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Whitepaper

Project CRM:
"Pre-CRM" Testing Techniques - Determining the Potential for Marketing ROI

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CRM can generate increased profitability for your business in two ways:

1. Reducing costs, usually in the call center or distribution system (operational CRM).

2. Increasing customer value (LifeTime Value) through marketing (analytical CRM).

It's possible to determine in advance whether your "customer marketing side" CRM initiative has the potential to increase the value of your customers. Going through this exercise will also help identify any special needs you may have to consider when choosing a CRM package and serve to educate participants in some core issues on customer valuation.

You can use the following methods "pre-CRM" to estimate the potential for the marketing side ROI of CRM investment, or use them to prove plain old database marketing will be as effective as the marketing / analytical side of CRM when trying to increase customer value.

Background

There's a lot of CRM commentary about having a "relationship" with your customers. How many companies do you want to have a "relationship" with? CRM shouldn't mean playing "kissy-face" with customers. You're in business to make money, not to fawn over customers. You have to provide good service, of course - that's a minimum requirement.

It seems somewhere along the line the proven techniques of Relationship Marketing have been spun and buzzed into a reason to buy a CRM package, to "create a relationship with the customer". Supposedly, if you create this mystical relationship with the customer, profits magically increase.

The fact is, many high-end CRM analytics packages rely on existing database marketing techniques used for decades, but the techniques themselves have been lost in the CRM shuffle. You can easily use these same proven techniques to model your likely success with analytical CRM before you buy.

Relationship Marketing, which appears to have been made a part of CRM, never talks about having a relationship with the customer, it's about having a dialog (sound familiar?) .This dialog is not a speaking conversation, it's about understanding the customer life cycle and responding proactively to it. The LifeCycle is defined by the customer's behavior from the first day of business with you until they stop doing business with you. It's the LifeCycle of the customer that determines Life Time Value. The concept of LifeTime Value without the LifeCycle is meaningless. You can increase LifeTime Value by affecting the LifeCycle, in one of two ways:

1. Extend the LifeCycle, creating more time for the customer to increase in value. This is usually accomplished by concentrating acquisition efforts on know long LifeCycle, high future value customers.

2. Increase average value within the existing LifeCycle. This is usually accomplished by knowing when customers are most likely to engage in revenue-generating activities with you, and taking action to get the business.

The implementation of “anti-defection" campaigns can be used to address both of the above issues. The following tests should give you a good idea if you have the kind of customer base that will respond in a profitable way to these techniques for increasing customer value.

The Tests

The first test, customer acquisition, addresses your ability to extend the LifeCycle. The second, Customer Retention, addresses your capability to increase average customer value during the LifeCycle and the potential effectiveness of anti-defection campaigns. Combined, they should give you a good idea if CRM (or database marketing without CRM) will work in a profitable way for you.

1. Customer Acquisition - Pick a start date, say one year ago, and calculate each customer's value from then until the present (you could use gross sales or total visits as a proxy for customer value in this case). Sort the customers by this value.
Look at the top 10% best (most profitable) customers, and the bottom 10% worst (least profitable) customers. Other than the revenue / profit variable, are they different? Are they from different places, were they acquired by different methods using different offers, do they tend to buy certain products?

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If you can find any significant differences between your best and worst customers, you have a shot at improving customer retention (increasing LifeTime Value) by fine-tuning customer acquisition methods.

The idea here is twofold: If you can identify high and low value customers by some data element, you can allocate a larger share of budget to acquiring high value customers, and automatically target follow-up programs to "fix" low value customers. If you have the data, look closely at elements of the first transaction (product, media, price, and offer); the first experience of a customer heavily influences the LifeCycle / LifeTime Value.

2. Customer Retention - Pick the highest value generating activity in the database. It's probably product sales, but it could be page views or other ideas. Sort your customers by their last date of this activity. Label the top 20% (those who engaged in the activity most Recently) of customers 5, the next lowest 20% 4, and so on, so the bottom (least Recent) 20% is labeled 1.

Take an equal sized sample of people from each 20% group, say 10%. Send them a promotion with broad appeal; don't be overly restrictive in your offer. You don't have to give away the store, just make sure the offer isn't "targeted" to any particular group. For commerce, this offer might be "10% off anything in the store". For content, it might be a free day of access to normally paid content as a "trial".

When you look at response rates to the promotion by the "scores" 5 down to 1, they should appear similar to the following:

Recency Group	Response Rate
(Most Recent) 5	40%
4	25%
3	10%
2	5%
(Most Distant) 1	1%

You won't see these numbers specifically, but the pattern should be evident. The customers who are "5" should have a response rate anywhere from 5 to 40 times higher than the customers labeled "1", and response should noticeably decrease at each level.

If you see this pattern, CRM marketing techniques, or what we used to call "Relationship Marketing", will be able to increase the average value of a customer within the existing LifeCycle. This kind of response pattern also indicates anti-defection campaigns will be a profitable way to both extend the LifeCycle and increase customer value within the existing LifeCycle.

These two tests should be enough to give you a Go/No Go feel for the customer side ROI of CRM.

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