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Lessons From Along Loyalty Lane

At the 9th Annual CRMC (Chicago, June 5, 2003) Brian Woolf, author of 'Loyalty Marketing: The Second Act' described some highly successful food retailers who are doing an outstanding job with CRM. This is a summary of his presentation...

by Brian Woolf (January 23, 2004)

CEOs embrace loyalty programs because of their economics. Consider the analogy of site location. When evaluating two possible new store sites, the one with the higher projected ROI will be chosen. The same logic applies to customers. A rational CEO will choose to focus on that customer segment which yields the highest projected (or actual) ROI. Loyalty marketing is, essentially, all about such economic differentiation. It's about deciding how to optimize our long term yield from the limited resources we have. Understanding our customers' behavior and economics (derived from our loyalty program) allows us to do just that. Some food retailers whose loyalty programs exemplify this thinking include Gerland's, Dorothy Lane, Big Y, A-Coop, and Tesco.

Gerland's
Gerland's, based in Houston, Texas uses a two-tiered pricing strategy. Customers receive lower prices on a wide range of shelf-identified items, triggered when their cards are presented at check-out. In addition, the company offers points on a selected range of identified items (typically private label and high gross margin items). When a customer has accumulated 400 points, a 5%-discount certificate (to be used against any subsequent purchase) is automatically generated and given to the customer when paying for her purchases.

The Gerland's loyalty program accomplishes three main goals. It:

1. Differentiates the company from its competitors
2. Keeps customers coming back to the store (the points and discounts act as hooks)

3. Provides marketing flexibility as the company can add varying amounts of points to any customers accounts as needed (eg, locking in new customers, holding selected customers when a competitor opens)

Issuing points on a varying number of higher-margin items is superior to the traditional one point per $1 spent program because it is more flexible and costs less.

Another unique element of the Gerland's program is that it gives its members additional rewards as their spending increases. The rewards available at four different spending levels are publicized and known to all customers. Rewards include check cashing privileges, earning your 5%-certificate at lower point thresholds, and lower spending amounts required to buy specially priced merchandise.

The most important aspects to note about the Gerland's loyalty program are that it is:

- Open
- Tiered
- Transparent (the different reward levels are known to all)

The basic principle behind Gerland's program is that customers who spend more contribute more to the company's profitability and, therefore, should receive greater rewards. Its program is grounded in logic and economics. It's no surprise that Gerland's has a very successful program.

Dorothy Lane
This three-store chain, based in Dayton, Ohio, launched its loyalty program six years ago. After just 14 weeks into the program Dorothy Lane replaced its weekly newspaper advertising with a monthly, 8-page newsletter mailed to just the top 30% of its customers. This was a very bold move—a first among food retailers—but it worked admirably. By focusing on the top 30% of its customers, who generate 75% of its sales, Dorothy Lane was applying basic economic sense: matching costs to revenues.

The same economic sense flowed over into its newsletter. The back page carries eight high-value coupon items: with different prices for the top 10%, next 10%, and third 10% of customers. Customers know the average weekly spending thresholds that trigger the different coupon prices. Therefore, customers set their own prices! At Dorothy Lane, the more they spend the lower their prices will be. This, of course, is the same set of rules that apply when businesses buy from suppliers.

Each month the company also sends customer-specific postcard offers for items they regularly buy. The pricing of these offers are so aggressive the postcards usually elicit a Wow! when received. So Dorothy Lane calls them their *Wow!*postcards.

By radically altering its promotional cost structure and increasing the value to its higher-spending customers on an individualized basis Dorothy Lane has been able to dramatically increase its profits.

Big Y
Springfield, MA-based Big Y, a privately-owned $1 billion food retailer has developed a unique program. Its marketing program is extremely promotional, rare for a loyalty program. Its weekly advertisements scream headlines such as:*10 Cent Sale! 25 Cent Sale! Unlimited Triple Coupons! Super Express Deals! Buy One, Get One Free! Buy Two, Get Three Free! And Buy One, Get Two Free!!!* The economics of some of these promotions are hard for competitors to understand, but somehow the overall combination works as they are regularly repeated and the company keeps growing.

These crazy promotional prices act as a magnet to draw customers to its stores and, once there, Big Y introduces another magnet: “coins” (actually, four different-colored plastic tokens). Big Y has never announced, either to its customers or employees, what triggers the generation of a red, blue, silver, or gold coin when a customer is checking out. Because coins are not issued in every transaction, “winning” a coin is a surprise to customers. As you can imagine, behind the scenes, Big Y carefully analyses customer behavior and spending. Then, after deciding which customers it wishes to reward or influence, it downloads computerized instructions to the stores’ point-of-sales terminals to give specific-colored coins to specific customers should they shop that week.

Obviously, the different colored coins carry different values and are redeemable for different identified items in its stores. (The range of items changes twice a month.) The coins have no expiration date and are redeemable only at Big Y. They act, in effect, as an alternative currency which brings the customers back to Big Y, rewarding them for their past patronage. They act as a brilliant exit barrier. How can a customer stop shopping at Big Y if she has a purse full of “coins” and more keep coming when she shops?

Like the previous programs mentioned, this program is highly successful because of its flexibility (the company decides who receives what coins and how often) and its adherence to economic differentiation: it is the higher-spending customers who receive the higher-value coins. A company which bases its program on these two foundations will always succeed.

A-Coop
A single store in a foreign country may not seem a likely place to learn great loyalty lessons but A-Coop, about 100 miles from Tokyo, is one of my favorite programs.

A-Coop's base program is very traditional—customers receive one point per ¥100 (approximately $1)—but its ingenuity lies in the way it rewards customers for spending "big" with them. Rather than appeal to customers with three-times-a-week advertisements (the norm in Japan), A-Coop dropped all advertising in 1996 and switched those monies to rewarding customers based on how much they spend. Since then, A-Coop's customers have received quintuple points on their purchases on the 5th, 15th, and 25th of every month. The result is that this program almost guarantees three very large purchases from customers every month.

And the points? A customer can insert her card into the store cardholder kiosk and read her latest balance at any time. Points are redeemable from the kiosk as certificates in 1000-point (the equivalent of $10) amounts. These can be used to reduce the cost of any purchase; or applied against any special event a customer bids on (eg, customers can enter a sweepstakes for a limited number of seats for a one-day visit to Tokyo Disneyworld, using the 1000-point certificates); or, can be used on the first Tuesday of December, when each 1000-point ($10) certificate increases in value by 50%, to $15! Not surprising, this is the busiest day of the year for A-Coop.

The genius of this program lies in its simplicity and its economic differentiation: those customers who spend more (particularly on certain easy-to-remember days each month) gain the greatest returns. Who needs to advertise with such a potent easy-to-understand formula?

Tesco
Tesco is the largest food retailer in the UK. Its uniqueness lies in how it has used its newly-gained customer information better than any other large retailer, anywhere in the world. Tesco's strategy is to *Circle the Customer*.

After gaining customer information from its simple 1%-rebate program (roughly, earn one point per £1 spent, receive a quarterly rebate check equal to 1% of quarterly spending) Tesco has converted that data into helping build its supermarket business—and a great deal more. Customer information has been used to help develop the leading UK food home-shopping business; build, from scratch, profitable banking and insurance businesses; lay the foundations for an extensive Internet shopping mall; and add to its market appeal by allowing Tesco points be earned and redeemed at other UK retailers.

The information gained by Tesco on its customer behavior has allowed it to understand their customers' myriad needs and then find profitable ways to solve them. Rather than just thinking how to increase customers' spending in its stores, Tesco is using its customer data to solve a bigger riddle: *In what ways can we satisfy more of our customers' needs (even if this means moving into new businesses to do so)?* Tesco is a classic example of what it means to be customer-centric.

Closing Comment
All of these companies have moved beyond deciles (breaking customers into ten equal groups), the traditional way of classifying customers. Rather, they classify customer spending based upon average weekly spending thresholds. For example, among food retailers in the US, the four typical spending thresholds are: Diamonds (over $100 week average); Rubies ($50-100); Opals ($25-50); and Pearls (under $25). A fifth group, New Customers, rounds out the customer classification.

The reason why thresholds are preferred to decile rankings is because they are so much easier to understand and manage. It's easier to aim at increasing the number of customers spending over $100 per week, for example, that improving the metrics of the top 10% of customers (as we don't know how many customers will be in the top 10%).

To date, the single best measurement for business success that I have found is: *By how much have we increased the average number of Best Customers (Diamonds and Rubies) Per Store this year over last year?* All of our efforts should be focused on improving that number—as do the retailers I have talked about today.

About the author...

Brian Woolf is a global leader in loyalty marketing and has written three definitive works on the subject, Measured Marketing: A Tool to Shape Food Store Strategy, Customer Specific Marketing, and Loyalty Marketing: The Second Act. He devotes his time to helping retailers develop, critique and strengthen their loyalty programs.

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