



## Case Study

### Is the Customer "In Fashion" with Leading U.S. Retailers?

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#### **Synopsis**

A picture is worth a thousand words, but since CEO's don't generally paint pictures, we have to listen to what they say. One of the best opportunities to listen is when business leaders speak to the investment community. In these venues, one has to assume that the priorities outlined are indicative of a company's current strategic direction and the talk is straight.

Hanifin Loyalty has been doing some listening and it is interesting to observe the emphasis placed on the Customer in general, and Loyalty and Rewards programs in particular. For this Case Study, we read through recent transcripts of earnings calls among leading U.S. fashion retailers including [Macy's Inc.](#), [Nordstrom, Inc.](#), [Chico's FAS Inc.](#), [Neiman Marcus, Inc.](#), and [Saks, Inc.](#) All of the transcripts may be found on [Seeking Alpha](#), and we have included source URL's at the end of this document as reference.

We searched each transcript for the words "Customer", "Loyalty", and "Rewards", believing that higher instances of each word would lead us to conversations about customer oriented marketing strategy. Only in the Nordstrom transcript did all three words appear. In the others, "Customer" was sprinkled about in various degrees, sometimes with obvious emphasis, though too often just in passing reference to improvements in "Customer Service".

This Case Study provides one angle of insight into just how "top of mind" the Customer is for leading U.S. fashion retailers as well as their emphasis on Customer Loyalty in today's market. By correlating these findings with stock price performance over the past year, there may even be a link between a retailer's view of the customer and its future financial performance.



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### **Nordstrom**

Customers took center stage with Nordstroms and Blake W. Nordstrom, President, treated customer centric marketing as a central theme of the company's 4th Quarter earnings call held on 2/23/09. The words Loyalty and Rewards were less evident and were introduced only in discussion of the company's store charge card.

Mr. Nordstrom summed up the importance of customer-centric marketing efforts by saying "The investments we've made in the last five years to enhance the one-on-one relationships our sales people have with our customers are more important to our business than ever."

The company is leveraging all available sales channels to improve performance, combining online shopping with in-store pick up, personal shopping services, and its fashion rewards program to meet customers where they are most comfortable shopping.

Nordstrom highly values its credit card business as Mr. Nordstrom explained "Our credit card business is a crucial part of our integrated business model and we strongly believe our credit card products and service enhance our ability to earn and retain the loyalty of our customers."

During the fall of 2008, the company identified that it was "in unprecedented times and customers are lacking confidence". While the loyal Nordstrom core customer still desired quality and fashion, they were also shopping less, making more deliberate purchases, and emphasizing value more than in recent years.

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To sustain the loyalty of "best customers", Nordstrom made a decision "to aggressively use our Nordstrom rewards program to encourage customers to shop with us." The company began offering double points, and even held a triple rewards event in September to encourage shopping at the beginning of the fall season.

Nordstrom's perspective on Rewards programs is unwavering as Mr. Nordstrom stated in the 3<sup>rd</sup> Quarter earnings call "Overall we believe our rewards program deepens the connection we have with our customers and adds significant value to their overall experience , while allowing us to maintain the integrity of our pricing."

This is a **key insight** as some marketers fear that Loyalty programs will erode margins. Just the opposite, says Nordstrom, indicating that loyal customers will continue to shop without enticement by non-targeted discounting.



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Nordstrom also understands the subtleties between promotions and rewards as tactics to encourage long term loyalty. In response to an investor question, Mr. Nordstrom replied "it's (the rewards program) much different than just a blanket percentage off. It's a way of being able to cultivate our best customers and being able to develop that relationship even further in a more targeted way.... we've tried some of those things. For the most part, I think they have worked out well for us."

#### **Macy's**

The retailer with the largest market capitalization included in this Case Study is placing corporate emphasis in tough times on **cost cutting and operational efficiency**. The Customer was mentioned only once during the Q4 2008 earnings call dated 2/24/09 and Loyalty and Rewards were absent in the conversation.

Karen M. Hoguet, Chief Financial Officer & Executive Vice President, talked about how customers like to shop and which sales channels they prefer "Customers shop in stores and then buy on line or the reverse.....they buy online and return in the stores and do other shopping while they are there....tight channel integration is going to continue to help the company as we go forward."

Otherwise, the focus is on running a tighter ship. Macy's plans to cut capital spending by \$450 million, save \$138 million in dividend expense, and reduce interest expense by \$7 million through debt restructuring.

Companion to the corporate cost cutting is investment in the "My Macy's" structure which is designed to "better localize our offering market-by-market and drive comp store sales". Ms. Hoguet commented that to make My Macy's work, "the people part of this is very important because we believe the merchandising and planning talent that we were able to take last year from the divisions that were being consolidated help accelerate our success in the new My Macy's district".

We have to respect the fiduciary responsibility being carried out by Macy's but the report had the ring of a company being led by its financial engineers. We only hope that Macy's doesn't put the customer in the back seat for too long.

#### **Neiman Marcus, Inc.**

The Neiman Marcus In Circle loyalty program (<http://www.incircle.com/>) is universally regarded as one of the most effectively structured and managed loyalty programs in U.S. retailing. Given the company's stature as a purveyor of clothing and accessories to an affluent audience, one would assume that the company's marketing focus would not stray far from the magic words: Customer, Loyalty, and Rewards.



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Not so. In our search of the First Quarter FY09 results dated 12/10/08, the words Loyalty and Rewards were noticeable by their absence. Read between the lines, however, and it is clear that scarcity of searchable syntax does not deny the company's commitment to fine customer service and personal attention.

Burton M. Tansky, President and Chief Executive Officer, outlined how the typical Neiman Marcus customer might be thinking these days: "We believe our most loyal customer still has the financial ability to shop with us, however, the uncertainty that is prevalent in the economic landscape has caused her to pull back on the quantity of her purchases.... Although she might have temporarily reduced her total spend, she still has a very strong desire for the quality of merchandise and the level of customer service that we offer."

Mr. Tansky seems convinced that while consumer demand exists, a greater marketing effort will be required to trigger store visits and purchase transactions. Neiman Marcus favors a mix of special events, exclusive merchandise offers, and a continuance of the historically strong NM customer service. As good as the tangible benefits of In Circle are, building loyalty to a luxury brand requires more and NM knows how to deliver.

There is **risk in gravitating towards the promotional side of retailing** and Mr. Tansky echoed similar comments from Nordstrom by stating "the promotional environment in our sector is more aggressive than we have seen in many, many years. We anticipate that the level of promotions will continue and as a result our margins will be under pressure."

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#### Saks

Saks has stated in public forum that its Loyalty Marketing efforts have been and will be tied to its credit payment products. The company uses a loyalty model that rewards points for purchases made with either the Saks Fifth Avenue MasterCard or SAKSFIRST credit card.

In the 4<sup>th</sup> Quarter 2008 earnings call dated 2/25/09, neither Loyalty or Rewards were mentioned by the presenters. Instead the focus of marketing comments was on temporary promotions designed to pump up sales in the midst of a flagging economy.

Speaking of curing an "imbalance in supply and demand" during the tough fall of 2008, Stephen I. Sadove, Chairman and Chief Executive Officer, elaborated "We developed a contingency plan to implement a much more aggressive promotional program if consumer demand continued to decelerate. When our customers did not respond to our annual private night sale in early November which offered 40% discounts on certain merchandise, we made the decision to execute the contingency plan and accelerate our post Thanksgiving Day sale activity by one week, in effect **taking already reduced product to 70% off** and to advance the sale break of our designer product by one week to meet competition".



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In a panel discussion featuring representatives of Best Buy, Macy's and Saks at Source Media's Card Forum 2009 on April 21, there was general agreement that consumers are hesitant to purchase at the first sign of discounts and wait for second and third tiers of price reduction before triggering a purchase decision. None of the presenters would be pinned to a specific figure, but there was general agreement that discounts needed to be 40% or more in order to motivate consumers to open their wallets.

Mr. Sadove pointed out the benefits of promotional discounting, saying "The increased discounts were very successful in reducing total inventory, and we were able to sell-through a high percentage of our clearance product".

Our conclusion is that Saks won the battle with these deep discounts, but a more enduring and well rounded strategy will be required as time goes along. The **limited tender loyalty strategy may create a hindrance** to bringing customers back as consumer attitudes towards credit products continue to change during this economic cycle and debit cards become increasingly attractive to shoppers in the future.

#### **Chico's FAS, Inc.**

Of the retailers studied for this document, Chico's may be the one least like the others. Judged by size, the company has a market capitalization of \$1.32 Billion, more than Saks, but does not operate a multi-department model nor market to the high fashion segment.

Still, the successful legacy of Loyalty Marketing at Chico's is undeniable and we could not resist including them here. Surprisingly, in the 4<sup>th</sup> Quarter 2008 earnings call dated 3/3/09, there was no explicit use of the terms Loyalty or Rewards.

Chico's FAS, Inc. sells its own brand of clothing and accessories to a well defined female audience with moderate to high income level and a desire for clothes that are casual and comfortable. Chico's "Passport Club" has been widely studied and was said to account for over 80% of sales in 2006. That's significant by anyone's measure.

David F. Dyer, Chief Executive Officer, described the company's commitment to understanding its customer and delivering excellent customer service across the board "The entire company is reenergized and focused on improving our performance and serving our customers. I've spent significant time in the stores listening to our customers and to the field organization and time here in Fort Myers listening to what our headquarters staff has to say".



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Mr. Dyer expressed confidence that the core Chico's audience remains passionate for the brand and is "rooting for our success", continuing that "we've become just a little too predictable and a little too cookie cutter, from store design to store assortment. Increased non-selling tasks have distracted our associates from job number one and that is delivering amazing personal service".

Clearly **the focus on customer service** will be reenergized in Chico's stores, though no tie in of these efforts to Passport Club was mentioned.

#### Summary

Increased use of promotional discounting by Neiman Marcus and Saks suggest how their marketing budgets may be allocated over the remainder of 2009. In addition, Saks will continue to revolve its loyalty efforts around credit payment products. Cost cutting efforts by Macy's define their approach to the market, and Chico's seems intent on fortifying customer service efforts.

Each of these strategies may pay dividends in swaying purchase decisions until the economy strengthens, but will need evolution to engage shoppers as consumer confidence rebounds.

Nordstrom seems to possess a well rounded approach to building customer loyalty and provided the most explicit view of a cohesive strategy. With foundations in the one-to-one relationships created over recent years, Nordstrom will combine its credit payment product, Loyalty program, and customer service to deliver a balanced and effective value proposition for its customers.

Seeking links between customer-centric marketing and financial performance, Hanifin Loyalty reviewed the performance of each retailer's stock over the past 12 months.

Neiman Marcus Group was not included as it was acquired by two private equity firms in 2005 and no longer has a publicly-traded stock.

Results are summarized in the table below.

	Mkt Cap	Price 5/1/09	52 Wk High	52 Wk Low	EPS	P/E
Macy's	5.68 B	13.47	27.08	5.07	-11.4	n/a
Nordstrom	4.85 B	22.53	38.65	6.61	1.83	12.3
Chico's	1.32 B	7.45	8.18	1.72	-0.11	n/a
Saks	709.7 M	5.02	14.58	1.5	-1.12	n/a



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While it is too early to present authoritative quantitative evidence, early findings reveal that Nordstrom has outperformed this competitive group for the moment. Whether this suggests a tangible link between customer-centric marketing strategy and financial performance remains to be seen, and Hanifin Loyalty will continue to track these figures going forward.

Regardless of today's confidence level in this linkage, we wouldn't bet against a customer-centric strategy as the path to success for U.S. fashion retailers. Shoppers in this segment have never felt more entitled to a first rate shopping experience and want to be rewarded and recognized for their patronage.

Cost cutting and inventory management are undeniably sensible in tough times, but when combined with non-targeted store-wide discounting, may impact hard earned brand reputations.

Now is the time to leverage historical data for "best" customers and ensure that these loyal customers remain so as the economy improves.

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**Footnote:**

*All quotations for each retailer came from transcripts published by Seeking Alpha:*

**Nordstrom:**

*2/23/09 4<sup>th</sup> Quarter earnings call*

*<http://seekingalpha.com/article/122160-nordstrom-f4q08-qtr-end-1-31-09-earnings-call-transcript?page=-1&find=customer>*

*11/13/08 3<sup>rd</sup> Quarter earnings call*

*<http://seekingalpha.com/article/105943-nordstrom-f3q08-qtr-end-11-1-08-earnings-call-transcript>*

**Macy's:**

*<http://seekingalpha.com/article/122398-macys-inc-q4-2008-earnings-call-transcript>*

**Neiman Marcus:**

*<http://seekingalpha.com/article/110182-neiman-marcus-inc-f1q09-qtr-end-11-01-08-earnings-call-transcript>*

**Saks:**

*<http://seekingalpha.com/article/122696-saks-q4-2008-earnings-call-transcriptv>*

**Chico's:**

*<http://seekingalpha.com/article/123886-chico-s-fas-inc-f4q08-qtr-end-1-31-09-earnings-call-transcript>*

**Seeking Alpha:**

*<http://seekingalpha.com/>*