Customer Relationship Marketing

Building Customer Relationships for Enduring Profits in a Wired Economy

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I. Introducing Customer Relationship Marketing

Marketers started the new millennium in one of two groups: those who practice **Customer Relationship Marketing,** and those who do not. Those who do are reorganizing their marketing programs to create and strengthen brand loyalty. They put as much emphasis on retaining customers as they do on attracting customers. These same marketers are also abandoning the notion that advertising's job ends with the sale, that it's goal is to effect some "hands-off" at some cash register. They recognize that the sale is the beginning of an opportunity to create an enduring, profitable brand relationship with the customer.

Those who do not practice Customer Relationship Marketing (CRM) may not have to—yet. But they will. They will if they are to survive in this millennium, if they are to sustain profitable growth in the face of diminishing returns from the marketing waves that preceded CRM. There are three such waves, which, collectively, have driven marketing since World War II.

- **Mass marketing** fostered growth through economies of scale and efficiencies of reach, constructs as old as the Industrial Revolution kept relevant by the post-war boom in population and uninterrupted gains in discretionary income. Mass products and services were mass marketed and mass distributed to mass markets through mass advertising in mass media.

- **Targeted marketing** took over when mass marketers realized that all customers are not created equal. Focused marketing led not only to specialized products and specialized distribution but also to specialized media, audiences and messages.

- **Global marketing,** which many marketers use to this day, is essentially a hybrid that takes the targeted approach across geography instead of within geography. To achieve the economies of scale promised by mass marketing, marketers searched for common target markets worldwide. When marketers discovered, for example, that teenagers in Melbourne, Munich, and Manhattan shared a great deal in common, this represented great opportunities for such global brands as Levi's, Coca-Cola, McDonald's, and Doc Martens.

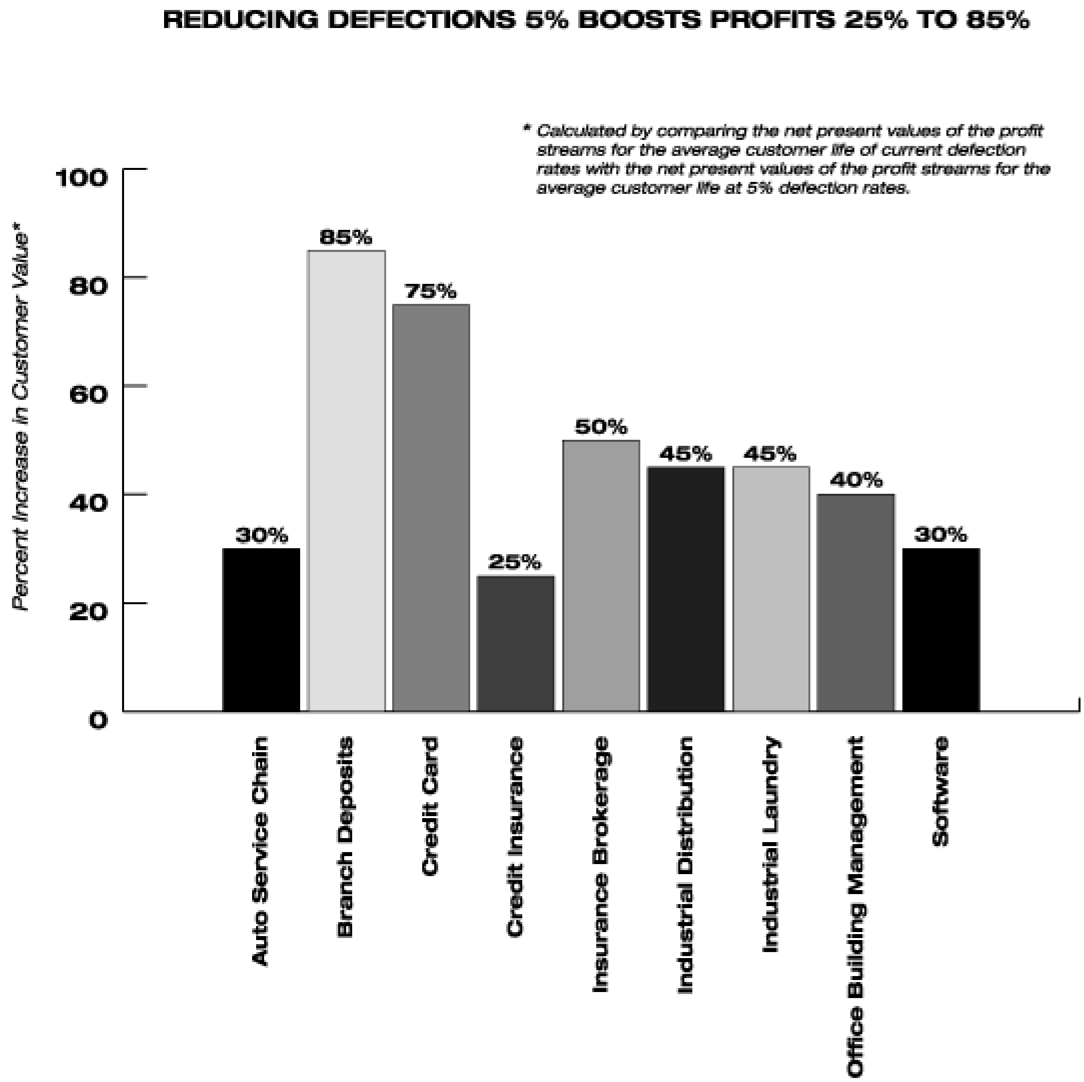
The first three marketing waves shared one thing in common. They focused on maximizing sales. The goals were to maximize sales in mass markets, targeted markets or global markets. Marketers are now discovering that it is unfortunately possible to increase sales without increasing profits. So, now marketers look at quality of share, not just quantity of share. Their objective is enduring profitable growth. The new marketing goal is to increase sales and to increase profits simultaneously. Marketers are beginning to appreciate that the basis for enduring profitable growth is the creation and reinforcement of building customer relationships.

II. Defining Customer Relationship Marketing

Customer Relationship Marketing is the fourth significant post-war wave. While marketers have long viewed brands as assets, the real asset is brand loyalty. A brand is not an asset. Brand loyalty is the asset. Without the loyalty of its customers, a brand is merely a trademark, an ownable, identifiable symbol with little value. With the loyalty of its customers, a brand is more than a trademark. A trademark identifies a product, a service, a corporation. A brand identifies a promise. A strong brand is a trustworthy, relevant, distinctive promise. It is more than a trademark. It is a trustmark of enormous value. Creating and increasing brand loyalty results in a corresponding increase in the value of the trustmark.

The new emphasis on building brand loyalty is encouraged by the fact that it costs four-to-six times more to convert a customer than it does to retain one. One study, conducted by Jagdish N. Sheth, specifically concluded that it "costs five times as much to replace a typical customer as it does to take actions that would have kept the customer in the first place."(1) After extensive research, the Technical Assistance Research Programs Institute (TARP) of the White House Office of Consumer Affairs observed that it costs significantly more to attract a customer than it does to retain one.(2) Slater and Narver observed that "Customer loyalty is extremely valuable because keeping a customer costs only about one-fifth as much as attracting a new one."(3)

As Frederick F. Reichheld and W. Earl Sasser Jr. conclude in their landmark study, "Zero Defections: Quality Comes to Services," the cost of forever chasing new customers instead of managing the loyalty of existing ones exacts an underappreciated but overwhelming toll. "Customer defections have a surprisingly powerful impact on the bottom line," the authors write. Loyalty can have more to do with a company's profits than "scale, market share, unit costs, and many other factors usually associated with competitive advantage. As a customer's relationship with the company lengthens, profits rise. And not just a little. Companies can boost profits by almost 100 percent by retaining just 5 percent more of their customers"(4)



The authors support this general thesis with a barrage of industry specifics: "Reducing defections by just 5 percent generated 85 percent more profits in one bank's branch system, 50 percent more in an insurance brokerage, and 30 percent more in an auto-service chain. [Credit-card company] MBNA America has found that a 5 percent improvement in defection rates increases its average customer value by more than 125 percent." This is the profitable by-product of creating and strengthening brand loyalty. (5)

In their book, *Managing to Keep the Customer*, Desatnick and Detzel ask us to consider the dollars associated with a lifetime of customer loyalty. They indicate that in the automobile industry a lifetime loyal customer is worth an average revenue of $140,000. In appliance manufacturing, a lifetime loyal customer is worth more than $2,800. The local supermarket gains around $4,400 each year from loyal customers. (6)

Building brand loyalty is the most effective way to achieve enduring profitable growth. Business must evolve from a transaction mentality to a relationship mentality, from focusing only on customer acquisition and conquests to focusing on customer retention and loyalty. The brand loyal customer is our best customer. We must know how to identify, attract, defend and strengthen brand loyalty.

Customer Relationship Marketing recognizes that it is not enough to attract buyers. The CRM goal is to convert buyers into loyalists and loyalists into enthusiasts/evangelists.

THE LOYALTY LADDER

For brands whose bad reputations result not in loyalty but in rejection or worse, the challenge is to neutralize *brand terrorists*, a disloyal group defined by Heskett, et al, in “Putting the Service-Profit Chain to Work” as “customers so unhappy that they speak out against a poorly delivered service (or product) at every opportunity.”(7) Brand terrorists so relish their mission that their fervor often outlives the source of their enmity. For confirmation, one need only spend a transcontinental flight seated next to a former frequent flyer of the formerly defunct Pan Am.

This loyalty ladder is the heart of CRM. Customer Relationship Marketers focus their resources on moving their customers up the loyalty ladder. This new view of marketing is not merely a better way to practice marketing; it will require fundamental changes in marketing practice.

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III. The Customer Relationship Marketing Revolution

Customer Relationship Marketing is not about an evolution of marketing thought. CRM is a genuine revolution in how marketers manage their brands. Each marketing wave has been swelled by its own agents of change. The development of network TV helped mass marketers like Procter & Gamble affect the lives of more Americans more deeply than any post-war politician or fiery brand of ideologue. The combination of the Internet and the untapped potential for interactivity will affect the future still more. Although these *facilitators* seldom render their predecessors obsolete, they always recast marketing priorities.

In addition to network TV, which complemented rather than supplanted network radio, America's **mass-marketing wave** was facilitated by department stores and supermarket chains—themselves the product of accelerated delivery systems—and by patent-protecting legislation for national brands. **Targeted marketing** got a boost from the demographic fractionization of the "Me Generation," from FM radio, specialty magazines, the birth of cable TV and other fragmented media, and from a retail revolution in which malls, filled with specialty stores, challenged department-store dominance. **Global marketing's** facilitators include legislation like NAFTA, the development of a European Economic Union, the increased reliance on global manufacturing, the growing interdependency of financial markets, the increasing accessibility and popularity of international travel, the development of international media, and the advent of the satellite dish, which allows anybody anywhere to pick off programming that isolationists previously contained.

The facilitators of **Customer Relationship Marketing** will make earlier agents of change look inadequate. The key facilitator is technology available to marketers. CRM weds the individual customer and technology in ways that are unique. These fourth-wave relationships, propelled by a confluence of technological advances, will themselves change at geometric rates.

"Every twenty years since 1900 the amount of computational power—machine brainpower—that can be bought with one dollar has increased by a factor of a thousand. That's more than a million-fold increase just since 1950," report Don Peppers and Dr. Martha Rogers in their book, *The One to One Future*. "Put another way, for what it cost a 1950 marketer to keep track of all the individual purchases and transactions of a single customer, today's marketer can track the individual purchases and transactions of several million individual customers, one at a time."(8)

Databases have made **one-to-one marketing** a reality. Scanner technology, currently in over 80 percent of food stores, is reducing the relevant market segment to a single household. **Database marketing** is the new marketing imperative. *Reader's Digest* recognizes that their real asset is their extraordinary database.(9) Seagram's uses its list of 10 million adults to launch new products and to build brand loyalty.(10) **Integrated marketing**, by removing conflicting communications signals, puts all forms of commercial persuasion about a brand on the same reinforcing track. Nestle's provides rest-stop structures alongside the highway where parents can feed and change their baby. Marketing Director Fabienne Petit says *Le Relais Bebe* "is a genuine showcase of brand image."(11) **Interactivity**, whether by phone, real-time, chat, email, fax or remote has made two-way communication a reality. **Relationship marketing** is rapidly replacing the monologue of old-fashioned marketing with the dialogue of genuine brand relationship-building programs. The Charles Schwab & Co. discount brokerage provides trading software packages and was the first to offer 24-hour service combined with an 800 number.(12)

The CRM model accommodates—solicits, really—customer feedback. Its practitioners rely on such tools as customer satisfaction research, 800 numbers, listening posts, response coupons, warranty cards, online surveys and questionnaires. All, however, are in the service of the same goal—building brand loyalty. All of these developments are part of the overarching Fourth Wave of Customer Relationship Marketing.

IV. Breaking From Tradition

Marketers who join the Fourth Wave stand to learn as much about their marketing as they do about their customers. Brand Loyalty will expose the folly of earlier ways and the misconceptions of earlier waves. Certain to succumb to this scrutiny is AIDA—the most dominant model of how advertising supposedly works.

AIDA, an acronym for Awareness, Interest, Desire and Action, theorizes that advertising's role is to create **awareness** of a brand, which over time generates **interest** in trying it, which is eventually transformed into **desire**, which builds and builds until, finally, the consumer is moved to **action**. Here the AIDA sequence ends and, with it, the role assigned to advertising also ends.

The problem with psychological cakewalk is that, while it makes sense in theory, it explains less than half of the reality. AIDA focuses only on the attitudes that lead to the purchase behavior and fails to recognize the significant value of the attitudes that follow behavior. Studies demonstrate again and again that the *reinforcement* effect of the advertising that follows the sale is at least as important as the effect of the advertising that led to the sale. Research on advertising effectiveness consistently demonstrates that advertising not only generates trial it also reinforces brand loyalty. As the "How Advertising Works" study by Information Resources, Inc., concluded after analyzing 400 brands over eight years, higher advertising budgets increased loyalty in existing customers more than they generated trial from new customers.(13)

The difference in advertising's effect on the two groups, which provide growth either through increased frequency or through increased penetration, is as profound as it is significant. For the average successful brand, only 30 percent of the sales increases attributed to a higher level of advertising came from new customers. The remaining 70 percent came from existing customers who, because of the increased advertising, moved a rung or two up the brand's loyalty ladder. Specifically, the IRI study's average brand posted a year-to-year sales increase in business from increased frequency (existing customers) of 14 percent, compared with an increase attributable to increased penetration (new customers) of 6 percent.(14)

This suggests that followers of AIDA, by overlooking the reinforcement role of advertising, fail to capture more than two-thirds of advertising's effectiveness. It is an oversight, to be sure, but it may not have been so glaring in the world before CRM. That is because demand exceeded supply throughout much of America's mass-marketing wave. In the post-war period, as the economy strained with pent-up demand, what got sold got sold. That condition most definitely suspended the need for the reinforcement of one's purchase decision. The marketing theme was "Build awareness" and they will come. Get them to try and our job is done."

Even with target marketing, advertising's job was, simply, to create awareness, to inform a newly defined segment of a newly customized benefit. It was the sort of job the AIDA model, with its awareness-leads-to-action claim, appeared to explain. And with global marketing, again the AIDA practitioners say the goal is to build awareness and get trial.

Not so. Today, the AIDA model is recognized as twice flawed; it not only ignores the reinforcement role of advertising but assumes, erroneously so, that a successful trial repeats itself. This assumption, like AIDA itself, makes sense in theory—*recognition* or *recall* of a brand's advertising (awareness) leads to an *attitude* (interest and desire), which induces *trial behavior* (action), when successful, produces *repeat behavior*. It is a convincing chain of consumer behavior often summed up as: "I think (about the brand), therefore I do (buy or try)."

While attitude change can lead to behavior change, the most significant attitude change often follows, not precedes, the behavior change. In discussing models like AIDA, Kristian Palda observed, "There is no good evidence that such changes in awareness precede rather than follow purchase."(15) Alan C. Middleton and John Dalla Costa explain in *Advertising Works*: "If there is low involvement then there may not be enough interest to generate an attitude before trial behavior; i.e., there may be an acceptance of very general information without the formation of an attitude. In this event…the process my be: I do (buy or try), therefore I am (thinking about the brand)."(16) Michael Ray, of Stanford Business School, presenting at a Marketing Science Institute Conference, observed that, "The learning hierarchy of effects fits only a minority of situations."(17) Yet, this theory, which, at best, fits only the exceptions, still persists as the conventional wisdom of how marketing, in general, and advertising, in particular, works in most situations.

As consumer psychologists know, the customer's attitude is often shaped more after trial than before trial. The need for reinforcement is such that the most avid readers of a travel advertisement are travelers who recently returned for the advertised destination. Giep Franzen of the Netherlands reported, "Advertising confirms and reinforces the consumer's own perception of usage experience."(18) His review of hundreds of cases shows that users of a brand are the number one group of people that attend to and are the most affected by an advertising exposure. Why? They are seeking reinforcement of the wisdom of their behavior.

While models like AIDA seem to make so much common sense, Leon Festinger, a renowned psychologist, once observed that "The few relevant studies certainly show that this 'obvious' relationship between attitude change and subsequent behavior does not exist."(19) We must reject the funnel-vision view of marketing and replace it with the up-to-date Customer Relationship Marketing view.

CRM VIEW OF HOW ADVERTISING REALLY WORKS

As behavioral psychologists know, attitudes do not predict behavior as well as behavior predicts attitudes. This revision dramatically reshuffles the AIDA chain. For market researchers, this change has major implications. Attitudes are much better at explaining behavior than they are at predicting behavior. Psychologists tell us that consumers actually observe their behavior and then develop attitudes and beliefs consistent with their behavior. In other words, *awareness* does not normally lead to committed *attitudes* but to a tentative *expectation* leading to *trial*. The *trial* experience then becomes a determinant of *attitude*. Marketing, including advertising, then reinforces this attitude. The reinforced *attitude*, if sufficiently positive, leads to an increased probability of *repeat behavior*. With further reinforcement, the repeat behavior leads to *beliefs* and with more reinforcement leads to *loyal behavior*. Marketing plays a significant role, not only in generating the initial awareness and trial but also in moving customers from triers to repeaters to loyalists. Advertising also plays an important role in building brand loyalty. Yet, this role of advertising is too often ignored.

The reinforcement role of advertising is particularly important. Andrew Ehrenberg of the London Business School has studied hundreds of brands and has published widely on this subject. His conclusion is that "Advertising reinforces consumer behaviors by reducing cognitive dissonance, increasing brand satisfaction, and rekindling brand awareness."(20)

What is key about this new Customer Relationship Marketing view is that it does not assume, As AIDA assumes, that nothing stands between *trial behavior* and *repeat behavior*. In the revised version, *attitudes and beliefs* stand between the two, and these feelings, as Frederick F. Reichheld determines in "Loyalty-Based Management," are at best fickle and complicated beast.(21)

"Between 65 and 85 percent of customers who defect say they were satisfied or very satisfied with their former supplier," Reichheld writes of one business-to-business study. Even in the auto industry, a high-involvement category if ever there was one (thus given more to "I think, therefore I do" behavior), Reichheld discovered the most damning evidence imaginable against the AIDA legacy. Repurchase rates averaged only 40 percent—even though satisfaction scores ranged between 85 percent and 95 percent.(22)

What does that mean? Is marketing so intrusive, misguided and destructive it sends more than half of those who otherwise satisfied with a brand scurrying to competitors? Or are customers so capricious, inattentive and unmoved by marketing gestures they reward a supplier with repeat business—even when they are completely satisfied—less than half the time? The answer is, fortunately, is neither.

To create, nurture, defend, strengthen brand loyalty, attitudes following purchase behavior must be reinforced. Reinforcement of brand-loyal behavior is an ongoing, year-in, year-out responsibility. Customer-loyalty studies corroborate the importance of the reinforcement role of advertising that the traditional view of advertising has ignored. More specifically, these studies expose how misguided this view is in the case of low-involvement categories and how misleading it can be in the case of high-involvement categories.

Benefiting from such insights—whether intuitive or counter-intuitive—Customer Relationship Marketing reconciles marketing theory and marketing reality. Doing so, however, requires that marketers not only appreciate the importance of winning customer loyalty but also of reinforcing it through a loyalty loop that traditional (and outdated) marketing models lack.

Marketers are appreciating the enormous importance of creating and reinforcing brand loyalty. They respect and cherish the brand relationship with loyalists. Ford used Mustang Club members to actually help in redesigning the new Mustang launched in 1994. Then they asked these same members to help participate in the brand launch.(23)

CRM applies to the new brands, too. How you create a brand from the start set the stage for building future loyalty. Attract new customers based on a deal and expect customers who are deal loyal not brand loyal. Saturn launched their brand with a policy of "no haggle" pricing. Their advertising focused on building and reinforcing brand equity from the start.(24) Their promotional events as well as their advertising are designed to create and reinforce an enduring brand bond with their customers. Sears, J.C. Penney, and Nieman

Marcus have special discounts and services designated for frequent shoppers.(25) McDonald's is focusing its marketing attention on the SHU's (super-heavy users) who eat at McDonald's an average of three to five times per week and account for 77 percent of sales.(26)

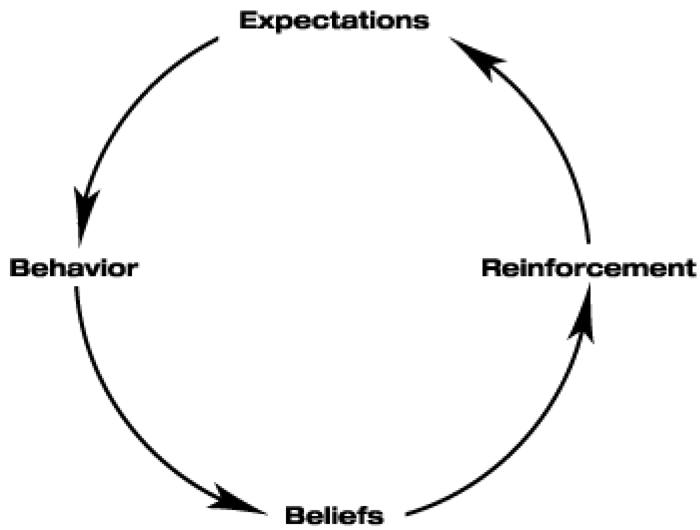
V. Getting Loyalty Into The Loop

Marketers worldwide recognize that quality is critical to brand success. However, marketers are only beginning to appreciate that marketing affects the perception of quality. A quality brand is more than a quality product. A quality brand relationship is more than just an outcome of product and service performance. A quality brand is a quality product and/or service marketed in a quality manner.

Advertising helps to build a quality expectation. Advertising reinforces a quality experience. Advertising helps to reinforce the quality beliefs that follow the experience. Bradley Gale, in his book, *Managing Customer Value*, reports on some research on the renowned PIMS (Profit Impact of Marketing Strategies) database. He states, "We've shown that advertising usually improves relative perceived quality and, by doing so, increases profitability."(27) Max Blackston, also examining the PIMS data, reported that there was a significant positive relationship between advertising expenditures and product quality ratings. He demonstrated that businesses with advertising-to-sales ratios exceeding competitors receive higher relative quality ratings.(28)

Practitioners of CRM actually reorganize their marketing efforts around a **loyalty loop**—a feedback loop that reinforces their relationship with carefully targeted customers. In doing so, marketing communications are transformed from a one-way blast into two-way discussion. To quote Joel Rubinson, the chief research officer of The NPD Group, brand loyalty is "the DNA of marketing."(29) Unraveling the many mysteries of this metaphorical DNA requires marketers to segment customers by the nature of their loyalty. Unlike consumer-behavior models that have misguided marketers since the 1950s, Customer Relationship Marketers distinguish between customers who habitually betray a category's brands and those who are brand loyal. Only then can they be sure of reinforcing customer relationships in a way that elicits just the right *attitude* from just the right customer groups.

THE LOYALTY LOOP



According to Allan Baldinger, Vice President of The NPD Group, in "Scanner Data and Strategy, a research paper, "Loyalty drives market share." This examination of scanner data also pointed to the role loyalty plays in helping brands remain inelastic to price fluctuations. As Baldinger puts it, " A loyal customer, all else being equal, will be less likely to switch away to your competitor based on the price appeal of your competitor." The data go on to reveal that loyal customers are willing to pay more for your brand. This study showed that the more loyal customers are the higher the average price they will pay for your brand.(30)

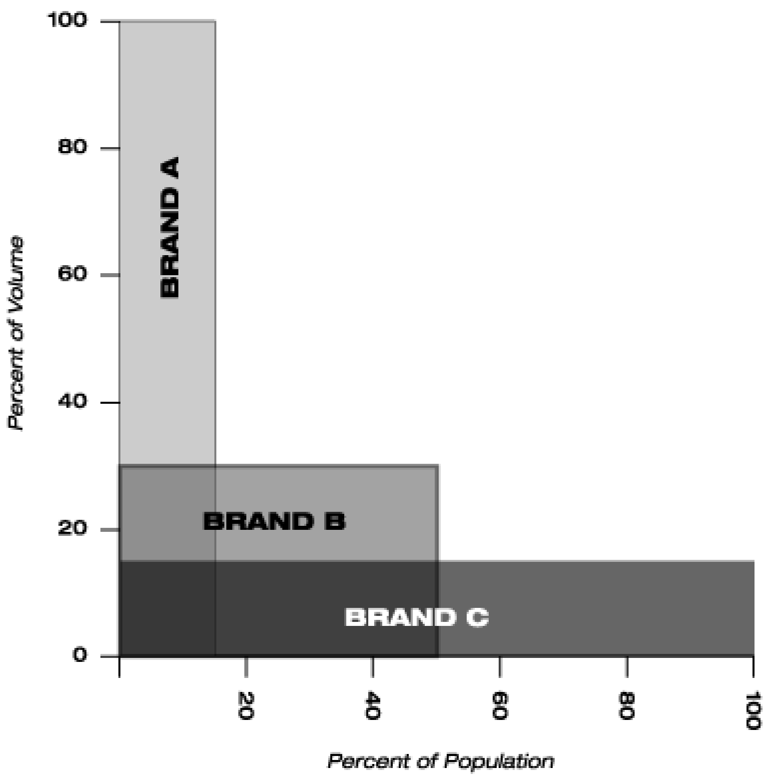
Josh McQueen, of the Leo Burnett Company, has also studied the profitability of brand loyalty. McQueen concluded that the more loyal groups pay higher relative prices while the less loyal groups "are more influenced by relative price and short-term deals."(31) Creating brand loyal customers and moving them up the loyalty ladder is a key element in business success. Increasing brand loyalty drives business profitability.

So much for the easy part. The hard part is implementation. As Reichheld puts it in *Loyalty-Based Management:* "Creating a loyalty-based system in any company requires a radical departure from traditional business thinking. It puts creating customer value—not maximizing profits and shareholder value—at the center of business strategy, and it demands significant changes in business practice." He goes on to say that, "While senior executives may be daunted by the time and investment required to engineer an entire business system for high retention, they may have no alternative. *Customer loyalty appears to be the only way to achieve sustainably superior profits.*"(32)

VI. Measuring Loyalty

Just as customers are not all created equal, neither are market shares—not even *equal* market shares. Consider, for example, the following cases, each with a 15 percent share. Brand A gets its share by inducing the entire user populations to buy its product 15 percent of the time. At the other extreme, Brand B gets its share by inducing 15 percent of the user population to buy its product all the time any by leaving the remainder of the population to other brands. Its narrow but extremely loyal customer base consists entirely of brand enthusiasts. Brand C represents the perfect compromise: half of the population buys its product 30 percent of the time and the other half never does. Each of these three brands have equal shares of 15 percent, but they will have unequal profitability.

EQUAL SHARES-UNEQUAL PROFITABILITY



Marketers who embark on such explorations quickly learn the old 20/80 rule (20 percent of customers account for 80 percent of sales) is dangerously inadequate. It is common for marketers to define their biggest customers as their best customers. This is not necessarily the case. We must also consider brand loyalty. According to a study by MRCA Information Services, presented by its Chief Executive David Learner, identification of a brand’s heavy users is not enough. It is not even close when, in case after case, category after category, an extraordinary share of sales can be traced to a tiny share of *loyal heavy users*.

Here are a few examples: For one brand, MRCA found that 5.8 percent of users accounted for 77.5 percent of volume. For another, 9.8 percent of users accounted for 75.1 percent of volume. And in a third buy by no means unique case, less than 1 percent of users accounted for 53.1 percent of volume. It is not enough to know who the heavy users are. The core of a brand's profitability rests with the core customer, the brand-loyal heavy user.(33)

The Four Pillars of CRM

These are the Four Pillars of Customer Relationship Marketing: Knowing how to **identify, attract, defend** and **strengthen** brand loyalty is the new marketing imperative. William Moran, in a paper on brand loyalty and advertising performance concluded that, "Loyalty is the key ingredient of brand equity and to the brand's future marketing profitability." He also points out that, "Your core customers are you key target." Furthermore, while advertising can change non-user attitudes, "The most important task of advertising is to affirm and reinforce its core customers' existing convictions about the brand. Non-users will be tempted more by price incentives than by advertising. Then, the brand experience itself will be the most effective attitude-changer for them. After that, it is advertising's job to articulate for them the reasons why they find the brand attractive." Finally, he concludes that, "The job of advertising is to build and harden the core."(34)

Such observations invariably galvanize marketers, as well they should, to determine the **Value Of A Customer (VOAC)**. Indeed, if the heart of CRM is customer loyalty, then its brain is VOAC. The Campbell Soup Co. learned as much from a study several years ago that evaluated marketing-expenditure efficiency, identified waste factors and put a price tag on its most valuable consumers. Although parts of the study remain proprietary, Kathleen MacDonnell, the former President of Campbell's frozen-foods group, shared one brand's results.

The study began with Campbell's using scanner data to segment brand buyers into four consumer groups: *most profitable, profitable, borderline* and *avoid*. Thus, the company learned that only 4 percent of brand users fell into the *most profitable* group, which in turn accounted for only 15 percent of sales volume. No matter, for Campbell's also learned its *most profitable* group delivered three times the profit of the breakeven *borderline* group. The second-most *profitable* group accounted for another 6 percent of the user total and only 9 percent of the volume.

That meant all of the brand's profits came from a mere 10 percent of its customer base. At the other extreme, 65 percent of brand users fell into the unprofitable *avoid* group and accounted for 51 percent of the sales volume. This group more than lived up to its name by returning only 38 cents on every marketing dollar spent to reach them. "The research into one specific brand showed that during the past two years, 60 percent of our marketing dollars were wasted. So were 63 percent of trade promotion spending and 95 percent of advertising and media spending. That meant that out of a $33 million marketing budget, over $20 million would have been better off unspent."(35)

MacDonnell later elaborated on the results at an Advertising Research Foundation workshop: "On an EBIT {earnings before interest and tax] per household basis, (the *most profitable* group) calculates to $3.38 return on marketing investment versus only $1.00 for the *borderline* group. Furthermore, the *most profitable* group tends to pay more for your product, buys less frequently on deal and is very positively disposed towards your brand…The *most profitable* group is (also) most highly susceptible to advertising and consumer promotion, especially multiple purchase incentives. Trade promotions, or cents-off deals, are not cost effective with this group because you are only subsidizing their planned purchases."(36)

VII. Getting The Right Mix

We do not mean that advertising and promotion have to be at loggerheads. But it does underscore the importance of keeping the two in concert, not in conflict. As seminal studies by Bob Prentice throughout the 1980s show, there is a need to be assured that the two are in the proper balance.

"I had been classifying expenditures in the traditional advertising versus promotion split, " Prentice admitted, adding that the determinant of this erroneous yet universally accepted classification hinged on whether the media choice was commissionable or not. "But certain promotions that work like advertising , if executed properly, also can implant ideas about a brand's unique attributes…but only if the brand's unique advertising message is effectively delivered with the sample of cut-price coupon.

"This is an important distinction," Prentice went on. Hence the Consumer Franchise Building (CFB) concept that Prentice came up with to unlock the secrets of brand performance. "I decided to classify marketing activities by whether they registered a brand's *unique* advantages or attributes in the consumer's mind or simply offered a *non-unique* incentive (for example a price cut)," he explained.

So it was that, in Prentice's world, all marketing activities were deemed either CFB (Consumer Franchise Building) or non-CFB. Advertising and select promotions contributed to the former; price-off couponing, multi-brand vehicles, including free-standing inserts, as well as sweepstakes and other extraneous incentives made up the latter. This distinction allowed Prentice to calculate what he called the CFB Ratio: the percentage of CFB expenditures to the CFB and non-CFB total. He then examined the 10-year profit performance of more than 20 packaged-goods brands, which revealed, to a startling degree, the "same general relationship."

When a brand's CFB Ratio fell below 50 to 55 percent," he said, referring to those instances when less than half of a brand's marketing budget went toward building its franchise, "profits almost always declined, either immediately or within two years."

Prentice could not help extending his research to areas other than packaged goods, where, with modest qualification, he found the "same general relationship" for 45 case histories. The qualification was that in "some commodity-type categories, with little brand differentiation and heavy trade- and price-dealing," sometimes "profits did not begin to drop until the CFB Ratio fell below 30 to 35 percent."

His overall conclusion, however, was without qualification: “The CFB Ratio danger-point seems to vary somewhat by product category, but there is a danger point.” Averaging across all of Prentice’s 65 brands, we observe an average “danger point” in the range of 40 to 45 percent. Prentice derived what he would call the *CFB Calculated Franchise Formula* after reasoning that CFB expenditures, such as an ad campaign, ought to leave impressions that persist for four years while non-CFB expenditures serve primarily as an immediate sales incentive with little lasting effect. While on the surface this calculation may seem like an oversimplification, the CFB concept proved to be as predictive as it was instructive.

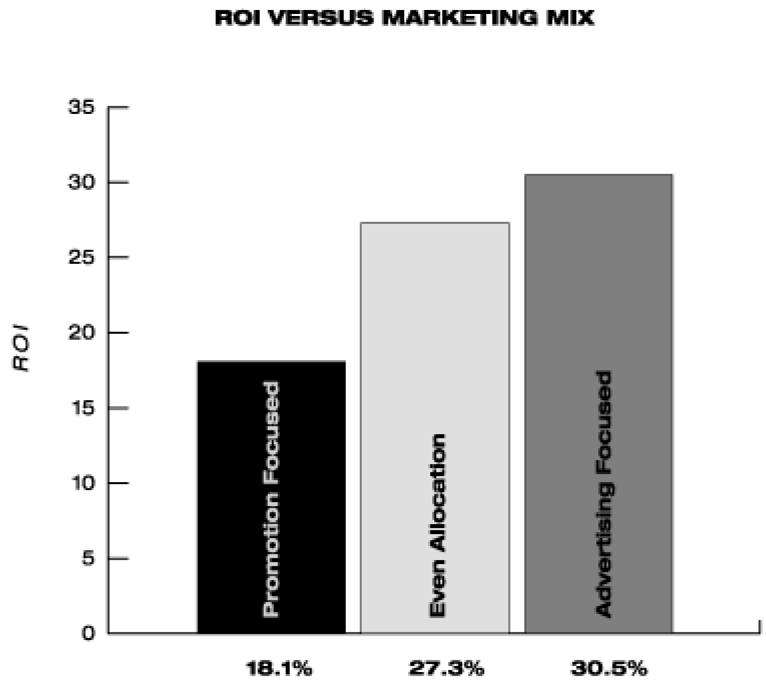
A statistical analysis of 45 case histories, each averaging eight years, revealed that there is an 80 to 96 percent correlation between shares of CFB and non-CFB spending and actual market share.(37)

You Get What You Pay For

Several important studies address the critical issue of market resource allocation. First let us look at the relationship between advertising weight and business results. Max Blackston reports that there is a positive relationship between advertising and market share. Businesses with advertising-to-sales ratios higher than their competition achieve shares averaging 28 percent higher than their competitors. Furthermore, there is a positive correlation between advertising and profitability. “Brands with much higher A:S ratios versus competitors earn a rate of return 45 percent higher than those with A:S equal to competitors.” And, “Those with much lower A:S ratios earn returns that are 22 percent lower.”(38) The conclusion is clear. You get what you pay for.

Getting the marketing mix right matters. How much you spend matters. Howe you allocate what you spend matters, too. Returning to Bradley Gale’s research of PIMS data, he states that the long-run result of promotions is likely to be a decline in profitability. “We found that the average return on investment for promotionally oriented businesses (with about two-thirds of their advertising and promotion budget spent on promotions) 18.1 percent. The average ROI for those that split their advertising and promotion budget about evenly was 27.3 percent. And, the average for advertising-oriented businesses (with approximately two-thirds of the budget allocated to advertising) was 30.5 percent.(39)

Alexander Biel stated, in a presentation to the Advertising Research Foundation, “it is clear that there is a positive relationship between the emphasis on investment in advertising and profitability. Those businesses that allocate most of their budgets to promotion tend to have lower profit margins.”(40)



Larry Light has confirmed this same pattern in further research. He also found a correlation between market resource allocation and market rank. He found that if a marketer's advertising ratio (Adv./(Adv.+Promo.) falls below 40 percent, then the marketer can expect to be a follower and achieve the profits associated with a follower rather than a leader. Act like a follower, expect the results of a follower. It takes money to become a market leader. It takes money to stay a profitable leader.(41)

VIII. Righting Marketing Wrongs

The customer is our boss. Marketers have been mouthing this sentiment since World War II, but has it ever been true? Certainly not in the age of mass marketing, when mass production fed mass brands to a mass audience reached by mass media. For almost two decades after the war, customers were but homogenous blurs behind cash registers. They would remain invisible as individuals as long as their collective demand for goods and services, fueled by uninterrupted gains in discretionary income, exceeded whatever marketers could supply.

In the age of targeted marketing, customers assumed more respect but in no way called the shots. They were corralled into groups instead of being addressed *en masse*, the particular segment of each determined by something as objective as demographics (for example, women, 18-to-34) or as subjective as psychographics (emulators, strugglers, achievers or experiencers). This let to specialized products, fragmented media and tailored commercial messages. But in no way did its customization resemble the *customerization* that customers truly deserve.

The age of global marketing, which prevails to this day, simply combines the economies of mass with the focus of segments. It is seductive in that it promises the benefits of tow apparently conflicting worlds—mass marketing and targeted marketing. But, with all these developments in marketing thought, sales often go up without commensurate profit increases. Why?

Customer Relationship Marketing holds the key! CRM says the sale is not the goal. Enduring, profitable growth is the goal. The job of marketing does not end with the sale. The sale is the beginning of the opportunity to turn a purchaser into a loyalist. Marketing today is entering its brand-loyalty stage, because customer-relationship marketing, and only customer-relationship marketing, can deliver enduring, profitable growth.

Even the most entrenched of mass marketers is heeding the call. Durk Jager, the Procter & Gamble President and CEO, told *Advertising Age* in a Question and Answer session that the media's obsession with EDLP (every day low pricing) in many ways misses the point. "It is a *different* use of pricing," he asserted. "We take money away from…temporary price reductions, big features, half-price sales—which appeal to people who have no propensity to be loyal. Their motivation to buy a brand is to have a price reduction or a coupon."(42)

The numbers support Jager's assertion. Although P&G's list prices, taken cumulatively, were down the equivalent of $1.6 billion at the time of the interview, Jager noted that $1.2 billion of that amount "comes out of other pricing elements—like coupons, allowances, refunds. You can redirect money to a loyal user base and reward them for their loyalty," he continued. "In essence, you take money away from people who are not loyal. That shift is the fundamental issue of value pricing as it relates to the consumer. It's a loyalty-building device."(43)

But that is just for starters. CRM is much more than better, smarter, and fairer pricing. It is changing what marketers do, not improving what they do. It is a new way of doing business, not just a new way of marketing. It is not business as usual but business *not* as usual. Customer Relationship Marketers are not just waking up to this fact; they are already acting on it. Every aspect of an organization must be reconsidered, retooled, even reorganized—a process that, as P&G's Jager knows well, can be as painful as it is productive.

"There's been no point in P&G's history in which more fundamental changes have been brought about," he concluded in his *Ad Age* interview. "I'll just give you some organizational things: the change to category management—a profound impact on the total company and its focus on categories of business. The changes we have made in the structure of the sales force—the move away from a geographic orientation to one that has a customer orientation. That's a change of enormous magnitude. The change in our plant restructuring. The change in pricing and promotion. This kind of change has never happened—the kind of changes that we've brought about to get consumer loyalty back and strengthen our brands. It's never happened to this magnitude."(44)

In other words, branding policy has become business policy. Behind all the change is the realization that creating, nurturing and reinforcing brand loyalty is the only way to ensure enduring, profitable growth. That is the maxim behind CRM. That is why marketing's New Wave is, in many ways, the first wave where marketing truly matters. It is the first wave where marketing does not focus on mere awareness or on attitudes as the goals; it is the first wave that does not focus on the sales as the goal; it is the first wave that does focus on enduring, profitable growth. Knowing, serving and indulging one's best customers no longer conflicts with widening profitable growth as the goal. Frequent-flyer, frequent-visitor, frequent-buyer, programs are a regular fact of CRM life. Brand Loyalty Marketers know that it is better to reward brand loyalty than to exploit brand loyalty while diverting resources in trying to attract the indifferent. Knowing, serving and indulging one's loyal customers is the best way to serve consumers and it is the best way to serve shareholders.

The Customer Relationship Marketing model, unlike its predecessors, steers marketers and their customers into a mutually beneficial dialogue. The marketer proposes; the customer disposes. And it is more than coincidental that the latter has always been the privilege of a boss.

IX. The Basics Of Customer Relationship Marketing

Building brand loyalty is the only basis for enduring, profitable growth.

Customer Relationship Marketing has many implications for market planning, employee training, advertising, promotion, public relations, direct marketing, package design, and so on. Customer Relationship Marketing requires us to refocus our attention on the economic value of brands. CRM demands that we consider the price of brand exploitation versus the benefits of brand building. The Customer Relationship Marketer's goal is to win and keep brand loyal customers. Building enduring, profitable, growing brands is all about creating, nurturing, defending and strengthening loyal brand relationships. Conquest, acquisition, and trial are important for growth. But, when studies show that it costs four to six times as much to get a new customer as it does to keep a customer loyal, we must focus on the new marketing imperative. We must build brand loyalty.

The goal is not merely to attract customers. It is to attract and retain customer loyalty. The loyal customer is the most profitable customer, yet the focus is still often only on attracting new customers. Focusing on customer acquisition without paying sufficient attention to strengthening customer loyalty is one way to grow sales, but it is not the way to grow sales profitably. The Brand Loyalty Marketer knows that the real goal must be to increase sales volume and brand value at the same time.

Difficult? Yes. Impossible? No. Here are a few basic steps.

1. Reject Funnel-Vision

The most widely accepted view of how marketing works is the sometimes referred to as the AIDA model. AIDA is the acronym for Awareness-Interest-Desire-Action. The AIDA view of how advertising works is that advertising builds awareness, generates interest, creating desire, leading to action.

Research shows that models like these work, at best, in only a minority of cases. Reject this out-of-date and misleading funnel-vision view of marketing.

The new CRM view recognizes the importance of reinforcement. The constant interaction between brand use and marketing helps to reinforce attitudes leading to increased brand loyalty. The marketing that happens after the sales is at least as important as the marketing works is having a dramatic effect on how we plan, execute and evaluate marketing programs.

Keep you loyal customers loyal. To the Customer Relationship Marketer, the sale is not the end goal of marketing. The sale is the beginning of the opportunity to build brand loyalty. It is the beginning of the opportunity to convert a brand purchaser into a brand loyalist.

2. Know the value of your customers

Know the value of your marketing effort in attracting and retaining customer loyalty. In some cases, marketing efforts punish loyalty instead of reinforcing loyalty.

Looking at heavy users is not enough. In category after category, a tiny share of *loyal heavy users* account for an extraordinary share of a brand's profits. Who are the members of this *critical core*? Know the value of your best prospects and customers. Know the value of customer loyalty.

You establish a loyal customer base by identifying, attracting, nurturing, defending, and developing *the right customers*. Do you know who the most valuable customers and/or prospects are for your brands? Do you know the effects and efficiency of our marketing activities? Do you know how to identify loyalists? Do you know how to attract, reach and persuade the most valuable prospects and customers? Do you know what to say to and how to reach each type of loyalist? Do you know which media plan works best for each loyalty group?

Do you know how your marketing efforts are moving customers along the Loyalty Ladder? Enthusiast/Evangelists will pay significantly more than category loyalists. A loyal customer can be nine times as profitable as a disloyal customer. The evidence shows that small increases in brand loyalty can result in big increases in brand profitability.

Know the value of your marketing effort in attracting and retaining customer loyalty. In some cases, marketing efforts discourage brand loyalty rather than reinforce loyalty.

3. Get the marketing mix right

How much you spend matters, but how you allocate what you spend matters, too. Advertising and promotion must work in concert, not in conflict. The key is to get the balance right.

Research shows that there is a "danger point," a point beyond which too much of the marketing mix is spent on price promotion instead of on brand-loyalty-building activities. Cross the danger point and brand health will suffer at an increasing rate.

The battle between advertising and promotion is a false debate. You need both for profitable growth. However, the mix matters. Allocating too much of the marketing mix to price promotion can build sales while hurting brand loyalty.

Advertising plays an important role in building brand loyalty. For example, one study showed that two-thirds of the effect of successful advertising was to increase brand loyalty. Other research shows that more than half the value of advertising is to reinforce brand loyalty. Advertising's role in building brand loyalty is critical to marketing success. Yet, this is still largely unappreciated and often ignored.

4. Avoid punishing loyalists while rewarding disloyals

Do you know whether your marketing efforts are rewarding or punishing brand loyalty? Brand-loyal customers need support, too. There are some who believe that loyalty is so durable, once a loyalist always a loyalist. This is misleading. It takes marketing effort to build brand loyalty; it takes marketing effort to retain brand loyalty. Companies that purchase brands believing that brand loyalty does not need marketing support are in for a disappointing marketing surprise. Brand loyalty is both valuable and fragile. Winning and keeping brand loyalty is an ongoing, year-in, year-out process. Undermine brand loyalty and your profitability will erode.

Customer Relationship Marketers appreciate the importance of attracting new customers. You need new customers to grow. But, creating and building brand loyalty is an imperative for enduring, profitable growth. Keep you loyalists sold. Worrying about the relationship you don't have, rather than strengthening the valuable brand relationship you do have, is mismarketing, not Customer Relationship Marketing.

5. Sell on quality, not on price

Over-emphasis on price, whether in a promotional vehicle or in a promotional ad, is destroying brand loyalty not building it. Sell on quality, not on price. If the primary emphasis of the marketing message is on price, whether in a promotional vehicle or in a price advertisement, then brand loyalty is being exploited not enhanced. The primary focus of your brand message must be on how special you are, not on how cheap you are. Whether in advertising or promotion, the goal must be to sell the distinctive quality of the brand.

6. Measure what matters

People manage what is measured. Measure both sales volume and brand value. Measure and monitor changes in brand loyalty. Do quantitative research.

Remember that repeat behavior is not the same as loyalty. Repeat behavior can be bought through bribes. Loyalty must be earned over time. Customer satisfaction is not the same as loyalty, although customer satisfaction is necessary for loyalty. All sales increases are not created equal. Do not increase sales at the expense of brand loyalty. You must always aim to create, defend, strengthen and increase brand loyalty. It is possible to increase sales at the expense of the brand. Customer Relationship Marketers recognize the importance of volume. But they also recognize that sales increases can be accompanied by profit decreases. You need sales volume to be a market leader. You need brand loyalty to be a profitable market leader.

7. Recognize and reward Customer Relationship Marketing

Customer Relationship Marketers understand that the goal is to build sales volume and brand value simultaneously. This is difficult. But it is the only way to ensure enduring, profitable growth. Enduring, profitable growth must be earned by building brand value as well as volume. It is not easy to increase volume and brand loyalty simultaneously. Marketers should recognize and reward those who are clever enough and effective enough to increase market share and brand loyalty, both at the same time. Some marketers are including measures of brand strength in their internal recognition and reward systems.

8. Make branding policy your business policy

Customer Relationship Marketing will require a radical departure in business policies and practices. Customer Relationship Marketing is not only for big, established brands or only for large companies. It is also an important concept for small brands and new brands. It is especially important for new brands where brand loyalty still needs to be nurtured. How you create trial set the stage for future loyalty.

Adopt the loyalty-based view of brand marketing. The brand marketer’s goal must be to win and keep loyal customers. Building enduring, profitable growing brands is all about creating, nurturing, defending and strengthening loyal brand relationships.

Remember the four pillars of Customer Relationship Marketing. Every marketing plan should contain these four basic elements: How do we plan to identify, defend, and strengthen brand loyalty?

9. Focus on brand loyalty as the asset

The financial valuators of brands tell us that brands are worth billions of dollars. “Brands are assets,” they say. A brand is not an asset. Brand loyalty is the asset! Without brand loyalty, the brand has little value. Without brand loyalty, the brand is a mere trademark. With brand loyalty, brands not only have value, they have enduring value.

There are many definitions of “brand equity.” From a marketing point of view, there is only one definition that makes marketing sense. Brand equity is the financial value of brand loyalty.

The CRM marketing equation is as follows: brand loyalty is the basis for brand equity that leads to profit. This is easy to say, but it is hard to practice.

Customer Relationship Marketing Pays

Brands do not have life cycles. Factories can burn down. Machinery wears out. Technology becomes outdated. Founders die. But a brand can live forever. A brand can grow in value over time. There is no such thing as product loyalty; we never speak of trademark loyalty. We refer only to brand loyalty. Why? Because brand loyalty is what endures. Brand loyalty is the basis for enduring, profitable growth.

Brands do not die a natural death. But they can be murdered by misguided marketing practices. Declines in brand loyalty are *not* primarily due to some unfortunate underlying consumer trend. Declines in brand loyalty are primarily due to self-inflicted wounds of mistaken marketing actions. Unfortunately, when brand loyalty declines, so does brand profitability.

Enduring, profitable growth must be earned by building brand value as well as volume. A brand can grow in value over time. Brand loyalty is what endures.

Does all this emphasis on Customer Relationship Marketing pay? Yes. The evidence is consistent; it is dramatic; it is clear. Build brand loyalty. Brand loyalty is the basis for enduring, profitable growth.

As brand loyalty goes up, price sensitivity goes down. As brand loyalty goes up, marketing costs go down. As brand loyalty goes up, sensitivity to competitive promotions goes down. As brand loyalty goes up, interest in trying new products and/or services from the brand also goes up.

A small change in loyalty can make a big difference in profitability. Research shows that a 5 percent change in loyalty can result in a 25 percent to more than 100 percent change in profitability. As brand loyalty goes up, business profitability goes up.

Customer Relationship Marketing is all about winning and keeping customer loyalty to our brands every day. This is a never-ending commitment. Brand Loyalty does not just happen. We must make it happen!

X. End Notes

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