

Altman Dedicated Direct

STRATEGY... TACTICS... RESULTS

MultiChannel Merchant Magazine – October 2005

CROSS CHANNEL

LOYAL SUBJECTS

Making a loyalty program work is a long-term but rewarding commitment

I periodically get calls from prospective clients stating that they “want to start a loyalty program or club”. When I begin to probe and try to understand what they feel the goals of their loyalty program should be, most typically reply with a vague “have greater loyalty from our customers”. Many direct response marketers assume that a formal loyalty program or club is the only option to consider. And most have only a vague idea as to why one should start a formal loyalty program and what such a program can actually achieve.

Let’s start out by addressing what loyalty programs can’t do – loyalty programs can’t create loyalty. Sounds contradictory doesn’t it? But the reality is that true loyalty is garnered by positive experiences your customer has with your brand: your products, your customer service staff, your web site, your retail store and your catalog. If there isn’t enough value in the products you offer, or your customer service staff is surly or unavailable, if your web site is confusing and inaccessible.... all these will reduce loyalty. No formal loyalty program or club can make up for poor quality products or service.

Formal loyalty programs aren’t always the answer. Sometimes there are other actions that will bring bigger payback, sooner. And sometimes there are obstacles that make formal loyalty programs difficult or impossible to implement.

Loyalty programs take time to set-up and execute, and then time to track and analyze to determine results. If your situation demands quick results, a formal loyalty program may not make sense for your firm at this time.

There are also system requirements that need to be met and lacking the ability to execute these may keep you from developing a formal program. Every loyalty program has operational requirements to track members, and ensure they receive the benefits offered. If program memberships are renewed annually then you also need to be able to identify anniversary dates for membership.

And formal loyalty programs are also hard to eliminate. Once you announce your program in your catalog, on your web site and in your stores, taking it back may engender anger from existing members.

All of this means you need to think long and hard about a formal loyalty program before embarking on one, making sure it is indeed the best solution to achieve the goals



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you are aiming for. For example, if analysis shows that getting an increasing the number of one-time buyers who make a second purchase will bring large dividends for your firm, consider if a simple personalized letter and one-time special offer sent at the appropriate number of months after the first purchase if no 2nd purchase has been made, might not achieve your goal with a lot less cost, risk, and time than developing a formal loyalty program.

So what can loyalty programs do? Loyalty programs can enhance existing brand loyalty, increase customer retention and lifetime value, and increase “share of wallet” (the percent of dollars in the product category that the customer spends with your brand) for your firm over competitors.

The first step in crafting any loyalty program is to start with the end in mind – which of the viable goals are you trying to achieve, and for which customer segments? I think it’s important to look at a loyalty program as part of the bigger picture of customer retention. To do that we need to examine questions like:

- How long (on average), have customers been active buyers?
- How long does it take the average new buyer to make their second purchase? At what point after the first purchase does it become more likely that the new buyer will NOT buy again and go inactive?
- For 2x or greater active buyers, how many months after the last purchase is it more likely they will become inactive, rather than purchase again before you classify them as inactive?
- How do you define your “best” (and presumably most profitable) buyers? What purchasing characteristics do they have in terms of how long they have been customers, the number of purchases made per year, number of items and average order size, etc.

If there are different segments of your file based on demographics, psychographics, product categories of purchase or other segmentation characteristics, the answer to these questions may be different for each of those segments. But the point is to look at understanding how and when interaction with your brand is “at risk” of going



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inactive, as well as what actions separate the unprofitable customers from profitable customers and highly profitable customers.

Once you understand what is happening on your file, you can consider what loyalty and retention tactics, including consideration of a formal loyalty program, may make sense to improve the situation. At the heart of every loyalty program (formal or not) you want to focus on:

1. Identifying which unprofitable customers can be made profitable, and what actions are required on your part to move those unprofitable customers to profitable status.
2. Identifying what offers in terms of added value products and services can provide incentive for profitable customers to become more like your best customers.

If after examining your file, if you can meet certain criteria and requirements a formal loyalty program may be the best approach for you. Can you answer yes to the following?

1. Your brand enjoys a certain amount of loyalty already – your products and service satisfy customers most of the time.
2. Your retention goals are multiple and you have defined which segments you want to target with your retention goals.
3. Offering a formal loyalty program will give you an advantage over competitors (and the chance to increase your firm's share of the customer's wallet in your product category)
4. You are prepared to invest the time to develop and analyze results for testing a formal loyalty program
5. You can manage a formal program operationally
6. You accept that implementing a formal loyalty program is a long-term strategy



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If so, a formal loyalty program may be the best approach for you.

If you have done the thinking and after assessing your firm's operational situation has concluded a formal loyalty program makes sense, there are several issues to address and options to consider. Key among your considerations is:

- How do customers become members?
 - Will you charge a fee or allow customers to qualify after a certain number of purchases? Many loyalty programs charge an annual or one-time fee. Marketers with continuity programs such as Principal Secret and Alexis Vogel often automatically enroll subscribers into their loyalty programs.
 - If you charge a fee, will you guarantee the value of the membership? In other words, will you rebate the membership fee if the customer feels the membership has not netted them the value in savings and other offers that you touted when you sold it? Programs who do charge fees, but that have strong guarantees are much easier for a customer to say, "yes" to (Eurosport Goal Club, Camping World's President's Club, Heartland America's Value Club, Sportsman's Guide Buyer's Club).
- What will your membership term be? One year? Lifetime? Annual terms bring more revenue though each year customers once again consider whether or not membership continues to make sense. Lifetime memberships bring less revenue in the long run, but are easier for customers to envision they will surely get the value back versus the fee they paid to join.
- How will renewals be implemented – automatically? Through reminder notices? If you have an annual membership fee, we strongly recommend a reminder notice prior to automatic billing. In other words, make it easy for someone to remain a member (if they don't opt out their credit card will be charged for the next year's membership) but of course provide them notification and ample time to contact you if they don't want to continue as a member.
- Which hard and soft benefits will you offer?



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- Hard benefits refer to items with direct monetary value such as discounts (almost every program offers these), free or free upgraded shipping (Road Runner Sports Run America Club, Eastwood Buyers' Club), free gifts (Improvements, Home Focus), and special payment plans (Sportsman's Guide Buyer's Club) that your member has available as a benefit of membership, and is not available to non-members. Will the discounts you offer be available on all items or only selected items (Improvements, Home Focus)? Selected items may be ok, so long as it's a sufficient number and they include popular items, nit just the "dogs" of your product line.
- Which combination of hard benefits to offer is something to address in light of your margins and the desires of your audience. Do they crave fast delivery? Desire special treatment and recognition when they call in? Get ecstatic over free gift items? Consider what will really get your audience excited.
- Consider making loyalty program discounts explicit in your catalog and on your web site, showing the member price visibly (Principal Secret, Eurosport Goal Club). This tactic has two benefits. First, it lets current members readily see how much their membership is saving them without calculations. Plus, as they decide what to buy versus their overall mental budget for this shopping event in your catalog or at your web sites, they will be tallying up the discounted member prices in their mind and purchase more because they are clear on what the true cost to them is. The second benefit of explicitly showing member pricing is that is an added enticement to prospects and non-member customers to sign up for your loyalty program.
- Soft benefits are added-value services available only to members, or only to members without charge. These include special member toll-free service lines (Sportsman's Guide Buyer's Club, Heartland America Value Club), private early announcements about sales and deals as well as previews of new merchandise (Eastwood Buyers Club), extended guarantees (Road Runner Sports Run America Club, Heartland America Value Club), member newsletters or magazines (Camping World's President's Club), etc. Soft



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benefits can consist of just about anything you can think of that your customers would value that is service oriented.

- Will you track points for members to redeem at a later date (Eurosport Goal Club) or discount purchases immediately? Tracking points requires appropriate software to maintain balances and deduct when points are used. Also assigning points can have less impact because it isn't as immediate as a discount on the spot. Eurosport's Goal Club solves this problem by offering both immediate discounts AND points for future purchases.
- Will you have only one tier of membership, or two (Heartland America Value Club, Road Runner Sports Run America Club)? Two tiers may make sense to move customer up step by step, but it does add complexity operationally. Two tiers may also make sense to ensure your best customers get the message that you consider them Extra” special.

Once you establish the tactics you want to include in your formal loyalty program, take a step back and make sure that what you've put together is clear and understandable. A formal loyalty program with confusing and complicated rules will only serve to stop customers from joining or at a minimum, frustrate and annoy those who do join your program.

So put your customer hat on, and scrutinize how customers join your loyalty program, as well as how they gain access to and use the membership benefits you've identified. Make sure things are simple, straightforward and readily understood, and that you've put enough “meat on the bone” in terms of real value in the benefits offered. For those customer segments that you've targeted to become loyalty program members and increase their retention and lifetime value with you, have you created sufficient value such that they would feel they are missing out if they don't become members?

Once you've identified your tactics, it's time to execute a test. Here's where patience and willingness to spend the money and time necessary executing a controlled test properly is a real virtue.

To test the loyalty program you want to offer, segment a sampling of the audience who is your target. Pull out some of your test segment as your control group who aren't



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offered the loyalty program, and then begin promoting the program to the customers in your test group.

Promoting the new program may mean a separate version of your catalog or perhaps a separate mailing and email to the test group announcing the program and outlining the benefits. Remember that if you rush in and make a blanket offer to every customer and prospect you come in contact with you are making a long-term commitment. It is nearly impossible to “close the gate to the barn after the horse is out”. Once that formal loyalty program is announced in every catalog and on your public web site you won’t be able to “take it back: if you decide that the program isn’t working for you in terms of achieving the projected sales and profitability, and increased customer lifetime value that you were looking to achieve.

It’s hard to say exactly how long a test should run because it all boils down to how confident you want to be in the results, but most will want to test for 6 months before deciding on a full scale roll out. Not only does this allow you to see whether the sales, profit and lifetime value goals you set are beginning to show fruition, but it also allows you to put your loyalty program operations through it’s paces and ensure there are no major “hiccups”.

One final point – make sure that everyone in your firm is up to speed on your loyalty program plans and tests, especially your customer service team. You don’t want a well-meaning customer service rep starting to offer loyalty club membership to everyone while you are trying to limit exposure to the segments of your file you decided to test the concept on.

Formal loyalty programs can be challenging to implement and they may not be necessary for the goals you have to improve retention and lifetime value. When they are done right, formal loyalty programs can help you achieve multiple customer retention goals by converting more prospects to buyers, and getting existing buyers to behave more like your best customers. Keep the end goal in mind, and use that as well as operational realities to guide your strategy and tactics to ensure your loyalty program really delivers enhanced retention and profits for your brand.



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