CASE STUDY

The Gabriel Hansen Foundation (lifetime value)

Introduction

The Gabriel Hansen Foundation (not its real name) is the fundraising arm of a major European research hospital called the Gabriel Hansen Cancer Institute that specializes in fighting various forms of cancer. With a staff of 300 full-time researchers, 550 resident physicians, and 1,200 nurses, it is one of the largest specialized hospitals in the world. In addition to its regular hospital activity (diagnosis, treatment, recovery), the Gabriel Hansen Cancer Institute also conducts advanced medical research and clinical trials. The Institute houses 35 different research teams, and its medical research budget alone is 75M€ per year (about $90M). Resident physicians are also specialized researchers who allocate much of their time to medical research, analysis and experiments. Direct access to patients is a great advantage for the researchers, and the patients benefit from access to the latest medical advances and clinical trials. The Institute also houses top-notch research facilities and has gained a reputation as a world renowned hospital in recent years.

But medical research, clinical trials, and medical equipment are expensive. About twenty years ago, the Institute decided to focus significant effort on generating private donations to supplement their regular revenues and other sources of funding, and to professionalize their fundraising activity. To that end, they created the Gabriel Hansen Foundation.

The Gabriel Hansen Foundation is a separate legal entity, a nonprofit organization whose mission is to raise money to finance the Gabriel Hansen Institute's research activities. But after a few years of rapid growth, the amount of money the Institute was able to raise flattened out, while the Institute's needs continued to grow. The Gabriel Hansen Foundation is under intense pressure to collect more without an increase in spending.

Eva Johansson

Eva Johansson[1] is the new fundraising director of the Gabriel Hansen Foundation; she reports directly to Dr. Sørensen, a fantastic and renowned oncologist who has taken over the management of the Hansen Institute almost a decade ago.

Dr. Sørensen had an extremely strong reputation as a doctor and turned out to be a brilliant director for the Institute. One of the toughest challenges in a large medical institute like the Hansen Cancer Institute is to manage the doctors and researchers, who tend to act like "divas" and have a hard time falling in line or aligning with the general strategy of the organization. Being a highly reputed oncologist himself, this was no challenge for Dr. Sørensen. Besides, with his aura, media presence, and contact list, he also turned out to be a major asset for the fundraising efforts of the Foundation.

Unfortunately for Eva, Dr. Sørensen also has very little understanding of marketing in general, and of fundraising in particular. Although he is a fantastic fundraiser at gala parties and major events, he does not fully understand the ins and outs of customer relationship management, marketing strategy, or direct and database marketing. With his strong personality, he is accustomed to being listened to without being questioned, let alone being contradicted. In other

[1] Eva Johansson is a fictional character based on the combined and transformed stories of two actual fundraising managers the author has worked with in the past.

words, Dr. Sørensen is smart, talented, and strong-minded… but a little too strong-minded, probably. And while always a perfect gentleman, he dislikes being proven wrong.

Eva knows the type and has no problem dealing with that kind of personality. After a thirteen-year experience in one of the top consulting firms in the world, she is no stranger to the challenges of dealing with strong personalities. After all, she consulted and advised the CEOs of several of the top 100 corporations in the world, and needless to say, several of them had difficult personalities and held strong opinions as well. In strategic consulting, she has learned to tell the truth and speak her mind, even if it meant challenging the client's opinion.

Eva Johansson is 43 years old. After graduating from the BI Norwegian Business School, and following a specialization at the London Business School, she worked several years in the pharmaceutical industry, mostly in marketing and sales. She then did an MBA at INSEAD, and soon joined one of the largest and most renowned consulting firms in the world, where she stayed for 13 years.

She was a Partner at the firm and about to make Director when tragedy struck. The doctors diagnosed her 7-year old son with acute lymphocytic leukemia, a rare form of leukemia, and one of the most rapidly progressing types of cancer. Although more than 90% of children aged 14 or younger survive their leukemia for five years or more after they are diagnosed, Eva's son, who had fragile health to begin with, ended up on the wrong side of the statistics. Despite top-notch treatments and aggressive chemotherapy, he died barely more than a year after being diagnosed.

After this tragedy, Eva took a one-year sabbatical to reevaluate her life priorities. She eventually decided to leave the global consulting firm and use her managerial and marketing skills to try to make a difference in the world. The job she obtained at the Hansen Cancer Foundation was probably not the best she could get (the budget she was managing was miniscule compared to what she was used to dealing with), but it was a good entry point into the fundraising industry and a perfect match with her personal values and goals.

Interestingly, she told no one about her personal story, even during the recruiting interviews. Not even her close colleagues know about her story today. She wanted to be judged through the lenses of her professional skills exclusively, not at the light of her personal life.

Donor segmentation

The Gabriel Hansen Foundation relies heavily on direct mail as a fundraising strategy, although the Foundation has explored other tactics, such as encouraging donors to enroll into their automatic deduction (i.e., monthly donation) program, or to raise money through fundraising events or peer-to-peer fundraising.

The Gabriel Hansen Foundation segments its donor list in fourteen segments, based on their recency, yearly donation amount, acquisition source, and type of donation. The first two segments group individuals who agreed to enter the monthly donation program:

- Regular DM — This segment groups individuals who have registered in the monthly donation program, and are giving money through automatic deductions. Although the Institute has a lot of donors under automatic deduction today, this figure was mostly achieved in the past by *converting* existing one-off donors to automatic deductions, especially through end-of-year phone campaigns. These conversion campaigns were costly and were progressively abandoned. A few tests have been conducted to *acquire* donors directly through automatic deductions through mailings, i.e., direct marketing, but these efforts have been drastically reduced over the last few years as well. It was extremely hard, and therefore costly, to convince people to commit to automatic deductions immediately, and the direct marketing acquisition campaigns were judged not profitable, at least not fast enough given the Institute's priorities.
- Regular Street — The Hansen Institute has hired the services of OneWayStreet, a marketing firm specialized in street marketing, to acquire donors directly under automatic deductions. OneWayStreet places associates in business districts, shopping centers, or busy avenues, and they stop people in the street to present them the activities and needs of the Hansen Institute, asking passing-by individuals if they would be interested in giving money. The average donation amount obtained using street marketing is much smaller than through direct marketing, and those individuals acquired in the street tend to drop out of the monthly donation program faster. Consequently, the fundraising department decided to track them as a separate segment. OneWayStreet receives a flat-fee of 60€ for each donor acquired through that channel, regardless of how much time or efforts it took them. They do not guarantee more than 1,200 new donors per year, though, and that's the upper limit the Hansen Foundation is allowed to work with.

The Gabriel Hansen Foundation "acquires" new donors through various channels, but the largest source of donor acquisition is through direct marketing campaigns. The Gabriel Hansen Foundation buys, rents, or exchanges lists of potential donors with other charities or list providers, and asks the prospective donors on these lists to donate to the Gabriel Hansen Institute. The return rate is usually low (typically between .75% and 1.20% based on the source and the specific appeal used), and associated campaigns provide negative returns much of the time. The lists of prospective donors have been classified into two groups: "A" and "B".

- New donors A — Lists "A" include rental and commercial lists, for instance, lists of magazine subscribers. Historically, the results on these contact lists have been disappointing, and acquiring donors through lists of type "A" is expensive.
- New donors B — The second type of new donor acquisition is achieved by exchanging lists with other charities. When a donor has stopped giving for several years, the address is "exchanged" with other charities. People who have contributed to charities in the past are more likely to make additional donations in the future to other charities ("once a donor, always a donor"), and acquisition campaign results are usually better on lists "B" than on lists "A." Unfortunately, the addresses of these individuals end up being shared by many different nonprofit organizations, and consequently, they tend to be often solicited by competing charities.

Donors who have made their last donation over the last 12 months, and who are neither under automatic deductions nor have been recently acquired, are classified into:

- Active Top — Donors who have been active in the last 12 months for an annual contribution of 300 € or more.
- Active Middle — Active donors with an annual contribution between 60 and 300 €.
- Active Bottom — Active donors with an annual contribution of less than 60 €.

If donors do not renew their contribution or do not make another donation over a period of 12 months, they fall into one of the following "warm" segments, depending on which active segments they were in previously. Warm donors are individuals who have made their last donations within the last 13-24 months:

- Warm Regular — When a donor under automatic deduction exits the monthly donation program and does not make any additional donations, he or she is moved to the "Warm regular" segment.
- Warm New — This segment groups donors acquired last year (either in the "New donors A" or "New donors B" segment) but who have not been active since then. In fundraising jargon, it is often said they have not been "consolidated."
- Warm Top — Donors who used to be in the "Active Top" segment a year ago but who have not been active recently.
- Warm Middle — Donors who used to be in the "Active Middle" segment.
- Warm Bottom — Donors who used to be in the "Active Bottom" segment.

Finally, if donors do not give to the Institute for an extended period of time, they fall into:

- Cold — Donors whose last donation occurred 25 to 36 months ago.
- Lost — Donors whose last contribution was more than 36 months ago. With more than three years of inactivity, they are considered lost forever.

Donor acquisition

Last year, the Gabriel Hansen Cancer Foundation relied on several donor acquisition campaigns:

1. Two waves of direct marketing campaigns (a smaller one in May-June, a larger one in November-December) to acquire individuals from purchased, rented, and exchanged lists. They sent a total of 840,000 solicitation letters, with an average return rate of 0.91% (a little less than anticipated).
2. One test campaign of 50,000 mailings to acquire new donors directly into their monthly donation program. This test turned out to be catastrophic, as it helped acquire only 60 new donors in the Institute's monthly donation program (a return rate of 0.12%). The campaign cost amounted to 50,000 €, which translated into the exorbitant sum of 833 € per newly acquired donor.
3. Their contract with OneWayStreet, which generated 1,200 new donors under automatic deduction, and cost only 72,000 €. In other words, street marketing acquired 20 times more monthly donors for only +44% of the investment!

The table below displays the detailed results of last year's donor acquisition results:

Category	Mails sent	Cost per mail	Total cost	Return rate	New donors	Gross acquisition cost per donor
Regular DM	50,000	1.00 €	50,000 €	0.12%	60	833 €
Regular Street	n/a	n/a	72,000 €	n/a	1,200	60 €
New donors A	275,000	1.10 €	302,500 €	0.67%	1,836	165 €
New donors B	600,000	0.90 €	540,000 €	0.97%	5,845	92 €
Total			964,500 €		8,941	

Table 1 – Gross acquisition cost represents how much money had to be invested in acquiring one new donor. It does not take into account how much money these individuals contributed in the year of their acquisition. Last year, the total budget for acquisition campaigns was 964,500 €.

When Eva Johansson took over, next year's marketing plan for new donor acquisition campaigns was almost finalized based on the following assumptions and decisions:

- Return rates for New donors A and B were expected to slightly increase, especially since a new copy-editor for the letter has been hired based on the excellent results of A/B tests from last year.
- Despite intense negotiations, OneStreetMarketing refused to guarantee more than 1,200 new monthly donors per year.
- Following the catastrophic results of the Regular DM acquisition campaign, it was decided to entirely abandon direct marketing efforts to acquire monthly donors. The return rate was too low, and the cost of acquisition unacceptable.

The current plan looked as follows:

Category	Mails sent	Cost per mail	Total cost	Return rate (*)	New donors (*)	Gross acquisition cost per donor (*)
Regular DM	0	1.00 €	0 €	0.12%	0	833 €
Regular Street	n/a	n/a	72,000 €	n/a	1,200	60 €
New donors A	300,000	1.10 €	330,000 €	0.71%	2,130	155 €
New donors B	660,000	0.90 €	594,000 €	1.05%	6,930	86 €
Total			996,000 €		10,260	

Table 2 – Next year's marketing plan for donor acquisition. (*) = expected

The first major crisis

Only a couple of months into the job, Eva went through her first major crisis. Dr. Sørensen summoned her into his office and told her:

> "Listen, Eva, I know you are not going to like it, and I'm sorry about it. Believe me, there is nothing personal, but I have a really hard time with next year's budget. Public Services have yet again reduced their financial contribution to the hospital, and our financial needs have never been higher. I have reviewed our major cost centers, and one of them strikes out like a sore thumb: the budget we set aside for the donor acquisition campaign next year. Initially, we planned to invest almost a million euros [see Table 2], but these campaigns will barely generate 600K € in fundraising, for a net loss of more than 400K €. We cannot afford that. I know we need to invest in our donor database and make it grow for the future, you told me that a million times, but in the current situation, it's just too expensive. Besides, we have a solid base of loyal donors, so I'm sure we'll be fine. We can't afford to invest so heavily in donor acquisition right now. I'm sorry, but I'll need to strike down that line of budget. We'll simply freeze donor acquisition campaigns for a year. Just a year, don't worry, no more. We'll start the process again when we have a bit more breathing room…"

Eva left the meeting unnerved but determined to change Dr. Sørensen's mind. However, she knew she lacked ammunition to do so. She believed his strategy was business suicide, but he was convinced otherwise. When two strong opinions collapse heads-on in a "battle of faith," the outcome is often based on politics, not facts, and she knew she was not in a position to convince Dr. Sørensen his strategy was dangerously myopic. It was a classic "demonstrate the ROI or die" kind of situation, and right now, she had nothing to show for herself.

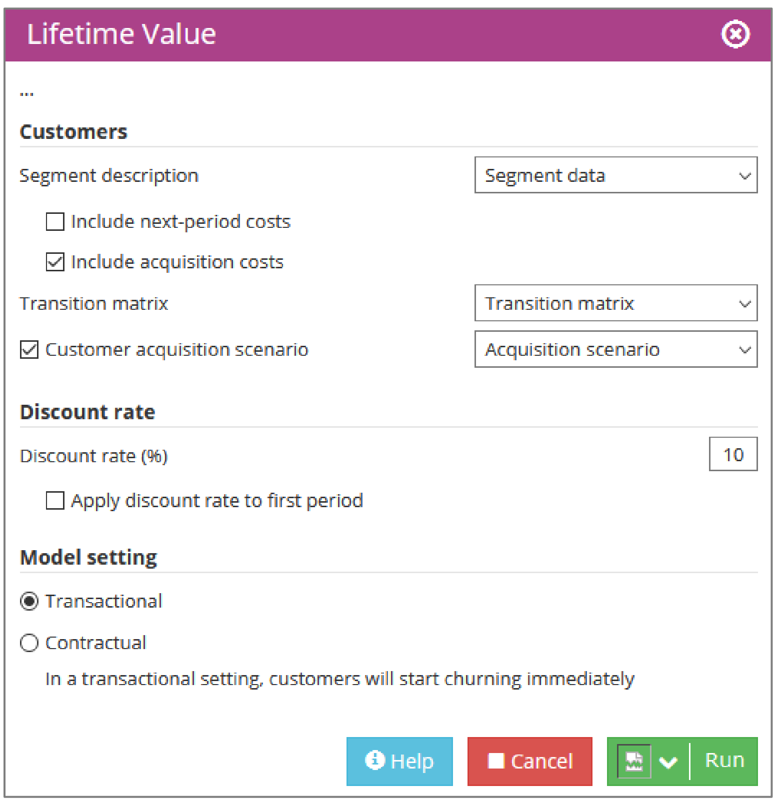
She swiftly reached out to a colleague and friend at her former consulting firm, a math genius and analytics wizard named Sumon Mukherjee. He agreed to work on her problem pro bono (pro bono work is a big part of the consulting firm's culture). This is what they did together:

1. Eva sent Sumon an anonymized version of the donor database containing the full history of past donations and solicitations.
2. Sumon loaded the data and segmented the database into the 14 segments described earlier, both in terms of in which segments donors are classified today, but also recursively over the last few years to see in which segments they used to be in the past.
3. Sumon also computed how much money a typical member of each segment donated per year on average, minus the costs of solicitations and marketing campaigns incurred for each segment's member, and labeled this figure "Net margin per year". This figure does <u>not</u> include acquisition costs. For instance, to acquire a "New donor A" costs on average 155 € (see Table 2), but a typical individual in that segment will give 60 € in the year he or she is acquired (that amount includes his or her first donation). Therefore, the *net* acquisition cost of a "New donor A" in the first year is 95 €.
4. Then, he computed the transition matrix of donors across segments, year over year, as shown in Table 4.
5. Using this setting, and assuming the transition matrix observed recently would remain stable for the next few years, they simulated how much money the Institute would raise under two scenarios: if the acquisition budget was maintained next year, and if it was not.

Question 1
Dr. Sørensen stated that donor acquisition campaigns would generate a net loss of 400K€ next year, and that the Institute could not afford it. Is this figure correct? How did he reach it?

Question 2
Using lifetime value simulations, develop your arguments to powerfully demonstrate that cutting donor acquisition campaigns, even for just a year, would be a terrible idea. Develop the arguments Eva must have used a few months ago.

For all your simulations, use a discount rate of 10%, not applied to the first period, and a transactional setting[2], as shown below:



[2] Technically, donors under automatic deduction are in a contractual setting (the Institute knows when they exit the monthly donation program; and while they are in the program, their donation payments are scheduled and known in advance), whereas all the other donors who make one-off donations are in a transactional setting. For these simulations, just assume a transactional setting for all.

Segment	Donors (as of today)	Net margin per year
Regular DM	12,452	336 €
Regular Street	6,531	132 €
New donors A	1,836	60 €
New donors B	5,845	42 €
Active Top	1,521	853 €
Active Middle	6,594	128 €
Active Bottom	18,006	40 €
Warm Regular	1,411	
Warm New	4,320	
Warm Top	543	
Warm Middle	2,142	
Warm Bottom	9,652	
Cold	14,210	
Lost	63,521	
Total	148,584	

Table 3 – Segment count and net margin per donor in a segment. On average, and after taking into account the cost of solicitations throughout the year, a donor in the "Active Top" segment contributes 853 € net per year. These figures do not include acquisition costs.

	Regular DM	Regular Street	New donors A	New donors B	Active Top	Active Middle	Active Bottom	Warm Regular	Warm New	Warm Top	Warm Middle	Warm Bottom	Cold	Lost
Regular DM	96%							4%						
Regular Street		81%						19%						
New donors A	2%				5%	19%	6%		68%					
New donors B	1%				1%	14%	24%		60%					
Active Top	1%				49%	13%	1%			36%				
Active Middle	2%				5%	52%	12%				29%			
Active Bottom						5%	43%					52%		
Warm Regular					1%	2%	3%						94%	
Warm New					1%	11%	5%						83%	
Warm Top					16%	4%	1%						79%	
Warm Middle					2%	19%	4%						75%	
Warm Bottom						3%	13%						84%	
Cold						2%	5%							93%
Lost														100%

Table 4 – Transition matrix. The leftmost column represents the segments in which donors were a year ago; the topmost row represents the segments to which they transition a year later. Each row sums up to 100%.

Planning for next year

After presenting her arguments (see Question 2), Eva managed to convince Dr. Sørensen to maintain the 1M € budget for next year's donor acquisition campaigns, but she knew it was a close call; she used a lot of her political capital to make him change his mind. Now was not the time to disappoint.

Last year, the Foundation had generated a net revenue of 7.1M €, but it had been a disappointing year; actually, it was the first year that the Institute raised less money than the previous year (which is probably why the former fundraising manager was gently pushed through the door, and why Eva got the job in the first place). The year prior, the net revenue was 7.2M €.

This year, knowing that the budget for donor acquisition had been slightly increased (from 964,500 € to 996,000 €) and that return rates were expected to be slightly improved (see Table 1 and Table 2), Eva's objectives for next year did not appear to be extremely ambitious, or at least so she thought when she discussed them with her superior: "Simply bring it back to a 7.2M € net revenue figure," Dr. Sørensen said. "That's where we were two years ago, and you have a larger budget than your predecessor used to have then. I'm sure it will be no challenge for you."

Question 3
Everything else being equal, and based on lifetime simulations, will Eva be able to reach her yearly objectives next year? If not, why not? Can you intuitively explain what is happening right now with the Hansen Cancer Institute's fundraising?

Question 4 (advanced question)
By modifying the donor acquisition plan for next year, could Eva Johansson achieve her yearly objectives? How? At what cost? Feel free to modify donor acquisition scenarios at will, as long as (a) you do not plan more than 1,200 new "Regular Street" per year, and (b) your overall budget does not exceed 996,000 €.

Planning for the long term

Beyond her yearly financial objective of achieving 7.2M € of net revenue, Eva wants the Hansen Foundation to succeed in the long term. It is not only a question of short-term business objectives for her.

Of course, if she fails to achieve her yearly objective the very first year she is hired, her prospect with the Institute might be short-lived, and she knows it. She has to balance short-term results and long-term strategy.

Question 5
Investigate: For each of the four donor-acquisition segments (Regular DM, Regular Street, New donors A, New donors B), answer the following questions:

- Taking into account both acquisition costs and net margins generated in the first year, how much net margin does each new donor generate in their first year?
- Answer the same question in terms of long-term, lifetime value. Use a 10% discount rate and the options discussed above.
- For 100 donors acquired in each segment, how many will have been lost already after ten years, that is, how many will end up in the "lost" segment after ten years?

Question 6
Imagine Eva faced absolutely no short-term constraint at all, and she could invest 996,000 € in donor acquisition campaigns, every year. What would happen if she exclusively focused on acquiring:

- Regular DM?
- Regular Street?
- New donors A?
- New donors B

Focusing only on the long-term, and assuming a 10% discount rate, what would be the optimal donor acquisition strategy?

Question 7 (advanced question)
Suggest a donor-acquisition strategy that balances short-term constraints and long-term success, what would it be?

Question 8 (advanced question)
If you dared to break free from the 996.000 € budget constraint and to suggest a more aggressive plan, what would it be? Create your ideal marketing plan and present powerful and convincing arguments to Dr. Sørensen to defend your plan.