Building Competitive Advantage on the Internet using Relationship Marketing

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Abstract
This paper examines how relationship marketing, enhanced by data analysis techniques, can be applied to Internet marketing. One possible technique that can help the Internet marketer to build relationships with individual customers and hence achieve competitive advantage, is that of Direct Marketing.

This paper begins by defining Relationship marketing (RM), examining its theoretical basis and its origins before moving to a discussion of some of the processes by which it can be applied to the Internet market. The first processes are marketing based and relate to a new paradigm of relationship marketing that implies the development of a relationship and hence loyalty. The second series of processes relate to data analysis procedures that can provide the marketer with accurate and current high-level knowledge about consumer behaviour.

1. Introduction
RM is a relatively new paradigm within the marketing discipline, emphasising long-term relationships with individual customers over short-term marketing transactions. Companies pursuing a relationship marketing strategy focus on delivering a value-enhancing relationship, thus creating a competitive advantage over companies whose focus is transaction oriented.

There is little, if any, agreement within the marketing literature on a definition of RM. However, within the great range of RM definitions, many concepts recur: contracting, relational marketing, working partnerships, working partnerships, symbiotic marketing, strategic alliances and co-marketing alliances. In this paper, we focus on relationship marketing as opposed to relational marketing. Some writers consider the two terms interchangeable, however there is considerable differences in scope, [Mor94] criticise recent RM definitions for failing to acknowledge that "many instances of RM do not have a "customer" as one of the exchange participants". For example, in strategic alliances between competitors, there are no buyers, sellers nor customers - only partners exchanging resources - such is the nature of relational marketing. Consequently, [Mor94] define RM as essentially any relational exchange between any marketing partners, which are therefore not limited to buying and selling. On the other hand, a more straightforward definition by

[Ber91] states that RM "concerns attracting, developing, and retaining customer relationships". Similarly, [Gum95] defines RM, as "based on relationships, interactions and networks".

1.2. The Emergence of Relationship Marketing
It can be argued that there are two sources for the emergence of relationship marketing, one being the maturing and increasing sophistication of Service Marketing, and the other being as a consequence of the increasingly competitive business environment.

The concept of RM is thought to have first emerged within Service Marketing where according to [Aij96] "the customer is an integral part of the marketing process and delivery process which necessitates a close relationship between the service provider and the customer". This notion gradually gives rise to the importance of relationships within the marketing discipline. More importantly, RM emerged as a result of an increasingly competitive climate coupled with market fragmentation and increased consumer sophistication. [Ber83] determined that particular developments within service marketing gave rise to RM, in particular, low growth rates and deregulation resulted in "everyone getting into everyone else's business" and hence greater competition.

The 'new' business environment also provided organisations with the technology to become more efficient providers of products or services. [Tap93] states that the new business transformation shows seven key characteristics:

1. Higher productivity of knowledge and service workers;
2. Higher quality expectations;
3. Need for better and faster responsiveness (even mass customisation);
4. Globalisation;
5. Outsourcing;
6. Partnering (extended enterprise);
7. Employee empowerment combined with social and environmental responsibility

[Tap93] show a clear correspondence between the changes in Information Technology and the changes stated above in today's business. The so-called information revolution provides organisations with a variety of means to become leaner, more flexible, and innovative, and possibly more importantly to get 'closer to the customer' through improved customer information. The radical transformation in the business climate has resulted in greater emphasis on keeping customers through improved customer service and effective targeted marketing activities - the main concepts of RM.

As stated earlier, RM had some origins in Service marketing theory, but it can be argued that the main concepts of RM have been evident in 'general' marketing theory.

1.3 Theoretical Underpinnings of Relationship Marketing
The most notable attempt at generating a theory of Marketing was presented by [She88]. The authors presented 12 schools of thought rather than one general theory. This framework is, according to [She88] "generally dominated at any one point in time by one prevailing perspective" and offer "strategic marketing" with its emphasis on competitive advantage as the prevailing perspective today. Although RM is not included in the framework, it is interesting that [She88] ask "what is, or should be, the dominant perspective in marketing?" and conclude that "Each perspective... represents only a partial picture....In our opinion, the main purpose of marketing is to create and distribute values

among the market parties through the process of market transactions and market relationships".

1.4 The Development of RM
Unquestionably, the Nordic School of Service has helped to extend the concept of RM from service marketing to the point of defining it as the new marketing paradigm. [Gro96] argues that since the late 1970s the Nordic School of Service and IMP Group, have advocated that managing marketing normally has to be built on relationships rather than transactions.

However, the latest trend is the attempt to deepen and develop the concept of RM as well as test it empirically by applying it to various industries and areas of marketing. This paper attempts to develop the concept of RM by applying it to the Internet market.

1.5 RM - the new Marketing Paradigm
So, having defined RM and traced its origins and applications, it is useful now to determine the key components of a RM strategy. [Gro96] states that there are three tactical elements of a relationship strategy:

1. Seek direct contacts with customers and other stakeholders;
2. Build a database covering necessary information about customers and others;
3. Develop a customer-oriented service system;

Further, [Gro96] acknowledges three strategic elements of a typical relationship marketing approach:

1. To redefine the business as a service business and the key competitive element as service competition;
2. To look as the organisation from a process management perspective and not from a functionalist perspective (to manage the process of creating value);
3. To establish partnerships and a network to be able to handle the whole service process.

In examining both the tactical and strategic elements suggested by [Gro96] it is evident that the development of a customer database and the search for competitive advantage based upon service, are critical. It is a feature of RM that with appropriate customer data, it is possible to develop a relationship through highly targeted marketing activities. A common form of such targeted activities is that of direct marketing: marketing aimed specifically at the most profitable existing and potential customers.

There is a clear need for highly targeted marketing activities within the Internet environment, a collection of 'smaller submarkets', where developing relationships with Internet consumers results in sales, repeat sales and profits [Lev95]. However, applying relationship marketing techniques to the Internet is not straightforward.

2. Applying RM to the Internet
The Internet marketer must realise that such marketing involves one-to-one promotion. The difficulty may be that the demographics of the Internet consumer do not favour relationship building: 67% of Internet newcomers are male, 88% own a home computer, 39% have a college degree and 17% live in households with incomes of $80,000 or more [Hic97]. The Internet consumers could be described as impatient, having no allegiance to particular web sites, in short, Internet consumers are 'switchers', empowered to choose which site they visit so that when faced with a barrage of Internet advertising, they simply

switch to a different web site [Mul97b]. It could be said that the Internet consumer might not want to enter into a relationship. Given these characteristics, the task of building long-term Internet relationships, it would seem, is problematic. The key is to achieve customer loyalty, which should lead to a competitive advantage, based on increased shareholder value and asset efficiency [Blo97] and to minimise customer switching, which can reduce profitability and market share [Pau97].

2.1 RM strategy for the Internet: Developing Internet Customer Loyalty
According to [Blo97] customer satisfaction is assumed to "have a direct positive link to customer loyalty". [Bar97] suggests that there is a 'myriad of approaches' to building customer loyalty and to tailoring marketing programmes. These generally include direct marketing, database marketing, and loyalty programmes. This paper will focus on the use of direct and database marketing as methods of securing Internet customer loyalty. [Kot97] believes that financial benefits, social benefits and adding structural ties will encourage 'bonding' and 'satisfaction'. [Lev95] highlights three possible approaches to achieving Internet customer loyalty: give consumers an emotional stake; multiply the number of visits; and increase the quality of each contact. The process of convincing the customer to 'stay a customer' is highly dependent on the customer's perception of 'value'. In consumer markets it is only possible to achieve competitiveness through superior customer value [Jen97]. Thus, the marketing strategy must make superior contributions to the consumers' perception of and attitude to value. A critical component of any Internet relationship marketing strategy, then, has to be an understanding of the salient dimensions of Internet customer value.

2.2 RM tactics for the Internet: Direct Marketing
Direct marketing is a process that can help Internet marketers achieve customer loyalty, by converting 'switchers' into loyal and repeat purchasers. It is a tool for direct communication of a special product and promotion offer that has a high chance of appealing to targeted customers [Dic97]. With the creation of a database, targeted sales promotions can be offered Internet to 'hot prospects' rather than, as in the case of the Internet pull environment, promotions aimed at disinterested, impatient, unspecified and more importantly unlikely to buy groups of consumers. Hence, the opportunity is provided for a push strategy. The traditional process of direct marketing is outlined in Figure 1.

It is possible to adapt the traditional process of Direct Marketing to the Internet Marketing environment. One of the most recent developments in the direct marketing process, it is simply another channel of marketing where a firm can "meet and condition a prospect" [Kot97]. Not surprisingly Microsoft promotes its products on the Internet. In 1996, an extra dimension was added when the company provided a definitive Internet guide to the Euro '96 Soccer championships. A web site was set up for four weeks to give access to the information that only the press and the championship organisers had previously been able to obtain. The web site recorded 18 million hits during the championships, 1.26 million of them during the peak day. Over the same period, traffic to Microsoft's permanent UK web site increased by 78%.

1	Database elements are specified, such as name, address, phone, fax, gender, income, hobbies, product usage situations, benefits sought etc. The source of record and date are added
2	Customer sends in warranty card, enters a competition, or has name on list of company selling related products or services. Permission is given and information is used for direct marketing
3	Record is added to database using database software
4	Target segment is specified and statistical analysis performed. Hobbies, interests, usage situation, and promotion preference identified
5	Most appealing direct-marketing campaign is designed to promote most appealing products and features to target segment
6	Database is updated, recording response of customer to campaign

Figure 1. The Direct Marketing Process, adapted from [Dic97]

2.3 RM tactics for the Internet: Database Marketing

It can be seen from Figure 1, that Database Marketing is critical to the process of direct marketing. The database can be used in four major ways: to identify target groups or prospects; to decide which customers receive which offers; to build customer loyalty; and to reactivate customer purchases [Kot97]. When rating and selecting people from the database [Sto93] recommends applying the R-F-M formula (recency, frequency and monetary amount). The best customer targets are those who bought most recently, those who buy frequently and those who spend the most. Points are established at various R-F-M levels and individual customers are scored - the higher the score, the 'hotter' the prospect.

3. Applying RM tactics to Internet Retailing

Internet retailers, in particular, can benefit from the adaptation of the traditional processes of direct marketing and database marketing. A sales promotion based on previous shopping behaviour and other descriptors can be offered at the end of an Internet shopping visit. An illustration of how direct marketing might be adapted for Internet shopping is shown below.
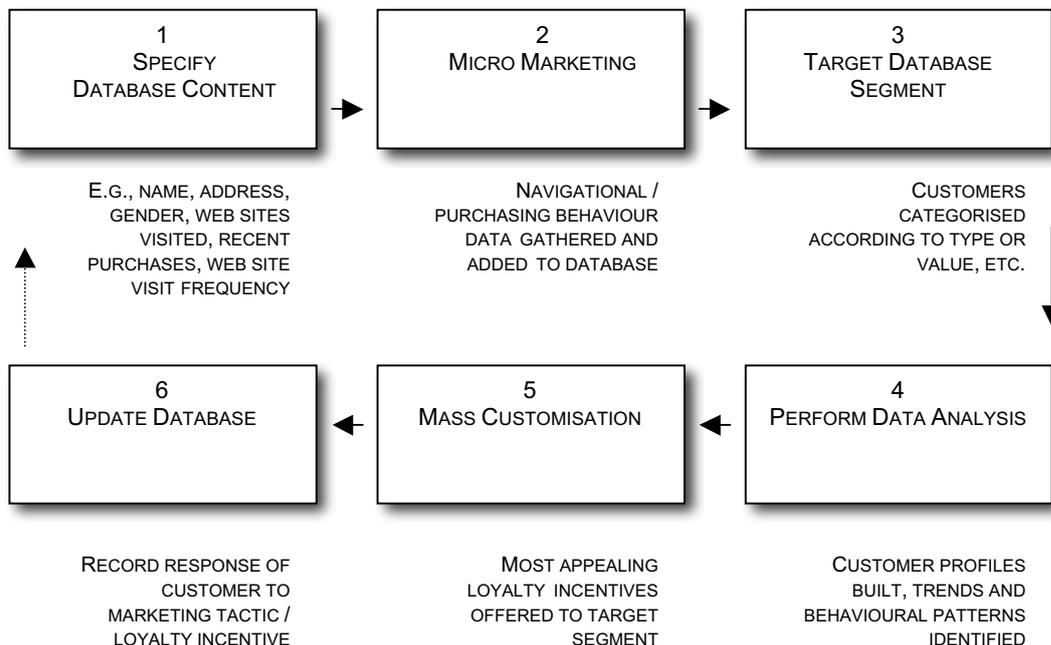
1 SPECIFY DATABASE CONTENT	2 MICRO MARKETING	3 TARGET DATABASE SEGMENT
E.G., NAME, ADDRESS, GENDER, WEB SITES VISITED, RECENT PURCHASES, WEB SITE VISIT FREQUENCY	NAVIGATIONAL / PURCHASING BEHAVIOUR DATA GATHERED AND ADDED TO DATABASE	CUSTOMERS CATEGORISED ACCORDING TO TYPE OR VALUE, ETC.
6 UPDATE DATABASE	5 MASS CUSTOMISATION	4 PERFORM DATA ANALYSIS
RECORD RESPONSE OF CUSTOMER TO MARKETING TACTIC / LOYALTY INCENTIVE	MOST APPEALING LOYALTY INCENTIVES OFFERED TO TARGET SEGMENT	CUSTOMER PROFILES BUILT, TRENDS AND BEHAVIOURAL PATTERNS IDENTIFIED

Figure 2. Application of the Direct Marketing Process to Internet Retailing

Stage 1: Database elements specified
In stage one, management must ensure that the elements of data to be captured are relevant and appropriate to the organisation. Data capture should not be limited to customer transactions but should also include enquiries and complaints.

Stage 2: Micro Marketing
It is in stage two that the patterns in customer transactions and navigational behaviour are monitored. Using this data, Internet marketers can identify target segments.

Stage 3: Segment Specified
In stage three, customers are categorised according to type or value.

Stage 4: Data Analysis
Data analysis, stage four, is the use of any technique that helps to reveal useful and actionable information about the domain from which the data is collected. The most common techniques available for data analysis include: statistical measures; visualisation aids; and knowledge-based systems. This latter technique encompasses 'intelligent' systems, a research focus that includes: artificial neural networks; genetic algorithms; data mining; fuzzy logic and 'soft' systems; and many more.

Data mining is the automated discovery of non-obvious, potentially useful and previously unknown information from large data sources [Fra91]. It uses induction algorithms to generate natural language rules and associations that may be both useful *and* actionable.

Within the context of relationship marketing data analysis, data mining can provide knowledge about the unique characteristics of identified customer segments, so that business decisions may be made in relation to customer value and appropriate loyalty incentives can be developed [Mul97a].

Stage 5: Mass Customisation
Stage five, mass customisation implies different incentives for different customers. Moreover the incentives should be fashioned to reward long-term behaviour, in order to discourage short-term deal seeking by Internet consumers.

Stage 6: Database Updated
And finally, stage six records and measures the success or otherwise of the loyalty programme. The information can be used to take corrective action for future loyalty programmes.

The Internet direct marketing tool proposed here achieves highly targeted direct communication with Internet customers of special product and promotion incentives or offers. Targeting does not have to involve price discounts, it could mean making certain types of consumer more aware of relevant services or products, or service enhancements, special recognition or even inviting them to participate in special events. Because the promotion can be tailored to 'hot' prospects, it has a high chance of success. However, its success is based on descriptive and behavioural consumer data. Without this data, the Internet marketer is in danger of creating promotions aimed at disinterested, impatient, unspecified and more importantly unlikely to buy consumers, typical of the Internet 'pull' environment. In this situation, it is impossible to build Internet customer relationships and any opportunity for competitive advantage is lost.

3.2 Importance of Internet Consumer Data

Consumer data has been described as "the bedrock of all targeted marketing activities allowing marketers to understand and predict how their customers will behave" [Hof95][Cur96]. Internet transaction details are of some value, but for many Internet marketers the most important consumer data is that concerned with patterns in transactions, such as an increasing revenue over time or the range of products purchased over a period of time. According to [Von96] "Selling on the Internet no longer will be based on demographics...it's all psychographics. You want to know what a consumer is thinking."

This is now a clear possibility since Internet technology offers businesses the opportunity to gather consumer data and monitor consumer choice through customers revealed preferences in navigational and purchasing behaviour on the web [Nor97]. Such data can enable a business to customise future offerings for individual customers.

3.3 Value of the Database in Internet RM

It is evident that such technology facilitates RM, when the database, in particular, is an integral part of the process. The significance of the database lies in its ability to capture, store, analyse and segment customer information. The value of this information is that it enables a company to start calculating real customer value, and can help to measure key customer variables such as margins, longevity and loyalty. In other words, data available from a database must be converted into information and then used to create knowledge for key decision-makers [Hum96].

The database can be used in four ways: to decide which customers receive which offers; to build customer loyalty; to identify target groups or prospects; and to reactivate customer purchases [Kot97]. When selecting 'hot' prospects, [Sto93] recommends applying the R-F-M formula (recency, frequency and monetary amount). The best customer targets are those who bought most recently, those who buy frequently and those who spend the most. Points are established at various R-F-M levels and individual customers are scored - the higher the score, the hotter the prospect. This rather simplistic method whilst useful is certainly not the answer to the Internet marketers quest in search of competitive advantage. However, it can be greatly enhanced by the process of data mining.

3.4 Analysis of Consumer Data

Data mining allows marketers to reveal layers of information about markets or subsets of markets in ever increasing detail, enabling consumer profiles to be built and the identification of profitable and non-profitable segments. The application of data mining techniques to Internet shopping data provides high-level knowledge in the form of rules that describe consumer navigational and purchasing behaviour [Mul97b]. These rules capture trends and behaviour patterns that may be applied within a RM strategy. For example, the high level mined rules may be incorporated as a rule-based system into the architecture of an Internet shopping mall service. When each new customer interacts with the Internet mall to navigate and purchase goods or services, their behavioural patterns are identified by the rule-based system. When this happens, the Internet mall system immediately reacts to change dynamically the information presented to that consumer.

The potential for Internet direct marketing and hence competitive advantage increases enormously with data mining techniques. With behavioural and descriptive data about Internet consumers, it is possible to target: those who spend the most with offers of generous incentives; those who have not purchased for some weeks or months; or perhaps those who have switched to a rival company. The information provided by the database

and data mining is related to customers, earning these two technologies an important place within relationship marketing.

3.4 Implementing Internet RM

Full commitment from management is essential if all the benefits are to be gained from a database driven approach to Internet RM [Har95, Yov95]. Measurement standards must be agreed prior to the establishment of a database, and the company should expect long-term rather than short-term returns on database and data mining investments [Dav97]. [Wan94] has suggested that firms should see a payoff within one year.

4. Conclusion

In conclusion, this paper demonstrates that relationship marketing facilitates the achievement of competitive advantage on the Internet. An Internet marketing strategy based upon relationship marketing (a new paradigm within the marketing discipline) will enable companies to deliver value-enhancing relationships which in turn, help to create customer loyalty.

However, the Internet consumer profile poses a problem for Internet marketers, typically it is one of impatient, switching and astute consumers. This paper has proposed the use of relationship marketing tactics – direct marketing and database marketing – as a means of securing loyalty amongst Internet consumers. Direct marketing can help the Internet marketer to achieve highly targeted direct communication with Internet consumers. This communication may include special offers, messages of service enhancements or competitions.

Direct marketing techniques rely on measurable and actionable consumer data. One of the major advantages of Internet technology is that it facilitates the retrieval of not only transaction details but also transaction patterns (behavioural information about the browsing habits of individual consumers). And, whilst it is important for Internet marketers to possess descriptive data about their Internet consumers, there can be no doubt that the possession of behavioural and psychographic knowledge is a major breakthrough in the search for competitive advantage.

We argue that the process of data mining provides enhanced facilities for data analysis. The algorithms used in data mining are well suited to the processing of large, distributed and often heterogeneous databases that store the transactional and behavioural data gathered by Internet trading organisations. The potential of data mining is enormous, but its market application may be tempered by customers and consumer organisations who may react negatively to the collection and 'mining' of aggregated personal information [Tor98].

The implications are far reaching for Internet marketers, since data mining can improve their understanding of Internet consumer behaviour. It seems evident then, that Internet marketing activities will be characterised by sophisticated targeting of consumers. Ultimately, competitive advantage on the Internet may be determined by the ability of Internet marketers to collect and manage customer databases.

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