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NON-TRADITIONAL MARKETING THROUGH BROADCAST MEDIA

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- o Products: life, health
- o Media selection
- o Expenses
- o Analysis of efforts

MR. JOHN D. LADLEY: I'm a consulting actuary with Huggins in Philadelphia. I've done considerable product and other work in direct response marketing, including broadcast media marketing. Following my opening comments, Gary Kauffman, who is president of Direct Marketing Advisory Service, in Rye, New York, will discuss the basic principles involved in selling insurance through television. Gary's company is a direct response specialty firm for insurance and financial services, dealing with the evaluation, planning and execution of marketing efforts.

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review and analyze video tapes and will examine in some detail the construction of a commercial making a sale of insurance. He'll touch on, in addition to television, the marketing of insurance through radio and cable and present some other broadcast media ideas. Both Gary and Gene, incidentally, held senior positions at National Liberty in the Philadelphia area.

In the discussion of a new non-traditional topic, it will be helpful to describe and define some of the issues and some of the terminology that will be used. That's because in evaluating direct response sales of insurance, we deal with a very much different approach then we do when we move from, say, just analyzing brokerage products into analyzing general agency products.

The direct response business is not a very simple business, although many people will attempt to reduce it to a discussion of response rates. It has been, and is becoming more so, a very sophisticated and a very scientific business. This is doubly true because it provides the insurer or other distributor control over methods, products, costs and compensation levels and ultimately over the end customers. Therefore, with a few exceptions, it is a company-oriented business in planning, analysis and evaluation.

There is, of course, greater risk associated with the element of enhanced corporate control; that is, when we spend the marketing dollar, unlike a commissioned product, there's no guarantee of receiving a revenue dollar. Thus, much of what we will discuss will describe the planning and management of that particular risk. You may have questions, for example, on whether the apparent risk aversion on the part of companies implied by the very simple products we see in direct response is in fact a reality. You may have questions on the appropriate rates of return given these risk levels.

We will illustrate a prototype direct response sale analysis using the same sale data. The analysis concentrates on the marketing cost side of the sale of insurance through direct response, as opposed to looking at the profitability side or the return side from the product.

This type of analysis is useful, and it's usually mandatory in a lot of ways in looking at a direct response sale in order to get some of the definitions of response rates, conversion rates and the various associated costs. Primarily, the process is directed towards the logical breakdown of the cost of acquiring business. This analysis will be for the roll-out sale of universal life on television. First of all we need to identify those costs that are associated with generating an initial response to an offer. These are frequently done on a unit cost basis; that would be appropriate for, perhaps, a mail offer, where you had a high degree of certainty as to how many pieces you were sending out, and what your universe of solicitations actually was. On television and other broadcast media, that probably won't be the case. In this case, we consider gross cost levels. It is primarily a television offer, so you will not see much data processing or postage or mail processing costs in what's known as the first step. We have a response rate target that should be "10,000;" 10,000 responses coming out of our commercial. A campaign like this undoubtedly would have been tested before it would have been rolled out; we would not take a full, say, $260,000 risk that there would be virtually no returns on our solicitation without testing. Then we can take our cost converted from the initial response target, and we have a cost per response generated; in this case, it's $26 -- this seems relatively inexpensive at this point.

The second step in our analysis is fulfillment, also known as conversion and by a variety of other names. In this case, we're sending out a first-class envelope. To follow up, this will be a pretty high quality "kit" or package, and we're going to attempt to "convert" or have those individuals send in some money for a first premium payment and, essentially, take a policy. A 20% conversion rate would be relatively high, but conversion rates can vary considerably. For television that might be somewhat high. We could see, then, the cost per conversion is $52, roughly twice the cost of generating a response.

Issue-related expense is our third step. We have issue and underwriting, and rejection and not-taken rates factored in here. The way this works is, when we had 10,000 responses to start, we wound up with 1,600 premium paying policies at the end, after they move through conversion, not-taken, and the underwriting process. We can also put in a developmental cost allocation, or an overhead cost allocation, to each policy that becomes a premium-paying policy, ultimately. So, you see, we have three separate steps: We have to be careful not to talk about response rates without relating that to conversion rates, without relating it to not-taken and underwriting, rejection rates, or rating, and we have to relate all those to the costs generated in those individual steps.

Thus, all these costs are response related costs when translated into converted policies that are successfully issued and taken. We can see the $26 first step response cost actually translates to $161, approximately, of cost per paid new issue. Fulfillment related expenses (where we actually converted the responses into a premium-paying policy), and the issue and underwriting related expenses are also translated. Our total cost per paid new issue in this case happened to be $436.81, a fairly substantial cost in direct response terms.

We can compare some data that are usually external to this analysis and could be known as allowable acquisition costs or a frequently used terminology would be T/MC "total annualized premium -- to a marketing cost" comparison. But however you define that, what you're trying to do is compare your marketing cost with your allowable. acquisition cost or, essentially, the present value of all the profits you expect on the business that you've sold. You would normally obtain that profitability information at some desired discount rate. You'd consider before and after tax and many other factors.

Let's say if we hit all our response rate and conversion targets and it's going to cost $436.81. Assume the preset value of profits, without acquisition costs on the universal life product that we're selling, is $390. We can see that we really can't afford to sell the policy for that much; we have a shortfall of $46.81 per policy. However, there are certain other factors that insurance carriers and other financial service companies will look at, and those might be the sales of future products, to actual customers, or to the unconverted customers who have not turned into an actual paid issue. I should point out this is especially significant when we deal with broadcast media, because usually the tendency is to get a relatively high response rate and a relatively lower conversion rate, so that some additional value is frequently in mind.

You'll see variations of what I have outlined, but my discussion of the various steps involved in the process and the associated costs should provide a framework for the discussions about to follow.

NON-TRADITIONAL MARKETING THROUGH BROADCAST MEDIA

MR. GARY A. KAUFFMAN: While broadcast is defined as radio, TV, cable, and other areas, I'm going to concentrate on television, a very complex and involved medium. What I will try to do is share with you some observations relative to the dynamics and psychology of direct response television, review some of the key cost factors that would be used in the decision making process, and then review with you a financial model that would be used from a marketing acquisition standpoint to evaluate both the test and the roll-out.

When we look at what we would consider successful direct response commercials, we find that they all have one thing in common -- and that is that they are effective in creating momentum. And the way we create momentum is through a constant flow of very graphic words and images that present information in such a way that it will transform a passive television viewer into an active telephone dialing consumer. One of the most graphic illustrations of momentum is the telethon. Anyone who has ever watched the Jerry Lewis telethon over its 21-hour span period will realize that the intensity of donations per hour increases as the telethon grows older. And that's because Jerry Lewis, in his emotional appeals, his tears, the filmstrips, the young children, the research centers, is creating that momentum. You also see momentum in revival sessions, and we see it at church on Sunday: You have to believe it's more than coincidence that the collection plate is passed at the point of greatest momentum, at the end of the sermon. That's probably why most direct response commercials are at least 2 minutes in length, because no one has really found a consistent formula to create momentum in less time. Some have found an effective way to do it in 60 seconds, but not in a consistent manner, and no one has done it in 30 seconds. And, in fact, there may be a trend to go in the opposite direction. I'm sure we've all seen half-hour ads for "How to Make a Million Dollars Investing in Real Estate." And now, with the advent of home shopping on cable, we are exposed within those 1- and 2-hour programs to a group of 5- and 10-minute commercials.

Over the years, what has changed dramatically is the quality of the commercials. But what hasn't changed is the momentum. To be successful, you have to have momentum; it's just packaged differently to reflect today's lifestyles.
The other thing is that the players in the direct response commercials have changed. We used to think that the people who would advertise had pots and

pans, knives, records, companies we never heard of; many people thought they were fly-by-night companies. Today, we have *Time-Life* books, *Sports Illustrated*, Dreyfus Mutual Funds, MCI Communications, and organizations like the Franklin Mint selling $1,500 grandfather clocks; all of these are on TV.

In looking at the construction of direct marketing insurance commercials, and direct response TV commercials in general, there are a lot of similarities in the way we construct those commercials when we compare them with the construction of a direct mail marketing campaign. Those similarities go far beyond the obvious one -- that both are trying to create an immediate response. When we develop a direct mail packet, the letter is a very personal item; we try to make it as close to a one-on-one, face-to-face presentation as possible. We're able to do that in today's information and technology age because we know who you are, your age, your birth date, your income -- we may know things about you that you wish we didn't. And we use all of that in our direct mail letters.

Well, in broadcast, we can't talk to you by name, but the more we study our product, and the more we understand the consumer, the more we know our market -- by age, by income, and in fact, we can even use that information in developing our media plan, because we should know what programs those people watch and when they watch television. And when you watch a direct response TV commercial, it's very, very similar to the direct mail kit. For those of you who might be in the direct mail marketing business, when you develop that kit, you spend inordinate amounts of time on the outside envelope. And the reason you do that is no matter how good the offer is, no matter how good the product you're selling, and no matter how effective the creative execution inside the package, if the prospect doesn't open the envelope, he's never going to find out how good the offer is. It is the same thing on TV: The first 5 to 10 seconds must create that attention -- that's the outside envelope. Because if you don't create the attention, then, you lose them to the refrigerator, to the bathroom, and within the last few years, to these great remote control devices that allow you to zap commercials.

The next thing is the letter. But in a TV commercial, the letter is the spokesperson, whether it's a personality or a pitchman, when he's looking you right in the eye, as if he knows you, and he's using that demographic information to relate that product to your needs. And while we don't have a brochure in TV -- the brochure would illustrate the many ways that that product could serve you -- the brochure on TV is the graphics behind the spokesperson. And then in the direct mail kit you have your order card. Well, the last 20 seconds of a direct response TV commercial are your order card. The only difference is, instead of mailing it in, you phone it in.

Now, why television? You know, there are more and more companies that are getting into the direct marketing of insurance these days. But almost every company that is getting into the business seems to concentrate its efforts in direct mail. And while there's a great increase in the use of telemarketing, for the most part the efforts are in conjunction with and in support of the direct mail efforts. For some reason, television and broadcast direct response marketing remains the domain of a few. And I think part of the reason is that there are some myths that have been created that really aren't true. There is a perception that television is very expensive to test. There's a perception that television is very expensive and creates great downside upon roll-out. Well, that's true in almost any new venture you try. It may be the perception is greater in TV because there are so few companies that have been involved in the medium and so little expertise is out there. But in reality, television is just as predictable as direct mail, or as unpredictable. When you are marketing on television, although your cost per lead may be a variable, if you are rolling out and doing your program in markets that are similar to what you tested, your conversion rates, your average premiums, your persistency are just as predictable as they were before.

Another reason why you should be on TV is that you have more control on roll-out than in direct mail. When you are rolling out a direct mail kit, and you have tested lists and you decide you are going to mail 10 lists that are 300,000 names each, you are spending approximately $100,000-$120,000 on each of those lists. That would be $1,200,000 in your roll-out campaign. And while you're basing the roll-out on test results, we all know that lists don't always act the same way, and that the quality of names as we get into our list are not always the same as the test names. The problem is that, once you've spent that $1,200,000 and you've put the mail in the post office, there's nothing you can do if the results aren't coming in the way you want -- that money is sunk, and you can't react to it until you have your total response in. Television is a very dynamic media. We can look at each TV station as a list. If you're out there with a 13-week television program and its costing you $1,000 a day for 2 spots, 7 days a week, we're talking about $91,000 per station. This is similar in cost to the lists that we talked about, but there's one major difference: with television you can cancel your time with 72 hours' notice. That means that, as you roll out you can monitor your results and that your exposure (if you're talking about $1,000 a day on average per station) is from the time you identify the station as not performing as it did in tests plus 72 hours. You can cancel, and you'll spend only $3,000 more (72 hours = 3 days). You don't have the same sunk costs as direct mail. And because television is dynamic, it allows you to continue to retest while you're in roll-out. If you're canceling these stations that don't perform, you can add new stations that you would like to test. And if they don't perform, you can cancel them; if they do perform, you can expand. The problem is, most people don't understand how to control television; they don't understand how to read the results; and they're not willing to spend the time to read those results day in and day out, the first thing every morning. But if you do, TV will be more controllable and more flexible than direct mail.

The next thing is to develop a large base of policyholders and names. When you're marketing through direct mail, you're out there looking for a sale. If you mail 1,000,000 names and you generate 2,000 applications, the other 998,000 names can't be used again. But when you're marketing on television, you're looking for a lead, and if you go out and get 500,000 leads, even though you may convert only 7,000 or 8,000 of those in the initial sale, you have 500,000 people who raised their hand and said, "My name is Gary Kauffman. I am 42 years old. I was born July 16, 1944. Here is where I live. I may have even told you I have a MasterCard. Maybe I've given you information about my spouse. And more important than all, I have raised my hand and told you that I'm interested in insurance --- maybe not the product you're selling me today -- but I'm interested in insurance. You have just developed a major asset that you can cross sell other programs to; to the tune of an additional 10 or 12% penetration. That is a very significant feature, because we also say that television may allow you to spend more to acquire a sale than in direct mail, and that's the reason. Because in direct mail, you do not have any ancillary benefit; you have sunk the cost and can't use the names. If you have an effective policyowner marketing program, if you have an effective cross-sell program to those leads that didn't convert, you can justify spending more than the normal acquisition allowance because you know those cross-sell programs will prove more efficient than programs that are mailed to fresh names who have not qualified themselves as prospects. That's one of the keys to direct response TV marketing.

List Rental Income is something most companies will resist. But if you're out there in direct mail and develop 500,000 or a million names through TV you're going to hear names from someone else -- someone in an unaffiliated business is renting you names that have responded to their offer. Now, if you generate a million names and you can clear $40 per a thousand names from renting them to someone else, that's $40,000 per rental, and it would not be unlikely that you could rent those names at least 10 to 12 times during a 12-month period. That's a half a million dollars that can go to increasing your allowable acquisition cost to generate more leads the next time out to sell more programs. Now, people will say, "Why would I want to rent out the names that I've generated?" Well, you may not want to rent them out for a competing offer for life and health insurance, but the fact is, the person who's selling auto, homeowner's, or another financial service is going to rent those names and he is going to rent them from someone else. You're mailbox is just filled with mail today; your name is being rented from a variety of sources. There is no reason why you shouldn't be out there taking advantage of that list rental income yourself.

When you're testing direct response television, while it's true that something that works in mail will not necessarily always work in broadcast and the other way around, if you have a very successful product in mail, you certainly would be well advised to test that as your initial vehicle; it doesn't make sense to go out and test something that hasn't proven itself anywhere. You should go out and test products that work, with the same offer, the same proposition, the same positioning that worked for you in direct mail. And don't expand too rapidly. When we test direct mail lists, if we test 15,000 names from a list in which there might be a million in the universe, and the list performs well, we don't mail a million names next time. We might mail 50,000; if the list did really well, we might mail 150,000 or 200,000. You have to use the same caution and discretion in TV; you must expand at a proven rate. And when you do expand, expand in similar markets with similar characteristics. It's amazing how many people will test initially in the same markets that their mail works. If Scranton, Pennsylvania, and Bakersfield, California, are good direct mail marketing response areas, certainly you would want to test TV in those markets.

The mistake people make is the fact that because TV worked in Bakersfield, California, and Scranton, Pennsylvania, they then expand to Los Angeles and Philadelphia. The facts are that Nashville, Tennessee, is closer to Bakersfield, California, in response characteristics than Los Angeles; and Buffalo, New York, is much more similar to Scranton, Pennsylvania, than Philadelphia. Large, similar markets are better then small, similar markets; it's simply a matter of economy of scale. A TV station, like any other business, has fixed costs; and the larger the viewing audience, the cheaper it should be for you to reach a dealer.

The cheapest television time is two-minute time; it's called run-of-schedule. The reason it's cheap is that it's a combination of time that the station is not able to sell to people who want 30- and 60-second spots. If you and I have a merchandise store with a radio we can't sell, we can reduce it and sell it tomorrow, or reduce it further next week until it's sold. But once 8:30 this morning has passed, a TV station cannot reduce the cost of that time. Run-of-schedule time, therefore, is a combination of 30- and 60-second spots that can't be sold; and oftentimes they're sold at a rate cheaper than what a 30-second spot might cost. As a result, if demand increases or if somebody comes in at the last minute and wishes to buy a 30- or 60-second spot, you will be preempted. It is most common to expect to be preempted 25% of the time and if demand increases. At certain times of the year, when demand is very strong, 40% to 60% preemptions are not uncommon.

When you're buying two-minute time and when you're buying run-of-schedule, what the station is saying to you is, "Because you're getting it so cheap, we have the right to run this commercial anytime we wish." In order to control what you're doing, you have to try and control when those commercials are run. Now you can ask for a commercial to be run at a specific time and in a specific show, but oftentimes, unless you're willing to pay a premium, it's unlikely that request would be honored. But you do have a realistic chance of telling a station where you're ordering 14 spots a week to run three spots from 9 to 12 in the morning; three from 3 to 5 in the afternoon; and eight of them 8 to 10 at night. Again, the station doesn't have to honor it, but if you are not producing the cost per leads that are acceptable, or the quality of leads that are acceptable, you can go to the station, tell them your problem, and if they're not willing to change, you can just take your commercial off. If it's a sellers' market, you'll end up taking your commercial off.

In regard to the consumer goods advertising, the big ad agencies tell people that they have to get the maximum gross rating points. The general advertiser is out there trying to create an image for some future action; therefore, he wants maximum penetration, maximum audience, maximum visibility. We are trying to create a response right now; we're not trying to to create a future situation. Therefore, we are not interested in gross rating points -- we are interested in advertising on those stations that will have the greatest audience that's likely to buy. And that also means that we may not want the most popular shows. Certainly, on Friday night people are not likely to get out of their chair in the middle of a Dallas show to call an 800 number. They might do so, on a Perry Mason rerun. So, we like to call it "the boredom factor." Once you've defined your audience, and the shows it is watching, the more boring the show, the better prospect it is for your direct response commercial.

Rates are much, much lower in the first quarter and third quarter than the rest of the year. And that's obvious because in the fourth quarter you have all the retailers on seeking time for the Christmas season. And in the second quarter, we have Easter, Mother's Day and Father's Day. The difference in rates is so dramatic that generally direct response advertisers find it not feasible to promote their products in that time. And that is why you will see a concentration of direct response ads coming on the air the day after Christmas and lasting until the beginning of March. And then you will see the ads come on again in the summertime through sometime in September.

We talked before about how dynamic TV is. You must be able to track your commercial by hour and by day. It's very, very important, because that's where you lose control and that's where you throw a lot of money down the drain. Obviously, if you're on 100 stations and you're not tracking it, the advantage you have of being able to cancel in 72 hours is what creates a potential dramatic downside.

Let's talk about some of the marketing test-cost categories that are involved in putting together your test plan and roll-out. First thing is the cost of the personality -- if you use a personality. Companies get enamored with personalities. A company that's never been in the business thinks it's great to have this famous person represent it. Personalities can work, but sometimes they don't. You have to make sure that the person and what he represents to the public fits the product and the image you're trying to create. And more importantly, when we get into cost, you have to make sure that the cost of the personality fits your structure.

A test of the direct response commercial may cost a quarter of a million dollars. It doesn't pay to skimp a few thousand dollars in developing a commercial. Go to someone who has an experienced track record of success in creating direct response TV commercials.

Commercials can cost anywhere from $5,000 or $10,000 to the "sky is the limit." If you allow the creative talents to get carried away, you could spend more money than you would ever spend in a roll-out in producing just the commercial. You have to temper what it is you want to achieve and what you see your upside potential as being.

Media is the biggest cost in your plan. It'll become the factor we look at in the financial model that we use later. But media, generally, will range from 50-70% of the total cost that you expend. It's your leverage point, it's your control point, it's where you can maximize the profitability of a plan, or if necessary, minimize the losses.

We can illustrate what it would cost to go out to test the 15,000 leads on a hospital indemnity product. Now, all these costs aren't exact; they're a composite of different types of programs. The media cost represents 60% of the total. But we've also isolated incremental test costs because, when you go out with this test, the costs of writing and producing the commercial, say $58,000, when you roll out, will not be a recurring cost, or doesn't have to be. And therefore, if the test is successful, we'll want to take that $58,000 and amortize it over the roll-out. Depending on what our roll-out is, if it's 100,000 leads or 200,000 leads, it creates that unit cost. So we're using a roll-out sample of 100,000 leads. And when we put all these costs together, it should cost us about $11.83, the way we have constructed the test. Again, note that $7 of media cost (60% of 11.83), and that's strictly the cost of buying TV time, will become a leverage point.

We can also illustrate a financial model of results of the test that will allow you to have flexibility. Penetration levels are how many people sent in an application without money. We have a conversion factor that assumes that 50% of those people ultimately sent in the first premium. With an average premium of $270, you can find the total annualized premium under different scenarios. We've assumed 70% of that annualized premium will be collected over the first 12 months of the program and that the acquisitional allowance that has been placed into the plan is that you can spend 125% of first-year expected collected premium -- 125% of that 70% collection factor. If we take that number and divide it by the 100,000 leads, that shows you what your allowable cost per lead would be at those different penetration levels. Now remember, if we roll out in similar markets, the conversion factors, and the average premium numbers, will not vary much; what will vary as we expand will be the up-front penetration.

Now someone may say that if we only achieve a response rate of 10% and we could only spend $10.04 per lead, that the program was a failure. But that's what it costs us over *all* the leads that were in the program. Remember, we were spending $7 for a media lead. Before, we said that we could spend $11.83. Because our leverage factor is the media, it may mean we have a smaller program, but if we increase or decrease the media costs by that $1.80 ($11.83-10.04), we can go out and generate all the leads that we are able to generate from those stations that came in at $5.20 a lead. The converse is, if we end up getting higher penetration, we have a couple of choices. We may not have any more money to spend and we've just maximized profitability of the program. Or if we find that we could spend $13 a lead, we can go out and increase the number of leads by spending $8 and some cents for the media. Now, clearly, there are other ways to maximize the response; we would always do creative testing and find ways to get that 50% factor up, or to increase the average premium. But the media cost is where your leverage point is. And as the program matures and you practice segmentation, the media becomes even more important, because after your first year or two in the business, you'll find that a $5 lead in one market is not the same as a $5 lead somewhere else. You will be able to identify certain markets where your conversion rate was 65% and not 50% and markets where your average premium was $320, not $270, and then you can start developing models that alter your cost per lead by market. You may find markets, as you go on, where persistency falls off or where claims are high.

It's important to ultimately develop your data base so that the media cost relates not just to the up-front response (that's all you have in the beginning) but relates to those other factors. It's also important because when you're dealing with people who are buying your media, you can think you're being a tough guy and tell the media buyer that you're not going to spend more than $5.50 a lead. If you're too tough, the media buyer knows that, if you want a million leads at $5.50, he can get them for you; they may only convert to 30%, but just like in direct mail, where there are lists that respond much better than others but have very little response rates, the same is true in TV. So, such a model is valid, but we have to temper it; we're using the data that we gather in our data base over a period of time.

The last thing that I want to highlight are the factors that create success. We oftentimes become enamored over the development of the mail packages and the creative effort. One of the things that I do want to mention is that, when people develop your fulfillment materials, it's very important that, even though they're probably not the same people who develop the commercial, they work hand-in-hand. You're spending a lot of money to create a commercial that creates a momentum and causes a person to call on the telephone. You'd make a major mistake if the materials that you send out in the back end don't create the same momentum, use the same positioning, use the same emotional appeal that was in the TV commercial. You'd be amazed at how many people use different sources and different appeals on the front end and the back end.

Now, this model is assuming that we're using a product that has already worked for us in direct mail. And in that scenario, the creative efforts, while they're important, really maximize our opportunity or minimize our loss. In direct response marketing, whether it's direct mail or whether it's TV, media is the market. If the media is good, refined, and successful, it can overcome less than superb creative efforts. The best creative effort in a mail kit and the best creative effort on TV cannot help you overcome poor media selection.

MR. EUGENE R. RAITT: As a direct marketer, one of the problems that you often have is that you never get to see the results on a one-to-one basis of anything that you've done. This means that you're never there when someone goes to their mailbox and takes out their mail and just rifles through it and finds your piece and either opens it or tosses it aside. And you're very rarely in a room somewhere, if you've done something on TV, where you can get to see someone's reaction. Chris Stag, who's a very well known direct response copywriter, tells a story. Several years ago, he wrote a package for the *Wall Street Journal*, soliciting subscriptions. And one day he was on the bus in New York City, and he sat down next to a guy who got on at the same stop. This guy opened up his briefcase and he took out the package that Chris Stag had produced. Chris said he was just thrilled to death. He sensed an air of excitement in himself, and he watched the guy as he opened up the envelope, took out the letter, read it, went through the brochure, and fingered the order form. Then the guy eventually put everything back, and he stared very, very thoughtfully, at least Chris thought thoughtfully, ahead for awhile. He went back to the letter and he took out a pen and he started circling some things that Chris thought might have been key point on the letter, and then he looked up again and he thought for awhile, and Chris was really excited about this whole thing. And then all of a sudden the guy reached down and he just ripped the thing in three pieces and put it back in his briefcase, totally deflating Chris' ego.

Well, I had a similar experience. Years ago, when I worked for National Liberty, I was directing a project that included Roger Staubach as one of our personality endorsers on TV in the Veterans' market. My father, who for a long time had continually asked me what I did for a living, and I could never explain it to him, happened to be in my house one day. It was a Sunday and we were watching some reruns of some sort, the Roger Staubach commercial came on.

I glanced over at my father very expectantly because he was a Veteran, and I thought, "Gee he is really going to watch this, and now after he sees this, I'm really going to have a chance to explain to him what it is I do."

So Roger Staubach came on after somebody said, "The following is an important announcement for United States Veterans." As soon as the guy said that, my father got up and left the room; that was the last time I let him back in the house.

But, little did he know I'd worked six months on this; that there was a tremendous amount of planning; that we had worked first at creating the conversion material that was going out to everybody that responded; that we had spent weeks negotiating and selecting an inbound 800 answering service, and that even as we sat there, there were people standing by ready to take his call; that we had lined up a fulfillment house somewhere else that was waiting to get the data from the inbound answering service so that it could immediately start personalizing an application and insert it in the preprinted kit and mail it out to him; and that there were people waiting back at National Liberty who were ready to receive the applications; and that it was a special policy form. He didn't know that we had spent months designing this particular product. A team of product development people were involved in it. So in other words, what my father saw there was the very, very, tip of the iceberg. There are tremendous amounts of moving parts involved in direct response marketing and television in particular.

In order to make it work, there are some things that are absolutely essential:

(1) You have to remember that television is a tactic and not a strategy. If you think of it as a strategy, you may wind up spending a lot of money unnecessarily. It's a tactic in your overall direct marketing strategy,

(2) In order to make this work successfully in a company, it requires a very serious and substantial commitment on the part of senior management. It is not something you can do half-heartedly or with a view towards, "Well let's just test something and see what happens and we can always get out of it very quickly if it doesn't work." It needs to be viewed as a tactic in an overall strategy that has the serious philosophical as well as financial commitment of the company. I'm talking about the senior management levels.

I want to give you a sense that there are a considerable number of moving parts, each element of which could take one person's full time effort just to oversee, if not actually, perform. Bear in mind that the companies that Gary alluded to before, which are already in the direct response television business and have been for years, have traditionally viewed it, as I said, as a tactic in the overall direct marketing strategy and are market driven. One of the problems that we typically face is that companies that are new to direct marketing, let alone television as a medium in direct marketing, tend to be the older companies which have used traditional forms of distribution and are traditionally product driven rather than market driven.

One of the distinguishing features of the commercial is that they tend to focus on markets. As Gary said for example in the Veterans commercials; the fact is that an implied affinity is essentially doing the job of the outside envelope. Obviously, it didn't work on my father, but the objective is that, when a veteran is sitting in front of his television screen and he hears someone say, "The following is an important announcement for United States Veterans between the ages of 45 to 75," that is designed to make that particular person sit up and say, "That's me, I better see what this is all about." At that point all we are trying to do is to get them to watch the rest of the commercial. When you factor in the use of a celebrity endorser like Roger Staubach, or whoever it might happen to be, that adds an additional amount of credibility

The focal point is really on the market and in this case the market being veterans between a certain age, the product starts to become secondary at that point. So, if you buy into that philosophy, the companies that are seriously into this business usually use that market driven philosophy as a way to do their product development. They say, "What is it that this particular market needs that it doesn't have?" or "What does it already have that we can modify or attached some other unique selling proposition to?"

Then eventually after you've done all your strategic thinking and planning is when you get into the creative development side of this. I wanted to spend some time telling you actually how these things are done creatively.

You have to bear in mind that in direct marketing in general, there are three key factors: 1) Media, 2) Offer, and 3) Creative Effort. That is their order of importance.

Generally speaking, the media, whether it is television or any other type of medium, accounts fully for 50% of the overall degree of success or failure of any given project. Typically the offer accounts for another 30% and that leaves only 20% for creative effort. So there is an old maxim in direct response marketing that says, "You can mail a horrible looking package to a great list and get acceptable levels of response if not an outright success."

But conversely, you can't take a package that is absolutely perfect in every way, an award winner that is beautiful, with a mediocre or even good offer and mail it to a bad list and get any kind of results at all. The same holds true in television.

It all starts with the media. In order to do it correctly, you need someone either internally or externally who is an expert at buying direct-response-media television. That person is very different from the buyer who buys television time in general. There are a few people in a few firms nationally that specialize in this kind of buying. When they do this kind of buying that is all they buy. There is no such thing as a weight card price for this type of television time as Gary alluded to. All of it, and I mean 100%, is strictly negotiated, and frequently the price you pay depends directly upon the skill, the presence, and the other work that your immediate buyer has done before.

And even though it is generally true that, when you are buying time like this, it is run of station and that means that you don't necessarily have any control of where it goes, some people who are very experienced in this type of media buying can, in fact, position the commercials in the right parts of the day to gain the maximum possible advantage. People who are involved in direct marketing are in the business of cost effectiveness.

They are not selling insurance; they are not selling pots and pans; what they are selling is cost efficiencies, and their goal in life is to deliver the product or service or whatever it is to the ultimate consumer at the most cost effective level possible. And in this case, since media counts for so much of the overall mix in the test, let alone the roll-out, it is absolutely critical that that ingredient is covered by someone who is skilled in what they are doing.

When you go about the creative process, generally speaking the first thing you see, such as the television commercial if you are a consumer, is generally the last thing that is done. At least in our case at National Liberty, when we put together a campaign, we actually started from back to front. It is what we call breaking the back of the problem. The problem is how are we going to get these people to buy whatever it is we are trying to sell them?

Ultimately, we know that a certain percentage of people will have in their hands some piece of mail, some package, that we call the conversion kit. That's really where the sale is made. As Gary pointed out, this is just the upfront part, to get as many leads as we can in the door. The ultimate task is to convert them into premium paying customers. So we start at the back and work forwards. What is the overall strategy and what are the detail tactics that we are going to use to get these people to buy?

Are we going to use a personalized letter front and back? Is it going to be two pages, four pages? What is the brochure going to look like? Are we going to use any kind of incentive or premium like a medallion or a key chain or some other piece or something that has a perceived value? Are we going to use some kind of additional premium to get customers to buy once they've paid their first full premium or are we going to ask for money? If we are going to ask for money, is it going to be credit card, or direct bill monthly? What are the key graphics going to be? If it is a Veterans case, are we going to play off their military affiliation, or are we going to try to segment them by their branch of service and go after them that way? Or are we going to try to zero in on some other factor? So we start from the back working forward and eventually wind up creating the commercial that we think is going to play into the conversion strategy.

It is then that we start thinking about the media and the markets that we are going to test in. As Gary pointed out, even if you know that your maximum allowable acquisition cost, at least as it relates to the lead generating portion of your program, is $11.83, that does not necessarily mean that the Phoenix Arizona KPHO station which is projected out at $17.67 per inquiry may not be cost effective on the back end. For some reason, the conversions that comes in from that station may be higher than the ones that come in from a Philadelphia station that is listed at $8.56. Unless you're privy to the financial pro forma of a program like this, it's hard to make a judgment based on the lead generating costs.

In some cases it is still possible to structure a deal with a television station, primarily Cable, which will air your commercial on what is called a PI (Per Inquiry) basis. This means that there is no real charge for the air time, but rather you the marketer/company wind up paying the station only for inquiries that you receive. So if the station has a commercial of yours that it perceives to be a real good one, it will show your commercial as often as possible. The more times the station shows it, the more money the station makes because it is getting paid on a per inquiry basis.

Obviously it is going to wear out because the station is going to show the commercial a lot. The commercial will be shown until it reaches a point diminishing return, and then the station will put someone else on and then turn around and put yours on again sometime later. That technique of buying on a per inquiry basis is something that is very difficult to do and can probably only be done by a few people who specialize in direct response television buying.

When you are working backwards on a commercial to the beginning and then start to look at some other considerations, one of the considerations is frequently whether should you use a celebrity or someone who doesn't have a famous name. Sometimes the question is, should we use the President of our Company? This is not the best idea, typically! Most companies that are in this seriously have tended to use celebrities because, through extensive testing in similar markets, they've discovered that celebrities are more cost efficient to use than the non-celebrities.

Making a selection of the celebrity usually also refers back to the market driven philosophy. You're trying to find someone who fits the images of the market you are trying to penetrate. For example; in a commercial with Buddy Ebsen for the Health Market, it was implied but not stated that the market he was really speaking to were people who were 45 or 50 and up. Obviously he was talking to people who were perceived as being the same age bracket or ranges he's in.

You've probably seen Robert Stack, who is a United States Veteran, get up speaking directly to his buddies who are veterans. Of course, Roger Staubach also is a very well known veteran, and he fits in perfectly with that market. Other companies have used Ed McMahon, targeting the people who are in the 50 to 80 year old market, and you've seen any number of other celebrities also supposedly geared toward the market they are serving.

When you start to look for a celebrity, depending on how sophisticated you'd like to be, most companies do one of two things. They might look at what is called the actor or celebrities "Q" Rating. The "Q" index is simply a number that's put together by companies that watch the television business like Arbitron and Nielsen, and they assign an index based on National Consumer Surveys done for people who watch television. It is strictly a recognizability index. So, for instance, if you find somebody with an index of say, 100 that might mean that *everybody* who either hears that person's name or sees his picture, knows immediately who he is. (And it may also mean that people attach a certain level of confidence to that person.) Whereas if someone has a "Q" rating of 25, it might mean that only one out of four people have ever heard of this person. Some companies use that as their real cut point. Other companies take the trouble to actually do personality testing where they or their agency select a number of personalities, and they narrow it down according to the market they are going to go in. Then they take the time to spend another $8,000 - $10,000 to actually do some consumer survey work relative to those particular personalities to measure, on a quantitative basis, their target audience's degree of recognition of that person and also the amount of credibility and trust that the audience will give that person.

Now, once again, you have to bear in mind that direct marketers don't ordinarily make these judgments in a vacuum. The reason that they are doing these things is because they've already tested them and they know the answer to the question relative to cost efficiencies. At National Liberty for instance, we got into a point where we thought, "You know, maybe if we spend a little more money on these things, they'd do better in a down market." So we tested using different production techniques to see if there really was any difference.

And just a very brief aside on production values; the network quality that you generally see is something that is filmed on 35mm film transferred to tape. As a result of that it can have filters and other special effects added in, it can look much softer and it definitely looks a lot better than just straight tape whereas if you do a straight tape commercial it is very obviously video tape, much the same as the video tape that you would do if you were taking home tapes or using a machine in your own house. So those are the two extremes in terms of production values.

I guess it was in 1980 or so at National Liberty, we tested the same personality (it happened to be Fran Tarkenton), same offer, same script, same location, with different production values in similar markets to confirm what we already knew to be true: which is that production values and direct response television marketing don't add any additional perceived value and definitely don't increase the response rates that you have over the cheapest possible production.

Next we have to start to consider whether we should do it on a static set in some studio or whether we should go on location. More and more now you are seeing location shots like the one with Buddy Ebsen. Once again, however, location type shooting has not added any value in direct response television marketing, and therefore you tend to see the same old tired format. But the reason that you see that format is that's what is working, and the reason it is working is because the production dollars spent on it were kept to the absolute bare minimum. So we could probably put together back-to-back five or six different commercials selling the same type of product for five or six different type of companies like Continental American, National Liberty, Union Fidelity, and Colonial Penn, and you might even wind up seeing the same type of set behind whoever the personality is in a position we call a "Talking Head." So, once again those are some of the considerations you have to come out to once you start putting these together.

And then finally, you have to make a determination as to whether or not you are going to attach any residual value to the names that you generate or to the image if any that you are going to create by using television as a tactic in your overall strategy.

Jack Ladley suggested that there is an incremental value to a lead whether or not you make a sale the first time around. This is because, obviously you've had people raise their hands and identify themselves as a prospect, if not for what you are selling them now, then certainly for another product that you will be offering them. If you are in this business, you will be offering them another product within the next twelve to fifteen months. (Maybe they didn't want graded benefit life, maybe they wanted term or vice versa.)

Direct marketers essentially think that they are in the business of cost efficiencies, and tracking is critical. What you may not realize is that in order to track accurately, someone either internally or externally needs to find an outside inbound 800 answering service, preferably one that is automated, and on line, to do the tracking. Because, if you wind up being in a "roll-out" situation where you are in with 100 different markets with 100 different television stations, somebody actually has to assign 100 different phone numbers to each one of those stations, so that when you look at the results on a daily basis, you know which station generated which responses. It can get quite confusing particularly if you're in a market like New York City where there might be five or six independent stations, and you can be on all of them at once. You can't automatically assume that any responses that come from a given market came from a particular station unless you know precisely that someone saw it there and called in. The only way to know that is to have the last four digits of the telephone number tied back to the individual station.

If you are on an automated basis or using a station that has the automated basis, it can give you a read out of the cost per inquiry on a per station basis so that you can begin the process of weeding out the ones that are not profitable or too far above your maximum allowable acquisition costs and perhaps beefing up the immediate dollars that you are spending on the stations that are producing a better than maximum allowable acquisition cost lead.

Who does all of this type of work? Is it done by somebody internally or is it done by someone externally? I think you need both but I think that it's absolutely essential to have someone internally that truly understands this type of business, who understands this method of marketing, and who has a handle on all the moving parts and knows what's involved. Because ultimately that's the only way you as a company will be able to retain the control over the overall process and, therefore, somewhere down the line, your costs.

MR. SCOTT K. LUCHESEI: You described the direct benefit in terms of being revenue or greater than the allowable acquisition costs. I found that to be true in the past fairly often. What allowed you to go ahead with the project was the incremental value you added to leads plus the value of the add on program you might conduct later.

With an operation just getting into the utilization of broadcast media, it becomes very difficult to place a value of the future utility of those names that you've generated. Do you have any recommendations as how you might evaluate that or keep from getting out of a broadcast program before you've made a true evaluation as to its ultimate worth.

MR. LADLEY: I think you can examine a couple of things:

1. You can get some experience as to the frequency and the intensity of the kinds of additional penetration you might get into your various customer bases. Out of a single solicitation, that might be the non-converts, it might be the actual people who take policies; it might be some sort of

referral process that you go through; it might be lapsed policies; or there might be any number of those.

2. You can then develop some sort of plan which would take the form of a projection, but it ought to be a plan to re-solicit or show a different product or service to those people.

It's important to have the plan. For example, one of the things it would lead you to realize is that your direct response activity is not merely a one product or one process activity and that you need a series of products and services to do a lot of what is known as back-end marketing in a lot of areas. You need all those products fairly quickly in order to do re-solicitation.

MR. LUCHESI: Well, obviously, we always use historical results to make the projections on that. But if you don't have any historical results, what do you do next?

MR. RAITT: We've always used historical results to do those kinds of projections, and we generally think that it is reasonable to assume that, if your existing customer base typically buys at X% level when you re-solicit it for either add-on, upgrade, or a cross-sell, it is reasonable to assume that a new customer who you add on that same product line will respond in like style to future offerings.

If you don't have any historical trend data to go by, I think the best that you can possibly do is get some other numbers, maybe put together some compiled numbers from some other marketer's experience and make projections based on that.

MR. KIRAN DESAI: I heard Gary and Gene discuss the various factors which make an inquirer conversion tick, but I fail to see the product design and all the actuarial work that goes into it and wonder what we actually do after hearing all this?

MR. LADLEY: There is no question about it, that there are a lot of peculiarities of the products used in direct response. Even Universal Life will have to undergo some significant changes if it is to work in most direct response broadcast media situations we could think of. So, you have a basic issue of product design including simplification -- usually benefit structure, premium structure, and other factors. You may also have very different experience in terms of persistency, mortality, and morbidity.

I don't recall any of the panelists talking about it, but there can be, particularly with broadcast media, a much greater opportunity for anti-selection and some fairly dishonest practices actually taking place because of the ready availability of response. All of these things have to be factored into the product development process as well.

I didn't cover it in great detail at the beginning but we had that concept of allowable acquisition cost, and that recognizes the present value of profits on a product including all the factors that are peculiar to that product.

You would normally recognize much more experience differentials in direct response by segment. A simple example of segmentation in direct response, but certainly not the only one, is that, if you recognize your present values by issue age, you almost always find that the low premium products (usually at the younger issue ages) would provide you a lot less allowable acquisition cost. That is a very important segmentation distinction right there, and there are many others, some obvious, some not so obvious, which have to be looked at.

Actually, the same thing carries over into agency business as well, but there it just tends to there be looked at in terms of a percentage of premium as opposed to dollars available for making the sale.

MR. BRADLEY M. SMITH: Jack, you talked about allowable marketing costs and present value of profits in the front versus the present value of profits on the back and in the value of the list. Would you address exactly what you've seen as far as how deep companies are willing to go on the front end as far as taking a loss counting on back end profits. That is, what kind of discount rate are they using or are they willing to lose $10 per policy or 10% of premium or 5% of premium as a GAAP profit margin, say, on the front end, planning on making it back on the back end?

The second question has to do with the GAAP accounting of that. Are companies generally recognizing the loss as unrecoverable and then recognizing the gain on the back end of the product or are they deferring the entire acquisition in the front end assuming that it will be recoverable front end and back end?

MR. LADLEY: In response to your first question, which, I believe, is related to how much companies wanted to "subsidize." That would depend on the kind of model that gets created for the particular effort you've got. If you're creating nine leads for every one and you have a very successful program for converting those leads, that would obviously permit you, if you were of this philosophical bent, to spend considerably more up front.

MR. KAUFFMAN: It clearly varies by company, but one of the ways has to be totally related to what you have in place as available cross-sell and add-ons, not which you hope to have in the future.

One way you can go about it is, if you are selling a given group of products and, for simplicity, let's say that all of them are in a general direct mail campaign, that you could spend 125% of first year collected premium, given the other assumptions hold true.

You might decide based on your present policy or cross sell cycle which might be four offers during the next 12 months, that penetrating these qualified leads allows you to bring in new business at 70% on a dollar as opposed to125% and put that present value on to the TV sale. Maybe it allows you to use 175%. But the formula really needs to be one that is related to what you really have. You can't kill yourself. We usually don't recommend TV as a medium for people who are just starting in the business. You really need to have all the other elements in place.

MR. RAITT: In our experience, there is a pretty wide continuum all the way from one end where companies will say, "We are not going to do this unless we can break even or better in the first year," in which case they don't do it because that is virtually impossible. This goes all the way to companies being as aggressive as possible because they know that they've got the mechanism that Gary spoke about in place and that they are going to hit prospects with four cross-sell opportunities and maybe two add-ons or upgrades, etc. They've been doing it for a number of years and can historically project what the actual real dollar value is of each one of those names that they are putting on the books. It is purely a function of your company's individual philosophy.

MR. LADLEY: If I didn't emphasize it enough, that philosophical difference is very important. In some companies, which reject that notion, there is very strong feeling that policies ought to be, using the phrase, "Self-Supporting" and stand on their own. There is not much that you can do to change that philosophy, not that you want to change it, and that's the way they are going to approach the business. Others are willing to take advantage of every opportunity they have.

MR. RAITT: Jack, there is another aspect of that. In today's market both in the agency side and in the direct response side, we've always been in the business of "buying a customer." And in buying a customer, even though we may have spent $X amount on the agency side in commission, we could make $X amount in profit, but competition is taking out a lot of those profit margins.

One of the main advantages of direct response TV or direct mail, is that it allows you to intensify the relationship. I think that is a key phrase. When you buy a new customer, the advantage is that you can now intensify the relationship with the customer, sell multiple products, and have more control over what you sell within the limits of the profit margins. So it really pays for you to have this type of back end marketing program because not only are you leveraging those leads for which you can attribute the cost of a customer, but also it is important to remember that the products you sell, those that intensify relationships, are products that can inherently have greater profit margins because they are your own policy or prospect base. That might be the case if you are asking an agent to go out and sell another product to a customer where the same price philosophy and competitive philosophy and lower profit margins are going to come into play.

MR. LADLEY: In regard to what some of the GAAP treatments could be or what some of the GAAP treatments are, the idea would be that if you are spending more than what you know to be the present value of profits in the business, what do you do with that excess? I guess I should point out that this doesn't just occur in direct response, and it doesn't occur just in this situation of spending more. There are a lot of expenses that occur in direct response that deal with testing and other areas developing some of your marketing functions which are staff type but will lead directly to new business production in the future that are very difficult to assess or defer on a GAAP basis.

Again, I'd have to answer from a philosophical point of view. (First I have to point out that the difference between how you may assess profitability of a product and how you may assess its GAAP treatment would very likely be different, for one the discount rate and for another some of the other assumptions).

Let's say for now, as Brad suggested, that you are spending more than even the GAAP present value of profits. I think most direct marketers, people who specialize in marketing products through direct response as opposed to direct response actuaries, would tell you that you do have something of an asset there and that can be evaluated then.

Some companies take that kind of approach when they develop values for lists and perform other activities. Another approach is many companies make use of an agency set-up, not through the insurance company itself. A third way that comes to mind would be to make the kind of GAAP demonstration that might be made based on an entire block of business which would include add-ons, upgrades, list rentals, all of the other things, bounce backs, and such, and show that the total block is, in GAAP terminology, recoverable.

MR. DESAI: You could create a separate corporate entity so that the value taken for the insurance entity is only the present value of profits that matches and the excess entity cost in the corporate entity so your arms length transactions essentially get the effect of the GAAP. That is one of the ways of actually letting the profits emerge; they can't emerge in a non-insurance entity as one of the by-pass methods.

We have found that value of the name on a list does increase exponentially by the way and Gary is right. As you have more products, not only the value of the name increases because you are selling to your own clients but it increases expotentially.

MR. LADLEY: We've seen hospital indemnity commercial and graded benefit life commercials. Do you think that Universal Life, Individual Retirement Accounts and perhaps even other more complex benefit plans can be sold through broadcast media?

MR. RAITT: The secret is going to be to simplify the product so that it is not complicated, but I believe a Universal Life type product can be sold, it just has to be formulated differently.