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FEATURES

A Measure of Success

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You know a lot about your customers. You know who they are, where they live, what their buying habits are. And if you're like most companies, you've done absolutely nothing with that pile of market intelligence. It just sits there, earning you no money and creating zero shareholder value. Here's what your company needs to do to put all that hard-won information to work.

Hey, American Express -- do you know us?

Do you ever. You know where we travel and when, on which airlines, in which class of service. You know the restaurants where we eat and the stores where we buy wine and books and clothes. You know this and much else for millions of us. And no one else has that very same data! (While AmEx's (AXP) headquarters was damaged in the World Trade Center attack, no data was lost.) The company should enjoy an awesome competitive advantage.

Yet it doesn't -- at least none that the stock market has noticed. American Express trades at just 22 times earnings, when the market average is 26. In fact, AmEx's price/earnings ratio has averaged around 20 percent below market averages during the past three years.

AmEx is hardly the only data-rich, value-poor corporation that comes to mind. Think of other financial services firms, phone companies, airlines, retailers, hotel chains, rental car companies, service providers - the infotech revolution was supposed to make their customer knowledge the killer competitive advantage of our time. Consultants like Don Peppers and Martha Rogers (*The One to One Future*, *Enterprise One to One*) have been writing about the possibilities for years. Yet far from commanding premium P/Es, these companies almost invariably trade at crummy multiples (click on chart below). The missed opportunity is stunning: If the 10 firms represented by [our chart](#) could nudge their multiples up to the market average, they would create more than \$500 billion of new shareholder wealth. Why they've failed to make use of the massive troves of customer data they possess is one of the great business puzzles of the Info Age.

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It's important to note that this is not mainly a technology problem. While integrating data scattered among a hodgepodge of business units and computer platforms is no layup, it is no longer an insurmountable hurdle. The proof is that a few companies, such as Dell Computer ([DELL](#)), are using the technology well and delivering premium P/E multiples in this down market.

If technology isn't to blame, what is? Not privacy concerns, regulatory restrictions, or other apparent obstacles that managers like to cite (see "[Don't Buy These Excuses](#)"). Talk with managers at companies that use customer data effectively, as well as those at companies that are struggling, and it's clear that the most important problems lie within. Converting customer data into real shareholder value -- a process we call customer knowledge management (CKM) -- starts with the right corporate mind-set, organization, accountability, and leadership. Until an organization squares these away, even the fanciest new tools will do little but run up the IT budget.

Our analysis of successes and failures in the use of customer data shows that every company needs a strong foundation made of seven elements. As we describe them, ask yourself which ones your company has, needs to build, or needs to strengthen. Give your company a score of 0 to 10 on each trait. At the end we'll explain what your total means.

1. Leadership committed to delivering and maintaining a premium P/E multiple.

Great companies recognize that they must excel in the eyes of their capital suppliers -- the shareowners. A weak stock means you'll have a tough time attracting the best employees. It's harder to please customers when you're struggling to fund research and customer service. When you need to buy companies to get technology, talent, or access to key markets, a strong stock may be your best currency. That's why many leading companies focus explicitly on maintaining a P/E multiple that's superior to some broad market benchmark such as the S&P 500.

Yet in our experience, most companies are unwilling to set -- even internally -- such an aggressive goal. This is a major problem, since using customer data more effectively often requires wrenching institutional change. Many of the companies sitting on untapped gold mines of customer data typically benchmark against peers, not the broad market. If the whole industry is in the dumps, a poor performer can look good by comparison and the urgency to improve vanishes. Set the capital market goals low, and the customer service goals will almost certainly be low as well.

2. Strategic planning built around customer segments -- and a cultural belief that not all customers should be treated identically.

With the CKM tools now available, it's far easier than ever for a company to learn a piece of crucial information: how much money it's making (or losing) on each customer. You'd think every company would want to segment customers by expected profitability and treat the most profitable customers best. After all, extensive research -- most notably by consultant Frederick F. Reichheld -- proves that retaining current customers is enormously more profitable than bringing in new ones, a finding that goes double or triple for the most profitable customers.

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Yet many companies resist. Often a key reason is that the corporate culture regards it as unfair to treat some customers better than others. It's an odd attitude; after all, as consumers we almost always feel we deserve special treatment if we're loyal customers, and getting it makes us more inclined to do additional business. It's important to keep that in mind. Because customer loyalty is so valuable, the most profitable customers should get better treatment.

Applying that principle isn't always easy. To satisfy your best customers, you must be able to segment not just by profitability but also by needs. For example, a bank might find that its most profitable customers include young professionals with big mortgages as well as elderly widows who keep large balances in savings accounts. But only one of those groups would be a logical prospect for sophisticated investment products.

Fidelity Investments has made significant progress in the past three years in creating (and acting on) multiple segments. The company long held that treating all customers equally was almost a moral obligation. Now it has come around to tailoring different strategies for different groups segmented by revenue, then subsegmented by profitability, with third-party data and customer interactions used to gauge needs. Each revenue category includes profitable and unprofitable customers (an extreme example of the latter being one customer who calls Fidelity some 3,900 times a year). Fidelity then applies all this data in several ways: to develop products and services for each group, to create marketing programs, and to differentiate service. The results are higher customer loyalty, better returns on marketing investments, and a bigger share of customers' total spending on financial services.

Nevertheless, many companies remain wary of similar opportunities in their businesses. Failure to differentiate becomes an even bigger problem when the economy tanks. Companies cut head count in branches, call centers, and installation centers, reducing customer service "equitably." Just when it's most essential to keep the most valuable customers and get more of their business, these undifferentiated cost cutters do exactly the opposite.

3. A truly customer-centric mind-set and a corporate organization built around customer segments.

At most companies the world revolves around products or functions or geography. Customers endure the all-too-familiar experience of contacting different parts of the organization and finding that each part knows nothing about that customer's experience with the others. Have you ever called your local phone company and tried to order a new service like, say, a DSL connection? Depending on where you live, you may be treated like a total stranger, even if you've been a customer for decades.

For that to change, someone must "own" the customer -- and that means each customer segment must be a business unit run by a manager with profit-and-loss accountability. This is a radical change at most companies, but it works. Dell is organized this way, a key element in its knockout performance during the past 15 years. Why don't more companies follow suit? Corporate politics are a major factor. A reorganization would take power from today's product-, function-, and territory-based barons, all of whom command formidable resources with which to kill the new system.

More fundamentally, the problem is one of mind-set -- what the company perceives itself to be all about. No company uses customer data better than Amazon ([AMZN](#)). Ask former CFO Joy Covey why, and she replies immediately, "It's the mind-set." From day one, founder Jeff Bezos made clear that Amazon would use its information about customers to build relationships with them and make them happy. There simply was no other way of operating.

Not many companies inherit a customer-centric mind-set from their founders. But those that weren't born with one will need to get one -- and organize on that basis -- before hoping to turn customer data

into shareholder value. "We're building toward that customer-centric model," says Stephen Butler, a Verizon (VZ) executive who's among those trying to shake things up at a company with roots going back more than a century to life as a regulated utility. It's a long slog, but Butler is starting with the right insight. "It's more than just technology," he says. "It's a change in culture and organization."

4. Caring enough about customer data to invest in developing it -- and then holding managers accountable for returns on those investments.

It's remarkable how many companies just don't care about customer data. Banks in the United States are exhibit A. "As an industry we always had the data, but we threw it away," says Sylvia Reynolds, who recently joined Wells Fargo as head of marketing for the National Home Equity Group. Wells Fargo is emphatic about not throwing data away today, as it cranks up a major effort to create more value from what it knows. Reynolds adds: "When I first got into the industry, I was amazed at what you could learn in a mortgage application. You could ask for someone's divorce papers! I started thinking of all the things we could do with this information."

Even companies that spend a lot on infotech often spend remarkably little on developing customer knowledge. At most of the companies we've investigated, infotech investment is conceived as building infrastructure -- with the payoff defined vaguely at best -- rather than as pursuing profitable projects.

It needn't be that way. General Electric (GE) has coined the phrase "drive it to the ledger," meaning that if something is worth doing, its bottom-line benefits must be planned and tracked. Excellent companies routinely apply that practice to such activities as cost cutting and working capital management because managers are accountable for those things. So if a company wants to make wise investments in developing customer knowledge, it will need to make managers accountable for the profitability of customer segments. Those managers will have to guide those customer-knowledge investments -- and drive them to the ledger.

5. A culture that enthusiastically examines customer data, uses it to form hypotheses, experiments, and applies the results.

In any company, different people respond to data in different ways, some useful, others counterproductive. We saw an excellent example of the latter at a major global retailer. During a review, managers excitedly told the company's senior marketing executive that a study had discovered that the top 1 percent of customers accounted for about 25 percent of the company's total credit card sales. But the executive wouldn't believe it. With millions of customers coming into the firm's stores every day, it simply couldn't be true that a mere 1 percent were that important. Intent on proving his own intuition, he attacked the data and the design of the study -- and resisted an insight that might unlock a new value proposition for his most important customers. His passionate subordinates eventually prevailed -- a year later.

The best companies evaluate the data without prejudice, make inferences, and figure out ways to use it. At Fidelity (FBIC), managers sift through the data every day, looking for insights. The culture is similar at Travelocity.com (TVLY), the largest player in the largest category of e-commerce. The culture must endorse such behavior and penalize the more common unproductive responses to customer data.

6. A record of merging operations successfully, with zero decline in satisfaction among the most valuable customer segments.

In any company more than a few years old, customer data probably resides in several computer systems across the enterprise -- marketing, production, shipping, billing. Putting those together is a big job, but in many companies it's even bigger because the company has recently gone through a merger.

Obviously no organization can form a complete picture of its customers until it combines data from all of its component companies, a massive infotech assignment. But here again, the greatest challenge is managerial. Consolidating customer data requires employees to cooperate in ways they may not be accustomed to. Making that happen day by day is a specific management task, and some companies are better at it than others. The best are companies with lots of experience in integrating acquisitions. Among those, the very best are the firms that made acquisitions with a customer-centric mind-set.

7. Top management that spends at least 25 percent of its time teaching these principles to all levels of the organization.

Fully exploited, enlightened use of customer data will almost always drive a company toward profound organizational changes. That's why top management commitment is indispensable. Just consolidating data can become so contentious a process that it may fail unless participants know that the CEO is watching and expecting it to succeed.

More deeply, a truly customer-centric company is unlike almost anything that now exists. No company that we're aware of has fully adopted all of these principles. How far in that direction can a company go? No one knows, but we'll likely find out in the next few years.

Now add up your scores. Here's how we interpret the total:

0-25: Don't even try extracting more value from your customer data. Until you improve on the basics, applying today's customer knowledge management tools for this purpose will just tie your company in knots.

26-50: You've got a shot at success, but you'll need to improve your lowest scores quickly.

51-70: Go for it. The management challenges won't be easy, but you're better prepared for them than most. Move now and you could build a strong competitive advantage that delivers a premium P/E for your shareowners.

One final observation: In this application of infotech, as in many others, the future could be just the opposite of what the pundits expect. The friction-free, Internetworked world was going to be a place where buyers flitted from vendor to vendor at the click of a mouse. In reality, it may be that the best users of consumer data can learn enough about their customers to create continuously better products and services -- a competitive advantage that will just get stronger. If that's the future, then the most customer-centric firms will get even better in the years ahead, and the gap between the strong and the weak will widen. If you're on the wrong side of that gap, you'd better move fast. ♦

For a case study of how established firms can use customer data to their advantage, check out "[Boise Cascade Gets That Old Data Religion](#)."

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