Turning Rewards into Loyalty

When Marriott International announced it was buying the Starwood chain of hotels, many members of the Starwood loyalty program took to social media, anxious that Marriott might spoil their beloved perks. The eruption was just one reminder of the intensity with which many consumers cherish rewards programs.

Some old-school rewards programs in the airline, lodging and retailing industries appear to be more valuable than ever, with credit card companies paying record prices for the right to use them. Innovation has thrived in recent years as companies incorporate new mobile and other digital features, which can reduce price sensitivity and expand share of wallet.

Yet just as there are hundreds of failed or fizzled start-ups for every tech unicorn, most of the thousands of rewards programs do not generate enduring loyalty. Worse, some also-ran programs end up with all of the cost and little benefit, paying customers extra for behavior that would occur anyway. Even in these cases, management teams may resist shutting them down to avoid customer backlash.

Getting loyalty right isn't just about designing and executing a stellar program. Companies need to consider how the program fits into the broader market mix, how the messaging will align with messaging in other channels, and how it may affect operations or customer service. The Chili's chain, an early innovator in casual dining rewards, initially stumbled when it introduced My Chili's Rewards, because it stopped its email marketing program and focused the wait staff on signing up customers, which took attention away from selling appetizers and drinks. Both traffic and average ticket size decreased temporarily. As Chili's illustrates, the transition to a new system requires careful planning and testing.

Successful rewards programs reach a high return on investment by building loyalty through customers who stay longer, buy more, cost less to serve and recommend the company to others—all combining to increase the customer's lifetime value. That stands in marked contrast to reward schemes that merely bribe customers with extra points, freebies or discounts in ways that layer on extra costs without producing incremental value. The best rewards programs have adapted to the rise of digital channels and data analytics by emphasizing some combination of the following traits:

Informed. If a company knows how much each of its customers is worth and can identify customers with the highest current lifetime value and estimated full potential value, it has a solid base. It also benefits from using a system to measure the incremental value of the program or any campaign results. A/B testing or, better yet, multivariate testing known as experimental design, can determine which mix of rewards features and marketing messages will spur the greatest lift in spending. Such tests uncover the microeconomics of individual customer behavior. Casino and resort firm Caesars has a long history of testing to, say, learn a customer's gambling stop-loss level, so that the casino can send him or her an offer of show tickets right before reaching the limit; that way, the customer can end the night on a high and might be willing to return to the tables the next day, rather than cutting off gambling for the whole weekend.

Targeted. Campaigns to change customer behaviors work best when they are highly targeted, based on location, frequency and so on. Starbucks collects data on its customers' demographics, their payments and transactions, their beverage preferences, and more. Using geolocation technology, its mobile application targets users with personalized messages. Loyalty program members might get time-limited coupons, which helps Starbucks raise store use during non-peak periods. Nearly one-fourth of the chain's in-store purchases in the US now flow through the app.

Experiential. Sophisticated programs provide customers with a better experience, rather than just more points. Airlines and hotels have done this for decades by offering status-based upgrades, early boarding and the like, in part because the perceived value to the customer usually exceeds the company's delivery cost by a wide margin. Recently, mobile gaming firms have discovered the power of "free to play" games that provide status tiers based on cumulative in-app purchase amounts allowing more rapid progress, faster cool-downs before the action resets and better daily check-in rewards. Some brick-and-mortar retailers have begun deploying beacon technology to recognize "platinum" customers as soon as they walk into a store, and send them messages relevant to that store.

Easy. Rewards programs must be effortless to join or use. Too many companies have an application form that on first blush appears to be simple, but then devolves into a multistep process that turns off potential joiners. Note, though, that customers do need to opt in; if they're enrolled automatically, they may not be aware of the program and would not change behavior.

Responsive. It's not sufficient to identify the high-value customers and treat them better. Customers also expect their providers to know when they had a bad experience and to recover from those failures quickly and effectively. Companies thus need a feedback process to measure customers' perceptions of their interactions, fix problems that arise, and close the loop by following up with the customers in question. The rewards program itself can offer a channel for customers to provide immediate feedback, for service agents to react, and for the system to track changes in lifetime value based on that reaction.

Feedback loops and service recovery are built into new software tools from vendors such as Thanx, which counts restaurant chains among its clients. Thanx offers restaurants a prepackaged rewards system tied to a guest's credit card. The customer, after registering for the restaurant's program, simply uses the registered card to pay for a meal, earning points in the restaurant's program, with the value and redemption options determined locally. As soon as the transaction goes through the system, customers receive a notification from Thanx's app with a link to a request for feedback, using the Net Promoter Score®. Tomatina, an Italian restaurant chain in California, gets feedback from about 75 guests every week, and at last count between 20% and 25% took the time to add written comments in the Thanx system. Thanx research has shown that consumers are 7% more likely to return in the next two months after being asked for feedback—regardless of their response. A restaurant can also benefit from service recovery when, for instance, it learns about a service problem through Net Promoter® feedback and immediately responds with an apology and a coupon for a next visit.

Rewards programs have thrived in the airline and lodging industries, where firms work with low-variable-cost, highly perishable inventory. Companies with different types of offerings must get more creative to make the economics work, so that they're not simply bolting on programs that create a dollar-for-dollar rebate system. For a rewards program to yield an acceptable ROI, it must identify the best potential customers, treat them better, and based on their feedback, make relevant offers that raise their loyalty and lifetime value.

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