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Database Marketing: A Potent Tool for Hospitality Marketers

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Abstract

Nearly every industry, including hospitality, has adopted database marketing techniques. Why have they become so popular and what advantages do they offer for hospitality companies? The authors examine these issues.

Database marketing: A potent tool for hospitality marketers

by Karl J. Mayer
and Richard S. Lapidus

Nearly every industry, including hospitality, has adopted database marketing techniques. Why have they become so popular and what advantages do they offer for hospitality companies? The authors examine these issues.

Database Marketing (DBM) has become a popular tool among hospitality marketers. Increasingly, hotels, restaurants, casinos, and other hospitality businesses are turning to DBM methods in order to establish or expand their guest bases. Like virtually every other industry, hospitality operators have recognized that the ability to market to individual customers will result in a competitive advantage for their firms. Indeed, failure to adopt this new perspective may have dire consequences for their future ability to compete.

DBM may serve as a new basis of competition in hospitality because of its ability to establish a bond with specific customers. Berry has identified three distinct levels at which a company can practice DBM, depending upon the nature of the bond between a firm and its customers, the degree of service customization required, and the potential it provides for sustainable competitive advantage.[1] Similarly, Oppermann developed a three-level application framework in order to survey database marketing practices in Nevada's hotel and motel industry.[2] Oppermann's three application levels covered customer retention, product promotion, and new customer creation. Very few of the hotels that responded to his survey appeared to be acting at the highest level in all three areas. Thus, although its popularity is growing, DBM still appears to represent an untapped strategic opportunity for many hoteliers.

DBM's distinct advantages in new customer prospecting are summarized by Emily F. Soell, vice chairman and chief creative officer of Rapp Collins Worldwide, Inc.: "We've found that database marketing helps us seek out those people who have the need, the propensity and

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the money to buy a certain product. We can then not only selectively market to those favorably predisposed people who have identified themselves, but in fact clone them – model them statistically and find their twins who have heretofore been unknown to us."[3]

Thus, DBM can enable hospitality companies to expand their customer bases by reaching out to likely new prospects who share the same propensities as their current customers. It is evident, then, that DBM has become a potent tool for competing in the hospitality industry.

What does a database approach entail?

The concept of DBM is also known by a variety of other names: direct marketing, relationship marketing, frequency marketing, target marketing, niche marketing, and one-to-one marketing. It is most often associated with direct mail, couponing, telemarketing, narrowcast cable television, interactive television, and geographic information systems. In actuality, all of these media and methods can be used by a hotel, restaurant, or casino as part of a DBM approach. DBM seeks to appeal to consumers on an individual basis as compared to traditional advertising and marketing methods which emphasize a less targeted appeal to various consumer segments.[4]

In theory, although a DBM approach might reach consumers at higher costs per unit than traditional methods, these higher unit costs often are offset by higher sales volumes or increased purchases per sale since the message is individually tailored to consumers based upon their needs and previous buying behavior. DBM's proponents contend that the investment in start-up costs and increase in operating costs that are required to build and operate a database are well worth it. AT&T's experience with response rates from database-directed offers sometimes runs as high as 20 to 30 percent, compared to the low single digits for broader, more conventional direct mailings.[5] The Trump International Hotel located in New York City reported that its pre-opening direct mail campaign, which cost $20,000 to produce, has generated over $900,000 in bookings.[6] Clearly, the results of going "direct" can be quite impressive.

It has been argued by advocates of DBM that even well-segmented consumer appeals represent a "mass" approach, without the ability to target individual consumers.[7] They contend that such "non-individualized" appeals have lost their effectiveness for several reasons, including the following:

- Most markets are now highly fragmented into segments having very different needs; as a result, a "shotgun" type of message approach no longer fits everyone.
- An immense amount of "noise" resounds in the marketplace as

companies bombard potential consumers with information and sales pitches; advertisers must now fight to establish the relevance of their products in a very cluttered marketplace.

* Technology has improved to a point that while it is relatively easy to send personalized messages to consumers, differentiating oneself on this basis has become much more difficult; because consumers understand that technology is often lurking behind "personalized" mass mailings, the technique may have lost much of its unique impact and its resulting ability to pull consumers to a product or service.

Database marketing has a different perspective

Berry discusses DBM in the context of "relationship marketing" which he defines as attracting, maintaining, and enhancing customer relationships.[8] He states that it is a "new-old" concept that was even practiced by the earliest merchants. Certainly, the core concepts of modern DBM have been in use since the 1920s, such as RFM (Recency, Frequency, Monetary) analysis.[9] While this is the case, it was the advent of credit cards in the 1950s and computer technology in the 1960s that really revolutionized the direct marketing discipline and allowed it to blossom beyond the realm of generating customer mailing lists into a full-fledged discipline in its own right.

There are five key tenets that form an underlying belief system for tourism marketers who practice DBM:[10]

* Past consumer behavior is the best predictor of future behavior.
* A purchase is simply one event in a customer's life. To figure a customer's true worth, you have to calculate lifetime value.
* Customers are more important than non-customers.
* Certain customers are more important than other customers.
* Customers are likely to share certain characteristics.

Indeed, these five tenets seem to capture the essence of DBM; however, one additional tenet seems appropriate:[11] If you can't measure it, you shouldn't be doing it.

This last tenet emphasizes the database marketer's utilitarian approach to consumer marketing. It implies that the measurement methods of traditional mass media are less concrete than those employed under DBM's behavioral measurement approach. Database marketers focus on measuring consumers' final behavior, rather than pre-cursors to their behavior.

Paraphrased in four principles, the six tenets of DBM offer great insight into why it is such a potentially powerful marketing method for hospitality practitioners:

- There is an emphasis on behavior.
- Customers are judged based upon their lifetime value rather than by single or even multiple transactions.
- Eighty percent of any business's revenue comes from 20 percent of its customers.
- Highly explicit customer segmentation is the key to reaching them effectively.

While the last two principles are by no means revolutionary, DBM's direct emphasis on customer behavior and the long term, relationship nature of DBM may still be fairly novel ideas to hospitality industry owners and managers. Casino gaming operators have begun to calculate customer lifetime values, which are determined by how much a player wins and receives in "comps" versus his projected losses over his years of active play. Casino managers are then faced with hard choices about whether an individual player is "worth it or not."[12]

Customers are evaluated on lifetime value

Indeed, the notion of evaluating customers based upon their lifetime value to a firm is a relatively recent concept in most business settings. Fornell and Wernerfelt described how defensive marketing strategy can be employed to reduce customer defections and brand switching, thus extending their lifetime values to a firm.[13] Their approach is based upon improved management of customer dissatisfaction, as opposed to a focus on customer satisfaction.

Reichheld and Sasser analyzed customer defection rates in various industries in order to determine lifetime values of customers.[14] In the credit card business, they estimated that retaining 2 percent more customers has the same bottom line effect as cutting unit costs by 10 percent. Their research across nine different industries showed that reducing customer defections by just 5 percent boosted company profits from a low of 25 percent to as high as 85 percent, depending upon the industry. Wider recognition of the primacy of the concept of customer lifetime value has undoubtedly contributed to greater acceptance and use of DBM methods.

With respect to customer segmentation, it is the degree of customer segmentation that can be achieved with DBM that represents a significant departure from traditional segmentation approaches. While database marketers are interested in clustered customer groups, in its most robust application, DBM segmentation extends down to the level of the individual household. Hoteliers may have only recently begun to adopt this perspective in their marketing efforts. Vladimir observed that the conventional wisdom in the hotel business has always been to appeal to as many market segments as possible.[15] In contrast to this conventional viewpoint, Wilcox avers that DBM is not

mass marketing, or even segmented marketing — rather, it represents *individual* marketing.[16] For example, Fingerhut, the fourth largest U.S. mail order company and a recognized leader in DBM, captures as many as 1,400 pieces of information about a single household. Fingerhut's database includes not only demographic items like income and home ownership, but also data on the name, age, sex, and birthday of each child in the household.[17]

The case of a marketing giant like American Express (AmEx) serves to further underscore the individualized segmentation approach associated with DBM methods. Even though AmEx has millions of names of its cardholder members in its database, some of the promotional offers which AmEx has sent out with its monthly billing statements have gone to as few as 20 people.[18] AmEx's approach typifies a database marketer's underlying philosophy of targeting only a few key customers who share certain characteristics from among millions who do not.

In reality, it is hard to conceive of a world without mass media, and it is unlikely that many hospitality businesses will forsake the use of mass media to opt completely in favor of DBM. On balance, marketers agree that general advertising is still necessary, and that mass marketing will not become extinct.[19] In fact, the power of DBM is actually enhanced by solid image advertising campaigns. However, DBM should allow hospitality companies to stop wasting money on non-prospects who will never buy their services.

Consistent with this perspective, many hotels have made a pronounced shift in spending patterns for marketing communications away from traditional advertising media. For example, the Hyatt Hotels Corporation has divided its marketing communications budget equally between media advertising and DBM. In 1997, Hyatt will spend $12 million on each.[20] In another instance, a privately-held New York City hotel operator has relied almost exclusively on sophisticated direct mail pieces, spending more than $1 million annually to direct market its properties to potential guests.[21]

Technology plays a key role

More than any other single factor, technological innovations have made it increasingly possible for every business to have a direct relationship with the people who use its products and services.[22] Radisson Hotels initiated its commitment to technology over a decade ago under the leadership of its president, Jurgen Bartels, who credits technology with nurturing the rapid growth of the chain from 30 hotels in 1984 to over 250 properties in just 10 years. For example, Radisson's central reservations network (its "Pierre" system) handles an estimated 660,000 calls per months and books about 43 percent of the chain's business. In order to handle such high call volume, Radis-

son has invested in a computer system that can respond at a rate of 194 million instructions per second.[23]

Indeed, technological developments are the principal ingredient that has led to the widespread adoption of DBM methods. The ability to gather and analyze vast quantities of data is the foundation of all targeted marketing efforts, but the key requirement of using new technology is that it must improve understanding of customer behavior and allow more efficient communication with customers and guests.[24] Major technology innovations that have spurred DBM's growth include the following:[25]

- **Universal Product Code (UPC) scanning equipment** in retail stores, which tracks individual purchases if the consumer uses a "frequent-buyer's bonus card" issued by the merchant
- **relational database technology**, which has simplified the organization and retrieval of data within a database; relational database software operates by cross-indexing data records into giant matrices, which makes finding specified records much easier
- **new kinds of audience measurement**, such as "people meters," which can tell media planners which people are watching what channels and programs
- **telecommunication technologies**, such as automatic number identification and voice response capabilities, which recognize respondents to advertisements who call manufacturers' 800 and 900 telephone numbers

Fortunately, many technology innovations have not necessarily been accompanied by cost increases. While cost issues are still a major deterrent for many firms which want to make use of DBM, computer equipment manufacturers are rapidly improving their products while keeping prices in line or bringing prices down. This trend makes it affordable for smaller hospitality companies to build, own, and maintain proprietary databases. For instance, an operator can start with a simple database and then increase its features over time. Once the initial system has been outgrown, the data can simply be transferred to a larger platform.[26]

Hotels are moving into new technology

The hotel industry is being challenged by the need to understand how to effectively utilize the growing power of information technology in their operations.[27] Some hotel companies appear to have taken the lead in applying new technology to their operations. For example, the Ritz-Carlton hotel chain has installed a knowledge-based system that tracks customers' preferences and needs as part of its customer information database.[28] This data is automatically transmitted throughout

the hotel chain's properties worldwide. If a customer in one city had a specific request (i.e., for six hypoallergenic pillows), then that customer could expect to find that request fulfilled the next time he/she stayed at any Ritz-Carlton hotel anywhere in the world. A knowledge-based system like the one Ritz-Carlton is using has the ability to learn more about the customer and then put that information to good use in the future. Similarly, Preferred Hotels & Resorts has deployed a "Guestnet" software package that enables its member hotels to track personal preferences of their guests from a centralized database.[29]

The use of DBM in hospitality will also be affected by advances in decision-aiding technologies. Decision-aiding properties include those that facilitate the ability to store and retrieve large amounts of information more quickly and inexpensively; more rapidly and selectively access information created outside the organization; more rapidly and accurately combine and reconfigure information so as to create new information; more compactly store and quickly use the judgment and decision models developed in the minds of experts, and stored as expert systems; and more reliably and inexpensively record and retrieve information about the content and nature of organizational transactions.[30]

Neural-networks and statistical modeling are important decision-aiding technologies that will affect the growth of DBM. A neural network performs computing by mimicking the workings of the human brain. It does so by using an artificial neuron with multiple inputs that enables the software to learn through training and go beyond simply executing a fixed set of commands.[31] In the realm of DBM, neural networks can automatically build a model of customer behavior based upon analysis of previous transactions.

Predictive modeling of customer behavior is another target area for advancing the state of DBM. Miglautsch maintains that the emerging science of statistical modeling will serve to validate the direct marketing process.[32] Statistical modeling allows a marketer to project the profit of individual slices of customers' files, based upon a marriage of their purchase history with other information, such as the kind of neighborhood in which they live. Fingerhut is a leading company in the application of predictive modeling techniques to its customer information database, which allows it to automatically sift through customer data to carefully target appropriate promotional material.[33]

The inherent potential of such advanced systems to be of benefit to both hospitality marketers and consumers is impressive. However, other "less advanced" technologies will also have an impact upon DBM as new developments emerge in these areas. For instance, advances in print media capabilities will include "versioning" software programs, which will have the ability to rapidly assemble up to hundreds of versions of the same ad, switching and reassembling the products and prices all over again.[34] This advance will allow hospital-

ity marketers to more cost-effectively create individually-tailored media for the very narrow consumer segments targeted by DBM methods. Use of print media will also be enhanced by new printing press technology that will allow for two-color personalized messages and higher quality custom printing. This development will lead to greater automation in targeted promotions and advertising presumably at lower cost levels.

Databases have strategic implications

DBM provides hospitality marketers with the means to convey appropriate messages to many market segments about many products because it allows them to sort out the most relevant information from the daily flood of data which a company receives. As such, the customer database has really become a sophisticated information system. This system can give companies a strategic advantage because it allows for an approach which differs from traditional marketing in at least three ways:[35]

- The scale of the database can be far greater than in the past, often including information on tens of millions of households.
- The depth of the information or the amount of information captured about each individual and household can also be much greater. Hundreds or even thousands of data items can be collected and analyzed on each household, including complete purchasing histories.
- The degree to which this information can be used as part of a highly automated business function bears little resemblance to the scattershot mass-marketing campaigns of the past.

Several authors have suggested that DBM's emergence is of crucial strategic importance, and has effectively shifted the balance of power in certain industries. Robinson and Kearney examined the development and role of DBM in the travel industry.[36] They concluded that DBM is altering the relationships between service providers, travel agents, and consumers, and that channel power is shifting away from travel agents as key intermediaries. Due to their travel information systems, the major airlines are thus in a position to reshape the contour of the travel service market.

Further evidence of an important strategic context for DBM is that it appears to be figuring heavily in the acquisition plans of companies. For example, Hospitality Franchise Systems, Inc., the largest operator of franchised hotels in the United States, announced its intention to acquire Resort Condominiums International in October 1996.[37] Surprisingly, Henry Silverman, chairman of HFS, confessed to knowing nothing about the timeshare business until a year prior

Table 1
Reported Sizes of Proprietary Information Databases:
Large Companies

Company Name	Size of Database	Unit of Database
Blockbuster Entertainment Corp.	36 million	No. of households
Kraft General Foods	30 million	No. of households
Philip Morris	26 million	No. of households
General Motors Corp.	12 million	No. of households
Joseph E. Seagram & Sons, Inc.	10 million	No. of households
Sears, Roebuck & Company	77 million	No. of households
Harrah's Entertainment	17 million	No. of 'names'
Mirage Resorts	5 million	No. of 'records'
American Airlines	45 million	No. of 'airfares'
Fingerhut Companies	2 trillion	No. of 'characters'

Adapted from Berry, et. al.,41 Besson,42 Ballinger,43 McKee,44 and Slatter,45

to the transaction. Evidently then, a major part of HFS's interest in this acquisition must be to link Resort's customer database of two million timeshare owners with those of HFS's other operations, in order to cross-sell hotel, real estate, and car rental services to Resort's customers.

Gaming operators focus on retention

In another area of hospitality, gaming operators appear to be focusing their DBM efforts on customer retention rather than market expansion.[38] This tendency may be due to the fact that available gaming customers are heavily sought after by a number of casinos who seek to bring them in-house. Thus, customer direct mail pieces often employ a tiered approach based upon a customer's perceived value to the casino. Each mailing may contain a half dozen or more different offers, depending upon whether a gambler is a low roller, high roller, or somewhere in between.[39]

Companies are building databases in order to "own the customer" in a strategic sense.[40] Although marketers once aimed to build market share, they now aim to own a market niche. Large corporations have never been thought of as particularly adept at niche marketing, leaving that to the domain of smaller firms. However, DBM has given the large players the ability to successfully focus on these micro-markets in an effort to expand their activities and challenge smaller companies. Further, the very large scale and capital investment required of a company that adopts DBM can serve as an imposing entry barrier to any competitor which might be considering entering a new segment.

Along these lines, Table 1 lists some leading database practitioners and the size of the customer information databases that they have already assembled. Each of the companies listed in Table 1 has made a significant commitment to DBM; some have taken many years to get to the point where they are now. Competitors who are just starting down the path of DBM will need a long time to catch up to the group of early movers, which will likely work to that group's advantage.

In a strategic sense, marketers will have failed if, as has often been the case, their use of DBM has focused too heavily on coupons, promotion, and discounting.[46] An overemphasis on promotion simply leads to less brand loyalty and ruinous price-based competition, which can result if DBM methods are inappropriately applied. For example, Child, Dennis, Gokey, and McGuire note as follows:

> Many retailers offer discounts, rebates, or goods if customers present loyalty cards at every purchase, yet they fail to use the resulting information to tailor their offerings to the individual customers' tastes, buying patterns, or value to the company. In the United Kingdom, the grocery industry appears to be rushing to introduce loyalty card schemes at a cost that could reduce industry profitability by as much as 20 percent.[47]

Promotional incentives cut profitability

A similar pattern appears to have developed among the gaming operators in Atlantic City, New Jersey.[48] Aztar Gaming's 1996 corporate profit was off by 99 percent from its 1995 levels, principally due to difficulties at its Atlantic City casino. The difficulties are being caused by expensive marketing skirmishes among Atlantic City casino operators, resulting from their initiation of a continuing round of promotional incentives in order to induce gamblers to visit their property, typically on bus tour packages. Although the Atlantic City effects may not be directly linked to DBM efforts by the casinos, the ruinous effect upon the market is still the same as in the United Kingdom grocery example. These cases are indicative of the possible downside of DBM if it is used as only as a promotional tool and linked to giveaways in the name of building customer loyalty. The misuse of DBM can have dramatic negative consequences as both of the above examples demonstrate.

Finally, the strategic implications of DBM have a potential linkage to developments in government regulation. More stringent regulation of personal information, if it were to occur, would likely increase the strategic leverage for those companies that have already adopted DBM. For one thing, developing such customer databases would then become even more expensive for companies without proprietary cus-

tomer information systems.[49] Thus, it might be concluded that all companies would not view their ethical responsibilities vis-à-vis database marketing in the same objective light.

Three observations are significant

In conclusion, three observations seem appropriate about the role of DBM as a tool for the hospitality field:

- DBM has moved well beyond the stage of a fad and has assumed a primary role in current hospitality marketing practice. Its emphasis on targeting individuals and their behavior is consistent with current trends in media selection, which offer marketers many ways to communicate to their target segments. Although it will likely never replace mass media appeals for most consumer products, DBM can function as a powerful complement to other media methods. Within most sectors of the hospitality industry, its use is decidedly on the upswing.
- Advances in technology, especially in computer processing analytic methods, will continue to be the prime mover behind further adoption of DBM methods. As more sophisticated analytic tools and improved computing power become available at lower costs, more hospitality companies will find it beneficial to take the plunge into DBM, or take their existing database efforts to an even higher level.
- DBM appears to be emerging as an important strategic element in how hospitality companies compete. It appears to be an explicit part of the strategy of how some companies, such as HFS, intend to compete. As is the case in other industries, this trend will likely favor larger, well-capitalized players. Even though most hospitality concerns should be able to afford the investment required to get up and running on a customer database, the costs of owning, operating and maintaining a large database are quite significant. However, it may have already become yet another cost of doing business.

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