

# Chapter 1

STRATEGIC MARKETING

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**Don Peppers** and **Martha Rogers** are founding partners of Peppers & Rogers Group, a worldwide management consulting and media firm dedicated to helping clients improve the customer-facing sides of their businesses.

Peppers and Rogers have co-authored many best-selling books that offer new insights on customer strategy and building the value of the customer. They have devised an entirely new way of measuring the value that businesses create. Their latest book *Rules to Break & Laws to Follow: How Your Business Can Beat the Crisis of Short-Termism* shows how to maximise long-term profit by revealing what empowered customers, networked employees, innovation and trust can achieve for businesses.

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*Marketing's development over the past 100 years has been dynamic, delivering to enterprises genuine value from a wide range of benefits, including branding, customer relationships, innovation, and digital and social marketing. This dynamism has also produced significant challenges in promoting, selling and distributing products and services, challenges that stem from long-standing, but flawed, assumptions about how enterprises create real shareholder value. A long-term strategy for marketing – one that focuses on customer equity and not solely on current profits – can provide marketing with the context and objectives needed to maximise the overall value created by each customer. This is strategic marketing.*

## The past is ... past

Marketing strategy has too often been shaped by the need to imitate what worked in the past, what has been perceived to be successful for other companies or what is currently generating revenue for the company. Decision makers within enterprises review case studies and pursue best-practice guidance centred on the historical success of other companies, and while these behaviours can be reasonable adaptive approaches to the delivery of success, they function as default mechanisms. This behavioural mimicry is hard to overcome. However, our research and experience suggest that mimicking what worked for immediate profits in the past now leads businesses to settle for less and to make irrational decisions that overlook chances for real growth.

The unrelenting pressure to make concrete numbers right now submerges the instinct to do what is 'right for the company' and stalls forward-thinking business intelligence, eroding the long-term value of customer-first marketing strategies. We call this management development the crisis of short-termism.

Strategic marketing is future-oriented, requiring energy and the ability to balance hard, rational analysis with soft skills such as creativity. It also requires flexibility and the capacity to learn and change. Our suggestion to twenty-first-century business executives who seek to avoid the crisis of short-termism is to consider making a change in their mental model of success,

for both quarterly numbers and long-term financial results. Whether you are running a complicated business, developing the marketing strategy for that business, or conducting a marketing campaign, two straightforward principles for the model are that a) customer trust is an indisputable element for future business success; and b) employees' trust in the company is fundamental to their commitment to earning your customers' trust.

## The fallacy of short-term thinking

The fundamental task for marketing in the twenty-first century is to help businesses triumph over the fallacy of short-term thinking that seems to erode corporate performance at all levels. We identify some of these flawed assumptions about marketing as rules to break. Some of the truths we've learnt about long-term business thinking we call laws to follow, which we expand on later in this chapter. Most important for now, more than any other issue, is that these rules to break and laws to follow all point to the crisis of short-termism and how to make sure your company is not part of it.

It is tempting to believe that the best measures, or rules, for business success are a company's current sales and profits; that the right sales and marketing efforts will always get a company more customers; and that company value is created by offering differentiated products and services. These are assumptions about how a business thrives that are tied to the past, and they simply don't work any more. The speed and scope of technological innovation in the past two decades, particularly in the areas of analytics, interactivity and mass customisation, have made formerly accurate, useful and reasonable marketing assumptions obsolete. Adhering to these false assumptions leads to short-termism, a way of thinking that, rather than creating more value, ensnares companies in a cycle of value destruction. Businesses become obsessively focused on short-term shareholder value, revenue and profit at the expense of longer-term returns and the overall future value of the company.

### Short-termism and the Return on Customer metric

Business history is full of examples of once-great companies that managed for the short term and as a result no longer exist (or are certainly no longer

as great as they once were). Sometimes short-termism results from simple complacency: a belief that the firm is 'too large to fail', or that it is so venerated that the future will simply look after itself. At other times, short-termism is bred by outright fraud and corruption, as happened in the cases of Enron and Ameriquest.

Strategic marketing plays an essential role in capturing the greatest benefits for an organisation by developing a corporate culture and focus that look at each customer not only in terms of immediate profit to be generated, but also in terms of long-term value to be created.

Companies are tempted to – and frequently do – concentrate on short-term profit, because poor earnings numbers have serious repercussions for an enterprise's share price and the ability to raise investment, calling the business's future into question. The problem is that the narrow focus of short-termism does not maximise profits by thoroughly tapping customer loyalty and satisfaction opportunities, but instead leads to customer churn, which destroys loyalty and strengthens competitors while raising customer acquisition and maintenance costs and lowering profitability. Strategic marketing is based on accurate, relevant measurements that better reveal where a company's true value lies and it therefore mandates a balance of short-term success and long-term value building. It is essential to assess the return from each customer – what we call Return on Customer (ROC).

The ROC metric is a vital part of valuing a company's financial potential and determining strategic marketing priorities to realise that potential. ROC measures the value that a business creates or destroys with its actions, and ROC-efficient companies take action to build and maintain their Customer Equity (CE).

### The ROC equation

The long-term value of customers is often both poorly understood and improperly quantified. The best businesses operate as though customers are scarce and markets are

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competitive. To obtain maximum lifetime value from each customer, enterprises need to adopt an approach to marketing strategy that incorporates all areas of a business, but the most important territory to manage is how companies win and lose the trust of customers. ROC equals a firm's current-period cash flow from its customers plus any changes in the underlying Customer Equity (CE), divided by the total CE at the beginning of the period.

*The Return on Customer equation*

Return on Customer can be calculated as follows:

$$\text{ROC} = \frac{\Pi_i + \Delta\text{CE}_i}{\text{CE}_{i-1}}$$

Where  $\Pi_i$  = Cash flow from customers during period  $i$   
 $\Delta\text{CE}_i$  = change in customer equity during period  $i$   
 $\text{CE}_{i-1}$  = customer equity at the beginning of period  $i$

This calculation requires us to define what we mean by CE, which, unlike the tangible business asset of capital, is seen as an intangible business asset. A company's value, aside from its capital assets, relies on the sum total of its customers' combined lifetime value (LTV), a fact that by itself can help to determine how CE is used, consumed, altered and replenished in the course of business. It is necessary to keep in mind that there exists no fixed set of customers for enterprises to depend on, no guaranteed patronage pattern; customers can change their minds at any time about what to consume and how much of their money they spend doing so. It is companies' own actions that influence the future behaviour of their existing and prospective customers, and CE depends on every customer interaction being viewed as an opportunity to increase the customer's lifetime value.

Customer equity can be estimated by adding the future revenue stream received from each customer (a customer's lifetime value, or LTV) and adding to it all the lifetime values of current and future customers. By calculating the ROC, businesses will better know where they need to concentrate their resources and where they need to improve. Also, by knowing the potential future cash flows a customer is likely to generate over time, companies will know if the level of investment involved in acquiring that customer is justified.

The link between shareholder return and ROC is impossible to avoid: ROC measures the value that a business creates or destroys with its actions, and ROC-efficient companies build and maintain their CE. Essentially, they are two ways of looking at the same thing: how to maximise potential profit.

### **Key questions about strategic marketing**

- How does your company create value? How do your competitors?
- How could you deliver even greater value for your customers?
- How well do you and your colleagues know your customers? How strong are your customer relationships?
- Do you measure the Return on Customer? Do you see the value of a customer beyond the current purchase they have made? What do you do to get the customer to buy from you in the future?
- Does your business have the right balance between achieving short-term results and planning for the long term? How could this improve?

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