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HOW SEGMENTING YOUR CUSTOMER BASE HELPS STRENGTHEN RELATIONSHIPS

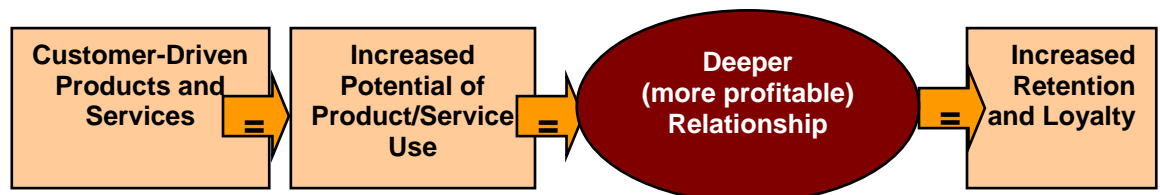
Customer retention is arguably one of the best predictors of company profits.

- The longer a customer stays with a company, the more that customer is worth. Long-term customers buy more, take less of the company's time, are less sensitive to price, and bring in new customers.
- Best of all, there are no acquisition or start-up costs associated with them.

We know from previous research we've conducted among various industries that a key factor in the retention (and loyalty) of customers is increasing their perceptions of the relationships *value*.

- In a recent example, we found that approximately half the customers complaining about value used their relationship for nothing more than the basics (placing orders, paying bills...). Another one-third used additional products or services sporadically (without loyalty). These customers were also less aware of the products and services available to them.
- Conversely, those who described value in the relationship were making use of the full menu of products and services available to them. These were also the most loyal customers

By becoming more customer-focused, you can create products and services, even service levels, that are targeted to specific customer segments...thus increasing the likelihood that they will use them, find value in them, deepen their relationship with you, and (bottom line) become more loyal.



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Building a Customer Relationship

Start with the basics:

- Who are you?
- What is your Vision Statement?
- What is your Value Proposition?
- What is your Strategy?

These definitions become the foundation of your existence and the building block for developing unique and enduring customer *relationships*. Once defined, you can set your course down a clear path and begin “opening the front door” to customers to seek and “closing the back door” to the customers to keep.

As a company develops the technological sophistication to better know its customers, it also creates an environment capable of relationship marketing...cross-selling to build deeper, more profitable and enduring relationships with existing customers.

This effort to deepen the company’s relationship with customers (and be more customer-driven) will ultimately serve to:

- Increase customer perceptions of the value of their relationship with you,
- Increase customer loyalty and retention, and
- Increase the likelihood of purchasing additional products and services.

Why Segmentation Research?

A benchmark segmentation effort is designed to maximize your ability to target similar customers with the products and services they are likely to want, need....and purchase.

Segmentation research allows us to associate customer profitability with demographics and specific needs/expectations so that we can target more effectively to specific groups of customers.

At the least, most companies typically know how a *market-defined segment* (large vs small customers, for example) contributes to the bottom line. They may even have specific marketing and sales efforts addressing these market-defined segments.

Many companies also know how each *customer’s profitability* contributes to the bottom line. This is where the power of Segmentation can truly impact business success.

- However, profit contribution is an end effect.
- Satisfactory delivery on customer needs and expectations directly affects profit, not the other way around.



Objectives of Segmentation Research

The overall objective of most segmentation efforts is to learn how best to build deeper, more profitable relationships that will increase loyalty and retention among customers.

Specific objectives typically include the following:

- Assessing differences between contribution segments based upon customer needs and expectations of your services,
- Profiling differences in awareness and usage of your services,
- Measuring impact of specific services, and service levels, on customer loyalty and retention,
- Assessing the value placed on specific services by customers, and determining which services add greatest value to a long-term relationship.

To increase the usefulness of this research effort, research findings should not only provide you with comparisons between contribution segments, but should also provide you with the means for effective targeting of marketing and sales efforts in order to move customers from one contribution segment to another.

To this end, the following additional objectives are also accomplished:

- Assessing the customer needs and expectations that drive purchase likelihood of various products and services, and
- Developing a predictive tool for determining which customers to target specific products and services to.

In a recent example, a client had analyzed their customer database and created "contribution-based" segments that provided interesting observations, not the least of which were that there seemed to be three useful marketing clusters:

- It appeared that approximately 23% of the customer base created 82% of the company's revenue (clusters 1, 2 and 3).
 - Long-term customers of 21+ years were most apt to fit into these "high value" segments.
 - Approximately 54% of the membership created the remaining 18% of the company's revenue ("mid-value" clusters 4, 5 and 6).
 - Customers in "low-value" clusters 7 and 8 were currently costing the company money.
- We saw a high degree of fluidity between clusters...which presented opportunities for the Company to influence customers with specifically targeted products and services that would move them into the "high value" segments.

Results of segmentation research showed that a strategic marketing approach need not be limited to targeting these contribution-based clusters, but rather, allowed the ability to seek out subgroups within, and throughout, these clusters based on our ability to predict the likelihood of using /purchasing company services. Hence, building a long-term relationship.



Building and Improving Customer Loyalty

At A·D·R, we believe the best place to begin analysis is by looking *forward* to the results.

- What are the marketing questions we need to answer?
- More importantly, what are the marketing decisions that need to be made?

Our bottom-line concern is that your research results be useful and actionable.

With the increased sophistication of databases, companies today have a much stronger opportunity than ever before to leverage and strengthen their relationship with customers.

- Segmentation research has made targeted marketing efforts a highly plausible reality, minimizing risk to the company and maximizing the return on the marketing dollar.
- To be actionable, however, the research has to complement database capabilities. For example, efforts to differentiate customers has to be accomplished in such a way that they can easily target specific customers based on key variables that were already in the database or could easily be appended.

To this end, we expect Segmentation Research to be able to answer the following marketing questions:

- What customer needs and expectations best serve to predict purchase likelihood within general product/service categories or of specific products and services?
- What key predictors can best serve to target specific customers for specific product/service categories?
- How do segments of similar customers differ in terms of the needs and expectations of the customers in each segment?
- What are the marketing “hot buttons” to target each segment with?
- What existing services best meet the needs of customers in each segment?
- What potential new products, services/service levels best meet the needs of customers in each segment?
- What factors have the greatest influence on retention and/or loyalty?



Developing Useful Segments

Segmentation analysis is often more “art” than “science” as every business situation creates variations to the norm when analyzing and interpreting results. As such, pulling a “segmentation process” off the shelf is rarely a successful solution.

Basic steps to our segmentation approach:

- Foundation of analysis is based on business realities.
 - In preparatory analyses, as well as the actual segmentation derivation process, a “bottom line” orientation is utilized to assure that the results are actionable and driven by business realities.
 - This helps focus on “useful” vs “nice to have” information.
- An initial “deep dive” look at the data identifies any and (if possible) all sources of variation that may be present in the data.
 - These sources of variation are taken into account throughout all of the analytic work.
 - This is not a broad brush, general look.
 - Detailed knowledge of the data is critical to ensure the segments are actionable with respect to their purpose.
- Our approach to segmentation development is a multi-step, iterative process using a variety of analytical techniques.
 - Iterations continue until the results indicate that the greatest possible number of respondents have been classified correctly.
 - We then work with you to determine the optimum number of segments (typically a trade-off between the best representation vs the degree of variability explained between solutions vs practicality).
 - The segments are differentiated from one another using the variables included in the analytical process.
 - A descriptive profile of each segment is developed focusing on “bottom line” “actionability” and importantly, functionality and usefulness among your internal audiences.

If requested at the onset of the analysis, we can derive a classification algorithm so that the customer database may be coded to indicate which segment each customer aligns most closely with.

- This last step facilitates ease of use of the database for appropriate “target” marketing opportunities as well as relationship building activities.
- Classifying the database requires robust customer files with data which can tie into the segmentation effort.



Segmentation Research White Paper

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Segment membership is not a static proposition.

- In the ideal solution, the coding of a database (based on segmentation analysis) will identify movement between the segments, suggesting business strengths and weaknesses.
- Segmentation updates are generally required every two-to-four years, depending upon the degree of change in the marketplace.

Why Go Through the Process of Segmenting?

The creation of Customer Segments is not for everyone. The worst is to go thru the expense and end up with "Segments" that are not truly useful.

We avoid this by going thru a careful process to make sure the research needed to create customer segments matches up with the way you do business. And at the backend of the analysis, where Art and Science meet, we make sure to include you in the process to make sure the segments are named and described in ways that are clearly identifiable throughout your organization.

With *actionable* Customer Segments in hand, you have the huge benefit of target marketing to enhance profitability among existing customers and to increase your opportunity among targeted prospects.

...A bottom line approach that insures you are communicating with relevance to your customers and prospects.

ADR Associates, Inc

...Helping Connect With Customers

ADR Associates is a corporation founded in 1994 specializing in strategic positioning, market research and communication counsel. Based at Red Hawk Ranch, a unique executive off-site location, ADR brings the customer voice into management's focus. Helping clients understand customer perceptions is often the foundation of ADR's involvement and becomes a driving force for creating and fine-tuning successful business strategies.

Red Hawk Ranch is headquartered in California's Temecula Valley Wine Region. Visit us at www.redhawkcranch.tv.