



LOYALTY PROGRAMS: BUILDING CUSTOMER LOYALTY TO BUILD PROFITS

“Loyalty is one of the great engines of business success.”

Frederick F. Reicheld, author of *The Loyalty Effect*

Today's successful businesses recognize the importance of customer retention in their efforts to grow operational profits. To achieve this, more and more merchants are implementing loyalty programs as a competitive marketing strategy to build long-term relationships with customers, allocate marketing dollars based on the customer's value and derive as much as revenue as possible from them over a lifetime.

Of course, loyalty is more than a business strategy. It is an ongoing, two-way relationship based on respect, trust and commitment – a relationship in which the customer feels all-important. A successful loyalty program builds and nurtures such a relationship by accomplishing two critical tasks. The first is to gather information that will help merchants understand their customers' tastes, needs and expectations. The second is to offer recognition and rewards that are relevant to their customers as a reward for their loyalty – and as a trade for the personal and transactional data that starts the loyalty cycle and keeps it going. By tracking members' transactions, companies can identify the various segments of their customer base to create strategies that keep their customers coming back for more.

Customer Information is Key

Effective loyalty programs generate incremental spending – more dollars spent, more frequently, from customers whose needs and expectations are understood and met. With 80% of merchants' business being generated from as little as 20% of their customers, identifying and understanding their needs and expectations of this 20% is crucial. By gathering customer information, merchants can make intelligent marketing decisions that will keep their best and most profitable customers more loyal. They can also leverage this thinking to increase sales the under-performing segments of their customer base.

The most valuable loyalty programs to merchants are those which utilize advanced technology to collect data at the point of sale, track valuable information about customer purchase behavior, and provide access to rich database reports and analysis that can be used to increase the effectiveness of merchants' marketing campaigns.

What Customers Expect

Today's consumers are more savvy and sophisticated than ever. They expect loyalty programs to offer:

- Easy participation
- Instant rewards
- Flexible rewards
- Fast accumulation of rewards
- Rewards claimed at any participating establishment
- Special offers
- Instant win opportunities

Types of Rewards

Hard benefits and Soft Benefits

Loyalty program rewards can be classified into two main categories: hard benefits and soft benefits. Hard benefits appeal to the rational component of customer loyalty with "tangible" rewards such as free travel. Hard benefits compel customers to immediately take advantage of an extraordinary opportunity that may not last long. Conversely, soft benefits appeal to the emotional component of customer loyalty and are slower to reward. Discounts are considered soft benefits, as they require the member to spend in order to receive and do not differentiate merchants from the competition. Focusing the member's attention on price and not on the issue of a compelling reward, soft benefits are equally important to merchants' most valuable customers, whose loyalty demands legitimate evidence of their special status. Special status means special treatment, special deals, special access and special events - whatever it takes to reinforce the sense of importance of a merchant's top-tier, high-value customers. Defining soft benefits sets apart your relationship with your best customers, offering experiences unique to your product or service and unavailable to non-members.

Types of Loyalty Programs

Mid-market merchants or groups of merchants owned by a parent company will benefit from using a program that will enable them to increase their customer transactions and retention through points programs, electronic couponing, instant messaging and special offers, while the customer is present in their location – in real time, at the point of sale. There are several types of programs to choose from.

Merchant Benefits

Regardless of what type is chosen, an effective electronic loyalty program offers merchants:

- Automated marketing through the elimination of coupons, rolls of till tape, manual intervention or back-end processing required.
- Ability to target selected customers rather than employing blanket-marketing strategies.
- Ability to reward customers at point-of-sale rather than at another time, avoiding fulfillment costs.
- Ability to cost effectively run incentive programs for small transactions and modify programs regularly.
- Prevention of fraud and over-claiming
- Rewards tailored to various customer groups (ex., a restaurant's best customers can be automatically identified and given a better or increased reward over an infrequent guest)
- Compatibility with any and all payment methods
- Ability to operate multiple programs can simultaneously
- Multiple programs for each transaction
- Cross sell opportunities and incentives
- Ability to change parameters based on business cycles
- Detailed reports of transactions – purchases and redemption
- Re-loadable electronic gift cards and coupons

"Closed-Loop" Programs

A "closed-loop" loyalty program involves only one company or chain of locations within a particular industry, such as Marie Calendar's in the restaurant industry. In a closed-loop program, points are exchanged exclusively within participating outlets, greatly reducing the cost base of issued and outstanding points.

Closed-loop programs require a private-label or in-house co-branded credit card to enable transactions.

Using "Private Label" cards, national, regional and small to mid size merchants can operate their own "closed loop" loyalty programs. Generally, cardholders are instantly enrolled at the participating merchants' POS and in all cases a co-branded or generic private label card is issued to the party enrolling.

How "Closed-Loop", Private Label Programs Work:

"Private Label" programs are executed through the following steps:

- 1) Customer presents his or her designated (specific bank or affinity) credit card or "Private Label" Loyalty Card at a participating merchant
- 2) When the card is swiped through a certified terminal or electronic cash register system, the payment processing and customer transaction data are captured at the loyalty program's host.
- 3) The Merchant's financial institution handled credit/debit authorization as normal. There is no effect to the Merchant's existing banking or processing relationship.

- 4) The Loyalty Host recognizes loyalty transaction through encoded information and processes it accordingly. The customer has the option to redeem earned rewards at the point of sale or continue accumulating. The receipt generated from the Program Terminal provides the customer with a mini-statement each time they use their card.
- 5) The transaction details are collected, tracked and stored at the Loyalty Host's Data Warehouse, maintained by Global Loyalty.
- 6) Loyalty Host maintains the program's Data Warehouse and can produce specialized database marketing reports for the Merchant based on their requirements.
- 7) Merchants can disseminate precise information and implement innovative new marketing programs or judge the effectiveness of existing ones. Specific customer behavioral data opens the door to establish new markets while maintaining the needs of current ones.
- 8) At the point of sale, a Merchant can then inform his customers of new promotions, special privileges, events and increased rewards. A Merchant can also tailor a specific message (up to 160 characters) live, on-demand (host change required, done within 24 hrs), on all customer receipts.

Open/ Cross-Sell Programs

An "open" or cross-sell loyalty program involves multiple types of companies and industries. Participating merchants are typically national or regional chains (category killers) that do not compete for each other's customers, but share similar demographic and psychographic profiles.

An open program consists of a group of participating merchants that allow customers – cardholders – to earn and redeem points at each participating merchant within the group. For example, if Marie Calendar's were to become part of an open program with The Gap, a customer could use their Marie Calendar loyalty points at the Gap, and vice versa.

Using advanced systems developed by top-tier loyalty program specialists, chain merchants using their existing terminal or POS system can operate multiple cross-sell programs between departments and in parallel with other non-competitive chains. In an open or cross-sell program, revenues are generated from membership points (optional) and transaction fees and through system access fees and program set-up fees if applicable.

Real-Time Points Programs

Real-time points programs are a powerful tool for merchants to reward loyal customers for making purchases. Point are accumulated as a percentage of the dollar amount spend and a reward for frequenting your location. Points can be adjusted to align with merchants' seasonal business cycles (double points, bonus points, etc.).

All points are accrued and or redeemed at the POS in real-time. Points in effect instantly become an electronic currency that can be redeemed at all merchants

participating in the coalition program. This means merchants can avoid the hassle of producing expensive month-end statements for customers, and customers experience the excitement for instant gratification each time they use their card.

Real-time points programs offer POS instant statements that include customers' current point total, accrued balance, life time points and up to 360 characters of instant custom messaging or the printing of an electronic coupon.

Recent Innovations and Trends

Script programs

Script programs are becoming more and more common. Using a script program, merchants can attract and retain customers by giving a percentage of revenues to charitable organizations. For example, every time a customer uses his or her Club Card at a particular grocery chain, a percentage of the purchase would be contributed to a school system's Script program – meaning schools receive money from the grocery chain.

Customer Loyalty in Commerce

Customer loyalty is becoming a crucial issue in eCommerce. Competition is fierce, and with the free flow of information over the Internet, customers can discover competitive products in record time compared to the traditional world. With the marketing and advertising costs involved in starting up a new online business, acquiring customers online can be an expensive process. Therefore, retaining customers is critical.

The concept behind loyalty programs in the traditional world translates easily to the Internet. Given the wealth of customer tracking software already on the market and the continual evolution of technology to greater and greater levels of speed and efficiency, online loyalty programs

InterAuct, an auction site, rewards its members with points for every transaction conducted over the site. Points can be redeemed for items available to the InterAuct customer, or "The Preferred One," as the company tries to build prestige in the program. Again, as in the traditional world, information is key. Online loyalty programs must coax invisible customers into revealing information about them in order to gauge their potential as a customer.

Marketing Partner or Merchant Coalition Programs

A Marketing Partner Program is an on-line loyalty program that enables a credit card issuer to accrue and redeem points in real-time by purchasing goods and services from participating merchants. The program may include multiple marketing partners and participating merchants are acquired in close geographic proximity to the cardholder base of the marketing partner. A marketing partner represents a large, highly targeted and segmented customer base which may be national or regional in scope and in most cases already provide their cardholders with an electronically encoded transaction /tracking card. Examples include a financial institution's credit and debit cardholders,

telecommunication providers, ISP's, sport franchises and newspaper and magazine publishers.

Participating merchants in this program generally include a cross-section of lifestyle category merchants ranging from smaller independent merchants to regional or national chains. Revenues are generated in a marketing partner program predominately from membership points charged to participating cardholders (and liquidated through usage of the program) and transaction fees billed to merchants.

The program enables marketing partners to communicate with their cardholders through an instant statement combined with their credit card receipt. Statements can include point balances, instant wins, contests, electronic coupons and instant messaging.

Conclusion

Increased Customer Loyalty Results in Increased Profits

Electronic loyalty programs are proven to dramatically increase response rates and average customer spending. In particular, "Private Label" Card loyalty programs provide merchants with a flexible solution with little monetary investment, and minimize the need to participate in traditional direct mail or paper-based couponing programs. Recently, a Canadian restaurant chain using a Private Label card loyalty program increased transactions in terms of dollars spent by 15-20% on average.

In the long term, organizations will want to change their loyalty programs in some way in response to economic, competitive, seasonal and other conditions. Since changes or additions can be difficult, expensive and time consuming, ISO's should offer loyalty programs that accommodate quick and cost-efficient modification based on individual merchant's needs and objectives.

AUTHOR---RICHARD TRIEBER
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