

Dancing Shoes for Honeybees

BREAKOUT



Mission: Possible

September 11, 2006

Darwin's turtle Harriet passed away



1835 - 2006

**It is not the strongest of
the species that survives,
not the most intelligent,
but the one most
responsive to change.**

Charles Darwin

Shorter business horizons

- A study of 6800 companies in 40 industries spanning 25 years showed:
 - Periods of persistent superior economic performance are declining in duration, over time
 - Hyper-competition not limited to tech sector
 - Successful companies now string together short-lived competitive advantages to sustain their success
 - Neither a large market share nor a concentrated industry correlate with sustainable success
- Other studies show similar results

Source: Wiggins and Ruefli study, 2001

Companies are at greater risk of failing

- Individual equity stocks are now more volatile than before
 - But market as a whole is no more or less volatile
- Average life of a company in the S&P 500 list in the 1950's was 25 to 35 years
- Today, it is 10 to 15 years

The velocity of innovation is increasing

- Economist Paul Romer estimates human beings are on average 30 times wealthier today than just 200 years ago
 - Despite having many times more people dividing up the same quantity of earthly resources
- Re-arranging our finite physical resources to create value requires two tasks:
 - Discovering new “instructions” for how to arrange resources
 - Carrying out those instructions

New ideas and innovations have their own “network effect”

Andy Grove and Gordon Moore at Intel, 1984



“If we got kicked out and they brought in a new CEO, what do you think he would do?”

“Why shouldn’t you and I walk out that door, come back in, and do it ourselves?”

Source: *Creative Destruction*, Foster and Kaplan, 2001

Some issues customer focus poses for your firm

- Adapting to an ever faster rate of change
- Avoiding “short-termism”
- Competing for a limited supply of customers
- Customer “co-creation”
- Dealing with customers who communicate with each other

Customers create value for a business two ways

**First, they generate current-period sales
and costs**

**But second, they change their *intent* to buy,
or their *likelihood* of buying, in the future**

Balancing between short term and long term

Attempts to increase current income affect a customer's lifetime value, and vice versa

- Marketing too aggressively can damage lifetime value, while
- Improving service to boost lifetime value costs money currently

**Taking a balanced approach
is critical**

Businesses face a crisis of short-termism

Would you give up real economic value to make this quarter's numbers?

What portion of American listed-company CFOs answer "yes" to this question?

In a recent survey, nearly 4 out of 5!

ROC is Similar to ROI

Both money and customers are used by a business when it creates more value

$$\text{ROI} = \frac{\text{Profit from investment} + \text{Change in value of investment}}{\text{Starting value of investment}}$$

$$\text{ROC} = \frac{\text{Profit from customer} + \text{Change in value of customer}}{\text{Starting value of customer}}$$

ROI answers the question:

How much value do you get for the *money* you have to use?

ROC answers the question:

How much value do you get for the *customers* you have to use?

Which Resource Will You Run Out of First?

Evaluating two possible customer experience expenditures	Value of customer	Investment required per customer	Net new value created per customer	ROI	ROC
Experience 1	\$100	\$10	\$30	300%	30%
Experience 2	\$100	\$40	\$100	250%	100%

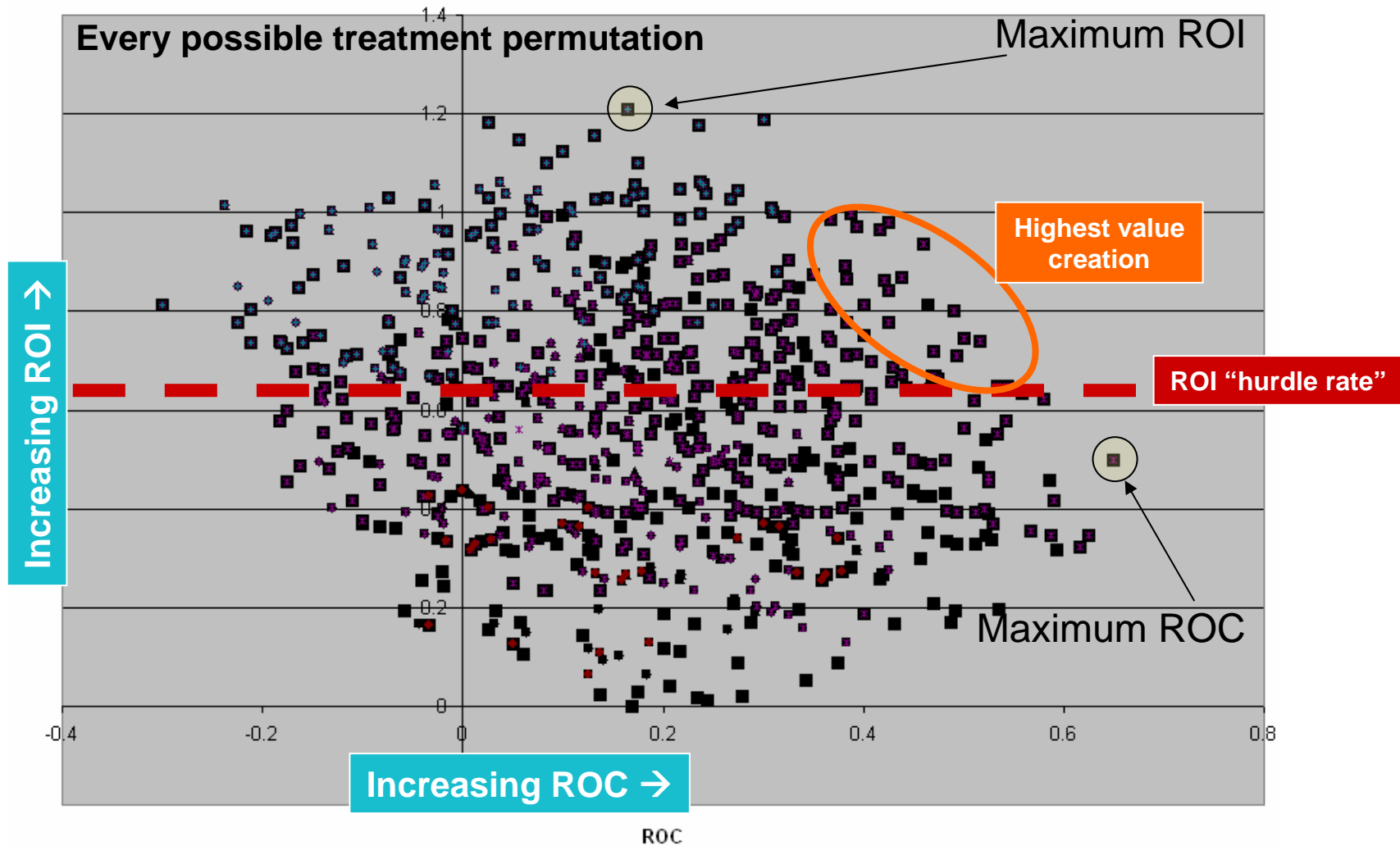
If **cash** is scarce

	Cash available	Customers affected	Net new value created
Experience 1	\$5,000,000	500,000	\$15,000,000
Experience 2	\$5,000,000	125,000	\$12,500,000

If **customers** are scarce

	Customers available	Investment required	Net new value created
Experience 1	300,000	\$3,000,000	\$9,000,000
Experience 2	300,000	\$12,000,000	\$30,000,000

ROI and ROC – Both measures together



How are humans and vampire bats similar?



Except for humans and some other primates, only vampire bats are capable of trusting non-relatives

Trust involves balancing an uncertain long-term benefit against a known short-term cost

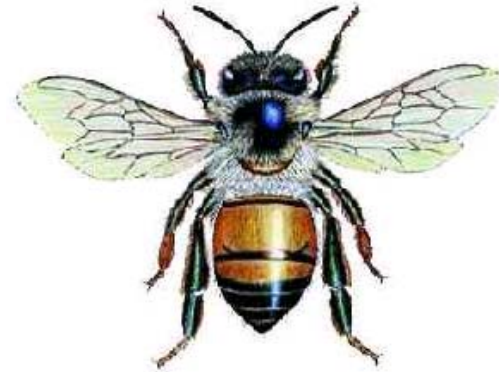
Creating a culture of customer trust



“Treat the customer the way you would want to be treated if you were the customer.”

- Forrester survey rated USAA highest in “customer advocacy”
“the perception by customers that a firm is doing what’s best for them and not just for the firm’s bottom line”
- According to Forrester, customer advocacy is...
 - “...the best indicator of whether financial services companies are able to achieve cross-sell success to a customer base”
“Firms that score highest, such as USAA, are considered the most for future purchases of products and services.”

Balancing exploitation and exploration



- Ants leave chemical trails, and honey bees do a dance
- But in addition to exploiting known food sources, ants and bees also explore to find new food sources
- Exploitation helps social insects live in the short-term, while exploration ensures long-term survival

Source: *Swarm Intelligence*, Kennedy and Eberhart, 2001

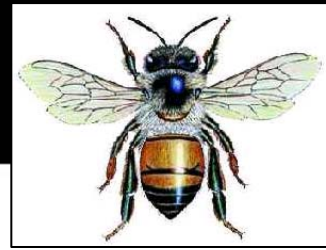
Suppose you were a bee food source...



Bright colors can get any single bee to take a look

- But a bee only does his dance to tell the other bees if he was satisfied with the nectar
- Moral: In the absence of communication among your customers, advertising rules
- Once your customers communicate with each other, it's the **customer experience** that counts

Give your honeybees dancing shoes

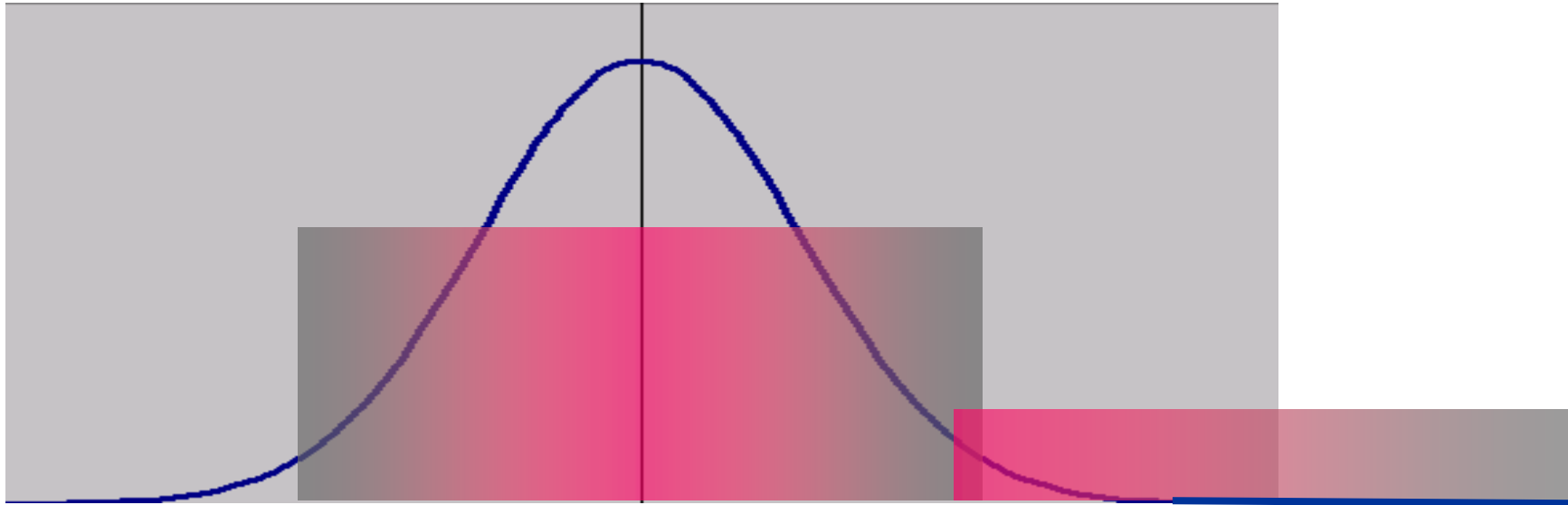


- Improve your “architecture of participation” by making it easy, interesting, and rewarding
- Rite-Solutions (software for military applications) has an internal “stock market” for good ideas
- 3M relies on “lead user” customers to experiment with home-made improvements and upgrades
- National Semiconductor provides an online platform for customers to design their own product improvements
- Innocentive signed up 30 blue-chip firms and more than 90,000 independent professionals, from 175 countries

Source: “Under New Management,” *New York Times*, 26 March 2006

Long tails and fat tails

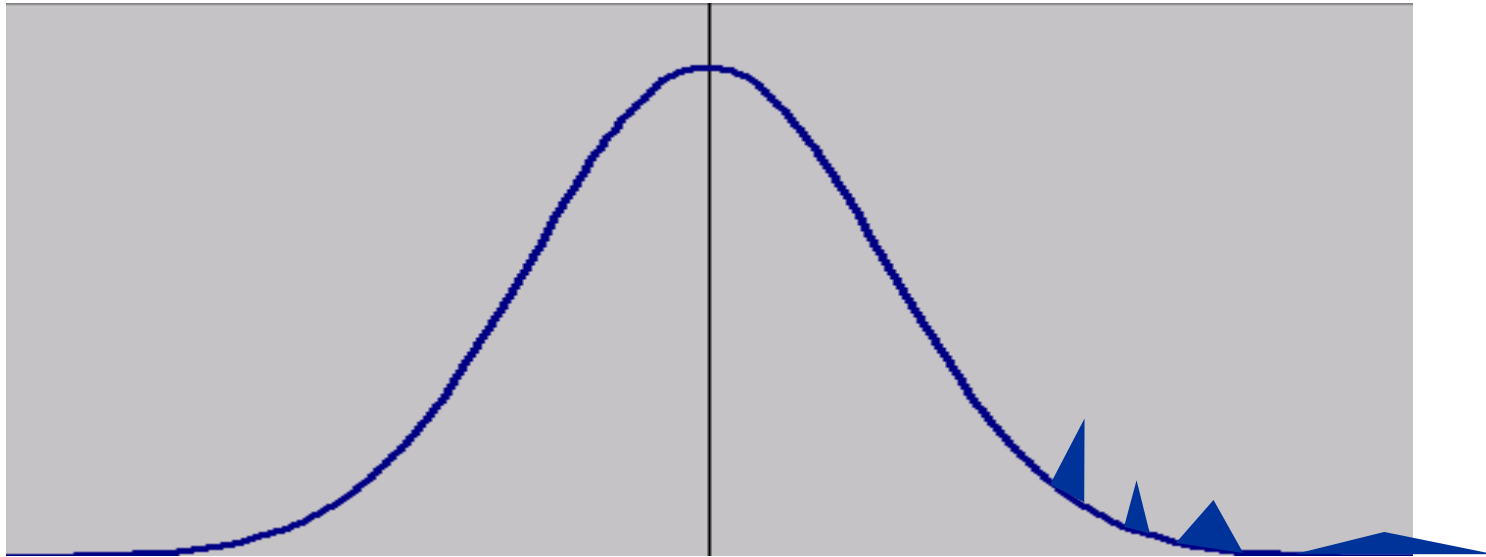
- In a non-1to1 world, products are designed for the large numbers of customers who are closest to the norm



- But as 1to1 marketing progresses, companies are increasingly serving the “long tail” of outliers

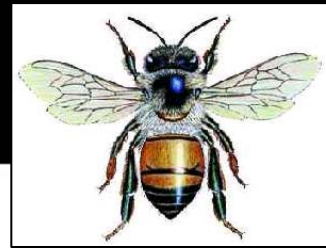
Fat tails occur when customers talk to each other

- Normal curves are designed for independent, non-interacting markets of customers, buyers, or investors



- But when customers imitate each other, fads and other irrational, unpredictable events happen
- “Fat tails” explain fads, stock market bubbles, weather patterns and galaxy formation

What do “fat tails” mean for you?



- Fat tails mean you cannot fully predict how customers will behave
 - It is impossible to “manage” word-of-mouth marketing
- Go ahead and give dancing shoes to your honeybees, but
 - Be prepared for that one irrationally cranky bee with a million close friends

Your most powerful competitive tool: *Trust*

*In addition to getting
customers to trust you...*

*...customer centricity will require
you to trust your customers!*

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