

# WHY LOYALTY POINTS PROGRAMMES WORK NOW AND WHAT IS THEIR FUTURE

*Loyalty points have come a long way from primitive beginnings and their development is accelerating. Ignore them at your peril.*

Loyalty points are not a new invention, but increasingly sophisticated technology and the falling expense of collecting and storing data have recently combined to allow loyalty points to become an integral part of any enterprise's marketing strategy. As we shall see they provide insight and knowledge about an enterprise's most valuable customers.

In this article we will explore the world of loyalty points, the advantages to the issuers of points and their marketing departments, and the benefits that points programmes have for consumers. We will also make some predictions as to where loyalty points will be heading in the future.

## *The Beginning*

One might postulate that loyalty points programmes began with the "green stamp" phenomena found in various forms in Europe and North America in the 50s and 60s. Usually issued by grocery chains, consumers would collect booklets fill them with stamps in order to be able to exchange them for merchandise. These predecessors differed in one significant aspect from their modern day counterparts: they were a one-way communication. The issuer merely rewarded frequent purchases; it did not collect any information about them. Today's loyalty programmes are decidedly two-way. In exchange for loyalty points, issuers collect a substantial amount of information from their frequent customers including demographic, geographic, and purchase behaviour, and often link it to lifestyle and psychographic data collected independently through market research.

## *Issuers*

Airlines are arguably at the leading edge of modern day loyalty programmes, issuing points in the form of "miles" redeemable for travel and other rewards. Other issuers include grocery and retail chains, car rental companies, hotel chains, gas/petrol station companies, credit card companies and most recently banks and financial service companies. We even know of a government-owned liquor monopoly that issues loyalty points, but cannot fathom the rationale for doing so since if a consumer wants to purchase wine or spirits there is only one supplier, so how issuing points increases loyalty is beyond us!

## *Behavioural Impact*

There is no question that issuing points changes consumer behaviour. During the latter part of the 70s and through to the mid 90s there were two principal airlines operating in Canada, both of which issued airline miles. Repeatedly, travellers would go out of their way to select flights operated by the airline from which they were accumulating points, often committing to more complex or longer itineraries purely to maximize point accumulation. Issuing loyalty points can clearly have a strong effect in inducing behavioural loyalty and continuous repeat purchases for a company.

Simultaneously, loyalty point issuing programmes can be an additional means of differentiation, particularly in commodity markets. Petrol/gas station companies have employed these programmes success-

*« Be an additional means of differentiation »*

fully. Although we do have to caution that often the rewards/value offered can be quickly replicated by competitors and soon as this is done, the playing field becomes level once more with the consumer the only winner!

Retail stores use loyalty points to influence consumer behaviour successfully by offering incentives such as “double points” on the introduction of new lines of products. Simple tags underneath the shelf space of such new lines are sufficient to tempt trial customers.

### *Information is Power*

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Although motivating different human behaviour is a primal reason for employing loyalty points programmes, a secondary benefit which is potentially more powerful, is the use of data garnered from such programmes. More often than not, an enterprise’s customers are shrouded in anonymity with little or no dialogue taking place. The introduction of a loyalty points programme enables light to be thrown on the huge vista of a customer-base.

Suddenly, one can begin to classify one’s customers according to where they live, their preferred purchases, the frequency of those purchases, and, depending on the information collected during the sign-up process, a large amount of demographic data such as age, marital status, dependents, etc. Models of customer profitability can be constructed allowing for much more informed business decisions. For example a drug store chain is able to learn a lot about the catchment area of each of its locations and the demographic purchasing patterns of customers in each catchment area. This allows for sophisticated consumer segmentation matrices to be built, which in turn enable an enterprise to deliver relevant, specific and high value offers to their customers.

Again, airlines have progressed a long way in this art, segmenting their customers according to travel patterns, differentiating between different types of leisure and business travel as well as the total spend by each individual customer. Not only do they use this information to plan their business strategy using predictive modelling techniques, but also they use it to create attractive value propositions for all levels of customers. Without doubt the array of rewards including upgrades, free flights, specific vacation opportunities, etc. they offer to their most profitable customers induces a high degree of loyalty and increased

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“share of wallet” from them. In fact, Aeroplan, (the loyalty points business unit of Air Canada), will shortly be taking its profound knowledge and expertise in this area into an independent enterprise dedicated to providing other companies with services that will enable them to build and maximise the use of their own loyalty points programmes.

### *Consumer Benefits*

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We do have one word of caution for any company embarking on a loyalty points programme: often too much emphasis in the design is put on how it will enrich the business decision processes for the company itself, and not enough thought or calculation is given to the benefits for the consumer.

Consumers are increasingly savvy concerning these programmes and will shun those that do not provide sufficient benefit in return for the information they provide in exchange to the issuing company.

Collectors of loyalty points reap both tangible and intangible benefits. At the tangible, and most simplistic level, points are collected to obtain a discount on a future purchase. Consumers have always rationally been attracted by discounts. For example, the prospect of being able to obtain free train tickets from a North American railway company not only draws in a large customer base but also attracts traffic away from the competing short haul flight and coach competitors.

Yet it is perhaps the intangible benefits to the customer that have more power in the long run. Receiving

the tacit recognition of being a loyal customer is reinforcing and gratifying in and of itself. Giving customers higher tiers of recognition in return for greater business works for them. The top tier/gold customers feel their status and it adds to their personal identity. Gold and Platinum credit cards used to have the same effect until they became so completely devalued. We also believe that consumers derive a sense of virtue out of accumulating points as a form of well earned saving.

Naturally, a carefully designed combination of both tangible and intangible benefits creates the most powerful appeal. Consumers appreciate the benefits of being given special service treatment for consistent repeat purchase behaviour. It becomes a virtuous circle: preferential treatment of the most valuable customers lead to greater consumption by them which makes them even more profitable to the company, and so on.

For example, access to private lounges provided by airlines to their most frequent flyers is a much sought-after benefit of airline loyalty programmes. We have known instances when an airline has tried to reduce some of the benefits to its top tier customers and met with verbal outrage. Customers can become passionate about the benefits of their loyalty programmes!

### *The Future*

We believe loyalty point programmes are still in their infancy. At the moment, they tend to be administered on a rather remote basis, usually by means of mailed out statements. Furthermore, they are fragmented with individual companies each having their own programme. This will change radically in the next few years.

Loyalty point programmes will become much more immediate, and with points being instantly redeemable at the point of sale, with statements available instantly online.

Redemptions of points will become more intimately tailored to an individual consumer's preferences. They will not be restricted to just more goods and services provided by the issuer but will be opened up to a whole gamut of selection and choice.

Furthermore, we predict consolidation across different geographies and industries. Loyalty point programmes will become "clubs" where one participant



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between consumers and supplier. »*

from each industry in each geography will become an issuing member of a particular club. Redemption of points will be able to occur across the industries and geographies of the clubs. Thus it will be strategically important for issuers to be the first in these clubs as they form. Exclusion would be a permanent competitive disadvantage.

Clearly, the data shared amongst the club participants will be very much richer in this scenario. A participating company will not only have the consumer behavioural data associated with the purchases of their own goods and services, but also that of the other participants, thus enabling complete life-style and preference pictures of their consumers to be built on real data. The ability to build value propositions that truly anticipate each individual consumer's expectations will become a closer reality.

Above all, however, we believe that loyalty programmes will begin to metamorphose into vehicles for continuous dialogue between consumer and supplier. They will become the platform from which they intercommunicate, and more insightful and understanding relationships will be built – a far cry from the early beginnings of "green stamps".

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