Using Multichannel Forensics To Understand Key Inflection Points
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If there's one thing catalogers and retailers have been taught since 1995, it is that we have to be "multichannel".

Multichannel experts approach the concept from several angles. Some strategies, like aligning inventory across telephone, website and retail channels, make perfect sense.

But other strategies aren't always appropriate. We're told that "multichannel customers are the best customers". We're told that "our customers expect to be able to buy online, and pickup in stores". We're given matchback analytics that tell us our marketing activities drive sales across all channels.

Well-meaning experts tell us these stories. Later, these individuals ask us to align our creative execution, pricing strategies, and marketing activities across channels, offering us multichannel products and solutions to help aid us in achieving multichannel nirvana.

In the past year, I've conducted Multichannel Forensics projects for sixty brand/channel combinations at many leading American and European multichannel retailers. What I've learned is that each business exhibits unique customer behavior that sets the business apart from others. I've learned how important it is for each brand to capitalize on its own unique customer behavior.

By now, you've heard all about Multichannel Forensics, a framework for understanding how customers interact with products, brands and channels. The framework was developed during my days as Vice President of Database Marketing at Nordstrom. In 2004, our executive team decided to shut down our catalog division, causing many leaders (myself included) to feel nervous about sales growth in the online channel. I needed to develop a tool to understand what impact this decision would have on our online and retail channels.

The first step was to determine how loyal customers were within each channel. We classified each channel into one of three loyalty modes, based on the likelihood of last year's customer purchasing within the channel again this year:

- Retention Mode: 60% or more of last year's customers purchase again this year.
- Hybrid Mode: 40% to 60% of last year's customers purchase again this year.
- Acquisition Mode: 0% to 40% of last year's customers purchase again this year.

We learned that retail customers were in "Retention Mode". These customers were extremely loyal. We learned that online customers were in "Acquisition Mode", meaning that they were not very likely to purchase from the online channel in the next twelve months. We learned that catalog customers were in "Hybrid Mode", meaning they had an average probability of buying from the catalog channel again within twelve months.

The second step was to determine how customers migrated across channels. We classified each channel into one of four migration modes, based on the channels customers were likely to migrate to:

- Isolation Mode: When customers are unwilling to migrate from one channel to another.
- Equilibrium Mode: When customers are willing to try different channels.
- Transfer Mode: When customers want to shift shopping behavior from one channel to another channel.
- Oscillation Mode: When customers shop one channel this year, then another channel next year, then switch back to the original channel in the third year.

We learned many interesting things about customer behavior across channels. Retail customers were in “isolation mode”, meaning they were not likely to shop the online or catalog channels. Online customers were in “equilibrium mode” with retail, and were in “isolation mode” with catalog. In other words, online customers were willing to shop in Nordstrom stores, but were not likely to pick up the phone and purchase from a catalog they received in the mail. Catalog customers were in “equilibrium mode” with both the online and retail channels, meaning that they were willing to shop on the website, or shop in stores.

This is where the “rubber meets the road”. Multichannel pundits tell you to have a seamless, consistent shopping experience across all channels. But in reality, retail customers didn’t want to shop via our website or catalog, and online customers didn’t want to shop via our catalog.

Because our retail channel generated the vast majority of sales, and because the online channel generated more sales than our catalog/telephone channel, it became possible to explore discontinuation of the catalog marketing program.

Of course, our financial folks wanted to understand the sales and profit impact of discontinuing a catalog marketing program. By understanding the in-flow of new customers by channel, by calculating the likelihood of customers purchasing again next year, and by quantifying which channels customers migrate to in the future, we were able to build five year sales forecasts that illustrated how sales were likely to change.

In our case, we learned that the online channel was great for acquiring truly new customers to the brand. Once the customer purchased on the website, the customer frequently placed her next order in a store. After that purchase, the customer became a loyal customer that used the website to research merchandise, but used our store channel to purchase merchandise.

This became the model for the direct-to-consumer channel at Nordstrom. We discontinued our catalog marketing program, opting instead for a brand-building monthly magazine mailed to best housefile customers. We discontinued our traditional catalog customer acquisition program (i.e. list rental, list management, and co-op participation). We re-allocated catalog marketing funds across various online marketing strategies. We then forecast the long-term impact of these strategies, finding that we could continue to increase overall profit on an annual basis. We were surprised to learn that we could continue to grow our online channel, without $36,000,000 of catalog marketing to support online sales growth.

This is an example of a five year sales forecast produced from a Multichannel Forensics analysis. The data is for an undisclosed brand, and is not meant to reflect the actual situation we encountered at Nordstrom.

Multichannel Forensics: Three Channel And Five Year Forecast									
				Beginning	After	After	After	After	After
	Retail	Internet	Catalog	Inventory	One Year	Two Years	Three Years	Four Years	Five Years
Existing Buyer	No	No	Yes	82,503	88,618	80,457	68,360	57,104	47,047
	No	Yes	No	85,692	97,904	106,142	113,283	120,062	126,729
	No	Yes	Yes	5,094	4,977	5,143	5,167	5,114	5,049
	Yes	No	No	588,608	604,164	622,131	640,638	659,386	678,477
	Yes	No	Yes	9,840	9,665	9,631	9,434	9,147	8,846
	Yes	Yes	No	33,983	34,909	35,107	34,937	34,608	34,220
	Yes	Yes	Yes	2,775	2,988	3,041	3,030	2,978	2,912
Newbies	No	No	Yes	67,739	60,000	50,000	40,000	32,000	25,000
	No	Yes	No	59,670	65,000	70,000	75,000	80,000	85,000
	No	Yes	Yes	1,901	1,901	1,901	1,901	1,901	1,901
	Yes	No	No	346,385	356,777	367,480	378,504	389,859	401,555
	Yes	No	Yes	3,612	3,400	3,200	3,000	2,800	2,600
	Yes	Yes	No	11,897	10,000	9,000	8,000	7,000	6,000
	Yes	Yes	Yes	640	500	450	400	350	300
12 Month Buyers, Total			Retail	635,206	651,726	669,909	688,039	706,119	724,455
			Internet	127,544	140,778	149,433	156,417	162,762	168,910
			Catalog	100,212	106,248	98,273	85,991	74,343	63,855
			Totals	808,495	843,225	861,652	874,849	888,398	903,280
12 Month Volume, Total			Retail		$92,809,058	$95,307,475	$97,789,765	$100,244,606	$102,722,700
			Internet		$26,908,557	$28,596,707	$29,909,727	$31,072,964	$32,189,143
			Catalog		$23,895,113	$22,413,750	$19,764,827	$17,146,078	$14,771,951
			Totals		$143,612,729	$146,317,933	$147,464,319	$148,463,648	$149,683,795

The advantage of a Multichannel Forensics analysis is the ability to accurately forecast long-term sales trends by channel.

At Nordstrom, we learned the following:

- Catalog marketing could be discontinued. Multichannel customer purchasing behavior did not significantly change as a consequence. Catalog-only customers largely stopped shopping at Nordstrom once the catalog was discontinued.
- The online channel had customers with marginal loyalty, customers who were willing to migrate to our retail channel. The online channel would be used to acquire customers who later migrated to the retail channel.
- The retail channel had customers who were unlikely to purchase online, but were willing to research merchandise online. As a result of this research, the website became a key multichannel research tool that facilitated e-commerce purchases if the customer felt compelled to buy online. But by and large, retail customers only liked shopping in stores, and were not likely to buy something online.
- Without a traditional catalog marketing program, we were able to continue to grow online sales, and were able to continue to grow retail sales.

As mentioned earlier, I analyzed customer behavior across sixty brand/channel combinations over the past twelve months, using the Multichannel Forensics. In nearly every case, there is a unique and evolving dynamic involving the catalog and online channels. This dynamic becomes very important to understand, given the pressure organizations like Catalog Choice are likely to exert upon catalogers in the future.

For the cataloger, the most important dynamic to understand is the relationship between the telephone channel, the online channel using a catalog key code, and a pure online channel order not influenced by catalog marketing.

The analyses of the past twelve months hint at a general trend that should be familiar to all catalogers:

- Customer used to order via catalog key code, over the phone.
- Customer switches channels, ordering via catalog key code on the website.
- Customer changes behavior again, ordering online without use of a catalog key code.

It is this evolution of behavior that must be thoroughly understood by the catalog marketer. Throughout the history of the multichannel movement, customers in the “telephone channel” and in the “catalog key code ordering online” channel were basically in “equilibrium”. As long as this trend held constant, catalog marketing was a critical piece of the marketing toolkit.

However, when customers “ordering online via a catalog key code” move into equilibrium/transfer with “online ordering without a catalog key code”, a fundamental change occurs. It is in this situation that matchback analytics become highly flawed. See, we can mail customers catalogs, but it doesn’t mean that the customer uses the catalog to purchase online. In other words, our matchback analytics frequently overstate the importance of catalog marketing among customers who become loyal to the online channel.

My experience indicates that this is the key inflection point where catalog marketing can be cut back without significant impact to sales or profit.

If I could share anything with catalog marketers, it would be this: “***Use Multichannel Forensics to understand key inflection points in the evolution of customer behavior, and adjust marketing spend across channels accordingly***”. Here are the key inflection points catalog marketers should understand, using the Multichannel Forensics framework.

- Identify the inflection point where customers shift from ordering over the phone to using catalog key codes to order online.
- Identify the inflection point where customers shift from using catalog key codes to order online to instead order online without the benefit of catalog marketing.
- When the latter shift occurs, begin scaling back catalog marketing expense among these customers, and then forecast the five year impact of this strategic change in direction.

This is the best way for the multichannel cataloger to apply Multichannel Forensics in 2008.

Questions:

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