



GETTING YOUR LOYALTY PROGRAMME TO WORK FOR YOU

Many marketers believe that loyalty programmes are passé. The flaws, however, are in the execution — not in the concept

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Modern-day loyalty programmes first came into being in the 1970s in the airline industry. These programmes were originally launched with a motive of gathering data on the most popular routes. Airlines soon realised the underlying marketing opportunity and began giving frequent-flier miles as rewards. Hospitality, leisure, retail, FMCG, cinema multiplexes and credit card providers followed suit. The apparent

success of companies like Tesco's Clubcard and Neiman Marcus' InCircle programme convinced many retailers that a loyalty programme was critical to success. Further impetus came in the 1990s due to increased competitive activity, advances in technology and the evolution of marketing analytics. Today there are very few consumer categories without a loyalty programme.

However, despite the increased prevalence of loyalty programmes, questions remain over their effectiveness and their role is greatly misunder-



Jet Airways aircraft stand on the tarmac at the domestic airport terminal in Mumbai

PHOTOS: REUTERS

stood. Do such programmes really create loyalty? Do the returns on such initiatives justify their expense? Or is this simply another form of discounting that retailers are being forced into because of competitive pressures?

The evidence is mixed. There are several programmes that have been outstanding successes in meeting their business objectives. Examples include American Express, Harrah's Entertainment, Neiman Marcus, Harley Davidson, Tesco's and Jet Airways. However, a majority of programmes are still losing propositions. In our research, we find that marketers who set out clear objectives and align their programme design to these objectives are able to create benefits for themselves and for their consumers. On the other hand, lack of design clarity and copycat tendencies have destroyed many programmes — and caused all-round dissonance.

The failure of loyalty programmes is down to four fatal flaws:

■ **Lack of clear objective setting:** A loyalty programme is one of many marketing initiatives that managers can use to build brand equity. Therefore, like any other initiative, loyalty programmes need to be properly designed and executed effectively to deliver a significant RoI. Well-designed loyalty programmes can be used to increase market share, understand consumer behaviour, introduce new products and build a buzz around the brand at significantly lower costs. Unfortunately, far too many

MEASURING YOUR LOYALTY PROGRAMME

If you're struggling to understand or justify the effectiveness of your loyalty programme, the following questions may help:

- Why did your brand create a loyalty programme? What were the starting objectives? Are these objectives clear or blurred?
- Did you make these objectives an integral part of the programme design?
- Have you created the metrics that track success against these objectives? Is the brand *really* using any of the customer data that has been collected?
- When is the last time you refreshed your programme? Does your design provide a differentiation from other brands?
- Would you want to be part of your own programme? Are the benefits compelling enough for you give up another brand for it?

companies start a loyalty programme as a competitive response, with little clarity on the objectives of their programme — or how they will use it to create differentiation. As a result, they create me-too programmes which ultimately become cash sinks with little benefit to the company.

■ **Not thinking through the design:** Most companies try to cater to all possible customers with their programme. By not adopting a segmented

FEW PROGRAMMES ARE DIFFERENTIATING ON DESIGN

Programme structure	Brand						
	A	B	C	D	E	F	G
Membership cost / minimum fees	Purchase of Rs 5,000	First purchase	Single purchase of Rs 7,500	Purchase of Rs 4,000	Fee of Rs 150	Purchase of Rs 2,500	Purchase of Rs 2,000 and fee of Rs 150
Number of tiers	4	2	2	3	3	4	2
Reward %	2%, 5%, 7%	NA	NA	NA	0.7%-2.1%	NA	2%, 2.5%
Redemption threshold	200 points (Rs 10,000)	NA	NA	NA	None	NA	200 points (Rs 10,000)
Rewards	Gift vouchers	10% off (for platinum)	5-10% off ¹	Gifts (goods & vouchers)	Redemption vouchers	5-10% discount ¹	POS discount
Benefits	<ul style="list-style-type: none"> • Valet parking • Exchange policy • Offers at hotels / airport lounges • Monogramming • Previews • Event invites 						
	<ul style="list-style-type: none"> • Information updates • Previews • Event invites 						
	<ul style="list-style-type: none"> • Add-on card given to spouse on total of Rs 50,000 						

1. Depending upon membership tier. Source: MXV Research

approach, they struggle to develop a compelling proposition for their truly valuable and otherwise loyal customers. Effective programmes ensure that the benefits and spends are closely aligned with the lifetime value of the customers, as well as their purchase behaviour.

■ **Failing to understand the economics:** The key difference between any other marketing initiatives and a loyalty programme is the exit cost. A loyalty programme has long-term implications on the brand and its profitability, and requires careful analysis. Customers are being encouraged to move from transactional behaviour to a relationship — and the company needs to keep up its end of the bargain.

If that relationship were to degenerate into an “on-today-off-tomorrow” scenario, the impact on the brand could be severe. Again, we find that too many brands underestimate the costs and efforts of running the programme and overestimate the impact on loyalty and revenues. They are then forced to find face-saving ways to exit the programme.

■ Creating static programmes that fail to engage:

Few companies are able to maintain consumer excitement after a point of time. At best, they degenerate to cash-back schemes or databases for mailing. This happens once the strategic focus is lost. Engagement comes from staying relevant. Like other marketing efforts loyalty programmes also need to

THINKING THROUGH THE ECONOMICS

Analysis of a cinema chain's loyalty programme

■ Direct cost of running the programme

- For a customer who spends Rs 100 on a ticket and Rs 50 on concessions: Points earned = 20
- Assuming cost of concessions = 30% of sale price, redemption value = Rs 6
- Effective pay-back to the customer = Rs 6/Rs 150 = 4%

■ This does not include the cost of card printing, marketing materials, telephone agents, help desk, separate counters etc

- Overall cost likely to be ~ 5-6%

■ Assuming overall contribution margins of 50%, the volume increase is required to be 10-12% in order to break even on the programme

- Since 70% are unlikely to show any volume increase, the other 30% must have an increase of 33-40%, a very ambitious target for the programme

⇒ Our analysis suggested that the programme would be loss-making. As it turned out, the company was forced to withdraw from the scheme and cut its losses

continuously evolve with the changing consumer and competitive landscape. Analytics can be used to sharpen consumer behaviour understanding and tailor-make new consumer offerings and experiences. There are huge rewards for those who retain this focus.

Clarity of objectives

In our discussions with marketers, we often start with the obvious question — “What does the organisation intend to achieve through this programme?” Shockingly few companies provide a clear response to this question. We believe that a loyalty programme must have a definitive business objective with clearly defined metrics and RoI expectations. Not having such an expectation causes the programme to be treated as a cost centre and eventually reduces it to a discounting scheme.

There are at least three definite objectives that a company may have from its loyalty initiative:

Active Harley Owners’ Group members are so aligned with the brand that they spend considerably more on vehicle purchases, parts and accessories

■ **Increase in sales and market share:** Keeping customers in by serving them better

A loyalty programme offers an unparalleled opportunity to sharpen consumer understanding and use that to design new

consumer offerings and experiences. Consumer responses to these new offerings can be fed again into the analytics engine and the brand offering tweaked again. This continuous, two-way communication helps a brand align itself closely with consumers’ needs and behaviour — offering products and services that are more valuable to them. In turn, this leads to a significant preference for the brand’s offerings amongst its loyal consumers. With time, this preference leads to a greater share of the wallet and a significant barrier for competition to overcome. In the case of Harrah’s Entertainment, their loyalty programme helped identify their most profitable consumer segment (not the high-rollers!) and design their service experience accordingly. As a result, they managed to

Harley Davidson employees and biking enthusiasts prepare to ride Harley Davidson motorcycles during a promotional event in Mumbai



achieve significantly higher share of wallet among their target group.

■ **Increase in profitability:
Focussed marketing spends**

A loyalty programme allows companies to create a database capturing different facets about their consumers' lives and behaviour. Marketers can use this data to reach out to their regular and potential consumers in a much more scientific manner, eliminating significant wastage. The content of the message can be tailored to the consumer's specific needs. The right combination of these factors improves response rates dramatically (by a multiple of two-five times). Tesco has used such database marketing to achieve dominance in the UK market. The company has developed 5,000 customer "needs" segments, with each segment receiving personalised coupons. Their coupon redemption rate is as high as 90 per cent.

■ **Increase in brand value:
Expanding the consumer franchise**

Consumers today are surrounded by very high levels of media clutter. Having a loyalty programme allows the creation of touch points at low cost and creates a two-way communication channel with regular consumers. This ensures that the brand retains top-of-mind awareness and remains in the consideration set for future purchases. The company

A loyalty programme must have a definitive business objective with clearly defined metrics and return-on-investment expectations

develops the ability to take a specific consumer through successive positive experiences. This converts many of them into Brand Ambassadors who do an evangelist's job of converting more and more people to the brand.

Harley Davidson, through its Harley Owners' Group programme, reaps the benefit of increased brand value. Active HOG members are so aligned with the brand and its experience that they spend considerably more on vehicle purchases, parts and accessories and general merchandise, and are instrumental in raising awareness about the brand.

Getting the customer to care

Good loyalty programmes are like two-way streets bringing benefits both to brands and consumers. During the design stage, one must therefore ask "What is in it for the consumer?" and "Is there value in what we are offering?"

There are fundamentally five ways in which an organisation can use a loyalty programme to reward customers:

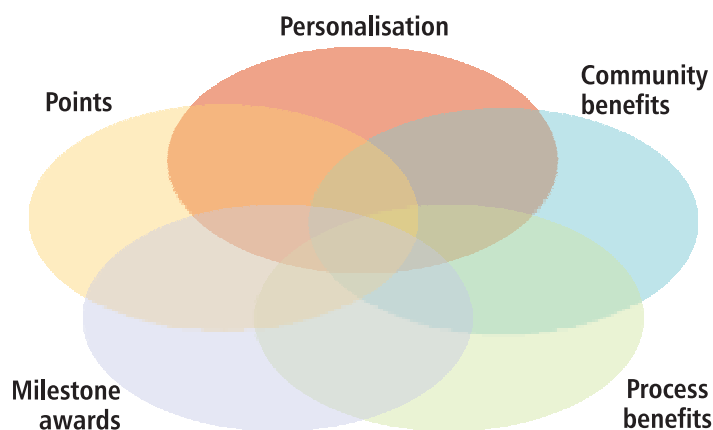
■ **Points**

This is the most common mechanism used across programmes. Despite the simplicity and universal usage of this lever, it remains a very strong driver of consumer loyalty. This tool works best where there are high-value and repeat purchases (airlines, hotels), but also works well even when with lower-value but frequent transactions (books, music). However, points can be expensive — and must be given with care. Many marketers struggle to justify the RoI on the points they give out (Indian cinema chains fell in this trap a few years back). On the other extreme, some marketers try to retain complete control over their points system — to the extent that they do not even disclose the pay-back process to customers. Naturally, such schemes are not very attractive to consumers.

■ **Milestone awards**

Milestone rewards offer a subtle and important variation to the points system — by creating an "accomplishment" orientation among consumers. There is really nothing for a consumer to feel pleased about upon completing 50 flights on an airline, nor on

FIVE TYPES OF REWARDS



HARLEY DAVIDSON HAS TAKEN COMMUNITY BUILDING TO A NEW LEVEL

Membership benefits (for full members; Associate members have limited programme benefits)

- HOG membership manual
- HOG touring Handbook
- Enthusiast magazine (3 times a year): Published since 1916 - the oldest continually published motorcycle magazine in the world
- HOG tales (6 times a year): Official publication of HOG
- Members only site: Information on HOG events, pre and post event coverage. Person can also renew memberships, register for rallies, request a new card, update profiles etc
- HOG Ride and Fly: fly to nearly 40 locations in the US, Canada, Europe and Australia. Pick-up a Harley Davidson from a local dealer and tour (paid)
- HOG Hospitality: Hospitality areas at HOG events
- Open Houses: Factory open houses to see how a Harley is made
- Rallies and events: National, international, state and touring event
- Chapter meetings (Monthly meetings, Dinner rides, Parades, Observation runs, Toy runs for charity, Holiday events)

Earning rewards

- ABCs of Touring: Objective is to visit cities, towns, countries beginning with as many different letters of the alphabet as possible
- Points for attending rallies, visiting national parks or forests as well as Harley Davidson facilities.
- Prizes at the end of the year and winners featured in HOG tales and the members website
- Mileage programme: Pins, patches and medallions awarded for miles completed on a Harley Davidson. Mileage checked by an authorised dealer
- Safe rider skills
- Prizes given for writing LOH memories
- Pins and patches awarded for event participation

Source: Harley Davidson

spending Rs 25,000 at a retailer. If at all, the consumer would feel upset about the amount she has travelled, or spent! But, by creating a milestone reward, marketers can actually make a consumer want to take that 50th flight or spend that extra Rs 649. The milestone reward is a very clever marketing tool that can dramatically impact buying behaviour leading to significant consolidation as a person gets close to the reward. Jet Airways very successfully exploits this tool to drive consumer behaviour in its favour.

■ Process benefits

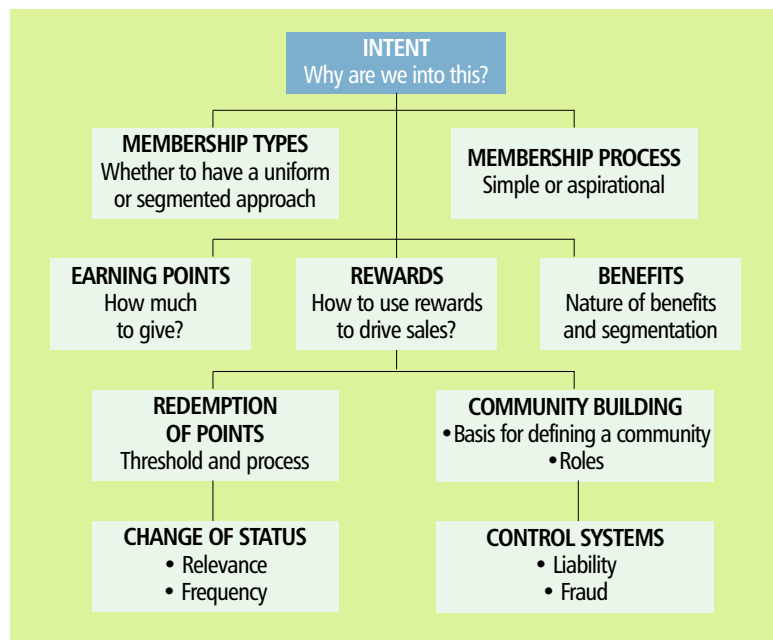
Every customer likes to be treated special. Loyalty programmes allow a company to create the right kind of recognition and services to be provided to customers. Importantly, this can now be done at the organisational level — and is not solely dependent on individuals. Harrah's Entertainment uses data from its programme to segment and design its services accordingly. It delivers visible recognition that customers have gotten accustomed to. As a result it has among the most devoted and loyal customers in the casino industry — one that is notoriously poor on loyalty.

■ Community benefits

Wherever the involvement with the product is strong, there is an opportunity to build and harness a community of users who in turn become evangelists for the brand. Harley Davidson has done this brilliantly. Harley Owner's Group (HOG) is a vibrant community of more than one million passionate bikers with 1,400 chapters worldwide. Harley organises biking events for its customers across the world and has created a community of bikers throughout the world, enabling them to share their passion for driving bikes and to have fun in the process. Naturally, the community has become a very powerful and visible symbol of the Harley experience.

■ Personalisation

The most desired, but not necessarily the hardest to deliver, benefits lie in the form of personalisation. Given the advancements in consumer analytics and technology, it is possible to understand and design distinctive benefits for individual consumers. Many variations of this theme are provided to the top-end customers of a brand. However, personalisation can be delivered in many ways. The Leaders Club is a three-tiered programme run by the "Leading Hotels of the World". At all three levels, members receive room upgrades, early check-



Harrah's loyalty programme helped identify its most profitable consumer segment and design its service experience accordingly



File photo of a view of the marquee sign in front of the Harrah's Las Vegas casino on the Las Vegas Strip

LOYALTY PROGRAMMES WORK BEST WHEN ALL THE ELEMENTS COME TOGETHER

Tesco:
Understand and drive customer behaviour

- Free, easy membership – maximise participation
- Cost minimisation: 1% rewards
- Significant analytics capabilities
- Drive behaviour: Coupons, not discounts
- Create communities around buying behaviour

Jet Airways:
Retain top-tier customers

- Segment customers – Tiers increased from 1->3->5
- Spoil top tier customers with upgrades, process privileges – create significant incentive to consolidate spending
- Extensive and relevant partner network
- Minimal expense on base customers

Harley-Davidson:
Create a cult brand using emotional appeal

- Build community of people with a passion for riding
- Well organised, large, aspirational events where participation is restricted to members
- Forums for people to share experiences and deepen their passion
- Rewards linked to riding and greater use of product
- Rewards centred around community recognition

in, late check-out and welcome gifts. However, the primary benefit is a personal information registry, which is shared among all Leading Hotels to ensure that every hotel can deliver custom-tailored service, with every stay.

Come together!

Getting a loyalty programme to work is not magic — but it does take a certain amount of art. The key is to get right the alignment among programme objectives, design and its actual implementation. MXV Consulting has developed a 10-point framework that helps structure and evaluate a loyalty programme. This is illustrated below:

On each of the design parameters, there are best (and worst!) practices that can be seen in the marketplace. MXV's research of 50 such programmes has helped identify more than 40 best practices in the area. For successful programmes, the starting point is a clear definition of the objective(s) of the initiative and then using that as



A shopper enters a Neiman Marcus store in a Chicago suburb

the criteria for the rest of the design process. We list below three examples of such programmes — where the intent is firmly driven through the design and implementation. Each of these has been successful in building and retaining their con-

sumer franchise, and in reducing the cost of marketing for the brand.

Metrics that work

Like any marketing initiative, a loyalty programme needs to have clear metrics that link to the overall objectives. By developing a balanced set of measures, it becomes possible to assess the effectiveness of the initiative and identify levers that need to be tweaked. Some sample metrics are outlined on the left.

Creating the right set of metrics goes a long way in ensuring a high return on marketing investments. In our experience, however, we have rarely seen more than a couple of basic measures of programme effectiveness. Few marketing managers are able to provide a convincing estimate of the metrics mentioned above. And, in a telling indictment of most loyalty programmes, the most common number we hear is the “total outflow” from the company. **IM**

SAMPLE METRICS

Programme objectives	Sample metrics
Build knowledge of buying behaviour and use as part of marketing strategy	Percentage of customers / transactions covered under loyalty programme Conversion rate on each DM campaign Overall sales growth by tier Overall cost of marketing as percentage of sales
Provide service that is differentiated enough to be an exit barrier for the consumer	Spend per person before and after entering the tier Percentage of members who retain their status
Create a reason for the person to consolidate spends with the brand	Number of purchases per customer p.a. by tier Percentage redemption of points by tier

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