This column is the second in a regular series by **Ian Gordon**, president of Convergence Management Consultants, that explores marketing and management issues that are important to readers of *Home Style*. In this issue, we take a look at maintaining customer loyalty.

Q. "With so many shopping choices out there today, how can I make sure that my customers stay loyal to my store?"

A.

Customers are more demanding than ever. Even when you do everything they ask for and more, you still have no assurance they will be back. Is this just how they are or can you do something about this? Is there really such a thing as a loyal customer anymore?"

Keeping customers has never been more important – or more difficult. The importance of customer retention cannot be overstated. It costs less to secure business from existing customers than to find new ones, the profitability of customers rises with the longevity of the relationship, and the quality of customer relationships is the most important predictor of success. Research suggests that retaining 5% more customers has the potential to raise profitability materially – perhaps between 25% and 85%, depending upon the business category.

Everyone says that customers are less loyal now than before. This need not be the case as companies like Apple and Harley-Davidson demonstrate in a counter-trend, and retailers, too, often achieve customer preference and high levels of loyalty. For example, Shoppers Drug Mart is achieving progressively better results with a differentiated product assortment that combines upscale cosmetics with health and personal-care items in a big-box store.

Unfortunately, the simultaneous proliferation of brands, products and retail capacity makes it more challenging than ever for retailers to achieve meaningful differentiation using the old rules of marketing.

Many retailers consider that "differentiation" applies not only to the competitive comparison of products and value but also to individual customers. That is, they seek to categorize customers and differentiate among them. Because better customer relationships start with a customer strategy, not technology implementation or simply service excellence, these retailers set customer-specific objectives and customize their treatment of every customer to achieve the relationships, preference and resulting loyalty they seek. This is what it means to build a business one customer at a time.

Customer Strategy

Traditional marketing principles involve market segmentation and target market selection and, at a very high level, these approaches have underpinned the success of many retailers' businesses. In a market where consumers differ from one another and where competitors have chosen similar market segments on which to focus, it is now useful to think in terms of satisfying individual customers rather than catering to the masses or even market segments. Many smaller retailers have catered to customers as individuals and now larger firms are looking to do so as well. These larger retailers often use the Peppers and Rogers customer-centric IDIC model to create new business value with individual customers. The acronym IDIC stands for the following and is described in Diagram 1 (shown on the next page):

- Identify customers,
- Differentiate customers,
- Interact with customers, and
- Customize treatment of customers.

In the first step, each customer is assigned a unique identifier and this tag forms the basis for tracking subsequent customer interactions and transactions. A customer database becomes an early priority to ensure that each customer can be recognized uniquely and that an individual's history of connections and purchases is fully visible to the retailer. Some companies use loyalty cards or telephone numbers to identify customers uniquely. Once all customers are identified (or as many as is practical), the next step is to differentiate among them.

Most retailers give all their customers the same value. Even the very best customers often receive the same treatment from the company and its employees as the very worst. Good customers buy at the same times as bad ones, profitable customers wait in lines behind unprofitable ones to return merchandise and good customers wait on the phone while unprofitable ones tie up the lines.

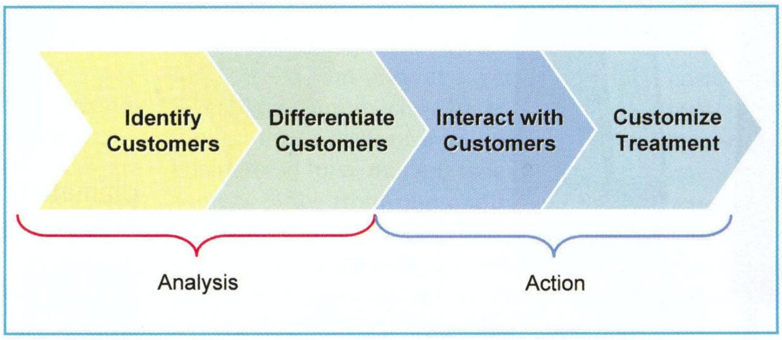
Only customers of average profitability receive the value they deserve, while the most profitable customers are penalized and the company's least profitable customers rewarded. Over time, the result of this value distortion is such that the company's customer portfolio is weakened with the firm's best customers leaving and bad customers staying – and bringing their friends along. To avoid this trap, retailers can triage to differentiate their customers, separating the best from the average and the average from the worst. This distinction among customers is usually done by measuring customer profitability, either over a defined period (say a year) or over a purchasing lifetime (say 10 years). We discuss customer profitability shortly.

Once customers are differentiated, retailers can set customer-specific objectives to attract, retain and develop customers. They can consider customer-specific strategies to reward and grow the best customers, develop average customers into better ones, and manage also the least profitable among their customers, perhaps by being selective about which ones to cater to, or by cutting costs to this audience. Some retailers group their customers into behavioural clusters that reflect customers' purchase behaviours – for example, how much customers spend and how many line items they purchase. Then these retailers develop strategies to manage customers' behaviours to "lift and shift" their spending.

The more retailers know about their customers, the more they can add value for and with them. Some retailers want dialogues that lead to learning relationships with individual customers. This means that interactions are bidirectional and each occurs in the context of prior communications so that future communications can build on prior ones. The essence of this approach is ensuring that the company talk with customers, not to them and never ask the customer the same question twice. As an example of how not to do things, most Canadian automated teller machines (ATMs) ask the customer how much money he/she wants to withdraw this time even though the customer may have been taking out the same amount at every occasion for many years.

Customizing treatment of customers involves adapting the company's processes and behaviours to reflect the value of each customer and the customer-specific strategy the retailer is pursuing. For example, some retailers stage tasting evenings and cooking classes for their best customers and others have product launches in-store to which big spenders are invited to preview the new offerings in an exclusive setting. In another example, a major retail chain has trained its salespeople to ask customers entering the store a few questions so customers can be profiled and their spending predicted, which leads to the customer receiving special treatment. This retailer wants to better manage its sales capacity and this profiling and subsequent treatment allows salespeople to be directed towards the highest profit opportunities.

Diagram 1: The IDIC Model



As noted previously, smaller retailers also apply the IDIC model but they usually do so without thinking specifically of these terms. Smaller retailers can often, for example:

- Identify their customers by name.
- Differentiate among their customers based on a sense of customers' purchase histories and the needs of their best ones.
- Interact with customers as individuals using a learning relationship by remembering what customers bought before, what customers' personal contexts and issues are, how customers are most likely to interpret information and which selling approaches are most likely to work, and
- Customize solutions or services, such as providing a personal gift register for events specific to a good customer, like a 25th wedding anniversary, for example. Smaller retailers are also better positioned than large firms to listen to their customers effectively and earn loyalty by catering to customers' emotional drivers by, for example, providing a free photo frame to a good customer who just said she has a new grandchild.

The September 2008 issue will carry the second part of this article and will review issues such as customer profitability and the building of deeper customer relationships. ■

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