

THE INSIDER'S GUIDE TO CUSTOMER LOYALTY



IN THIS INSIDER'S GUIDE YOU'LL LEARN:

- Why a loyalty program is your most valuable marketing investment
- The design criteria for effective loyalty programs
- How to measure loyalty program success
- How to select the right loyalty partner
- Which financial considerations are critical to program success

MEET YOUR EXPERTS

Any marketer who sets out to earn customer loyalty quickly learns that it can be an elusive goal. Loyalty is tricky. It can be hard to define, difficult to earn and far too easy to lose.

We created this guide to help you master the basics of loyalty and avoid the pitfalls on your path to creating a successful program.

You'll also learn some of the secrets we've discovered over 30 years of building and managing some of the largest and most complex loyalty programs in the world.



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ENGAGEMENT AND LOYALTY

DEFINITIONS

LOY-AL-TY

The tendency to prefer one brand or company over all its competitors.

EN-GAGE-MENT

The cumulative impact of meaningful interactions over time. Loyalty is about relationships, not response rates, so engagement is measured over a defined lifecycle and across many touchpoints.

LOY-AL-TY PRO-GRAM

A focused marketing initiative to identify, retain and nurture your most valuable customers. This typically includes providing unique recognition, rewards and targeted communications designed specifically for customers with the highest potential for growth.

FAST FACTS

REDUCING CUSTOMER
CHURN BY JUST

5%

CAN INCREASE
PROFITABILITY BY

25%

ACQUIRING A NEW
CUSTOMER COSTS

5X to 10X more
THAN KEEPING THE
ONES YOU HAVE

INSIDER TIP



“Once you have mastered these basic definitions, we want to get you thinking about the *loyalty experience*. This allows your brand to optimize relationships with your best high-potential customers and even your pre-loyal customers.”

– Cheryle Frenzel

CUSTOMER INSIGHTS

from The 2019 Maritz Motivation | Wise Marketer Loyalty Landscape

87%

of consumers consider loyalty programs to be important in their purchase decision-making process.

69%

of consumers say they are more likely to read/respond to communications when they are about the loyalty program.

70%

of consumers say they are brand loyal but still looking for the best deal.

With the right strategy and execution, a loyalty program can drive sales, improve customer engagement and create valuable differentiation in the marketplace. An effective program can be your brand's most valuable marketing investment.

DO YOU REALLY NEED A LOYALTY PROGRAM?

The answer to this question depends on the challenges you're facing as well as your available resources. While a loyalty initiative can address a wide range of business challenges, it is not a magic bullet.

A LOYALTY PROGRAM IS THE RIGHT STRATEGY IF YOU WANT TO:

- Identify and track active customers
- Increase the lifetime value of your customer base
- Boost purchase recency/frequency rate for your existing customers
- Improve customer retention and reduce churn
- Support customer satisfaction
- Incent customer advocacy/referrals

A LOYALTY PROGRAM **WILL NOT** EFFECTIVELY ADDRESS:

- Product quality issues
- Customer service issues
- Non-competitive pricing issues
- Extreme changes in the marketplace
- Product delivery or availability issues
- Employee morale issues



DO YOU HAVE THE RIGHT COMPONENTS IN PLACE TO SUPPORT A LOYALTY INITIATIVE?

- ✓ Your products/services have repeat purchasability
- ✓ You have readily accessible customer behavioral data
- ✓ You have metrics to identify active vs. inactive customers
- ✓ You have the ability to market directly to the consumers of your products/services
- ✓ You have executive support for the importance of a retention strategy

INSIDER TIP

“As you work within your company to build support for a loyalty program, it’s critical to educate your peers and executives from the start that loyalty takes time. Most programs do well to break even in year two and begin to show profitability in year three. Be sure to remind your stakeholders that loyalty is about building relationships, not response rates.”

– *Evan Snively*

WHO SHOULD BE THE TARGET OF YOUR PROGRAM?

Loyalty programs are narrow by design. Your program will be most successful if it is focused on a subset of customers that represent high current value or high potential value. For most companies, a successful program targets 40% or less of their customers.

Establishing a **value-based segmentation** scheme will be key to this approach. Value metrics can vary, but most companies start with some combination of spend, frequency, recency and number of products/services used.

INSIDER TIP

“Good loyalty programs drive revenue, but great ones show you which customers are worth reinvesting in.

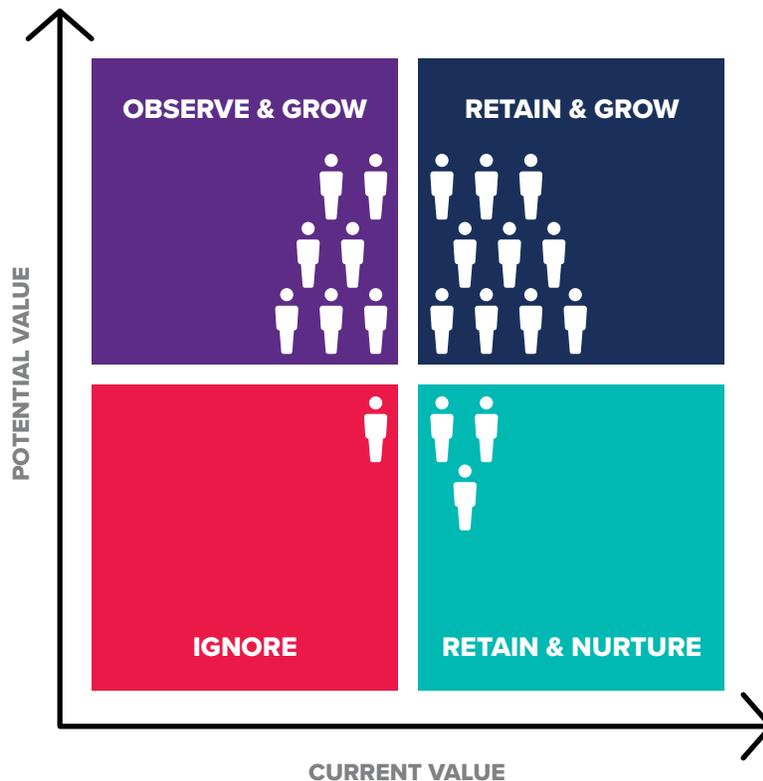
As you develop your loyalty program and the marketing strategy to go with it, you’ll be able to determine the value each customer represents to your business. Focus your budget on high-value customers, and you’ll get the best return on your investment.”

– JR Slubowski



VALUES-BASED SEGMENTATION MODEL

An evaluation of your customer base and the potential it holds



The above chart reflects customer behavior patterns and evaluates them based on their value to your business. For each segment, you should establish specific marketing strategies driven by data science.

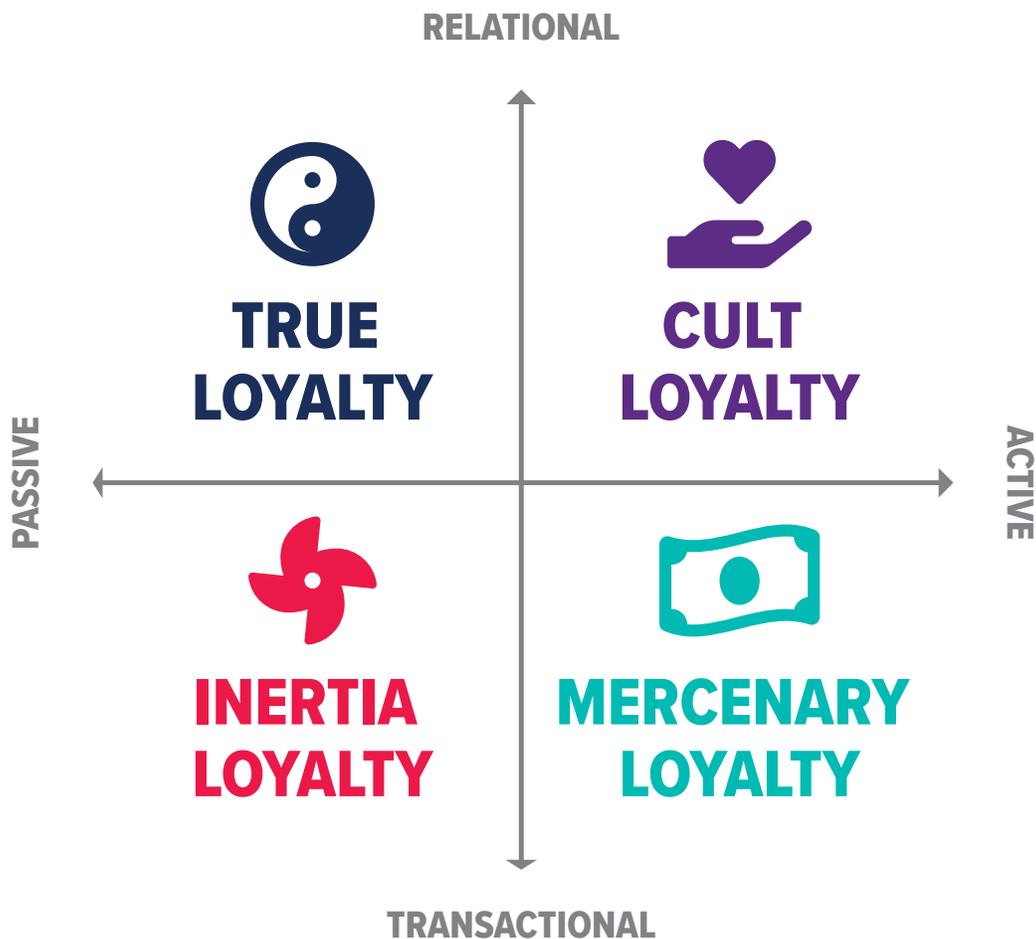
For instance, some customers will purchase your product once as a gift, but they are not likely to return or make additional purchases for themselves. These customers, while appreciated, are not going to build your business. As a result, they are of low overall value and should not be the target of your marketing communications. For all intents and purposes, they can be ignored.

At the other side of the chart, you'll find a customer who is of high current value and high potential value. Not only do they purchase your product for themselves, they're going to keep purchasing it, they'll purchase it as a gift, and they'll recommend it to everyone they meet. These customers hold the highest value to your business and should be the primary target of your retention and engagement strategies.

WHAT KIND OF LOYALTY DO YOU WANT TO BUILD?

The Multi-Loyalty Framework outlines four types of customer loyalty based on the behaviors and engagement of both program members and program brands.

This framework shows the relationship between the degree to which a program is transaction-based or relationship-driven, and the level of passive or active engagement of program members.





CULT LOYALTY

Members personally identify with the purpose and values of the brand and actively seek to connect with fellow brand loyalists.



TRUE LOYALTY

Focus is on the entire loyalty experience being engaging, not just the redemption. Earn behaviors share equal focus with burn behaviors through an engagement strategy that includes a refined member lifecycle, segmentation, a data-driven communications cadence, meaningful personalization and surprise-and-delight.



MERCENARY LOYALTY

Primarily focuses on customers being rewarded monetarily for purchase behaviors. Retention is usually driven via a hidden rebate offered to the member in terms of points redeemable for rewards and status.



INERTIA LOYALTY

Focuses on barriers to exit and is the answer to the question, “How do I best trap my customer into an ongoing interaction with my brand?” Brand stickiness is often developed through subscriptions and contracts, particularly those that auto-renew on a periodic basis.

Winning brands integrate the best elements of Cult, True and Mercenary Loyalty into a Multi-Loyalty strategy. They will combine diverse elements of three specific types of loyalty into an experience that activates engagement. This strategy uses a shared identity to connect members with the brand and with each other. This is the optimal approach for maximizing the benefits of the Multi-Loyalty Framework.



PROGRAM DESIGN FUNDAMENTALS

Loyalty programs are complex. They can involve a sophisticated and intricate mix of multiple strategies, tactics and audiences, but you don't have to start there. The best strategy when launching a new program is to keep it simple. You should aim for designing a program that is easy to understand and to execute at launch – with a specific plan to add to program sophistication over the first 24 months post-launch – and should include these four basic components: currency, rewards, communications and game mechanics.

CURRENCY



Program currency is what members earn for their purchase and engagement behaviors (points, miles, stars, credits, etc). It's also what they'll use to redeem for rewards. Your program design should include an earn-burn structure which establishes how members earn, how much they can earn and at what earning level they will be eligible to redeem.

REWARDS



Rewards are the most powerful motivator of member behavior and should be aligned with your brand as well as your customers' interests. A robust rewards mix generally offers a combination of merchandise, gift cards, e-gifts and travel at a range of values.

COMMUNICATIONS



Member communications are critical to maintaining engagement. The best programs use a mix of standard and segmented messaging through a combination of channels (email, direct mail, text messaging, mobile and web).

GAME MECHANICS



Game mechanics offer an additional engagement layer to your program beyond simply recognizing spend behaviors. Mechanics commonly found in loyalty programs include tiers/levels, challenges/missions, badges, progress bars, surprise-and-delight, auctions and virtual rewards.

THE THREE MOST COMMON LOYALTY PROGRAM STRUCTURES

An earn-and-burn structure is key to most successful programs. It provides the mercenary hook critical to attracting new members and maintaining the attention of legacy members. There are a wide variety of approaches to building earn-and-burn into your program, but the three most common structures include:



POINTS AND REWARDS

Seen in the majority of loyalty programs, this structure enables members to earn a currency for spend behaviors. That currency can then be redeemed at some later date for a pre-established catalog of reward items. This model optimizes the dynamics of anticipation and delayed gratification to drive engagement.



CASH BACK

This model focuses on rewarding members with a cash refund that usually represents a standard percentage of their brand spend. It's common within this program format to enable auto-redemption where rewards are issued with no redemption action required by the member.



OFFER-BASED

Most common in the retail space, this program structure primarily focuses on providing members with an array of special offers and discounts on products and services. These offers are generally richer than those provided to non-members and/or may give members early access to special deals.



CORE LOYALTY PROGRAM DESIGN CRITERIA

Ensuring that your loyalty program is structured to meet the specific needs and behaviors of your customers is the most critical design criteria. However, experience with many programs across multiple market verticals has shown us that some design criteria have applications across almost all successful loyalty programs, including:

1 HIGH PERCEIVED VALUE OF PROGRAM CURRENCY

No matter what your points are worth in terms of actual dollars, members must perceive those points as offering a true value reflective of their relationship with your brand and worthy of their active engagement in the program.

2 HIGH PERCEIVED VALUE OF REWARD OPTIONS

Points alone do not create a compelling value proposition. The items that points can be redeemed for are just as critical. Your reward mix should include a variety of options at different point values. However, make sure that your reward selection is curated to excite members without overwhelming them.

3 A COMPELLING EARN VELOCITY

According to our research, 40% of consumers cited that “benefits took too long to earn” as the primary reason for quitting a loyalty program. Well-designed loyalty programs ensure that the effort required by members to hit redemption thresholds is similar to competitors’ programs and linked to reasonable expectations for member spending.

4 A PERSONALIZED, SEGMENTED USER EXPERIENCE

A common mistake of newer loyalty programs is the temptation to cut corners by creating a single experience for all members. Remember, program members are offering you access to their behavioral data in return for a different kind of customer experience. The more segmented and targeted you can make that experience – taking into account their demographics, interests and needs – the more likely you are to engage them in the long run.

SUCCESS MEASUREMENT

A customer loyalty program is like any other marketing initiative – it's measured by evaluating quantifiable financial metrics against the investment required to design, launch and operate the program. The most common financial metrics include:



ROI

Return on Investment compares how much a program costs to the profits gained through changes in members' behavior.



CLV

Customer Lifetime Value is a prediction of the net profit attributed to the entire future relationship with a customer. This metric is especially relevant to loyalty initiatives, since the goal is to develop long-term relationships with your best customers.



RFM

Recency, Frequency, Monetary value is a scoring technique often used to calculate or estimate member value and retention.



PREDICT YOUR PROGRAM'S PROFIT

There's more to measurement than just your financial metrics. Loyalty programs encourage a number of useful new behaviors which, when tracked and analyzed, can act as powerful proxies for customer loyalty. They can become predictors of program profitability.

These new metrics include:

- Enrollment rates
- Point accrual rates
- Redemption rates
- Member churn
- Member campaign engagement
- Member referral

Your strategic goals and the maturity of your loyalty program will drive success metrics. The key is to establish a measurement plan and score your program on a regular basis.

INSIDER TIP

“As your program matures, one of the strongest temptations you will face is the inclination to shift your measurement focus from program profitability to program cost. In many companies, this turns into a fixation on reducing cost per point (CPP) versus driving member engagement. Resist this temptation.

Staying focused on your program as a profit driver will put you in a stronger position to grow the program and show its true value to the company.”

– Cheryle Frenzel

PROGRAM FINANCIALS

When launching a first-time loyalty program, you're bound to encounter a lot of new financial terms. Loyalty marketing has its own language – with terms like “point liability,” “cost per point” and “breakage” – which will be important for you to understand.

The financial aspects surrounding your new loyalty program are primarily associated with point liability. This refers to a holding account for points that have been earned but not redeemed yet. Points in this account are converted into a dollar amount and reflected on your balance sheet.

Think of point liability as your company's IOU to loyalty program members. The payout happens when those members redeem their points.



FACTORING POINTS INTO YOUR FINANCIALS

1

REWARDS EXPENSE IS INCURRED WHEN POINTS ARE ISSUED.

While the actual cash flows out when the points are redeemed and you pay for a reward, your marketing budget is impacted at the time points are issued. This is different from short-term marketing strategies where expenses are incurred at the same time as cash flow.

2

IN THE HEALTHIEST OF PROGRAMS, NEARLY ONE THIRD OF ALL POINTS WILL GO UNREDEEMED.

This is known as breakage, or points that are never expected to be redeemed, either due to expiration or member forfeitures. Expected breakage is normally estimated up front and is technically never put into your point liability. This also means it should never hit your expense line.

3

TYPICALLY, YOUR PROGRAM'S ROI WILL BREAK EVEN IN THE SECOND YEAR.

A point expiration policy will help you estimate breakage. Most program members prefer that their points never expire, but there are financial and engagement advantages to having an official point expiration policy. Knowing that there is a time when points no longer exist helps you determine a better estimate of breakage. It lowers program expense and gives you more budget dollars for other marketing initiatives. And it gives your members a reason to stay active and use their points for redemption, one of the most powerful drivers of ongoing engagement in a loyalty program.

Don't let these financial concepts take your attention away from your main goal: creating a compelling loyalty program for your members. Your program not only needs financial stability but also the investment required to build an experience that's worthy of your customers' time and money.

HOW TO SELECT THE RIGHT LOYALTY PARTNER

Once you've determined it's time to develop a loyalty program, the next step is selecting the right loyalty partner.

Your new loyalty partner will act as an extension of your brand. Similar to any consumer loyalty program, you should expect and plan for a lasting relationship. Most loyalty partner contracts are initially written for 3-5 year terms and often run longer.

Even the most experienced marketers can find the process of researching and selecting a loyalty partner daunting. Contributing to this challenge is the tendency for many start-ups and novice loyalty providers to greatly overstate the simplicity of launching a new program and understate the expertise needed to do it well.

So, how can you cut through the clutter and find the right loyalty partner for your brand?



CHOOSE A PARTNER TO SUIT YOUR PROGRAM

1

YOU MAY NOT KNOW WHAT YOU DON'T KNOW.

It's hard for many marketers to own up to this one, but it's true. Loyalty marketing is an ever-evolving industry that is largely unknown to most marketing professionals. A good loyalty partner will confidently help you:

- Determine what type of loyalty you want from your customers
- Design an effective loyalty program (i.e. earn/burn rules, tiers, etc.)
- Establish loyalty-specific customer segmentation models
- Predict the financial commitment and likely return on a loyalty program using well-established financial models
- Keep members engaged with your brand from onboarding forward so that your program will deliver optimal results

2

WHAT TYPE OF LOYALTY PARTNER DO YOU NEED?

Most loyalty partners fall within one of the following two groups:

- **Limited Service Provider (LSP)** – generally provides one primary service related to launching or managing a loyalty initiative. These are often loyalty platform providers, loyalty design/analytics consultants, call center providers or rewards fulfillment providers.
- **Full Service Provider (FSP)** – provides all or most of the standard components of the loyalty service value chain, including: program design, program analytics/research, creative services, loyalty technology, program management and rewards fulfillment.

3

WHAT'S THE DIFFERENCE?

- LSPs generally have services and expertise in one specific area related to a loyalty program. They are typically enlisted for more mature programs with a network of suppliers in place, as they integrate discrete offerings to fill gaps.
- The FSPs are more flexible. They can provide a comprehensive solution from start to finish, or fill in specific loyalty services as needed. Even though you may not require all of these services immediately, FSPs are able to step in and assist clients at all levels of program maturity and across all service needs. FSPs are generally more attractive to new program initiatives, or for struggling programs looking for a reboot.

“ Investing in loyalty makes sense. Engaged and loyal customers will deliver more incremental profit. They’ll be significantly more resistant to competitive offers. And they’ll be a source of referral to acquire new customers who look just like them.

If you do loyalty well.

The trick is to recognize that loyalty is a different animal from any other type of marketing. It requires a focus on just the right customers, with just the right strategy and intention, and a clear understanding of tested and proven loyalty financial models.

Master those elements and your loyalty program will become a critical performer in achieving your goals for brand preference, growth and market share.”

– *Barry Kirk*

ABOUT MARITZ MOTIVATION

At Maritz Motivation, we help you build stronger relationships with your customers by delivering full-service loyalty solutions, including:

- Program design and strategy informed by loyalty industry expertise, best practices and deep insight into the science of human motivation
- A foundation of analytics and research that results in actionable insights to motivate the most profitable customer behaviors
- A world-class reward experience that is unique for each customer
- Flexible, state-of-the-art technology and creative services that bring your loyalty strategy to life

OUR FULL-SERVICE LOYALTY SOLUTION CONSISTS OF THE FOLLOWING COMPONENTS:



DATA & ANALYTICS



CONSULTING



PROGRAM DESIGN



TECHNOLOGY



EXECUTION



CREATIVE STRATEGY

Visit maritzmotivation.com to see how our loyalty programs can help your business.