

Customer Relationship Management

Target Marketing Best Practice Review

Competition for food basket share intensifies as new entrants, formats and concepts clash with the old order. Thirty-five percent of the average grocer's competition barely existed fifteen years ago. Non-conventional formats — only 27% of the market in 1980 — held a 77% share in 1995. Grocery marketers slice their targets into smaller, ever more precisely defined segments. Sharpshooting replaces yesterday's newspaper shotgun blasts as the weapon of choice. The war threatens to expand. Already, advance elements of the grocery elite skirmish fast food outlets for total stomach share.

Sharpshooting replaces yesterday's newspaper shotgun blasts as the weapon of choice.

<i>Format</i>	<i>1980</i>	<i>1990</i>	<i>1996</i>
Conventional	73	35	23
Superstore	18	34	42
Warehouse	4	13	8
Combo Food/Drug	4	13	20
Super WH	1	5	5

Growth in this complex marketplace increasingly requires the ability to target the best opportunities for converting potential shoppers — neighborhood by neighborhood — into regular customers through personalized customer management practices that are effectively communicated. In this new environment, a chain's

target marketing opportunities, procedures and needs can best be viewed against a backdrop of national trends.

The picture, nationally. In the broadest sense, grocery enjoys favorable business trends. At 35% market share, supermarket retailing is the largest non-durable trade channel. Since 1988 growth averaged 3.7% per year. Revenues in 1995 were \$410 Billion.

2.5%. In the 90's it has consistently hugged 2% — a 25% decline.

Chains invested heavily to increase the number of larger format stores (stores with 43% more square feet than conventional supermarkets) and increase the number of SKU's by 90%. The investment failed to expand sales.

— FROM —	— TO —
Major Growth Sales 7% in 1980's PreTax Profit in 2-3% range	Flat Growth 2% in 1990's PreTax Profit under 2%
Stable Channel Competition Drugstore Gasoline	Scrambled Channels Food, Photo, Promotional Food Mass Merchandisers
Conventional Formats 19,600 SF (selling) 11,000 SKU	New Formats DOMINATE 28,000 — 70,000 SF 21,000 — 50,000 SKU
Supply-Push Distribution	Demand-Pull Distribution
Traditional Demographics Customers of equal value	Growth of New Segments Top 30% do 77% of sales

This overall growth masks underlying trends detrimental to traditional formats.

Whereas grocery sales averaged a 7% annual increase in the 1980's, growth dropped to 2% for the first seven years of the 90's. Growth now averages 2%. Pre-tax profit in the 80's was

<i>Channel</i>	<i>1997 Share (%)</i>
Supermarkets	20.0
Dept/Discount Stores	17.3
Eat/Drink Places	15.7
Gas Stations	10.5
Specialty Apparel	7.8
Drug Stores	6.5
Liquor Stores	5.0
Other Gen Merchandise	3.9
Convenience Food	2.6
Variety Stores	2

"...reward loyalty to recapture the \$250 gold shoppers spend on monthly treks to a club store."

Customer Profiles

profile status	\$ per week	privilege level
A Diamond	100+	4
B Platinum	50-100	3
C Gold	20-50	2
D Silver	0-20	1
E New	--	1

Customer profiles drive Best Practice decision making. Market leader responses share a common trait. They focus on customer profiles to drive category management and merchandising decisions.

Not a band-aid, Customer Management requires fundamental change in corporate culture. *Everything* is subordinated to managing the enterprise's most valuable resource — its diamond clientele. In best practice operations, *every* management decision — inventory, deals, advertising, personnel policies, executive compensation, service — is driven by its effect on preferred customers.

A mere 362 customers generate 22.5% of the grocer's gross margin shown in the *Illustrative Overview* table. Together, 904 diamond and platinum shoppers produce 41% of the gross margin. This is known even though customer ID is captured for less than half the store's transactions.

If another 240 diamond customers are subsequently dug-out of the "other," unrecorded transactions — by rewarding shoppers to obtain and use courtesy cards — then a mere 600 customers will be known to contribute almost 40% of the gross margin.

Armed with this knowledge, best practice operators monitor the effect their actions have on preferred shoppers. What will it take, for example, to recapture the \$250 certain gold shoppers spend on their monthly trek to a club store? No one knows for sure. It varies from region to region. And, perhaps, from store to store.

But *Customer Movement* reports, such as those produced by the MicroNEX™ CRISP™ system identify when a particular promo-

Grocery stagnation has been blamed on various culprits — including fast food outlets. While the causes of stagnation are still uncertain, the leading candidate is "scrambled channels" with mass merchandisers stealing share with reduced price food items.

double coupons — while loyal customers fidget six deep to buy \$150 of 25% gross margin groceries.

Traditional solutions, such as asking for more manufacturer deals, fail because the same deals are available to mass merchants. Few perishables strategies succeed because supermarket losses to mass merchandisers have been in dry goods.

"Best Practice" operators are increasingly embracing Customer Management to:

- ▶ define customer profiles;
- ▶ assign each customer to a profile;
- ▶ reward most valuable customers by shifting rewards from least valuable customers; and,
- ▶ attract more diamond customers.

Market Segment Flux

Segment	Share (%)	
	1970	1997
Married	74	60
Never-Married	14	24
Ex-Married	12	17

A perverse form of target marketing has also contributed. Mass merchants target "diamond" shoppers — who endure herd-like conditions, limited selection, and \$25 membership fees for large savings. Supermarkets "target" cherry-pickers willing to buy 8-10 items at cost with express lanes and

Illustrative Overview of Customer Management

customer profile	no. of customers	----- weekly activity -----				percent of total					
		visits/ week	visits	average \$/ visit	total \$	gross margin \$	%	visits	sales	gross margin	
traditional (non-management) approach											
Other		5,768	38.56	222,414	52,490	23.6	100	100	100		
Total		5,768	38.56	222,414	52,490	23.6	100	100	100		
best practice approach											
P R O F I T E S	A diamond	362	1.74	629	75.71	47,597	11,804	24.8	10.9	21.4	22.5
	B platinum	542	1.23	669	60.50	40,479	9,836	24.3	11.6	18.2	18.7
	C gold	457	1.11	508	29.36	14,902	3,219	21.6	8.8	6.7	6.1
	D silver	451	0.79	358	10.57	3,781	620	16.4	6.2	1.7	1.2
	E new	453	1.15	519	40.27	20,907	4,955	23.7	9	9.4	9.4
	F other			3,086	30.70	94,748	22,055	23.3	53.5	42.6	42.0
	Total			5,768	38.56	222,414	52,490	23.6	100	100	100

tion succeeds in cutting club stores from gold customers' lives. Customer retention, transitions, losses, and additions by profile are compared to last year. For example, 67% of last year's platinum customers kept their platinum status; 13% moved-up to diamond status with higher purchases; and, 11% dropped to gold status. Gains and losses since last year are reported in the shaded area — 4% of all diamond customers quit, while 6% were recruited since last year.

Customer Movement													
percent movement by profile, this year versus last year													
customer profile	A diamond		B platinum		C gold		D silver		E new		% Total	number of members	
	Join	TY	LY	TY	LY	TY	LY	TY	LY	TY		LY	TY
retention & profile-to-profile transitions (%)													
A Diamond	72	13	23	7	9.8	2	5.2	5	8.3	6	124	314	390
B Platinum	14	8	67	8	6.4	6	8.9	7	6.6	5	102	552	562
C Gold	8	5.7	11	14	48	18	33	19	23	15	138	441	610
D Silver	2	0.8	4	2.7	16	8.6	38	14	8.9	18	77	819	631
E New								22		82	104	523	544
% Quit	4	5	21	36	33					Total		2,649	2,738
% Total LY	100	100	100	100	100					Change			3.3%

Overall, diamond customers increased from 314 to 390. The 13% of the platinum shoppers who moved-up constitute 23% of today's diamond shoppers. Similarly, 9.8% came from gold shoppers and 8.3% from last year's "new" shoppers.

Weekly Activity and Customer Management reports personalize the faceless "average shopper" traditionally used to base decision making. The actual number of preferred shoppers becomes quite manageable when wheat is separated from the chaff.

Personal contact, less costly and often more effective than mass advertising, becomes practical. Store managers learn the names and faces of their top 25 customers. Personal calls by store managers to 10 diamond shoppers each week increase near-term sales and boost long-term retention. Calling every diamond and platinum shopper who has not visited for 3 weeks has proven to cut defections by 25%.

One kiosk company activates the store manager's beeper when a "top 25" customer uses the kiosk so the customer can be personally greeted!

Best practice Customer Management cuts deeper than advertising and promotion. All services are revamped for "top" profiles.

MicroNEX's CRISP system, for example, integrates category and customer management as shown in the *Category Analysis by Customer Profile* report. In the week reported, diamond shoppers bought 42% of all baby food sold — and platinum shoppers bought 50% of all coffee. Platinum shoppers spent 2.63% of their shopping dollars on coffee, compared to only 0.9% for the average shopper — indicating coffee is of relatively high importance to platinum shoppers.

Category Analysis by Customer Profile																						
category sub. cat SKU	customer profile A (diamond)						customer profile B (platinum)						total									
	\$	percent (%) of			item count	\$	percent (%) of			item count	\$	percent of		item count	percent of							
		cat.	prfl	total			cat.	prfl	total			cat.	total		cat.	total						
baby food	4,724	42	0.9	0.4	3,913	43	2.6	0.70	3,149	28	4.2	.05	2,366	26	3.82	0.58	11,249	100	0.9	9,100	100	2.2
juice, dry	288	2.56	0.55	0.03	271	2.98	0.18	0.07	187	1.67	1.67	0.15	173	1.91	0.28	0.05	720	6.4	0	713	7.84	0.18
hnz apl, 6oz	16	0.15	0.03	0	14	0.16	0	0	8	0.08	0	0	7	0.08	0.02	0	41	3.7	0	39	4.29	0
coffee	2,771	28	0.52	0.22	712	20	0.48	0.17	4,948	50	2.63	0.39	1,673	47	2.70	0.41	9,897	100	0.8	3,560	100	0.9
tea	4,186	67	0.79	0.33	828	30	0.55	0.20	1,062	17	0.57	0.09	883	32	1.43	0.22	6,2490	100	0.5	2,761	100	0.7

More SKUs and higher service factors are assigned to categories important to diamond and platinum customers. Separate register prices are maintained for each profile. Deals are tailored to each profile.

Efficient, integrated credit sales at POS attract home shopping services, local non-profits, and other bulk business shoppers.

Best Practice ROI Review (for 5 store, 44 lane chain)				
	before		after*	
	- CRISP -		- CRISP -	
	\$ (000)	% of sales	\$ (000)	% of sales
Sales	60,000	100	67,680	100
Cost of Goods	45,360	75.6	51,166	75.6
Gross Margin	14,640	24.4	16,514	24.4
Operating Expense	13,440	22.4	13,912	20.6
PreTax	1,200	2.0	2,602	3.8

*Investment Required: \$554,042

Best practice operators use the reports¹ to continuously evaluate strategies to fund lower diamond and platinum effective gross margins by raising gold and silver gross margins, including:

- ▶ Straddling — shelf price higher, card price less than competitors.
- ▶ Convert Temporary Price Reductions to cardholder specials.
- ▶ Triple coupons for diamond, double coupons for platinum.
- ▶ Direct mail and kiosk coupons to diamond and platinum shoppers for items they individually buy.
- ▶ Automatically enter diamond shoppers in state lottery.

¹ Reports used in this paper to illustrate concept are static “snapshots” of key factors. Best practice reports by systems such as MicroNEX plot key factor rates-of-change using graphs and colors to highlight “out-of-trend” conditions.

- ▶ Targeted recipes, birthday presents, and “surprises.”
- ▶ Point systems, similar to airline frequent flier plans with ability to check status via PC or kiosk.

The reports provide the means and confidence to experiment with such alternatives to mass advertising² as:

- ▶ Home delivery of fliers.
- ▶ Partnering with local businesses, such as banks and auto dealers, to increase frequent shopper program outreach and excitement.
- ▶ Shopper recruitment drives in cooperation with local charities.

By focusing every action, every expenditure of resources on building residual value in loyal shoppers best practice operators grind down competitors who live from deal-to-deal.

Continuous market research is an invaluable customer management byproduct³ — with 100% sampling of real consumer response to services and promotions. One valuable use is “roll-out” — promotions that work for an entire demographic segment.

Best practice operators collect demographic data on diamond shoppers — do they have infants, pets, preteens; are they single, married, a working couple; what is their income, ethnic background. Demographic data is “crossed” with response data to identify potential roll-outs. Messages of previously proven

² A management consulting study by Strategy Partners Group found broad media coverage for a regional Baltimore, MD chain would cost \$7.8 million — significantly more than the \$1.8 million (0.8% of sales) advertising budget. Alternative, more effective, targeted advertising was designed for \$871,125!

³ The same study found traditional survey methods would cost \$3.6 million annually to produce data comparable to “free” customer management data.

effectiveness are communicated to the entire target group.

Technology under fire. The switch to target marketing puts traditional technology under fire. Legacy POS systems lack the ability to capture needed data — and the ability to react in realtime. Many headquarters systems lack data handling and analytical capabilities demanded by target marketing.

Early adaptors quickly recapture technology upgrade costs and build market share. As customer management becomes prevalent in a market, upgrading becomes a matter of survival and cost recapture increasingly difficult.

The management consulting firm, LogisTech, Inc. used ChainSym™ — software by EconoMetric that models the effect of advanced strategies on grocery chains — to estimate the impact of upgrading a small 5 store, 44 lane chain. Results are summarized in the *Best Practice ROI Review*.

Net income increased \$61,000 a month, from \$55,000 to \$116,000 per month. Projections assume that technology upgrades and procedural changes cost \$12,000 a month — based on \$550,000 of new POS hardware and MicroNEX CRISP chain management software.

To develop an economic model of your store or chain — or arrange a “best practices” return-on-investment analysis — call FMI at (561) 747-9450.

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