

The Two Important Principles of Direct Marketing

If you're going to make the most out of Direct Marketing you've got to know about these two important principles. They are:

1. **Knowing your customer**
2. **Knowing their Lifetime Value**

If you can understand what I mean by this then you've a great chance of keeping your marketing effective and profitable.

Let me start with knowing your customer.

There are two ways to know your customer. You can either meet all your customers personally and memorise all their details – or you can build yourself a database.

Let's assume it's the latter.

At this point we divide the strategy of Direct Marketing into two parts: **Acquisition** and **Retention** (sometimes also referred to as 'cold' and 'warm').

Acquisition

Acquisition is normally the hardest and the most expensive part of a Direct Marketing strategy. It means finding out who is likely to use our product or service and then trying to get them to respond to us.

Those who respond to us will form our new database. And that is pretty much the objective of Acquisition.

Retention

Retention is the second stage of a Direct Marketing strategy. This is where we use our database of customers to continue to make further DIRECT sales.

Retention is usually the easiest and most profitable part of Direct Marketing. This is because the people who have already used our product or service are the most likely to use them again.

Now here's the clever part (well, kind of). **Retention is SO PROFITABLE**

that, if we wanted to, we could make a LOSS on Acquisition.

This is the reason for the second important principle of Direct Marketing: Knowing the customer's Lifetime value.

Lifetime Value

The Lifetime Value is defined as the cumulative total of a customer's purchases over time. That value could be over three years, five years, or even twenty-five years.

Because the Lifetime value varies from customer to customer it makes sense to find and use an **average** Lifetime value. So when talking about Lifetime Values we tend to talk about groups of people rather than individual customers.

Calculations for Lifetime values can get a little complex. But for this tutorial the important thing is to understand the principle rather than the maths.

Banana Mobile Phones

Here's a simple example of how Acquisition, Retention and Lifetime Value all work together.

A mobile phone company called "Banana" is starting a new marketing campaign.

Banana carefully advertises to win 100 new customers. This advertising costs them £1000.

As part of the customers' deal, Banana gives away its phones for free. The phones cost £5 each. Total cost of phones to Banana is £500.

With the cost of the phones and the cost of the advertising, Banana has just spent £1,500 to recruit 100 new customers.

Now these 100 customers spend on average £100 a year on phone bills. That means that after one year Banana makes £1,000 in total income. £1,000 total income minus £1,500 costs means Banana has made a £500 loss.

Oh dear – not good for Banana. But hold on a second...



Banana are in this for the long-term. And they're confident they can do long-term profitable business with their new customers.

In the second year of Banana's trading – 50 of their 100 customers go elsewhere. They spotted a new deal by Orange (boom boom).

But the good news for Banana is that 50 customers decided to stay with them. Banana didn't spend any additional advertising to keep these customers and they haven't given them a new phone. So that's £0 marketing costs.



In the second year these 50 customers bring Banana another £100 each – so that's £500 total income in year 2.

Banana add this £500 profit on to their previous year's £500 loss, which now takes them to Break-Even.

Now in the THIRD year, 40 of Banana's 50 leftover customers continue to use their services. These 40 customers bring Banana another £400. Again, £0 marketing costs.

So over THREE years, altogether Banana has made a £400 profit!

What seemed to be a loss in the short-term has actually turned out to be long-term profit.

A simplified example? Absolutely. But the principle remains the same.

Selling on a regular basis to the same customers is a profitable way of doing long-term Direct Marketing business.

Admittedly, real life gets complicated. Tracking numerous costs, overheads and analysing numerous customer transactions isn't easy. But that's why we have spreadsheets and databases – the vital components of modern day Direct Marketing.

That in a banana-skin is the principle of knowing your customer and knowing their Lifetime Value.



As an aside, have you ever tried writing on a banana skin with a biro? It's surprisingly soothing. You should really try it some day.