



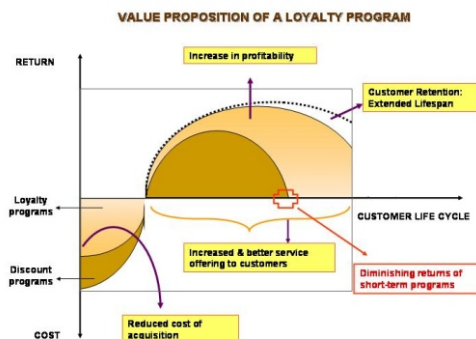
# 4 Strategic Dimensions for Building a Successful Loyalty Program

Studies reveal that a 5% incremental retention of customers through a successful loyalty program can lead to 75% increase in lifetime value. This is most applicable in a retail environment, where increased footfall is driven not only by increasing customer base, but by also influencing repeat purchase behavior. Investment in a good loyalty program can payback within 12-24 months leading to profitable growth of revenue in the long run.

However, unless the Loyalty program strategy has been thought through to the finest details, it has all the potential to become a white elephant, siphoning out huge profit margins, even if it does augment revenues. Lets look at what are the foundation blocks for building a successful Loyalty program, and what retailers should be aware of before launching one.

## 1. What financial benefits should the program entail, and by when?

Most loyalty programs that fail are those that have not got their



financial objectives right. Unfortunately, loyalty programs get defined with marketing and customer relationship perspectives only, discounting the profitability aspects of the program. Before one launches a loyalty program, the following questions need to be answered:

- What incremental revenue will the loyalty program bring in?
- What are the accrual and redemption terms of the program?

- What are the actual and contingent (unredeemed) costs involved?
- When will the loyalty program break-even?

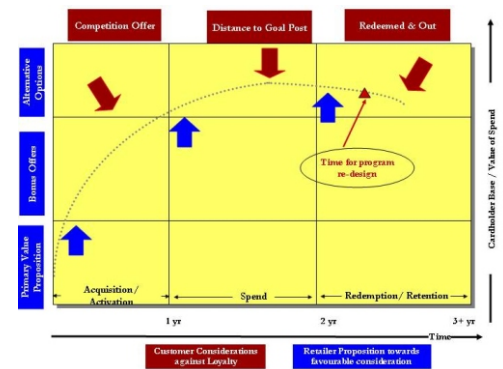
The answers to the above lie in the overall strategy of the organization and will significantly impact the design and structure of the program. A program with a fairly long-term break-even, for instance will have a different design than another, which has a very short-term view. As can be seen from the enclosed figure, short-term “discount- programs” can lead to diminishing returns. Measuring the performance of loyalty programs across each of the above, on a periodic basis will also provide insight into the strategic direction one should take with respect to Loyalty.

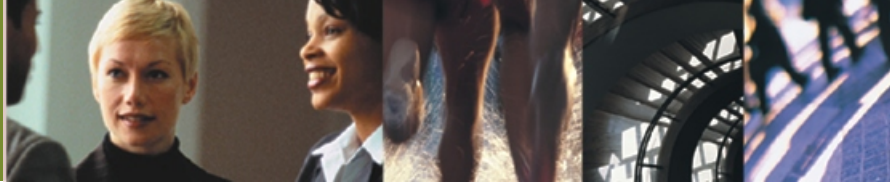
## 2. Who to attract, and why?

Loyalty is not just about attracting new customers, but more about retaining profitable customers. The critical element here is in identifying which segment of your customer base would you like to attract, and as a

logical extension of that, identify what would attract them. Features of the loyalty program should also align with the product and services being rendered.

For instance, in-store redemption may be a great feature for a super market chain, but not necessarily a shoe-mart where the next visit of the customer is not immediate. A possible approach in the latter case could be a tie-up with another partner. The program should also be aligned with external market factors, and the life cycle of the program should also be well defined. Building these scenarios right





are essential to make correct predictions in the business growth.

As one can see in the figure, the initial attraction that the customer has for the program has to be sustained through the life of the program. Examples here are bonus and alternative offers. There are 3 main distractions that any loyalty program faces:

- **Competitive offers:** A customer always compares your program with that of your competitor. Not only before joining, but all the time!
- **Distance to goal-post:** This is critical. Customers need to reap the benefits of any loyalty program with tangible value. If the program is about earning points over 2 years to get a teddy bear at the end of it, it is most likely to fail.
- **'Redeem and out' mindset:** 30% of loyalty customers tend to switch over, after their first redemption. A program has to constantly trigger customer preference.

The timeframes in the figure are illustrative, and change from one program to another. However, every program goes through a life-cycle of activation, spend and redemption. The "spend" phase is the most valuable period for reaping value of the program.

### 3. What processes are required to deliver the program?

Building customer expectations has to be fully complimented by building back-end processes. A dissatisfied customer can deter 10 potential new customers. Preparing for multiple scenarios and building well-defined operations behind the curtains are indispensable for successful delivery of the program. Understanding the steps involved in the accrual and redemption process, defining service level agreements with partners and importantly, identifying which of these should be automated will be mandatory for the program. Documentation and control aspects of the procedures to be adopted will also need to be defined.

### 4. Is the infrastructure ready?

While Information Systems constitute a critical component of the Back-end infrastructure, it is not the end-all of loyalty. Organizations

have realized (some of them the hard way) that for best results, one has to invest in a clear internal Loyalty Organization. In addition to a full-time product manager who shall coordinate the end-to-end of the program, there are clear roles across each function of the retailer: be it the marketing function which remains the customer touch-point, or the cashier with an operational role, or the finance department who will need to measure the performance of the program, there are incremental responsibilities that need to get performed across the organization.

There is a significant role that needs to get performed by the IT function as well. Loyalty programs typically entail having personalized cards (smart cards becoming more popular there) and have to be intricately twined through the information flow. The best model would of course be, where the customer card is recognized through the point of sale, and accrual/redemptions happen over the counter. This obviously has to relay back to the back-end systems for Financial and MIS purposes. Where there are external partners involved, IT function should lend itself further into data transmission, acceptance and reconciliation.

The benefits of having a successful loyalty program are fairly straightforward. Higher retention rates, better referral rates, and increase in spending all leading to incremental revenue. Also, over a period of time, costs of servicing tend to go down and customers also tend to become less price sensitive leading to incremental profits. Growing customer awareness of loyalty programs also helps: according to Retailindustry.com survey, 82% of the consumers believe retailers who operate loyalty program and seek information about their preferences are "more in touch" with their customers. Yet all these benefits can only be the fruits of a well-defined loyalty program that reward the 'right' customers, rightly!



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