MARKETING

The Philosophy of Rewards

BY RICK FERGUSON

We've all participated in enough loyalty and incentive programs to know a generic reward when we see one. Anemic discount or cash-back offers; gift certificates from the usual suspects; toasters, trinkets and trash providing scant instant gratification, while the impossible-to-obtain balloon rides, luxury getaways and plasma TVs make us skeptical of ever earning anything of value.

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— RICK FERGUSON

When a loyalty program fails, marketers are want to blame the strategy of loyalty marketing rather than take a hard look at the value proposition of their particular offering. Often, however, it's the reward strategy itself that's to blame. After all, who wants to participate in a program in which you can't afford the rewards you want and you don't want the rewards you can afford?

COLLOQUY promotes an alternative to the genericness inherent in most loyalty reward catalogs. Over the past five years, we've witnessed the evolution of enhanced value propositions that seek to leverage consumer desires for new, value-added, emotional, experiential, unique and compelling rewards. We call it the "Wow!" factor, and it has become the differentiator between loyalty programs that make a real impact with consumers, and those that just twitch reflexively, like fresh roadkill, before finally giving up the ghost.

Most loyalty marketers agree that a successful loyalty program should offer a perceived reward value of 5 percent. In other words, for every $100 members spend with you, they should earn a reward worth — at least to their minds — $5. For most programs, this is a minimum threshold. Some industries can afford higher funding rates depending on their business model and margin structure.

Note the difference between perceived value and actual cost. If you give back a penny off each gallon of gasoline, the *perceived value* and actual cost of the reward are identical: a penny is worth no more or less to your customer than it's worth to you. A free cup of coffee and a donut with each fill-up, on the other hand, may carry a perceived value of $5, while your actual cost is much lower. The gap between perceived and actual value represents your incremental profit. And profit, of course, is the ultimate reason to run a loyalty program.

How do you generate the perceived value that infuses your program with the "Wow!" factor? Here's a rundown on four of the most common methods.

In-kind Rewards

The low cost of delivery makes offering your own goods and services as rewards an easy way to generate perceived value. We call these "in-kind "rewards. You can list a variety of in-kind offers in your rewards catalog: carwashes, fuel, merchandise, food and beverage and anything else you sell.

In-kind rewards carry a distinct advantage over cash-back rewards, because the perceived value of the reward is greater than its actual cost. They offer better leverage than rewards you have to buy from outside vendors. Lastly, because they protect the integrity of your retail price points, they're far superior to discounts. The actual cost of delivering an in-kind reward is often so much lower than its perceived value that you may be able to decrease your funding rate while still delivering compelling hard benefits to your members.

Be aware, however, that customers can experience too much of a good thing. In-kind rewards offer great economic leverage, but they can quickly become boring and irrelevant. Even dedicated caffeine addicts can only drink so many free cups of coffee per week.

Other People's Money

All loyalty marketers have the opportunity to solicit third-party partners to play in their programs. In return for promotional considerations and access to your membership, they offer you rewards from their own portfolio of goods and services at wholesale. We call this technique "other people's money" (OPM), and it gives you more leverage than any other aspect of your loyalty program.

The premise is straightforward. Partner A want access to your members because either they're already his customers or they represent potentially lucrative new business. Partner A would normally have to spend money to acquire new customers by marketing through channels filled with people who have no interest in what he's selling. You, however, have the audience the partner seeks, and they're already engaged with your loyalty program. If Partner A wants to acquire new customers for a fraction of what he normally spends, all he has to do is put some money into your hands. You pass that money on to your members in the form of program value, and you reap the benefits without incurring additional expense.

OPM is an excellent way to stretch the value of your loyalty program rewards. You give members something to aspire to without paying the full retail price, and you generate more excitement around your program than is possible just with in-kind rewards. Ask a potential partner about his typical cost of acquisition, and then offer him access to your members for less. Chances are, he'll bite.

Merchandise Rewards

If you have the budgetary muscle to afford a full rewards catalog, offering an array of desirable third-party merchandise rewards can really help your program achieve critical mass. Because merchandise price points cover the entire spectrum from inexpensive to luxury goods, from music CDs to golf clubs to those awe-inspiring plasma TVs, you can include a variety of items in your reward catalog. Variety is important. Some members will redeem quickly for an inexpensive item, while others will save up for something they've dreamed about.

You can also apply the OPM principle to merchandise. A vendor may want you to push its stuff more aggressively than you push its competitor's stuff. Make the vendor pay for it — either to help fund a transactional bonus or to cut you a deal on a reward item. After all, you're delivering customers to that vendor.

Experiential Rewards

Every member in your program has a secret desire. One may want to attend a cooking class. Another may want to celebrate an anniversary at that swank five-star restaurant downtown. Still another may want to get behind the wheel of an Indy racecar. Experiential rewards appeal to a member's dreams and sense of personal fulfillment. They're the most powerful rewards in your arsenal — but they're also the most expensive to fulfill.

Survey your members to learn more about the types of rewards they dream about, and then secure a fulfillment partner to offer them. It may take a member several years of dedicated service to earn that coveted reward, but some will do so. You can help by increasing their velocity of earning with a co-branded or private-label credit card, or by awarding the most desirable rewards via a points auction or sweepstakes. The key here is to listen to your members. Don't just assume that everyone in your membership base wants to earn a weekend ski package.

Keep in mind that offering "Wow!" rewards doesn't have to break your budget. A free milkshake from your dairy bar can wow your members just as easily as a free flight to a tropical locale — if their transaction file and survey history tells of their fondness for milkshakes. Read your database and offer rewards that are both relevant and personalized, and high perceived value will follow as a matter of course. When it comes to loyalty rewards, customers don't expect the moon. They just want to know that you care.

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