



Sure, companies say they **put customers first**. But only a few do. They're the ones whose stock you want to own.

**BY LARRY SELDEN AND
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5 Rules for Finding the Next Dell

DELL, BEST BUY, and Royal Bank of Canada are stocks you wish you'd bought years ago. They've all been knock-out performers for shareholders for the same reason: Each

has truly put customers at the center of its business. And we mean truly—not in the golly-aren't-customers-great way that most companies have hyped for years but rather in a way that transforms the entire business. If you'd like to spot more such stocks, consider this vignette about electronics retailer Best Buy, related by UBS retail analyst Gary Balter:

Balter walked into one of the company's stores in Pasadena in May and met an employee named Matt. What was most remarkable about Matt wasn't his helpful demeanor or plentiful pleases and thank-yous but rather what he knew about his customers—including one key group of them. Best Buy even has a pet name for them. After carefully studying the area around its Pasadena store, the company concluded that one highly promising bunch were upper-income soccer moms, which the

WELCOME, MOMS
Best Buy's Pasadena store, aimed at "soccer moms," includes a shopping assistant (center).

company singularized as "Jill." And it wasn't just the store manager who knew about Jill and her shopping ways, but sales people right down the line. Matt, for instance, took

the time to explain to the visiting analyst that small appliances hadn't been selling well, even though they'd been chosen with Jill in mind. So, based on interactions with customers, hourly workers moved the items from high shelves above major appliances to low racks along the main walkway. Small appliances are an impulse buy for Jill, and this way, if she needed a kitchen mixer, she wouldn't have to go over to the stoves but could find it along an aisle she frequents. Small-appliance sales soon rocketed.

But that's not the best part of the story. More surprising was that employees understood how reconfiguring the sales floor would improve the Jill segment's sales and return on invested capital, a measure that drives Best Buy's stock price. In this case they knew that selling more small appliances would not only raise profits but also do so without increasing invested capital, since the store just turns the appliance inventory faster. At most companies, employees haven't a clue what their firm's return on invested capital is, let alone the returns on specific customer segments—and even if they knew, they'd be powerless to do anything

**BEST OF
THE
BUNCH**
30%

Fourth-quarter sales growth at Best Buy's seven customer-centric stores, vs. 9% for the chain overall.



You don't need inside information about a company. Your role as a customer can be one of the best investing tools.

HOME SWEET STORE Presenting goods in settings customers can relate to helps sales at Best Buy.

ational metrics as Matt in the Pasadena store.

To see if a company operates this way, ask someone at the company: “Is someone here fully accountable for my relationship with you?” The answer—and the way it’s answered—can tell you a lot. (If the rep on the other end of the phone has no idea what you’re talking about, that’s a clue.) Another way is to check with a part of the business you haven’t used before. If you have only a checking account with a bank, call the mortgage people and see if they’ve ever heard of you.

4 Is the company managed for shareholder value?

If it is, then everyone there knows that the game is about earning a return on invested capital that exceeds the cost of capital, plus investing increasing amounts of capital at that positive spread and maintaining that spread for as long as possible. At the end of the day, those are the only factors that drive the share price. Customer-centric companies apply those criteria to customer segments. They know how much capital they’ve invested in a segment and how much return they earn on it. They maintain the positive spread by creating and reinventing enduring customer relationships. Thus, when an RBC segment manager created a program to attract first-time mortgage borrowers, she knew those customers were more interested in guidance through the scary home-buying experience than in getting rock-bottom rates (good return on capital for the bank)

and were likely to become long-term customers (longer duration of positive spread). Such companies can and do link their success with customers directly to the price of their stock.

Customer-centricity means that all employees understand how their actions affect the share price. Talk to employees. If they speak the language of shareholder value, you may have a winner.

5 Is the company testing new customer offers and learning from the results?

Seven-Eleven Japan—consistently one of Japan’s most profitable companies—does just that. (Like America’s 7-Eleven, it’s a subsidiary of Ito-Yokado.) Every week employees from all over Japan meet to discuss specific hypotheses tested and verified in the stores. It can be as obvious as changing the noodle order for the next day’s lunch based on the weather forecast. (A cold day? Serve warm noodles!) Relentless learning about what customers want and a formal process for sharing it are critical to customer-centricity.

You’d think all companies would adhere to all five rules, but few do. Customer-centricity is hard. For investors, that’s an attraction: Companies that achieve it hold an advantage that can lead to a jump in share price. They are companies investors should focus on now. Our test can help you tell the real deals from the rapidly proliferating fakes. **F**

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