Quality Marketing: Making Marketing More Strategic

While most marketers are measuring something, survey results indicate there is room for improvement regarding metrics and the quality of these metrics. Many companies are investing more resources, both people and money into marketing performance measurement. IDC's study, "Planning Your 2006 Marketing Budget" released in September, indicated that over the next 12 months, 38% of the 95 companies participating in the study plan to deploy measurement processes. This undertaking will require new skills and capabilities which explains why 12% of these companies plan to launch new marketing operations teams or roles to address marketing performance management. Consider Elana Anderson, a principal analyst at Forrester Research earlier in 2005 said, "Marketing must improve its value to justify its existence as a centralized function." If we don't make our case and develop and communicate quality metrics, we may find the days of marketing as a stand alone department numbered and instead find ourselves absorbed into sales, finance, or some other function.
It's not like this is new phenomenon. The concept of measuring marketing has been around for a long time. The question is what metrics and how to measure them. In 2001, James Gregory's article in the Journal of Brand Management shared a proprietary model that linked various financial factors and corporate image to stock prices, sales and market share. Our own research at VisionEdge Marketing has found that most companies fail to measure such things as cost to acquire, order value, share of wallet, churn rate or brand equity, and key business variables marketing impacts. Rather they measure such things as response rate, demo participation, event traffic, number of new contacts or leads, number of press hits, cost per lead, and lead aging. While these metrics offer some insight into the results of specific programs, they do not link marketing to the business objectives. In fact our studies indicate that only about one in four marketers measure marketing's impact on the business and nearly two thirds of marketing plans do not even include metrics.

A Metrics Framework

Forrester Research, Marketing Management Analytics and the Association of National Advertisers conducted an online survey in the first half of 2005 to find out how marketing professionals leverage marketing analytics. Fifty percent of the respondents indicated that measurement remains the hardest part of marketing and 51% are dissatisfied with how they measure marketing ROI. Yet nearly all of the respondents realize measuring marketing is important and impacts senior management's confidence in the marketing personnel and programs.

To make progress on the marketing measurement front, marketing professionals must shift from tactically based metrics to metrics that are more linked to business outcomes. The measures must include both financial and non-financial goals. The figure below illustrates the continuum of marketing metrics and how marketing metrics are evolving.
(insert graphic "patterson-metrics.ai")

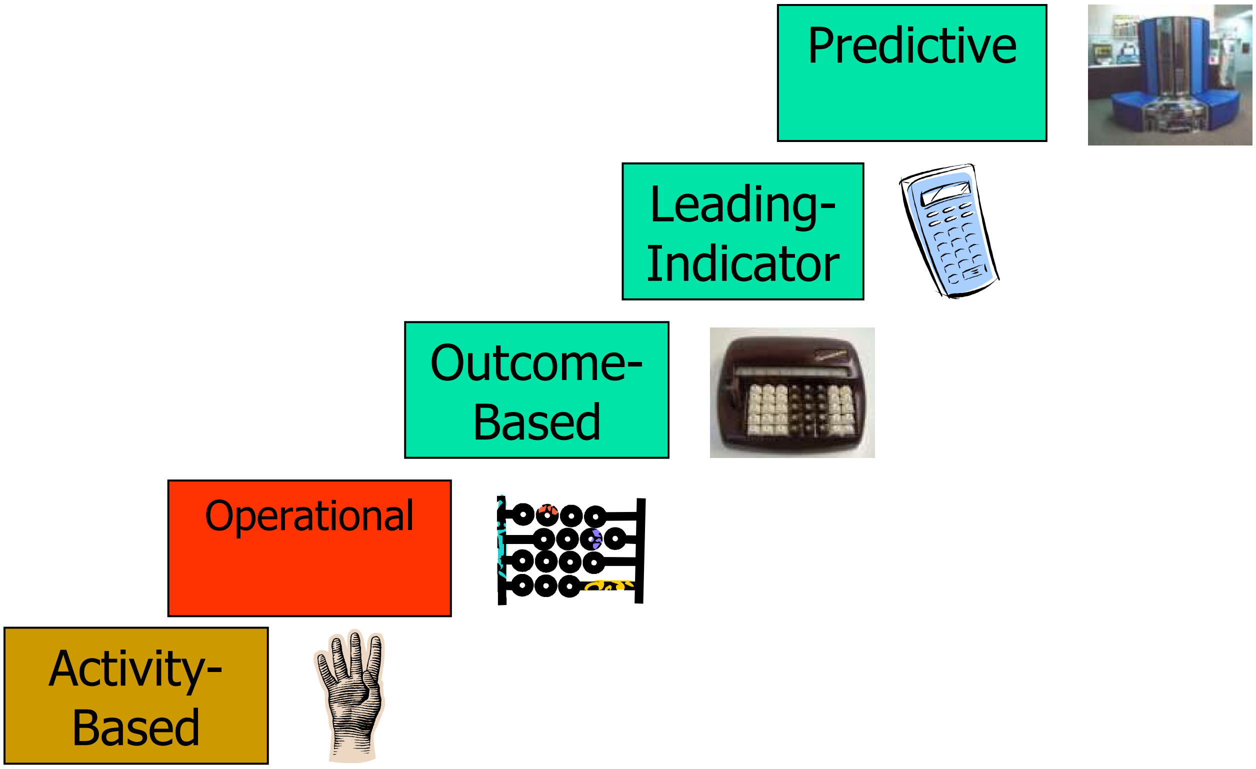

Figure 1: The Metrics Continuum: From Tactical to Strategic

Starting at the bottom left and working up and to the right, we can use this illustration as a framework to explore how marketing metrics are evolving from tactical to strategic. Activity-based metrics refer to those things we can count. This was marketing's first foray into the world of measuring – looking for things we could count, such as press hits, click through rates, CPMs (cost per thousand), and so-on. Most marketing plans today consist of activity lists, such as the number of ads to run, the number of tradeshows to attend, the number of new product brochures to produce, the number of research studies to conduct and so on. Marketing then reports on the status of these activities, sometimes in very creative ways such as red to indicate incomplete or in jeopardy and green to communicate completion or on track. These are then turned into charts in an attempt to present the marketing dashboard. Yet with activity-based metrics all we have is a colorful status report and no information on the impact of these activities on the business. The company cannot make any key business decisions or determine whether strategies are working.

Operational metrics, the next level, is a step forward. These metrics focus on improving the efficiency of the organization. Typical metrics in this stage include cost-per-lead, lead aging, leads-per-sales rep, campaign ROI (return on investment). The goal is to squeeze out any inefficiency. While this is a noble pursuit and an important one, marketing efficiency alone will not make a company successful. What really "moves the needle" in terms of business performance is how well its marketing identifies product opportunities, positions these products, builds market traction against the competition, and fosters customer loyalty. Performance outweighs efficiency.

Once we accomplish a systematic approach to Outcome-based Metrics we will have the basis for advancing to Leading Indicator Metrics, those metrics that help us determine the likelihood of a particular outcome and eventually creative models to use metrics to predict outcomes. And once we've mastered Leading Indicator Metrics, we're only a few financial models away from Predictive Metrics, those that allow us to predict a business outcome.

Both activity-based and operational metrics are a good place to start but neither serves as an accurate indicator of strategic effectiveness. Neither enable the organization to determine which efforts are having the greatest impact, provide a quality control process, focus on marketing's contribution to the company's overall valuation, or serve as a good way to demonstrate marketing's accountability. To address these marketing executives and professionals need to evolve to outcome-based metrics to develop quality measures. Outcome-based metrics focus on three specific business outcomes: market share, lifetime value, and brand equity.

The Role of Marketing in Business Outcomes

Phil Kotler in his book, *Kotler on Marketing* (1999) claimed that "Marketing has the main responsibility for achieving profitable revenue growth for the company (pg 18)." We do this by finding, keeping and growing profitable customers. Finding, keeping and growing profitable customers form the basis of marketing's role: Customer acquisition, customer penetration, and growing customer value. Each of these can be squarely aligned with three specific business outcomes as illustrated in the next figure: market share, lifetime value, and brand equity.

What company doesn't want to see each of these continue to improve over time? Most every company wants to be a dominant player in its market, however that market is defined. Most every company wants to retain its customers and increase their lifetime value. And ultimately, most every company whether private or public wants to increase its shareholder value. This depends on high brand equity. The higher the brand equity the greater the shareholder value. (insert graphic: patterson-marketing.ai)

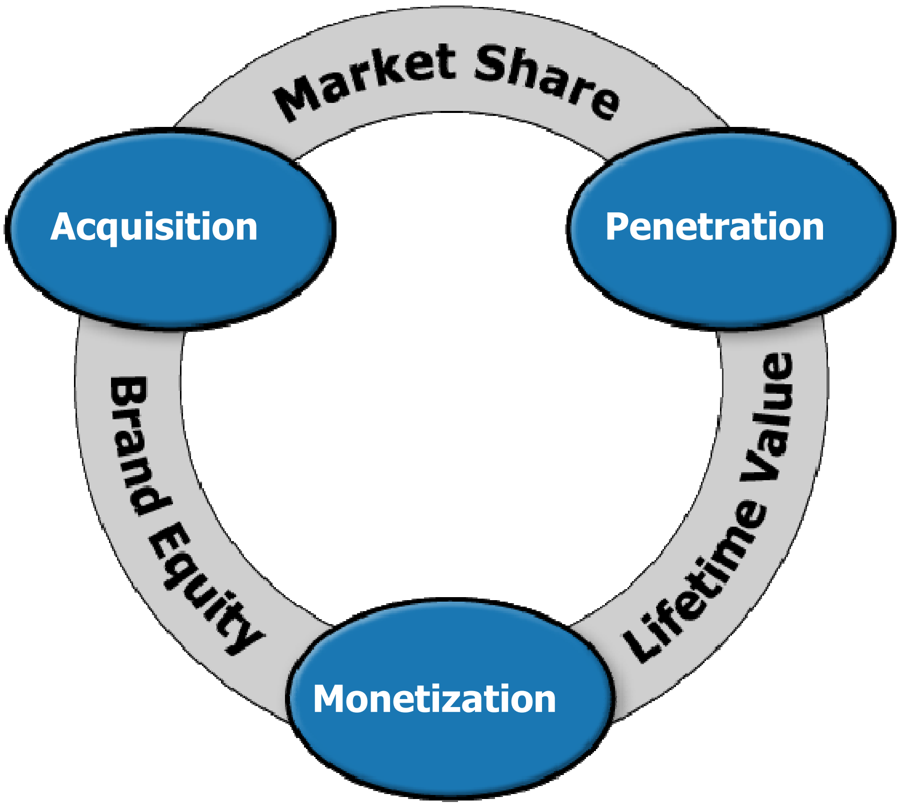

Figure 2: Marketing's Link to Business Outcomes

These three roles - market share, lifetime value, and brand equity - become the gauges that marketing monitors. Marketing objectives and strategies are deployed to move the needle on each gauge. The more effective the strategies and the better they are executed; the more positive impact marketing can have on improving each outcome.

Moving the Needle

These are the business outcomes marketing should address. Now the question becomes how we move the needle of each gauge. That is, what variables do we need to affect that will impact each outcome. For each outcome there is a specific set of variables.

Market Share
Market share is generally defined as the company's share of total sales of all the products within the category in which the company's brand/products compete. The share number is derived by dividing your company's product/brand sales volume by the total category sales volume.

$$MS = \frac{\text{Brand Sales Volume}}{\text{Total Category Sales}}$$

Indicators that your company is gaining share over the competition include the following variables.

1. First, more and more potential customers must be made aware of your offer. You must own a share of voice, which is the relative frequency, weight, and quality of your communication compared to the competition and clutter.
2. Once potential customers are aware of you they must put you on the short list of consideration. You must have some share of preference, the second variable to monitor.
3. Increasing the extent to which your channel partners recommend and sell your products versus competitive alternatives - this is known as share of distribution - the third variable. Two other variables are important factors.
4. The rate at which you attract and acquire new customers.
5. The rate of your growth compared to the growth of the category.

The actual numbers of customers you acquire as well as the rate of acquisition are key. While you may be able to have consideration, if the customer doesn't select you, you cannot gain share. You now have five quality measures. Strategies and tactics that positively impact these variables will ultimately affect your market share.

<u>Lifetime Value</u>

Acquiring a customer is just the start. The next key business outcome is to keep this customer and grow its value. Each customer is worth something and the typically the longer you keep the customer the more that individual customer is worth. Most companies know how long they need to keep the customer to recoup the cost to initially acquire that one customer. Lifetime value (LTV) is a powerful metric and a meaningful business outcome. If your company is merely a revolving door for customers, your profitability will suffer. Lifetime value is the net profit each customer contributes to the business over its entire time as a customer. Research suggests that companies with higher lifetime value customers spend less money on servicing customers, can increase their prices more easily, and can enjoy more referrals (a lower cost of acquistion).

The simplest LTV calculation (there are several) is total revenue received from the customer while a customer minus the costs of providing that customer with products/services. You will need to include costs of goods sold, selling costs and support costs. Using average costs per unit, while sufficient for calculating overall LTV can be deceiving if using LTV for customer segmentation purposes because the selling costs and support costs vary dramatically by customer.

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Sidebar –

A defected customer that comes back after the average Life Time number should be treated as a new customer, otherwise all customers will have "infinite" lifetimes, and you lose the relevance of the metric.

One way to get to customer service cost is take the number of units sold annually and divide by the annual customer service cost and to have a number for each unit. You can do the same thing for returns, support, invoicing, etc and eventually come up with a total cost per unit.

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Growing LTV is the ultimate indicator of a good return on marketing. In fact, return on marketing investment (ROMI) can be calculated by subtracting the last year's LTV from the current year LTV and dividing the sum by the current years marketing investment.

ROMI – <u>LTV current year – LTV previous year</u>
Marketing Investment

Four variables will help move the Lifetime Value gauge.

1. Tenure. The longer a customer is a customer the more likely they will continue to be a customer.
2. Frequency. The more frequently they purchase the greater the likelihood their lifetime value will grow.
3. Share of wallet. This is your share of the customer's budget allocated for your types of products/services, that you secure, is a valuable way to measure your ability to compete. If the customer is spending more of their allocated budget on products and services from your company as opposed to spreading their dollars around,
4. Advocacy. The more likely they are to continue to buy products from you, that is, the greater their loyalty, which is the final quality measure.

Perhaps a few examples will help illustrate this concept. It is one thing for a customer to consistently buy the same brand of dishwashing soap, printer paper, medical device, or test equipment again and again. This is purchase frequency. But let's say your company has several products, that is, you make and sell dishwashing soap, paper towels, toilet paper, shampoo, toothpaste, and so on. Most households buy a variety of these products. The company captures a greater share of this customer's wallet the more of these products the buyer purchases from the same company. The concept applies to any company whether they make medical devices, provide financial services, or sell software and services.

The last variable is loyalty. It's one thing to have a satisfied customer, it is another to have a loyal customer, a customer who is very unlikely to switch and is highly likely to refer. Again, when marketing focuses on strategies and tactics that improve these measures they will ultimately move the lifetime value needle.

<u>Brand Equity</u>

We can now discuss the last marketing metric and business outcome, brand equity. At this point, we are successfully acquiring customers and keeping them. There are numerous and complicated ways to measure brand equity. We'd like to suggest something simpler that drives home the contribution marketing makes. Brand equity is the sum of the value of your customer franchise times your price premium. Therefore, the greater the value of your customer franchise which is the aggregate value of purchases from all of your customers who repeatedly buy your brand and the more you can command for your product/service relative to competing offers within your category, the higher your company's brand equity.

Brand Equity = Customer Franchise Value * Price Premium

In addition to these two quality measures, three other variables impact brand equity. The rate at which new products are accepted, your product's profit margin compared to the profit margin in the category, and your overall net advocacy score. The advantage of a strong loyal customer base is that these customers are often the first to adopt you newest products and services thereby improving the rate of new product adoption which impacts the time to revenue for a new product. Existing customers give your new offer reference-ability and momentum. Existing customers are more likely to adopt a new product quicker and will help pave the way to entering adjacent markets.

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Sidebar – Creating a Market Strategy

If you are unfamiliar with developing a market strategy, a classic approach is to use the Asnoff matrix (figure 3). The matrix serves as a good strategic planning tool and also helps supports the idea of leveraging existing customers to enhance product adoption. Essentially, Asnoff suggests there are four primary strategies:

1. **Market Penetration** - done by selling more current products to existing markets by raising the retention rate, increasing customer spend or by winning competitor's customers. This is basically repeating what you are doing today.
2. **Product Development** – bringing new products to existing customers and markets. The company is leveraging its existing base.
3. **Market Development** - taking current products to new markets. This is taking proven products to customers and markets that are not familiar with you which are therefore harder than just bringing a new product to an existing customer who hopefully has a positive disposition to your company and its offers.
4. **Diversification** –involves both new products developed and brought to new markets. This is the hardest strategy. (insert graphic: "patterson-strategy.ai")

	Present Product	*New Product*
Present Market	**Market Penetration**	**Product Development**
New Market	**Market Development**	**Diversification**

Figure 3: Adapted from Igor Asnoff's book, *Implanting Strategic Management* (1990)

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With these quality measures every marketing professional and executive, can be both accountable and at the same time impact the company's strategic direction. By measuring and monitoring these factors and keeping an eye on the gauges marketing can begin to understand whether strategies are having an impact and how well tactics are being executed. And more importantly, we can take a seat at the executive table and participate in a meaningful discussion about the business rather than a tactical discussion about trade show logistics, ad placements, and email conversion rates. While these activities are important and still need to be monitored, they won't get us a seat at the executive table. And while focusing on these quality measures and key metrics won't stop the CFO from asking questions about ROI and costs, it will help change the dialogue to one that is about the impact of the marketing programs as a whole on the business.

Creating Your Dashboard

Marketing performance management and metrics tracking would be incomplete without a way to capture and report the metrics, that is, a dashboard. Ideally, metrics indicate the business health of your organization. A dashboard is the visual representation of a firm's health and provides a snapshot between actual performance and the goals. A good dashboard facilitates action. It not only reports on the metrics being monitored, but also serves as vehicle to help decide on what actions are required and their priorities. Yet, according to the June 2005 study conducted by CMO Magazine, three-fourths of marketers have no formal scorecard.

Creating a dashboard is more than just producing a few charts and graphs. A dashboard is the visual and diagnostic vehicle that communicates marketing's effectiveness and impact on business goals. Every metric provides a specific perspective on the firm's business. Some metrics indicate whether there is a problem today and others help alert marketing to a potential problem down the road. The status of the marketing organization on the metrics continuum will impact what kind of dashboard it can create. As the business goals change it will be important to revisit the dashboard to make sure the dashboard metrics are still in alignment with the business needs and goals.

As companies progress along the metrics continuum from Activity-Based to Outcome-Based, the dashboard will also evolve. Outcome-based Metrics involve a dashboard that hones in on the primary business outcomes we've discussed: market share, customer penetration, and customer value. Because these metrics tend to be more market centric, the dashboard begins to provide more strategic insight and direction.

The greatest challenge for the marketing organization is how to capture the metrics. Manual aggregation of data across multiple spreadsheets comes with potential issues ranging from error-prone reporting and poor utilization of internal resources. Moving from a spreadsheet-based system to an automated system provides greater benefits to the organization as a whole.

But you needn't invest huge resources in new systems to create dashboards. A basic set of charts such as those depicted below will serve the purpose. While perhaps a bit more time consuming this approach will help you really understand your measures and your business.

Here is a fictitious example (Figure 4) of a dashboard using some of the metrics we've discussed. In this example, these five charts paint an alarming picture. The company may be closing lots of deals, but might not be aware of the precipitous cliff facing them if they didn't know that their repeat orders and net advocacy or dropping off and that their market value index and wins compared to the competition are concerning. The fact they are experiencing a sharp decline in their prices suggest that their differentiation and therefore their brand strategy is no longer effective. This information can help them ask important questions and make key business decisions.
(insert graphic: "patterson-widget.ai)

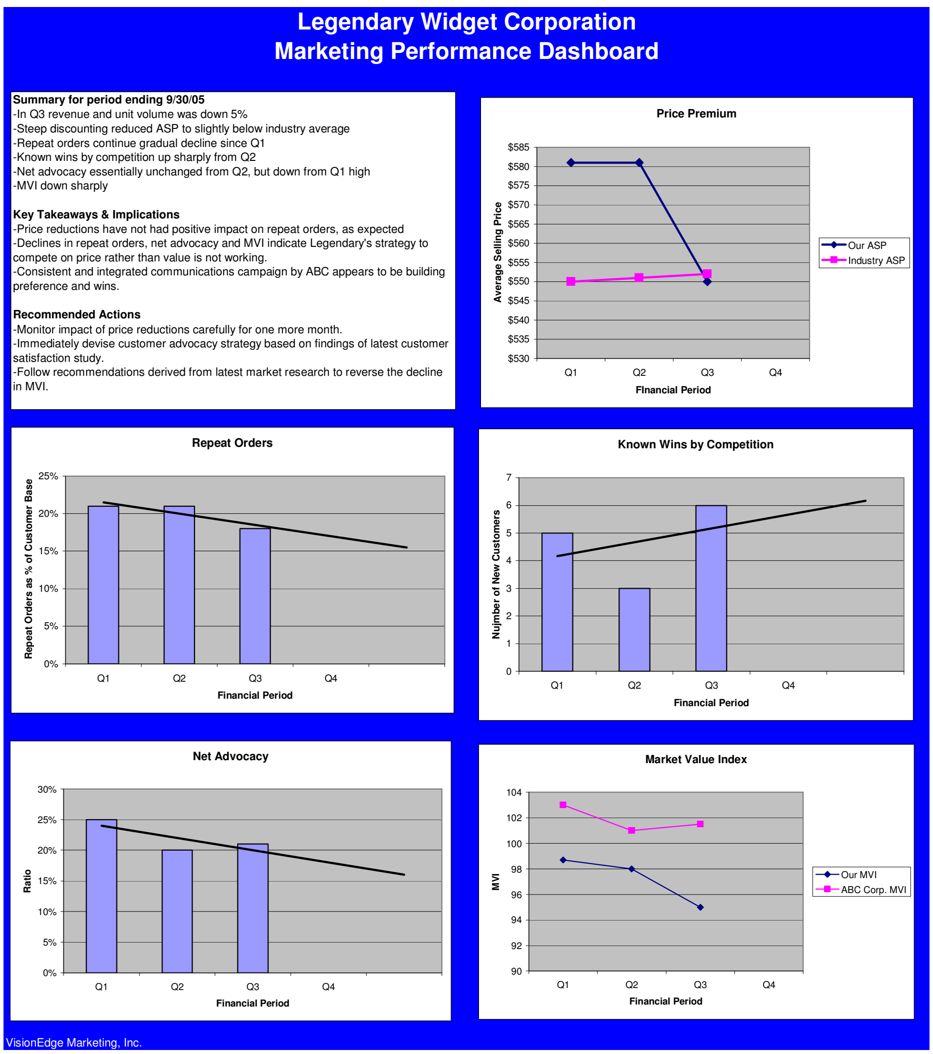

Figure 4: Fictitious dashboard example

Measure What Matters

We began this discussion about the need for marketing to be more accountable and to develop quality metrics. Hopefully as a result of this article/presentation, you have some new ideas on how to focus marketing metrics around business outcomes and how to develop quality metrics that will help you provide insight into how marketing is making a contribution to the company – and how to demonstrate that contribution to senior management. So in closing, we leave you with these three final thoughts:

- Stop talking about improving marketing performance and accountability and start taking action.
- Even if you don't have all the data, start with what you have, define your data gaps and develop a plan to close these gaps.
- Stop reporting on activities. Using activities as a dashboard doesn't give your leadership team the information they need to make important strategic decisions.

Use the measures we've posited to develop your dashboard. Measures that matter are those that help your company make decisions and take action. When used this way, marketing metrics enable a firm to seize a competitive advantage.

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