Finding The Next Customer

For companies that have matured beyond the days of easy growth, new and emerging customer segments may represent the next horizon. Financial service, consumer goods, healthcare, media, automotive, and technology firms are all looking to ramp sales by capturing that "next customer." They are tracking the increasing spending power of women, the spike in the Hispanic population, the influence of tweens, and the high loyalty rates of senior citizens. They are eyeing high value business owners, trend-setting college students, and growing communities of Asian Americans and African Americans. But how exactly do they lasso one of these segments and thereby capture the next customer? Put another way, how do they avoid becoming one of many companies to spend big but ultimately fail to win over a new segment?

This article describes an eight-step process and corresponding best practices to improve the odds for capturing the next customer. We lay out not only the theory but also tips from the trenches to help you properly define and sequence your target segments, design customer-facing and internal initiatives that address customer needs and behaviors, and calibrate your investment.

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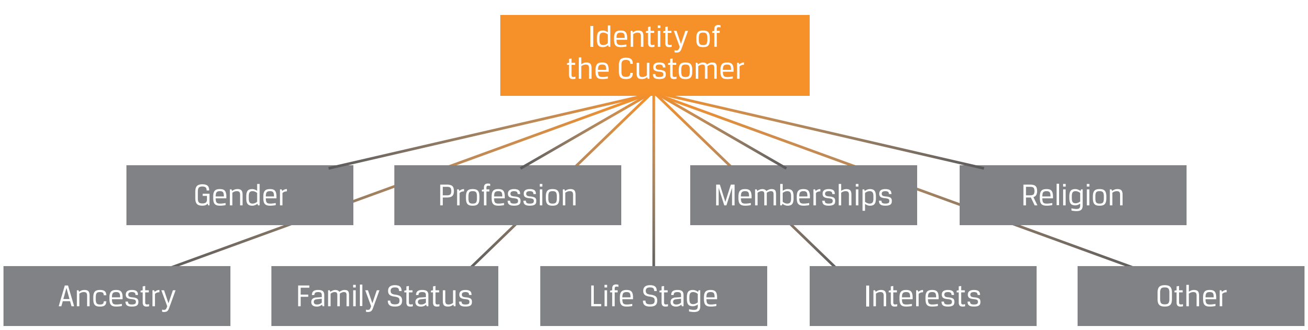
Step 1: Identify the Universe of Potential Segments

When you are looking for that next customer, where do you start? While many companies begin with one particular segment in mind – due to a mandate from the board or CEO, perhaps, or in response to a specific opportunity they are seeking to build upon – ideally you will develop a systematic portfolio of target segments. Rather than pursuing a segment "du jour," you should place it in context, ensure it is the most deserving of investment, and understand how it fits within your overarching segment strategy.

Begin by generating a master list of all possible next-wave segments for your company to pursue. Identify not only customer types who are naturally attracted to your product or service, but also those who have not traditionally been connected with your brand. To push your thinking beyond race and gender, consider all the ways that customers define their identities that could potentially serve as affinities you can approach. For example, brainstorm around ancestry, family status, profession, life stage, organizational memberships, interests, and possibly religion.

Do not worry about overlap at this early stage. Though some dimensions may be fleshed out in a mutually exclusive and collectively exhaustive manner – for example, family status could be subdivided into never married, married with children, married without children, separated or divorced, and widowed – others need not be. One financial services firm subdivided life stage into first-time car buyers, first-time home buyers, first-time parents, college students, retired workers, and relocators. There was obvious overlap between these groups, but they were still meaningful sub-segments for analysis given their differing needs, behaviors, and product demands. Adjustments for double-counting were made at a later stage.



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Step 2: Filter Segments for Distinctiveness and Growth Potential

Now that you have a comprehensive list of possible segments, you should apply a series of filters to prune your list. Answer the following three questions in sequence, narrowing the list along the way so that you do not invest time on non-starters:

Is this a meaningful segment for us to pursue?

Here, you are filtering out those segments that you do not expect to have unique needs in the context of your company's offering. If you cannot imagine a segment requiring specialized effort across marketing, product, distribution, or service, then delete it from your list. Similarly, if the segment's needs appear very likely to overlap entirely with those of your existing customer base, eliminate it from consideration.

You should also consider whether your organization could plausibly serve the needs of each segment. In some cases, there may be such a wide gap between a company's culture and a potential market segment that even an aggressive initiative could not bridge it. In other cases, there may be regulatory constraints that preclude you from pursuing a particular market segment. For example, certain financial service firms may run afoul of regulators if they vary product or service by race, ethnicity, or gender. Before discarding a segment on this basis, though, check whether it may be reframed or recast in an acceptable manner (e.g., targeting underserved zip codes rather than pursuing a particular race or ethnicity).

Is this segment demographically attractive?

Next, rank the remaining segments according to demographic data, demand indicators, and other measures of segment attractiveness. When assessing demographics, examine the size of the segment, the five-year population growth rate, and the degree of geographic overlap between the segment and your company's footprint. Useful sources for this exercise include raw data from the U.S. Census and Bureau of Labor and Statistics as well as third-party vendor databases.

Demand indicators help gauge likely consumption or expenditure levels. You should focus on data that is most relevant to your industry – insurance carriers, for example, might look to home and auto ownership rates and home and auto values while a consumer goods firm could use share of wallet. More generic demand indicators like buying power and age distribution (e.g., the percent of the segment that is 18 or older) may also prove useful. A segment may be large, fast-growing, and perfectly aligned with your company's footprint, but it is a

Step 2: Filter Segments for Distinctiveness and Growth Potential *(continued)*

nonstarter if it is likely to yield low-value customers. Socioeconomic data can supplement the more direct demand indicators. Data on median household income, income per capita, and educational attainment, for example, are readily available for many sub-markets.

To pare the segments at this stage, create a scorecard that spans the most relevant segment characteristics, weight them appropriately, and look for natural breaks in the list. Ideally, you will have 10 to 15 actionable segments at this point. If you are having trouble narrowing your list, you can add in a more subjective factor – your assessment of how strongly individuals in the segment identify with the group. For example, "home buyers" or "empty nesters" are legitimate segments, but (depending on the product or service) consumers may feel less affiliation to these aspects of their identity than to others.

Do we already have our fair share of this segment?

The third step in pruning is to eliminate those segments you have already captured in proportion to your overall market share. One healthcare firm thought that Hispanics were its "next customer" and spent millions pursuing them, only to learn retrospectively that it was already substantially over-penetrated in this market. In the meantime, Asian Americans were massively underrepresented in its customer base, especially considering the firm's geographic footprint.

Market share analysis is essential but tricky. The complexity and amount of creativity required will depend on the segment and the availability and quality of the data in your customer database. Gender tends to be easy. Asian American and Hispanic market share usually can be predicted with an algorithm using customers' first names, last names, and home addresses. Market share among African American prospects may need to be estimated using zip codes alone.

Beyond analyzing their databases, companies may choose to survey their customers or poll their employee and distribution forces. If your surveys suggest that 3% of your customer base in a given area lives in female-headed households, and Census data tells you that 15% of the population in that territory meets that criterion, then you can be confident that you are under-serving that segment. Surveys tend to be a good solution for probing dimensions like life stage or family status that may be unknowable otherwise. But they can be costly and time-consuming, and could be considered intrusive by customers or even by regulators depending on your industry and what dimension you are probing.

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Step 3: Build an Initial Portfolio Based on Cost, Impact, and Timing

At this point, you have probably trimmed your list to 5-10 segments. Your task now is to arrange these remaining segments into a portfolio of target markets. The portfolio approach avoids the folly of over-investing in a single target market. It also recognizes that the successful capture of some segments will require greater lead time, the acquisition of new skills or knowledge, and the careful pacing of investment.

To design your portfolio, you should plot each of the potential target segments according to likely timing, cost, and impact. Timing, which is shown as the X axis in the figure on the following page, represents the amount of lead time your company would likely require to assemble an initiative aimed at the target market. Target segments that are similar to your current core customer base may be addressed in the near-term, while those that are very different from your existing customer will require longer-term acquisition of capabilities and knowledge. Cost, shown on the Y axis, represents your back-of-the-envelope estimate of the investment required across marketing, distribution, product, and service to meet the needs of the target market. For now, assemble a cross-functional team to pool insights and to create a consensus estimate; over time, you will refine your cost projections as you gain greater clarity on the nature of the solutions you will be launching to capture each segment. Estimated revenue impact is reflected in the size of each bubble, with each bubble representing one target segment. Use the data on market size and demographics that you collected previously to build a mini-model that estimates the impact of capturing your fair share of each segment.

Once you have plotted the segments, you will need to assess and refine. Eliminate any segments that appear to require heavy or sustained investment out of proportion with likely impact. Make sure you have a mix of short-term incremental opportunities ("easy wins") and long-term payoffs ("game changers"); if not, you may need to reconsider previously eliminated segments. Finally, based on the contours of this chart, highlight the 5 or so segments that will be your greatest priorities. These should be those segments with the greatest impact in the short term and long term and the most attractive relationship between cost and impact.

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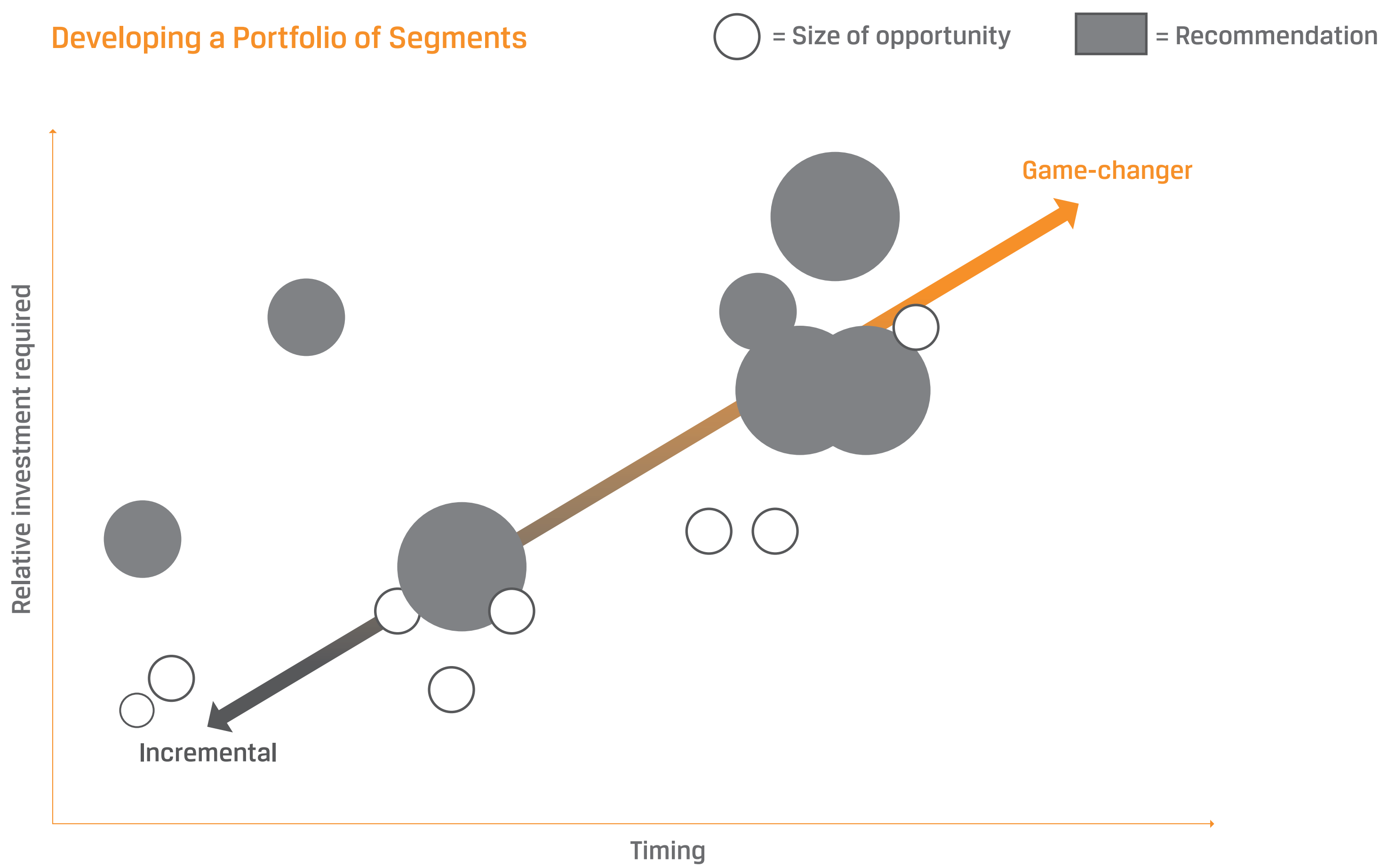
Though the rest of this article will focus on how to begin pursuing the markets you have just prioritized, you should expect to regularly revisit this portfolio analysis. First, you should use it to guide the staging of your investments. While you should be willing to spend today to capture near-term opportunities with modest investment required, you will have to pace your investments carefully with respect to longer-term, less familiar segments, investing in research and pilots to validate the opportunity prior to authorizing larger expenditures. Second, you should update the portfolio tool twice a year to make sure you still have a healthy mix of short and long-term opportunities. There is always another customer to pursue.

Developing a Portfolio of Segments



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Step 4: Create and Syndicate the Business Case for Initial Segments

Now that you have your short list of prioritized segments, you must build a financial model and business case document for each segment that will help you syndicate your recommendations and build institutional consensus. The most successful "next customer" initiatives are those with broadly communicated buy-in from top executives and early engagement of the sales and distribution force. The business case is the platform that you will use to tell the story of why the targeted segments warrant an investment of the company's attention, talent, and financial resources.

The business case should address the following:

What is the high-level opportunity presented by this segment?

- What are the demographics, demand indicators, and other measures of segment attractiveness that led you to prioritize this segment?
- What is the total addressable market size represented by this segment?
- What evidence supports the conclusion that your company is currently underrepresented in the target market?

What must the company do to capture the segment?

- What are the relevant needs and behaviors of the target segment?
- How great is the current gap between your company's baseline offering and these needs and behaviors?
- What are the current hypotheses on what customer-facing and company-facing initiatives (across each of marketing, distribution, product, and service) will be required to close the gap?

What is the projected financial impact for the company of pursuing the target segment?

- What are low, medium and high probability scenarios of the potential gain from capturing this market?
- Given the hypothesized initiatives, what costs do you expect (at a high level)?
- What is the bottom line financial impact, and how does this fit in with the company's five-year plan?

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Step 4: Create and Syndicate the Business Case for Initial Segments *(continued)*

The financial model will inform, in particular, the first and third sections of the story. Though the cost portion of the model will be underdeveloped at this stage (and will need to be revisited as part of Step 7 below), the revenue portion should be very robust at this point. Best practice is to model five-year economic projections on a quarterly basis and to integrate low, medium, and high scenario assumptions with a user-friendly toggle. Depending on the nature of your company and the targeted segment, you must decide whether to use a customer-centric or a sales force-centric modeling approach. The customer-centric approach drives revenue from customer decision-making and relies heavily on the demographic data used in the mini-model described above. The sales-force centric approach drives revenue from the likely impact on the behavior and traction of your sales force or distribution mechanisms. In either case, we recommend introducing sufficient granularity into your assumptions (for example, by sub-segment customer groups and swaths of your distribution force) to enhance the accuracy of your modeling.

The business case document itself – typically a presentation rather than prose – must achieve the dual goals of painting a perhaps-lofty vision and laying the tracks to completion. While all of the analysis, brainstorming, prioritization, and business case-building may have been completed by a relatively small group of team members up until now, going forward the initiatives in your business case must become a company-wide priority embraced by all functions and lines of business. This is the time to ensure corporate consensus. Along the way, ask for dedicated resources to join your team going forward, and ask for subject matter experts tasked with helping your core team during the solution design and implementation stages.

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Step 5: Conduct research if necessary

Primary research may be required at this stage to confirm the addressability of the target segment, to sub-segment markets when you have a hunch that a universal approach may fall short, and to gain deeper insights into needs and behaviors so as to enhance the efficacy of the solution design described below.

In our experience, addressability and sub-segmentation can be addressed largely through surveys, while insights into needs and behaviors are best elicited in focus groups. Focus groups will also be the proper venue to test creative work, positioning, and messaging down the road, while one-on-one interviews are most effective for in-depth usability testing after solution design has been largely completed.

Sub-segmentation is tricky. Some markets may be actionably segmented along demographics (for example, some financial service companies sub-divide the Asian American market into Asian Indian, Chinese/Taiwanese, Filipino, Korean, Vietnamese, and other). Others may require psychographic, geographic, or behavioral segmentation.

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Step 6: Identify and prioritize internal and external solutions

You have already developed a set of hypotheses on what customer-facing and internal-facing solutions will be required to attract, convert, and retain your target segments. You even previewed some of these as you syndicated the business case within your organization. Now you will take solution identification to the next level, collecting ideas from a much broader set of executives and front-line employees and harnessing research insights to round out your list of possible solutions. Then you will prioritize these solution ideas in much the same way you prioritized your target segments, developing a portfolio of solutions for each segment.

Your team is well prepared at this stage to facilitate an open but structured innovation session. You can hold one large-scale session with representatives from throughout the organization, or you can oversee a series of smaller group sessions. Either way, you should prep participants in advance with some of the insights you have gathered on the preferences, demographics, purchasing patterns, needs and behaviors of the target segment.

During the innovation sessions, make sure to:

- Remind participants of key highlights of the customer research
- Provide "big idea" case studies on how comparable companies in other industries captured the target segment
- Provide case studies on how competitors approached the target segment
- Organize breakout sessions either by function (e.g., marketing, distribution, product, and service) or by themes emanating from the customer research
- Rotate participants through breakout sessions, spreading out the representatives from each functional area or product line to ensure the cross-pollination of ideas
- Force participants to rank-prioritize suggested solutions

Once you have a comprehensive list of possible solutions, create a portfolio of solutions using the same approach you used to select your portfolio of segments. Using input from relevant stakeholders throughout your organization, plot the solutions according to likely impact, cost, and timing. Then select an array of solutions that offers both quick wins and longer-term game-changers. Be ruthless in controlling the scope of your efforts; we have found that very few organizations can successfully launch more than 3-5 customer-facing solutions and 3-5 internal-facing solutions at a time.

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Step 7: Create detailed implementation gameplans for each solution

Once you have filtered and prioritized, you are ready to flesh out the design of each major solution. By now, you should have a working group with representatives from all product and functional areas of the company. Create sub-teams for each major solution based on expertise and task them with creating a blueprint document that consists of:

- Key objectives of the solution
- Specific customer needs and behaviors the solution is intended to address
- Industry best practices and assessment of competitor approaches
- Overview of primary options for the form and delivery of the solution
- Detailed specifications, requirements, and features for the solution
- Assessment of roll-out options (e.g., pilot, staged, full roll-out)
- Budget with key milestones
- Human capital resource requirements
- Granular development timeline
- Ongoing metrics to track project success

Putting the "meat on the bones" of each solution can take two to three months depending on the complexity of the solution. This is where the team must work out the all-important but headache-inducing details. By way of example, one insurance carrier decided to revamp a customer-facing website to demonstrate its commitment to a newly selected customer segment. To create the blueprint for the website, the sub-team had to revisit their findings on how consumers used the web to purchase insurance; resolve longstanding disagreements among product lines over the integration of their sites; find ways to differentiate from competitor sites; tackle tough questions around the role of community features, social media, search engine optimization, and search engine marketing; manage an information architect and designer; and much more. Yet the investment paid off – by tackling every detail in the planning stage, they set themselves up for a smooth implementation and laid the groundwork for what was ultimately a highly successful launch.

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Step 8: Execute and Measure

If you have secured adequate funding, attention, and resources, you are ready for the implementation stage. You will guide your team – and, hopefully, an assembly of functional and product experts drawn from throughout your organization – in translating your blueprint into action.

For each solution you are pursuing, you must decide whether to start with a pilot or proceed with a full launch. Pilots can be an excellent tool in helping you calibrate your investment, as they permit you to test the waters prior to funding the solution fully. Pilots also may be implemented quickly and allow you to tweak and refine a solution prior to a broader roll-out. Yet pilots do not always make sense. To evaluate the appropriateness of a pilot, assess the following five factors (multiple "Yes" answers suggest a pilot):

- Does the investment in this solution scale as you increase the geographic reach? For example, the cost of opening new offices increases as you add geography, whereas the cost of developing a web site does not increase (provided you have the server capacity) as you make it accessible to additional geographies.
- Do you anticipate needing to revise your initial solution in the near term, as you receive feedback from the market? This is often the case when a solution is designed in an environment of uncertainty.
- Does the solution require the use or development of unfamiliar technologies, such that you are likely to run into technical obstacles?
- Does the research conducted to date indicate that this segment might be a "stretch" for your company, or that your distribution force might resist pursuing the segment?
- Is the solution you are launching fairly specific to the needs of the target segment (instead of being broadly applicable or even urgent for the company)?

Whether you have chosen a pilot or full launch, you will need to track each solution and the initiative as a whole. Ongoing measurement is essential to demonstrate the impact of your efforts, to create a feedback loop for continuous improvement, and to calibrate additional investment. It is easy to collect data; the hard part is collecting the right data and translating it into insights. Here are some tips:

- Develop both impact metrics and activity metrics. Impact metrics gauge whether your efforts to capture a segment are succeeding and driving financial results, and include trends in market share, cross-sell rates, account density, revenue, and net income. Activity metrics gauge whether your employees and field force are using tools you have

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provided and generally doing what you have asked them to do. For example, are they enrolling customers in a new program, making use of an online resource portal, or allocating marketing spend as planned?

- Start with your organization's goals for the initiative and turn these into specific questions that can be answered to assess your progress against these goals. For example, one company launched an initiative focused on the business owner segment to grow its share of business owner customers, attain a specified amount of incremental revenue, increase cross-sell rates to existing business owner customers, and help its distribution force achieve greater diversity in the distribution of their commissions across different lines of business. Each of these goals was translated into a question (e.g., Are our field agents becoming more balanced over time?), and the company then isolated two to three key statistics to answer each question.
- Include IT and Finance personnel early in the process. They are more familiar with the limitations of the company's systems and databases and can layer reality onto your list of ideal metrics. Equally important, the more they are looped into your team's thinking, the more they will understand the importance of the metrics and help push for systems modifications that enable reporting.
- Find ways to account for overlap with other initiatives and even for cannibalization of legacy efforts. If you fail to do so, you will lose credibility when you claim credit for the impact of your initiative. At times, overlap adjustments can feel quite data-driven and scientific, as when one organization created decision rules grounded in Census data to allocate credit for revenue growth among overlapping efforts to capture female, Asian American, and Hispanic prospects. At other times, the adjustments are more art than science. In either case, you should syndicate the overlap adjustments in advance to eliminate controversy down the line.

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Conclusion

Finding the "next customer" holds the promise of enhanced profitability and corporate longevity, but it also carries the risk of expensive failure. The eight steps outlined above are intended to help you maximize your chances through a data-driven selection of target segments, a portfolio approach that sensibly allocates risk and investment, a consensus-building process that generates institutional momentum, a matching of corporate initiatives to customer needs and behaviors, and a more rigorous implementation discipline. By adhering to these best practices rather than instinct or impulse, you can win over new segments and reach a new horizon of growth.