



Adopt PRI-STAT'S LifeStyle Segmentation and the Related Marketing?



1. Background.

LifeStyle segmentation is a new methodology for identifying consumer behavior and linking that behavior to specific motives. The methodology is the basis for achieving significant improvements in marketing results.

However, since the methodology is new clients often unsure about the proper decision-making process to follow when considering application of this method to their particular situation. The intent of this paper is to organize existing information in a way that is compatible with the process clients use when making decisions under conditions of uncertainty.

2. Decision process regarding the adoption of any new method

There are three types of information businesses use in making decisions of this type:

- **Facts.** This category includes, for example, any documentation of prior use (case histories) by others; trials or tests that have been conducted on the client's own operations and data or other forms of validation through laboratory or statistical means.
- **Utility or Loss Function Analysis.** This category includes estimates of the net value if the new method achieves (or underachieves) certain levels of performance. "Net value" means the benefits after accounting for the costs of implementation. The costs of implementation include "hard" costs like dollars and "soft" costs like behavior and process change.
- **Expectations Based on Prior Experience.** This category includes estimates of the probability of a new method actually succeeding in the client's environment given the organization's history of innovation.

In this paper we will attempt to organize information of all three types related to the consideration of PRI-STAT™ and LifeStyle segmentation.

3. Facts.

a. General Facts

- i. 71 million individuals living in households reporting \$75K or more in household income have been segmented by LifeStyle. This data base is updated every two months.
- ii. As a rule we are able to match 85-90% of a client's customers to this data base and identify the LIFESTYLE SEGMENTATION for those customers. In the remaining 10-15% of the records we are usually able to analyze transactions and assign those customers to the LIFESTYLE SEGMENT with the most similar transactions.
- iii. In the last 12 months we have performed this analysis for over a dozen clients whose customer data bases ranged from 30 records (an interior design firm) to 2.5M records (a national retailer). We have (or are) analyzing data bases from clients in fashion, travel, real estate, leisure activities, healthcare, financial services and retail.
- iv. In every case where we were given multi-year transaction-level data we have been able to show the aggregate value of each LIFESTYLE SEGMENT, the average transaction value, the margin contribution and purchase frequency of each LIFESTYLE SEGMENT, and the year-over-year changes in those figures. This analysis enables calculation of lifetime value by customer by LIFESTYLE SEGMENT. In most cases the LIFESTYLE SEGMENTS with the greatest overall revenues were not the segments with the greatest per-customer lifetime value.
- v. In all cases we have been able to show the client's market penetration by LIFESTYLE SEGMENT at the national level and, when the data was provided, at the market or individual store level. This calculation has demonstrated the client's growth potential in existing markets based on historic performance. The same information has been used to estimate the attractiveness of new markets (the distribution of LIFESTYLE SEGMENTS varies by local market).
- vi. We have been able to provide lists of prospects that match clients' best customers by LIFESTYLE SEGMENT as well as by income and demographics.
- vii. We have demonstrated that most sales associates and professional service providers analyzed are more successful (i.e. generate more revenues) with some LIFESTYLE SEGMENTS than with others.
- viii. In a prospecting test among 350,000 individuals with household income of \$175K or more and controlled by a third party agency we have demonstrated that LIFESTYLE SEGMENTATION-specific messaging creates 200-500% lift over responses from a control group that received generic messaging. This test demonstrated that LIFESTYLE SEGMENTATION messaging added to LIFESTYLE SEGMENTATION reduces acquisition costs by approximately 67%.

b. CLIENT Specific Facts (Based on a survey of 2500 CLIENT customers).

- i. The analysis, based on the recent customer survey, is a reasonable predictor of differences in purchase behavior by CLIENT *Custom* LifeStyle Segments. We recognize that this is self-reported behavior. If you would like an analysis of the actual transactions

for this sample so that compare the actual to the self-reported, we will do this. We were impressed by the number of statistically significant differences in self-reported behavior between segments in your analysis. In this analysis we will include responses to these additional questions:

- ii. What's their RFM? As indicated in prior analyses of CLIENT data, LIFESTYLE SEGMENTATION and RFM are most effective in combination. Grids reflecting the two methods have been previously prepared. An analysis of the sample by RFM-based segments determined meaningful differences.
- iii. What categories do they purchase? This portion of the customer survey, when segmented by LIFESTYLE was particularly informative for self-reported data. If we have similar SKU level data for the same, we can compare actual and self-reported behavior.
- iv. What channels do they shop? What cross-shopping activity do they exhibit? In this regard, we know the self-reported survey information indicated differences in channel behavior.
- v. How has their behavior trended This Year vs. Last Year? This analysis was not done.
- vi. What's the distribution of segments across the CLIENT customer base and how does that compare to the distribution across the US – both overall US and by specific DMAs? The answer to the first part of this question (i.e., distribution over the US) was provided in the analysis of the survey data. We pointed out that the distribution of survey respondents by LIFESTYLE was very different than the distribution of those segments in the population. It is our view that drawing attention to this disparity helped CLIENT avoid a very significant miscalculation in setting priorities among segments in terms of market potential. We can provide the distribution of custom LIFESTYLE SEGMENTS by DMA.
- vii. To what extent does the LS distribution differ by various CLIENT stores? To what extent do LIFESTYLE SEGMENTATION differences by store mimic the differences that exist by market? This question was addressed using the generic LIFESTYLE SEGMENTATION. The initial analysis was conducted across four markets (NJ, DC, CH and DFW). It indicated significant differences. This analysis has been conducted across seven markets (other than the four studied for CLIENT) for another client and confirmed the reality of market-to-market variance. We have every reason to believe there will be a difference among markets at the store level using the custom LIFESTYLE SEGMENTATION. In order to do this all we require is the ZIP code breakdown of trade area by CLIENT store.

4. Utility or Loss Function Analysis

Estimating the impact (results) of implementing LIFESTYLE SEGMENTATION is quite straightforward on the surface.

Net Benefit (Loss) = Increase (Decrease) in Revenues-Added costs of implementation +added efficiency

- a. The “hard” cost of implementing LifeStyle Segmentation involves the annual cost of appending LIFESTYLE SEGMENT information to each customer’s record¹. The cost of this “append” can range \$.05 per record to \$.25 per record depending on the number of customer records involved and the source² of the LifeStyle “append.” ***(In many cases this cost is offset by discontinuing subscriptions to other, less valuable appended information.)***
- b. The most obvious “soft” cost of implementing LIFESTYLE SEGMENTATION involves the cost of educating the organization and its other suppliers (e.g., advertising agencies, direct marketing agencies, SEO agencies, etc.) regarding the application of LIFESTYLE SEGMENTATION to various aspects of the marketing mix. This category of “soft” cost is hard to estimate in most organizations and for this reason is hard for clients to factor into the decision analysis.
- c. Two solutions to this difficulty are:
 - i. to implement LIFESTYLE SEGMENTATION on a pilot basis in a few locations to minimize the “soft” costs while validating the benefits , or;
 - ii. to include the adoption of LIFESTYLE SEGMENTATION and marketing along with some other change that is being implemented (e.g., release of a new product line) on a broader basis.
- d. The benefits of implementing LIFESTYLE SEGMENTATION, likewise fall into two categories: Increased revenues and increased efficiency. The challenge lies in estimating these benefits before the fact.
- e. To facilitate development of this information, Premium Knowledge Group routinely provides an analysis of a client’s current data and creates a set of alternative projections of the impact on LIFESTYLE SEGMENTATION marketing on increasing revenues and decreasing costs (e.g., reduction in expense of marketing to less profitable customers and less likely prospects). One such example (extrapolated from CLIENT data) is included in the white paper *Business Case for LifeStyle Marketing*. **This Case shows how a 50 unit retail organization can create 10% increase in revenues per store and a net benefit in excess of \$50M. We are very interested in building a more detailed the business case if CLIENT determines this would help in the decision process.**

¹ Additional “hard” costs might include any consulting fees invested in estimating the potential costs and benefits. Client organizations will determine if these costs can be amortized over a period of time or should be written off in the year of the initial implementation.

² LIFESTYLE SEGMENTATION is available from Premium Knowledge Group and from Knowledge Base Marketing.

5. Expectations Based on Prior Experience

Each organization has its own experience regarding innovations. We can visualize a spectrum

- a. At one end are organizations with a history of rejecting recommendations from 3rd parties (the “not invented here” syndrome). Some resist change from any source. Some have a history of starting initiatives but then withdrawing funding initially committed for these initiatives when revenues falter and budgets are being cut. In companies like this there may be a low expectation of success no matter how promising the new idea. Championing an innovation in this environment can be viewed as a career risk.
- b. By comparison some companies, like 3M, Virgin, H&M, Bosch or Cirque de Soleil, thrive on inventiveness and actually set goals for the adoption of new methods, products and services. Such companies usually have well-thought-out processes for testing new ideas and a tolerance for a certain amount of learning through trial and error. The R&D budgets in these companies are relatively consistent in good times and bad. Human resource policies nurture reasonable risk-taking. Championing innovations in this environment is considered a sign of leadership.
- c. Most companies fall somewhere along the range depicted above. Where a company falls in this range will heavily influence its expectation regarding the *probability of realizing* the potential benefit from implementing a new methodology. This institutional experience (or memory) influences its willingness to implement, or to make a full commitment to implementation.
- d. Changes in an industry, or to a company’s position in its industry, can cause a management team to become more or less risk-averse than its history would indicate.

6. Implications for Decision-making Related to LIFESTYLE SEGMENTATION and Marketing

To summarize: We realize that there are three types of information a prospective client processes when considering LIFESTYLE SEGMENTATION and the related marketing.

- What are the facts about LIFESTYLE SEGMENTATION and its application in other circumstances?
- What are the potential benefits, risks and costs of implementation in my company?
- What are the probabilities of a successful implementation (i.e., of achieving the benefits) in my company.

The facts: LIFESTYLE SEGMENTATION is a relatively new methodology. However, it has been tested. It has produced significant insights when used for analysis (especially in conjunction with transaction data). *Many of these facts have been demonstrated using CLIENT data, including recent survey data.*

LIFESTYLE SEGMENTATION has produced significant results (*up to 500% increase in response rates and 67% reduction in acquisition costs*) when used in combination with LifeStyle messaging.

The benefits: Estimation of net benefits from the application of LIFESTYLE SEGMENTATION and marketing is a straight-forward process. It is possible to create scenarios based on different rates of implementation and different levels of investment. The assumptions behind these estimates will be extrapolated from the facts, above. *If further estimation of the benefits and costs is required, please let us know.*

The expectation of success: A candid discussion about the history of the client organization, its current markets situation and the elements in its culture that will support or challenge implementation is important.

Summary

There are types of errors in making decisions of this type:

- a. Implementing a “false hypothesis.” For example, implementing LIFESTYLE SEGMENTATION if it, in fact, were not true that the purchase behavior of affluent consumers at CLIENT (and potential prospects) varies significantly by LIFESTYLE SEGMENT. Or implementing it if the benefits did not outweigh the costs or provide a sufficient rate of return on the investment. Or implementing it in the face of clear historic examples in this organization of marketing innovations failing.
- b. Failure to implement a “true hypothesis.” For example not implementing LIFESTYLE SEGMENTATION if it is true that the purchase behavior of affluent consumers at CLIENT (and potential CLIENT prospects) varies significantly by LIFESTYLE SEGMENT *and if* the benefits of implementation do outweigh the costs and provide an attractive return on investment, *and if* the organization has a definite interest in supporting implementation.

The cost of (a) is a real and visible cost. On the other hand (b) is an opportunity cost and will not show up as an expense on the books. In the short term it may be the lesser of two risks.

Let us work with you to develop any additional information necessary to make the best decision possible. Let us make certain you have all the types of information necessary.