

The 80/20 Rule & Affiliate Marketing

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What is the 80/20 Rule?

Vifredo Pareto (1848-1923) was an Italian economist who formulated the 80/20 principle:

'In any series of elements to be controlled, a selected small fraction in terms of number of elements almost always accounts for a large fraction in terms of effect.'

The 80/20 Rule is an extension of this principle. The 80/20 Rule is applied whenever there is a question of effectiveness versus diminishing returns on effort, expense or time. When applied to affiliate marketing, for example, the 80/20 Rule can be paraphrased as "twenty percent of your affiliates will yield 80% of your results, while the remaining eighty percent will yield 20% of the results."

The 80/20 Rule is widely applicable, both in the online and offline world. The 80/20 Rule is normal and merchants must prepare for it. How does an online merchant compete in this world with a limited number of super affiliates?

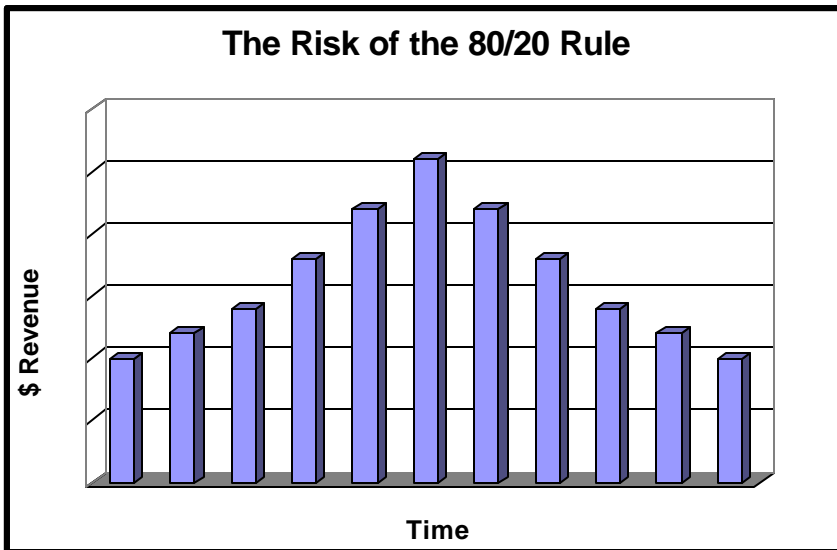
The goal of this paper is to describe the 80/20 Rule, understand if it applies to your affiliate program, what the risks are, and how LinkShare helps you win the 80/20 struggle with the power of the Network.

How the 80/20 Rule Affects All Affiliate Programs

The 80/20 Rule applies to all affiliate programs. The top 20% of your affiliates bring in enough revenue to cover your overhead and the cost of your affiliate program. These affiliates are very important to your program, and are key partners in driving sales through your site. As a matter of fact, many "affiliate marketing experts" recommend that you focus on the top 20% for these reasons. However, we at LinkShare see the danger in this.

Risk: As the top 20% of affiliates drive more traffic and sales to your site, they expect increased commissions and incentives. Placing initial focus on the top affiliates yields positive results - revenues quickly ramp up. However, this results in higher demands from these "super affiliates," leading to diminishing resources and lack of financial incentives to keep the top players loyal to your program. This is the risk of focusing on your top performers. Your program will quickly ramp up, peak, then quickly decline as the top performers leave your program for merchants with more competitive offers (as seen in the graph below). In order to grow your program effectively, you must also focus on the smaller, more cost effective affiliates to sell your products through their site.





Goal: In order to keep your costs fixed and prevent the quick decline, you must increase the number of performing affiliates in your program. Rather than focusing on your short-term goal of a quick ramp-up in revenue, we believe that you should think long-term, and build up your overall affiliate base including the “core partners”, or those affiliates who generate between one to five sales per month. You must build a large base of producers to ensure continued sales and lower overall cost to sale as described in the case study below.

Growing Your Program Effectively - The Importance of “Core Partners”

Your overall affiliate marketing strategy depends on keeping a close eye on your programs statistics and understanding the economics of your program. The top 20% of your affiliates are the backbone of your program and you must pay special attention to their needs. In order to ensure loyalty to your program, you should stay in touch with them personally and offer increased commissions and incentives for their continued success. This, however, costs money. Therefore, for every big affiliate who you must “wine and dine,” you need to remember the important core partners that are driving sales at a low cost. They are cheaper to keep, and over time will become higher producing affiliates. This will lessen the risk of your program (as shown in the graph above).

Core Partner: Affiliate who generates between one to five sales per month.

Power of the Network: The LinkShare NETWORK is so important since it provides you access to a million affiliate partners with the potential to



drive sales. The "Sweater.com" case study below shows how increased volume by lower tier affiliates lowers cost per order and offsets higher commissions to top tier affiliates. This is true of all affiliate programs, and proves the benefit of the network to make your program more competitive and successful.

Merchant Case Study:

Merchant Name: Sweater.com
 Goal: sell 1000 sweaters
 Price: \$100 each
 20% gross margins (they make \$20 per sweater sold).
 Affiliates: currently have 100 affiliates
 Baseline Offer: 5% of sale
 Top 20 affiliates: 15% of sale.

In order for Sweater.com to meet its goal of 1000 sweaters and profits of \$20,000, let's run the math to see how the 80/20 rule applies.

The top 20 affiliates produce 800 sales (80%) for \$80,000 worth of revenue. The cost to get these sales to Sweater.com is \$12,000 (15% of total sales). This cost per sale is \$12 with a profit of \$8.

The other 80 affiliates produce 200 sales (20%) for \$20,000 worth of revenue. The cost to get these sales to Sweater.com is \$1,000 (5% of total sales). This cost per sale is \$5 with a profit of \$15. We call these affiliates core partners because they drive one to five sales per month.

The combined cost for 1000 sweaters is \$13,000, or \$13 per sweater. So, by working with the core partners the overall program costs were reduced \$2 per sale or 13% and brought in an extra 200 sales.

| | Other 80 Affiliates | Top 20 Affiliates | Total Affiliates |
|---------------------------|--------------------------------|------------------------------|-----------------------------|
| # of Sweaters Sold | 200 | 800 | 1,000 |
| Price Per Unit | \$ 100.00 | \$ 100.00 | \$ 100.00 |
| Revenue | <u>\$ 20,000.00</u> 100% | <u>\$ 80,000.00</u> 100% | <u>\$ 100,000.00</u> |
| Rev Share | \$ 1,000.00 5% | \$ 12,000.00 15% | \$ 13,000.00 |
| Other Costs | <u>\$ 16,000.00</u> 80% | <u>\$ 64,000.00</u> 80% | <u>\$ 80,000.00</u> |
| Total Cost | <u>\$ 17,000.00</u> 85% | <u>\$ 76,000.00</u> 95% | <u>\$ 93,000.00</u> |
| Profit | <u>\$ 3,000.00</u> | <u>\$ 4,000.00</u> | <u>\$ 7,000.00</u> |



2. Review offer terms: monthly payments, low thresholds, and return days.
3. Analyze link type, placement of links, and creative.
4. Know your stats, share "active" best practices with inactives, communicate with your partners, and write newsletters keep you affiliates up-to-date and loyal.
5. Segment affiliates into groups to reward and recognize your top performers and motivate & activate your inactives.
6. Optimize core partners - incentivize affiliates selling a small volume of products to increase their sales via cash bonuses for new customers, free shipping, special promotions, and sweepstakes.
7. Welcome new affiliates and add excitement around your program.

In sum, be proactive! By educating and empowering your affiliates, you will see an even stronger top 20%, and a stronger, more active bottom 80%.

How LinkShare Helps You Win the 80/20 Struggle

The power of the LinkShare network resides in the extraordinary number of affiliates that you can partner with to increase traffic and sales through your site. We at LinkShare believe that you need the network to ensure enough partnerships to help you meet your goals.

Listed below are some of the tools and services that LinkShare provides to help you get full value from the Network.

1. Access to LinkShare Registrations - affiliates that register to join the LinkShare Network and B2B LinkShare.
2. Affiliate Referral Program - Affiliates that refer other affiliates to LinkShare receive compensation for every approved site.
3. Platinum Prospecting Program - Targeted efforts towards high quality affiliates.
4. Direct E-Mail - Compelling offers that target relevant content sites participating in opt-in e-mail lists.
5. LS Promote - Monthly emails containing limited time promotions available to affiliates.
6. Affiliate Application Filter - filter by site type, category, key words, or country.
7. Content Spider - identify offensive and competitive sites by key words.
8. Live Chat Hours: - average response in 6 seconds.
9. Reports in the Affiliate Management Section:
 - Affiliate acquisition numbers
 - Affiliate activation rate



- Sales by affiliate ranking
- Link use vs. effectiveness

