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FOOD INDUSTRY MANAGEMENT

CORNELL UNIVERSITY

EB 2003-02
February 2003

Customer Relationship Marketing (CRM) in the U.S. Supermarket Industry: Current Status and Prospects

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Abstract

The supermarket industry has been developing customer relationship marketing (CRM) programs and strategies for over 15 years. At this point the impacts of CRM on the supermarket industry are mixed at best. Despite the potential to radically change the way supermarket business is conducted, there is also the possibility that CRM could be marginalized by supermarket companies as just another management fad.

This study employed a combination of literature review, retailer surveys, interviews with supermarket and manufacturer executives, and consumer focus groups to examine CRM in the U.S. supermarket industry. Our research focused on identifying the current status of CRM programs, on the role of CPGs in those programs, and the industry-specific issues constraining the realization of full CRM benefits. This report also presents an overview of the future direction of CRM theory with perspectives on the supermarket industry.

Despite over 15 years of development in the supermarket industry, and more than three-quarters of sales transacted with loyalty cards, and several hundred million dollars invested in technology and programs, customer loyalty has not been significantly increased because most consumers belong to multiple programs that offer mostly undifferentiated benefits. Even though the underlying premise of CRM is that loyal customers are less price sensitive, contributing to their potential higher profitability, the major benefit offered by retailers and perceived by consumers in frequent shopper programs is price discounts. While retailers surveyed reported very positive results from their CRM Programs (e.g. increased transactions, shopping frequency, transaction size, overall sales, gross margin, net profit, and return on marketing investment), some of these trends are counterintuitive, perhaps reflecting the misuse of price discounts and other tactics that undermine CRM's foundation.

Fast-paced lifestyles limit the appetite of most consumers for targeted marketing activities, generally, and, the efforts of supermarket and CPG companies, specifically, are perceived as intrusive for most consumers. The importance of customer service cannot be overemphasized in determining the success or failure of retailer CRM programs. All the technology and analytical skills in the world will not prevent poor customer service from driving customers to competitors. At the same time, the critical role of store employee turnover in the success or failure of customer service cannot be overemphasized. For most retailers, the customer service issue will not be resolved until employee turnover is controlled.

As manufacturers continue to scrutinize the efficiency of their trade spending and retailers increase their dependence on trade promotion dollars, CRM initiatives could be limited by the internal retailer tug of war over how trade funds will be spent. At the same time, manufacturers and retailers must work closely together to meet the needs of their shared customers. By sharing information, learning and resources, the seemingly divergent goals of building both store loyalty and brand loyalty perhaps can be met simultaneously.

While funding and technology are the most pervasive barriers to CRM realization, relieving those constraints will be meaningless if the cultural issues that plague most retailers are not resolved. Organizational and cultural issues will prevent the attraction and retention of sufficient people with the technical, analytical, and customer service skills needed at all levels of the organization to make CRM succeed. According to leading academics and business visionaries, the future of CRM involves a dramatic shift in the identification and valuation of assets. Given the similarities in the physical assets such as locations, stores, products, and services across most retailers today, visionary retailers will realize that assets that will give them competitive advantage in the future are their customer relationships or customer equity. Now is the time to begin transforming retail companies into customer-centric organizations driven by the realization that customers are the only truly valuable assets.

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Section A: Introduction

Background

"What's in a name? That which we call a rose
By any other word would smell as sweet."
—Romeo and Juliet, II:2, William Shakespeare

In this paper CRM will be used as the abbreviation for Customer Relationship Marketing. However, CRM is also shorthand for at least two other nearly synonymous phrases such as "customer relationship management" or "continuous retention marketing." However, the nomenclature does not end with phrases abbreviated by CRM. A partial list of other labels commonly used in industry and academic literature includes:

- customer driven marketing,
- customer equity management,
- customer-specific marketing,
- one-to-one marketing,
- loyalty marketing,
- lifetime-value management,
- customer intimacy,
- customer centric marketing, and
- customer asset management.

By any name, the concept is roughly the same: identifying, understanding, nurturing, and retaining best customers and to maximize the profit of each customer's purchases.

The concepts underlying CRM are as old as retailing itself. In fact, all the goals of CRM were common practices in food retailing over a century ago when local neighborhood grocers knew customers by name and understood, anticipated, and catered to their individual needs and tastes. As supermarkets replaced corner grocers across the U.S., that type of customer intimacy largely disappeared as individual stores attracted more customers than even the best store managers could track.

Recent advances in scanning data collection, storage, and analysis have created the foundation for CRM strategies. The need for retailers to differentiate and improve productivity in a saturated and intensely competitive environment has created the motivation for CRM.

The underlying premise for CRM is that loyal customers are more profitable over their lifetime than their less loyal counterparts. Given the competitive environment in the retail industry, attracting new customers is increasingly challenging and costly. Therefore, to increase sales and profits, retailers must understand customer wants and needs, deliver those things with good value, and, hopefully, engender the loyal patronage of their customers.

Studies indicate that as much as 80 percent of supermarket sales are derived from as few as 30 percent of customers. This disproportionate share of spending combined with issues of price sensitivity and cost to serve form the underpinnings for the argument that loyal customers are more profitable. Supposedly, loyal customers tend to be less price sensitive than their bargain-seeking counterparts who may shift stores to save money. This makes loyal customers more attractive from the revenue and margin perspectives. On the expense side, loyal customers are seen as less costly to serve since their loyalty reduces the need for advertising and promotion. Combined, CRM pundits claim these revenue and expense effects make loyal customers more profitable to retailers.

There is continuing debate about the link between CRM and the success of food retailers. Research indicates that many CRM projects have produced disappointing results, including cost overruns and minimal effect on profits and customer loyalty. Surveys of retail food companies indicate that most loyalty programs have primarily been used as electronic coupon and price discount vehicles, thus violating the basic tenets of CRM regarding loyal customers.

Market saturation, format sameness, and intense price competition leave customers with numerous choices and low switching costs. Retailers have traditionally responded with strategies that do not discriminate between loyal (profitable) and disloyal (less profitable) customers. In theory, CRM offers a strategy for managing customer assets in a more productive manner. However, key questions remain:

- **What constraints are preventing retailers from realizing full CRM benefits?**
- **What role may consumer packaged goods (CPG) marketers play in the success of retailer CRM programs?**
- **What types of relationships do consumers want from supermarket and CPGs?**

This study attempted to answer these questions and others.

Methodology

A variety of data collection methods were employed:

- A comprehensive literature review.
- A survey of grocery retailers throughout the U.S.
- Personal interviews with executives at leading U.S. supermarket companies and consumer packaged goods manufacturers.
- Consumer focus groups.

Literature Review

Literature reviewed included academic, trade, and general business journals, web sites, and books. Relevant areas included consumer behavior, loyalty marketing, and customer relationship marketing. Over 150 items were catalogued and key references are listed at the end of the report.

Retailer survey

Our survey was distributed to the top 100 retailers in the U.S. Responding were 25 U.S. supermarket companies accounting for aggregate annual sales of approximately $190 billion in 2001, about 48% of total U.S. supermarket sales (Table A-1). The responding companies operated 8,727 stores, about 27% of the over 32,000 U.S. supermarkets. The responding companies' headquarters were geographically dispersed across the U.S. and they collectively operate stores in all 50 states. The smallest respondent operated 25 supermarkets. The largest companies operated more than 1,000 supermarkets.

Thus, although this sample was not intended to be statistically random, it is quite representative of the supermarket industry both in terms of structure and geographical distribution.

Key executive interviews

A select group of retailer and manufacturer executives were interviewed either in person or via telephone to further explore issues raised in the retailer surveys and literature review. While the sample is unscientific, the insights add greatly to the understanding of trends and issues.

Consumer focus groups

Consumer focus groups were utilized to explore frequent shopper card behavior and attitudes. Two focus groups were conducted in each of two cities: Long Beach, CA and Syracuse, NY. These cities were selected because both market areas have had frequent shopper cards in use for several years.

In each city, one of the focus groups was limited to shoppers between 25 and 41 years old while the other focus group included shoppers who were 42 to 65 years old. Ethnic diversity was a key objective in the selection of candidates for all four groups. All candidates were active frequent shopper card users.

The focus groups were organized and conducted by Dan Baron of Consumer Insights, a California-based consumer information company. The sessions were conducted at professional focus group facilities and the research team observed from an adjacent viewing room.

Organization of this Report

This report is organized into 9 sections, labeled with the letters A through I. After this Introduction section, the research results are presented in the following sections:

- Section B: CRM status
- Section C: Frequent shopper programs

Table A-1. Comparison of Survey Respondents with Total U.S. Supermarket Industry and Top 20 Supermarket Companies, 2001

	U.S. Supermarket Industry	Top 20 Firms[1]	Cornell Study[2]	% U.S. Industry	% Top 20 Firms
Total Sales (bil.)	$398.2	$257.6	$190.0	48%	74%
Total Stores (#)	32,265	14,648	8,727	27%	60%
Sales/Store (mil.)	$12.3	$17.6	$21.7	176%	123%

[1] Progressive Grocer, 69th Annual Report of the Grocery Industry, April, 2002.
[2] Cornell Study, 2002.

- Section D: Operational impacts of CRM
- Section E: CRM constraints
- Section F: The role of CPG marketers
- Section G: The future
- Section H: Summary and strategic perspectives

Throughout the report additional perspectives are shared in sidebars accompanying the main text.

The final section (I) lists references. The Table of Contents lists all sections and subsections with page numbers. There is also a List of Tables and a List of Figures presented with page numbers for quick reference.

Section B: CRM Status

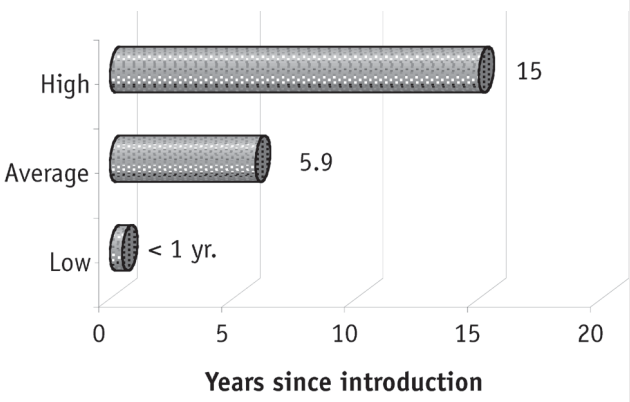
CRM Experience

Despite the logic of CRM, not all companies are pursuing CRM programs. Some companies have made a strategic decision to avoid heavy CRM involvement while others simply have not been able to actively pursue CRM strategies due to internal organizational issues.

At the time our survey was completed in the second quarter of 2002, twenty-two of the 25 responding companies (88%), were actively pursuing CRM (Figure B-1). The other 3 companies had no current plans to pursue CRM.

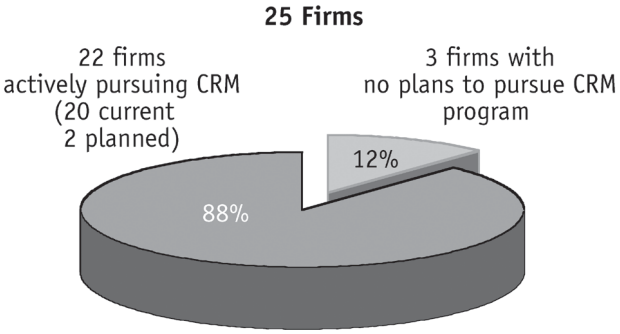
Of the 22 companies pursuing CRM, two were still in the planning and exploration stage but expected to launch their programs within 18 months. The other 20 companies were at various stages of actual CRM deployment, ranging from new launches to programs in existence for a decade or more.

Figure B-2. Years Since CRM Program Launch



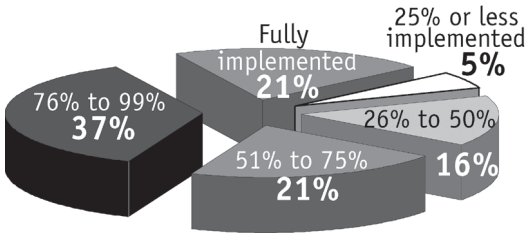
Source: Cornell Study, 2002.

Figure B-1. Extent of CRM Involvement, 2002



Source: Cornell Study, 2002.

Figure B-3. Degree of CRM Implementation



Source: Cornell Study, 2002.

The average length of time since inception of CRM activities was 5.9 years with a range of 15 years to less than 1 year (Figure B-2). Despite the relatively long average experience with CRM, only 20 percent of the companies reported that CRM was fully implemented. This may be indicative that CRM is an evolving strategy for retailers. Just over half (55%) of the companies said their CRM program was more than half but not completely deployed (Figure B-3).

Like any new technology or management process, the learning and experience of the early adopters typically helps later companies adopt it more quickly and effectively. Scanning technology is a great example of this phenomenon in the supermarket industry. The first scanning cash register systems were installed in 1974 but many benefits of the technology were not realized until more than 2 decades later with the development of sophisticated data mining and data warehouse systems. However, companies installing scanning systems today for the first time will realize all the technology's capabilities in a relatively short time, benefiting from the collective experience of those pioneering firms of the 1970s.

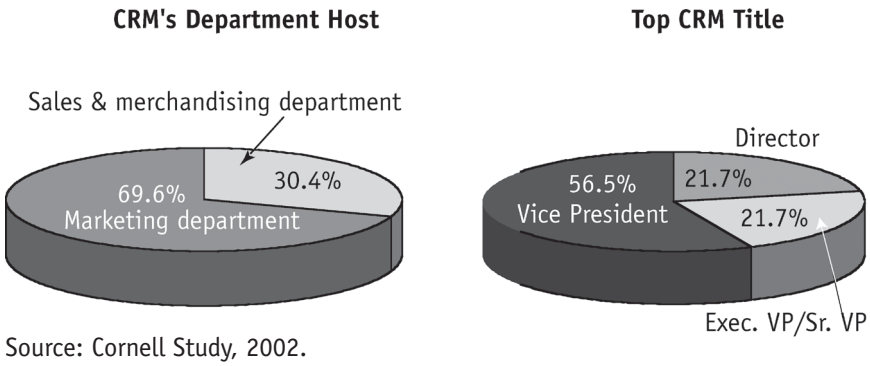
CRM in the retail organization

One of the challenges that many CRM executives cite as hampering full deployment is the cross-functional nature of CRM activity. In almost 74 percent of the companies, CRM is the responsibility of the senior marketing executive (Figure B-4). One company reported a title of Vice

President of CRM, a position that reports to the executive vice president of merchandising in that organization.

restaurants, and all retail channels are among the many industries trying to engender consumer loyalty.

Figure B-4. Where CRM Fits in the Retail Organization



Source: Cornell Study, 2002.

In terms of the corporate hierarchy, while most companies listed a vice president as the top CRM position, almost 22 percent indicated that "director" was the highest position responsible for CRM (Figure B-4). However, the same percentage listed a senior or executive vice president as the top position responsible for CRM. Three respondents also mentioned that the CEO, president, or COO had ultimate, if not direct, CRM responsibility, reflecting the type of top down organizational commitment that seems critical to CRM success.

Not surprisingly, funding for CRM is a somewhat contentious issue. In many organizations, CRM was envisioned as a replacement for traditional advertising and promotion activity. This has not happened in most cases, causing organizations to stretch budgets and seek new sources of funding. The majority of retailers reported CRM funding typically comes from the marketing budget. However, another contentious funding issue arises when CPG support for the retailer CRM program is elicited. Often the merchandisers feel that CPG funding for CRM programs reduces the trade promotion money typically allocated to merchandising activities. Retailers want CRM funding to represent additional dollars while CPGs often see the need for CRM money as a reallocation of their overall trade budget. Funding was the most common constraint mentioned by survey respondents and there is further discussion in Section E of this report beginning on page 30.

CRM role models

CRM is certainly not confined to the supermarket industry. In fact, most industries are faced with similar issues related to competition and loyalty to brands and companies. Banking, airlines, insurance, telecommunications,

When asked what other companies in any industry are outstanding at CRM, responses included a variety of types of businesses, specific non-grocery industry companies, and specific grocery industry companies. While the supermarket companies mentioned included no surprises, the listings for non-grocery industries and companies were worth noting and are listed in Table B-1.

Table B-1. Non-Grocery Industries and Companies Considered CRM Role Models by Survey Respondents

Industries	Companies	
•Airlines	•AAA	•Hallmark
•Banks	•Amazon.com	•Kohl's
•Casinos	•American Airlines	•The Limited
•Credit cards	•Best Buy	•Outback Steakhouse
•Doctors	•Blockbuster	•Saks
	•CVS	•Staples
	•Delta Airlines	•Valvoline Oil Change
	•Dick's Sporting Goods	

Examples of best-in-class CRM efforts in other industries include:

- Burger King Corporation has partnered with online auction site eBay for the first internet-based loyalty program in the fast food industry, called BKRewards (Sleep, 11/2001). The program rewards Burger King customers with points for certain purchases which are accumulated at a joint Burger King/eBay web site

where customers can use their points to bid on rewards. (Sleep, 11/2001).

- The casino gambling industry uses loyalty cards to track detailed information about guests during their stay at casinos. Each activity in the casino requires the patron to swipe a loyalty card, including non-gambling activities such as food purchases and guestroom preferences (Nash, 2001).

- McDonald's customers receive a code with each purchase that may be entered at road2rewards.com to receive points toward future McDonald's purchases or other merchandise. . Points are awarded based on spending levels and time of purchase and are redeemed on-line and rewards certificates are mailed within 4 weeks to the consumer's home. (www.mcdonalds.com, 9/2002)

Summary and perspectives

- The overwhelming majority of food retailers are pursuing CRM strategies but very few have fully deployed strategies in place.

- CRM is a cross-functional activity that is typically hosted in the marketing function of a retail food organization.

- Organizational friction often surrounds the issue of CRM funding, due at least in part to the fact that CRM strategies have not replaced traditional marketing programs as originally envisioned, thus forcing budget reallocation and/or retailers seeking new sources of funds from CPG companies.
- The reliance on CPG companies for funding of retail CRM programs is fueling a desire on the part of CPG companies to understand and measure the effect of CRM strategies.

And the winners are...

A 1to1 magazine poll asked CRM experts to identify the top loyalty marketing programs across industries. The group identified the following companies' programs:

- Hallmark Cards' "Gold Crown" program features a three-prong approach involving points accrual with rewards, a culture of service that treats members with special care, and a series of mailings depending on spending levels.

- American Airlines' "Your Someone Special" program is targeted at top business travelers, the airline's most profitable segment and rewards employees for serving these special members well. Members receive paper coupons with their account statements. If an employee provides exceptional service the member can write the employee's name on a coupon and hands it to the employee who then submits it to headquarters for points toward their own reward scheme.

- Stop & Shop Supermarkets' "Top Banana" program recognizes regular, highest tier spending customers with a special "Top Banana" sticker on their frequent shopper card. The sticker entitles them to free coffee and other special rewards but also recognition for their patronage, possibly creating an emotional bond between the customer and the store.

- The Vanguard Group's "Admiral Shares Program Special" entitles top customers, determined by either longevity or account balance, to special privileges and rewards. Members can transact their business on the Web and are charged one third less in account expenses for their loyalty.

- American Express' "Membership Rewards" allots one point per dollar spent with no limits on the number of points earned and no expiration date. Points are redeemable for a wide variety of items and Gold or Platinum members benefit from access to tickets Am Ex buys in blocks to major entertainment, theater, or sporting events.

- L.L. Bean's "L.L. Bean Visa" program features a no-annual-fee credit card that also features 6% back on L.L. Bean purchases and 3% back on purchases from other merchants. Additional benefits include free monogramming and free shipping.

- Lettuce Entertain You Enterprises' "The Frequent Diner Program" includes benefits at more than 60 different restaurants nationwide. Features include points for meals leading to discounts and free meals, invitations to special theme meals throughout the year, a free dinner course on the member's birthday, and individualized offers for pre-theater or post-shopping dinners.

(Paul, 2002).

Section C. Frequent Shopper Programs

A critical aspect of a CRM program is some type of customer identification system that allows purchases to be tracked at the household level. At the current stage of CRM adoption, most supermarket companies are relying on their shopper identification card program as the key component of their CRM efforts. The technology of shopper identification is expanding and evolving every day and these trends will be discussed later in this paper.

Customer identification

Shopper identification is an aspect of CRM that is also known by a variety of names. However, the most common shopper identification method is a plastic card or key chain tag with a magnetic strip, physically and functionally similar to a typical credit card. Commonly used names for shopper identification cards include:

- loyalty cards,
- frequent shopper cards,
- shopper cards,
- club cards,
- bonus cards,
- savings cards, etc.

For simplicity, this paper refers to these as frequent shopper cards.

While not absolutely required for CRM success, frequent shopper cards allow retailers to match purchasing behavior with a specific shopper or household. That matching is the cornerstone upon which most of the benefits of CRM are built.

Typically, frequent shopper card use is voluntary so customers who do not want to register for a card can opt out. In most cases, customers who sign up for a frequent shopper card do so with the understanding that they will receive benefits in exchange for allowing their purchases to be tracked. However, even customers who register for frequent shopper card programs typically have the option of opting out of receiving targeted promotions through mail, email or other media.

Ninety percent of responding companies with CRM programs offer frequent shopper card programs. Card program experience ranged from 15 years to less than 6 months since introduction.

Smart Cards

The vast majority of frequent shopper cards or key chain tags in use today are magnetic stripe cards, similar in functionality to a typical credit or debit card. Magnetic stripe card technology is not the only means to identify individuals or, in some cases, process payment for goods or services. The future is already here in terms of "smart cards" with a few prominent companies using this technology today.

Smart cards have a microchip memory device that can store information that can be accessed when the card is swiped at a kiosk, POS system, or other reader. The information stored on a smart card is instantaneously available, enabling cashiers, for example, to know something about the customer's preferences at the POS, perhaps enabling better customer service.

As a promotional tool the smart card memory could store the individual's product preferences or accumulated points for a sweepstakes. Upon swiping at a kiosk upon entering a supermarket, a variety of customized promotional offers, shopping lists, menu suggestions, or health information could be shared with the customer.

- Target has had a "smart" Visa card for several years. The cards contain a 64kb memory. Target has kiosks in stores that can read and write to the cards. Consumers will be able to download offers from their PCs or the kiosks to the card's chip to be redeemed at the POS (Garry, 7/2002)

- McDonald's restaurants in France are using smart cards to store targeted coupons on credit cards (Clark, 5/2001).

- Furr's Supermarkets is using a smart-loyalty card program in New Mexico to deliver electronic coupons to its customers based on the products each customer buys. As customers enter the store they swipe their card through an electronic smart card reader/encoder. After shopping, the customer again swipes the card at the checkout and the discounts are automatically deducted from the total purchase amount (Chain Store Age, 10/2000).

Consumer behavior and attitudes

A.C. Nielsen's 7th Annual Survey of Frequent Shopper Programs reported that participation in frequent shopper programs has doubled since 1996. In 2001, 78% of all U.S. households participated in at least one frequent shopper program, 63% belonged to 2 or more programs, and 10% registered for 4 or more programs (A.C. Nielsen, 2002).

While overall household penetration of frequent shopper programs is quite high, there is considerable debate about whether that translates into consumer loyalty, a key goal of CRM programs. The fact that most people belong to multiple programs raises concerns about the degree of loyalty card program membership engenders. In such competitive conditions, offering a loyalty card program can become simply a defensive measure to maintain parity with other retailers, as is often the case when double value manufacturer coupons are introduced in a market area. With all major retailers in a market area offering loyalty card programs, the competitive advantage and impact of the individual programs may be greatly diluted, especially if the programs are primarily utilized for electronic discounts. In this type of environment, those retailers with sophisticated frequent shopper programs that truly segment and reward loyal shoppers, will have an advantage.

One very clear outcome of the focus groups conducted for this project was that very few participants expressed any indications of store loyalty. In fact, the vast majority viewed frequent shopper cards simply as the current way to get price savings. The connection between using the card and receiving savings did not affect their preference for one store versus another since most people had multiple cards, one for each of the stores with programs in their trading area. Other related themes from our focus groups included the following:

- Most of the participants in our focus groups indicated they belong to multiple frequent shopper programs, continue to shop multiple stores by comparing specials and offers, and often find better prices at stores that do not offer frequent shopper programs.

- Not surprisingly, when asked to write down the positive aspects of using their frequent shopper cards, all of the participants listed price discounts as a major benefit. In fact, across all the positive aspects the participants listed, over 65% were variations on savings or discounts.

- Very few of our focus group participants expressed any interest in relationships with supermarkets or CPG manufacturers. The majority of participants saw such efforts as bothersome and costly, preferring that the money spent on direct mail, for example, be reflected instead in lower prices.

- In many cases, the relationship efforts of retailers and manufacturers were seen as disingenuous. A number of participants stated they consider postal or electronic mail overtures from retailers and manufacturers simply to be junk mail.

- At the same time, there was considerable sentiment among focus group participants that their loyalty to a supermarket was not recognized by the current benefits of frequent shopper programs because the price discounts are available to all cardholders, regardless of frequency, amount spent, or longevity.

- The general sentiment was that an additional incentive system should be in place to reward loyal customers and almost unanimously the incentive suggested involved some sort of sliding scale annual rebate based on spending levels, essentially another form of price discount.

- When asked if frequent shopper program membership had changed their shopping behavior, most people said they still shop essentially the same way, using the card for savings rather than clipping retailer inflyer coupons as required in the past.

- Of those whose behavior has changed since joining frequent shopper programs, several people indicated that they now stock up when there are buy-one-get-one offers and other special deals for cardholders. One person even purchased a freezer solely for stocking up purposes.

There have been several recent studies that cast doubt on the impact of frequent shopper programs on shopper loyalty. A study of 589 adults in the state of North Carolina found that shopper card usage did not have any positive affect on consumer loyalty to a particular grocery store. The results also indicated that those who use cards regularly are more active in external search behavior, exploring shopping opportunities at other stores as well. Further, the study found that using the card to take advantage of specific promotions did not relate to store loyalty. The author stated that "the very customers who are interested in a store's shopping bargains and deals are likely to abandon that store when there are better prices and deals to be had elsewhere" (Shaver, 2000).

In the United Kingdom, one consumer study conducted in 2000 found that just 16% of supermarket customers are influenced by loyalty programs and less than 33% spend more with a retailer after joining the retailer's loyalty pro-

gram (Marketing, 2000). Another U.K. study conducted in 2000 found that just 5% of consumers thought loyalty cards were a valuable service, compared with 22% for good customer service (CIES, 9/2002). A 2002 U.K. study (conducted by NOP and sponsored by Asda) found that 93% of respondents would prefer lower prices to loyalty cards (Retail Wire, 9/13/02).

In fact, two prominent U.K. supermarket companies, Safeway (UK) and Asda (now owned by Wal-mart) discontinued their loyalty card programs in recent years because they did not experience sufficient benefits to cover the program costs. When Safeway ended its program in 2000 it stated that it was able to put the $92 million per year it saved into weekly deep discount promotions that have proved very popular (CIES, 9/2002). Likewise, the Australian supermarket company Coles Myer has announced it will save $37.5 million a year when it discontinues its card program in 2004 (CIES 9/2002).

All demographic groups do not participate at the same rate in frequent shopper programs. For example, Hispanics are much less likely than non-Hispanics to join frequent shopper programs. In a separate study, A.C. Nielsen reported that just 52% of Hispanic households belong to a frequent shopper program. The rate for non-Hispanic households is 90% (A.C. Nielsen, 2002).

A.C. Nielsen reports that participation in frequent shopper programs varies with the degree of acculturation the household exhibits: the more acculturated the Hispanic household is, the more likely it is to participate in frequent shopper programs. The likelihood of multiple program memberships also increases as the household becomes more acculturated. For example, less acculturated Hispanic households participating are much more likely to belong to just one program (37%) than are their more acculturated counterparts (15%) (A.C. Nielsen, 2002).

The 51st State?

Even though most Canadians live within 200 miles of the northern U.S. border and the two countries have many shared interests and influences, there are distinct differences in supermarket shopping behavior and attitudes. For example, despite the many cultural similarities between the U.S. and Canada, frequent shopper program participation is markedly different between the two countries. Though 78% of U.S. households participate in frequent shopper programs, the rate for Canadian households is 93% (Table C-1). While 63% of U.S. households participate in 2 or more frequent shopper programs, the rate for Canadian households is 88%. Only 10% of U.S. consumers join 4 or more programs; 65% of their Canadian counterparts belong to 4 or more programs.

There is not only a difference in the participation rate between U.S. and Canadian consumer, their reasons for participation are also quite different. More than half (53%) of U.S. consumers cite discounts and savings as the primary reason for using their frequent shopper card while less than one quarter (24%) of Canadians are primarily motivated by the savings. The largest single reason (45%) why Canadians use their cards is the accompanying point accrual program.

Despite their higher loyalty card membership rate, however, Canadians seem to find less value in their memberships than their U.S. counterparts. In fact, while two-thirds (67%) of U.S. households feel that their frequent shopper program membership is valuable or very valuable, only just over one third (36%) of Canadians felt similarly about their own programs (Table I).

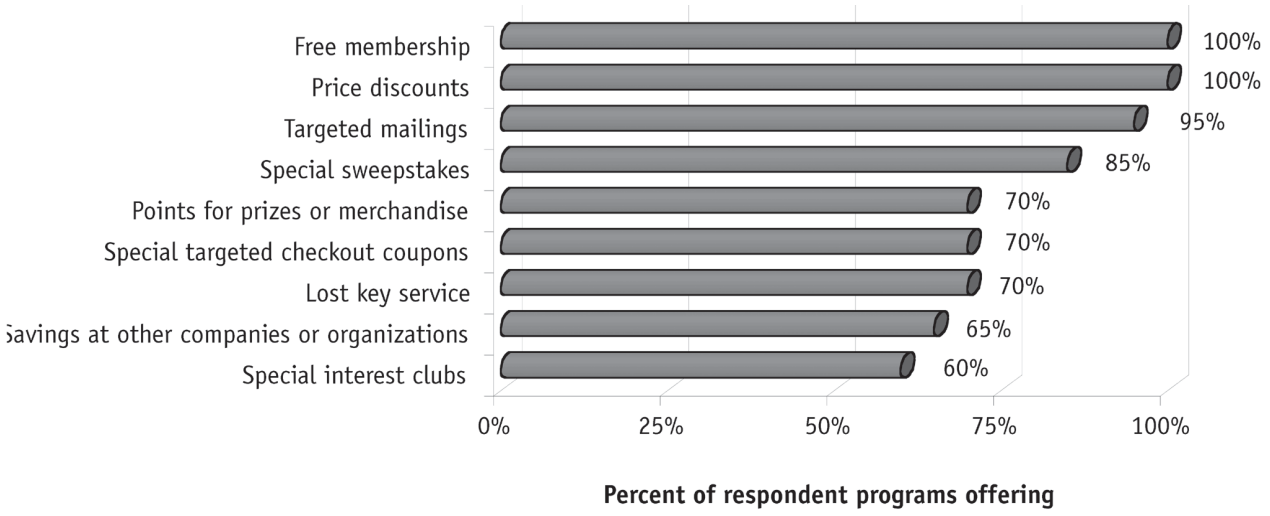
Table C-1. Comparison of U.S. and Canadian Frequent Shopper Program Participation, 2001

	U.S.	Canada
•Member of 1 or more frequent shopper programs	78%	93%
•Member of 2 or more	63%	88%
•Member of 4 or more	10%	65%
•Discounts/savings as main reason for using card	53%	24%
•Feel program is valuable or very valuable	67%	36%
•Program as one of top 3 reasons to shop at a particular store	42%	26%

Source: A. C. Nielsen's Sixth Annual Frequent Shopper Survey Study, 2002.

In the U.S. 42% of consumers listed frequent shopper programs as one of the top 3 reasons for shopping at a particular supermarket, the third most often mentioned reason after convenient location (70%) and store deals (55%). By contrast, Canadians listed five other reasons more often than frequent shopper programs. Only 26% of Canadians listed frequent shopper programs as one of the top 3 reasons for choosing a supermarket.

Figure C-1. Most Common Frequent Shopper Program Member Benefits



Source: Cornell Study, 2002.

Cardholder benefits

While enrollment is voluntary, card membership typically provides many benefits that make most people willing to provide the information required on the application form. To entice customers to participate in card programs, retailers offer a wide variety of benefits that enhance the value of the program.

Free membership

Anyone can join most supermarket frequent shopper programs and 100% of responding companies offer free membership (Figure C-1). The free membership offers a point of differentiation between supermarket programs and the wholesale membership club stores such as BJ's Wholesale Club, Costco and Sam's Club.

Price discounts

Price discounts are probably the most obvious benefit to consumers as most companies have gradually moved toward requiring the use of a card to receive most special prices. All the companies with card programs in the sample offer price discounts with card use (Figure C-1).

Research by the Roper organization in 2000 about frequent shopper programs across retail channels found that 65% of consumers surveyed said that receiving "a percentage discount on all purchases" is the feature that would "most likely" encourage them to participate. The result was 19 percentage points higher than the 46% of respondents surveyed in 1994 (Setlow, 3/25/02). In fact, the next five most likely features to encourage consumers to participate involved types of price discounts. These were advanced notice of upcoming sales (34%), special coupons for new products (31%), coupons or discounts on products and services from other vendors (31%), cash back offers (29%), and free gifts with purchase (21%) (Setlow, 3/25/02). Non-price inducements such as special events or parties (10%), personal shopping assistance (9%), member magazine (9%), or free baby-sitting (7%) were much less likely to encourage consumers to participate in a retailer frequent shopper program (Setlow, 3/25/02)

Price discounts appeal to most consumers because they are easy and provide instant rewards. From an operating cost perspective, price discounts are simple to administer and involve relatively simple accounting procedures.

Some of our focus group participants expressed concern that too few products are offered with cardholder savings. Another common sentiment was the suspicion that prices were raised on the non-discounted items to make up for the revenue lost on the discounted items. One person described his feeling about seeing the amount saved on his receipt as a "false sense of winning" because he felt he was probably paying higher prices for the non-discounted items.

Price discounts violate one of the basic tenets of CRM: that loyal customers are less price sensitive than less loyal customers and therefore will be more likely to pay full price. Discounts do not necessarily promote continuity since lower prices encourage stocking up that disrupts a consumer's normal shopping pattern. In the end, this strat-

egy accomplishes very little for the retailer since the ultimate goal of CRM is to encourage loyalty among customers using non-price incentives. If loyal customers are truly less price sensitive then offering discounts to loyal customers is preventing retailers from realizing the true profit potential of this market segment.

Targeted mailings

Ninety-five percent of respondents use targeted mailings in their frequent shopper program (Figure C-1). However, most companies allow members to opt out of receiving targeted mailings.

In its ultimate form, CRM could enable true one-to-one marketing in which each individual receives a specific message and offer that matches their specific tastes, wants, and needs. That utopian ideal, while technically possible today, is currently too expensive to attempt given the scale of retailer databases, cost of customization, and the staffing challenges most retailers face in technology positions.

As a realistic compromise, a first step employed by some companies is database segmentation to identify customer subsets to receive targeted messages. Segmenting allows retailers to send targeted messages to groups of customers who share common characteristics. Segmentation helps retailers identify groups of customers and provides a basis for rewarding "best" customers for their loyalty. Our survey revealed that 85 percent of retailers offer differential benefits for "best customers".

There are many potential bases for segmentation, depending on the retailer's objectives. Two basic segmentation premises are customer characteristics (demographics, location, etc.) and customer behaviors (spending level, shopping frequency, specific product or category purchase, etc.). The combination of any two or more of these bases results in nearly endless possibilities for segmenting target groups.

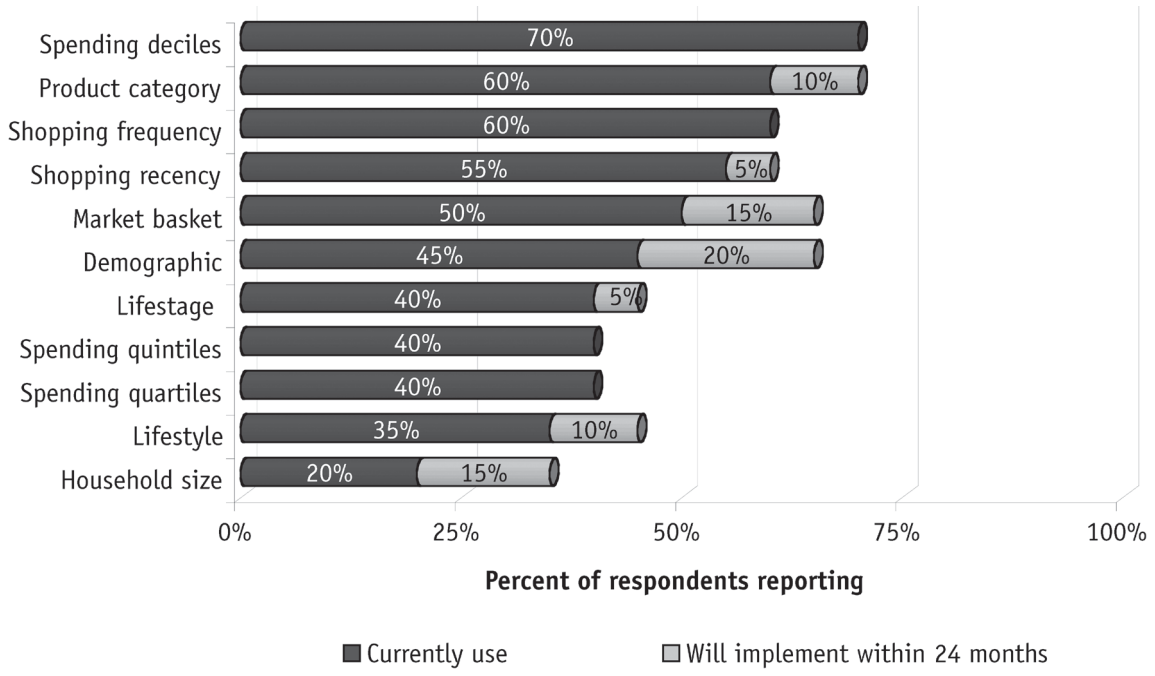
Spending level segmentation

Spending decile segmentation essentially ranks customers by average spending in the store and then divides the database into ten equal sized groups or deciles. The purpose is to identify "best" customers (those who spend the most) and "worst" customers, those spending the least

Our survey found spending decile segmentation to be the most common, with 70 percent of responding retailers already using this method (Figure C-2).

Other less common spending segmentation methods include spending quintile segmentation and spending quartile segmentation, both used 40% of responding companies (Figure C-2).

Figure C-2. Segmentation Methods Employed and Planned since CRM Launch



Source: Cornell Study, 2002.

One limitation of spending level segmentation is that the terms "best" and "worst" may be misleading since it is customer profitability that truly reflects the value of individual customers to the company. Simply focusing on high spending customers may cause retailers to overlook true "best" customers when measures such as profitability are considered.

Another limitation of spending level segmentation is that it might overlook many loyal customers whose life stage or situation prevents them from reaching the top deciles of total spending (Gustke, 2002). For example, empty nesters, singles, and many couples simply may not spend enough to rank in the top deciles. However, they may be very loyal shoppers, perhaps even spending as much as 100 percent of their grocery dollars at one store.

Product category segmentation

Product category segmentation was the second most common basis reported in our survey, with 60 percent segmenting customers by purchasing behavior relative to particular product categories (Figure C-2). Another 10 percent planned to use this method within 24 months. This behavioral type of segmentation is less concerned about whom the customer is than about what the customer buys. For example, a company might target pet food buyers with a specific offer from a pet food company, presuming that those who do not purchase pet food would not benefit from such an offer. The observed behavior is only what takes place at the company's stores. It could well be that some pet owners simply shop elsewhere for pet food and supplies while doing other shopping at the company's stores. In that case, scanning data would not reveal the opportunity for increased sales that this customer group represents.

Conversely, retailers may identify a group of people who do not purchase a particular product, product category, or department in order to send them a targeted offer to encourage them to make a trial purchase. For example, if only 65 percent of a store's customers purchase items from the in-store deli, the retailer may send a special offer to the 35 percent of customers who do not shop the deli. While there may be dietary reasons why some customers do not shop the deli, it may also be that they purchase deli products elsewhere or simply have not tried the in-store deli.

Shopping frequency segmentation

Another popular segmentation method is shopping frequency segmentation (60%), where the supermarket identifies and segments households according to how often they shop per week or month (Figure C-2).

There are Diamonds in Green Hills…

A pioneering retailer in the area of CRM is Green Hills Farms Market, a one-store operator in Syracuse, NY. Green Hills classifies its customers according to spending levels and treats the higher spending groups to a variety of special benefits that the lower spending groups do not enjoy.

The highest spending group, those spending at least $100 per week at Green Hills are labeled Diamonds. The next tier, those spending between $50 and $99 per week are called Rubies. Of the roughly 15,000 regular Green Hills customers, only about 300 qualify for Diamond status and about 1,000 earn Ruby status, less than 10 percent of the total customer base. The remaining 90-plus percent comprise lower tiers labeled Pearls and Opals (Greco, 6/2001).

Gary Hawkins, CEO of Green Hills Farms and a leading CRM consultant, measures customer shrink to judge his store's success at retaining loyal customers. Year after year, Green Hills retains more than 96 percent of its Diamond customers and over 80 percent overall (Greco, 6/2001).

However, high average sales alone do not necessarily lead to high profits. Hawkins also monitors average gross margin per customer tier and has consistently found the margin for top spending customers to be about 10 points higher than that of the bottom group.

Based on the combination of higher sales and gross margin, Green Hills pays much more attention to the upper tier shoppers and the results have been positive. Sales from the top tiers increased while sales from the lower tiers declined, with overall profit higher as well (Greco, 6/2001). Upon signing up for the program, card members receive $15 cash back for spending $100 or more and a personal tour of the store with a manager. Continuing to spend $100 per week entitles you to a free fresh turkey from a local turkey farm at Thanksgiving and a free Christmas tree, hand selected by the Hawkins family. Other perks include a $25 coupon for the garden shop in springtime and other special coupons throughout the year (Greco, 6/2001).

Shopping recency segmentation

Shopping recency segmentation simply segments customers by the length of time since their last visit to the store (Figure C-2). Supermarkets use this type of segmentation to encourage shoppers to return to the store after not shopping for a period of time. Over half (55%) of responding companies were already using this method and an additional 5 percent were planning to use this technique within 24 months. Recency segmentation is particularly useful to react to competitive store openings or other market environment changes such as road construction, store renovation, etc.

A commonly used segmentation combines recency, frequency, and monetary value. This method, often referred to in short hand as RFM, helps retailers identify and categorize active frequent customers according to spending levels.

Market basket segmentation

Market basket segmentation represents a higher degree of data analysis because it looks beyond total dollars spent to compare the contents of the shopping trip (i.e. the "market basket"). Given the greater number of variables tracked in this type of segmentation, the data storage and analysis needs are much greater than for the previously discussed methods. Fifty percent of respondents already used market basket segmentation and another 15 percent planned to use it (Figure C-2).

Understanding the composition of consumers' market baskets can provide insight into how the store is shopped, which products are complementary, and how the store might be better merchandised to drive sales of particular products and categories. Market basket analysis can also help "flesh out" the demographic profile of customers who otherwise are identified only by name and address in the database. For example, a market basket with disposable diapers, tofu, and cat food probably indicates the household has a pre-school child, at least eats a partial vegetarian diet, and owns a cat. While these presumptions may be incorrect on an individual household basis, when observed across the vast numbers of households in a typical supermarket's database, they can be very insightful.

Demographic segmentation

Almost half (45 percent) of responding companies used demographic segmentation to drive targeted marketing and another 20 percent planned to use this method within 24 months (Figure C-2). Demographic segmentation is based on customer characteristics such as age, ethnicity, income, geography, etc. While most retailer frequent shopper card application forms do not request sensitive information like income or age, data mining can infer some of these attributes with reasonable accuracy. Product purchase patterns combined with third party information about characteristics of buyers of various products can paint a fairly accurate picture of the consumer.

However, demographic attributes may not be as useful as other types of data at predicting consumer characteristics and shopping behavior. For example, recent research about consumer price sensitivity found that "shopping pattern variables, commonly available to retailers through means such as scannable "loyal shopper" cards, provide retailers with better information about household-level price sensitivity than, typically much more difficult to procure, household-level demographic data" (Kim, et al., 1999).

Life stage segmentation

Forty percent of respondents already used lifestage segmentation and another 5 percent were planning to use this method (Figure C-2). Life stage typically must be interpolated from the purchasing behavior of cardholders, as with demographics (see above).

Lifestyle segmentation

Over one third (35 percent) of respondents were using lifestyle segmentation, with an additional 10 percent planning to use it within 24 months (Figure C-2). Lifestyle segmentation typically utilized syndicated databases that infer lifestyle characteristics and purchasing tendencies based upon neighborhood characteristics. Combining this information with purchase behavior may confirm those assumptions. For example, ethnic neighborhoods might be roughly defined by certain streets. With this information confirmed by purchase pattern analysis of scanning data, retailers can target offers that interest those households specifically.

Household size segmentation

The least common, but fastest growing, method according to our survey was household size segmentation, with 20 percent of respondents already using and another 15 percent planning to use this method. Again, the limitations of card program application information prevent retailers from ascertaining this information directly. Therefore, it must be inferred via data mining based on purchase patterns and third party information (see above).

There are limitations to all of these segmentation methods individually that are not all overcome by combining two or more of the methods to fine tune the target groups. The biggest limitation is that these methods do not specifically identify customer groups by current or future profitability. Zeithaml, et al. (2001) empirically tested the

"80/20 rule," the observed phenomenon across industries that suggests that roughly 80 percent of profits (or sales) are generated by 20 percent of the firm's customers. Although they studied the banking industry, the findings are indicative of the importance of understanding customer profitability and the power of segmenting according to customer profitability. In fact, they found that the top 20 percent of customers in terms of profitability produced 82 percent of the bank's profits, confirming the "80-20 rule." More importantly, the study showed that the demographic profile of the top 20 percent were quite different from that of the bottom 20 percent of customers. The top 20 percent were more likely to be female, older, had higher income, had account balances almost 5 times as high, and were about 18 times as profitable as the customers in the bottom 20 percent of customers (Zeithaml et al., 2001).

Special sweepstakes

Another category of program benefits includes sweepstakes and contest- ninety percent of respondent card programs feature these benefits for customers (Figure C-1). Typically, these special sweepstakes offer significant prizes that a cardholder can win by shopping in a specified way over a specific time period. Typically, sweepstakes reward loyal shoppers because a shopper's chances of winning increase the more the person shops. Examples include:

- the monthly Kids' Club Express contest for items like mountain bikes at Clements' Market in Portsmouth, RI, (Cioletti, 2001) and
- Albertson's Preferred Savings Card introductory sweepstakes with a grand prize of $100,000 toward a new home purchase in the Dallas/Ft. Worth area (Albertson's, 11/2001).
- Kroger's Plus Card has run sweepstakes that enrolled shoppers upon purchase of certain products, such as those carrying the Good Housekeeping Seal, in a joint promotion with Good Housekeeping (Clark, 2/2000).

What's old is new again…

While none of the responding companies use third party point programs such as S&H Greenpoints or Gold Points in conjunction with their frequent shopper card, these programs offer a "turn key" solution that is especially attractive to smaller supermarket chains. Essentially these are an electronic version of the stamp programs that were very commonly used as continuity programs in the 1960s and '70s. The basic premise is the same: the more you spend, the more points you receive. The points can be redeemed for merchandise from a catalog or for in-store merchandise, creating loyalty to the store as well as the catalog merchandise.

- Carter's Food Centers, a 22-store chain that competes with Meijer, Wal-Mart, and other major chains in Michigan, introduced S&H greenpoints in 2001 (Progressive Grocer, 2002). The program's "turn key" nature, controllable cost aspect, and flexibility made it particularly attractive to a small chain like Carter's. Manufacturers can participate in the in-store item deals and Carter's knows the entire S&H program will cost around 1% of sales.

- Another small chain employing the S&H program is Tidyman's, based in Spokane, WA. Tidyman's announced in May 2002 that it was introducing the S&H greenpoints rewards program in its 22 stores in Idaho and Montana. Tidyman's shoppers receive 10 greenpoints per dollar spent and will earn bonus greenpoints on selected items throughout the store. Tidyman's shoppers can also earn greenpoints by shopping online at the S&H shopping portal (greenpoints.com) and can apply for an S&H greenpoints Visa card. To redeem greenpoints, shoppers can either use points toward merchandise in the S&H catalog or to receive free or discounted products at the checkout in-store (Supermarket News, 6/2002).

- PSK Supermarkets, operator of 11 Foodtown stores in the New York City metro area, has offered S&H greenpoints since 2000. By mid-2001, PSK had observed that about 60% of its shoppers redeemed their greenpoints for items in the S&H catalog while about 40% chose free merchandise from the supermarkets (Cioletti, 5/15/2001). PSK customers can also donate their greenpoints to charities such as the United Way or local schools.

Third party points programs make sense for larger companies as well. Lowes Foods, operator of 97 supermarkets in Virginia and North Carolina, introduce the S&H greenpoints program in July 2001 (Chain Store Age, 8/2001). A&P's Food Emporium Division announced in June 2002 that it was replacing its bonus savings club program with the Gold Points loyalty program in the fall of 2002 (Supermarket News, 6/2002). In addition to receiving Gold Points for purchases at Food Emporium stores, shoppers will also earn points for purchases at non-competing program partners including travel providers, restaurants, hotels, and other merchandise and services.

Point accrual programs

Various types of point accrual programs are featured in 70 percent of respondents' card programs (Figure C-1). These points can be accumulated on the basis of a stated number of points per dollar purchased. Various point thresholds correspond to redeemable merchandise or prizes. Point values can be manipulated at any time to encourage sales and to create excitement.

As mentioned earlier, according to A.C. Nielsen, Canadian consumers most often list point accrual programs (42%) as the primary reason for using frequent shopper cards (see Table C-1). Only 11% of U.S. consumers mentioned points programs among the top reasons for using frequent shopper cards.

The following are examples of some of the ways that retailers use point accrual programs to stimulate sales and maintain consumer interest:

- Superquinn, the leading supermarket operator in Ireland with a worldwide reputation for customer service, uses points in its frequent shopper program for a variety of reasons. For example, customers were offered triple points during the week before Easter if they would shop earlier in the week to help reduce overcrowding in the stores toward the end of the week (Turcsik, 2000). Superquinn cardholders also receive extra points for situations where customer service is not up to par such as a shopping cart with bad wheels, waiting too long in a checkout line, or not being offered a receipt by the cashier. These policies reinforce the importance of customer service for both customers and employees at Superquinn.
- In March 2002, Winn-Dixie Stores introduced its Customer Reward Card in its three Florida divisions. In addition to some typical card benefits the Winn-Dixie programs rewards cardholders with a point for each dollar spent. Accumulated points can be redeemed for special products. For example, cardholders accumulating 200 points during the 3 weeks prior to Easter/Passover could choose one of three rewards: a Hormel ham, a Butterball turkey breast, or a $10 Winn-Dixie gift card (Sleep, 3/2002).

Points programs have several advantages over non-point programs. Using points allows the retailer to de-emphasize price discounts, thus preserving margins while offering a loyalty mechanism. The consumer's perception of the value of points programs may be greater than the retailer's actual cost of the program. The cost of points programs can be estimated more accurately and even predetermined in the case of third party programs. Manipulating point values provides flexibility and versatility in rewarding consumers for special promotions. Point accumulation by nature involves consumers in an ongoing activity that provides continuity that straight price discounts do not engender.

Special targeted checkout coupons

Seventy percent of respondents offer special targeted electronic coupons at checkout based on cardholder purchases (Figure C-1). Smart cards may be the wave of the future in this area because of the smart card's memory can store information about the consumer's preferences. This information can trigger targeted offers when the smart card is swiped at an in-store kiosk or point-of-sale reader. For more details on smart cards see the box on page 7.

Up close and personal…

Biometrics is a term coined for a variety of technologies that use physical human attributes to verify the identification of individual people. The most commercially viable of these at this point is fingerprint scanning. Other technologies being developed in this arena are corneal scanning, face recognition, and voice recognition.

Thriftway Supermarkets in the state of Washington was one of the first supermarkets to experiment with fingerprint scanning technology in March, 2002 (Mulholland, 3/2002). At the time of this writing, the experiment was still ongoing but early consumer reactions were mostly positive and focused on the convenience of not needing to carry a shopper card or even a wallet.

Other supermarket companies that are experimenting with biometric technologies include Kroger and HE Butt. Outside the supermarket industry companies such as McDonald's, Blockbuster, and Walgreens are also exploring biometric technology applications (Supermarket Strategic Alert, 3/2002). Though there are many issues to resolve with most of these technologies, the potential for customer service combined with transaction cost savings, primarily through reduced credit card fees, is driving the rapid development and exploration of biometrics.

Lost key service

One challenge with card usage is that the card must be with the shopper and used at the time of the purchase to ensure that the data is captured and connected to that person or household. Thus, 70 percent of respondents' card programs offer lost key service as an added incentive to keep the card program's bar-coded tag on the key chain (Figure C-1). Most Americans carry their keys with them wherever they go. Credit card size frequent shopper cards are often left home or in the car when it's time for checking out. Some stores will ask for the shopper's phone number to ensure that the transaction data is tied correctly to the household. Unfortunately, when customers forget their cards, other relatively common practices include the cashier swiping a "house" card or asking the customer next in line to swipe their card. These practices create data integrity problems that are discussed in detail in Section E of this report beginning on page 30.

Benefits beyond the supermarket

Over two thirds of respondents' card programs feature additional savings opportunities at other businesses in the market area (Figure C-1). These non-competing businesses are eager to partner with the supermarket's card program for the additional advertising exposure and potential business. Opportunities for joint promotions and specials enhance the value for cardholders.

- When Albertson's introduced its Preferred Savings Card in November, 2001 in Dallas, cardholders also received substantial savings at a variety of hotel and rental car companies (Albertson's, 2001).

- Supervalu's Preferred Perks card program allows its independent operators to link with local businesses as well as national organizatoins. One Kentucky-based Supervalu retailer's Preferred Perks cardholders can take advantage of savings at a veterinary hospital, a tanning salon, a carpet cleaning service, a golf course, a jewelry store, an internet service provider, a music store, and a health club, among many other partners (www.supervalupaducah.com, 9/2002)

- Ukrop's Valued Customer Cardholders can enjoy savings at museums, ski areas, amusement parks, college basketball games, professional ice hockey, among many other special savings (www.ukrops.com, 9/2002).

Typically, supermarket companies may exchange advertising on shopping bags or similar in-kind activities for the value of the special offers other businesses provide to supermarket cardholders.

Special interest clubs

One CRM challenge for supermarkets is the relatively low level of personal involvement that characterizes consumers' general attitude toward supermarket shopping. Compared with other types of consumer goods such as clothing, electronics, automobiles, or travel, grocery shopping is often perceived as a routine, tedious, time-consuming chore. In order to establish and build customer relationships, supermarket companies try to focus efforts on products and categories that may engender emotional involvement, and loyalty, in consumers.

Pet products comprise a popular category for CRM attention. In addition to the pet category, responding companies identified 23 other specific product categories as having high potential for CRM. The most common of these were the baby products category, mentioned by 71 percent, the natural foods category (48%), pharmacy (43%), and wine and beer (33%) (Figure C-3).

Though mentioned less often, other high potential categories included ethnic foods, prepared foods, organic foods, and floral products.

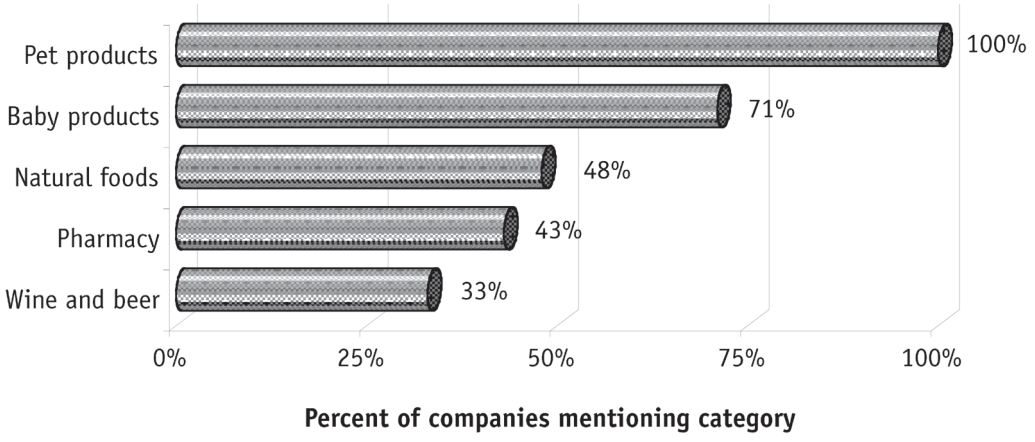
Retailers often offer special interest "clubs," which provide special benefits for purchases in these product categories or departments, etc. Baby products are often the focus of a special interest club. One example is the Baby Bonus Savings Club offered by A&P's Farmer Jack division in the Detroit region. An electronic marketing card automatically gives club members special prices when they buy baby items and tracks all club purchases. When a Farmer Jack customer accumulates a total of $200 of Baby Club purchases, the system alerts the cashier who gives the customer $20 in cash directly from the cash drawer (Cioletti, 2/2001).

Another approach to clubs is to address special interests or concerns such as gourmet foods or nutrition. Though none of the survey respondents offered a gourmet foods club, there was one company with a nutrition club.

A third premise for club formation in many supermarket companies is specific demographic groups such as seniors or kids. There are many examples of creative approaches to these two club themes. Here are a few examples:

- Clements' Markets, based in Portsmouth, Rhode Island has a program called Kid's Club Express which gives children a magnetic stripe identification card that they can swipe at a kiosk upon entering the store. Each day the child receives a different printout that may be a puzzle, a word scramble, a picture to color, or a coupon for a cookie from the bakery, etc. (Cioletti, 7/

Figure C-3. Top 5 Product Categories for CRM Activity



Source: Cornell Study, 2002.

2001). Each month Clements' runs a contest for which kids receive an instant entry form upon swiping their club card. The prizes are substantial items such as a mountain bike.

- In addition to the regular benefits other cardholders receive, members of Ralph's Senior Club also receive a $1 discount for every $10 they spend on Ralph's private label products (www.ralphs.com, 9/2002).

Check cashing

Check cashing is offered by 35 percent of respondents' card programs (Figure C-4). Although policies vary by company, many programs allow customers to write checks for more than the purchase amount to receive cash for the difference. Payroll and other types of third party checks often are covered by the check cashing features of card programs.

Double coupons

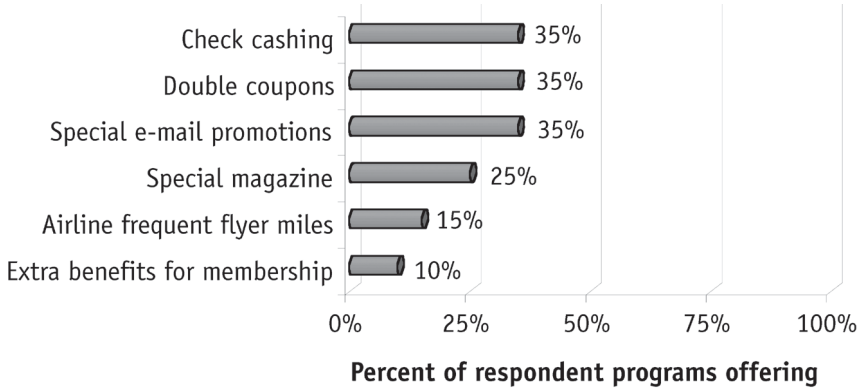
Only 35 percent offer cardholders double value on manufacturer coupons (Figure C-4. Retailers often adopt double coupon strategies as a defensive measure when a competitor initiates the practice. Some marketing areas have experienced double coupon activity by all major competitors for extended periods while the practice has been relatively rare in other market areas.

In some cases, intense competition has led to triple or more value offered for manufacturer coupons. Though most retailers realize that double coupon offers are very expensive and lose their promotional impact once all major competitors match the program, they often also feel they cannot afford to stop doubling coupon values for defensive reasons.

Special e-mail promotions

While special e-mail promotions were only offered by 35 percent of respondents, this technique is bound to increase in prevalence (Figure C-4). Many consumers are not yet able to receive e-mail but the penetration of Internet access continues to grow each year. The cost savings of e-mail make this a very efficient targeting method for retailers.

Figure C-4. Less Common Frequent Shopper Program Member Benefits



Source: Cornell Study, 2002.

Special magazine

One fifth of respondents' card programs include a special magazine for cardholders (Figure C-4). Retailers interviewed cited editorial content and cost as two major challenges in producing a magazine. Web-based magazines are no less challenging on the content side but may well have great advantages in terms of printing and delivery costs.

Airline frequent flyer miles

Some supermarket CRM programs feature partnerships with airline frequent flyer programs where mileage credit is accrued for every dollar spent at the supermarket. Only 3 of the card programs (15%), featured a link to an airline frequent flyer program where a specified number of frequent flyer miles are earned for each dollar spent in the supermarket (Figure C-4).

- An example can be found at Vons, where Club Card members receive 125 bonus miles in the United Airlines Mileage Plus program for every $250 of purchases made with their Vons' Club Card. (Not all purchases qualify.) (www.vons.com, 9/2002)

- For 6 years, Sainsbury, the second largest food retailer in the United Kingdom, had a relationship with British Airways in which Sainsbury shoppers accumulated points for in-store purchases which they could convert to "Air Miles" which could be used to buy flights on British Airways. However, in December 2001, British Airways informed Sainsbury that the contract would not be renewed. In January 2002, British Airways announced it was rewarding a more lucrative contract to Tesco, the largest UK supermarket company and Sainsbury's largest competitor (Sleep, 1/2002). Losing the British Airways contract was a major setback for Sainsbury's CRM program. The company reported a 1 percent decline in sales in the quarter following the end of the British Airways relationship (CIES, September 2002). In September 2002, Sainsbury has launched a new card program in conjunction with three major non-competing companies: BP, an oil company; Debenham's, a department store chain; and Barclaycard, a credit card company.

Extra benefits for membership fee

Although all the respondents' card programs offer free membership, two programs (10%) also offer an enhanced benefit package for an annual membership fee (Figure C-4). The notion of fee based memberships for an enhanced benefit package is not new. The wholesale club industry has always required businesses and consumers to pay annual membership fees to shop in their stores. Sam's Club and Costco have both introduced an opt-in $100 annual fee program featuring additional benefits that their basic membership fee does not offer, such as percentage rebates and roadside assistance (Raphel, 10/2001).

Other card program benefits

Other cardholder benefits mentioned included discount certificates for various spending levels, topical in-store seminars, in-store culinary classes, free donuts, and charitable donations based on shopping behavior.

Cardholders can support charities or schools through card use by electing to have a portion of their price savings designated for donation. This option has proven popular with consumers since their savings help the community. The feature allows the store to get involved in community fund raising and be recognized for their efforts by their own customers.

Table C-2. CRM Technologies Employed by Survey Respondents

	Currently in Use	Planned Used[1]	Projected Total[2]
Web site	85%	5%	90%
Electronic coupons	85%	5%	90%
Electronic kiosks	20%	10%	30%
Wireless devices	5%	15%	20%

[1] Percent of respondents who expect to deploy each technology within 24 months.
[2] Sum of percent currently in use and percent planned use.

Source: Cornell Study, 2002.

Table C-3. Frequency of CRM-Related Features in Supermarket Web Sites, with Feature's Rank in Top 24 Features

Send informational e-mailings (#8)	37%
On-line coupons (#9)	36%
Send promotional e-mailings (#10)	34%
Loyalty card information (#11)	32%
Full home shopping (#22)	10%
Local cross-promotions (#23)	7%

Source: Supermarket News, (July 1, 2002).

CRM technologies

In addition to frequent shopper cards, retailers utilize other technologies to enhance their relationships with customers.

Web sites and e-commerce

Eighty-five percent of responding companies had a web site and almost 65 percent reported an increase in web site traffic since CRM was adopted (Table C-2).

Seventy percent of respondents offered electronic savings at their web site through programs such as Value Page and Upons. Half the respondents participated in the Upromise college savings program and featured information and registration forms on-line. Upromise is an automatic college savings program that allows consumers to take advantage of the federal tax-free savings accounts though purchases made in the supermarkets and additionally for certain products and services both in supermarkets and beyond (www.upromise.com, 9/2002). A predetermined percentage of the purchase amount is automatically deposited in the customer's college savings account.

Only 35 percent of respondents were involved in direct on-line retailing, but over 70 percent of those reported increased on-line sales since CRM began. To put our survey respondents in perspective in this regard, FMI (2002) research found that almost 42 percent of supermarket companies offered on-line shopping.

A Supermarket News survey of supermarket company top 24 web site features found that the most common feature was company history (63% of the sites) (Supermarket News, 7/2002). However, CRM related features were much less common (Table C-3).

Many experts feel that supermarket companies with multichannel strategies that employ traditional store retailing with on-line retailing and perhaps catalog retailing will be best prepared to provide for the needs of today's and tomorrow's convenience-driven, time-conscious consumers (Lintner, 2002). Lintner cites research by the Boston Consulting Group in which customers shopping all three channels generate up to 9 times the sales as customers who shop only one of the channels.

Electronic coupons

Although not a recent development, electronic coupons continue to be popular. With 85 percent of respondents using some form and another 5 percent planning to do so, electronic coupons are becoming standard features for today's supermarket (Table C-2).

Electronic kiosks

In-store electronic kiosks were being used by 20% of respondents and another 10 percent planned to use them (Table C-2). These kiosks can be used for a wide range of services such as customer information, new product introductions, electronic coupons, customized shopping lists, customer-specific promotions, surveys, nutrition and menu planning, etc.

For over a decade, electronic kiosks have been used in stores for a variety of purposes from deli ordering to store directory assistance, with varying degrees of success. However, the latest kiosks feature card readers that allow targeted information to specific customers.

Some retailers have seen higher redemption rates on kiosk delivered coupons than for those delivered by targeted direct mail, at a much lower delivery cost as well. Kiosks have also been effectively used to encourage non-purchasers of particular products to make a trial purchase of that item when a given a coupon via the kiosk (Blank, 2000).

Wireless Devices

Wireless devices, used by 5% of respondents, facilitate customer shopping with customized lists, offers, nutritional information, store directory, etc. With another 15 percent planning to utilize wireless devices within 2 years, this is the fastest growing CRM technology. As this technology matures and applications are better developed more and more companies will adopt these devices because of their flexibility and efficiency.

The whole area of radio frequency identification (or RFID), a prime driver in the development of wireless devices, is rapidly evolving with better, smaller, cheaper RFID chips.

- The wireless identification and payment system called SpeedPass is being extended beyond its ExxonMobil fuel and convenience store base with companies such as Stop & Shop supermarkets experimenting with the technology (Convenience Store News, 7, 2002). The SpeedPass itself is becoming even more convenient as ExxonMobil and McDonald's are experimenting with a version of the technology that is embedded in Timex watches (Supermarket Strategic Alert, 4/2002).

- W.H. Smith, the UK-based bookstore chain, is using hand-held scanners to reduce lines at peak checkout times. Store staff use the devices to scan the items of customers waiting to checkout, the customer is given a receipt, and then pays for the purchase at the cashier station. In the test period, the company mea-

sured a 50% reduction in transaction time and a 14% increase in sales (CIES, 7/2002).

- One experiment currently under way with a group of 30 unrelated retailers in New York City uses wireless communication to send messages to cell phones and personal digital assistants (PDAs) to shoppers in stores and passing by on the sidewalk outside the store (CIES, 5/2002). The system sends messages continuously so passersby will also receive messages after stores are closed (CIES, 5/2002).

Smart shopping carts

Although not addressed in our survey, an emerging technology is a shopping cart that is computerized and receives and sends radio frequency signals. These smart shopping carts will not only provide targeted promotional messages to customers as they shop but will also transmit shopping behavior data to the company database. This technology will collect information about total time spent in the store, time spent waiting to check out, aisles shopped, time spent in departments, and other shopping pattern data that will give retailers unprecedented insight into consumers' in-store behavior. This information may help retailers design better stores, merchandise more effectively, schedule labor, etc.

Automated teller machines (ATMs)

Another technology not specifically addressed in our survey is the automated teller machine (ATM). Most consumers have long accepted the familiar ATM as a convenient means to conduct personal banking. However, a new generation of ATMs connected to the Internet is broadening the range of convenience applications for these ubiquitous machines (Supermarket Strategic Alert, 4/2002). Essentially, everything that can be done on the web could be done on these internet-linked ATMs.

- According to Supermarket Strategic Alert, "A well-publicized test is 7-Eleven's pilot, which allows check cashing and money transfers, targeted at those households without bank accounts and Web-junkies who are on the move" (Supermarket Strategic Alert, 4/2002).

Summary and perspectives

- Frequent shopper programs, which are the centerpiece of most CRM strategies, are now a ubiquitous part of the retail landscape. This, when combined with the fact that many frequent shopper programs have not evolved beyond vehicles for the widespread delivery of price discounts, has resulted in consumer attitudes and behaviors which are inconsistent with the underlying program goals of customer segmentation and loyalty creation.

- Frequent shopper programs may not increase customer loyalty because most consumers belong to multiple programs.

- Consumer attitudes seem to indicate that frequent shopper programs may not be living up to their early promise, when they were foreseen as being efficient, consumer-oriented replacements for traditional, mass-oriented print circular advertising.

- While many retailers have incorporated more targeted benefits in their frequent shopper programs (targeted mailings, clubs, point accrual systems), it is still price discounts that receive the most retailer and consumer attention.

- Consumer appetite for one-to-one relationships with supermarkets and CPG marketers seems very limited.

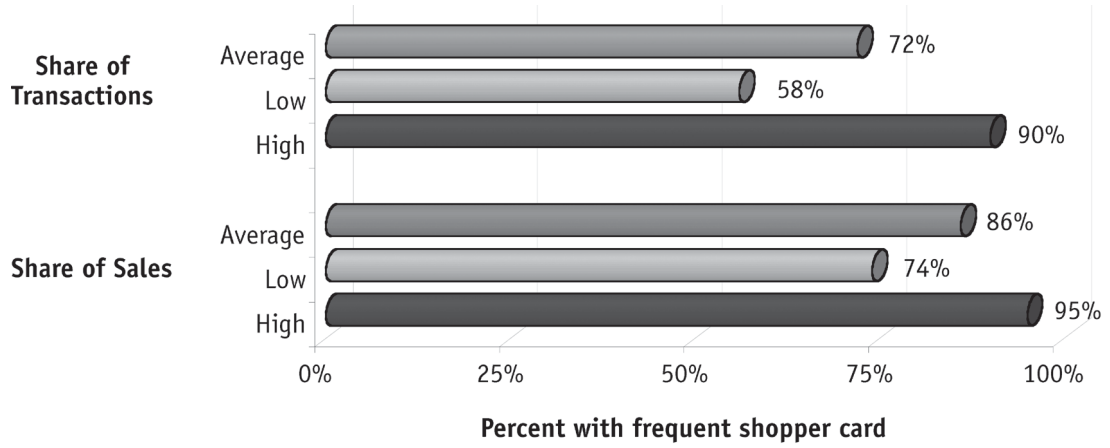
- The opportunity may exist for a retailer to break out from the reliance on price discounts and return to the basic tenants of CRM—creating customer-specific tactics that engender loyalty over the long term.

Customer transactions and sales

On average at responding companies, frequent shopper cards were used in almost 73 percent of transactions that accounted for an average of 86 percent of sales (Figure D-1). The share of transactions ranged from a low of 58% (by 2 companies) to a high of 90 percent. Sales share for frequent shopper card transactions ranged from 74 percent to 95 percent.

As expected, the companies with less than fully implemented CRM programs report lower average capture rates. It is noteworthy, however that all three groups averaged above 80 percent of sales captured with frequent shopper cards (Figure D-2). This discrepancy (i.e. similar sales capture rates but much different transaction capture rates) could be an indication that CRM's later adopters learned from the experiences of early adopters by limiting fre-

Figure D-1. Average Share of Customer Transactions Using Frequent Shopper Card, with Low and High Values

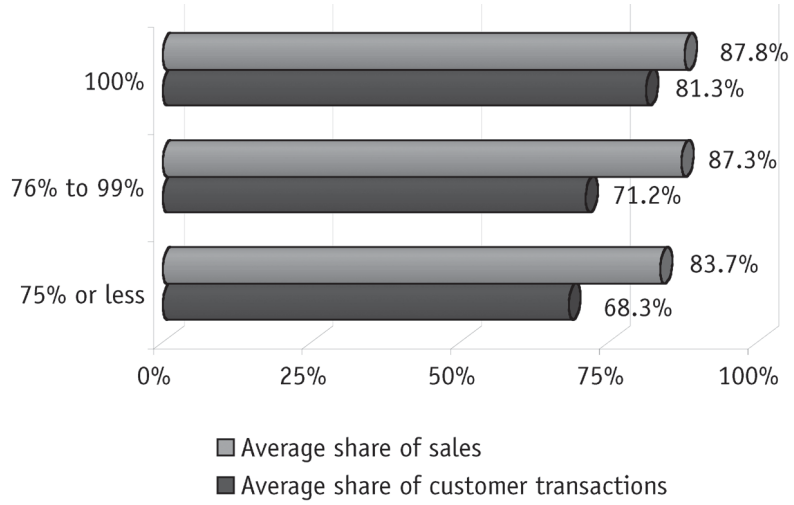


Source: Cornell Study, 2002.

Interpolating from these average percentages, sales per transaction is 138% higher (i.e. almost 2.4 times as large) with card use than for transactions without cards. There are at least two explanations for this discrepancy. First, it is probable that non-card users spend much less than card users and second, card users may not bother using the card for small, fill-in purchases.

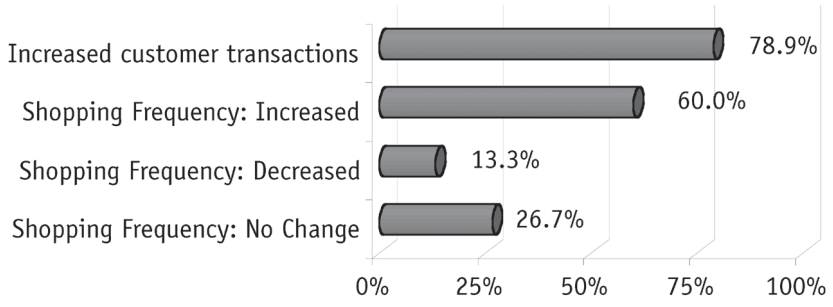
One indication of consumer acceptance of frequent shopper cards is how the share of sales and transactions varies by degree of CRM program implementation. On average, companies reporting complete CRM program implementation captured 87.8 percent of sales and 81.3 percent of transactions through frequent shopper card use (Figure D-2).

Figure D-2. Average Share of Customer Transactions and Sales Using Frequent Shopper Card, by Degree of CRM Implementation



Source: Cornell Study, 2002.

Figure D-3. Changes in Shopping Behavior since CRM Launch: Number of Customer Transactions and Shopping Frequency



Source: Cornell Study, 2002.

quent shopper benefits to higher spending customers. It could also be that the higher spending customers are the quickest to register since they have the most to gain from the program's price savings.

One potential outcome of CRM is that customer transactions (and perhaps total sales) might decrease as a result of focusing attention on more profitable customers and, thereby, discouraging less profitable customers from shopping the store. That is, the company might have fewer but more profitable transactions by discouraging the "cherry pickers" who purchase primarily on-sale items and on whom the retailer loses money. However, in our survey, almost 79 percent of retailers reported more customer transactions (Figure D-3) and 94 percent reported higher total sales (Figure D-4) since implementing CRM. This may simply be one indication of the futility of using frequent shopper programs primarily as price discount vehicles. Since everyone is eligible for a frequent shopper card and the price discounts it provides, no matter how profitable or loyal they are to the store, price discounts do not reward loyalty. There was similar sentiment expressed in our focus groups: many loyal shoppers did not feel like that frequent shopper programs sufficiently recognize their loyalty, since, in most cases, every cardholder received the same benefits.

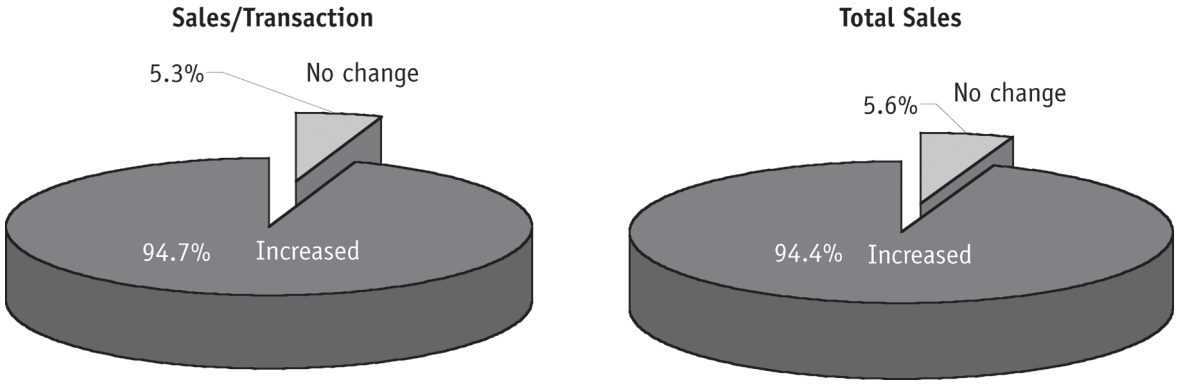
A more logical finding is that 95 percent reported higher sales per transaction (Figure D-4) since focusing on higher spending, more profitable customers would tend to increase average transaction size. A less intuitive result is that 60 percent reported increased average shopping frequency per customer. Perhaps this is an indication of success in encouraging individuals to use the card on every transaction, not just major shopping trips, though doing so would seem to lower sales per transaction, contrary to the increase reported above (Figure D-3).

Shopper conversion

Many retailers use spending level segmentation to divide their customer database into deciles based on total spending, ranked from highest to lowest. The top decile therefore represents the top 10% of customers in terms of average weekly sales per household.

One CRM tactic is to focus efforts on the top spending customers and limit promotional activity with the lowest spending customers. Another tactic is to try to increase the spending of middle decile shoppers so that they reach the levels of the high decile groups. *Shopper conversion* is the rate at which retailers are able to move shoppers from one spending level to a consistently higher level, thus becoming more "loyal" shoppers.

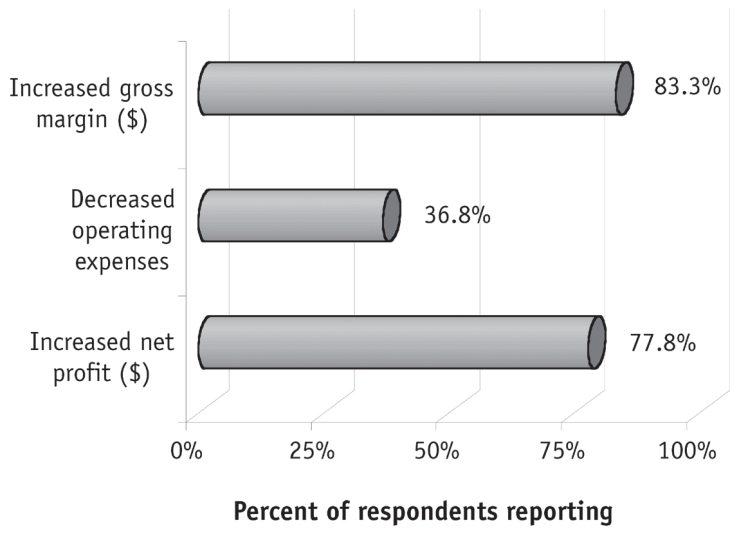
Figure D-4. Changes in Sales per Transaction and Total Sale since CRM Launch



Source: Cornell Study, 2002.

Almost 63% of responding companies reported increased shopper conversion, meaning that a greater share of their customer base is now comprised of loyal shoppers than prior to CRM implementation (Figure D-5). Over 94 percent of respondents reported that the sales share of their top 10% of customers has increased under CRM and almost 53 percent reported a decline in the sales share of the bottom 10% of their customers (Figure D-5).

Figure D-5. Changes in Gross Margin, Operating Expenses and Net Profit since CRM Launch



Source: Cornell Study, 2002.

Profitability

One of the major challenges facing all retailers is how to maintain or improve profitability in saturated, price-driven markets. Our survey found that about 83 percent of respondents experienced increased gross margin dollars and almost 78 percent have seen increased net profit dollars while only about 37 percent reported lower operating expenses since CRM began (Figure D-6). Since the majority of respondents reporting higher profitability apparently did not achieve those results through expense control, their higher margins might have resulted from fewer markdowns on advertised items, by perhaps discouraging "cherry pickers". Given the price competition that characterizes most market areas as competition intensifies from other supermarkets and companies like Wal-Mart, Costco, and Save-A-Lot, this finding seems improbable. However, a relatively common complaint from our consumer focus groups was that there were many items that never featured cardholder savings.

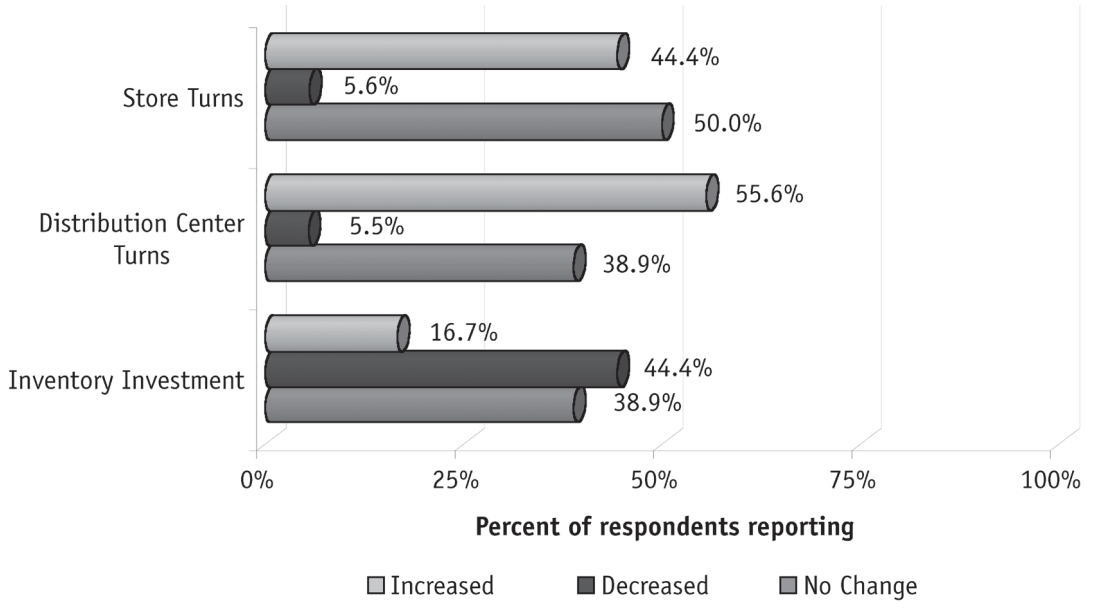
Return on marketing investment (ROMI)

One advantage of the CRM approach is the higher degree of measurability of targeted marketing that is enabled by the combination of scanning and frequent shopper cards. A ratio called Return on Marketing Investment (ROMI) is the industry's current measurement of advertising and promotion effectiveness. As the name implies, ROMI is sim-

There are Diamonds in Green Hills…

A pioneering retailer in the area of CRM is Green Hills Farms Market, a one-store operator in Syracuse, NY. Green Hills classifies its customers according to spending levels and treats the higher spending groups to a variety of special benefits that the lower spending groups do not enjoy. The highest spending group, those spending at least $100 per week at Green Hills are labeled Diamonds. The next tier, those spending between $50 and $99 per week are called Rubies. Of the roughly 15,000 regular Green Hills customers, only about 300 qualify for Diamond status and about 1,000 earn Ruby status, less than 10 percent of the total customer base. The remaining 90-plus percent comprise lower tiers labeled Pearls and Opals (Greco, 6/2001). Gary Hawkins, CEO of Green Hills Farms and a leading CRM consultant, measures customer shrink to judge his store's success at retaining loyal customers. Year after year, Green Hills retains more than 96 percent of its Diamond customers and over 80 percent overall (Greco, 6/2001). However, high average sales alone do not necessarily lead to high profits. Hawkins also monitors average gross margin per customer tier and has consistently found the margin for top spending customers to be about 10 points higher than that of the bottom group. Based on the combination of higher sales and gross margin, Green Hills pays much more attention to the upper tier shoppers and the results have been positive. Sales from the top tiers increased while sales from the lower tiers declined, with overall profit higher as well (Greco, 6/2001). Upon signing up for the program, card members receive $15 cash back for spending $100 or more and a personal tour of the store with a manager. Continuing to spend $100 per week entitles you to a free fresh turkey from a local turkey farm at Thanksgiving and a free Christmas tree, hand selected by the Hawkins family. Other perks include a $25 coupon for the garden shop in springtime and other special coupons throughout the year (Greco, 6/2001).

Figure D-6. Changes in Inventory Turnover for Stores and Distribution Centers and Overall Inventory Investment since CRM Launch



Source: Cornell Study, 2002.

ply the net profits generated from a marketing activity divided by the cost of that activity. While simple in theory, actually capturing the information components required for accurate measurement of ROMI can be a challenge for most companies. In fact, some retail executives interviewed for this study reported that accurately capturing the total cost of CRM initiatives is challenging because activity-based costing methods are not widespread.

Our survey found that over 87 percent of respondents reported increased ROMI since implementing CRM (Figure D-7). This finding is somewhat surprising since most studies report that companies in many industries have been disappointed in the results of their CRM programs. The 2001 Arthur Andersen Survey of Retail Information Technology reported that 52.5 percent of the retailers who are actively mining their databases said that data mining made no contribution to their bottom line (Chain Store Age, 10/2001). Other surveys published in 2001 found similar disappointing results across industries: Insight Technologies reported that 31% of companies implementing CRM reported no return on investment and Gartner Group reported that 51% of CRM projects generated no positive returns within three years (Journal of Business Strategy, 2001). A related finding by the Gartner Group survey was that a majority of businesses underestimate the costs of CRM programs by between 45% and 75% (Journal of Business Strategy, 2001).

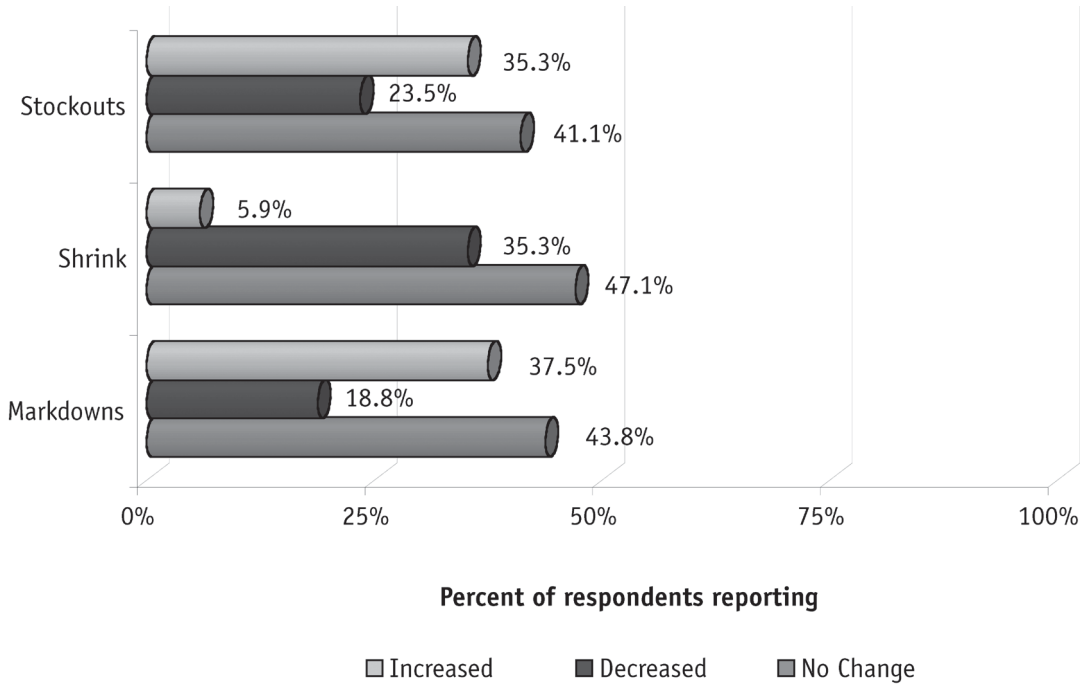
However, data mining capabilities are being enhanced by the rapid evolution and refinement of predictive software that can increase the return on targeted marketing investment by identifying shoppers most likely to respond to various offers (Mulholland, 3/2002). Retailers have reported redemption rates up to 3 times normal targeted mailing responses based on the fine tuning of targeted offers using predictive software (Mulholland, 3/2002).

Advertising and promotion

Like many new management practices, CRM represents a significant change in the way supermarkets have traditionally gone to market. This is very apparent in advertising and promotion tactics. In CRM theory, most of a supermarket's advertising and promotion budget would be shifted to CRM activities, maintaining enough traditional advertising for image and brand building, but no longer for sales promotion. This vision has not been realized on a broad scale partly because short-term pressures in competitive markets have forced CRM to stand along side traditional advertising. As a result, retailers have looked to CPG marketers to fund CRM initiatives more heavily than originally anticipated.

This has put pressure on retailer relationships with CPGs because retailers do not want manufacturers to reduce traditional trade promotion spending in order to fund CRM activities. Retailers would like additional or "new" CPG funding for CRM, while most CPGs see one pool of money

Figure D-7. Changes in Stockouts, Shrink, and Markdowns since CRM Launch



Source: Cornell Study, 2002.

that will be reallocated between CRM activities and traditional trade promotion. Likewise, this has strained relations within retail organizations between merchandising and CRM staffs. One retail executive described CRM as being "parallel" to merchandising, and the latter would rather get lower prices from CPGs than funding for CRM initiatives, thus putting the two retail groups in direct competition for CPG trade dollars.

This common scenario presents a challenge for CPGs whose trade spending has been declining over the past few years as a percent of sales (Heller, 2002; Supermarket Strategic Alert, 2002). According to the ACNielsen Trade Promotion Practices Study, total manufacturer trade promotion spending fell to 11% of manufacturer sales in the year 2000, the lowest level since the organization began tracking trade spending. Across broad product groups, the decline in trade spending was even more pronounced in nonfoods and general merchandise (9% of sales in 2000, down from 17%) and health and beauty care (5% in 2000, down from 10%).

One reason for the decline is that only 37% of manufacturers felt they were getting good or excellent value from trade promotion spending (Heller, 2002). While overall trade spending was down, manufacturer spending for retailer CRM program participation and for pay for performance promotions both increased. Reducing overall trade spending allowed manufacturers to shift more dollars to consumer ads and promotions. Clearly, manufacturers are attempting to optimize their own advertising and promotion spending by focusing on activities that help build brand equity and increase brand sales.

Ideally, CRM involves individualized, or at least targeted, messages delivered directly to individual customers or households. However, traditional supermarket advertising and promotion strategies have deployed mass oriented communication vehicles simply because the technology did not exist to identify individuals or homogeneous groups of customers. These strategies and vehicles are inefficient in terms of their ability to reach and appeal to specific customers. The early 20th century quote below from the founder of Wanamaker's Department Stores captures the futility that most retailers have always felt in analyzing advertising spending.

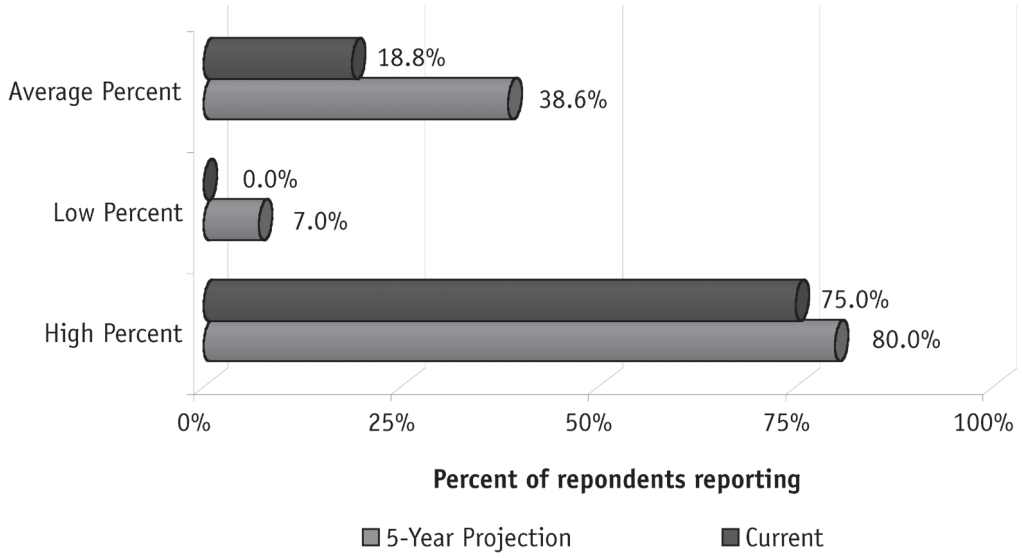
"I know that half of my advertising dollars are wasted.
I just don't know which half"
- John Wanamaker

Even the most progressive CRM practitioners have struggled with the correct balance between traditional advertising

and promotion spending for "the masses" and spending for targeted CRM initiatives. Given these trends, retailers are challenged to allocate their own advertising and promotion dollars effectively to drive CRM programs (Veiders, 2001). Perhaps reflecting these issues, over half the retailers responding to our survey reported increased overall advertising and promotion expense since introducing CRM. Further, CRM's average share of current advertising and promotion budgets is just under 19 percent (Figure D-8). The range of current allocations is from zero to 75 percent.

Despite the fact that these companies reported their CRM programs to be fully implemented, they also anticipate some growth in the allocation of advertising to CRM (Table D-1). Companies with the least developed CRM programs predicted average advertising allocations in 5 years of about the same magnitude as those companies with fully deployed programs, 34.4 % vs. 36% (Table D-1). Companies with more than three-quarters of their CRM program implemented predicted a much higher advertising allocation for CRM in 5 years, 46.4%. These predictions may offer a sense of the long-run allocation of advertising spending

Figure D-8. CRM's Share of Advertising and Promotion Budget, Current Actual and 5-Year Projection



Source: Cornell Study, 2002.

On average, respondents expect that CRM's share of advertising and promotion budgets in 5 years will be over 38 percent, more than doubling today's allocation. The estimated allocation in 5 years ranges from 7 percent to 80 percent of total advertising and promotion dollars (Figure D-8).

Looking at advertising allocation by degree of CRM implementation shows that the average allocation for companies with fully implemented CRM programs (33.5%) is almost 3 times the allocation for companies with the least developed programs (12.4%) (Table D-1). It is noteworthy that companies reporting fully implemented CRM programs are only allocating about a third of their advertising spending to CRM. This seems to indicate that, in the companies' concepts of "full" CRM programs, CRM is not the dominant marketing strategy.

for CRM, a percentage somewhere in the mid-30s to mid-40s. If that is the case, then retailers are predicting that CRM will not reach its full potential of replacing most spending on traditional advertising.

Table D-1. CRM's Share of Advertising Expense, Current and 5-Year Projections, by Degree of CRM Implementation

Degree of CRM Implementation	CRM's Current Share of Advertising	CRM's Share of Advertising in 5 Years	Percent Change
75% or less	12.4%	34.4%	177.4%
76% to 99%	25.0%	46.4%	85.6%
100%	33.5%	36.0%	7.5%

Source: Cornell Study, 2002.

Coupon redemption

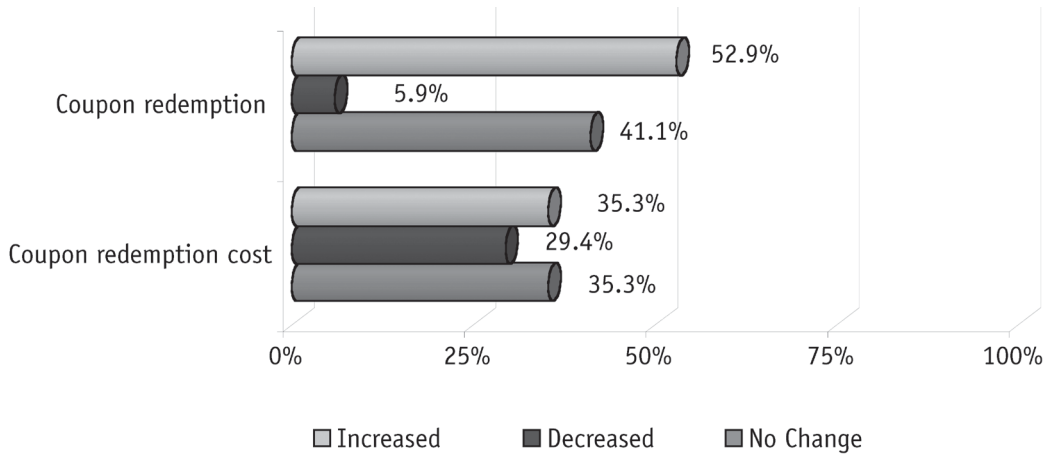
The impact of CRM on coupon activity has been mixed. Almost 53 percent of respondents reported that coupon redemption has increased since CRM was introduced while over 41 percent of companies have noticed no change in coupon redemption rates under CRM (Figure D-9). These results seem consistent with the goals of CRM since targeted coupons would be more efficient than traditional broadcast coupons. Since the broadcast variety still exist in great numbers and retailers' CRM programs are not all fully deployed, increased redemption rates may not yet be universally observed.

not been so focused can prove far more difficult than implementing the technology and frequent shopper card solutions.

Customer loyalty is a complex subject with perhaps as many dimensions as there are individual customers. The exact factors that influence one person to be loyal to a particular store may not engender loyalty in others. Despite this complexity there is little doubt that a key step in becoming a loyal customer is becoming a satisfied customer.

Customer satisfaction is a measure based on the individual's expectations and experiences. Retailers measure overall

Figure D-9. CRM's Impact on Coupon Redemption Rate and Cost



Source: Cornell Study, 2002.

CRM's impact on coupon redemption cost has been more mixed and is not as easily rationalized. Since targeted electronic coupons play a greater role in CRM, the logical presumption would be that coupon redemption cost would go down since there is minimal handling cost for electronic coupons. . However, less than 30 percent reported lower redemption cost (Figure D-9). About 35 percent reported higher coupon redemption cost while another 35 percent reported no change.

Customer service and satisfaction

The basic goal of CRM - increasing customer loyalty - is consistent with the notions of customer service and satisfaction. Naturally, companies with strong customer service cultures and traditions will have an advantage in adopting CRM over companies that are less customer-oriented. CRM can be misinterpreted as a technology-based solution but the reinforcement of CRM initiatives at store level cannot be over emphasized. Instilling a culture of customer service in an organization that traditionally has

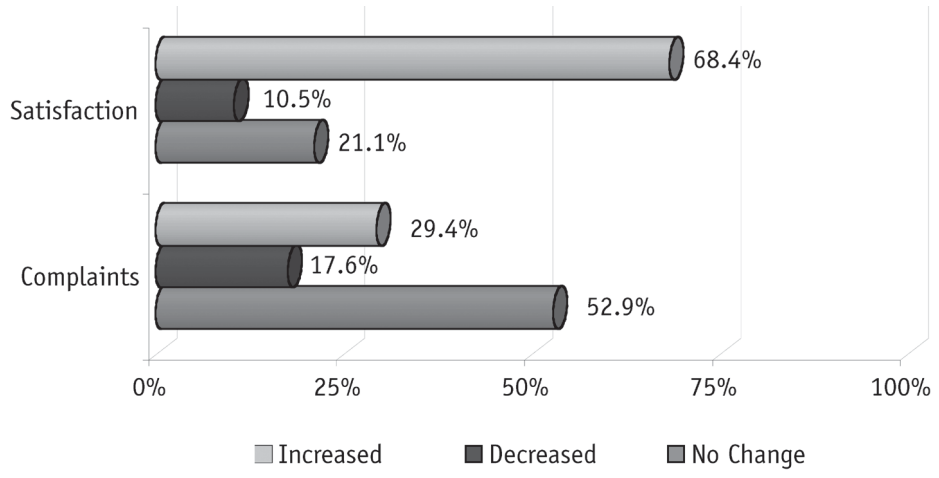
customer satisfaction through a variety of methods, including internal and external surveys, monitoring customer service requests, and cataloging customer complaints.

One challenge that retailers face with CRM programs is anticipating and responding to the potentially higher expectations consumers may have once they join a retailer's program. CRM programs typically promote special benefits, thus creating expectations and there could be an escalating threshold of consumer expectations and satisfaction. Our survey seems to indicate retailers are achieving some success in this regard. Over 68 percent of companies reported increased overall customer satisfaction (Figure D-10). However, only about 18 percent reported fewer customer complaints after CRM, perhaps reflecting consumers' heightened expectations.

Employee turnover

Labor represents a supermarket's largest operating expense, accounting for 53.1 percent of the total according to the

Figure D-10. Changes in Customer Satisfaction and Customer Complaints since CRM Launch



Source: Cornell Study, 2002.

Food Marketing Institute (FMI, 2002). While CRM implies more focus and effort on customer service and satisfaction, there may not necessarily be an accompanying increase in labor cost. However, employee turnover, an intractable problem that has plagued nearly all retailers in all channels of trade, is not only costly for supermarkets but also has an impact on customer satisfaction and retention. FMI also reported that average annual turnover for all store employees was 62 percent in 2001 and over 80 percent for part-time employees. In some regions, the part-time turnover rate was more than double the overall average (FMI, 2001).

A major study sponsored by the Coca-Cola Retailing Research Council estimated that on average 50% of new hourly supermarket employees terminate their employment within 97 days, a little more than 3 months, after hiring (Frank, 2000). While the rate for store management employees is much better, there are far more hourly employees interacting with customers on a daily basis. With that type of turnover, effective CRM implementation at store level is difficult because of employee inexperience and lack of familiarity in the two-way employee-customer relationship.

Our survey indicates that CRM has had no affect on employee turnover for over 82 percent of the companies. Two companies did report decreased employee turnover but there may be many other factors contributing to those results.

While there is no strong reason to suspect that an initiative like CRM would decrease employee turnover, it was hypothesized that CRM might result in engaging employees in the business more directly by clarifying their role in the company's success. Our retailer survey found a variety of practices supermarkets use to motivate employees to help drive CRM at store level. These include training programs that emphasize customer service, card program awareness, and recognition of best customers. Respondents also described a number of employee incentive programs including rewards, prizes, and recognition for outstanding CRM performance.

Summary and perspectives

- A high percentage of sales (86%) and transactions (72%) are captured with frequent shopper cards.

- Retailers report very positive results from their CRM Programs:
  - increased transactions
  - greater shopping frequency
  - increased transaction size
  - higher overall sales
  - increased margin and net profit
  - higher ROMI

- Marketing strategies have historically been difficult for retailers to measure due both to difficulty in controlling extraneous variables and inadequate analysis and testing procedures. The same is true for CRM strategies—the positive results reported by retailers are likely to be qualitative judgements as to the effects of CRM. The link between CRM strategies, cus-

tomer satisfaction, and retailer performance appears to offer great potential for future research.

- Retailers predict that CRM's share of their total advertising and promotional effort will more than double to 38% in 5 years.

- The original long-term premise of most CRM strategies was to replace inefficient mass advertising (mostly print) with more efficient targeted advertising and promotion. In reality, few retailers have traded off traditional advertising in lieu of CRM, most likely due to an unwillingness to risk sales effects in competitive marketplaces. Most CRM strategies now run parallel to traditional advertising programs, and many are incorporated within traditional print advertising programs via the widespread communication of card-based price discounts.

- CRM represents an additional layer of fixed and variable cost that for many retailers has resulted in internal cost pressures and increased demands by retailers to seek new sources of funds from manufacturers. Retailers still depend on trade promotion dollars for an important source of margin, marketing funds for their print advertising programs, and now seek "new" funds for CRM programs. This area of "trade spending," with its changed dynamics and complexity, offers a rich area for further research.

- There is anecdotal evidence that retailers tend to view CRM strategies separately and apart from their customer service strategies. As previously discussed in terms of marketing, there appears to be "break out" potential for a retailer to combine service and CRM tactics into a broad-based CRM strategy that is supported by customer-specific culture that links employee satisfaction and customer satisfaction.

Section E: CRM Constraints

While the logic of establishing and nurturing customer relationships makes intuitive sense to most supermarket executives, the transition from their traditional reality to realizing this new vision poses significant barriers.

Our survey asked retailers to list the top three factors preventing the realization of full CRM benefits in their company. The range of answers could easily be grouped into three broad categories of money, people, and technology. However, we have clustered the responses into finer groups to add the flavor of the sub-issues that support these three broad constraints. Likewise, for each of the sub-issues that follows we have included specific quotes from respondents that we think add additional insight.

Funding

The most common responses were related to funding (61%) (Figure E-1). A McKinsey study estimated that a loyalty card program launch can cost as much as $30 million in the first year with annual maintenance costs of $5 million to $10 million when marketing and IT infrastructure costs are included (Leech, 2002). The same study found that the leading frequent shopper card programs generated 1 to 3 percent more first year sales for the supermarket company (Leech, 2002).

Specific comments from survey respondents included the following:

- "Cost of maintenance, support, and development, including advertising & marketing"
- "Lack of resources—…will (the company) provide the IT and analytical resources to reach full potential"
- "Budget constraints while operating on slimmer margins to due competition…"
- "current marketing (budget) is focused on other areas"
- "expense of implementation—merchandising funds are not allocated to CRM programs"
- "costs—expensive to customize offers to specific customers and maintaining customer records"
- "marketing budget …very promotional in it's approach- most money spent on weekly flyer"
- "programming & software costs"
- "cost of launching a comprehensive program"
- "cost of software, hardware, and people to do effective data mining"

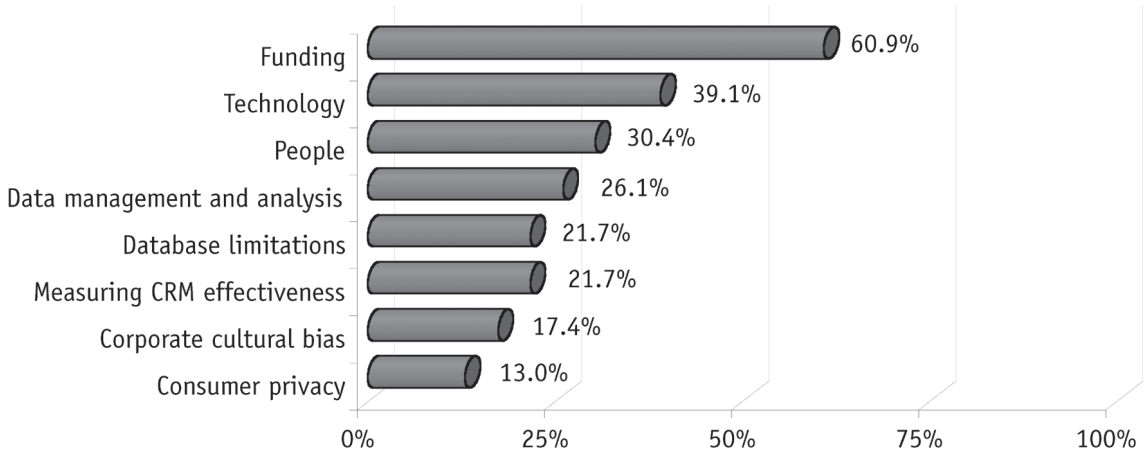
Funding issues are not unique to the supermarket industry. A recent survey by CIO magazine found that the slowing economy has cut into CRM spending across industries (Patton, 2002). The CIO study found that 64% of responding companies have learned to implement CRM projects in small steps rather than the larger components originally envisioned.

Technology

The second most common constraint was technology (39%) (Figure E-1). Following are quotes regarding the technological constraints to realizing full CRM benefits:

- "legacy systems (pricing host), network/common systems, no data warehouse"

Figure E-1. Constraints to Realizing Full CRM Benefits



Source: Cornell Study, 2002.

- "inability to retrieve consolidated data from all stores…"
- "being able to capture and format the information"
- "workable, cost effective technology that helps us run our loyalty marketing programs and other CRM efforts"
- "our current data mining tool is very cumbersome and time consuming to retrieve the detail of information needed to make marketing decisions"
- "transition of electronic systems due to a merger"
- "lack of adequate systems in our IT department to fully support our efforts"
- "IT systems- the cost to create a meaningful data bank and utilize needs further analysis"
- " in-house IT support of CRM initiatives"

While these comments represent the situations at companies responding to our survey, these situations are not uncommon in the supermarket industry and beyond. Despite the recent enthusiasm for CRM, the 2001 Andersen Survey of Retail Information Technology found that 64.4% of retailers representing many channels of trade were not planning to use dedicated technology to manage customer relationships (Chain Store Age, 10/2001).

People

The third leading CRM constraint involved people (30%) (Figure E-1). While the supermarket industry has challenges recruiting and retaining talented people at all levels of the organization, the technology area represents a particularly tough challenge. The collapse of many high-tech companies over the past three years has lessened the competition for technology talent to some degree. Even so, the supermarket industry still faces considerable challenges in this area.

The following comments distill some of the common issues and comments:

- "People! People! People! – Knowledgeable people (who) can…access all areas of the business, retrieve data from systems, and interpret into actionable plans"
- "human resources: skill sets, CRM talent, analytics"
- "the ability to retain high potential candidates in this demanding environment"
- "time and resources: FTEs"
- "the ability to attract high caliber candidates when competing with other more "glamorous" (industries)"
- "Trained personnel- if you are to have a disciplined CRM program, it is essential that store managers have new or upgraded skill sets. In addition, front end management and training become a crucial part of your overall CRM efforts."

According to our survey, the average number of full-time-equivalent positions specifically dedicated to CRM was 8.1 (Table E-1). An average of 6 percent of information technology (IT) effort was dedicated to CRM activities (Table E-1). Sorting responses by degree of CRM implementation shows that almost 10 percent of total IT spending was allotted to CRM for companies whose CRM programs are 75 percent or more complete (Table E-1).

Table E-1. Average Number of CRM-Dedicated Employees and CRM's Average Share of Information Technology (I.T.) Expenditures, Overall and by Degree of CRM Implementation

Degree of CRM Implementation	CRM FTE's (#)	CRM's Share of I.T. Expense (%)
Overall	8.1	6.0%
75% or less	5.1	5.3%
76% to 99%	15.4	9.8%
100%	20.5	5.7%

Source: Cornell Study, 2002.

Though the gist of the "people" constraints mentioned by our survey respondents is focused mostly on information technology and management people, a major issue for most companies has been and remains attracting and retaining competent store-level customer contact employees. In the U.S. these are mostly part-time employees and turnover, as referenced earlier, is a huge problem as supermarkets compete with myriad other entry level service industry employers for these same workers.

According to the U.K. survey referenced earlier, the most important factor consumers cited in determining their loyalty to a particular supermarket was the store's staff (Marketing, 2000).

Data mining

The next most frequently mentioned CRM constraint, database management and analysis (26%), is related to the people and technology issues noted above (Figure E-1). Data "mining" is the process of garnering knowledge from data. Data mining is a key to interpreting the information concealed in retailers' databases. And data mining requires high quality IT talent. Despite the people and technology challenges listed, only 40 percent of respondents indicated that they outsource data mining of their con-

sumer database. The following comments offer a glimpse of the many dimensions of this constraint:

- "storing, retrieving, and analyzing data"
- "analysis: being able to understand the information we have"
- "database management-the magnitude of information that is captured is extremely large, therefore making it difficult to manage…"
- "execution of data mining opportunities throughout a broad geographic region"
- "(database) management- which consumers do we focus on and how to reach them best"

The 2001 Andersen Survey of Retail Information Technology reported that 52.5% of retailers surveyed across many classes of trade were using data mining capabilities (Chain Store Age, 10/2001). The percentage was much higher (75%) for larger firms (sales above $500 million) but less than half (46.4%) for firms with sales between $200 million and $499 million (Chain Store Age, 10/2001).

The 2002 SN State of the Industry Report on Supermarket Technology reported that 29% of the supermarket retailers responding said they would test or launch a data mining program in 2002, up from 20% in the 2001 survey (Garry, 7/2002). In fact, data mining was the top priority in both 2002 and 2001 among projects supermarket companies were testing or launching, according to the SN survey (Garry, 7/2002).

Database limitations

Another frequently mentioned constraint is database limitations (22%) (Figure E-1). While related to the technology and database constraints mentioned earlier, the comments below give the flavor of the limitations that frustrate some retailers attempts to realize full CRM benefits:

- "we are not currently collecting household demographic information"
- "insufficient data- some cardholder information is not attached to the static information (i.e. name or household address)"
- "data integrity"
- "in-store card usage—store employees use non-customer-specific loyalty cards to give discounts, retrieving poor data"
- "tourist areas have large number of transient customers, making data collection harder in certain markets

As earlier mentioned, it has become common practice in many supermarket companies for cashiers to swipe a " house" card for shoppers who do not have or did not bring their own card or key tag. Another variation on this practice is for the cashier or the current customer to ask the next customer in the queue to swipe their card for both transactions, allowing the current customer to get the savings and the following customer to earn any accrual points toward sales or sweepstakes goals. Other data integrity problems include friends sharing cards, people shopping for others, and people registering for cards with assumed names and addresses.

These card-related issues are compounded by common cashier practices that distort sales information. For example, if a customer selects 12 yogurts, 3 of each of 4 flavors, but the cashier scans one container and enters a quantity of 12, the transaction is recorded incorrectly and sales of one flavor are inflated while the other flavors will eventually appear to have a shrink problem. These pervasive practices can be addressed with training that reinforces the importance of accurate scanning in maintaining data integrity.

Measuring CRM effectiveness

Related to the funding constraint, the issue of measuring the effectiveness of CRM (22%) is the next most commonly mentioned CRM constraint (Figure E-1). As mentioned earlier, the industry's preferred effectiveness measure is Return on Marketing Investment (ROMI). While the components of ROMI are well understood, the challenge lies in capturing the information comprising each of the components and allocating shared costs to specific activities. Supermarket executives interviewed for this study reported that they are under pressure to document CRM results and compare results with normal merchandising programs.

Here are representative comments regarding this constraint:

- "Overall cost and return on investment – it is very difficult to quantify the return on investment on CRM technologies and programs"
- "lack of effective measures to determine if what you are doing is working"
- "implementing tools to properly measure the effectiveness of CRM"
- "how do we show that we have moved individual consumers and changed behavior to show increased loyalty and profits?"

Corporate cultural bias

Another key constraint mentioned by companies in our survey was cultural bias toward traditional marketing (17%) (Figure E-1). Related comments included the following:

- "past history—it's still not "normal" in our organization to target promotional spending in this manner"
- "company culture—being able to formulate a plan and see it through based on the analysis"
- "barriers resulting from traditional senior management promotional strategies"
- "reluctance to move marketing/advertising dollars from general marketing to CRM—both our company and manufacturers"

These sentiments reflect organizational realities that are not unique to the supermarket industry. According to *Training* magazine: "… what senior management thinks is a technology issue is really more about company culture. Indeed, estimates suggest that between 30 and 75 percent of CRM initiatives fail because organizations have rolled them out without taking into account their cultural readiness…" (Simpson, 2002). Rigby et.al. (2002) assert that one of four keys to successful CRM implementation is that companies must first adopt customer-centric philosophies, change their structures and processes, and alter their corporate cultures accordingly. They also cited survey results indicating that 87% of managers pinned the failure of their CRM project on the lack of adequate change in management (Rigby, et.al., 2002).

Davids (1999) stressed that one of the 10 biggest mistakes in CRM is failing to understand the degree of cross-company involvement required. Further, Davids reported that, when CRM experts in manufacturing companies were asked who in the organization is most likely to resist CRM efforts, the unanimous answer was "the sales force, who care little about future profits and unrealized potential in their quest for the immediate sale."

These constraints are often interwoven. One example is the effect of cultural/organizational issues on the measurement of CRM effectiveness. A recent article in *Marketing Management* asserts that "adoption of CRM is becoming more of an organizational issue than one of measurability. … As innovative approaches close the gaps in ROI measurements, companies will need to create a solid understanding of how ROI can be used and install a culture that removes subjectivity in budget allocations and results measurements (Lenskold, 2002).

Consumer privacy

Multiple companies also mentioned consumer privacy concerns (13%) as constraints to achieving full CRM benefits (Figure E-1). However, later in the survey, when queried separately about their company's consumer confidentiality policy, almost one-quarter of respondents thought their privacy policy would prevent the company from realizing full benefits from CRM. Indicative comments of those who see confidentiality preventing full CRM benefits included:

- "It may prohibit some value-added services that could not be offered by us"
- "Our company will not compromise our customers' right to privacy in order to achieve full benefits of CRM"
- "…to avoid criticism, we will shy away from anything that even hints of invasion of privacy or a violation of confidentiality"
- "(if) full (means) reaching 100%—our opt-in policy will reduce those customers we can reach with specific mailings"

Comments from the majority who believe their company's confidentiality policy will not prevent full CRM benefits included:

- "We could work within those concerns to grow customer loyalty…"
- "Any program that is right for retail can be executed while maintaining confidentiality"
- "Confidentiality breeds trust with our customers"
- "We offer new members the option of not receiving special offers when they fill out their application. However, most want the offers."
- "We feel so strongly about customer privacy…We feel that the privacy issue strengthens our relationship with our customers"

In addition to the small but growing consumer backlash (see box on page 34) about privacy, there is also a wide range of regulatory and legislative activity dealing with privacy and restrictions on the use of personal information. In 1999 alone there were over 160 bills/amendments reviewed by legislative bodies and California passed the Supermarket Club Card Disclosure Act which regulates the use of information collected from consumers and prohibits supermarkets from asking customers for their social security number or their driver's license number (Janoff, 2000).

Retailers generally have a lot to lose and little to gain by violating consumer trust by compromising the privacy of their transaction data. The Federal Trade Commission (FTC) has been unambiguous in its position as indicated by its law suit against Toysmart.com, a failed Internet toy retailer, to prevent the bankrupt company from selling its customer database, in violation of its policy.

According to the Food Marketing Institute's Technology Review Highlights, 2002, 60 percent of responding supermarket companies have a stated consumer privacy policy, up from 40 percent in 1998, and 95 percent of supermarket companies do not share customer specific data with

third parties (FMI, 3/2002). All of the companies responding to our survey have privacy policies that prevent the use of customer specific information by any third party.

Privacy was a concern for some of the consumers who participated in the focus groups conducted for this project, though the majority expressed confidence that their personal information was relatively secure in the frequent shopper database. Despite the privacy concerns expressed by some participants, they were still active users of the cards.

The Roper survey referenced earlier in this report, found that the top two negative aspects consumers perceived about frequent shopper programs were related to privacy concerns. About a third of consumers surveyed expressed concern about the possibility of the retailer selling their confidential information to other companies (34%) and disliked the fact that joining a frequent shopper program involves giving private information to the retailer (33%). Despite these concerns, 80 percent of respondents felt the benefits outweigh the negative aspects of frequent shopper programs (Setlow, 3/35/02).

Two other technology trends are raising consumer concerns about privacy and testing consumer's tolerance for intrusions in their lives. One trend is the unrelenting proliferation of unsolicited electronic mail commonly referred to as "spam". By some estimates, the volume of spam e-mails almost tripled during the nine months prior to July 2002, by then comprising 12-15 percent of total e-mail traffic, about double the share of total e-mail traffic a year earlier (Lee, 6/2002). Likewise, access to high powered on-line search engines such as "Google" has allowed people to access personal information on other people without their knowledge or consent (Lee, 6/2002).

In addition to privacy, there is some concern that consumers may simply become fatigued by all the overtures from companies trying to create relationships with marketing efforts that may or may not deliver all that was promised (Sandberg, 2002). Fournier, et al. (1997) suggest that companies need to see the impact of their relationship efforts through the eyes of today's consumers. They make four major observations in this regard:

Is Everybody Happy?

Not all consumers are happy about the availability of supermarket frequent shopper card programs. While most consumers who object to the cards simply opt not to register for one or may register under fictitious names, there are a small but growing number of consumers who are actively protesting frequent shopper card programs. The main issues the protesters raise are the invasion of privacy implied by the data tracking that card usage enables, the allegation that prices are actually higher with frequent shopper cards than without, and the concern that retailers will exclude certain types of shoppers from card benefits through targeted marketing.

One "grassroots" organization that is growing in membership and visibility is CASPIAN, an acronym that stands for Citizens Against Supermarket Privacy Invasion and Numbering. According to CASPIAN's web site (www.nocards.org), the organization was founded in 1999 and it's "efforts are directed at educating consumers, condemning marketing strategies that invade shoppers' privacy, and encouraging privacy-conscious shopping habits.

CASPIAN has gained recognition and press coverage for its efforts in national media such as Business Week and Kiplinger's Personal Finance. CASPIAN has organized protests and demonstrations at supermarkets where frequent shopper card programs are being introduced, such as in January 2002 at Albertson's in Dallas and at QFC in Seattle in June 2002. While the number of actual protesters in each case has not been a significant percentage of each store's customers, their visibility and message has garnered press coverage.

While CASPIAN strongly recommends that consumers resist the urge to join frequent shopper programs and encourages them to shop only at stores that do not offer shopper cards, it also strongly recommends that consumers do not sign up for cards under assumed names or false addresses for a variety of reasons listed in its web site. The organization recognizes supermarket companies that do not offer frequent shopper programs at the CASPIAN web site with its "Triple Blue Ribbon of Privacy" rating. The web site also lists over 400 food retailers and rates each according to its use of frequent shopper programs.

While CASPIAN has perhaps had the highest profile, it is not the only activist organization addressing consumer privacy issues. For example, Privacy Activism (www.privacyactivism.org) is "a non-profit organization whose goal is to enable people to make well-informed decisions about the importance of privacy on both a personal and societal level" (Privacy Activism web site).

- "The number of one-on-one relationships that companies ask consumers to maintain is untenable. As a result, many marketing initiatives seem trivial and useless instead of unique and valuable."
- "There's a balance between giving and getting in a good relationship. But when companies ask their customers for friendship, loyalty, and respect, too often they don't give those customers friendship, loyalty, and respect in return."
- "Companies' claims that customer relationships are valued don't hold water. Sometimes people feel put at a disadvantage because of their loyalty. And sometimes a company's preoccupation with its so-called best customers leaves other revenue-generating customers feeling left out and underappreciated."
- "In their role as relationship partners, companies need people to think of them as allies and friends; but more often than not, they come across as enemies. Companies claim to offer solutions to consumers' problems; but in fact, they are creating more problems than they solve."

The authors support these observations with examples of consumer comments. Many of the comments in our focus group comments echoed these themes as well. Clearly, people are very sensitive to the intrusion of their home and personal space by marketing efforts, especially those for which they perceive little value.

Other constraints

Additionally, the following are several CRM constraints mentioned by only one or two companies each (with quotes where relevant):

- top management support,
- consumer acceptance,
- the EDLP business model,
- utilization throughout the organization,
- limited CRM knowledge of CPG account representatives,
- product vs. customer focus of CPGs and supermarket buyers,
- "…buyers/category managers are concerned with case movement vs. who and why customers purchase"
- execution at store level, and
- consumer response and awareness.
- "customers still ignore targeted mailings, just like other forms of media"

Summary and perspectives

- The survey indicates that funding and technology are the most pervasive barriers to the full realization of CRM benefits. CRM requires sophisticated information technology to collect, store, and analyze transactional data—capabilities that are beyond the traditional POS and merchandising systems of retailers.

- "People" are also a constraint, both from the perspective of quantity and quality. Companies with fully implemented CRM programs report 20.5 FTEs dedicated to the CRM effort.

- Another barrier to CRM implementation centers around the ability to measure effectiveness on an ongoing basis. Many researchers report that companies underestimate costs and achieve less than adequate ROI. As suggested earlier, the measurement of CRM effectiveness appears to be a rich area for further analysis.

- Cultural and organizational issues are constraints that could still derail effective CRM, even if the other constraints are overcome.

- Consumer privacy appears to be a potential barrier that generally has been managed well by retailers—relatively few consumers express concern and fewer report any violations by retailers. A growing, vocal consumer privacy advocacy movement might influence a broader spectrum of consumer attitudes about loyalty programs.

- Lastly, a minor but growing concern is consumer fatigue with attempts by companies to communicate and establish one-on-one relationships. Consumers perceive themselves to be time-starved and bombarded by choices- in this environment, CRM efforts, unless absolutely "on target," may backfire.

Section F: The Role of CPG Marketers

A challenge facing retailers is creating and maintaining a CRM package that rewards loyalty while continuing to spark consumer interest and enthusiasm. Successful reward programs tend to create increasing consumer expectations and continuing to meet those heightened expectations can be both expensive and creatively taxing.

CPGs (consumer packaged goods marketers) are facing an environment where media fragmentation, cultural diversity, retailer consolidation, private label competition, and their own brand extension efforts and short-term sales promotion strategies have combined to erode brand equity. Many well-known brands no longer convey to consumers the qualities that CPGs often spent decades developing.

It is increasingly rare for a brand to engender complete, exclusive loyalty in many consumers. Dowling and Uncles (1997) referred to this phenomenon as "polygamous loyalty," where consumers are "loyal" to more than one brand in a product category. While complete loyalty may not be necessary for a brand relationship, a recent study found that very few brands have earned true "relationship" status in consumers' minds. The study also found that consumers expect more from the brands that they do have relationships with. Consumers also cited few brands as relationship "winners," while many are disappointing (Direct Marketing, 5/01). The very nature of a brand is the "promise" it engenders about the expected performance of the product or service. While some brands may deliver on their promise, the type of product simply may not involve the level of emotional involvement that a relationship requires from consumers.

CPG goals can be opposed to retailer goals since CPGs are typically interested in building brand loyalty while retailers want to increase store loyalty. A joint project that builds brand loyalty may help the CPG but not the retailer while a project that builds store loyalty may help the retailer but damage the CPG's business with other retailers. Brand loyalty is a multi-channel, multi-store concept, thus CPGs prefer programs that focus broad attention on the brand. Retailers realize that store loyalty can be the difference between success and failure since most stores sell a similar selection of CPG brands.

A 2000 Deloitte Consulting survey found that approximately 70 percent of North American CPG manufacturers see collaboration with retailers as critical to their efforts to build relationships with end consumers (Deloitte Consulting, 2000).

Our interviews with executives at some of the leading CPG companies indicate great interest in actively participating in retailer CRM programs but also a bit of skepticism about the long term impact of retailer CRM programs on the marketing of CPG products.

CPG involvement in retailer CRM programs

Retailers often look to CPGs for assistance in maintaining CRM programs. CPG assistance typically includes financial support to defray the cost of activities like targeted direct mail and non-financial support such as sharing expertise and research findings. Our survey found that 75 percent of responding companies already partnered with CPGs to execute their CRM programs (Table F-1). A total of 80 percent of respondents expected to work with CPGs within a year.

Retailers reported an average of 15 CPGs playing a significant role in the retailer's CRM program (Table F-1). That number, on average, was forecast to increase to just over 34 CPGs a year from now, an increase of over 126 percent. In most cases, the significant role of CPGs involved the types of financial and non-financial assistance mentioned above and detailed in the following paragraphs.

Table F-1. Number of CPG Partners in Retailer CRM Program, Current and 1-Year Projection

	Current	Next Year
Percent of retailers partnering w/CPGs	75%	80%
Average number of CPG partners	15.0	34.3
Low number of CPG partners	0	0
High number of CPG partners	50	100

Source: Cornell Study, 2002.

The number of CPGs currently playing a significant CRM role ranged from 0 to 50. The estimated number of CPGs expected to be significantly involved in CRM next year ranged from 0 to 100. At least one responding company has no intentions of working with CPGs in the next year.

Sorting by degree of CRM implementation, retailers with fully implemented CRM programs not only reported the highest average number of CPG partners (20.5) but also anticipated working with even more CPGs in the next year

(Table F-2). Their projected average (44.3 CPGs), more than double the actual level, and the percent increase (116.1%) from the actual level were both higher than those of companies in the other categories.

Table F-2. Average Number of CPG Partners in Retailer CRM Programs, Current and 1-Year Projection, by Degree of CRM Implementation

Degree of CRM Implementation	Current Number of CPGs	Number CPGs in 1 Year	Percent Change
75% or less	16.2	26.6	64.2%
76% to 99%	10.3	21.7	110.7%
100%	20.5	44.3	116.1%

Source: Cornell Study, 2002.

Not surprisingly, the CPG roles that retailers perceive in their CRM programs closely mirror the constraints they face, referenced earlier in this report.

Promotion funding

Almost all respondents (90%) desire CPGs to provide funding for the retailer's CRM program (Figure F-1). The more that retailers can rely on manufacturer funding for CRM efforts, the further they can stretch their own budget dollars to develop the type of in-house talent and resources needed to fully exploit CRM opportunities.

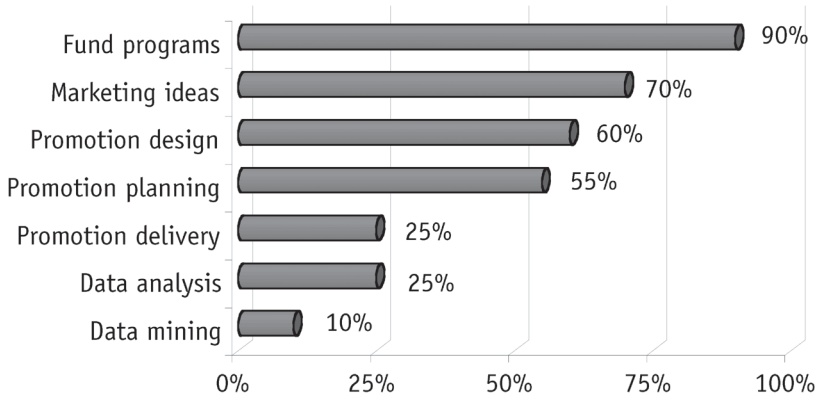
One of the issues arising here is the origin of the funds CPGs provide for retailer CRM programs. Retailers generally want CRM funds to be new or incremental funds, above and beyond the marketing and trade promotion money CPGs already give them for traditional sales promotion activity. CPGs prefer to redistribute already budgeted trade promotion money to proportionately reflect the distribution of sales activity at retail.

This funding source issue has repercussions within both the retail organization and the CPG organization. As earlier noted, CRM's home within the typical retail organization is the marketing department. Traditionally, CPG trade promotion dollars have been controlled by the merchandising department. Within the retail organization, a reallocation of trade promotion money by CPGs means that the sales department loses money while the marketing department gains funds. Likewise, on the CPG side there is often a conflict over where money should come from for retailer CRM program activity. In some CPG companies the marketing department funds CRM activity as part of its advertising budget; in others the activity is seen as part of the trade promotion activity of the sales department.

Marketing ideas

Seventy percent of respondents saw a key role for CPGs in providing marketing ideas to retailer CRM programs (Figure F-1). Given their long experience with consumer marketing programs, CPGs can offer marketing ideas that sustain and energize a retailer's CRM program. Likewise, since most CPGs work with a variety of retailer CRM programs, they have a sense of what works well in a wide variety of situations.

Figure F-1. Retailer's Preferred Roles for CPG Participation in Retailer CRM Programs



Source: Cornell Study, 2002.

Promotion design

Sixty percent of respondents want CPG involvement in promotion design (Figure F-1). CPGs either use internal resources or outsource promotion design to third parties. Many CPGs produce program templates for various brands that retailers can simply customize with their own names, logos, and conditions as a turnkey CRM program.

Promotion planning

More than half (55%) of respondents see a role for CPGs in promotion planning (Figure F-1). CPGs have tremendous experience in planning promotional activities and retailers have limited resources to dedicate to each promotional activity. CPGs can contribute the vast amount of category or product specific knowledge that they gather and purchase from third parties about the consumer preferences. This information, when joined with retailer transaction data, can help develop an accurate picture of the promotional opportunity at hand.

Promotion delivery

Despite the majority's desire for CPG help in designing and planning promotions, respondents were much less inclined to seek CPG involvement in promotion delivery (25%) (Figure F-1). This may reflect the retailers' goal of enhancing customer loyalty to their stores, not to the CPG brand. Where such efforts enhance the retailer brand as well as the CPG brand, retailers were more inclined to participate.

These responses echo findings from the Deloitte Research study referenced above. The majority of retailers in that survey said they would like manufacturers to contribute in three key areas: joint funding of consumer marketing activities, insight into consumer needs related to products in their category, and help to optimize total category performance (Deloitte Research, 2000).

Data analysis and management

Responding retailers saw very limited roles for CPGs in areas related to their consumer database such as data analysis (25%) (Figure F-1). While not many responding retailers want manufacturers analyzing their scanner data, our interviews with retail executives clearly indicate they are looking to manufacturers to provide other data and analysis about broader consumer trends and category or product-specific trends to help retailers interpret their scanner data trends. So manufacturers continue to add value to the retailers CRM program in much the same way that they add value to the category management process by providing the knowledge of trends beyond the specific retailer's stores.

Data access and targeting

Responding retailers were somewhat split about CPGs potentially using retailer CRM programs to build brand loyalty via direct consumer relationships. About 50 percent thought such CPG interest would be acceptable as long as it was consistent with the retailer's strategy and benefited the store and the customers. Related positive comments included:

- "…a delicate issue but we anticipate more collaborative uses of customer data—shared insights, aggregated data re: promotion effectiveness"
- "We would welcome manufacturer participation as long as all parties involved benefited and their involvement didn't run contrary to the retailer's CRM strategy"
- "CRM program information is a company asset. Use of the asset would be negotiated on a case by case basis."
- "If the (manufacturer/consumer) relationship is based on a transaction from our stores, that relationship should continue."
- "Although we realize this is a strategy, we are careful that any loyalty marketing is consistent with our overall marketing strategy. If what a manufacturer wants to do fits, we do it, if not, we pass."

About 40 percent said that such initiatives would be prohibited by the company's privacy policy.

In the 2000 Deloitte Research study referenced above, responding retailers identified the following perceived manufacturer characteristics as barriers to retailer-manufacturer collaboration:

- too product-focused rather than consumer-focused
- lack of information systems required to manage and analyze data
- inability to be truly objective
- lack of skilled resources
- lack understanding of retailer business priorities (Deloitte Research, 2000)

Whether these issues are real or perceived and whether they apply to every manufacturer equally are open questions for debate. In any case, these and other issues remain obstacles to the type of collaboration that would truly enable retailer CRM programs.

CPG manufacturers are clearly attempting to regain and build their brand equity and loyalty through direct rela-

tionships with consumers. The Deloitte Research study surveyed 60 CPG manufacturers based in North America, Europe, and Asia Pacific and classified the CPGs as leaders and followers in terms of customer centric marketing. Leaders were those CPGs that (1) had clearly defined strategies to acquire, maintain, and develop relationships with consumers and (2) had at least started to identify their preferred consumers on an individual basis. Almost half (48 percent) were considered leaders (Deloitte Research, 2000).

Among the findings of the Deloitte study was that leading CPGs were 60 percent more profitable than followers and 38 percent more likely to observe improved satisfaction and brand recognition as a result of their consumer relationship investments (Deloitte Research, 2000).

A key component of much of the CPG consumer relationship activity has been web site initiatives. Ninety-three percent of the CPGs in the Deloitte study had a web site presence, though not all of those were offering on-line sales direct to consumers. Only 26 percent of CPG leaders' web sites allowed consumers to purchase directly (Deloitte Research, 2000).

The Deloitte study also noted a shift in the major sources CPGs rely on for consumer information. At the time of the survey, over 60 percent of responding CPGs relied on retail partners as a critical source of consumer information, the largest percentage of any information source. However, responding CPGs projected that over the following 3 years retail partners would slip to the fourth largest source for consumer information, with the top source being their own data collected by phone, mail, e-mail, fax, or the Internet (Deloitte Research, 2000).

CPGs were using the information acquired through the Internet to enhance their brand equity in four major areas:

- direct consumer input to product innovation and development
- value-added benefits for consumers
- engaging influential members of the community
- offering entertainment features that enhance the brand (Deloitte Research, 2000).

Summary and prospects

- In progressively more difficult marketing environments characterized by media fragmentation, private label expansion, retailer consolidation, and cultural diversity, CPGs are increasingly attempting to bolster brand equity through direct relationships with consumers. Retailers are key gatekeepers in this effort, as their CRM programs provide information on the link between specific consumers and buying behavior. As a result, CPGs are active participants in retailer CRM programs…survey respondents reported an average of 15 CPG partners in their CRM programs, with a projected increase to over 34 next year.

- As noted earlier, many retailers have supplemented their traditional advertising programs with CRM strategies. As such, retailers seek CPG support in the form of new monies—cutbacks in traditional trade and marketing spending are viewed as being dilutive to margin and/or causing reductions in store traffic and sales. This demand for new monies has stressed retailer/manufacturer relationships and may in fact be a factor in the shifting balance of power from manufacturer to retailer.

- While retailers seek funding and marketing and promotional planning help, they are more reluctant to invite the CPG to participate in the delivery of promotions. There exists an inherent conflict in CPG vs. retailer goals—loyalty to brand vs. loyalty to store. Collaborative strategies that create both brand and store loyalty (including measurement) are areas that retailers and manufacturers are only beginning to explore.

Getting to know you…

Consumer packaged goods marketers are using a variety of methods to reach out directly to learn more about consumers of their products.

- Procter & Gamble uses "cohort" marketing through web sites that cluster a number of its products that are aimed at particular consumer segments (CIES, 5/2002). One P&G web site called HomeMadeSimple.com "markets five P&G cleaning brands and is supported by a free email newsletter sent to over 2 million subscribers"(CIES, 5/2002). "The lifestyle theme was seen as particularly important in increasing loyalty to cleaning products, which lack the kind of personal relationship enjoyed by cosmetics, for example" (CIES, 5/2002).

- Kraft has undertaken several noteworthy initiatives to drive brand loyalty for its broad range of products. Periodic exclusive Kraft free standing inserts (FSIs) focus consumer attention on Kraft brands and products with coupon savings to encourage trial and repeat purchases. The Kraft web site features, among other things, the Kraft Interactive Kitchen, where consumers can find recipes, cooking tips, nutrition information, menu planning, and other time saving resources. Kraft has also introduced its own magazine, "Food …….", for which subscription is free if the consumer is willing to share detailed information about their household composition and food consumption habits (www.kraft.com, 9/2002).

- In addition to a variety of consumer information and entertainment features, Kellogg's web site features information about its frequent flyer partnership with American Airlines. Consumers cut certificates from the packages of selected Kellogg's breakfast cereals they purchase and mail them to Kellogg's to accumulate miles in their American Airlines account. Each package has a certificate worth 100 miles upon redemption. For 2003, the maximum number of miles an individual can accumulate under the program is 100,000, roughly enough for 4 round trip air tickets on American Airlines, depending on the destinations, etc.

- Kellogg's site also offers direct on-line sales of its Kashi line of cereal products, not all of which are typically stocked in most supermarkets. (www.kelloggs.com, 8/2002).

- McCormick's web site features a "My McCormick" section where individuals can customize the site to their own interests. The site offers recipes, spice information, cooking techniques, time saving tips, and the opportunity to sign up for a free monthly email newsletter called Flavor Notes. Visitors can send "recipe greetings" to others via email. In one contest promoted at the site, consumers can win $10,000 by entering photos of meals they created using McCormick's Grill Mates products. While creating consumer excitement and generating sales, the contest also provides McCormick with great information about how consumers use their products and adds to the content of the web site by providing other recipes and cooking ideas to share with other consumers.

  While not directly selling its products on-line, McCormick does offer links to several on-line purveyors, two of which offer McCormick products exclusively. (www. mccormick.com, 9/2002)

- Ralston-Purina, now part of Nestle, has a complete pet health and nutrition resource at its web site for consumers, veterinarians, and other pet care professionals. This web based resource is linked to the actual Purina Pet Institute that is actively conducting and funding pet health and nutrition research in conjunction with leading vet schools around the world. (www.purina.com/institute, 8/2002)

- Nestle has a web site called verybestbaby.com that is a valuable resource about health and nutrition of babies, mothers, and families with babies. In addition to information about Nestle Carnation products for babies and mothers, the site includes a link to netgrocer.com where these products can be purchased on-line. (www.verybestbaby.com, 9/2002)

Though not a new concept, CRM is still being explored and evaluated by supermarket companies. At best, our survey indicates a wide range of implementation, experience, and results with supermarket CRM programs. The most advanced companies in our study appear to be still barely scratching the surface of the full potential and impact of the concept.

CRM could bring dramatic changes in how supermarket companies are organized, go to market, and perhaps valued by financial markets. However, there is also the possibility that the industry will become weary of CRM before realizing its full potential and value. CRM may simply be too great a cultural and organizational hurdle for many retailers to realize its full benefits.

The loyalty-profitability connection

The bedrock upon which CRM is built is the concept that loyal customers are more profitable customers, especially over their lifetime of business with the firm. The premises supporting this loyalty-profitability connection are that loyal customers are less costly to serve, less sensitive to price levels, and attract new customers through their recommendations.

Debate continues about the validity of these assumptions, especially when applied across a wide range of industries. Examining the basic CRM premises in the context of national catalog retailer, Reinartz and Kumar (2000) found that:

- a positive linear relationship between customer lifetime and company profits does not necessarily exist;
- both long and short-term customers can be profitable;
- profits do not necessarily increase with increasing customer lifetime;
- the cost of serving life-long customers is not lower;
- long-life customers do not pay higher prices.

While differences between catalog retailing and supermarkets may limit the applicability to the grocery industry, Reinartz and Kumar (2002) then extended their research to four other companies, including a French supermarket company. Although 36% of the supermarket customers were both long-term and highly profitable, there was also 15% of customers who were *short-term yet highly profitable*, exactly the same percentage who were *long-term yet low profit* (Reinartz and Kumar, 2002). Reinartz and Kumar (2002) also found that:

- the differences between long-term and short-term customers were smaller than expected,
- there was no significant difference in prices paid by long-term customers in any product category,
- overall, the link between customer longevity and word-of-mouth promotion was not very strong (although when attitudinal and behavioral loyalty are observed, those who scored high on both measures, were much more likely to be both active and passive word-of-mouth proponents of the store than their peers.)

On the other hand, a study of 5 retail sectors in the United Kingdom found for grocery retailing that loyal shoppers not only allocate more of their budget to their "first choice" store but also spend more on groceries in total than their less loyal peers (Knox and Denison, 2000). In fact, the study estimated that the combination of spending a higher proportion and having a larger budget for grocery spending resulted in loyal grocery shoppers spending as much as 4 times the amount their peers spend per month (Knox and Denison, 2000). These results mirror results of pioneering work done in the U.S. during the 1960s by Enis and Paul (1970), though the difference in spending between loyal and non-loyal customers is much greater in the U.K. study. Observations by Bain & Co. consultants across 12 industries over many years noted strong links between customer loyalty and company profits (Reichheld, 1996).

While direct comparisons of the results of any of these studies are complicated by the variations in methodologies, industries, countries, and other variables, the mixed results nonetheless are indicative of the uncertainty that pervades the CRM loyalty-equals-profitability presumption. Given the widespread deployment of CRM-based frequent shopper programs in the U.S., the opportunity exists for definitive research on the effect of such programs on customer satisfaction, shopping behavior, and retail sales and profitability.

The loyalty issue

Perhaps more basic than the loyal-profit relationship is the concept of loyalty itself. Since most shoppers have more than one frequent shopper card and seem to perceive the cards as a current means to lower prices, it seems that frequent shopper card programs are not necessarily creating loyal shoppers. Furthermore, since most supermarket frequent shopper programs offer price discounts to all cardholders, it does not appear that supermarkets are reaping any benefits from the notion that loyal customers may be less price sensitive.

The competitiveness of the supermarket industry tends to give first adopters of new practices a relatively short window of exclusivity before competitors match the offering, leveling the playing field once again. In most markets, it seems that simply offering a customer loyalty program will not necessarily increase customer loyalty.

The question is whether the competitive one-upmanship of most supermarket companies will simply add costs to the structure of otherwise undifferentiated retailers, thereby increasing the pricing advantage of non-CRM retailers. Another question is whether the level playing field phenomenon occurs because no retailer truly reaps the full benefits that CRM offers and, if so, is there an opportunity for a company to distance itself from the pack by doing so?

Dowling and Uncles (1997) concluded "all that a customer loyalty program will do is cost money to provide more benefits to (existing) customers- not all of which will be seen as relevant to the brand's value proposition and core positioning." Certainly there are successful retailers, Wal-mart, Publix, and HEB amongst them, who have eschewed the frequent shopper program concept to focus their efforts on customer service or lowering prices. Wal-mart, for example, is also very sophisticated at mining their data to understand customer needs and respond with merchandise and store formats that address those needs. The remarkable success and apparent customer loyalty these companies earn lends credence to the criticism of frequent shopper programs.

Simultaneously, the understanding of customer loyalty continues to evolve with research revealing more insight into the dynamics and complexity of customer loyalty. Examples of recent customer loyalty research findings include:

- Dowling and Uncles (1997) claim that "polygamous loyalty" captures the essence of actual consumer behavior better than brand switching, a clear transfer of loyalty from one product to another, or promiscuity, a more random purchase of products without strong loyalty to any in the set.

- While earlier efforts to describe loyal customers found that more loyal customers tended to be less educated and work in more blue-collar professions (Enis and Paul, 1970), more recent research has found that household income and education are positively related to store loyalty (Flavian, Martinez, and Polo, 2001).

- Store loyalty intentions (measured by intent to continue shopping, increase spending, and recommend the store) have been found to depend on supermarket customers' perceptions of service quality, merchandise quality, and, when there is a high degree of competitor attractiveness, value (Sirohi, McLaughlin, and Wittink, 1998).

- A McKinsey study of the attitudes of 1,200 U.S. households about companies in 12 industries, including the grocery industry, identified three basic attitudes of loyal customers—emotive, inertial, and deliberative, with emotive being the most loyal. Only 15% of supermarket customers were classified as emotive, about half the proportion of 8 of the other industries (Coyles and Gokey, 2002).

While the understanding of customer loyalty evolves so does the vision for where customer relationship marketing could lead. Only time will tell what the supermarket industry's verdict on CRM will be. However, there is a brighter future for CRM being espoused by leading academics and consultants: the concept of customer equity.

Customer equity

Blattberg and Deighton (1996) introduced the notion of *customer equity* as the sum of the discounted lifetime values of all the firm's customers. Customer equity management represents the full potential of CRM. Much has been written in the past 5 years about customer equity and the theoretical concept is now well defined, although it has not been widely observed in practice, especially in retailing. For excellent reviews of the evolution of the customer equity framework see Bell, et. al (2002) and Hogan, Lemon and Rust (2002).

Rust, et al. (2000) noted the essence of customer equity in the following way: "The business world is increasingly organizing itself around customers rather than products… Customer focus requires a new approach: managing according to Customer Equity (the value of a firm's customers), rather than Brand Equity (the value of a firm's brands), and focusing on customer profitability rather than product profitability."

Blattberg et al. (2001) added "customer equity's basic premise is straightforward: the customer is a financial asset that companies and organizations should measure, manage, and maximize just like any other asset." Earlier work by Grant and Schlesinger (1995) proposed that companies can " …link their investments in customer relationships to the return that customers generate." The authors refer to this as the "value exchange" and suggested that retailers should strive to "optimize the value exchange." According to Reichheld (1996), "To manage customers as assets, you have to be able to value them as

assets. This means you should be able to quantify and predict customer duration and lifecycle cash flow."

Customer lifetime value

Customer lifetime value (CLV) is the most prominent measurement tool for valuing customers as assets. CLV is defined as the present value of the future profit of a customer's lifetime of business with the company. Bell et al. (2002) observed that "CLV depends on assumptions about the future stream of income from a customer, the appropriate allocation of costs to customers, the discount factor, the expected "life" of a customer, and the probability that the customer is "alive" at a particular point in time." This idea recognizes that these variables are not consistent across customers, and, therefore individual customer profitability varies as well. Customer Equity is simply the sum of all CLVs (Blattberg et al. (2001).

Customer equity presumes that CLV can be measured and managed. Customer equity would be evaluated in two major ways: the present value of the customer base and the company's ability to manage the customer asset. According to Hogan, Lemon, and Rust (2002), the "ability to acquire, manage and model customer information is a key asset of the firm that can be a source of sustained advantage."

The supermarket industry does not appear to be among the leaders in exploring CLV. In our survey, only 20 percent of responding companies were exploring CLV calculations and, surprisingly, no other companies were planning to do so. The companies calculating CLV were clearly in the experimentation stage and had not yet seen any practical application of the concept.

The very nature of customers as assets presents a major challenge to the success of using customer equity management. Berger et al. (2002) observed that "when an asset is purchased, the firm can usually determine the revenue streams associated with it. If the asset is sold to another entity, the firm is compensated; and the firm can insure against the possibility that the asset is lost or destroyed. However, when the firm considers an individual customer as an asset, the association between the customer and the revenue streams that accrue to the firm is much more tenuous and difficult to identify."

The calculation of the value of individual customers must be continually updated since it will change over time based on many factors, among them the retailer's CRM efforts. Berger, et al. (2002) note that "a firm may use CLV estimates to target certain market segments with loyalty programs, whereas the existence of loyalty programs alters customers' purchase behavior and subsequently influences the calculation of CLV." This feedback effect further complicates the very complicated process of valuing customer assets.

Some argue that it may not be worth the effort to calculate the profitability of individual customers especially in the supermarket industry where tracking direct costs of serving each customer would be very challenging. Libai et al. (2002) argue that "a common misperception among scholars and managers is that it is necessary to use individual-level customer profitability models…" to make marketing resource allocation decisions. The authors go on to argue that "a segment-based assessment of customer profitability can be a reasonable alternative to an individual model."

There is also debate about the accuracy of accounting profit, even with discounted cash flows, as measure of CLV. Ryals (2002) suggests that economic value, reflecting risk, is a better measure of the value of the customer. However, the author argues that even risk-adjusted CLV may not be a true measure of the value of a customer to the firm because there are relationship benefits that should be valued as well (Ryals, 2002).

Customer Life Cycles (CLC)

A key to calculating customer lifetime value is to understand the dynamics of a customer's actual and potential business lifetime with respect to the supermarket and the patterns that describe the changes in it over time. These patterns comprise the customer life cycle (CLC). The typical consumer life cycle is not difficult to envision as the household progresses through the typical life stages and their shopping habits change in kind. The challenge for supermarket companies will be to anticipate, identify, and react to the myriad variations on the norm that our complex, rapidly changing society produces. Examples from our focus groups are particularly illustrative of the challenges inherent in understanding CLCs.

- One participant lived with her husband and three sons but 2 of the sons had just decided to join the Navy together. Trying to understand this family's CLC using a traditional mode such as the recency, frequency, and monetary value (RFM) method would project a very different CLV for this household than their reality would indicate.

- Another focus group participant and her husband were empty nesters for several years until one adult son returned home recently on a long-term basis. Targeting this household based on the transaction history to this point will miss great opportunities based on the son's preferences.

In both cases, the shopping profile, the lifecycle, and the lifetime value of the household had changed dramatically yet the only way the supermarket would know was by careful analysis of their transaction data. Even if the supermarket observed the changes in shopping behavior for these households, the range of potential explanations would include several that could lead to incorrect conclusions and, perhaps, wasted time, money, and effort. These kinds of changes are not exceptions in today's fluid society where "traditional" households are increasingly the exception. The U.S. Census Bureau reported that married-couple households with children were just 24 percent of total U.S. households in 2000 (A.C. Nielsen, 2002).

Significant Challenges

Bell et al. (2002) identified seven challenges facing any company or industry in effectively adopting customer equity management. These same challenges apply to CRM for the supermarket industry. Likewise, the implications of these seven challenges hold true for the CPG industry that is so directly connected to the supermarket channel. Using the seven challenges as a framework, the following section attempts to forecast prospects for the supermarket industry.

- ***Challenge #1: assemble individual-level, industry-wide consumer data.***

Supermarkets have an abundance of customer transaction data. The management and understanding of these data are major challenges and will continue to be for most companies. Mastering data issues is essential but not sufficient for customer equity management success. Bell, et. al (2002) warn that "learning from experience from the company's own customer data can be myopic; the challenge is getting data on prospective customers". Despite CRM's focus on retaining existing customers, attracting new customers is still essential to growth since attrition is unavoidable no matter how successful a retention strategy is employed.

In the best-case scenario today, supermarket companies are partnering with CPGs, using category or product-specific data from the CPGs and third parties to corroborate the retailer's scan data. As in the category management process, best CRM practitioners recognize that CPGs typically have more category-specific information on trends and consumer profiles than supermarkets.

To realize the full benefits of customer equity management, the best CRM practices will have to be enhanced by expertise and methods for forecasting future trends from the combination of data provided by retailers, CPGs, and third parties.

- ***Challenge #2: Track marketing's effects on the balance sheet, not just the income statement.***

Supermarket companies are just beginning to understand the components and dynamics of measures such as return on marketing investment (ROMI). While ROMI calculations are used today, it is clear from comments noted earlier that capturing the key components of the ROMI calculations remains a challenge for most.

Addressing the income statement vs. balance sheet dilemma, Hogan, Lemon, and Rust (2002) stated that "marketing expenditures once viewed as short-term expenses are now being viewed as investments in customer assets that create long-term value for the firm and its shareholders." Bell, et al. (2002) contend that, if marketing cost is expensed through the income statement in the period incurred, there is risk of under-investment in customer acquisition. Given the short-term, quarterly financial objective-driven horizon that plagues most publicly held supermarket companies today, this longer-term view of marketing as an investment in customer assets will not be easily adopted.

Customer asset valuation will be problematic for the supermarket industry since customers have so many shopping alternatives and relatively low switching costs.

- ***Challenge #3: Model future revenues appropriately.***

Forecasting future revenues, especially on an individual customer basis, is a particular challenge for retailers and especially for supermarkets. Though this may be one of the ultimate features of a fully developed CRM program,

Given the numbers of customers and their ease of switching, it is not likely that supermarket retailers will be able to accurately track the revenues of individual customers. Recent research has explored using segmentation to model customer profitability, an approach that probably makes more sense for industries like food retailing (Libai et. al, 2002).

While the basic model for calculating CLV is straightforward, estimating of future revenues is complicated and sensitive to a wide range of influences that must be factored into the calculation of CLV. Beyond the basic CLV calculation, Hogan et. al (2002) discuss extending the CLV to incorporate such factors as the risk of individual customers, social effects such as word of mouth advertising, and competitive effects and other external events.

- ***Challenge #4: Maximize (not just measure) CLV.***

Research has shown that simply retaining customers is not enough since "downward migration" in the spending of retained customers can have a large impact on sales and presage customer defection (Coyles and Gokey, 2002). Therefore, calculating CLV is an ongoing challenge with frequent adjustments necessary based on observed changes in shopping behavior.

Our survey indicates that very few supermarkets are measuring customer lifetime value (CLV). The industry must not only understand this metric and the factors influencing it but must use the information to drive strategies.

The more important issue here is maximizing CLV. While accepting that 100% customer loyalty is not likely on a broad scale, supermarkets must strive to maximize CLV to ensure the greatest return on marketing investment (ROMI).

- ***Challenge #5: Align organization with customer equity management activities.***

Most supermarket companies today are not customer-focused organizations. At the point of customer contact, most supermarkets experience rapid employee turnover, especially amongst part-time employees. This creates a nearly untenable customer service situation: new, inexperienced employees in training mode are serving customers preventing customers from forming bonds or developing limiting trust, key drivers of loyalty. Likewise, the longer-term, experienced employees are constantly faced with training the new hires, limiting their customer contact opportunities and dampening their enthusiasm.

Bain & Co., examining dozens of companies across many industries, observed: "there is a cause-and-effect relationship between the two (customer loyalty and employee loyalty); it was impossible to maintain a loyal customer base without a base of loyal employees; and that the best employees preferred to work for companies that deliver the kind of superior value that builds customer loyalty (Reichheld, 1996)."

While the customer contact employee issue is a huge challenge for most supermarket companies, there is an equally dramatic shift necessary in the overall structure and culture of most supermarket companies to become customer driven. A recent study of 299 businesses determined that CRM success depends on an organization's "customer relating capability," which includes three components: *configuration*, *orientation*, and *information* (Day and Van den Bulte, 2002). Day and Van den Bulte assess the relative contribution of the three components in the following ways:

- "The *configuration* component, which incorporates the organizational structure, incentives and accountabilities, is overall the most important element of the customer relating capability."
- "The *orientation* component, comprising the mindset, values, and organizational priorities toward customer relationships, sets the leaders apart from the rest."
- "The information component, including databases and customer information system, contributes little to the overall capability once a minimum level of competency has been attained" (Day and Van den Bulte, 2002).

CRM is a comprehensive effort that extends beyond the limits of frequent shopper programs.

- ***Challenge #6: Respect the sensitivity of customer data.***

A participant in our focus groups succinctly captured the essence of the privacy issue when she said "Food is food. It's personal." Consumers may actually risk revealing more "sensitive" personal information through transactions with other businesses such as video rentals or casinos but grocery shopping is perceived as being perhaps more personal than most other transactions where personal information is required.

On top of the sensitive nature of grocery shopping is the growing fatigue and frustration consumers feel toward direct marketing efforts that clog their mailboxes and e-mail accounts each day. The general feeling expressed by our focus group participants is that these endless and sometimes off-target overtures simply add clutter to and steal precious time from their frenetic lifestyles.

- ***Challenge #7: Evolve the chairman from an efficiency tool to a service improvement tool.***

Bell et al. (2002) observed that "industry study The customer equity driven organization of the future will be differ from top to bottom from today's typical supermarket company organization. In fact, Rust, Zeithaml, and Lemon (2000) in their book "Driving Customer Equity" redefined CEO to mean Customer Equity Officer. The implications of the title change are more than semantic, with ripple effects throughout the organization that positions customer focus as the top priority.

With the senior executive charged with enhancing customer equity, the cultural changes that CRM involves for most supermarket companies will occur at a greatly accelerated pace. Supermarket chief executives must view CRM as the company's mission and the means to sales and profit growth rather than a marketing or IT initiative.

Section H. Summary and Strategic Perspectives

The supermarket industry has been developing customer relationship marketing (CRM) programs and strategies for over 15 years. At this point the impacts of CRM on the supermarket industry are mixed at best.

This study focused on identifying the current status of CRM programs at U.S. supermarket companies, on the role of CPGs in those programs, and the issues constraining the realization of full CRM benefits in the supermarket industry. This report also presents an overview of the future direction of CRM theory with perspectives on the supermarket industry. Key learning is summarized below with strategic implications indicated for the supermarket and CPG companies.

- Despite 15 years of development in the supermarket industry, over three-quarters of sales transacted with loyalty cards, and millions of dollars invested in technology and programs, customer loyalty has not been significantly increased because most consumers belong to multiple programs that offer mostly undifferentiated benefits.

- Despite the CRM premise that loyal customers are less price sensitive, contributing to their potential higher profitability, the major benefit offered by retailers and perceived by consumers in frequent shopper programs is price discounts.

- Although most companies have frequent shopper programs, the company cultures and organizational structures have not become customer-focused, thereby limiting the acceptance and success of CRM as a marketing strategy.

- Fast-paced lifestyles limit the appetite of most consumers for targeted marketing activities, generally, and, the efforts of supermarket and CPG companies, specifically, are perceived as intrusive for most consumers.

- Given the ubiquitous and undifferentiated state of frequent shopper programs in most market areas, there may be opportunities for retailers to break from reliance on price discounts and return to the basic tenets of CRM—creating customer-specific tactics that engender loyalty over the long term.

- Retailers report very positive results from their CRM Programs, including: increased transactions, shopping frequency, transaction size, overall sales, gross margin, net profit, and ROMI. However, some of these trends are counterintuitive, perhaps reflecting the misuse of price discounts and other tactics that undermine CRM's foundation.

- Marketing strategies have historically been difficult for retailers to measure due both to difficulty in controlling extraneous variables and inadequate analysis and testing procedures. However, measuring CRM effectiveness on an ongoing basis will be critical to convert the critics. Many researchers report that companies underestimate costs and achieve less than adequate ROI. The measurement of CRM effectiveness in the supermarket industry appears to be a rich area for further analysis.

- Retailers report that a high percentage of sales (86%) and transactions (72%) are captured with frequent shopper cards. This level of information coverage should provide tremendous learning about customers if the data is mined properly and people with analytical skills are available to interpret the information.

- While retailers predict that CRM's share of their total advertising and promotional effort will more than double to 38% in 5 years, that might not be soon enough nor of sufficient scale to convince the traditionalists in most companies that CRM is a viable strategy. Since traditional advertising and promotion strategies will most likely continue to run in parallel with CRM strategies, the battle lines will continue to be drawn in many organizations between those who believe in traditional advertising methods and those who see CRM as the future.

- As manufacturers continue to reduce trade spending while retailers continue to increase dependence on trade promotion dollars, CRM initiatives could be limited by the internal retailer tug of war over how trade funds are spent.

- The importance of customer service cannot be overemphasized in determining the success or failure of retailer CRM programs. All the technology and analytical skills in the world will not prevent poor customer service from driving customers to competitors. At the same time, the critical role of store employee turnover in the success or failure of customer service cannot be overemphasized. For most retailers, the customer service issue will not be resolved until employee turnover is controlled.

- While funding and technology are the most pervasive barriers to CRM realization, relieving those constraints will be meaningless if the cultural issues that plague most retailers are not resolved. Organizational and cultural issues will prevent the attraction and retention of sufficient people with the technical, analytical, and customer service skills needed at all levels of the organization to make CRM succeed.

- Consumer privacy appears to be a potential barrier that generally has been managed well by retailers. However, a growing and vocal privacy advocacy movement might influence a broader spectrum of consumer attitudes about loyalty programs. As retailers become more sophisticated with data mining and targeting the potential exists for more negative consumer reaction to such efforts driven both by privacy concerns and pure consumer fatigue with marketing overtures.

- CPGs must work closely with retailers to meet the needs of their shared customers. By sharing information, learning and resources, store loyalty and brand equity can be built simultaneously.

- According to leading academics and business visionaries, the future of CRM involves a dramatic shift in the identification and valuation of assets. Given the similarities in the physical assets such as locations, stores, products, and services across most retailers today, visionary retailers will realize that assets that will give them competitive advantage in the future are their customer relationships or customer equity. The time is now to begin the cultural shift that transforms retail companies into customer-centric organizations driven by the realization that customers are their only truly valuable assets.

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