Reevaluating affiliate marketing

No wonder this teddy isn't smiling: First-quarter sales at Annie's Attic parent company Dynamic Resource Group were down 6%.

Affiliate marketing was all the rage during the infancy of Web commerce. In the e-commerce equivalent of locker-room bragging, marketers boasted about how many affiliates they were linked to. Quantity was quality, or so it seemed.

But as online marketers were discovering that buying commercial time during Super Bowl wasn't the most effective use of advertising dollars, they also realized that more affiliates didn't necessarily translate to more sales. For numerous i.merchants, other means of attracting shoppers, such as search engine optimization, provided a better return on investment. In terms of buzzwords, "affiliate marketing" was going the way of "hits" and "stickiness."

Nonetheless, success stories abound. Food marketer Omaha Steaks estimates that affiliate marketing generates 10%-15% of its online sales. Discount apparel pure-play Bluefly credits affiliate marketing with much of its 33% sales growth last year. And apparel and home goods mailer Blair Corp. has gained substantial incremental sales via affiliate marketing.

Affiliate marketing takes many forms. Basically, it's striking up an agreement with another Website to feature a link for your site. Web marketers often use third-party service providers, such as Chicago-based Performics, New York-based Linkshare, or Marlborough, MA-based Be Free, to seek appropriate affiliate partners, track results, and manage payments.

Omaha Steaks has more than 23,000 affiliates; revenue from its programs grew 70% last year.

In the early days of e-commerce-seven years ago or so-affiliate marketing was much looser. Often Websites swapped links without worrying too much about commission structures; the goal was simply to capture eyeballs and drive traffic. Back then the trend was to pay per click rather than pay for performance. In other words, a Website would pay an affiliate a few pennies for each visitor who came from the affiliate's site, even if the visitors didn't make a purchase.

"In the beginning, merchants who went online paid millions of dollars for billions of banner impressions wherever they could get them," says Chris Park, affiliate/ partnership manager for Performics. "Once banner ads became relatively insignificant in the overall online marketing realm, merchants backed away from the Internet and regrouped. But now they can get advertising space as highly targeted as they desire and pay only for results."

Setting a price

Omaha Steaks, like most other affiliate marketers today, works on a pay-for-performance model. If John Doe clicks on the Omaha Steaks link on USA Today and then buys from the Omaha Steaks Website, the cataloger pays USA Today a percentage of the sale.

Jim Paschal, director of online marketing for Omaha Steaks, won't reveal his company's payment structure. But Chris Henger, vice president of sales and marketing for Performics, says commissions can range from as low as 5% to more than 20% of the sale, depending on many variables, including the product category, average order amount, the brand, and conversion rates.

At Blair Corp., a number of other factors come into play as well. Jeff Parnell, vice president/general manager, e-commerce for the Warren, PA-based multititle mailer, says key metrics include customer acquisition costs, selling expenses, and customer lifetime value.

Along with the commission rate, the marketers have to agree on the commission duration. The commission duration takes into consideration that shoppers don't always buy from a site the first time they visit it. Let's say Omaha Steaks and USA Today have a 10-day commission duration. So

long as John Doe bought from Omaha Steaks within 10 days after he first visited the site from that of USA Today the cataloger would pay the newspaper a percentage of the sale.

According to Henger, the nature of the product typically determines the commission duration, which can range from five days to three months. A high-end consumer electronics marketer will generally have a longer commission duration than a gifts marketer because it usually takes an electronics shopper longer to make the purchase decision.

To encourage affiliates to give their links prominent Website placement, marketers often create stepped-up commission structures. For example, the 6,500 affiliates of gifts and housewares cataloger Lillian Vernon Corp. earn a 6% on sales of up to $3,499. On sales of $3,500-$9,999, affiliates earn a 7% commission. And on sales of $10,000 or more, affiliates receive an 8% commission.

Lillian Vernon also pays Linkshare a percentage of its monthly sales generated from affiliates for administrative and accounting services, such as distributing checks between the affiliates as well as keeping tracking of the overall affiliate activity. Linkshare helped the cataloger launch its affiliate program in March 2002.

Determining a fair payment structure can be a bit of a balancing act. If commissions are too low, you'll have trouble acquiring partners and getting effective placements on the partners' Websites. On the other hand, if the percentage is too high, you'll get lots of sales at a price you can't afford, because the overall name acquisition cost is too high.

New York-based Bluefly has apparently struck a correct balance. Affiliate marketing is one of the company's least expensive acquisition tools, says vice president of marketing Alanna Richter. "We are always on the lookout for high-traffic sites touting visitors with relevant demographics and psychographics," she says.

Last year, the $30.6 million Bluefly acquired 100,000 customers, a "significant percentage" of whom, Richter says, were acquired through its 1,000-plus affiliates. Since it began working with service provider Be Free in November 2001, Richter says, Bluefly's overall customer acquisition costs have dropped dramatically, to $17 a customer, aided largely by the affiliate program. (She wouldn't specify the company's former acquisition costs, nor what Bluefly pays to Be Free.)

Bluefly credits its more than 1,000 affiliates for helping to boost sales 33%.

"The beauty of the affiliate program is that, for the most part, affiliates find us either on our Website or through Be Free," Richter says. "We do also solicit applications from large, targeted Websites that are active in the affiliate world and that have a good fit with our business model. For instance, our 75%-off discounts make us appealing to Websites that cater to discount-seekers. At the same time, our high-fashion image is attractive to luxury Websites."

Affiliate affinity

An effective affiliate marketing program can not only generate new customers, but it can also introduce a cataloger to new audiences. A toy cataloger, for instance, may gain entre to the grandparent market by affiliating itself with a Website catering to retirees.

By the same token, a lack of affinity among affiliates can doom a program. Or as Performics' Henger puts it, there has to be a reason the visitor to the originating Website would be interested in visiting the affiliate. The same retirees who might click onto a Website selling Raggedy Ann dolls and shiny suits when it's time to buy their grandkids a gift probably wouldn't consider buying them BMX equipment. So a cataloger selling extreme-sports gear might think twice about partnering with AARP the Magazine.

Amy Steel, senior manager of marketing for Philadelphia-based Anthropologie, says concerns about affinity have kept the cataloger/retailer of eclectic women's apparel and home furnishings from getting involved in affiliate marketing. "We've been unable to find companies that match our brand close enough for us to be affiliated with," she says. "We wouldn't want to do anything that might eclipse who we are."

Indeed, "we're very careful about reviewing each site before agreeing to have them as authorized affiliates," says Omaha Steaks' Paschal. "We actually reject about 15%-20% of the sites we review, because we want to make sure there's no conflict between our brand image and where we're selling our product. There are a lot of sites out there that we don't want to be affiliated with." For instance, Omaha Steaks rejects sites that feature pornographic content or gambling.

Despite its criteria, the Omaha, NE-based cataloger has more than 23,000 affiliates, Paschal says. Of its affiliates, 5%-10% are active, he says, having generated orders within the past 30 days.

Last year, revenue from Omaha Steaks' affiliate marketing program grew about 70% to represent 10%-15% of the cataloger's overall Web-generated revenue. "We've had considerable growth in new customer revenue during the past five years due to our affiliate marketing program," Paschal says.

Beware unsavory partners

While Omaha Steaks continues to add to its list of affiliates, Frederick's of Hollywood has gotten rid of most of its partnerships. The women's apparel cataloger/retailer had more than 4,000 affiliates two years ago. Now it works with only about 50 other sites.

Anthropologie has refrained from affiliate marketing because it hasn't found companies that match its brand close enough.

"We have a very small affiliate program, which represents only about 2%-3% of our Internet income," says Jennifer Bedolla, senior marketing manager, online for Hollywood, CA-based Frederick's.

Danielle Savin, vice president of Frederick's direct division, says that affiliates infringed on the Frederick's name in order to gain commissions. These companies would buy "Frederick's of Hollywood" or similar keywords on search engines, Savin explains. Customers seeking Frederick's would end up at the affiliates, which would then direct the customers to Frederick's. If those shoppers made a purchase, Frederick's was obligated to pay the affiliates-even if the customers had been hoping to head directly to Frederick's in the first place.

A number of Frederick's affiliates, Savin says, had outbid Frederick's for use of its name as a search engine keyword. For example, Frederick's sent Web marketer Love Fifi.com a cease-and-desist letter after Love Fifi bought the Frederick's name through a search engine. (Love Fifi.com did not respond to CATALOG AGE'S calls by press time.)

Today Frederick's has a staffer policing its affiliates. To that point, Savin notes, having 50 or so affiliates is far more manageable than 4,000.

As a result of Frederick's experience with affiliates, Savin is skeptical of affiliate marketing in general. "No branded marketer should be doing affiliate marketing," she declares, unless the business has some way of policing affiliates.

But Omaha Steaks' Paschal believes his company's brand won't end up in the wrong place-as long as his company constantly reviews affiliate sites carefully.

"You can be overly conservative as to where your brand is presented," Paschal says. "That goes back to fundamentals of what you're selling. We find that if we monitor our affiliates and go with reputable Websites, there aren't many risks."

Setting Up An Affiliate Program

Without question, affiliate marketing can add sales. But it can also cause you headaches if you're not careful in establishing and maintaining your program. Here, some tips to get you started:

* Set your financial and marketing goals prior to launching the program. Base your goals on sales objectives and margins to determine a targeted return on investment.

* Establish strategic relationships that have long-term potential during the early stages of your program.

* When choosing partners, be sure their customers and target market are consistent with the image you want your brand to project.

* Remember that the top tier of your affiliate base will drive the majority of your business (ie., the 80/20 rule). Identify high-volume partners early in a program, and devote time and resources to make the most of those deals. Test creative and placements on the partner sites and communicate with them frequently. In short, spend your time, energy, and focus where you get the best results.

* Identify other affiliates whose audience and business models are similar to those of your high-volume partners and put a recruitment and communication plan in place to improve the performance of those affiliates.

* Don't limit your efforts to the busier months of the year. Leverage your affiliate relationships to help drive business during off-peak seasons.

* Understand how your best affiliate partners drive Website traffic. Do they advertise online? If so, where? Are they building an opt-in e-mail list? If so, how often do they contact their names? Do they purchase search engine keywords? Once you understand the affiliates' source of traffic and the value proposition they offer their customers, you can tailor offers and media placements to most effectively advertise to those customers.

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