Security Grounds the CEO Agenda

by Mark Gerencser and DeAnne Aguirre

While United States chief executive officers are confident about the ability of their companies to continue serving customers in the U.S. and abroad, the September 11 attacks and their aftermath will permanently change the way they operate.

The findings are part of a Booz Allen Hamilton survey of Fortune 1000 CEOs conducted during the last two months of 2001. Undertaken by RoperASW, the study also found that most CEOs have heightened security concerns.

Seventy-two CEOs from firms with more than $1 billion in annual revenues responded to the Booz Allen survey, which examined how the September terrorist attacks, the anthrax mailings, and the aftershocks of both events had affected CEOs' view of security in their own firms, their organizations' operations, and their companies' relationships with federal and local government authorities.

The survey suggests that CEOs are paying closest attention to internal operations. More than three-quarters of the executives questioned express increased concern for such day-to-day activities as mail processing, travel, and protection of employees. Eighty-six percent of CEOs express heightened apprehension about mail processing, and 85 percent have similar worries about travel. Risk assessment, employee morale, and protection of offices and infrastructure are also among CEOs' top concerns.

Prior to the attacks, corporate security was a midlevel concern for U.S. CEOs, averaging 6.0 on a 10-point scale, with 10 representing the greatest level of concern. Since September 11, this concern level has increased to 7.5. These results are consistent across industries, company size, and dependence on overseas sales. Those who don't plan increases in corporate security — including some energy and transportation companies — report that security already was a major concern (7.3) before the raids. The CEOs with heightened concern about security expect this concern to last at least one to two years; half of this group project that this heightened concern over security will continue for at least five years.

Another management priority is a proactive employee-safety measure that will also reduce costs: using videoconferencing to replace air travel. Interestingly, only a few chief executives (7 percent) appear concerned about lowering their own public profile.

Nearly half of the surveyed CEOs (49 percent) are reviewing alternatives to their existing supply chains in case of disruptions; 42 percent are reviewing their suppliers' abilities to ensure production is safe from sabotage. U.S. businesses lost hundreds of millions of dollars because of supply chain disruptions when U.S. borders and airports were closed following the attacks.

Despite the CEOs' increased

sensitivity to their companies' operational vulnerabilities, participants in this survey appear confident in their ability to maintain quality of service for their U.S. customers. Most of the respondents agree that corporate security is unlikely to make customers uneasy. Nearly three-quarters of CEOs (72 percent) believe that the quality of corporate security is no more important now for customers than it was prior to September 11, and that customers' willingness to purchase from their companies will not be affected. However, chief executives of non-financial firms are more concerned — more than a third believe that the quality of their corporate security is now a more important factor in customers' willingness to purchase their products and services.

Globalization strategies have been largely unaffected by events of the recent past, including the terrorist attacks and protests in Seattle and Genoa, according to these CEOs. Half of those questioned believe that any new barriers to previously open borders, both in the U.S. and abroad, will have either an insignificant impact or no impact on their companies. However, CEOs of the smaller Fortune 1000 firms believe that the aftereffects of September 11 will hinder their competitiveness. A third of the surveyed chief executive officers believe that any new barriers will have a moderate or very significant effect on their companies.

Three-quarters of CEOs (74 percent) believe that recent events will not change their companies' relationships with federal and state authorities. Of those who do believe these relationships will change, most expect changes to involve coordinating protection of physical locations within the U.S.

Any additional costs for new corporate security should be shared by government, shareholders, and customers, according to two-thirds of those CEOs who believe such additional security costs are possible. A third of the CEOs surveyed believe that new security costs will not be substantial. +

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A Bull Market in Market Research

by Ely Dahan

Focus groups, surveys, and other traditional market research tools have their place in predicting demand for consumer goods. But mock stock exchanges, which trade in ideas, may provide an even better way of doing so, especially when marketers need to analyze a large number of products and opportunities.

In such an exchange, the relative value of different product concepts or product attributes is determined by the buying and selling of shares on an open market. By watching how the value of product ideas fluctuates, companies can glean insights into what consumers like, don't like, and want.

Consider the Hollywood Stock Exchange (www.hsx.com). The 850,000 members of this Internet bourse buy and sell shares of "MovieStocks" with "Hollywood Dollars" (H$), with H$1 representing a million dollars of box-office receipts in the first four weeks of the movie's release. A month before the release of *The Lord of the Rings*, the movie's stock was priced at H$233.89 million. Four weeks after the movie's release, the actual box-office take was strikingly close, at $228.32 million.

Studios can watch a movie's stock price to see how the public is reacting to prerelease advertising and promotional campaigns. Combining this new market research technique with traditional methods, studios can also pay HSX for additional market intelligence. For instance, HSX segments its users by demographics and surveys them about their moviegoing behavior (e.g., which movies they see). The company can even compare and contrast the demographics of traders interested in different movies. Studios can use such information to adjust their promotional campaigns and distribution strategies.

The Iowa Electronic Markets (www.biz.uiowa.edu/iem/), run by the University of Iowa Tippie College of Business, is a similar mock stock exchange that focuses on election outcomes. Political campaigns regularly use election data from the market, which often is more accurate than preelection polls.

Another such idea exchange is the Foresight Exchange Prediction Market (www.ideosphere.com/fx/), which invites traders to do an IPO of an event stock, such as "Apple Computer dies by 2005." Subsequent trading focuses on the probability the event will actually happen.

Monitoring trading in ideas may seem a roundabout way of evaluating consumer opinion. But observing the outcome of a group's trading provides an indirect reading of its members' collective opinions — and the information gleaned from watching mock stock markets is potentially more revealing than the answers to direct questions posed in surveys and focus groups. These latter methods sometimes are flawed because not everyone in the sample is equally knowledgeable about, or interested in, the product in question (individuals might participate only for giveaways or money, particularly in the case of focus groups), but everyone's responses are given the same weight.

Information gleaned from mock stock markets is more revealing than answers to questions posed in focus groups.

Because marketplaces like HSX are fun, engaging, and filled with people who are interested in the products traded, stock prices reflect consensus opinion with remarkable accuracy. This is true even though there are always traders who buy and sell stocks for reasons unrelated to the underlying product, for example, arbitrageurs who buy undervalued stocks and momentum investors who flock to rising stocks and push prices higher. (Interestingly, such herd behavior mimics how some consumers choose which movies to see.)

Stock trading aligns the players' motivations with telling the truth; traders try to maximize the financial value of their stock portfolios and, in the process, reveal their real opinions. By contrast, surveys and focus groups can discourage honest responses. It is not unusual for people to want to please the interviewer or conform to others' opinions.

With a little imagination — and software — a company might create a market in ideas to weigh decisions as diverse as selecting the preferred ingredients for a chicken soup or picking an advertising campaign pitchperson for an automobile launch. Stock prices can stabilize quickly — perhaps within 15 minutes. Comparing valuations then gives a sense of the optimal composition for the soup, or which actor would be the best spokesperson. Stock trading games can be conducted in various settings — at a central interviewing facility, during an industry conference, over the Internet, etc.

The greatest value of mock stock exchanges may be that they enable analysis of hundreds of ideas, which can be whittled down rapidly to a few candidates. Traditional market research is not nearly as efficient because it's virtually impossible to design a single useful survey that incorporates so many product concepts or attributes.

Who knows? As the technique is refined, it may save us from another *Pearl Harbor*. The movie, that is. +

Information Is the Fuel for Automotive CRM

by Steven Wheeler

Mass marketing is clearly at a crossroads, as companies recoil from the inefficiencies they perceive in conventional media spending. Merrill Lynch & Company is predicting a 4 percent decline in U.S. television advertising spending this year, following a similar fall last year. Seeking greater accountability and returns, many firms are investing in customer relationship management (CRM) systems. Analysts predict that global spending on CRM systems will total between $20 billion and $45 billion in 2002.

But marketing executives are beginning to discover that CRM system implementation — in which simple database consolidation can run from $20 million to $30 million — is not an easy fix to the problem of communicating to, wooing, and retaining customers.

In the auto industry, the reason for CRM systems' ineffectiveness should be obvious. On average, interaction between an auto company and a customer occurs 1.2 times per year. That simply does not provide enough data to answer such crucial questions as, Which people should get what offer on which product at what time?

To gain the information necessary to embrace the customer, relationship programs must be based on two principles:

• First, they cannot wait until the first purchase is consummated to begin to understand consumer interests, concerns, desires, and habits. The key to unlocking value is to recognize that different customers follow different purchase paths. Effective CRM systems must dive deep into the purchase decision before the purchase is made. Call this purchase-cycle intimacy.

• Second, because different customers follow different ownership paths, effective CRM systems must link deeply and broadly to the individual's ownership experience — the consumer's relationship with the car throughout the ownership cycle.

Acting on these two principles requires companies to bring otherwise separate technology programs together in complementary ways. For example, Internet-enabled communication systems make it increasingly possible to capture valuable insights about consumers in the middle of the purchase process. Interactive kiosks in dealerships — or in alternative sales venues, such as malls — are proving to be excellent tools to begin to engage consumers in dialogue.

Online activity at home or in the office represents another vital opportunity to achieve purchase-cycle intimacy. The bursting of the e-commerce bubble should not obscure the fact that some 70 percent of consumers in the U.S. use the Internet at some point during the automotive purchase process.

Now consider what happens to a company's ability to achieve and use purchase-cycle intimacy when these tailored consumer engagements move from the Internet into home entertainment centers. With personal video recorders (PVRs) like TiVo being built into set-top boxes — Forrester Research Inc. predicts more than half of U.S. households will have interactive TV capability by 2005 — assisted sales processes will occur in the lean-back comfort of the family-room sofa. Even with privacy protections in place, the data flowing back to manufacturers and dealers will enable them to tailor follow-up campaigns that effectively bridge the gap between marketing and sales. The ability to develop incentive packages tailored to the way different sets of customers go through the purchase cycle and to get customized packages in front of receptive audiences is vastly preferable to slapping a $2,000 incentive on a vehicle and offering that same package to everybody.

The challenge for dealers and manufacturers is to partner so that customer data can flow seamlessly along the chain.

Advanced automotive marketers are already experimenting with cross-platform marketing, using PVRs as the central control device. Toyota helped launch the Lexus ES-300 earlier this year with a TiVo cross-promotion sweepstakes that uploaded commercials into the box; invited sampling of other commercials programmed into NBC network shows; and asked viewers to register for the contest on the Web. Imagine the opportunities when these platforms — television, PVRs, and the Web, and entertainment, brand advertising, and interactive direct marketing — converge on a single screen.

Postpurchase, another interactive technology — vehicle-based telematics — can help automotive marketers comprehend the intricacies of the ownership experience. Telematics are the growing number of wireless devices that seamlessly capture and communicate vehicle data, enabling the automotive marketer to understand the driver's usage requirements, influence downstream services, and facilitate remarketing. Telematics, whose use is increasing, allow vehicle relationship management to buttress customer relationship management.

Already, the OnStar system and "black box" programs innovated by companies like GM and Peugeot are returning vehicle and customer data to companies, which enable them, in turn, to shape concierge services and maintenance programs for individual customers. A Booz Allen Hamilton analysis projects telematics revenues of $20 billion to $40 billion within the next 10 years.

Adapting to telematics will not be easy for automakers. There is the ongoing difficulty of shifting from marketing that is built on the concept of mass advertising to marketing that is premised on intimate customer understanding. Auto companies also need to overcome their historical "slow follower" habits relative to technology. And the strategic plays around telematics can be complex, requiring both defensive postures, to protect existing business territory, and offensive maneuvering, to create value beyond the existing business.

The greatest challenge for the manufacturers and the dealers is to partner around this intimate customer information, so that the data can flow seamlessly up and down the chain. Only through such partnerships will the average salesperson be able to craft plans relevant to consumers walking into the dealership, offering each potential buyer excitement — excitement shaped by the right value proposition. ✚

Who Profits from Brainpower?

by Russell W. Coff

Knowledge assets are essential for competitive advantage today, but they don't guarantee shareholders above-average returns. Why? Because even though firms may be producing more value than ever from brainpower, not all of that value goes to shareholders. Rather, some portion goes into employees' pockets — in the form of higher salaries, bonuses, stock options, incentive plans, and discretionary spending. And employees deserve it.

After all, ownership of stock doesn't mean ownership of all of the company's assets. Such intangibles as know-how and star power belong to, and are controlled by, individual employees. For example, when the six stars of the successful sitcom *Friends* recently made joint salary demands, they got what they wanted. AOL Time Warner Inc. (which owns Warner Bros. Television, the show's producer) and General Electric Company (which owns NBC, the show's network) may earn higher revenues from advertisers and ancillary products associated with the popular show, but profits don't necessarily rise, because most of the additional revenues go to paying the television show's stars.

Similar situations occur in other kinds of businesses with individuals who own other kinds of intangible assets — scientific knowledge, production experience, customer relationships, etc. To be clear, these business "stars" aren't stealing from the firm; they're simply exercising their right to a fair portion of the unique value that they generate.

Star employees who are not given their due may be attracted by other opportunities. For example, when Amazon.com Inc. was ramping up its crucial distribution strategy in 1997, Richard Dalzell, then the highly celebrated chief information officer of Wal-Mart Stores Inc., joined Amazon, which offered stock options worth millions of dollars and a salary Wal-Mart could not match. (In 1999, Wal-Mart, renowned for its distribution system, sued Amazon for poaching its talented supply chain master to steal trade secrets, but they later settled the suit.)

The point is, when such intangible assets as an individual's intellectual capital produce increased revenues, these valuable employees compete with shareholders for those additional dollars. Investors may still earn average returns. But they shouldn't necessarily expect knowledge-based assets to produce spectacular returns because key employees need to be retained, and that is costly to the bottom line.

But how does management determine how much compensation represents the knowledge workers' fair share of the value-added? And how can companies gain more control over their knowledge assets?

Never forget that when individuals have highly valued knowledge, it gives them bargaining power. Still, firms can transfer ownership of some knowledge from individuals to the firm. Patents, for instance, give ownership of ideas to the firm. IBM files for thousands of patents every year and earns impressive revenues from them. In this way, companies stake a claim to knowledge assets, from which the firms can earn income for shareholders.

Similarly, enterprise software that encodes business processes or records customer information captures the practices and knowledge held by individual employees for the shareholders' benefit, even if key "knowledgeholders," like Wal-Mart's Mr. Dalzell, leave.

Nevertheless, much of the value of knowledge assets remains inaccessible to investors. Patents reflect advances that are established and fully codified. But patents come from much broader tacit knowledge, which is the engine of breakthroughs, the foundation of the firm's future value, and the most difficult value to realize because it must be extracted from the brains of employees. IBM's existing patents bring in revenues, but its future patents depend on the ongoing research and genius of its scientists and engineers. Shareholders cannot expect to capture the full value of future breakthroughs through patents.

A healthy firm with a knowledge-based advantage must compensate all stakeholders, but especially the employees whose intellectual capital creates and sustains that advantage. Shareholders will realize a fair rate of return, but key employees may keep the lion's share. +

Shareholders don't own all of the company's assets. Intangibles like know-how and star power belong to employees.