

Direct Marketing and MASB

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DMA

What is Direct Marketing?

- **Direct Marketing:**
 - “The planned communication of marketing offers to individually selected customers or prospects in order to generate a trackable transaction behavior (normally monetary) with the original marketer”
- **Differs from “mass/general/brand” marketing:**
 - “the communication of product or seller attributes to anonymous potential purchasers with no expectation of a behavioral connection to a monetary transaction directly observable by the original marketer”
- **Brand or “mass” marketing can also be seen as “indirect” marketing: advertising by national manufacturers that drives sales to third party retailers**

Why Is DM Significant for Marketing Accounting?

- “Interactive” nature of traditional Direct Marketing confers “targetability” to promotion activity and “trackability” to customers’ individual behavioral response (normally purchase activity)
- Trackable orders (response rates) attributable via key codes to media and promotion=Very predictable ROI from Marketing Budget
- Properly executed, interactivity directly supports precise accounting metrics without recourse to marketing or accounting surrogates
- makes ROI of DM promotion expenditure and supporting infrastructure investment normally highly measurable and controllable from an accounting standpoint

Economics of Direct vs. Indirect Marketing

- Resulting efficiencies in customer acquisition have traditionally been DM's principal competitive advantage vs. indirect mktg.
- Economics of advertising established products to anonymous repeat consumers and driving them to purchase "indirectly" via local retailing though inherently less measurable is normally profitable for all retentional selling, except for high-margin niche products requiring national efficiencies of scope
- Thus, measurability not necessarily correlated with profitability or efficiency

Economics of Direct vs. Indirect Marketing Cont'd

Thus, though ROI of direct marketing normally highly measurable, these measures revealed DM traditionally unprofitable for all but high-margin niche products, for most national advertisers

- Why is this?:
 - Individualized customer information is expensive to acquire and maintain (list rental, hygiene, databases, software) and conferred incremental marketing leverage only for a limited class of goods and customers
 - Historical limits to universality and cost of interactivity in national media
 - Logistics costs (Bulk rate for mass marketing, vs. piece-rate for direct marketing) of goods shipment via common carriers (sea, rail, road transport) favor third party retail distribution networks -- esp. “big box” retailing

How Does DM Fit Within the MASB Agenda?

Through most of 20th century, lack of interactivity in broadcast media meant that mass/brand marketers were unable to directly measure their marketing ROI, or were forced to devise ad hoc surrogates

- MASB thus a valuable resource for mass marketers, were best practice surrogates and alternative indirect measures need to be standardized and validated
- However, value of such surrogates to direct marketers not clear given its traditional targeting and tracking practices
- In addition, as explained below, there is significant and growing risk that universalizing standards devised to compensate for lack of direct financial accountability will be inappropriate in an era when digitalization of media increases interactivity and hence, opportunities for direct accountability

Digital Interactivity Changes The Game

- This picture has begun to change significantly in last 10 years due to digitalization of media and products
- As interactivity grows in importance across media, DMers see traditional DM accounting principles and practices as increasingly adaptable and efficient
- Key objective for DMA is
 - promote understanding of interactive economic and accounting assumptions beyond confines of DM
 - ensure economic efficiencies of interactive marketing not eroded by adoption of marketing accounting principles devised for non-interactive media

DM Core accounting practices:

- Traditional interactive Direct Marketing accounting has always focused on predicting and tracking individual customer purchase behavior in response to various combinations of list, offer, media, and creative
- Databases for Dmers today run to >500 billion transactions/yr, with 100-250 PhD statisticians or econometricians for an average firm
- Expenditure: Marginal cost of promotion activity is highly controllable, down to individual units;
 - Net of Cost of Goods Sold
 - Retention: Recency, frequency, monetary value
 - Customer Acquisition
 - List Rental=Cost of Acquisition
 - Average order size
 - Testability of offer, list, creative
- Revenue: Customer Retention
 - Planned contribution to overhead and profit
 - Lifetime value

Growing Interactivity in Marketing: Three Phases

- Direct marketing practices and accounting principles have always presupposed economically efficient national interactive media and common carrier networks
- changing economies of scope in addressability and responsiveness in different media (interactivity) resulted in three phases of utilization of DM practices and principles
- Traditional Phase: Original Interactive Media Channels:
 - Direct Mail
 - Telemarketing
 - (Later) Email
- “Direct Response” Marketing
 - DR newspaper, magazine
 - DR television, radio
- “Interactive” Marketing
 - Online Advertising
 - Search Marketing

Phase 1: Traditional Direct Marketing

- **Definition:** The targeting of marketing offers to likely buyers via the financial and statistical analysis of lists of recent/similar purchasers
- **Requirements: National Media**
 - Addressable at individual level
 - Unit-based pricing
 - Universal penetration and usage
 - National common carrier network for product fulfillment
- **Low cost marketing databases**
- **List rental market of previous purchasers**

Traditional Direct Marketing

■ Advantages

- For some products, allowed for low barriers to entry, high growth and profitability

■ Disadvantages:

- not efficient for most high volume, established or commodity products
- Introduction of direct marketing techniques into other media introduces element of “interference” in accounting principles

Phase 2: Direct Response Marketing

- **Definition:** the use of broadcast or print media to make response-based marketing offers leading to a final purchase from a national manufacturer or merchant
- **Requirements**
 - A separate order taking channel (telephone, website, fax) that facilitates customer response independent of the promotion media
 - Response costs must be borne by marketer but must be competitive with alternative sales channels, esp. retail
- **Crucial accounting step** involves the coding and tracking of a direct response mechanism e.g. an 800 number, URL, etc.

Direct Response Marketing

- **Advantages**
 - Facilitates trackable response from broadcast media
 - Allows wider reach than traditional direct media alone
 - Permits targeted and trackable upsell and cross sell during inbound response phase
- **Challenges**
 - Not yet targetable at individual level
 - Can't yet buy prior purchase behaviors, only audiences
 - Key coding and trackability is more costly, time consuming, more error-prone
 - Accessibility of response channels means some residual sales not directly attributable to original promotion
 - Full ROI analysis requires supplementary media mix modeling

Phase 3: Interactive Marketing

- **Definition: The optimization of on-line ad placement and sales portals to facilitate the making of inquiries or purchases by individual end customers directly from a national manufacturer or merchant without the intermediation of third-parties**
- **Includes both Targeted Online Advertising and Search**
- **Two search variants: “organic” and “paid” search**

3A. Targeted Advertising

- Much online advertising currently resembles broadcast advertising in that it is priced in terms of CPMs of publisher viewer demographics
- However, the superior economics of addressability (via ISPs) and tracking via cookies and self-registration is rapidly shifting online advertising to cost-per-action pricing based on unique customer attributes
- True targeting of online advertising based on viewer's purchase behavior will be next evolution, and is currently being developed by direct marketing analytics firms

3B. Search Marketing

- Two search variants: “organic” and “paid” search
- Organic search optimization is similar to retail: site selection, traffic measurement (volume, flow patterns), shopping cart optimization, etc.
- Paid search is similar to classic yellow pages advertising, but now with fewer geographic restrictions
- Crucial accounting step is tracking of search engine metrics
- Problem is that searching does not yet distinguish between true search (acquisition) vs. retention search (repeat visits to known sites sourced from search engine rather than address bar)

Conclusion: Current Situation

Emerging Issues

- Digitalization of media (TV, newspapers) and products (downloads, conversion of purchasing from transactions to subscriptions) driving increased integration of DM techniques across entire economy
- DMA sees adoption of DM accounting techniques by former mass market national advertisers will be next logical step
- Direct marketers see role for MASB in facilitating this development

Next Steps (Direct)

- Review What is Known & DMA POV @ Summit (Peter 7/7/08)
- Identify Project Partner @ Summit (Peter et al 7/7/08)
- Draft Project Frame-Up for MASB Review (Peter Sept 08)