

## Changing the Game *How Smart Enterprises Leverage Customer Intelligence to Win.*

By Britton Manasco



As Michael Lewis powerfully demonstrates in his recent best-seller *Moneyball: The Art of Winning an Unfair Game*, organizational success is not, essentially, about the *amount* of money you spend. It's about the *return* you generate on that money. How else might one explain the ability of one of baseball's poorest teams – the Oakland A's – to consistently win games and secure a position in the post-season playoffs?

While other teams paid top dollar for top stars, Oakland crunched the numbers and analyzed the statistics to determine which players were *undervalued* – and therefore, who to draft and who to trade. The team even reexamined conventional baseball statistics and learned how such stats entice others to make irrational, ineffective and financially reckless decisions.

With a payroll less than one-third the size of many unsuccessful teams in the league, the A's have reached the playoffs for the past four consecutive years – an incomprehensible feat to all those who think money rules the game. “At the bottom of the Oakland experiment,” writes Lewis, “was a willingness to rethink baseball: how it is managed, how it is played, who is best suited to play it, and why.”

Oakland General Manager Billy Beane, the story's hero, proves that organizations with rigorous analytical capabilities, actionable intelligence and a willingness to defy conventional wisdom can outmaneuver the entrenched, established and well-financed.

But this new knowledge is not merely for the Davids who wish to slay the Goliaths. Even successful, league-leading teams – or market-leading companies – can secure their standing by investing in initiatives that promise the highest payoff. Statistical analysis – *the numbers*, in other words – can tell us what our own gut, our intuition, our rules of thumb, our experiences and our conventional wisdom cannot.

It's not enough, however, to simply compete on one's smarts. In the realm of business and other fields, it's also critical to *leverage* that intelligence. “This is really a game, if you will, not only about how much you know about your customers but how well you can act on what you know,” says Scott Nelson, vice president and research director with Stamford, Conn.-based Gartner.

“If you can develop valuable insights about your customers and then, act on them, you are going to beat a rival that doesn't really know their clients in the first place or even one that can do the analysis but can't turn it into actionable advice,” he says. “Put those two pieces together and it doesn't really matter what your size

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is, what your brand is – any of that stuff. You’ll be in a position to make intelligent decisions that your rivals cannot.”

While the value of truly intelligent decision-making can be expected to become more clear and pronounced in the coming years, there are a number of companies that stand out now. There is something different – something powerful, yet not fully appreciated – about their strategies and their cultures.

These companies analyze customer opportunities to determine where the highest returns lie, but they also have the processes, resources, metrics, incentives and technology to act on this insight. They are actively measuring the impact of their actions, learning from experience, and then, improving or optimizing their approaches. They are willing to *listen to the numbers* and act on them. These low-key powerhouses offer a glimpse of where business is headed – just as the A’s offer a window on the future of baseball.

## Actionable Intelligence

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Consider another organization that knows how to win even when everyone else is expecting defeat: Harrah’s Entertainment. The company became an underdog when it steadfastly refused to join the recent building boom that filled the Las Vegas skyline with imaginative, eye-catching and tremendously expensive new hotels and casinos.

How, wondered its critics, could homely Harrah’s compete against the captivating visual experiences promised by Treasure Island, Bellagio and New York, New York? The answer, it turns out, was through an intensive, analytical focus on customer relationships. Driven by this strategy, Harrah’s posted more than \$4 billion in revenue and \$235 million net income last year – rising more than 50 places on the *Fortune 500*.

In years past, Harrah’s has launched a set of loyalty programs – known as “Total Gold” and “Total Rewards” – enabling it to provide deeply personal service to customers and track their behavior in extremely sophisticated ways. In fact, it can track individual casino and hotel guests across all of its properties (26 casinos in 13 states). This enables the organization to actively monitor individual levels of play (and other activities), analyze preferences and interests, assess lifetime customer values, and provide personal offers or services based on what has been learned.

Through such efforts, Harrah’s learned its most profitable customers are not necessarily the high rollers to which all the other casinos attentively cater. They turned out to be “former teachers, doctors, bankers and machinists – middle aged and senior adults with discretionary time and income who enjoyed playing slot machines.” Instead of rewarding these clients with steak dinners and stage shows, Harrah’s found they typically were more inclined to appreciate a \$60 stack of chips so they could dive right into the games. Many

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also valued the luxury of being expedited through lines or receiving differentiated customer service, and took steps to achieve Platinum or Diamond status.

In an article last year in *Harvard Business Review*, Harrah's CEO Gary Loveman stated that the company has strengthened customer loyalty and profitability in two key ways: "First, we use database marketing and decision-science based analytical tools to widen the gap between us and casino operators who base their customer incentives more on intuition than evidence. Second, we deliver the great service that consumers demand. In short, we've come out on top in the casino wars by mining our customer data deeply, running market experiments and using the results to develop and implement finely tuned marketing and services strategies that keep our customers coming back."

Several other examples of analytically rigorous, knowledge-driven business success can be found in the financial services arena. Credit card issuer Capital One, which posted revenue of more than \$9.6 billion and net income of nearly \$900 million last year, conducts more than 80,000 tests a year in order to thoroughly focus and refine its marketing efforts. Indeed, it tests everything from marketing copy to price points to credit lines in order to ensure it is matching customer priorities and preferences.

"As a statistician, I love this because it gives us the rigor of testing appropriately and doing predictive modeling [to ensure success] going forward," said Dave Jeppesen, vice president of Capital One's Direct Marketing Center in a recent keynote speech at the National Center for Direct Marketing winter conference in Orlando. "We are going after the holy grail of direct marketing – to get the right product on the right terms to the right customer at the right time through the right channel. We believe we are pretty far along."

One recent Capital One campaign actively leveraged customer analysis and an advanced credit decision engine. This sophisticated, data-driven approach enabled the company to determine it was sensible to increase customer credit lines and offer an extremely low fixed rate (4.99%) on a new card. "We saw \$3 billion come onto our books because of one offer in one quarter," says Jeppesen. "It was because of the insight we found through our use of technology."

Still another financial services player that is setting itself apart from the competition is Toronto-based CIBC, which has more than 8 million personal banking and business customers. One of the central challenges the bank faced when it built a data warehouse eight years ago was determining how to manage customers across independent lines of business: credit cards; mortgages; commercial loans; checking; mutual funds; and certificates of deposit.

Taking a customer-focused perspective, CIBC collected data across business lines and employed analytical intelligence technology to better understand and predict customer behavior. The company learned to more effectively segment its customers by needs and preferences as well as profitability and potential. Capitalizing

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on its customer analysis, CIBC now is attaining tremendous predictability and accuracy in its marketing campaigns and customer management initiatives.

Daymond Ling, director of modeling and analytics at CIBC, points to intelligence-driven campaigns for pre-approved credit cards that are generating astounding acceptance rates of 20-30%. He also maintains that some personalized campaigns reaching out to new customers generate a 300% return on investment. "The benefits come from multiple sources including goodwill, which translates into strengthened relationships in the long term," he says. "In the short term, the customers see you as an institution that they're willing to trust with their financial transactions. They also purchase more products."

As a result of such successes, CIBC has become deeply committed to competing, marketing and managing customers in a very analytical way. "If a campaign is not supported by a predictive model of some sort, the business people immediately ask why," says Ling. "So we've got them trained. They have accepted the practice and they do not want to go back to the days when they didn't have models."

And while CIBC certainly has powerful analytic capabilities, it recognizes that customer insight is useless unless it is operationalized. With that in mind, the bank's customer marketing group actively works to support sales and service operations, and establish strong relationships with channel partners. "Our challenge lies in our ability to bring focused insight and stories about customer behavior to the table to enable customer-centric decision-making to happen," says Ling. "It's not about customer analysis, per se. It's about getting people used to [applying the analysis] and having them talking about customer considerations as a culture."

## The Rigorous and the Relentless

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As business success stories such as these suggest, winning isn't simply about having the highest IQ in the room. Despite their large departments of analysts, statisticians and data modelers (decorated with MBAs and PhDs from prestigious schools), many companies are failing to perform in today's hyper-competitive markets. While intelligence certainly matters, the real challenge lies in putting it to work.

"A truly analytical company is one that measures its actions and tries to understand the implications of its measurements," says Naras Eechambadi, founder and CEO of Charlotte-based Quaero, a customer strategy consulting firm. "It designs and drives its marketing programs based on actual facts and learning that emerge from past experience...Sophisticated analytics and models are not the key. It's about how well the learning is disseminated across the organization so decision-makers can apply it to new campaigns and front-line service people can make discretionary judgments about how they ought to treat individual customers."

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While such approaches may be difficult for many companies to internalize and execute, the economic downturn in recent years seems to have led to even greater hesitancy. Recognizing the necessity for significant change, many executives are deeply reluctant to take the challenging and unfamiliar steps

required to lead an organization in this fashion. Some companies even face the danger of slipping into a kind of *death spiral* – where customer information has not been applied or valued over the years and thus, is no longer even being collected out in the field.

“As the economy turns around and they want to engage in customer-focused activities again, they are really going to be hurting,” says Cynthia Stuckey, vice president of consulting for Milwaukee-based Hunter Business Group.

Of course, it can be painfully difficult to change the way people think or introduce a new order of things. It takes leadership. It takes evidence. And it takes time. Major League Baseball, for the moment, remains a prisoner to the discredited view that money and star power rule – even as baseball organizations such as Oakland, Toronto and Boston begin to challenge this hidebound orthodoxy.

So, too, Corporate America often seems a captive to its own rigid beliefs and irrational approaches to decision-making. One 2002 study by executive search firm Christian & Timbers found that fully 45% of corporate executives rely more on instincts than facts and figures in running their enterprises. And while instinct and intuition may be key attributes of leadership, they may not provide the best foundations for the increasingly complex decisions we are forced to make in an era of global, real-time commerce.

Over the years, executive intuitions often have found expression in vast – yet poorly measured and managed – corporate acquisitions, information technology projects, and mass-advertising campaigns. Indeed, the unwillingness to apply rigorous process discipline and measurement to such familiar growth strategies makes it hard to rationally consider the alternatives. Even as the evidence mounts, many executives never quite grasp that their real, definable and measurable opportunities might lie in building deeper, more powerful relationships with their customers.

Ultimately, one wonders whether Major League Baseball is merely a strange backwater of flawed management and misspent capital – or a vivid reflecting pool that shows us the extraordinary waste and irrationality associated with all business today.

What seems clear is that a number of smart and disciplined companies – in a handful of industries – already know the secret that allowed Billy Beane’s cash-starved team to win a place in the playoffs for the last four years. They are quietly transforming their own sectors and re-setting the pace. Eventually, these rigorous and relentless visionaries will have changed the game completely.

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## Inside Oakland's Success

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The contrarian and counter-intuitive insights behind the A's winning strategy can be traced back to one eccentric, yet exceptional Kansan named Bill James. Having studied literature and economics at the University of Kansas, it was as a night-watchman at a Stokley Van Camp pork and beans factory that he first began writing down his thoughts and analysis about baseball.

In his self-published *1977 Baseball Abstract: Featuring 18 Categories of Statistical Information that You Just Can't Find Anywhere Else*, James took his first stab at challenging the statistical assumptions underlying the game. The conventional stats not only misled decision-makers, as he saw it. They *lied*. As he continued to publish annually, he built a modest following as he challenged everything from fielding errors to "runs batted in" as meaningful measures of a player's value.

One of James' most important contributions would be his defense of "on base percentage" as a superior metric to batting average. By this thinking, a humble walk – which didn't change one's batting average at all – was nearly as important as a single because it got you to first base and three bags closer to a run. It also demonstrated what the A's front office would later celebrate in their players as "plate discipline."

As player salaries rose over the years (often to stratospheric heights), the potential value of such analysis also rose. Beyond the realm of official baseball, amateur enthusiasts of all kinds – think tank statisticians, government economists and even a research scientist at a large pharmaceutical company – were making intelligent contributions to an emerging field of advanced baseball analysis. Hoping to commercialize this knowledge, a new company – STATS, Inc. – was formed in the mid-1980s. Baseball insiders, however, showed little interest.

It wasn't until Billy Beane became general manager of the Oakland A's in 1997 that the ideas promoted by James and other outsiders got their first real tryout. Beane had read all twelve of James' *Abstracts* and they spoke to him. As a former player who had washed out and failed to meet the grand expectations of those who'd recruited him, Beane had an axe to grind. He knew first-hand that the value of a baseball player could not be accurately assessed through traditional approaches and metrics.

Beane was determined to challenge the status quo. His first – and perhaps most important – draft pick in this crusade was Paul Podesta. A Harvard graduate with a particular interest in the linkages between psychology and economics, Podesta was hired as Beane's assistant and, laptop in hand, began diligently employing and extending the knowledge developed by James and his cohorts.

He came up with new hypotheses, and ran his own tests and experiments. He carefully analyzed the statistics and saw things that others did not. Out of Podesta's computer would pop lists of potential recruits that had been overlooked by all the major league scouts (who tended to heavily judge players on their physical attributes).

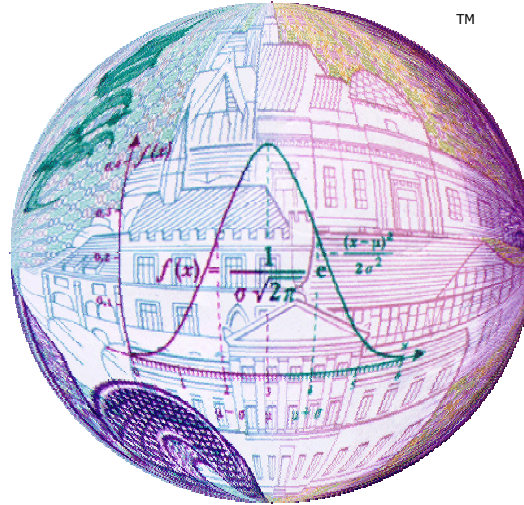
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Employing this approach, the A's would acquire talented, yet underappreciated, new players for a song. And – to the surprise of even the A's scouts – they would *perform*.

But this is not simply a story of technocrats crunching numbers on laptops – the triumph of the scientific method. The *art* of the A's success would lie in Billy Beane's leadership. It was his courage to defy tradition, and his ability to drive change in the A's organization – even as resistance mounted. With relentless force, he *acted* on Podesta's analysis to execute a pioneering, new strategy. There were no clear roadmaps for these accomplishments....and the road certainly had its pot holes.

Interestingly, Beane's management style is described in *Moneyball* as being largely visceral, intuitive and emotionally charged. (One memorable vignette recounts him violently throwing a chair at a wall – "...it didn't bang and clang; it exploded..." – to express displeasure with his lead scout.) "Reason, even science, was what Billy Beane was intent on bringing to baseball," writes Michael Lewis. "He used many unreasonable means – anger, passion, even physical intimidation – to do it."

Of course, it's not advisable for corporate executives to try to get ahead through physical intimidation. However, the A's success does seem to involve a complex interplay of passion and precision, intuition and analysis, leadership and execution. And while it's not clear the A's can continue differentiating themselves now that the story is out, tremendous opportunities for knowledge-driven, competitive differentiation still remain within grasp in today's business world. The question is: Who is ready to play ball?



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### About MIG

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