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Are Customer Reward Programs Really Rewarding?

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Abstract: The concept of a customer loyalty program can be traced back over 300 years when merchants would give customers wooden coins in return for their patronage. Two points are clear: Customer reward loyalty programs are prevalent and costly aspects of most hospitality firms' marketing strategy. From an academic viewpoint our understanding of the theoretical drivers of these programs is muddled and confused. That is, despite many years of existence there is scant research suggesting the underlying theoretical logic of a program. In this paper, we briefly review the current reward program landscape suggesting that the overwhelming presence of reward programs has shifted the consumer emphasis from a reward to an expectation. The implications for future research and program management emerge from this social norm expectation of a program are presented. The paper concludes with a call for collaborative interaction between academics and senior firm management to help further our understanding of this significant, expensive and seemingly necessary business offering.

The concept of a customer loyalty program can be traced as far back as the 1700's when merchants would give customers wooden coins in return for their patronage. The Robinson and Ballou Grocery chain of Troy, New York issued brass tokens as far back as 1863 while the Grand Union Tea Company issued cardboard checks in 1872. The next large-scale program involved providing customers with trading stamps in 1896 when Sperry and Hutchinson launched its Green Stamp program. Under this program, Sperry and Hutchinson sold "green stamps" to retailers that were then provided to customers as a reward for their patronage. Customers could paste their stamps into books and redeem those filled books for a variety of products in the S&H Green Stamp catalog. The green stamp phenomenon provided a clear demonstration of the potential of reward programs, as it created an advantage for retailers that offered the stamps and created a risk for retailers that did not offer such a program. Building on this basic concept of customer rewards, American Airlines launched the first contemporary hospitality industry customer reward program in 1981. Soon after, numerous hospitality and retail firms followed suit and developed rewards programs focused on rewarding their "best" customers, with the goals of securing their loyalty.

Thirty-seven years later, most hospitality and retail firms maintain frequent guest rewards program although the structure and nature of these programs differ wildly (Bertini, Gourville, González & Keller, (2011). Despite the programs' proliferation, many questions remain unanswered as to how these programs can be designed and managed for best effect. We have frequently heard the following two questions from managers:

• What are the key success drivers among the best programs?

• How can a program differentiate itself in a sea of commoditized reward programs?

From an academic viewpoint our understanding of the theoretical drivers of the current stable of loyalty programs is equally muddled. That is, despite many years of existence there is scant research suggesting the underlying theoretical logic of a program. If it were to be a straightforward behavioral reinforcement model, managers might then draw upon a vast and significant psychological literature that describes reinforcement schedules that produce optimal behaviors and in appropriate frequency. The problem is that repeat patronage is but one part of a modern customer reward program. Increasingly, firms must relay on such customer-centric variables as word of mouth, public satisfaction reviews and other forms of firm advocacy. Further, as more and more companies in all sectors of industry have adopted these programs, the question of whether they are truly a reward program versus a customer expectation looms large. More and more the existence of a loyalty program has become the norm and an expensive norm for most businesses. Below, we begin the process of peeling back these layers with the goal of providing future direction for both academics and managers

Customer reward and loyalty programs are prominent and costly aspects of most hospitality firms' marketing strategy. Although most hospitality operators are convinced that these programs are of critical importance—and offer a strong return on the investment—little evidence about the benefits of these programs has been provided in either the academic or popular press. Even when companies claim that their program is a key reason for revenue growth, as occurred in 2013 with both Starbucks and Walgreens, for example, firms are hard pressed to demonstrate continued revenue benefits using existing metrics. Public claims of program effectiveness by major corporations like these often fuel demand for increased accountability of reward programs, but important details are often missing, and so are the actual results needed to support the findings and derive useful insights

These issues play out against a competitive background that essentially requires every hotel firm to offer some kind of loyalty program. Mindful of loyalty program managers' need for a solid methodology to justify the investment in their chain's program, we review some key outcomes of reward programs in this report.

Understanding the Benefits of Reward Programs. A major challenge in determining loyalty program benefits is simply defining exactly what these benefits should be— beyond matching competitors' programs (McCall, Voorhees & Calantone, 2010). Given the dynamic nature of market competition and the natural evolution of a loyalty program, the benefits sought by firms change from program launch to maturity. For example, firms pioneering a loyalty program may explicitly focus on customer acquisition and increased spending among current customers. The program's accomplishments should be relatively easy to gauge in these instances, since one could tally incremental revenue and contribution generated by the program before and after its launch (or before and after a guest joins). Given a competitive market saturated with loyalty programs, however, revenue growth and increased customer acquisition may be unrealistic goals. Instead, the program goal may be reduction of customer churn or switching, meaning that the program is structured as a switching barrier for current consumers (Brierley, 2012). In that case, the firm would have to determine how to measure those outcomes. In the lodging industry, an additional motivation for investing in a reward program is to encourage direct booking by customers (on Brand.com) in an effort to avoid fees charged by intermediaries, particularly online travel agents (OTAs). The challenge inherent in focusing on improving firm performance at a broad level is that many factors influence that metric. Instead, hospitality firms need to be able to assess specific, measurable results from their loyalty programs. If a firm has in fact set up its program as a switching barrier, then the program should be calibrated on its ability to retain consumers, generate more business from loyal customers, and reduce consumer attrition. Those results are quite different from a program that is intended to improve customer acquisition (Voorhees, McCall, & Calantone, 2011). Without clearly establishing logical goals up front, a program cannot be effectively evaluated or designed, and it is near impossible to assess its "benefits."

Barriers to Program Evaluation. This measurement challenge has come through in our discussions with hospitality managers.

One hotel executive told us: "*You know, I have this customer reward program. It is kind of expensive, but I feel like I have to have a program because everyone else has one. Honestly, I don't know what if anything it actually does for me.*"

As this quote suggests, many programs' goal is simply to help firms level the playing field with their competitors. In these instances, loyalty programs are often written off as a cost of doing business and there is little follow through on assessing whether they do provide any value. We think this state of confusion has been caused by several key issues, including the very important notion of the commoditization of reward programs.

Commoditization of Reward programs. One major issue plaguing reward programs is commoditization, as competitors quickly copy any program innovation. As hospitality reward program provisions converge, they become less effective as marketing tools, since customers who are members of multiple programs simply book as they please and collect their points. If a program has no differentiated value over those of its main competitors, assessing potential benefits of increased customer acquisition may be a fruitless exercise. Ultimately, firms will have basically provided a universal discount for all their customers without promoting differentiation between competing brands. So, the result is that market share stays the same and profits drop by the cost of the loyalty programs.

Multi-focused Framework for Program Evaluation. Our tiered approach involves matching the level of evaluation to the firm's size and available data. At the most basic level, firms can simply monitor consumer assessments of the program directly through attitudinal surveys. Alternatively, they may rely on social media to monitor consumers' assessment of the program and any changes to that sentiment. At increasingly sophisticated levels, firms can continually evaluate program effectiveness at every level and maintain a regularly updated management dashboard for their program. At the most advanced level, firms can optimize their programs based on a comprehensive set of attitudinal, behavioral, and cost data.

Where to go From Here. As we step back from this overview of the current state of affairs, it is clear that some form of organizing structure is needed. More importantly, as we have discussed here, management is looking for guidance as to how they might structure their programs to maximize the return on investment Taken together, this brings a series of new avenues for senior management and academic collaboration. For instance, have reward programs become an expected form of repayment for customer patronage? If so, are they really functioning as rewards or more like social norms. This same question has emerged from the restaurant tipping literature where questions about the expectation of a tip by servers is re-defining the practice (Conlin, Lynn, & O'Donoghue, 2003). How do consumers react to rewards ranging in acquisition and exchange utility? In other words, reward "points" have become common place; what perceived non-monetary value do consumers place on this crypto-currency. To what extent do individual consumer characteristics influence these perceptions? Lesser albeit other important opportunities for collaborative inquisition would include: How do consumers evaluate enduring relations rewards (i.e., free upgrades, club-level access, etc.) relative to one-time exchange rewards? What factors are driving these evaluations? In what ways do rewards affect consumers' evaluations of competitive offerings and related switching behavior? Finally, are there other more important value propositions to be pursued other than the acquisition and accumulation of points that can build stronger levels consumer engagement?

Conclusions and Managerial Implications

In the three decades since the modern-day reward program was launched by American Airlines, these programs have grown rampantly throughout the hospitality industry, including hotel companies. A chief goal of the analysis we presented here was to gain better control of these programs. We have suggested here and elsewhere that a properly conceived and executed program can and does deliver positive results in terms of revenue, stay frequency, and consumer spending. This increase in average customer spending was observed even after accounting for the potential benefit associated with direct hotel booking. Consequently, we have begun to answer questions about the true benefit of a rewards program. Managers can now take this information and begin thinking about how they might structure their programs to optimize the "lift" that their program can offer. Future research can also begin to understand how program structure and reward frequency might further encourage customer spending. Finally, there is also value in gaining a better understanding of how a program might drive bookings to the hotel website and away from alternative booking venues. Membership matters and targeting your "best" customers to become members will have an overall positive impact for your firm.

Although reward programs have and continue to proliferate in the hospitality industry, there is still a lack of empirical evidence that demonstrates a direct causal relationship between program membership and attitudinal and behavioral loyalty. The recommendations outlined here are practical in orientation, but they are derived from various theories of human decision and consumption behavior. In closing, these recommendations are meant to serve as broad, guiding principles for programs in the hospitality and gaming sectors. Because each company and each program are distinct, there is no universal recipe for designing a loyalty program that is both effective and beyond imitation. Above all else, the most important strategic investment in any program is customer research. By understanding your customer base and loyalty program members, managers can make informed decisions on how to advance their programs. We think a review of rewards and loyalty program operations is timely, because many seem to have hit maturity, and the companies that can effectively advance their programs through effective differentiation that meets members' needs will capture a lead in the battle for customer loyalty. We hope that the call for collaboration introduced in this report can provide managers with an initial set of factors to consider as they evaluate and advance their programs.

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