

Customer Relationship Management

CHAPTER 11

Questions

- What is customer relationship management?
- Why do retailers want to treat customers differently?
- What is customer lifetime value?
- How do retailers determine who their best customers are?
- How can retailers build customer loyalty?
- What can retailers do to increase their share of wallet?
- What can retailers do to alleviate the privacy concerns of their customers?

Customer Relationship Management (CRM)

- A business philosophy and set of strategies, programs, and systems that focus on identifying and building loyalty with a retailer's most valuable customers.

CRM

- All customers are not equally profitable, and more or less profitable customers need to be treated differently
- Retailers now concentrate on providing more value to their best customers using targeted promotions and services to increase their share of wallet – the percentage of the customers' purchases made from the retailer

Customer Loyalty

- Committed to purchasing merchandise and services from a retailer
- Resist efforts of competitors to attract the loyal customer
- Emotional attachment to retailer
 - Personal attention
 - Memorable positive experiences
 - Brand building communications programs

Can Offering Price Discounts Achieve Customer Loyalty?

No!

Retail strategies like these can be copied by competitors

These strategies encourage customers to be always looking for the best deal rather than developing a relationship with a retailer

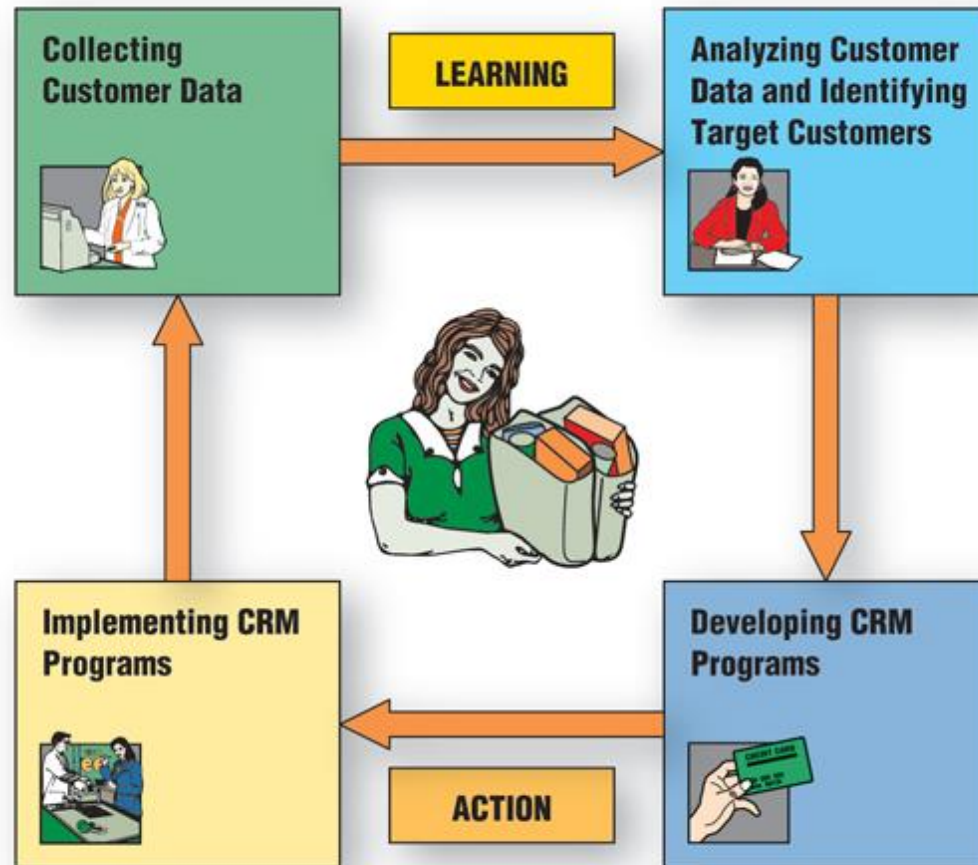


The CRM Process

CRM is an iterative process that turns customer data into customer loyalty through four activities:

1. Collecting customer data
2. Analyzing the customer data and identifying target customers
3. Developing CRM programs
4. Implementing CRM programs

CRM Process Cycle



Collecting Customer Data: Customer Database

- Transactions – a complete history of purchases
 - Purchase date, price paid, SKUs bought, whether or not the purchase was stimulated by a promotion
- Customer contacts by retailer (touch points) --visits to web site, inquires to call center, direct mail sent to customer
- Customer preferences
- Descriptive information about customer
 - Demographic and psychographic data
- Customer's responses to marketing activities

Collecting Customer Data: Identifying Information

Approaches that store-based retailers use:

- Asking for identifying information
 - Telephone number, name and address
- Offering frequent shopper cards
 - Loyalty programs that identify and provide rewards to customers who patronize a retailer
 - Private label credit card (that has the store's name on it)
- Connecting Internet purchasing data with the stores

Privacy Concerns

- Control over Collection
 - Do customers know what information is being collected?
 - Do customers feel they can decide upon the amount and type of information collected by retailers?
- Control over Use
 - Do customers know how the information will be used by the retailer?
 - Will the retailer share the information with third parties?

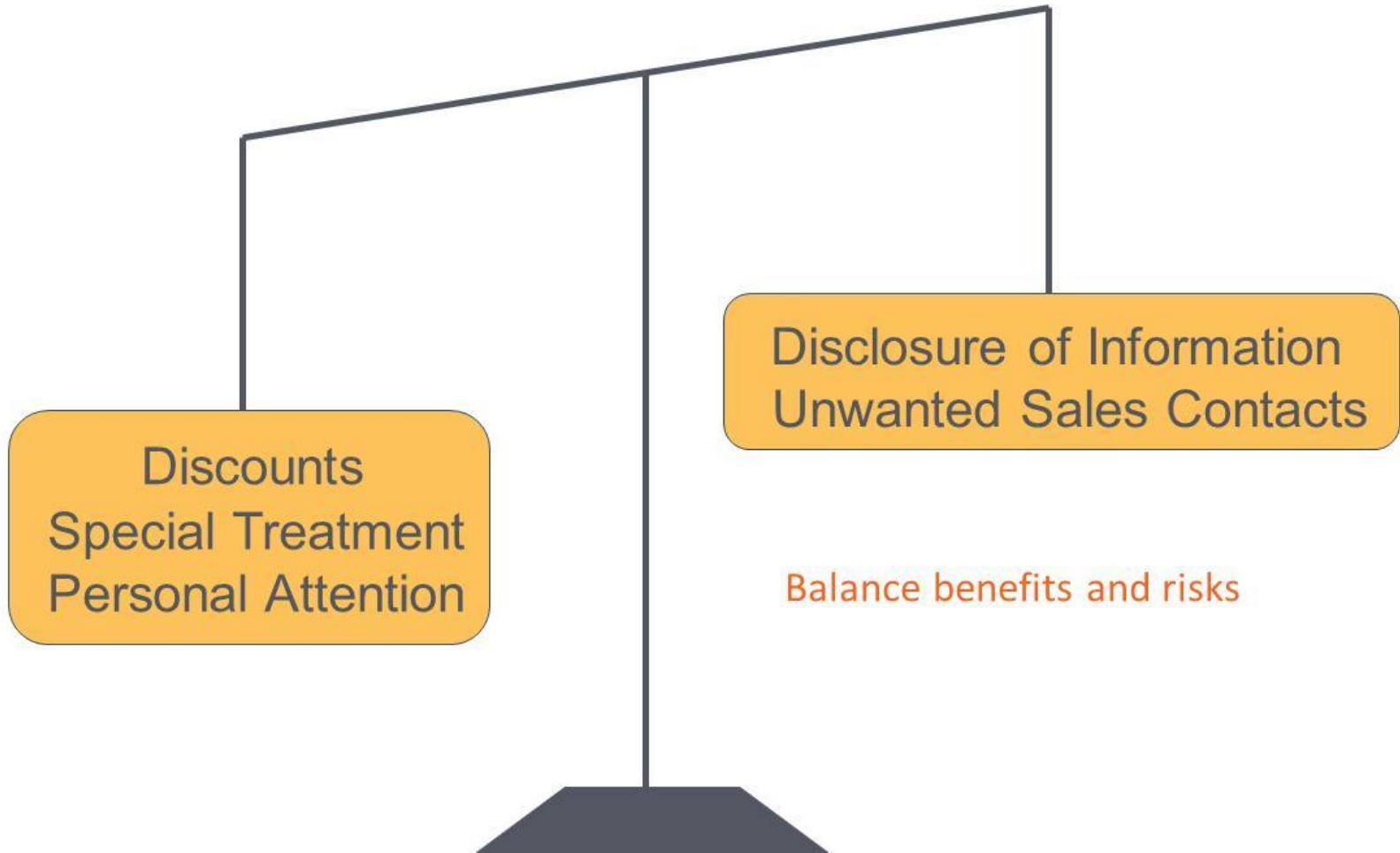


Heighten Privacy Concerns When Using Electronic Channel

- Information collected without the awareness of customers
- Collecting click stream data using cookies
 - Similar to an invisible person videotaping a customer as they walk through a store



Customer's Decision to Offer Information



Protecting Customer Privacy: Differences between U.S. and EU

United States

- Limited protection in specific areas
 - Credit reporting
 - Video rentals
 - Banking
 - Medical records
- Opt out: Consumers must explicitly tell retailers not to use their personal information

European Union

- Stringent consumer privacy laws
 - Information only can be collected for specific purposes
 - Purpose must be disclosed to customer
 - Information can only be used for specific purpose
 - Information cannot be exported to countries with less stringent regulations
- Opt in: Consumers own their personal information, and retailers must get consumers to explicitly agree to share this personal information

FTC Guideline for Fair Information Practices

- **Notice and awareness**
comprehensive statement about information storage, manipulation, and dissemination
- **Choice/consent**
Opt-in and opt-out options
- **Access/participation**
Customer able to confirm accuracy
- **Integrity/security**
Controls for theft and tampering
- **Enforcement/redress**
Mechanism to insure compliance



Analyzing Customer Data and Identifying Target Customers

Analyze the customer database and convert the data into information that will help retailers develop programs for building customer loyalty

Data Mining – technique used to identify patterns in data

- Market Basket Analysis
- Identifying Market Segments
- Identifying Best Customers



Market Basket Analysis

Data analysis focusing upon the composition of the customer's market basket – what items are bought during a single shopping occasion

Uses:

- Adjacencies for displaying merchandise
- Joint promotions
 - Bananas in the cereal aisle as well as in the produce section
 - Beer with baby dippers
 - Tissues with cold medicine



Market Basket Analysis Taught Wal-Mart to Change!

Product

Placed Near

Bananas	—————→	cornflakes, produce
Kleenex	—————→	paper goods, cold medicine
Measuring spoons	—————→	housewares, Crisco shortening
Flashlights	—————→	hardware, Halloween costumes
Little Debbie snack cakes	—————→	coffee
Bug spray	—————→	hunting gear

Identifying Best Customers

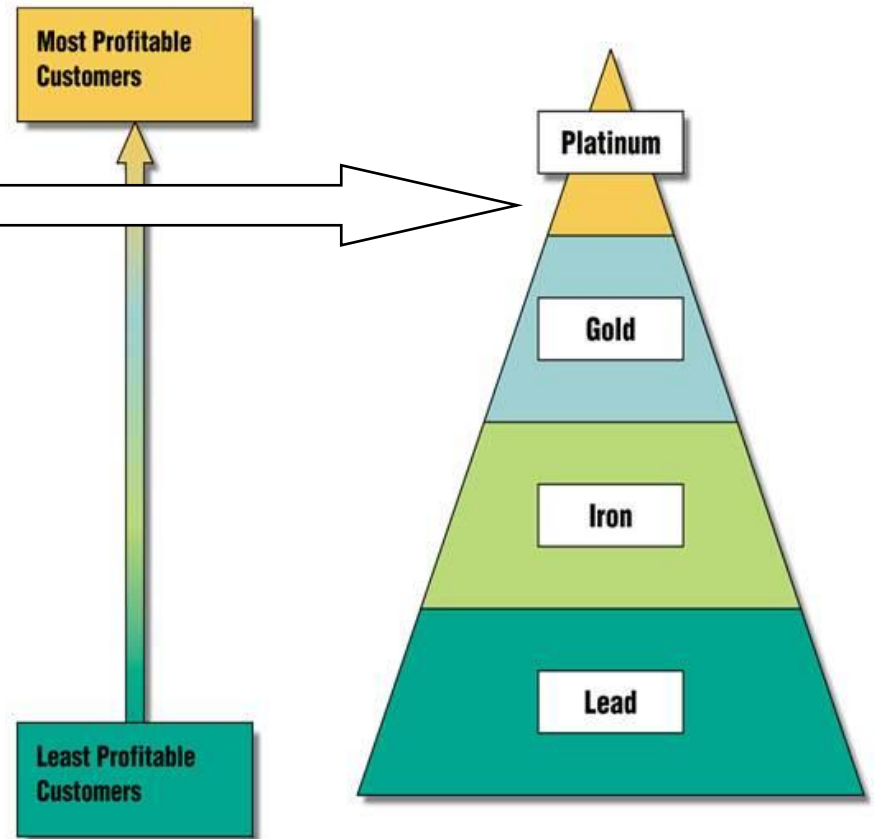
- Estimating Lifetime Value (LTV)
 - The expected contribution from the customer to the retailer's profits over his or her entire relationship with the retailer
- Use past behaviors to forecast future purchases, the gross margin from these purchases, and the costs associated with serving the customers
- Classifying Customers by recency, frequency, and monetary value of purchases ([RFM Analysis](#))



Customer Pyramid

Platinum
Best
Most loyal
Least price sensitive

80-20 rule:
80% of sales or profits come from
20% of the customers



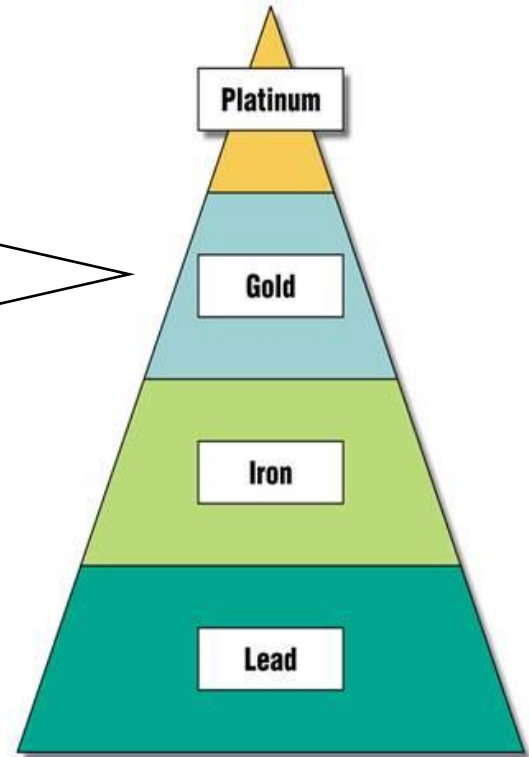
SOURCE: Valerie Zeithaml, Roland Rust, and Katherine Lemon, "The Customer Pyramid: Creating and Serving Profitable Customers," *California Management Review* 43 (Summer 2001), p. 125.

Customer Pyramid

Gold
Next best
Not as loyal

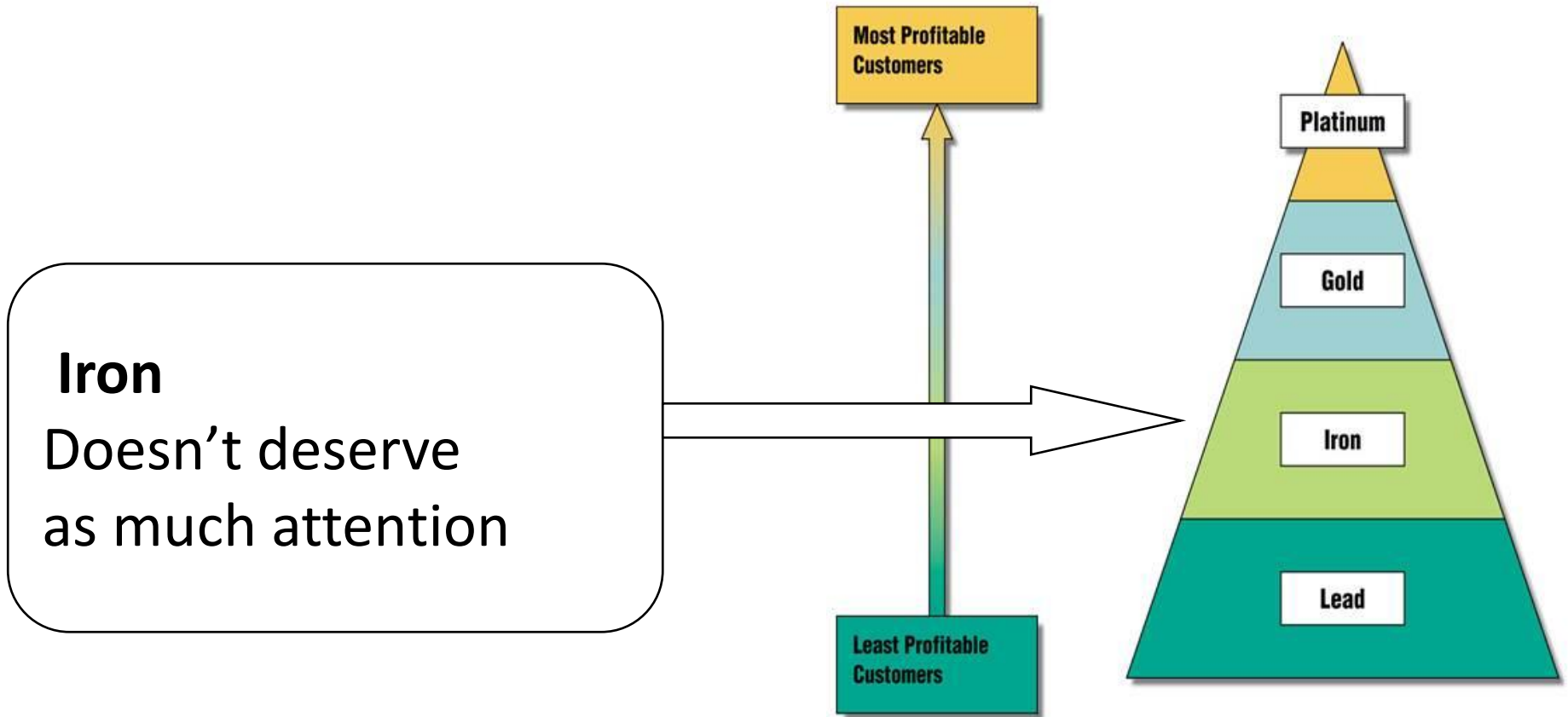
Most Profitable Customers

Least Profitable Customers



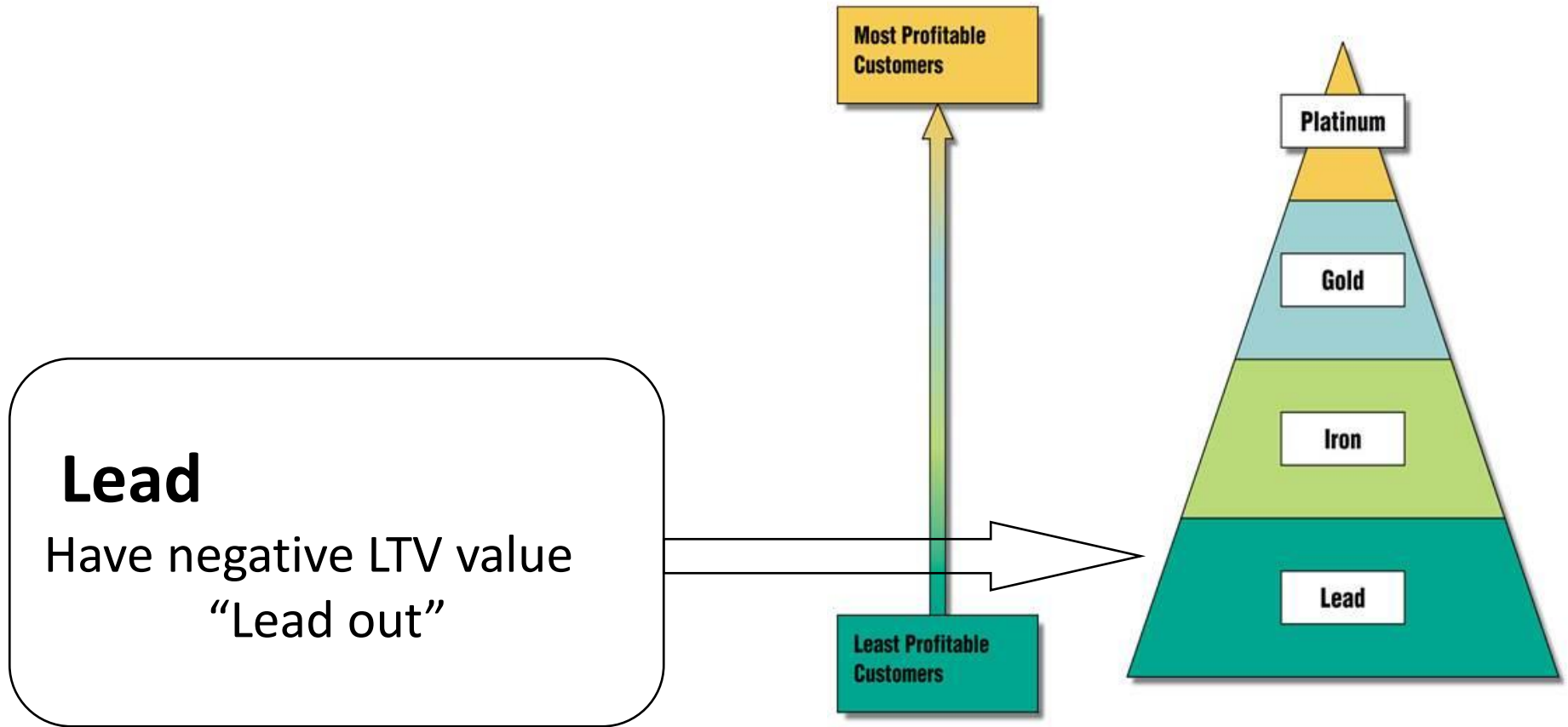
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RFM Analysis

Used by catalog retailers and direct marketers

Recency: how recently customers have made a purchase

Frequency: how frequently they make purchases

Monetary: how much they have bought

Frequency	Monetary	RECENCY			
		0-2 months	3-4 months	5-6 months	Over 6 months
1-2	<\$50	5.0%*	3.5%	1.0%	0.1%
1-2	Over \$50	5.0	3.6	1.1	0.1
3-4	<\$50	8.0	5.0	1.5	0.6
3-4	Over \$150	8.8	5.0	1.7	0.8
5-6	<\$300	10.0	6.0	2.5	1.0
5-6	Over \$300	12.0	8.0	2.7	1.2
Over 6	<\$450	15.0	10.0	3.5	1.8
Over 6	Over \$450	16.0	11.0	4.0	2.0

RFM Target Strategies

Frequency	Monetary	RECENCY			
		0–2 months	3–4 months	5–6 months	Over 6 months
1–2	<\$50	First-time customers		Low-value customers	
1–2	Over \$50				
3–4	<\$150	Early repeat customers		Defectors	
3–4	Over \$150				
5–6	<\$300	High-value customers		Core defectors	
5–6	Over \$300				
Over 6	<\$450				
Over 6	Over \$450				

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Illustration of RFM Application

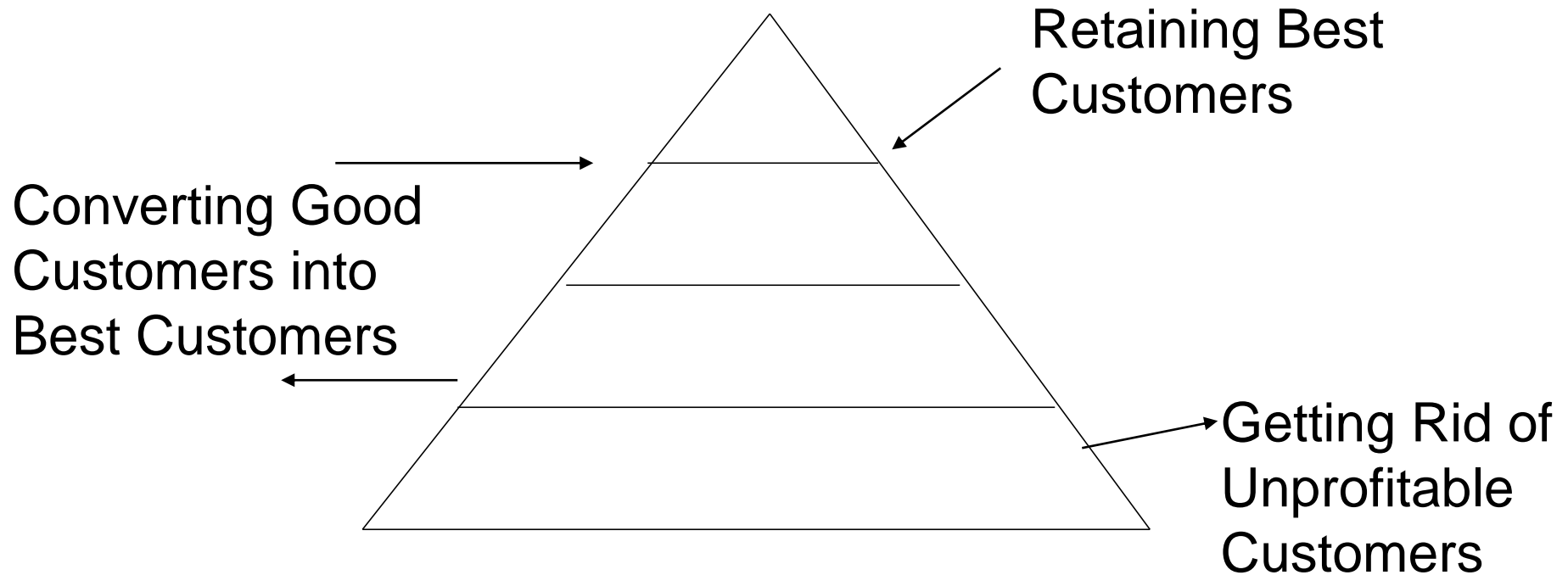
- A catalog retailer is deciding which group of customers to send a catalog. Based on experience and an RFM analysis of customer database:
 - Average order size for customers in cell - \$40
 - Contribution margin – 50%
 - Response rate – 5%
 - Cost of catalog and mailing -\$.75
- Will the retailer make a profit mailing to this RFM segment?

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$$\begin{aligned} & \$20.00 \text{ contribution} \times .05 \text{ response rate} - \$0.75 \text{ cost} \\ & = \$0.25 \text{ profit per catalog mailed} \end{aligned}$$

Developing CRM Programs



Customer Retention



- [Frequent Shopper Programs](#)
- Special Customer Services
- Personalization
 - [1-to1 Retailing](#)
- Community

Elements in Effective Frequent Shopper Programs

- Tiered rewards based on customer value
- Offer choices of rewards
 - No all customers value the same rewards
 - Non-monetary incentives, altruistic rewards
- Reward all transactions to ensure the collection of all customer transaction data and encourage repeat purchases
- Transparent and simple so that customers easily understand when they will receive rewards

Issues with Effective Frequent Shopper Programs

- Expense
- Difficulty in Making Changes
- Impact on Loyalty Questionable
- Easily Duplicated – Difficult to Gain Competitive Advantage
 - Need to offer “invisible” benefits



Personalization

The screenshot displays the Amazon.com homepage for user Keri Johnson. The top navigation bar includes the Amazon logo, a personalized greeting, and links for Today's Deals, Gifts & Wish Lists, and Gift Cards. A search bar is set to 'All Departments'. Below the navigation bar, a 'Keri, Welcome to Your Amazon.com' message is followed by a 'Today's Recommendations For You' section. This section features four items: 'Sent (Missing)' by Margaret Peterson Haddix, 'Books #1-4 + Cd (Bob Books...)' by Bobby Lynn Maslen, 'Scrabble Slam Cards', and 'These Days (Audio CD) ~ Bon Jovi'. To the right, a 'Tap into Your Friends' section encourages connecting to Facebook. Below the recommendations, a 'Coming Soon for You' section lists 'Mockingjay (The Final Book of...)' by Suzanne Collins, 'Camp Rock 2: The Final Jam (Audio CD) ~ Various Artists', 'Camp Rock 2: The Final Jam... DVD ~ Alyson Stoner', and 'Gold's Gym Dance Workout'. A 'See more recommended future releases' link is at the bottom left. On the right side, an 'Improve Your Recommendations' section shows 'Penn Court 1 Tennis Balls (Single Can)' with a rating and checkboxes for 'This was a gift' and 'Don't use for recommendations'. The page also includes a 'FREE Two-Day Shipping for College' banner and a 'Your Account | Help' link.

amazon.com Hello, Keri Johnson. We have [recommendations](#) for you. (Not Keri?)
Keri's Amazon.com | Today's Deals | Gifts & Wish Lists | Gift Cards | Your Account | Help

Shop All Departments Search All Departments GO Cart Wish List

Your Amazon.com Your Browsing History Recommended For You Rate These Items Improve Your Recommendations Your Profile Your Communities Learn More

Keri, Welcome to Your Amazon.com (If you're not Keri Johnson, click here.)

Today's Recommendations For You

Here's a daily sample of items recommended for you. Click here to [see all recommendations](#). Page 1 of 44

- Sent (Missing) (Hardcover) by Margaret Peterson Haddix
★★★★☆ (20) \$10.87
[Fix this recommendation](#)
- Books #1-4 + Cd (Bob Books...) (Hardcover) by Bobby Lynn Maslen
★★★★☆ (6) \$6.99
[Fix this recommendation](#)
- Scrabble Slam Cards
★★★★☆ (88) \$5.99
[Fix this recommendation](#)
- These Days (Audio CD) ~ Bon Jovi
★★★★☆ (65) \$11.68
[Fix this recommendation](#)

Tap into Your Friends

BETA

Connect to Facebook to get Amazon recommendations for you and discover your friends' Favorites and Likes.

[Learn more and Connect](#) (You can disconnect at any time)

Coming Soon for You

Page 1 of 3

- Mockingjay (The Final Book of...) (Hardcover) by Suzanne Collins
\$8.45
[Fix this recommendation](#)
- Camp Rock 2: The Final Jam (Audio CD) ~ Various Artists
\$11.99
[Fix this recommendation](#)
- Camp Rock 2: The Final Jam... DVD ~ Alyson Stoner
\$18.49
[Fix this recommendation](#)
- Gold's Gym Dance Workout
\$29.99
[Fix this recommendation](#)

[See more recommended future releases](#)

Improve Your Recommendations

Penn Court 1 Tennis Balls (Single Can)

Rate this item
x|★★★★☆

This was a gift
 Don't use for recommendations

Items you own (237)
Items you've rated (1)

Converting Good Customers into Best Customers

- Customer alchemy: converting iron and gold customers into platinum customers
- Add-on selling as a way to achieve customer alchemy
 - Involves offering and selling more products and services to existing customers and increasing the retailer's share of wallet with these customers
 - The Oprah Winfrey Show to sell books, movies, and TV specials (Harpo Productions), a cable channel (Oxygen Media), a Web site (<http://www.oprah.com>), magazine (O)

Shopping Buddy



Dealing with Unprofitable Customers

- Offer less costly approaches for dealing with these customers
- Charge customers for extra services demanded



Implementing CRM Programs

- More than CRM management, computer systems, and communication about the importance of customers.
- In addition.....
 - Close coordination between departments – Marketing, MIS, Operations, HR
- Shift in orientation
 - Product Centric
 - Customer Centric



Keywords

- **RFM (recency, frequency, monetary) analysis** Often used by catalog retailers and direct marketers, a scheme for segmenting customers on the basis of how recently they have made a purchase, how frequently they make purchases, and how much they have bought.
- **frequent-shopper program** A reward and communication program used by a retailer to encourage continued purchases from the retailer's best customers.
- **1-to-1 retailing** Developing retail programs for small groups or individual customers.

REFERENCES

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