EXECUTIVE INSIGHTS

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Accelerating the Paper-to-Digital Migration

Catalog marketing has a problem. Consumers are rapidly going digital, and the mailbox at the end of the driveway is looking more and more like a trash can. Some consumers just don't need or respond to paper-based "stimulation" anymore, and others simply need less of it. We see this in declining catalog ad ratios and inability to accurately forecast what was once a fairly predictable advertising medium. While this is all easy to observe, very few retailers have been able to meaningfully right-size their catalog spend due to fear of unacceptably impacting the top-line.

These dynamics are forcing retail executives to answer two core questions:

- How do we reduce direct marketing costs without putting the business at risk?
- How and where do we invest to ensure an impactful surrogate for the catalog?

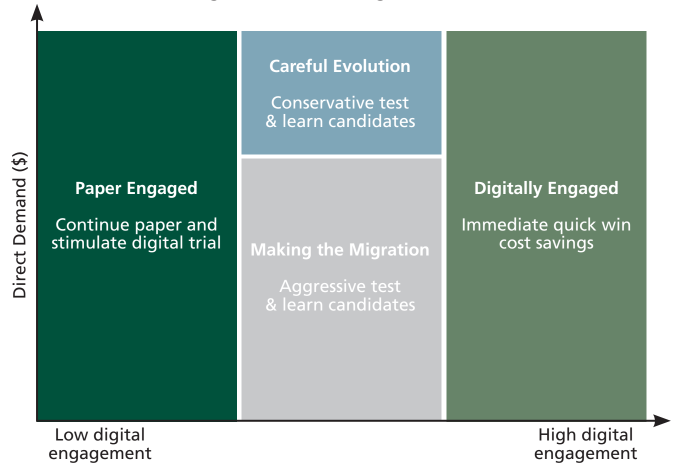
How Should Retailers Reduce Direct Marketing Costs Without Putting the Business at Risk?

Identify the Digital Behavioral Signals ™

Every day, your customers are communicating just where they sit along the continuum of "digital engagement" – you just need to be paying attention. The beautiful thing about digital behavior is that we can see it in real time and, by analyzing this

Figure 1

Digital Customer Segmentation



Source: L.E.K. analysis

behavior, we can start classifying customers in a way that allows us to treat them differently. In L.E.K.'s experience, most catalog marketers' customer files can be segmented relatively quickly into manageable groups, which serve as the foundation for strategies to rationalize paper-based outreach. We can simplify this to core dimensions of expenditure and digital participation (Figure 1).

Historically, most catalog distribution algorithms have been largely based on some variant of a recency, frequency and spend model. Retailers would build the catalog first, and then decide who should receive it. This approach, while normally resulting in positive overall ROI, can also eventually lead to suboptimal, costly over-mailing. Retailers have only fairly recently been able

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to turn this model on its head and look at the individual customer first and then decide which content she should be served – and how and when. Today, valuable data exists on customers' digital behaviors (i.e., what, when, where, and how they react to and engage across digital platforms) that allows marketers to be much more precise in calibrating their holistic outreach to each individual.

Initially, this precision takes the form of selective, systematic cost cutting, including:

- Eliminating or reducing select catalog drops based on customers' historical response profile to content, category weights or seasonality
- Building shorter, versioned books tailored more closely to individual preferences
- Using different and less costly forms of stimuli (e.g., postcards) depending on the role of an individual mailing with an individual customer segment

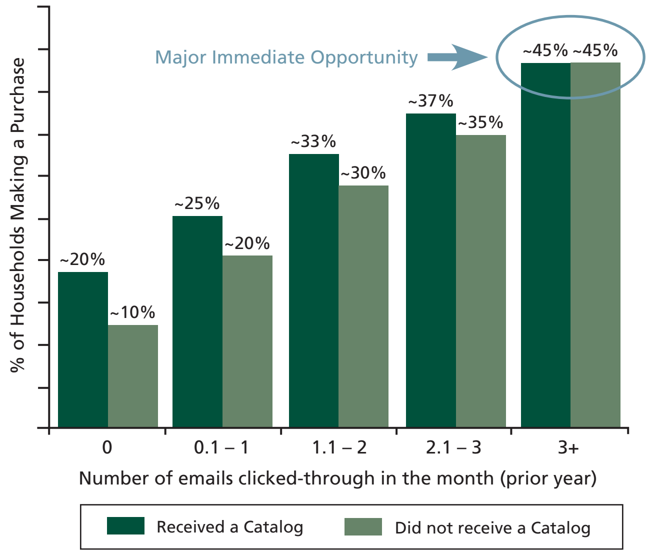
Notice we used the words "customer segment." By this, we don't mean the brand marketing segments, the customer profitability analysis sitting on your shelf or the litter of other segmentations that get wheeled out during every strategic planning cycle. We are specifically talking about a "digital engagement segmentation" that will allow you to pragmatically code each relationship in your file and methodically cut paper in the way most likely to succeed.

The fundamental principal is simple: reduce paper expense with your most digitally engaged customers first. This may not be a large group today, but it is a quick win with an immediate payback and it builds the confidence to start experimenting (more carefully) with the next tier. The tricky part is identifying and coding who is in which group. This starts with a robust investigation of which Digital Behavioral Signals you actively track. Digital Behavioral Signals are the footprints left by your customers as evidence of their level and complexion of digital engagement. A variety of attributes might be considered as potential Digital Behavioral Signals (e.g., e-mail click-through rate, web site dwell time, etc.) but the ones to watch vary by retailer and customer type. Once the signals are selected, the next step is analyzing which combinations of these attributes are most strongly correlated to how the customer responds (or doesn't respond) to different combinations of media. These predictive "markers" enable you to meaningfully segment the customer file (Figure 2).

Figure 2

Digital Behavior Analysis

Consumer Purchase Behavior with and without a Catalog



Source: L.E.K. analysis

Once the digitally engaged group is identified, the goal should be to strategically index each segment along the continuum and begin to rationalize the "middle." Those customers who "need" the catalog should clearly be left alone. And higher spenders should obviously be treated with kid gloves, particularly those in the "middle" gray area.

A note of caution: while the rewards of paper reduction can be great, companies can easily go too deep in their cuts. Although it's easy to sensationalize all the facts about the death of paper, the reality today is that catalogs are still very effective at stimulating purchase behavior for many customers, and this medium will remain a profitable part of the mix for years. Thus, rationalizing catalog distribution without putting the business at risk requires strong analytics and strategic insight into your customers' behavior; and a good dose of testing.

How and where do we invest to ensure an impactful surrogate for the catalog?

Give Your Customers a Reason to "Go Digital"

In order for paper reduction to work without a major hit to the top line, it is critical to have a clear strategy to encourage greater digital engagement in all customers and proactively seek to migrate as many as possible. There is clear upside to helping customers go digital. The logic at face value is simple: more digital customers equals reduced paper marketing cost. But a digital experience and marketing overhaul can be prohibitively expensive, so it is critical to appropriately prioritize investment. The first step is clear discipline and understanding of the objectives and responsibilities of each marketing contact point.

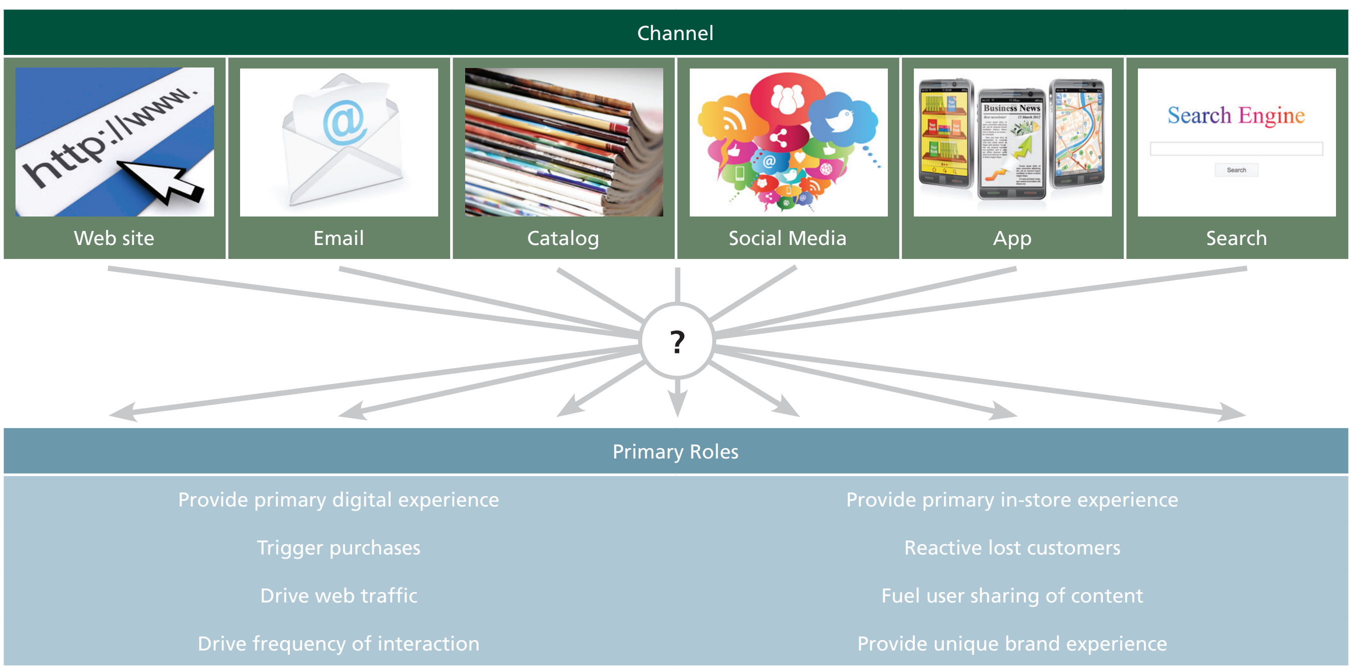
Identifying the right marketing media mix begins with clear definition of each medium's role in the customer's experience. The goal is to create a cohesive digital experience for the customer where each channel is complementary and not duplicative. For example, a mobile app that replicates the web site is a waste of money; it needs a clear and unique purpose (Figure 3).

For direct marketers, the most critical element of the digital strategy is the web site. The most effective direct marketers are able to use their web site to create a holistic brand and product experience for their customers, complimenting and potentially replacing the need for a catalog experience in some customers. Victoria's Secret, REI and others have done an outstanding job in this regard; effectively making the web site an "essential stop" in the passionate customer's rotating 20 channel attention span. Clearly this is a much easier task for a lifestyle brand, but every catalog marketer desperately needs to "create a reason" why a customer should proactively check back in. A clear brand identity and unique experiences within the web site also strengthens the customer's relationship with the brand beyond what is delivered by traditional transactional web sites. This is not a problem for IT to solve; this decision should be the foundation of the marketing team's brand plan.

At the highest level, a marketer should be able to point to the media being used to drive customer stickiness versus new customer acquisition easily. It is hard to do even one job well, so the various tools and channels should not all be trying to

Figure 3

Marketing Contact Point Role Definition



Source: L.E.K. analysis

accomplish everything but instead work in concert to achieve the myriad aims of acquisition, reactivation, stimulation, engagement, transaction, up-sell, etc. Clarity around these differing objectives should then directly guide the investment prioritization around initiatives such as increased usability of platforms, compelling content creation, driving social sharing, and behavioral change incentives.

Conclusion

The benefits of making the migration to digital are immediate. Each catalog marketer's customers are different, but nearly all are making the paper-to-digital transition in some aspects of their lives with or without retailers coaxing them. Customers are telling marketers how they want to be treated and are rewarding the retailers who listen. The secret is in finding your digital customer before the competition and being sure you have the ability to listen to what they are telling you. The rewards for successful retailers are rapid profit improvement and a much more defensible long-term positioning.

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