5 Principles Supporting Lifelong Loyalty

November 2022
Loyalty programmes are increasingly important to companies across sectors

Change in Mentions of Loyalty programmes in Annual Reports¹ 2017-21 by Sector

- Apparel: 138%
- Restaurants / Fast Food: 100%
- Hotel Operators: 58%
- Grocers: 26%
- Utility Companies: 25%
- Other Retailers (Non- Grocers/Apparel): 16%
- Airlines: -2%
- Banks: -8%

¹ Top 5 UK listed companies reviewed across sectors
When (re-)designing loyalty programmes, we believe there are 5 principles for Lifelong Loyalty

1. Start with the strategic objective
   Loyalty programmes must support and enhance business priorities, and have a clear customer focus

2. ‘Earning’ must be simple and demonstrate tangible value
   The best programmes offer a simple, ‘universal’ way to earn, while encouraging additional engagement to earn faster / more

3. You want members to use their benefits!
   Benefits should appeal broadly, celebrate the individual and offer choice to address specific target customer segments

4. The economics must be understood overall and by customer group
   Monetising free / low-cost assets, minimising cannibalisation, and passing costs to partners / suppliers are critical levers to managing cost, and increasing ROI

5. Maximising value requires integration across the business
   Loyalty cannot stand alone – it is essential to integrate across customer facing touchpoints and across business operations
Loyalty programmes need to be designed to support business objectives, with a clear focus on target customer groups.

**Questions to ask of your programme**

**What priorities** can loyalty support? Is loyalty the best way? Eg vs investment in price / marketing

**Which customer groups** are you attempting to reach through loyalty? Do you understand how much each group is worth and how much you’re willing to invest?

**Common objectives for loyalty programmes**

- **Increase preference** and capture share of wallet
- **Retain customers** / stimulate next purchase
- **Understand** customers better
- **Expand repertoire** / purchase higher margin products
- **Increase usage of new / preferred channels**
- **Smooth demand / increase utilisation** during off-peak
- **Monetise customer database**

Common objectives across virtually all loyalty programmes – essential to consider which customer groups you want to reach through loyalty – and their needs / value.

Important for companies with store / offline interactions.

Focus on these objectives varies by company – and by customer group. For example, capturing customer data (especially with marketing rights) is highly valued amongst lower frequency groups.
Influencing channel behaviours is an increasingly important objective for loyalty programmes

**Channel Objectives**

- **Travel Operators**
  - Encourage ‘direct’ bookings - maintaining/reclaiming volumes vs OTAs

- **Retail**
  - Encourage use of apps to enhance (and influence) store shopping experience

- **Hospitality**
  - Encourage use of apps to streamline ordering (and reduce cost to serve) and maintain ownership of customer (vs 3rd party platforms)

**Recent Examples Include**

- Hilton Honors Members can choose their room – selecting eg rooms with great views, use digital key, order room service, chat with front desk

- Asda’s new Pounds not Points programme tasks shoppers with in-store app missions – to collect rewards

- McDonalds new loyalty programme requires ordering via the app to earn rewards
Earning something is a powerful motivator. This must have a simple, mass-appeal mechanic.

Questions to ask of your programme

Can you describe the reason to join in a short sentence?

Does the mechanic have broad appeal across your customer base?

Does the mechanic give you scope to target specific customer behaviours you want to change?

“Which of the following would encourage you to join a loyalty programme? Select all that apply

- Ongoing discounts: 50%
- Earning towards a future purchase: 47%
- Access to special deals (e.g. birthday treat): 44%
- Points system with tiered rewards: 44%
- Personalized rewards based on past orders: 37%
- Ongoing freebies: 32%
- Offers mobile ordering/payment: 25%
- Cause-driven initiatives (e.g. towards social cause): 15%

Source: Kantar Profiles/Mintel - January 2022
Tesco shifted focus from a ‘rewards later’ (Points) to a ‘rewards now’ scheme in 2019 through launch of member only Clubcard Prices

Highly visible in store, the shift has delivered a step-change in Clubcard’s already high usage

…and allowed Tesco to maintain share – the only Big 4 grocer to do so in context of Discounter growth

Accessing Tesco Clubcard Prices create a ‘must join’ reason for shoppers to sign-up and realise instant benefit

% Sales from Clubcard Holders

<table>
<thead>
<tr>
<th>Year</th>
<th>% Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>71%</td>
</tr>
<tr>
<td>2021</td>
<td>86%</td>
</tr>
</tbody>
</table>

App usage increased from 2m to 9m Users

Clubcard Prices now account for 100% of Tesco’s promotions
Starbucks Rewards is simple – yet flexible, to nudge customers towards desired behaviours

**Broad appeal and simple mechanic**

- **Universally relevant** as reward (free drinks) are the core proposition
- **Readily understandable** in markets where loyalty schemes are common (eg US, Europe)

**Flexible mechanic which can be used to encourage desired customer behaviour**

Additional stars can be earned through **games and promotional periods**, rewarding customers who engage (and buy) more…

…while customers are steered towards customer journeys which Starbucks wants to promote – eg app / cobrand credit card

1★ per dollar  
Pay as you go

2★ per dollar  
Add funds in the app

3★ per dollar  
With Starbucks® Rewards Visa® Card
SHEIN issues loyalty points to encourage user-generated content eg reviewing clothing

SHEIN awards points for purchase – and for engagement

The simplest way to earn additional points is through leaving reviews

Highly informative user generated content is encouraged as members receive more points for posts with size information and photos

Members can earn up to $20 per day in points through reviews

Most popular items have 1000+ reviews

50 bonus points are awarded for the ‘most helpful’
Earning can encourage ‘everyday’ engagement – half a billion members ‘plant trees’ in Alipay’s Ant Forest

Members of Alipay earn ‘green energy’ from everyday activities – eg walking instead of driving.

Alipay rewards members with virtual trees – planted in app based world…

…which supports Alipay’s commitment to the environment – planting a real tree for each virtual tree

100m+ trees planted

500m members participate
Earning praise can be ‘gamified’ – lifestyle apps have put this front and centre of their approach to customer loyalty

Highly local competitions through Strava’s activity tracking encourage regular participation

Spotify codifies behaviours in sharable soundbites – encouraging social conversations

Peloton uses multiple awards, streaks and competitions to nudge users to regular activity and try new classes
Benefits should be designed to be used. Redemption should encourage incremental purchases.

Questions to ask of your programme

Enrolment isn’t enough – active engagement is key

Average number of loyalty programmes each adult is enrolled in

Average number of loyalty programmes each adult uses regularly

Example Uplift in Share of Wallet for Travel Loyalty programme

Enrolled Member

- 30-35%

Non-Member

- c.30%

Programme Member Uses Regularly

- +0-5%pt

- +20%pt

- 50%+

Are your members regularly using their benefits? Are these benefits valued?

How can redemption be used to stimulate incremental purchases?
TOMS benefits are designed to initiate a new basket – and capture incremental spend

TOMS has designed its points-based loyalty programme with the intention of points being used ‘little and often’ – helping members see tangible value on most orders.

For example – if a member placed a $50 order, they would earn 50 points – redeemable for free shipping on their next purchase.

Redemption encourages the next basket – while never giving away too much.

Excess stock is cleared through points redemption.

TOMS’ social mission is reinforced through charity donation benefits.

Support MENTAL HEALTH
Support ACCESS TO OPPORTUNITIES
Support DISASTER RESPONSES
Support ENDING GUN VIOLENCE

TOMS Gear

520 Points
Women’s Alp Recycled Canvas In 6 colors

520 Points
Men’s Alp Recycled Canvas In 5 colors

620 Points
Women’s Alp Mule In 9 colors

720 Points
Men’s Alp Mule In 5 colors

330 Points
Tiny f
Adidas’ adiClub membership encourages brand engagement, and initiates purchase through exclusive access to launches.

adiClub gives members **priority access** to product launches and events – creating regular engagement with customers, while ensuring that new products are purchased and promoted by Adidas’ best customers first.

**LEVEL 1**
**CHALLENGER**
- Welcome Rewards
- GIVE BACK
- CREATORS CLUB EXCLUSIVES
- HYPER ACCESS
- EARLY ACCESS

0-999 points
Challenger members can also join local events and enjoy member-only discounts and bonuses.

**LEVEL 4**
**ICON**
- Exclusive rewards
- SPECIAL EVENTS
- HYPER PRIORITY ACCESS
- ADIDAS RUNTASTIC PREMIUM 12MTHS*
- ICON BONUS

9,000+ points
Creators Club Icon members receive exclusive access to the very best of Adidas—first.

**5m members**
**56m KM of running recorded by members in adidas training apps**

*Benefits readily available (at a low cost) to all – eg early access, donations to charity*

*Money can’t buy benefits* (eg meeting Messi) offered to a very limited number of adidas’ highest influence customers
IHOP’s new programme gives members more choice in how to spend their rewards through the ‘stack market’

Each $5 spent rewards customers with one PanCoin – 3 PanCoins can be redeemed for pancakes
Halfords’ freemium model is designed to encourage cross-shop between 2 business divisions.

Halfords Freemium loyalty programme stimulates new visits by offering discounted and free services visits. These benefits are targeted at services with ‘known value’ eg MOTs which drives value perception of the programme, and encourages trade-up to paid-for programme.

Since launching in March 2022, Halfords motoring club has >0.5M members and aims to have 1M by April 2023.
Loyalty programmes need to deliver sufficient value to customers as to encourage usage, while minimising cost to deliver.

Questions to ask of your programme

Do you understand the cost / benefit overall and at customer segment level of your loyalty programme?

Do you understand how dialling up / down specific benefits can influence customer behaviour – and programme economics?

3 approaches are commonly used to support loyalty programme economics

<table>
<thead>
<tr>
<th>Monetise ‘free’ assets</th>
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<tr>
<td>Most loyalty programmes create value from monetising assets which are otherwise given away – eg priority access, or have very marginal cost to deliver – eg enhanced service / product</td>
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<td>Making the economics work requires minimising cannibalisation of existing super-user spend (eg limited redemption on high demand lines / dates), while investing just enough to change behaviours of lower frequency customers</td>
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<th>Pass on Costs to Suppliers &amp; Partners</th>
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<td>Customer access is the most valuable asset of any rewards scheme – programmes need to understand the value of a customer to a specific supplier / partner and charge accordingly</td>
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Loyalty programmes of fixed asset businesses (eg travel) can be more ‘generous’, retailers must work hard to create customer value

<table>
<thead>
<tr>
<th>Category</th>
<th>Typical Monetary Value to Customers of Rewards Points</th>
<th>Typical Implied Cost to Deliver</th>
<th>Share of Cost Covered by Partners</th>
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<tr>
<td>Hotels</td>
<td>10.0%</td>
<td>3.0%</td>
<td>High (when franchised)</td>
</tr>
<tr>
<td>Restaurants / QSR</td>
<td>8.0%</td>
<td>2.0%</td>
<td>Low</td>
</tr>
<tr>
<td>Airlines</td>
<td>3.0%</td>
<td>2.0%</td>
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</tr>
<tr>
<td>Retail (excl Grocery)</td>
<td>2.0%</td>
<td>1.2%</td>
<td>Mid</td>
</tr>
<tr>
<td>Grocery</td>
<td>1.0%</td>
<td>0.8%</td>
<td>High</td>
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<tr>
<td>Credit Cards</td>
<td>0.5%</td>
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1. Calculated using PointsGuy.com conversion rates

- **Fixed inventory hotels** commonly operate with c.30% spare capacity which can be ‘given away’ as rewards at a low marginal cost to serve.

- Restaurants **high gross margins** and potential for incremental gross visits / larger orders support generous rewards.

- **Retailers inventory is expensive to give-away**. Reflecting this retailers try to minimise the giveaway of prime stock – encouraging redemption on sale items / priority access. In Grocery, redemption is largely covered by CPG suppliers paying for product promotions.
Fixed inventory businesses eg Hotels, monetise unused capacity through loyalty rewards – marginal cost is low; perceived value high

**Points**

- **Monetise ‘free’ assets**
  - Points redeemed on inventory – few hotels are 100% full allowing assets to monetised at marginal cost

- **Minimise Cannibalisation**
  - Dynamic pricing and black-out dates encourages redemption on lower-occupancy nights

- **Pass on Costs to Franchise Partners**
  - Loyalty members book direct – creating a low cost customer acquisition channel for franchisees who cover the cost of points issued

**Other Low Cost Assets Monetised**

- Members can chose their room – selecting eg, quiet rooms / rooms with great views
- Free / discounted breakfasts and drinks encourage on-property consumption – increasing overall revenue
High restaurant margins support generous redemption rates – a wide range is common to encourage trialing / bolt-on purchases

**Range of implied value from points redemption across menu items**

**Effective Cash Back Rate on Spend with…**

1. **Starbucks**
   
   - Drinks
     - 6%
   
   - Food
     - 7%
   
   - Total
     - 14%

2. **Chick-fil-A**
   
   - Drinks
     - 5%
   
   - Food
     - 7%
   
   - Total
     - 9%

3. **McDonald’s**
   
   - Drinks
     - 7%
   
   - Food
     - 13%
   
   - Total
     - 18%

**Drinks are typically lower value, as rewards often cannibalise existing sales, while food purchases are more likely to be incremental – with uptake encouraged through more generous redemption pricing.**

**Single units are priced more generously than meals – as potential to stimulate new incremental snacking visit, or add on to an existing order.**

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1. Assumes earn rate of 2 per $1 (received from using digital wallet)
2. Menu pricing for major metro areas
Financial Services must ‘work harder’ to make the economics add up – learnings re: eg partnerships are relevant for all

Compare the Market uses *Meerkat Movies* rewards programme as the businesses main marketing tool – and differentiation versus other price comparison websites

The reward appears to be generous to consumers (2 for 1 movie tickets), but is funded by major cinemas as the offer is limited to low utilisation days – Tuesdays and Wednesdays, where incremental ticket sales are highly valued (even when effectively half price)

Understanding ‘the ask’ of potential partners (often customer access), and designing programme benefits with this in mind helps maximise perceived customer value, while minimising the cost to deliver

Low margins in retail banking, a focus on headline rates and sticky customer relationships leave little scope to invest in loyalty rewards. Barclays Blue addresses this by explicitly linking rewards to customers taking out more products with Barclays

Creating explicit links between new products taken and benefits is a great way to manage cannibalisation of existing loyal base, and provide steady, positive programme economics

NB – Markets with higher credit card interchange fees (eg USA) have more latitude to offer generous benefits
Maximising value requires integration across the business

Questions to ask of your programme

Are investments in loyalty considered alongside other price and promo decisions?

How is enhanced customer knowledge being used to improve user experience?

Are you willing to ‘hold-back’ your best proposition for loyalty members? *Eg member only pricing*
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Thank you!