



Interview: Steve Johnson, CEO ChoiceStream

By Michael Huang

Think Equity Partners (TEP): Thanks for joining us Steve. Please help us understand ChoiceStream – what is the key problem you solve and why should customers and investors care about ChoiceStream.

Steve Johnson (SJ): ChoiceStream helps companies derive insights from their customers' interactions. The key is that we are using customers' activities to understand their preferences and intentions, as opposed to confronting consumers with a long list of questions that they need to fill out in order to gain a similar understanding. Our clients include companies like AOL, Yahoo! My Movies, Blockbuster, DirecTV, Overstock to name a few. And we're engaged in several trials right now.

TEP: Would you characterize ChoiceStream as a Behavioral-targeting company?

SJ: The Behavioral-targeting companies are different; they have a pretty good knowledge of high level categories where a particular consumer has been, and what he or she has reacted to. And that's very valuable information. But it's even better if you can go one step further and deeper, and create more knowledge across many more categories about a particular consumer, like you can with our platform. For some of our customers, we're taking that next step and we're combining our data with Behavioral-targeting data to run more targeted promotions and advertising.

TEP: Where are customers on the maturity curve? Is it getting easier to sell to your customers vs. a year ago?

SJ: It's getting much easier to sell. From 2000 to about 2004, organizations were just getting the online infrastructure in place, capturing a critical mass of consumer base to get a business

started. And so personalization wasn't on the top of anyone's list. I'd say the market started maturing around 2005 when online retailers and portals had critical masses of customers that they wanted to hang on to and derive more from. And so retention, convenience, relevance, and discovery became of primary importance. Although personalization success stories were well known (metrics like Netflix shipping 60% of their DVDs from recommendations and Amazon deriving 30% of their bottom line from personalization), organizations had a tough time figuring out how personalization could be applied to their specific businesses. So we'd have to do a pilot or a trial. Now, even that is becoming less and less necessary. In 2006, the entertainment distribution industry woke up to the need for personalization. Entertainment was no longer just television shows, but Web video, music, games, and user-generated content. We've gone from a 500 channel problem to a 500,000 channel problem times at least three different screens, the PC, the television, and the mobile. And of course, personalization is a necessary ingredient because consumers would be overwhelmed otherwise. The mantra that's universal with the entertainment industry is that they want activity on any one of the screens to improve the experience on all of the other screens.

TEP: Are you also trying to get insights from customers' off-line activities?

SJ: Multi channel retailers are among our customers and they all want to use their offline data. In general, we can ingest data of many kinds, from catalog sales or offline sales. We can also take the demographic data or captured logs of advertising click streams, and feed it into our models and build a more-informed user profile.



TEP: What is your secret sauce?

SJ: There are three sides of this platform, and all three sides are equally important. First, it's the statistical analysis engine that can take chunks of data and perform meaningful analysis, and we have a fabulous scientific team that continues to extend the statistical side of the platform. Second is the classification engines that can take the content, including music, movies, or TV shows, and decompose the content into its constituent parts and derive characteristics or attributes of that object. We think of those things in terms of 60 or 70 attributes. So when the consumer starts browsing or downloading or purchasing or writing, those are expressions of interest or intention in a collection of attributes. That gives us much quicker and more-refined insight into the consumer's behavior because we know a lot about what the consumer is interacting with. Third is to use this understanding of consumer's intention to provide the consumer with a list of recommendations.

TEP: How do your customers benefit from the ChoiceStream offering; are the recommendations creating new revenue streams?

SJ: First, our clients can drive more demand for their products. For example, a common consumption pattern with entertainment retailers is fast and furious downloading of the first 20 or 30 titles before activity starts to wane off. Our engine learns about consumer interest during the first few interactions in order to keep feeding customers relevant ideas, focusing their experiences on the most relevant portions of a catalog or library. So, every time these customers get on the service, they see something compelling, which triggers them to buy or to add to their queue lists. Second, personalization creates a magnetic experience which keeps customers coming back; we could lengthen the lifetime of subscribers in subscription programs. At eMusic, for example, which is a music subscription service, they give us credit for more than doubling the average lifetime of a subscriber. Additionally, within each session, our clients sell more products because customers can more easily find the most relevant products.

TEP: What are some of the other ways that your clients use ChoiceStream?

SJ: Our customers also use this personalization platform for sending personalized e-mails or connecting people to other people. Using very refined preference profiles generated by ChoiceStream, customers can target advertising and place promotions to not just different audience segments and different market segments, but also to specific consumers. In other words, our engine helps create a more effective, higher-yielding advertising platform. A couple of our customers are starting to use ChoiceStream in their call centers; so when someone calls in, the call center agent can associate recommendations offered by our platform to the customer; which can be effectively used to up-sell and cross-sell.

TEP: How big is the addressable market?

SJ: We carve the opportunity into three markets: entertainment, general merchandise or multi channel retail, and advertising. Each of these markets is a multi-billion dollar opportunity and growing rapidly. We're very careful about staging our growth. To date, ChoiceStream has been very focused on entertainment. Last year, we launched with online retailer, Overstock.com and began to commercialize the retail platform in 2007. For the advertising market, we're in the development stage right now, and not ready to commercialize. However, we're engaged in many different trials with customers to get the solution right and find the best ways to use personalization data to do targeted advertising. We'll have our first commercialization of that next year.

TEP: What is your pricing model, and what's the typical deal size?

SJ: We license our platform on a recurring basis, and there's usually a variable component that's linked to usage. For a retailer, there's generally a revenue share component from the transactions that are generated by recommendations or personalization. For a subscription service, the licensing fees are tied to the number of subscribers. For an ad-supported site, we charge a cost per recommendation clicked. We also have a services component, because generally our customers like to have us involved in the design process. Our average deal size, keeping in mind that we are focused on major customers, is between \$250,000 to multi million dollars.



TEP: What is your sales model?

SJ: At the moment, we're purely direct sales, although we're talking to four or five OEM partners and we will be, I'm sure, making a couple of major announcements during the next few months.. We're also talking to some system integrators that want to use our best-of-breed components.

TEP: Who would you characterize as your top competitors? And where do you expect that competition could be headed over the next couple of years?

SJ: We are almost never in a situation where there are competing vendors. Historically, our main competitors have been internally developed approaches. Now, I think, even internal developments are starting to become less significant, so our main challenge is keeping up with demand. Now I can't say that that won't change. I think there are some companies who have been in the past strictly in the behavioral ad targeting space, who are just starting to market their approach as providing personalization. I think that there's a growing recognition that personalization is much more important now, given that there's really an overwhelming choice of content and product available to consumers. And I think this recognition is going to start attracting other players into the game. I think Google certainly has done a lot of work in contextual targeting of advertising. It wouldn't surprise me, if they started getting more and more into behavioral targeting of advertising, and then possibly into personalization.

TEP: Where do you see ChoiceStream in five years from now?

SJ: We're a public company five years from now. And we've got fully developed product lines in each of those three markets and probably more than 100 people.

TEP: Thank you Steve and best of luck!

