# LOYALTY PROGRAMS: DO COMPANIES REALLY MAKE CONSUMERS LOYAL?

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***Abstract***

*In the markets of different products and services, the interests of both, companies and consumers collide. Companies that offer products and services expect a return on investment and higher profits. They can achieve these goals only if they have regular consumers, preferably loyal who will buy products and services more often or in larger quantities. The companies are interested in achieving long-term and sustainable relationships with the consumers and they want to minimize the churn and their switching to competitors. Consumers, on the other hand, have more sophisticated demands and expect more value for less money. They are interested not only in the quality of the product, but also in packaging, discounts, cashback, rewards, additional customer services, free shipping, maintenance, special treatments, reputation, etc. To meet these consumer expectations, companies offer many promotional activities, including loyalty programs. Loyalty programs, as part of the CRM (customer relationship management), are marketing programs that reward consumers for their repeated purchases over a longer period of time. Unlike other promotional tools, loyalty programs need to build a long-term relationship between companies and their consumers. But despite the offer of such programs, many studies show that consumers are not loyal and do not fully enjoy the benefits of the programs. Do companies give "something for nothing" and spend their money in vain? What are the reasons for the downfall of loyalty programs? This paper aims to investigate the reasons for consumer disloyalty despite the offered companies' loyalty programs. The paper will also provide guidance for companies to design loyalty programs that will attract more consumers.*

***Keywords:*** *loyalty program, consumer loyalty, customer retention, promotion, customer relationship marketing (CRM), rewards*

***JEL Codes:*** *M31, M37, M39*

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## 1. Introduction

Having in mind the current business environment in which many companies operate, characterized by strong competition, high customers' expectations, their new sophisticated needs and requirements, intensive use of advanced technology (social platforms, mobiles), relatively homogeneous offer of goods and services on the market, companies are under pressure to find new ways to attract new or to retain the existing consumers. Every company has two main goals: to increase popularity of the brand and attract new customers while improving value to existing ones and strengthens their loyalty. (Zlateva, 2016, p. 95) However, acquiring new customers is difficult, but retaining them is even harder. Companies are struggling for consumers (existing and potential) because they depend on them, their survival, turnover and profitability.

Nowadays, companies offer a wide range of different promotional activities for their consumers. Some promotional activities, such as sales promotions, are temporary (short term) reward programs and they are valid for a limited or pre-determined period. This kind of promotion is more convenient for new, potential consumers. However, in order to build long-term customer relationships, and stimulate repeat and more frequent purchases, companies use loyalty programs. Loyalty programs are more related to the existing consumers. They are part of the CRM (customer relationship management) that helps companies to build and grow customer relationships across the entire customer lifecycle. Loyalty programs are not new. The first loyalty program was launched by American Airlines in 1981 that invited customers to collect air miles that later could be redeemed for free flights (Oracle, 2005). Historically, loyalty programs are implemented in different ways, through different instruments, with different technology, but their purpose remains the same. Both in the past and now their goal is to identify, reward and retain consumers. Their purpose is to stimulate repeated and frequent patronage, as well as to keep consumers from defecting to competitor's products.

Today, companies are increasingly paying attention to marketing relationships aimed at establishing contact with the customer, promoting and maintaining his loyalty. (Zlateva, 2020, p. 173) On the other hand consumers love the promotional activities of companies. They perceive them as fun and entertainment that give them something more than they purchase or deserve. According to some studies in most developed markets, more than half of the adult population is enrolled in at least one loyalty program. According to Nielsen, 84% of consumers worldwide will likely choose retailers that offer loyalty programs (Nielsen, 2013). Consumers are guided by the saying that "if it's free, it's for me!" That is why the same Nielsen survey shows that customers are mostly interested in discounts and free products.

But Nielsen's report also notes a worrying fact. Namely, the survey that was conducted in 58 countries, for 16 different product categories and covered 29,000 Internet users, showed that more respondents professed no loyalty than complete

devotion to brands, service providers and retailers. According to another study, each consumer, in average, possesses from 10-15 loyalty cards in their wallet from companies that offer the same or similar products. This shows that consumers are not completely loyal to companies.
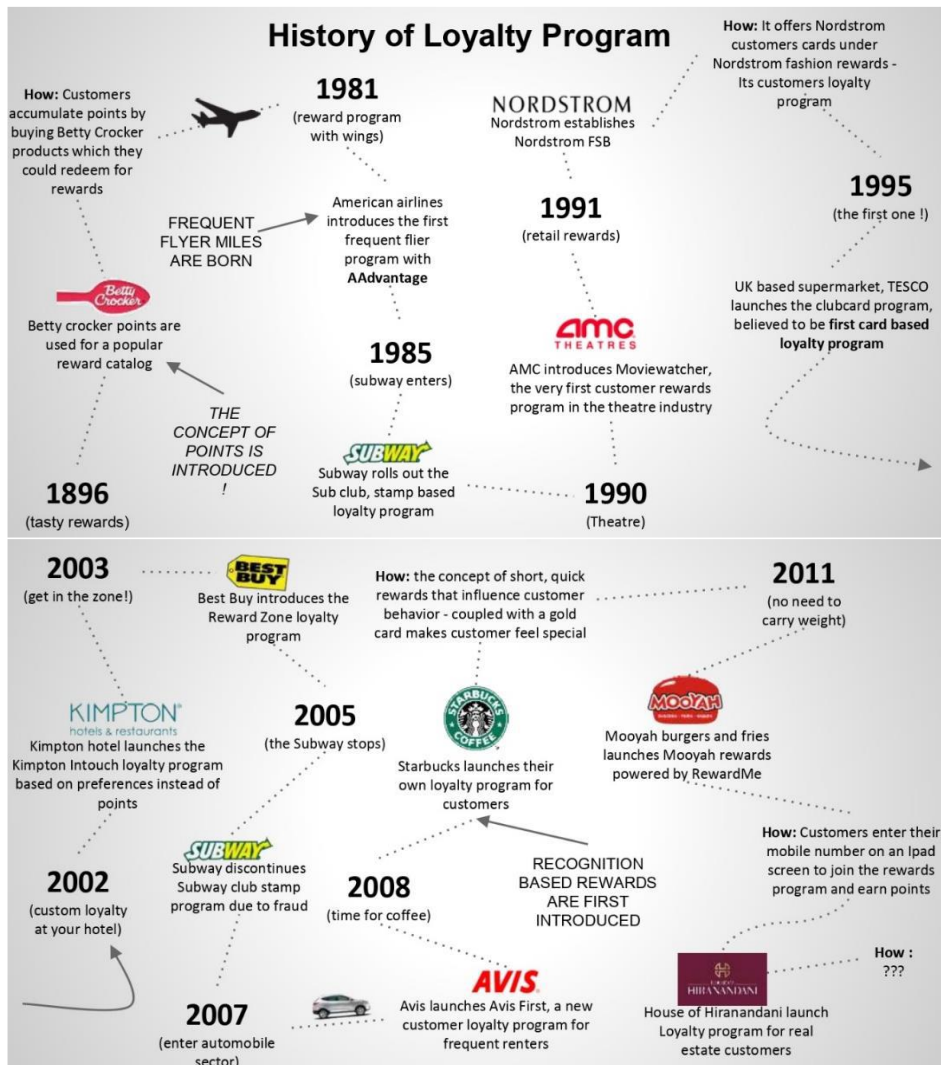
## 2. Literature Review

Before discussing loyalty programs in more detail, it is important to determine what is meant by loyalty. Loyalty is defined in different ways and most often it is correlated with satisfaction. However, in order to have loyalty, the satisfaction of the consumer is a precondition, but not every satisfaction leads to loyalty. These two terms are different. "**Loyalty** is a positive belief in the value that a company provides, leading to increased purchases over time" (Oracle, 2005). Customer loyalty is a measure of a customer's likeliness to do repeat business with a company or brand. Customer loyalty is an ongoing positive relationship between a customer and a business. It's what drives repeat purchases and prompts existing customers to choose your company over a competitor offering similar benefits (Qualtrics, 2021). According to Kotler, Bowen and Makens, customer loyalty is "how likely customers are to return and their willingness to perform partner-shipping activities for the organization" (1999, p. 351). Kotler urges that two factors are critical for loyalty to grow. The first factor is customer's emotional attachment toward one certain product or service. The second factor is customer's repeat purchase. Loyalty programs are a ubiquitous instrument of customer relationship management. **Customer satisfaction** is an "opinion measure" about company performance and how customers feel their needs were met in past interactions or by past purchases, whereas customer loyalty is a results measure that includes expectations of future behavior (Oracle, 2005).

So, how loyalty program is defined? "**Loyalty programs**, sponsored by retailers and other businesses, offer rewards, discounts, and other special incentives as a way to attract and retain customers" (Chen, 2021). They are designed to encourage repeat business, offering people a reward for store/brand loyalty. Typically, the more often a customer patronizes the merchant, and the more they spend, the greater their rewards. Loyalty programs are the programs offered to the customers in order to build an emotional attachment to the brand. Customer loyalty programs are incentives companies use to get people to return to their store or website.

There are a lot of **different names given for these programs**. For instance, in the hotel industry, the loyalty program is often named as Guest Frequent Program; while in the airline industry, it is called Frequent Flyer Program. In other industries, it is also named as Bonus Program, Customer Club, Customer Card, Fly Buys and so forth (Butscher, 2002). However, those different names basically do not differentiate one program from the others. The key differentiators are the types and the benefits offered by the programs. **The historical development** of loyalty programs is best illustrated by Nandal and all:

*Picture 1. Historical development of Loyalty programs*



**History of Loyalty Program**

**1981**
(reward program with wings)

**How:** Customers accumulate points by buying Betty Crocker products which they could redeem for rewards

FREQUENT FLYER MILES ARE BORN

American airlines introduces the first frequent flier program with **AAdvantage**

NORDSTROM
Nordstrom establishes Nordstrom FSB

**How:** It offers Nordstrom customers cards under Nordstrom fashion rewards - Its customers loyalty program

**1991**
(retail rewards)

**1995**
(the first one !)

Betty crocker points are used for a popular reward catalog

UK based supermarket, TESCO launches the clubcard program, believed to be **first card based loyalty program**

**1985**
(subway enters)

**amc THEATRES**

AMC introduces Moviewatcher, the very first customer rewards program in the theatre industry

*THE CONCEPT OF POINTS IS INTRODUCED !*

**1896**
(tasty rewards)

**SUBWAY**
Subway rolls out the Sub club, stamp based loyalty program

**1990**
(Theatre)

**2003**
(get in the zone!)

**BEST BUY**
Best Buy introduces the Reward Zone loyalty program

**How:** the concept of short, quick rewards that influence customer behavior - coupled with a gold card makes customer feel special

**2011**
(no need to carry weight)

**KIMPTON** hotels & restaurants
Kimpton hotel launches the Kimpton Intouch loyalty program based on preferences instead of points

**2005**
(the Subway stops)

**STARBUCKS COFFEE**
Starbucks launches their own loyalty program for customers

**MOOYAH**
Mooyah burgers and fries launches Mooyah rewards powered by RewardMe

**2002**
(custom loyalty at your hotel)

**SUBWAY**
Subway discontinues Subway club stamp program due to fraud

**2008**
(time for coffee)

RECOGNITION BASED REWARDS ARE FIRST INTRODUCED

**How:** Customers enter their mobile number on an Ipad screen to join the rewards program and earn points

**How :** ???

**AVIS**
Avis launches Avis First, a new customer loyalty program for frequent renters

**HIRANANDANI**
House of Hiranandani launch Loyalty program for real estate customers

**2007**
(enter automobile sector)

**How loyalty programs work?** To join a loyalty program, customers typically register their personal information with the company and are given a unique identifier, such as a numerical ID or membership card. They use that identifier when making a purchase. In terms of membership, there are **two types of customer loyalty programs**, namely **limited and open**. A limited loyalty program cannot be joined by just everybody. There is a formal procedure to become a member of the program such as paying joining fees and sometimes there are certain criteria in order to be eligible

as a member such as certain purchase volume and minimum income. On the other hand, an open loyalty program can be joined by every individual and usually does not have formal criteria and application procedures. Additionally, in terms of the benefits offered, there are two types of benefits namely **hard and soft benefits**. Hard benefits are tangible benefits which are immediately recognizable by all members and lead to savings in some form or another. In most cases, hard benefits are financial benefits, for example discounts, rebates or coupons. These benefits can be easily imitated by competitors. Soft benefits are the special offers, the value-added services, the special treatment, the recognition and reward that the customer is looking for.  It is mostly intangible, company and product related and less copied by competitors (Butscher, 2002).

A properly executed loyalty program can deliver significant, **long-lasting benefits** to the host company, such as:

- Product and service differentiation and get ahead of competitors;
- Customer retention;
- Profitability;
- Greater customer knowledge;
- Find new customers;
- Improve brand/ company reputation;
- Improve customer engagement & experience;
- Increased customer lifetime value.

There are **several types of loyalty program** such as (E-Satisfaction, 2021):

- **Point program**: Customers earn points on each purchase. This is the most common and the simplest program, based on a principle: "Spend more to get more". Customers who purchase more will earn more points that later can be translated into some types of reward (discount, special treatment, additional services, tickets, free gifts, etc.).

- **Tiered program**: This one is based on how much loyal the customer is. Companies divide consumers into different tiers depending on their purchase volume. On every purchase customer gets certain points. As the points increases, the level of loyalty also increases.

- **Paid program**-**VIP member card**: Customer pays annual or monthly fee to join the VIP member club with access to special services, discounts, unique perks, exclusive rewards. This loyalty program is based on subscription and it's not for free.

- **Partnered program**: The host company together with its partners offer variety of rewards to customers. On one side this program is good for companies which could deepen their cooperation and partnership with other businesses and on the other it is very effective for consumers who have a wider choice of rewards.

- **Game program**: Sometimes loyalty programs are boring. Companies need to make them more involving and interesting. They can do it by converting loyalty programs into game application to encourage repeat purchases. As soon as the

consumer completes a certain level of the game, he/she receives a certain reward. Higher level of games needs to ensure more exclusive rewards.

- **Cashback loyalty program**: Customers earn money after crossing a certain spend limit. They can then spend this earned cash on their future purchases.

- **Hybrid program**: In this program, two or more different systems are merged. For example, a merge of tier and game program means that whenever customers completed a certain level of game, they reach a new level of loyalty and can get more rewards. The most commonly used combination is point-based system with tier program because in this calculation of points is easy for the customers and motivates them to so for next loyalty level by making more purchases.

### 3. Methodology

The methodology applied in this paper is descriptive in nature. For data collection, secondary resources are used. Various studies, reports, papers, expert opinions, blogs have been referred in the present research. The sources from where the data has been collected for the present study is listed below:

- Research paper on related topic;
- Web resources related to the topic;
- All the other published material has been referred during the research.

### 4. Analysis and discussion

Although loyalty programs can be very expensive to develop and maintain, many studies show that they do not achieve the desired goals. They either do not cause significant repeated or frequent purchases or do not improve the company's profitability. Around 77% of loyalty programs fail within their first two years (Davis, 2021). The key reasons why loyalty programs fail are:

- **Wrong reward selection**: Consumers are not fully aware of what loyalty programs offer. A study by Edgell Knowledge Network investigating the loyalty programmes of 60 retailers found the vast majority of customers (81%) weren't aware what their rewards entitlements consist of or how they're redeemed (Wheeler, 2018). Also, sometimes the terms and conditions of loyalty programs are not clear, or are very complicated and do not align with the business offerings. Customers do not see the benefits and the real added value of the programs. Complicating the process only serves to turn customers off, as they lose interest as soon as the program seems like too much effort.

- **Unappealing or unattainable rewards**: Loyalty programs can fail because they do not offer tangible benefits. Sometimes they require an unreasonable amount of commitment in order to attain them. Consumer enthusiasm and excitement diminishes if they are asked to perform many transactions or spend more money than planned to redeem the rewards. One of the top reasons that loyalty programs fail is

that customers perceive the rewards as too difficult to earn, causing them to favor a competitor with an easier rewards system.

- **Poor program promotion and marketing campaign**: The company's lack of clear communication with consumers is considered to be one of the main reasons for the failure of loyalty programs. Often times, companies do not put sufficient efforts to manage communication with the customer. As a result, the program may not get the response as expected. So, how can consumers "reap" the benefits of programs if they do not know about them? It is not enough for consumers to get involved in loyalty programs. They need to be constantly reminded of their status in the program, gained reward points and awards that follow. That communication can be realized via social media, emails, direct mail, telephones, etc. Otherwise, the purpose of the program may not be fulfilled.

- **Lack of fun and engaging elements to provide "thrills"**: In order to boost engagement and to retain consumers, companies need to offer something interesting, innovative perks, gamified functions in the programs, unexpected gifts. Consumers love surprises, freebies, discounts, more value for less money.

- **The omnichannel experience is non-existent**: Omnichannel engagement means customers can interact with company via its in-store staff, website, social media channels, over the phone and numerous other mediums with no gaps or faults in the customer experience. A digital loyalty program needs to be integrated with all the other channels.

- **Personalization and tiering the consumers**: In this day and age, a 'one-size fits all' approach simply doesn't work. Consumers who spend more on a brand should receive higher rewards. Also, a more detailed personalization strategy could be more impactful.

**So, what do customers want from a loyalty program?** Customer loyalty in 2021 is very different to what it was 10 years ago. According to Davis, the following list of consumers' list is very important for companies when designing a loyalty program:

- **Simplicity:** Loyalty program needs to be simple so that customers can understand it easily.

- **Value-add marketing:** Companies need to provide their consumers with high quality content that will enhance their overall experience.

- **Setting right rewards:** Consumers need to be interested in gaining the rewards. Studies show that they prefer hard rewards (financial rewards, such as bonuses, free gifts, cashback), but they also like soft rewards, that are intangible, such as additional services, tickets, special treatments, exclusive gifts, etc.

- **Usage of tier programs:** Tiered program is one of the best ways to reward the best customers with greater deals.

- **Better communication with consumers:** Companies need to remind their customers to use the earned points. Hence, they need to send customized email/SMS messages based on buying habits.
- **Surprise and delight:** Surprising and delighting the consumers with spontaneous rewards and unexpected gifts can enhance their experience with the company or its brand. It could be a random "double points day", or an unannounced gift on the anniversary of their loyalty program registration. An upfront reward just for signing up to the loyalty program is also a welcome surprise. It provides the customer with a sense of instant gratification, and gets them motivated to earn points and redeem more rewards.
- **Personalization:** By storing and analyzing customer data, company has valuable insights to customer spending habits, and can send tailored communications based on each individual customer's previous transactions and various other interactions with the brand. Perhaps one customer would appreciate 50% off all ties and collared shirts for one week only, while another customer would prefer free shipping on their next purchase of jewelry and accessories.
- **Gamification:** Everyone likes games and playing. So, instead of boring loyal programs, companies can offer different types of games and their different levels could bring different rewards based on purchases.
- **Omnichannel engagement:** Omnichannel engagement allows the customer to interact with the brand seamlessly across numerous channels, consistently picking up where they left off last time.

The current state of customer loyalty has been impacted by the global COVID-19 pandemic. It could be expected an increased focus on developing technology that will further enhance personalization through segmentation, as well as a continuing shift towards customer lifetime value based on the consumer experience, rather than the value of the product.

### 5. Conclusion

Loyalty programs are profitable if they are conducted right. A company which provides loyalty program benefits enjoys a competitive advantage over their competitors. The aim of each loyalty program is to attract consumers to purchase more in quantity or in frequency. Also, it helps in building a long-term and profitable relation with customers as well as building a personal relation with them. However, loyalty programs should be implemented carefully so that the profitability does not get impacted. There should be a proper mechanism for feedback from customers by which one can identify the response towards its loyalty program.

The implementation of loyalty programs is not an easy task for companies. Repeated purchases do not guarantee the customers loyalty towards the company. Customers are very vulnerable and easily switch to other brands or companies as they have a lot of options to choose. Thus, managers should fully understand that

making customers loyal to the company means not only to encourage them to make repeat purchases, but also to build customers' emotional attachment to the company.

The best way companies to meet the expectations of consumers is to do a thorough marketing research of their needs and wants. Based on the results, companies need to offer a tailor-made, personalized, entertaining loyal programs. Having in mind the new technology, it is also recommendable to use innovative concepts in the online space.

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