FEATURES corporate strategy

A Measure of Success

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.

By Larry Selden and Geoffrey Colvin, November 2001 Issue

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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.

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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

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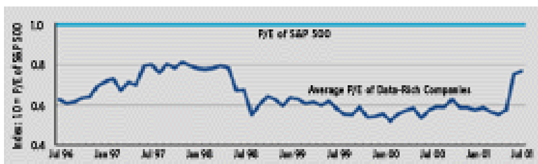
their customer knowledge the killer competitive advantage of our time. Consultants like Don Peppers and Martha Rogers (*The One to One Future*, *Enterprise One to One*) have been writing about the possibilities for years. Yet far from commanding premium P/Es, these companies almost invariably trade at 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.



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

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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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