

The Coming Evolution in Affiliate Marketing: A Focus on Quality

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ABSTRACT—Affiliate marketing—a multibillion dollar industry and one of the fastest growing segments of online marketing—has seen fewer studies during the past decade than other channels, like search engine marketing or search engine optimization. Much sought-after performance data from advertisers has been scarce, as affiliate program management is generally outsourced and internal teams tend to be small. When eBay brought its affiliate program in-house last year, the company gained valuable insights from performance data analysis. These insights suggest advertisers may be able to improve ROI and performance by evolving their programs to better calculate and compensate for the value delivered by their affiliates.

INTRODUCTION

The affiliate marketing opportunity is perhaps the best kept secret in the online ad space. Projected 13 percent year-over-year increases through 2012¹ make the \$6 billion+² industry one of online advertising's fastest growing segments.

Yet surprisingly, fewer studies have been published on affiliate marketing by advertisers and industry analysts like Forrester or Jupiter than almost every other Internet marketing channel. Internet Retailer data shows most (almost 80%) of the top 100 online retailers outsource their affiliate programs³. As a result, detailed affiliate performance data is scarce, as many companies lack the internal teams to develop detailed analyses on data beyond typical affiliate click and conversion metrics.

When eBay brought its affiliate program in-house in April 2008 and created the eBay Partner Network, it gained direct access to affiliate performance data. After analyzing this new information, the company has begun to rethink some of the traditional notions of affiliate marketing.

A FOCUS ON AFFILIATE QUALITY

Affiliate programs are generally designed to pay affiliates

only for leads and sales, and the belief—borne out in payment structures—is that all leads and sales are the same.

The basic thinking is that all non-fraudulent activity is of average quality, and therefore all affiliates are paid equitably, with notable exceptions being the volume tiers found in most programs, and bonuses offered to well-known affiliates. The more sales and leads an affiliate sends a merchant (or the better known he is), the better he must be, and the more the merchant will pay.

This approach can lead to suboptimal results for advertisers who overpay for larger volumes of lower-quality traffic, as well as lost opportunity for affiliates who may do a better job of sending more valuable traffic, albeit at lower volumes.

However, beyond conversion rates, relatively little has been written about, or has been done to manage, the quality of the traffic that affiliates send advertisers. Most of the writing, thinking, and action in the affiliate space has been focused on how to attract and retain affiliates.

When advertisers do attempt to manage affiliate program effectiveness or quality, they primarily use broad brushstrokes at the program level, such as changing pricing and cookie latencies. Little is done to measure and reward quality and performance at an individual affiliate level, other than perhaps taking action on conspicuously fraudulent affiliates and manually bonusing certain top affiliates.

eBay's findings, described below, show how using affiliate performance data to revise the traditional program model can benefit both the advertiser and the affiliate.

1. *Not all leads are created equal.* In a pay-per-lead affiliate program, a merchant makes an estimate of the lifetime value of a new customer and pays an affiliate a portion of that value. But just as years of traditional marketing have shown how some customers are worth more to a company than others, it turns out that the average quality and value of customers delivered by an affiliate can vary significantly and consistently as well.

Some affiliates—known as incentive affiliates—pay customers to register, leading to new sign-ups from customers who seek the reward but do little else. Others might attract audiences with lower purchasing power, or by

¹ Source: Jupiter Research US Online Affiliate Marketing Forecast, 2007 to 2012

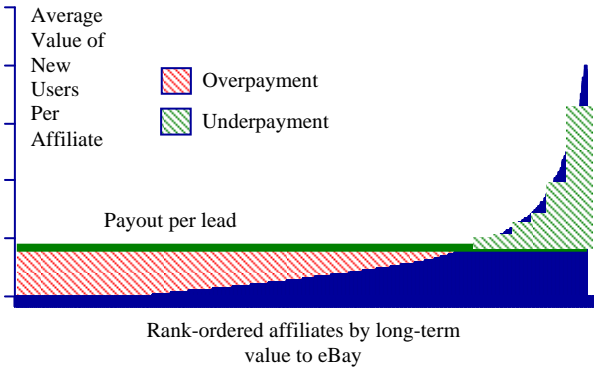
² Marketing Sherpa Affiliate Marketing Report 2007

³ Source: eBay analysis on 2007 Internet Retailer Top 500 Guide data.

The figure is an estimate based on 80 out of 100 top retailers that reported who they used to manage their affiliate marketing programs

highlighting items of low value. As one example, an affiliate site appealing to buyers of value-priced, entry-level DVD players will very likely yield customers with a lower lifetime value than affiliate sites that cater to videophiles who are looking for the latest in high-end Blu-ray Disc players. The effect of these differences is shown in Table I.

TABLE I



A typical affiliate program paying a flat fee per lead will tend to overpay affiliates who deliver customers worth less than this value (to the left of the chart), and underpay for customers worth more (toward the right). As the graph shows, the value of customers delivered can vary widely and, in some cases, the over- or under-payment can be significant.

eBay hypothesized that if it could adjust the commission to match the value and pay more for high-quality leads and less for lower-quality leads, it might begin to affect the quality of the new traffic driven to eBay through affiliates in the program. In fact, that is exactly what was found.

Payouts for Active New Registered Users (ACRUs—or new and active eBay members) were adjusted from \$25 to \$35 under the old system (based on volume) to five new value-based tiers that pay \$1 to \$50 per lead (the tiers are \$1, \$10, \$28, \$40, and \$50).

In the four months since the new pricing launched, and combined with some efforts to reduce overall fraud, the number of new users referred by affiliates qualifying for the top two tiers increased by 80 percent⁴, and the number of new users in the lowest tier has decreased by 86 percent. Although overall costs for eBay have decreased, and ROI has significantly increased, thousands of affiliates receive increased compensation of \$28 and up, which is higher than the \$25 most were receiving in the previous system.

2. *Not all sales are created equal, either.* This quality-based approach can also be applied to sales. Most advertisers tend to focus on getting their affiliates to

drive more sales, when there should be more emphasis on driving incremental sales, which eBay defines as sales that would not have happened were it not for the efforts of the affiliate. But if sales aren't the metric to watch, what is?

Metrics that describe user behavior around the sale can be quite revealing in terms of the quality of an advertiser and its placements. For example, time on the merchant's site and average page-views after a click can be a proxy to measure how effectively an affiliate generated interest for a merchant's products or how well its audience aligns with a merchant's target audience.

An affiliate whose customers spend a very short time on a merchant's site after a click (eBay has seen averages as low as 1 to 10 seconds) are probably either not reaching the right audience for that particular merchant or potentially even tricking unsuspecting users into clicking the links. Many are later caught engaging in fraudulent behavior, such as cookie stuffing. Although the advertiser won't pay for those clicks, cookies will be placed on those users' machines. Any time that user goes back to the merchant site within the time the cookie is active, the sale will be attributed to that affiliate.

Although this "cookie sprinkling" disproportionately affects sites with a large reach like eBay, any advertiser with a long cookie latency is encouraging this practice. Fraudsters know that the longer the cookie duration, the larger the potential benefits of placing cookies out on many users' machines.

eBay is now tracking several dozen other variables that closely correlate with quality and incrementality. Click-to-sale conversion rates, number of masked or unknown referring URLs, and percentage of buyers with fraudulent credit cards can be very indicative of the quality of an affiliate's traffic. These will of course vary for each merchant and its objectives.

SEGMENTING BY VALUE

Using this value-based approach, one can start segmenting affiliates with different business models and separating affiliates who send high-quality incremental traffic from those who don't. While eBay's findings could fill another paper, some high-level conclusions have begun to emerge.

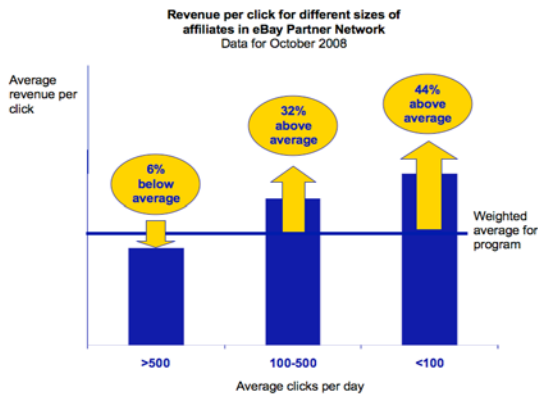
- Some of the models that have historically produced the highest volumes of clicks and sales in affiliate programs, like remnant inventory ad networks, are some of the least incremental along these quality-based metrics.
- Affiliates who take the time to create high-quality sites with value-added content tend to perform better than those who simply slap together hundreds of sites that

⁴ These figures exclude the typically high-performing Christmas season

contain very little other than affiliate ads and AdSense. It probably doesn't come as a shock that ads crammed five or ten to a page on ringtone sites don't capture the same quality of users as well conceived ads thoughtfully integrated into product-oriented content.

- Because of the great care many small affiliates put into their sites, they often can outperform large affiliates in terms of the traffic quality. This challenges

TABLE II



some of the conventional wisdom in affiliate program compensation, as most programs are set up precisely to reward bigger affiliates more. A different picture emerges when you look at the results in Table II above. The data would seem to suggest that some small affiliates driving quality traffic should be compensated, bonused and rewarded just as much as—or even more than—large affiliates.

This can be difficult, as the manual process of bonusing large affiliates is hard to scale and carry out for hundreds or thousands of smaller affiliates. Advertisers will need to invest in better technology and more innovative commission structures to reward and grow the best affiliates in their programs.

MOVING AFFILIATE MARKETING INTO THE FUTURE

Metrics and pricing are no silver bullet for affiliate marketing success—they must always be complemented by capable people who can develop close personal relationships with top affiliates, help them attract and send over higher quality traffic, and identify new types of fraud when they occur.

The affiliate community needs to continue to ask these questions and help provide the right guidance and incentives to enhance both our networks and the industry as a whole. Compensation in the affiliate channel needs to continue to evolve to reward and encourage the best affiliate models and to create a win-win situation for advertisers and affiliates.

Some of the world's leading affiliate and ad networks are

already using this type of thinking to reward their best publishers. AdSense adjusts its cost-per-click payouts based on a series of quality-based metrics it has developed during the past few years. Amazon encourages quality in a way by compensating more for deep linking and some of its tools, which it presumably has tied to better-quality publishers and overall results.

Hopefully this data invites more debate and studies about quality in the affiliate channel and how advertisers can better work with affiliates to improve some of these metrics.

The more Internet marketing groups can raise the bar and prove the incrementality of affiliate marketing in their own organizations, the larger the investments in commissions, tools and people that can be devoted to help this channel and its best affiliates reach their full potential.

About the Authors



Will Martin-Gill, Senior Manager, Internet Marketing, manages the North America and Asia Pacific affiliate programs on eBay Partner Network. Before joining eBay, Will was a Consultant with Boston Consulting Group. His projects included an engagement on the start-up team that created and launched Orbitz.com. Will holds a B.S. in systems engineering from the University of Virginia, and an M.B.A. from Harvard Business School.



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Kim Thai, Senior Manager, eBay Partner Network Operations Team, has over eight years of experience in the hi-tech industry. She joined eBay in 2005, managing various International and Trust and Safety programs. Kim graduated from UC Berkeley with a B.S. in economics.



Chad Wehrmaker, Senior Manager at eBay, has been managing eBay Partner Network operations since 2007. He joined eBay in 2003 as part of the acquisition of FairMarket, Inc. where he spent five years managing various aspects of private-labeled auction websites, including Sam's Club, Playboy Enterprises, CompUSA and Dell Auctions. Chad graduated from Trinity University with a B.S. in business administration.

About eBay

Founded in 1995, eBay pioneers communities built on commerce, sustained by trust, and inspired by opportunity. eBay enables ecommerce on a local, national and international basis with an array of websites—including the eBay Marketplaces, PayPal, Skype, Kijiji, Rent.com and Shopping.com—that bring together millions of buyers and sellers every day.