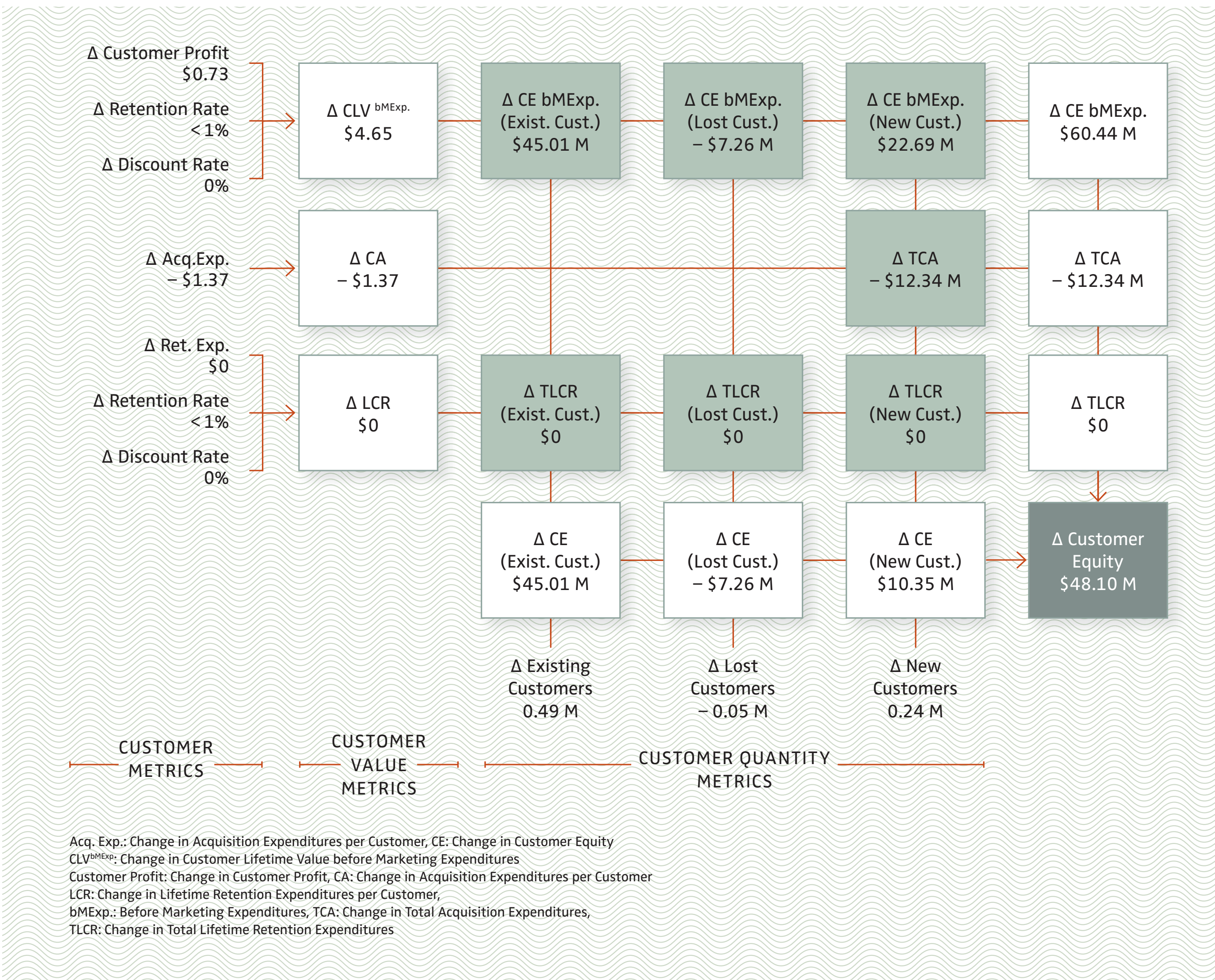

Acq. Exp.: Acquisition Expenditures per Customer, CE: Customer Equity, $CLV^{bMExp}$: Customer Lifetime Value before Marketing Expenditures, CA: Acquisition Expenditures per Customer, LCR: Lifetime Retention Expenditures per Customer, MExp.: Marketing Expenditures, TCA: Total Lifetime Acquisition Expenditures, TLCR: Total Lifetime Retention Expenditures, bMExp.: Before Marketing Expenditures

Furthermore, Figure 5 indicates the changes in customer metrics, customer value metrics, and customer quantity metrics, thus summarizing what has happened during this period and the future-oriented effects of those changes, for example, in customer equity. Another good example is that Netflix.com increased its existing customers (0.49 million) in Q3 2006, but lost more customers than in Q2 2006 (–0.05 million), yet gained more customers than in Q2 2006 (0.24 million). Therefore, it increased the value of the whole customer base, primarily because its average profit per customer ($0.73) rose during that period.

In addition to breaking down changes in customer equity for several components, managers and investors might want to know which metrics caused those changes. These results are provided in Table 3, which includes the total effect (total change), value effects (changes due to shifts in customer value metrics), quantity effects (changes due to the number of existing, lost, and new customers) and interaction effects (changes due to simultaneous changes in customer value and quantity metrics).

*Figure 5:*

NETFLIX.COM'S CUSTOMER EQUITY FLOW STATEMENT (Q2–Q3 2006)

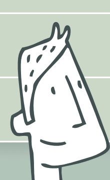



According to Table 3 (next page), the major sources of Netflix.com's increased customer equity in Q2 – Q3 2006 ($48.10 million) are positive value effects ($22.35 million) and quantity effects ($23.22 million), which indicate that Netflix.com boosted the value of its customer base by having more and more valuable customers. Furthermore, the change in profit per customer raised customer equity by $21.98 million, supported by the increase in customer lifetime ($1.84 million) but this was partly compensated for by higher acquisition expenditure (–$1.47 million). The positive interaction effects ($2.53 million) also suggest that the profit per customer and retention rate increases prompt positive customer lifetime value effects for existing and new customers, but also lead to a more negative effect for the lost customers. In order to understand Table 3 better, it also includes trends compared with the previous quarter. These trends show that management has done a good job in reducing the increase of acquisition costs. However, management was not able to sustain the robust increase in profit per customer and customer lifetime value any longer. The value of new customers is still significantly higher than

*Table 3:*

## NETFLIX.COM'S CUSTOMER EQUITY FLOW STATEMENT (Q2 – Q3 2006): EFFECTS VIEW

| In Thousands $ | Q1 – Q2 2006 | Q2 – Q3 2006 | Trend |
|---|---|---|---|
| Total Effect | 63,543.91 | 48,098.98 | ↓ |
| Value effects | 27,342.54 | 22,351.47 | ↓ |
| Customer profit | 28,515.11 | 21,977.91 | ↓ |
| Customer lifetime | 6,373.39 | 1,839.46 | ↓ |
| Acquisition expenditure | – 7,545.96 | – 1,465.90 | ↑ |
| Quantity effects | 32,166.34 | 23,218.85 | ↓ |
| Lost customers | – 47,269.71 | – 56,503.34 | ↓ |
| New customers | 79,436.05 | 79,722.18 | ↑ |
| Interaction effects | 4,035.03 | 2,528.67 | ↓ |
| Lost customers | – 5,664.43 | – 3,782.62 | ↑ |
| Customer profit | – 4,494.67 | – 3,473.78 | ↑ |
| Customer lifetime | – 1,169.75 | – 308.84 | ↑ |
| New customers | 8,949.88 | 6,179.70 | ↓ |
| Customer profit | 6,270.28 | 5,569.95 | ↓ |
| Customer lifetime | 2,679.60 | 609.75 | ↓ |
| Lifetime | | | |
| Customer profit | 1,753.39 | 234.67 | ↓ |
| Other | – 1,003.80 | – 103.08 | ↑ |



the value of lost customers. Yet, management could not continue supporting the growth in new customers, but unfortunately now faces an increase in the value of lost customers. If these trends continue, then management will quickly face a situation in which the value of new and lost customers will be comparable, indicating that management is no longer able to improve growth by the number of customers.

### Conclusions

We emphasize that reporting future-oriented customer metrics assists managers in leading their company and taking strategic decisions as well as helping investors make investment decisions. Therefore, we propose a means to report customer equity that allows for better reflection of a firm´s long-term value creation, which should lead to decisions that are more long-term than short-term value-oriented. It should avoid increasing short-term profits at the expense of long-term value creation. Additionally, customer equity reporting matches financial reporting criteria. It enables investors, creditors, and other ''consumers'' of financial reports to clearly understand the firm's capability to generate shareholder value. In this sense, customer equity reporting faces the demand for additional information that facilitates investors' decision making. Moreover, it contributes to the discussion about marketing accountability and may support marketing's re-entry into the boardroom, because it aligns customer management with corporate goals and the investor's perspective. •

## FURTHER READING

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KEYWORDS:

Customer Management, Customer Equity, Customer Equity Statement, Customer Equity Flow Statement

{ *Pieter Nota* }

#### ABOUT BEIERSDORF AG

Beiersdorf AG is a cosmetics company headquartered in Hamburg, Germany, that employs more than 20,000 people worldwide and that generated sales of €5.748 billion in 2009. The company has been listed in the DAX since December 2008. Its flagship Nivea brand is the world's largest skin and beauty care brand.* Other names in its internationally successful brand portfolio include Eucerin, La Prairie, Labello, 8×4, and Hansaplast / Elastoplast. The affiliate tesa SE is one of the world's leading manufacturers of self-adhesive product and system solutions for industry, trade, and consumers. Beiersdorf has more than 125 years' experience in skin and beauty care and stands for innovative and high-quality products. •

* **Source:** Euromonitor, "Skin and Beauty Care Products excluding Scents and Hair Dyes by Sales, 2008"


#### ABOUT PIETER NOTA

Born 1964 in Wageningen (Netherlands)
Studied business administration in the Netherlands and the USA

*Unilever, Netherlands*
1990 – 1992 Brand Manager
1992 – 1994 Product Group Manager
1994 – 1995 National Account Manager

*Unilever, United Kingdom*
1996 – 1998 Marketing Manager Innovations Europe

*Unilever, Poland*
1998 – 2002 Marketing Director

*Unilever, Germany*
2002 – 2005 Marketing Director

*Beiersdorf AG*
Since 2005 Executive Board Member
Brands: Marketing/R&D/Sales

#### THE INTERVIEWER

This interview was conducted on February 18, 2010 by the Editor-in-Chief, *Professor Hermann Diller*

# MIR TALKS TO PIETER NOTA, EXECUTIVE BOARD MEMBER BEIERSDORF AG

*Interview by Hermann Diller*

Today, it is not enough for Marketing Intelligence services to merely generate insights: it also has to manage them in such a way that they can ultimately result in successful marketing activities. In February 2010, MIR talked about such topics to Pieter Nota, Executive Board Member of Beiersdorf AG, a leading global player within the cosmetics industry. Pieter Nota is responsible for brand leadership of well known brands such as Nivea and Eucerin and he is renowned for his challenging ideas in marketing management.

**MIR:** *Mr. Nota, each industry is faced with specific marketing challenges. Some are focused on innovation, while others concentrate on cost optimization, and others still are heavily affected by the Internet or need to emphasize speed in marketing. How would you describe the key challenges in the personal hygiene and cosmetics industry?*

**NOTA:** In cosmetics, the relevance of innovation is certainly very high. This was true before the crisis, and it still is now, as consumers are very open to the launch of new products and problem solutions when it comes to cosmetics. I'd say it is also very relevant in the area of brand management for big brands to follow the principle of continuity on the one hand, but to stay modern and up-to-date by providing constant innovations on the other. Of course, this is particularly true for our Nivea brand, but also for other brands we produce, like, for instance, Eucerin. We ensure that this recency based on consumer insights and also on new technologies, because it is very important for brands to be cutting-edge technologically.

**MIR:** *You mean the economic crisis has not really caused much change? Perhaps a significant change has occured elsewhere?*

**NOTA:** From my personal perspective, the crisis is over. We have already been living in a so-called new reality for quite some time with continuing economic uncertainty and volatility, moderate market growth and a change in the behavior of retailers. And this new reality basically means a much stronger value orientation on the consumer side.

**MIR:** *Could you explain what you mean by this?*

**NOTA:** Consumers are much more demanding than before, they claim value. This is something that has changed the markets permanently. Before the end of 2008, a great deal happened simply because markets tended to grow in general. Consumers in many parts of the world were always ready to participate in upgradings, and were happy to take higher priced products of an assumed higher value. The stronger value orientation we feel now does not necessarily mean that it has to be dirt cheap, but offers are critically screened for value for money. This is certainly favorable for brands like Nivea, because ''being good value for money'' is exactly how it is positioned in all segments. As a result, we warmly welcome this new trend.

**MIR:** *Presumably, this is different for the Eucerin brand, because Eucerin is probably a premium brand?*

**NOTA:** No, not exactly. Eucerin is distributed in a very different channel. Nivea plays a very important role in the mass market and Eucerin is distributed in pharmacies. And precisely there, advisory skills are very important.

**MIR:** *You mean that consumers are willing to pay a confidence fee when it comes to higher prices?*

**NOTA:** It´s quite interesting: if you rank professional categories according to the confidence they enjoy, then doctors or pharmacists rank very, very highly in contrast to car dealers or politicians, just to name a few examples, who can be found in the lowest section. Naturally, this fact provides strong support for a brand like Eucerin. Compared to the mass market, Eucerin is more highly priced, but this is offset by the much higher value for the consumer, due to its proven efficacy in conjunction with the expert advice of the pharmacist or the recommendation of a doctor.

**MIR:** *This certainly is an interesting aspect. If I may dig deeper here, it means that the trust a brand is able to build up is brand capital which somehow needs to be defined and measured? Do you have specific approaches to this?*

**NOTA:** Yes, of course we very regularly monitor our brands. Key brand values like trust, liability or similar aspects are queried. In this way, we can also clearly see the evolution of brand trust and we know where we need to countersteer or to accelerate. The brand monitor is a really important tool for us. We gain a lot of information on the health of our brand equity.

**MIR:** *Wouldn´t you agree that it might be necessary to open the perspective of market research a bit? To monitor not only brand trust and related constructs, but also, for instance, corporate social responsibility as perceived by consumers?*

**NOTA:** Yes, of course this is very important, but somehow, it needs to be part of the brands. Because ultimately the purchase decision for a brand is made in front of the shelf. Therefore, it is important to accurately measure issues like sustainability within the brand monitor. The results need to be taken seriously by the company.

**MIR:** *Mr. Nota, may I get back to your assessment of premium brands. Do you consider it a general trend that the long lasting and abundant growth of premium brands is approaching its limits?*

**NOTA:** No, for me that's much too sweeping a statement. But there is more of a challenge nowadays. Premium brands were riding on a wave of success between 2002 and 2008, in the sense that wealth itself was growing and consumers were willing to pay more for a certain added value. Now, consumers are clearly more critical. The value orientation is considerably higher. This does not mean that it is impossible to sell premium brands, but a higher price needs to be paired with a clearly evident added value, either functionally and / or emotionally. In any case, I believe that it won´t be so easy any more to sell at a higher price level without an added value that can be easily understood.

**MIR:** *This is why some of your competitors have introduced low priced products to the market, to account for this sort of value orientation. Is this the right way and does Beiersdorf also intend to take this path?*

**NOTA:** ...This is not our way, if you mean low price versions of specific products...

**MIR:** *Yes, for instance, professional hair shampoos, that have lately also been offered as second, low price labels by market leaders.*

**NOTA:** Well yes, they are something like slimmed down versions. Maybe that´s another strategy to gain a share of the low price market. But that is something we would certainly approach differently and it must be handled with care. In particular, you have to make sure not to build potentially schizophrenic brands. In the case of Nivea, we believe that we already have a very strong presence in the mass market, including at mass price level. And we even have a series of lower priced variations, but they are always specific product concepts with a clear difference to the basic product, e.g. Nivea Basic or the like. They are independent product concepts positioned at a lower price level. If you have a look at

» From my perspective, the crisis is over. We have already been living in a so-called new reality for quite some time ...And this new reality basically means a much stronger value orientation on the consumer side. «

Nivea facecare products, for instance, you'll find the ''Nivea Visage'' product line at a fairly high price level. However, the consumer could also use the very different, still good but inexpensive product, ''Nivea Soft.'' This is a product with its own specific concept, and not just a cheap second label for the higher value Nivea Visage line. I consider it very important to have concepts with sufficiently distinct profiles.

**MIR:** *Mr. Nota, let me return to the crisis one more time. Cost pressure is something that really affects every industry, but it seemed to be particularly high in times of crises, because declining volumes had to be compensated somehow. Do you feel such increased cost pressure? How do you handle it and how does it affect marketing intelligence?*

**NOTA:** Of course, there is also some cost pressure in our market environment. But for me it is important not to respond to it with a reduction of marketing investments or by reduced spending for marketing intelligence. I believe that we really stressed this point, to maintain our expenditure.

Naturally, there is potential to increase efficiency here or there, no doubt about that and we are always working on it. We are not naive, and we are very aware that it is absolutely possible to obtain the same output for less money in marketing investments or other marketing intelligence services. In this respect, we have been very successful in some areas in 2009. But it is the output that counts, and we were able to keep the level of media spending as well as marketing-intelligence expenses stable, which means that we kept the services we purchased constant, on a quantity basis at least.

**MIR:** *There is some change going on in terms of Internet use for communication and benefiting from significantly lower CpIs. Does this apply to you, too? Do you take advantage of these "economies of Internet"?*

**NOTA:** Yes, that´s true. However, one cannot just replace media like TV on a 1:1 basis. The Internet has a clearly distinct and different character. But of course, we do use it and the expenses for online activities have reached a significant level. For us, it is no longer a marginal medium. This issue has to be handled very specifically for different target groups. If we look at our product line ''Nivea for Men'' for instance, the Internet plays a very important role, as it is almost impossible to reach young men via TV.

**MIR:** *Mr. Nota, let us now talk about marketing intelligence in more general terms. Have you also observed system changes in many companies, including perhaps in yours, from project based market research towards a more holistic system? This then includes not only secondary market research, some rather classical surveys and continuous panels, but also dashboards including CRM and controlling figures, as well as sales information systems and the like? Is something new and significant emerging in this field?*


**NOTA:** Definitely yes. We have instruments such as dashboards or similar. In addition, we have — and this is fully integrated in our brand monitoring — what we call the brand-funnel. This is the well known cascade from ad and brand awareness up to loyalty. This enables us to precisely measure the position of certain Nivea or other products in a specific category, to see where deficits exist and consequently, where marketing tools need to be applied to ultimately increase the total value. And this is really helpful, because it makes very precise marketing possible, so that the answer is no longer just to pump more money into advertising. Frequently, while I have no problem with brand awareness, I do with considerations associated with purchasing or other behavioral variables. By means of the brand funnel I know which tools are applied most reasonably, and when.

**MIR:** *Who is responsible for the data? Do you have a market research department or how do you organize marketing intelligence?*

**NOTA:** We have a department which we established in its current form in 2008, meaning that it is fairly new. We call it Consumer & Market Intelligence (CMI) and all the competencies are concentrated there, from ongoing market-research, that is basically all the typical panel information from GfK and Nielsen, to the entire management of consumer insights. The major challenge here is to improve consumer insights management permanently, so that we can investigate real insights which are completely different from mere observations.

» … ultimately the purchase decision for a brand is made in front of the shelf. Therefore, it is important to accurately measure issues like sustainability within the brand monitor. «

**MIR:** *How can these responsibilities be mastered?*

**NOTA:** First, market intelligence and insights management is really a top priority. And we are very successful because CMI is directly cross-linked with our innovation management. We have an entire process within our company that starts with consumer insights at the place where the consumer insights are generated. Then they are translated into specific consumer concepts and integrated into the innovation process. We have a very clear role allocation here.

**MIR:** *That is, the value chain of market research has expanded from the mere collection of information into the generation of and transformation into useable insights, which can then be integrated into concepts or innovations?*

**NOTA:** Yes, that is absolutely correct and it is almost the most important service that I expect from a CMI function. That it doesn't just collect data retrospectively, "how has all this evolved," but also generates forward-looking data, therefore real information, consumer insights. This helps us to identify the relevant issues and where we need to provide input stimulations for future innovations.

**MIR:** *Well, I assume this is best accomplished by team work, integrating users or product developers. Who is cooperating with CMI?*

**NOTA:** Directly in CMI, we have a sort of account management, where specific personnel are assigned to the international marketing teams they serve, and who in turn are in direct contact with our R&D people. CMI itself is a relatively compact department, in charge of insight management, but it provides extremely important services to international marketing units and also to R&D.

**MIR:** *That´s also interesting for personnel development. Such people cannot be hired off campus most likely. Presumably, they do not yet have the experience needed. How do you find the right people for these tasks, or how can they be developed to be giving them the capability to generate such insights? Are they originally from product management?*

**NOTA:** It varies greatly. They might come from product management, but personnel with a technical background might also be suitable. However, they tend to mostly be from product management.

**MIR:** *You mentioned that your insights always have to be of international use, because of the global presence of Beiersdorf. Are there something like homogenous consumer insights which are valid for the whole world, or is it necessary to differentiate heavily, for instance, between developments in Europe and Asia?*

**NOTA:** We differentiate very much and insights are very different for each region. The responsibility for generating insights is clearly located at the level of the respective markets, rather than in our CMI department itself. In addition, we use local experts in specific countries to generate insights. They deliver their data to a specific unit in Hamburg and there clustering is applied. You can see that the insight generation is really very close to the market.

**MIR:** *Basically you use a local organizational structure for insights generation and central organization for implementation?*

**NOTA:** Yes, the generation of insight is very, very local, that´s correct.

**MIR:** *…and its implementation rather central?*

**NOTA:** Yes. The insights are concentrated in a central unit and when it comes to using the insights for specific concept developments or innovation as well as communication concepts the implementation takes place centrally. After all, in marketing or R&D, we cannot work with hundreds of different projects. That´s why we use clusters based on importance, potential and critical mass.

**MIR:** *Do you keep a central database to store such knowledge? Is it correct to talk of knowledge management in this field?*

**NOTA:** That´s exactly what we have.

**MIR:** *And it is, if I can put it like this, "loaded" globally?*

**NOTA:** Yes, indeed, from different regions of the world.

**MIR:** *And you also have experience of how marketing works in different regions. Do you document these experiences?*

**NOTA:** Absolutely! We coordinate that explicitly.

**MIR:** *Let us return to the role of controlling once more. I would assume that you compare efficiency and effectiveness of marketing in different regions and that strengths and weaknesses can be derived and lessons be learned. Do you practice this systematically?*

**NOTA:** Yes, we have a system here, that we call MSE — Marketing Spend Efficiency. It is part of our annual planning process, where the efficiency of our marketing spending is challenged and where people are explicitly prompted to look into the allocation of different marketing investments.

A range of variables, such as competition, innovation pipeline etc. are integrated here and, of course, some strategic priorities concerning portfolios as well. This is part and parcel of our annual planning.

**MIR:** *I see. And a crucial element of knowledge also refers to the retail market?*

**NOTA:** Yes.

**MIR:** *But this knowledge is often located more in sales and less in the product management scene in marketing. How do you succeed in nailing down specific retail insights and to develop sound and impactful vertical strategies?*

**NOTA:** Well, the CMI department not only has stewardship for collecting well structured consumer insights, but also for what we call shopper insights. We clearly differentiate between these two. For instance, consumer insights are a question of: if I use a product as a consumer, e.g. at home, a certain cream, what are my needs, what are the products that are important to me and how can Beiersdorf respond. Shopper insights, on the other hand, are engaged in questions like consumer shopping behavior, or how points of purchase are selected, e.g. if drugstores, supermarkets or pharmacies are preferred for certain products. It goes down to the level of the point of orientation within a shelf. That´s how we understand shopper insights, and here, we also build on the competencies of our key account managers with their insights concerning retailer behavior.

**MIR:** *More and more consumer goods companies have aimed to establish direct contact with their ultimate consumers, even if it means millions, in your case maybe even billions. Would you confirm this observation? What does it mean for marketing intelligence?*

**NOTA:** Yes, we agree and that is why it is important to talk about CRM tools. But sometimes, it is also quite crucial to break new ground, as we have done, for instance, with our ''Nivea House'' to render possible a real brand experience for the consumer. Of course, we also try to establish direct contact with individual customers there.

**MIR:** *Has this flagship store concept with several hundred square meters of sales floor in a prime city location for nothing but Nivea products proved its value? Is it efficient?*

**NOTA:** Yes, in Hamburg we have almost 800 square meters and this certainly is a real flagship store. In Berlin, we have a smaller, reduced concept that holds its ground very well. Right now, we are testing possible limits and it is our clear objective to make such concepts profitable. Even if we also see it as a marketing tool in part, we are definitely aiming for profitability. And we are absolutely sure that it is possible.

» Now, consumers are clearly more critical. A higher price needs to be paired with a clearly evident added value, either functionally and / or emotionally. «

» Market research definitely plays an important role in innovation management, but it couldn't take over the wheel. It's the people who decide, the managers who are in charge, and not the research tools of the market researchers. «

**MIR:** *Do you plan an international roll-out?*

**NOTA:** We are still testing here, and at the moment, we only have 3 stores of this kind worldwide.

**MIR:** *But you have thousands of products, if I may broach this subject a little. Your range of products has surely grown enormously during the last 20 years. What does this mean for your marketing intelligence system? If I imagine an actual product report you receive, it might well encompass a thousand pages? This hardly seems feasible. How can you handle it?*

**NOTA:** Certainly, there are product clusters, and there are only several hundred, not thousands of products. It is still possible to keep an overview. I believe the actual question is: how can I make sure that consumers do not get lost? And that is also where consumer marketing intelligence becomes relevant. This really is extremely important and ranges from the question: how can I help him or her at the shelf and, how can shelf navigation be designed to be as good as possible up to the point of managing the overall impression of a specific category, how is it seen, what is optimum in terms of the whole category? And at times you can see that less can actually be more! In this respect, we constantly subject what might be the best assortment within a category to very stringent screening.

**MIR:** *Mr. Nota, finally and in conclusion, a question to summarize: how would you estimate the contribution of your marketing intelligence systems to the great success of the Nivea brand?*

**NOTA:** This is really hard to quantify. I cannot just give you a number for that. But from a qualitative point of view, it is indispensable that we keep up with our consumers. And that is where marketing intelligence certainly helps. Eventually, you have to generate real insights and this becomes increasingly important. However, in the end final decisions are made by product managers with a great deal of experience in branding. Market research definitely plays an important role in innovation management, but it couldn't take over the wheel. It´s the people who decide, the managers who are in charge, and not the research tools of the market researchers.

**MIR:** *But one could still say that today customer insight management constitutes an indispensable part of the business model of the consumer goods industry?*

**NOTA:** Absolutely, that´s right. It would be hard to imagine the success of the major brands without it.

**MIR:** *Thank you very much and keep up the good work in marketing and marketing intelligence!* •

{*Deutsche Zusammenfassung*}

# Gut für andere, gut für mich: PRODUKTWERBUNG KOMBINIERT MIT SOZIALEM ENGAGEMENT: WARUM SIE WIRKT UND WIE SIE FUNKTIONIERT

***Ty Henderson und Neeraj Arora***

Immer mehr Marken verbinden ihr eigentliches Geschäft mit der Unterstützung sozialer Anliegen. In der Marketingfachsprache wird dieser Trend als Cause Related Marketing bezeichnet und resultiert aus der zunehmenden Diskussion um die soziale Verantwortung von Unternehmen. Im vorliegenden Beitrag wird die Wirksamkeit von einzelnen Werbekampagnen untersucht, bei denen ein deklarierter Teil des Kaufpreises einem sozialen Zweck zugeführt wird. Die Autoren bezeichnen diese Form des Cause Related Marketing als „embedded premium" (EP).

Anhand der Ergebnisse von drei Untersuchungen konnten die Autoren zahlreiche interessante Erkenntnisse zu dieser Form der Produktwerbung gewinnen.

1) EPs funktionieren. Allein das Vorhandensein einer EP erhöht die Entscheidungswahrscheinlichkeit für das entsprechende Produkt. Unbekanntere Marken profitieren stärker von EPs als gut etablierte Marken, da positive EP-Assoziationen die Qualitätswahrnehmung des unbekannteren Produktes stärker unterstützen (bei bekannten Marken ist die Qualitätsanmutung im Regelfall bereits etabliert).

2) Die Höhe des Sozialbeitrags ist fast nebensächlich. Bereits kleine Beträge zeigen Wirkung und diese verändert sich nicht wesentlich durch die Erhöhung des Betrags. Bei kleinen Beträgen wirken EPs besser als z. B. Rabatte oder Preisreduktionen in gleicher Höhe.

3) Die Wahrscheinlichkeit, durch eine EP neue Kunden zu gewinnen, ist höher, wenn die Markenloyalität zu den etablierten Marken niedrig ist. Im Gegensatz zu herkömmlichen Promotions scheinen EP-Kampagnen aber die Kunden preisunempfindlicher zu machen. Qualitätsaspekte werden bei der Entscheidungsfindung stärker mit einbezogen.

4) Positive Wirkungen hat eine Wahloption für den Verwendungszweck. Wenn die Kunden aktiv bestimmen können, welche Angelegenheit unterstützt werden soll, ist die Wirkung der EP deutlich besser. Das Anbieten mehrerer sozialer Anliegen „als Bündel" ohne direkte Beeinflussbarkeit durch den Kunden verbessert hingegen die Wirkung nicht.

5) Bei der Wahloption zwischen einer als signifikant wahrgenommenen Preisreduktion und einer EP-Strategie zeigt sich zwar, dass 80 % die Ersparnis lieber selbst genießen. Aber ein Segment von immerhin ca. 20 % entscheidet sich altruistisch für die EP-Promotion mit Auswahlmöglichkeit in Bezug auf den sozialen Zweck.

Zusammengefasst können EPs als effektives Marketinginstrument betrachtet werden, das nicht nur die Verkaufszahlen steigert, sondern auch die Wahrnehmung von Marken ändern kann. Der positive Nebeneffekt liegt darin, dass zusätzlich zur Organisation selbst auch noch soziale Einrichtungen davon profitieren. •

***Den ausführlichen Artikel in englischer Sprache (mit zahlreichen Links zu Beispielen) finden Sie auf Seite …***

… 8.


*Schlüsselbegriffe:*
***Produktwerbung, Preisreduktionen, Cause Related Marketing, Sozialaktionen***

*{Deutsche Zusammenfassung}*

# Alle Kunden sind gleich, aber manche sind gleicher
## LOHNT SICH DIE PRIORISIERUNG WERTVOLLER KUNDEN?

***Christian Homburg, Dirk Totzek und Mathias Droll***

In der Theorie des Kundenmanagements wird häufig die Forderung erhoben, wertvollen Kunden größere Aufmerksamkeit zu schenken und sie intensiver zu betreuen als weniger wertvolle. Unternehmen sollen also eine Strategie der Kundenpriorisierung verfolgen, anstatt weiter eine Marktbearbeitung nach dem Gießkannenprinzip zu betreiben. Dadurch könnten erstens Marketingkosten eingespart und zweitens größere Kundenpotenziale erschlossen werden. Dabei bleibt allerdings meist die dunkle Seite einer solchen Kundenpriorisierung unberücksichtigt. Sie liegt darin, dass sich die weniger gut betreuten Kunden u. U. vernachlässigt fühlen, unzufriedener werden und entsprechend geringere Loyalität entwickeln sowie weniger Weiterempfehlungen generieren.

Die Autoren überprüften die positiven und die negativen Effekte einer Kundenpriorisierung anhand einer Befragung von 310 Geschäftseinheiten aus Firmen ganz unterschiedlicher Industrie- und Dienstleistungsbranchen in Deutschland und validierten die Ergebnisse zusätzlich durch eine Kundenbefragung. Durch Konzipierung eines Itemkatalogs zur Messung des Ausmaßes der Kundenpriorisierung (vgl. Tab. 1, Seite 19) und durch Schätzung von Strukturgleichungsmodellen gelang es, die Marketingerfolge der stark priorisierenden Firmen mit denen der schwach priorisierenden Firmen zu vergleichen. Darüber hinaus konnte die moderierende Wirkung der Implementationsstärke einer solchen Priorisierungsstrategie offengelegt werden.

Die Ergebnisse der Studie bestätigen die These der gewinnsteigernden Wirkung der Kundenpriorisierung nachdrücklich. Sie kommt durch einen höheren Durchschnittsumsatz pro Kunde zustande, der wiederum von der höheren Kundenzufriedenheit, -loyalität und -durchdringung getrieben wird. Darüber hinaus sinken die Marketing- und Vertriebskosten. Insgesamt kommt es dadurch zu einem beträchtlichen Profitabilitätsvorteil gegenüber jenen Firmen, die ihre Kunden relativ gleichmäßig, d. h. nach dem Gießkannenprinzip, betreuen (vgl. Abb. 2, Seite 21).

Interessanterweise gelingt es aber nicht allen befragten Unternehmen gleich gut, eine Kundenpriorisierung tatsächlich zu implementieren. 80 % aller befragten Firmen verfolgen zwar diese Strategie, aber nur 40 % vermögen sie entsprechend dem von den Autoren eingesetzten Messsystem (voll) umzusetzen. Auf der Suche nach den Voraussetzungen für eine erfolgreiche Umsetzung entdecken die Autoren folgende Einflussgrößen, welche die profitabilitätssteigernde Wirkung der Kundenpriorisierung moderieren und damit entsprechende Ansatzpunkte für das Management bieten:

1) die Fähigkeit zur Messung der individuellen Kundenprofitabilitäten
2) die Qualität des Kundeninformationssystems
3) die gesonderte organisatorische Betreuung der besonders wertvollen Kunden (Key-Account-Management)
4) der Einsatz von Mitarbeitern aus dem Top-Management zur Betreuung der besonders wertvollen Kunden
5) der differenzierte Feinheitsgrad der kundenspezifischen Planung und Kontrolle
6) der Einsatz von Incentive-Systemen zur Unterstützung der Priorisierung (vgl. Abb. 3, Seite 22)

Der Erfolg einer Kundenpriorisierungsstrategie kommt demnach nicht von selbst, vielmehr muss diese durch die genannten Maßnahmen flankiert werden. •

***Den ausführlichen Artikel in englischer Sprache finden Sie auf Seite …***

… 16.


*Schlüsselbegriffe:*
***CRM, Beziehungsmanagement, Salesmanagement, Kundenmanagement***

{*Deutsche Zusammenfassung*}

# Willst du mein „Freund" werden?
## DER WERT VON MUNDPROPAGANDA IN ONLINE-COMMUNITYS

***Michael Trusov, Randolph E. Bucklin und Koen Pauwels***

Das Generieren von Mundpropaganda (WOM, vom englischen "word-of-mouth") via E-Mail oder Internet gewinnt im Kommunikationsmix vieler Branchen immer größere Bedeutung. Prototypisch ist die inzwischen weitverbreitete Nutzung sogenannter Social Websites wie XING oder Facebook, die von ihren Mitgliedern vor allem zum Social Networking benutzt werden. Hier bieten sich gewaltige Chancen zur rasanten Ausbreitung von Botschaften. Im Juni 2009 generierte z. B. die weltweit größte Social Website Facebook 122 Millionen Besucher (unique visitors) pro Monat. Diese enorme Besucherfrequenz fordert geradezu Werbeaktivitäten heraus. Zu vergleichsweise geringen Kosten kann eine starke Verbreitung der Botschaften bei einem geringeren Widerstand der Zielpersonen enorme Erfolge erzielen.

Die Autoren berichten über eine Studie zusammen mit einem Social-Website-Unternehmen. Über 36 Wochen hinweg wurden täglich Daten über die Registrierung neuer Mitglieder einerseits und Einladungen zur Registrierung durch bestehende Teilnehmer sowie einschlägige Marketingevents und Mediaaktivitäten andererseits gesammelt. Die Daten wurden auf aggregiertem Niveau mittels eines autoregressiven Schätzmodells ausgewertet, welches die dynamischen Systemzusammenhänge abbildet (vgl. Abb. 3, Seite 29).

Die in Abb. 4 (Seite 30) wiedergegebenen Schätzfunktionen zeigen, dass der Effekt eines einmaligen Anstiegs von Mundpropaganda drei Wochen lang Wirkung auf die Neukundeneinschreibungen zeitigt, während diese Effekte bei Mediawerbung bzw. bei Promotions innerhalb weniger Tage verschwinden. Klassische Werbekampagnen zeigen nach acht Tagen zeitweilig sogar ein negatives Ergebnis, da lediglich vorgezogene Neukundeneffekte zu beobachten sind. Im Vergleich zu den herkömmlichen Marketingaktivitäten erzeugen WOM-Empfehlungen sowohl einen größeren kurzfristigen Erfolg als auch einen deutlich längeren Carry-over-Effekt.

Um Angaben über die Zeitmuster der Effekte zu erhalten, unterscheiden die Autoren die Elastizitäten (also die Verhältnisse der Output- zu den Inputveränderungen) für einen, drei und sieben Tage sowie über den Gesamtzeitraum summiert (vgl. Abb. 5, Seite 31). Die Ein-Tages-Elastizität für WOM beträgt danach 0,068 und ist damit 8,5-mal höher als jene traditioneller Marketingaktivitäten (0,008). Zudem steigt diese Diskrepanz im Zeitablauf. Langfristig gesehen funktionieren WOM-Empfehlungen nach dem Schneeballprinzip, da sich die Anzahl der potenziell Empfehlenden laufend erhöht. Deshalb ist die langfristige Elastizität von WOM-Empfehlungen etwa 20-mal höher als jene für Marketingevents (0,53 vs. 0,026) und 30-mal höher als die Elastizität für Media Aktivitäten (0,53 vs. 0,017)! Das Generieren von WOM erweist sich also als sehr effektiv.

Gemessen an den marktgängigen Erlösen für 1.000 Impressions (CPM) und der Anzahl der Impressions pro Kunde über dessen gesamten kalkulierten Lebenszyklus hinweg lässt sich der ökonomische Wert der durch WOM-Empfehlungen gewonnenen Neukunden berechnen. Unterstellt man 0,40 \$ als CPM, durchschnittlich 130 Impressions pro Monat und Kunde und zwei bis drei Banner pro Seite, kalkulieren die Autoren dafür etwa 13 Cents pro Monat oder ca. 1,50 \$ pro Jahr. Kombiniert mit den berechneten Elastizitäten folgt daraus, dass zehn WOM-Empfehlungen etwa fünf neue Nutzer über durchschnittlich drei Wochen erbringen. Damit berechnet sich der Wert jeder WOM-Empfehlung auf ca. 75 Cent pro Jahr. Wenn jedes Mitglied des Netzwerks zehn neue Mitglieder wirbt, bedeutet das ca. 7,50 \$ für die Firma. Dieser Wert kann als Richtlinie für die Verteilung des Werbebudgets für neue Kunden dienen. Insbesondere gibt dieser Wert darüber Aufschluss, wie viel das Unternehmen in die gezielte Generierung von WOM Empfehlungen (WOM-Kampagne) investieren soll. Naturgemäß sind solche Werte branchenindividuell und müssen an die jeweiligen Verhältnisse angepasst werden. •

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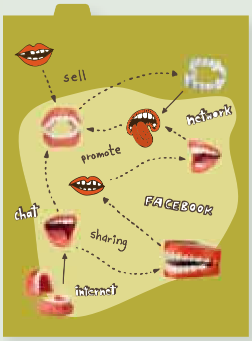
*Schlüsselbegriffe:*
***Mundpropaganda, WOM, Kommunikationsstrategie, Neukundengewinnung***



*{Deutsche Zusammenfassung}*

# Marketing ist Vorstandssache!
## DER EINFLUSS DER MARKETINGABTEILUNG IN UNTERNEHMEN

***Peter C. Verhoef und Peter S. H. Leeflang***

Der Beitrag behandelt den Einfluss der Marketingabteilung in Unternehmen, die Bedeutung eines hohen Einflusses des Marketings und Faktoren, die das unternehmensinterne Standing des Marketings positiv beeinflussen können.

In den letzten Jahren wurde vielfach diskutiert, dass der Einfluss von Marketingabteilungen in Unternehmen abnimmt. Der Tenor lautet, dass Marketing seine strategische Rolle verloren habe und sich stattdessen hauptsächlich mit taktischen Aufgaben wie Werbung, PR oder Verkaufsunterstützung beschäftige. Daraus resultiert, dass Marketingangelegenheiten kaum mehr auf Vorstandsebene diskutiert werden. Marketing wird eher als Kostenfaktor anstatt als Investition gesehen, mögliche Synergien verschiedener Marketingentscheidungen können nicht realisiert werden und der Einfluss von „Pfennigfuchsern und Zahlenschiebern" auf den Vorstand nimmt auf Kosten der Marketingleiter zu. Zudem scheint die Marketingleitung mit einer durchschnittlichen Verbleibdauer von nur knapp 23 Monaten ein Schleudersitz zu sein.

Der Vergleich der Daten einer aktuellen Untersuchung aus den Niederlanden mit einer Studie aus dem Jahr 1999 zeigt, dass der Einfluss des Marketings im Bereich Werbung sowie Kundenzufriedenheitsmessung und -management zugenommen, bei Aufgaben wie der Produktentwicklung, der Strategieentwicklung, der Expansion in neue Märkte oder der Auswahl von Geschäftspartnern aber abgenommen hat. Besonders stark ist der Rückgang des Einflusses beim Pricing und der Distribution. In diesen beiden Gebieten überwiegt der Einfluss des Vertriebs. Generell betrachtet, wird dem Marketing ein nur mittelmäßiger Einfluss bescheinigt. Wenn nach dem Einfluss des Marketings gefragt wird, schätzen dabei die Marketingmanager selbst ihren eigenen Einfluss höher ein als andere Manager im Unternehmen.

Diese Ergebnisse sind bemerkenswert, zumal gleichzeitig in mehreren Studien dokumentiert ist, dass Unternehmen mit starken Marketingbereichen aufgrund ihrer höheren Einflussmöglichkeiten und einer daraus resultierenden stärkeren Marktorientierung bessere Ergebnisse erzielen.

Einige Schlüsselfaktoren spielen eine wichtige Rolle bei der Sicherstellung des Marketingeinflusses.

> Zurechenbarkeit von Ergebnissen: Dabei geht es um die zunehmend gefragte Fähigkeit der Marketingverantwortlichen, ihre eigenen Leistungen messbar zu machen und ihren Einfluss auf die Unternehmensergebnisse zu dokumentieren.
> Innovationsfähigkeit: Sie ist der Motor einer erfolgreichen Unternehmensentwicklung und betrifft die Fähigkeit des Marketings, einen wesentlichen Beitrag zur Entwicklung neuer Produkte zu leisten.
> Kunden-Konnex: Hier geht es um die Fähigkeit, Kundenbedürfnisse aufzuspüren und in Lösungen zu übersetzen, die dem Marktbedarf entsprechen.

Die Untersuchungen haben gezeigt, dass das Marketing im Bereich des Kunden-Konnexes gut abschneidet. Die Innovationsfähigkeit und die Fähigkeit, die Ergebnisse der eigenen Leistungen nachzuweisen, sind dagegen deutlich verbesserbar. Speziell diese beiden Punkte sollten von Marketingverantwortlichen aufgegriffen werden. Dadurch können auch zukünftig ein entsprechendes Standing und ein adäquater Einfluss des Marketings im Unternehmen sichergestellt werden. Das wiederum sollte sich in einer positiven Unternehmensentwicklung niederschlagen. •

***Den ausführlichen Artikel in englischer Sprache finden Sie auf Seite …***

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*Schlüsselbegriffe:*
***Marketingfunktion, Marketingorganisation, Marktorientierung, Marketingfähigkeiten, Marketingführung***

{Deutsche Zusammenfassung}

# Meine Kunden sind besser als deine!
## ÜBER DIE BILANZIERUNG DES KUNDENWERTS

***Thorsten Wiesel, Bernd Skiera und Julian Villanueva***

Manager und Investoren sind heutzutage mit einer Vielzahl von Informationen über die Leistungsfähigkeit von Unternehmen konfrontiert. Diese Informationen sollen Managern bei der Unternehmensführung helfen sowie Investoren bei ihren Investitionsentscheidungen unterstützen. Sicherlich ist bereits die Sammlung der Informationen sehr zeitaufwendig und mit vielen Problemen behaftet; meistens bereitet jedoch die strukturierte Aufarbeitung und Darstellung der Informationen noch mehr Schwierigkeiten. Generell lässt sich feststellen, dass Informationen, die für das Führen von Unternehmen wichtig sind, meistens auch wichtig sind für Investoren, welche die Leistungsfähigkeit und die Zukunftsaussichten beurteilen wollen.

Der Aufsatz präsentiert eine Möglichkeit zur Erfassung des Werts der Kundenbasis für die unternehmensinterne und unternehmensexterne Berichterstattung: das Customer Equity Reporting. Die Grundidee besteht dabei darin, den langfristigen Wert der Kundenbasis zu erfassen und damit die eher kurzfristig orientierten Maße des Jahresabschlusses und des internen Berichtswesens um ein am langfristig zu realisierenden Wert orientiertes Maß zu erweitern. Dabei wird zwischen dem Customer Equity Statement, das den zukünftigen Wert der jetzigen Kundenbasis erfasst, sowie dem Customer Equity Flow Statement, das die Veränderung des Werts der Kundenbasis gegenüber dem Wert der Vorperiode erfasst, unterschieden. Zudem werden unter anderem Veränderungen im durchschnittlichen Wert einzelner Kunden getrennt von Veränderungen in der Anzahl der Kunden betrachtet, um so die Ursachen für die Veränderungen im Wert der Kundenbasis besser zu erkennen.

Die Anwendung des Konzepts wird anhand von Zahlenbeispielen und der Bewertung der Kundenbasis des Unternehmens Netflix in den Jahren 2001 bis 2006 illustriert. Deutlich wird dabei, dass Customer Equity Reporting Veränderungen im Wert der Kundenbasis sehr gut und einfach erfasst. Vorteilhaft ist dabei vor allem, dass der Gesamteffekt gegenläufiger Entwicklungen (z. B. eine Erhöhung der Anzahl der Kunden bei gleichzeitig verringerter Marge) durch das Ermitteln einer einzigen Kennzahl ermöglicht wird und gleichzeitig der isolierte Effekt einer Veränderung ermittelt werden kann. Das Management erhält so einen Anreiz zu einer am langfristigen Wert ausgerichteten Unternehmenspolitik. •

***Den ausführlichen Artikel in englischer Sprache finden Sie auf Seite …***

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*Schlüsselbegriffe:*
***Kundenmanagement, Kundenwert, Kundenwertbilanzierung***

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## ERRATUM

We apologize for citing two authors in MIR issue 2 incorrectly in two places. The article "Implementing Profitability Through A Customer Lifetime Value Management Framework," is authored by V. Kumar, R. Venkatesan and B. Rajan. D. Beckmann did not contribute to this version.

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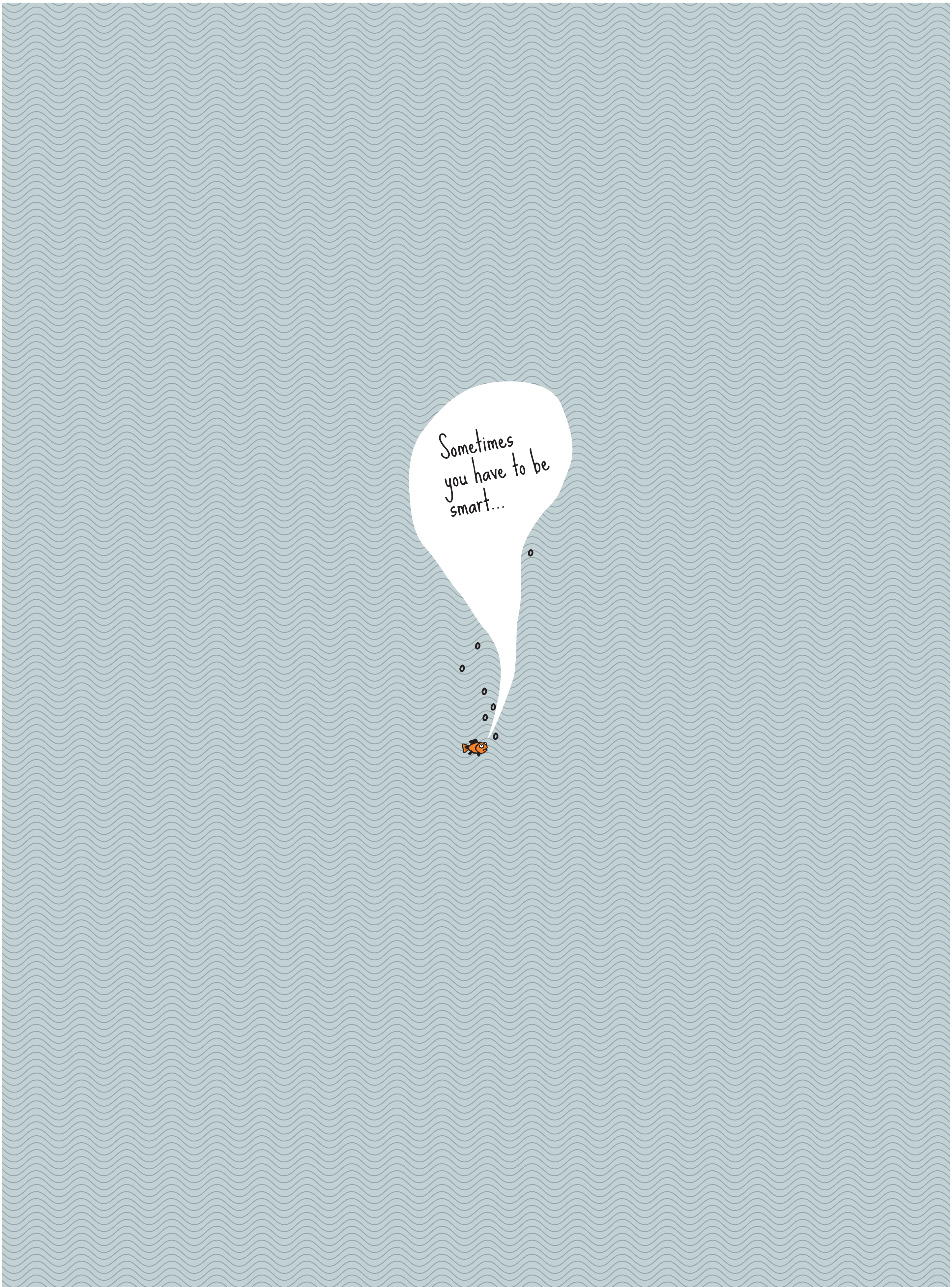
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