

## Hillstrom's Zip Code Forensics:

The Relationship Between Multichannel Marketing And Geography

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### Easy and Actionable.

These are two words that Executives mention when discussing Multichannel Marketing concepts. Executives are not looking for complex concepts that are challenging to implement. Executives want simplicity that leads to improved business performance in the short term.

Few things in Multichannel Marketing are easier to understand than the concept of geography. For decades, leading marketers used various geographic segmentation schemes to understand customer behavior. Some of the popular geographic segmentation schemes employ more than fifty different dimensions.

Anytime a geographic segmentation strategy includes more than fifty dimensions, complexity is involved. Executives want something that is easy and actionable. Clearly, we need a solution that is tailored to the direct marketing and online marketing community, a solution that is exceptionally easy to understand, a solution that can be implemented quickly.

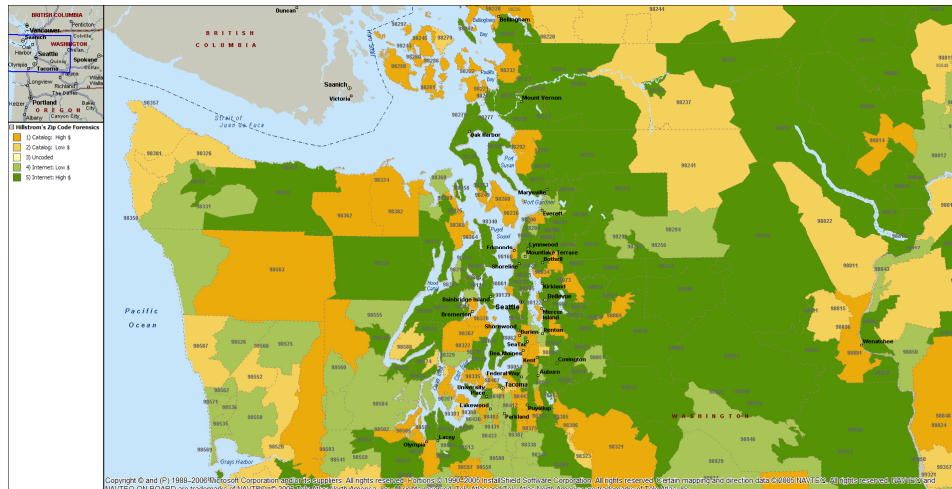
Maybe the solution includes a new tool, called “**Hillstrom's Zip Code Forensics**”.

Designed specifically for online marketers, direct marketers, and catalog marketers, “Hillstrom's Zip Code Forensics” result in every zip code in the United States being classified into four simple segments:

- **Catalog, High Spend:** These are customers who live in zip codes that prefer traditional direct marketing. The zip codes are high-potential, including customers who are likely to spend a lot of money if marketed to.
- **Catalog, Low Spend:** Customers in this segment live in zip codes that prefer traditional direct marketing. However, these customers do not have the spending potential of customers in high-potential segments.
- **Online, Low Spend:** Customers in this segment prefer digital marketing strategies like e-mail marketing, paid search, natural search, affiliate programs, shopping comparison marketing, and social media. However, customers in these zip codes are not likely to be high-potential customers.
- **Online, High Spend:** The final segment of customers include customers who prefer digital marketing, and are high-potential customers. These are the customers that the online marketer craves!

Every zip code in the United States is allocated to one of the four classifications.

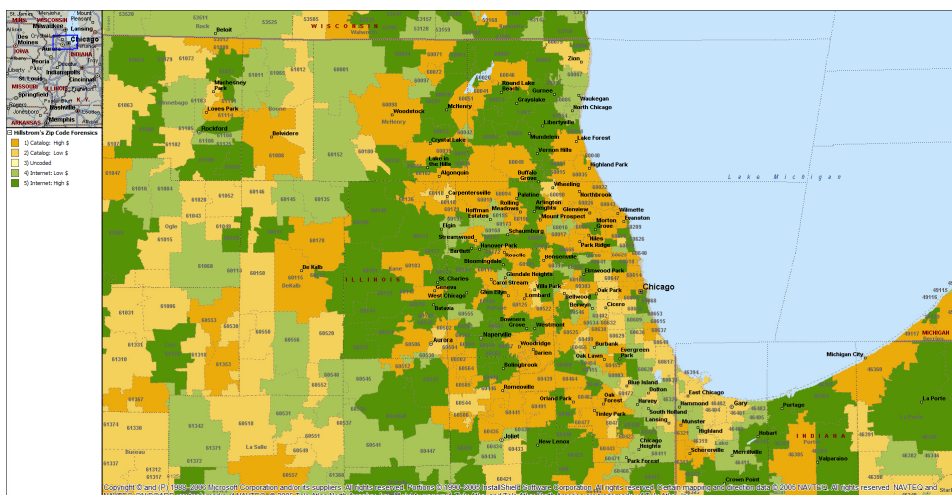
On the next page, we illustrate a map of the beta version of “Hillstrom's Zip Code Forensics”, featuring the Seattle market. Take a look that the trends that become apparent as you view the map.



Traditional customers live in zip codes colored orange (high potential) and yellow (lower potential). Customers who thrive on online strategies live in the dark green (high potential) and light green (low potential) zip codes.

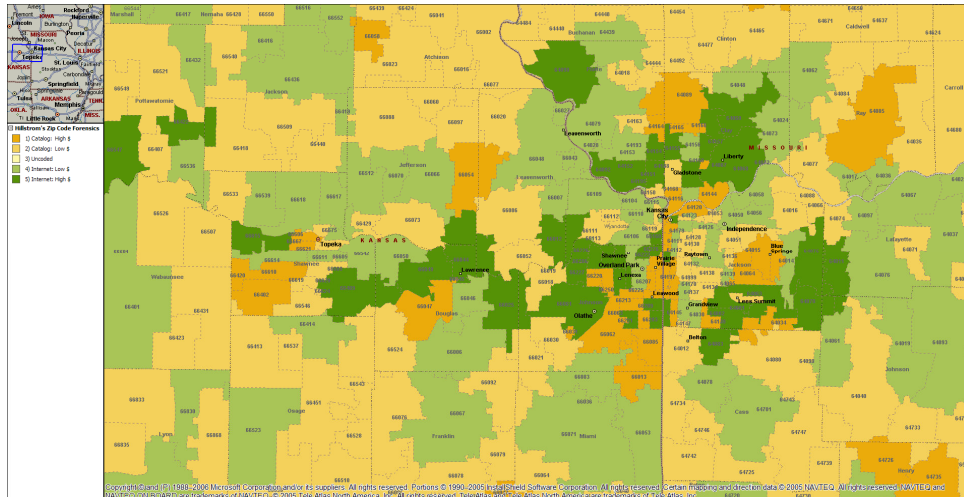
Not surprisingly, the east-side of Seattle, dominated by folks who work at Microsoft, represent high-potential online customers. Similarly, customers living up in the San Juan Islands, in the far northwest corner of Washington, are traditional customers who respond to traditional marketing strategies like catalog marketing.

Next, we look at the Chicago area.

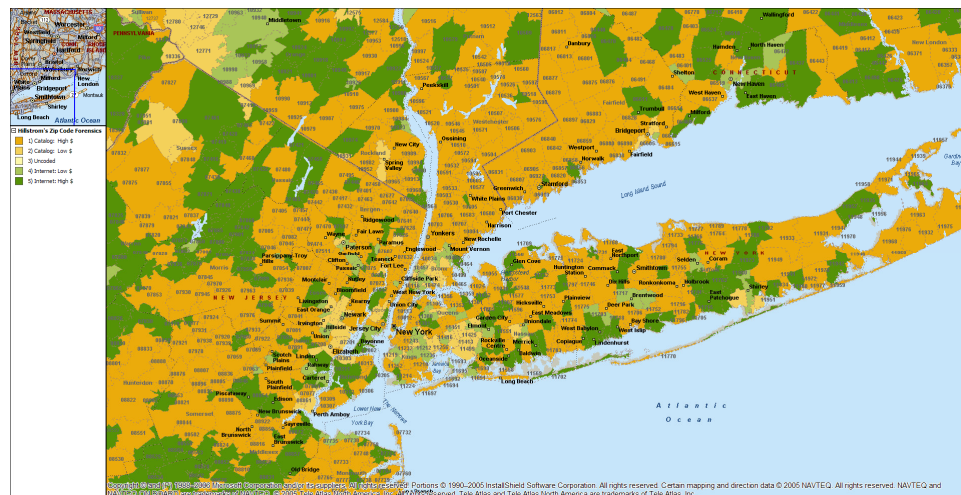


Dark green areas, in the northwest suburbs, represent high potential online customers. Orange areas, closer to the city on average, represent high potential catalog customers. On the south side of Chicago, we see lower potential customers.

This map shows us the Kansas City area. Notice that when you get outside of Kansas City, the sales potential of customers decreases --- the map is filled with light green and light orange zip codes representing low-potential customers. Also notice that there are higher potential customers along the Interstate highway between Kansas City and Topeka.



Let's look at one more map, featuring the New York City area.



Notice all of the orange on this map. The New York City area is loaded with high potential customers, customers that are very responsive to traditional catalog marketing. Catalog brands have thrived on relationships with these customers for decades.

## How Does The Segmentation Scheme Work?

The segmentation scheme is developed by aggregating the anonymous data of online and catalog marketers at a zip code level. The direct marketer provides a file of sales by channel by zip code for the past twelve months. The Excel spreadsheet looks something like this:

Zip Code	Phone Sales	Online Sales	Retail Sales
98101	\$29,348	\$35,004	\$225
98102	\$14,395	\$7,553	\$10,559
98103	\$3,371	\$3,508	\$3,262
98104	\$63,400	\$67,339	\$8,580

Total sales by channel and by zip code are compiled, on a completely anonymous basis.

The data, across multiple retailers, are aggregated. Then, a sophisticated algorithm combines Census Data and contributed zip code sales by channel, yielding the four segments that make up "Hillstrom's Zip Code Forensics".

### Can I Use The Segmentation System To Increase Profitability?

Without a doubt, the direct marketer can apply this segmentation system to direct marketing activities, and increase profit in the process.

On the next page, I illustrate an example of how a catalog marketer can apply the segmentation strategy to increase sales and profit. In this case, the catalog marketer is working with a prospect list from a co-op vendor. The prospect list performs at breakeven. The cataloger would like to overlay the segmentation scheme against the co-op list, selecting only customers who are in productive segments.

Let's look at the example.

Hillstrom's Zip Code Forensics: Case Study					
	<u>\$/Book</u>	<u>Profit</u>	<u>Phone</u>	<u>Internet</u>	<u>Total</u>
Catalog: High Performance	\$2.18	\$0.06	24%	-1%	9%
Catalog: Low Performance	\$1.46	(\$0.19)	14%	-54%	-27%
Internet: Low Performance	\$1.68	(\$0.11)	-38%	-2%	-16%
Internet: High Performance	\$2.14	\$0.05	-12%	18%	6%
Grand Totals	\$2.01	\$0.00			
Total Demand, Entire Segment	\$63,749	31,716 Customers In Segment			
Total Marketing Expense	\$22,201				
Total Profit, Entire Segment	\$0				
Total Demand, High Performance	\$49,930	23,109 Customers In Segment			
Total Marketing Expense	\$16,176				
Total Profit, High Performance	\$1,299				

There are 31,716 customers in the list provided by the co-op vendor. The cataloger can expect the list to generate \$63,749 demand, \$2.01 per catalog mailed, and can expect breakeven performance.

By selecting only the customers in the high performance zip codes (both catalog and online high performance zip codes), the cataloger eliminates 8,607 unproductive customers, generating an additional \$1,299 profit in the process.

This process is repeated across all unproductive segments. The cataloger only selects customers who live in productive zip codes. The profit generated across each list, across each catalog on an annual basis, more than pay for the cost of the segmentation strategy. The profit generated by the strategy allow the catalog marketer to open up more lists, lists that were previously unprofitable. Now, the cataloger cherry picks only the zip codes that provide highly productive customers.

## Business Evolution

Part of being a “multichannel” company involves taking steps to demonstrate that the marketing strategy aligns with customer productivity. Leading multichannel brands make sure that customer acquisition fuels high value segments. We can use our segmentation scheme to measure the evolution of a business. Take a look at the following example.

Hillstrom's Zip Code Forensics: File Evolution						
	2004	2005	2006	2007	2008	Chg/04-08
Catalog: High Performance	71,825	70,072	74,648	75,487	82,653	15.1%
Catalog: Low Performance	15,869	15,815	16,855	16,641	16,241	2.3%
Internet: Low Performance	25,362	25,612	27,176	26,398	27,657	9.0%
Internet: High Performance	57,744	56,642	59,722	64,446	73,027	26.5%
Totals	170,800	168,140	178,400	182,972	199,576	16.8%

This brand was able to grow by focusing on customers who live in high performance zip codes.

This style of analysis applies to channels and products. The business can be analyzed at a channel level, to understand if there is a mis-match between channel advertising strategies and the customers who are being advertised to.

## How Do I Participate?

“Hillstrom's Zip Code Forensics” is currently in beta mode. A preliminary strategy has been developed, one that appears to provide sufficient differentiation between zip codes, differentiation that can result in increased profit and reduced expense.

To complete the model, I am looking for ten additional online marketers, catalog marketers, or direct marketers to provide anonymous zip code sales data. If this algorithm truly becomes a product, the marketer will enjoy free updates and free access to the model for at least one year, and will receive quarterly updates at no cost, during at least the first year.

If this algorithm truly becomes a product, remaining participants will be able to join the database for an annual cost of \$5,000, and will receive quarterly updates at no cost during the course of the year.

The quality of the information will only improve as more companies contribute information to the database. Furthermore, as channels expand and change, the model will be updated to reflect changes in consumer behavior. Should enough multichannel brands with a store presence elect to contribute store data, the segmentation scheme will be expanded to include store information, allowing the participant to see where the vaunted “multichannel customer” resides.

## The Process

**Step 1:** Contact me ([kevinh@minethatdata.com](mailto:kevinh@minethatdata.com)) for instructions on sending your information to me. It may be that your information can be e-mailed to me, or delivered on a compact disk. You will provide contact information, including e-mail address, phone number, and mailing address. This information will be used only for model update purposes. You will provide me with data that is formatted similar to the illustration below (either in an Excel spreadsheet, csv format, tab-delimited format, or text format).



<u>Zip Code</u>	<u>Phone Sales</u>	<u>Online Sales</u>	<u>Retail Sales</u>
98101	\$29,348	\$35,004	\$225
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**Step 2:** I use programming logic to integrate your anonymous data into the database. The mathematical algorithm that determines each of the four segments is updated with your information and the information from other database participants.

**Step 3:** Should this algorithm become an actual product, you will be invoiced for the project fee (remember, the first ten marketers are included at zero cost). When payment has been received, you will receive a file with one row per zip code. A segment identifier will be attached to each zip code, containing the segment that the zip code belongs to.

**Step 4:** On a quarterly basis, you will receive an updated file containing new channel assignments (as marketing channels evolve) and updated segmentation as a result of changes to the mathematical algorithm.

### Questions:

**How is this segmentation system different than those offered by leading companies?** Basically, this system is designed for direct marketers, allowing direct marketers to execute catalog marketing and e-mail marketing campaigns against customers who live in different geographical regions. Other zip code algorithms focus on demographic attributes. Hillstrom's Zip Code Forensics is designed for direct marketers who wish to more profitably execute direct marketing campaigns.

**Why can't I simply develop my own zip code model, avoiding having to pay you to do this work?** You are more than welcome to develop your own zip code model! I've spent two decades building zip code models, and know full well that internally developed models are effective. If you choose to use this model, you will benefit from the contributed information of companies just like yours, and you benefit from the mathematical algorithms developed in this process.

**Is "Hillstrom's Zip Code Forensics" guaranteed to increase sales and profit?** No. Hillstrom's Zip Code Forensics will work differently for every company. Some companies are likely to see significant increases in the profitability of their direct marketing activities. Other companies will see minimal increases in profit. Some companies will elect to use the segmentation scheme to better understand customer behavior, incorporating the segmentation strategy in their business intelligence reporting dashboards.

**How might a cataloger use "Hillstrom's Zip Code Forensics"?** The cataloger will identify segments or lists that perform at or below breakeven. These lists will be sub-segmented based on the segments assigned to each zip code. The catalog marketer will not mail customers who live in marginal zip codes, and will mail customers who live in productive zip codes. The cataloger will likely analyze customer behavior over time, based on the segment the customer belongs to. In particular, the cataloger will determine if the mix of customers is evolving favorably or unfavorably over time. The cataloger is likely to monitor where new customers are being acquired, determining the impact this has on the brand over time.

**How might an e-mail marketer use "Hillstrom's Zip Code Forensics"?** The e-mail marketer will segment customers, potentially increasing e-mail frequency among productive segments, or reducing e-mail frequency among marginal zip codes.

**I work for a big brand. Will my information be disproportionate to smaller brands, causing my data to be “leveraged” by others?** The algorithm incorporates adjustments that discount the importance and influence of large brands.

**Will I get to see the other companies that participate in the database?** No, all information is anonymous. You will not get to see who the other companies are.

**Will my data be used in any other manner?** No, your data is completely anonymous, and will not be used for any other purpose. Your information will never be shared. Your information will only be used anonymously within the database, for the purpose of improving the algorithm that determines the segmentation scheme.