Evaluating the Impact of a Loyalty Program on Brand Loyalty

Can loyalty programs produce deviations from established 'Dirichlet' patterns of repeat-purchase?

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Evaluating the Impact of a Loyalty Program on Brand Loyalty: Can loyalty programs produce deviations from established ‘Dirichlet’ patterns of repeat-purchase?

Abstract

This thesis evaluates an intervention in the marketplace. It examines the impact of a loyalty program on brand loyalty in a series of seven studies/replications across two countries and five product categories.

The primary purpose, in terms of knowledge generation, is to provide an indication of the expected effects of a loyalty program on repeat-buying patterns.

The research reported in this thesis adopted a novel approach to assessing this effect. Panels of respondents were set up close after the introduction of the loyalty program and weekly purchasing data were collected from individual households. This repeat-purchase information was used to calculate the Dirichlet model of repeat-purchase which provides norms for repeat purchase statistics by brand. Dirichlet provides stationary market norms, that is, it describes how the market should normally look and predictions of how it will look if purchase patterns are not disrupted, say by a successful marketing intervention. By comparing Dirichlet predictions of key repeat-purchase statistics with the same statistics based on the observed data I sought to identify and quantify the impact of the loyalty program intervention in terms of bringing about “excess” purchase loyalty.

Loyalty programs are designed in a way that appeals primarily to existing customers, encouraging them to increase their purchase loyalty. A loyalty programs should, therefore, not have the usual disproportionate effect on a brand’s market penetration (number of customers) over its effect on purchase loyalty. Indeed a loyalty programs would rather be expected to have a disproportionate effect on purchase loyalty and no, or little, effect on penetration. This would result in deviations from Dirichlet predictions in terms of the
Dirichlet model underpredicting the brand's level of purchase loyalty and overpredicting its level of penetration.

A panel was set up to gather information on the impact of the launch of the FlyBuys loyalty program in Australia. It covered four product categories: retail fuel, supermarkets, department stores, and credit cards. A similar panel was established in New Zealand to evaluate the impact of FlyBuys in that market, this panel covered retail fuel, credit cards and home telecommunications (toll call provider).

Overall the methodology appeared to work well; it appeared to be able to identify the hypothesised marketplace changes when they occurred. It did so in spite of the changes being quite subtle particularly in terms of marketshare shifts. It did so very early in the loyalty program launch using quite a limited period of data collection. It did so in spite of simultaneous other market interventions, and it provided some tests of causality.

In the three 'repertoire' categories in Australia (retail fuel, supermarkets, and department stores) the loyalty program was associated with mild and inconsistent 'excess loyalty' effects. Overall this appears to be evidence of an effect, though very weak, on repeat-buying patterns. In the one 'subscription' category, credit cards, where brand switching or even changes in share of category requirements would be especially difficult to achieve, there was evidence of the loyalty program instead increasing the amount of usage by existing customers. The same sort of pattern was observed in the New Zealand credit card category.

In the New Zealand retail fuel category, where there was virtually no brand level differentiation, the loyalty program produced a more obvious excess loyalty effect. A simultaneous sales promotion for another brand also delivered a small degree of excess loyalty though far less pronounced.

A summary of key findings follows:

1. This research has supported the use of Dirichlet norms to assess the impact of marketplace interventions, or at least loyalty initiatives. The comparisons against Dirichlet predictions seemed to work as expected in being able to show the impact, or lack of impact, of these marketing interventions. The thesis provides a methodological and analytical framework for further studies of this kind.
2. The research has provided significant support for the contention that, when loyalty programs successfully impact on buying behaviour, they bring about excess loyalty rather than 'normal' patterns of market share gain.

3. Loyalty programs seem, at best, to have a weak impact on the market. They produce a small or even no degree of excess loyalty.

4. Loyalty programs do not appear to attract mainly heavy buyers of the category, but rather attract existing buyers of the loyalty program brand(s); both heavy and light buyers. Most of these customers will receive loyalty program points for undertaking no change in buying behaviour. Even if they do change behaviour they will still be given points for a substantial amount of buying that they would have undertaken anyway regardless of the loyalty program.

5. Loyalty programs are therefore best thought of as highly defensive, and, in line with their name, they are for increasing the loyalty of existing customers rather than winning new customers.

6. The research supports those who have argued that changing fundamental repeat-purchase patterns is very difficult. Brands typically show only small differences in purchase loyalty. The findings in this thesis show that this remains the case, even when some degree of excess loyalty has been achieved by loyalty program brands. Loyalty programs do not seem to induce market partitioning and they certainly do not turn repertoire categories into subscription categories.

7. The research has supported the argument that loyalty programs are unlikely to have a substantial effect on market share, and that even if they impact on repeat buying behaviour and bring about excess loyalty they may not produce substantial market share movement. The argument that market share or sales gains are an inappropriate way to assess loyalty program performance is supported by the empirical evidence in this thesis.

8. Loyalty programs appear able to stimulate increased usage in subscription markets. As expected, there was no evidence that they could encourage brand switching in subscription markets. In repertoire markets loyalty programs appear to have little or no ability to induce brand switching, nor induce other substantial changes in repertoire weights.
9. A lack of brand level differentiation (including price differentiation) seems strongly related to increased loyalty program impact. Markets that are promotion sensitive appear to be loyalty program sensitive as well. The magnitude of the effect observed in such conditions was approximately one extra repeat buy every 10 repeat buys. This is probably the upper bound of loyalty program impact on purchase loyalty.

10. The research also provides some evidence that promotions, rather surprisingly, also create excess loyalty rather than excess penetration or the normal ratio of gains in penetration and average purchase frequency. This provides further support for the contention that promotions are taken up largely by existing customers (Ehrenberg et al. 1994). However, they do appear to have a more 'normal' impact on purchase patterns than loyalty programs. That is, what was observed suggested a reasonable, though less than expected, degree of penetration growth to accompany purchase loyalty increases.

11. Loyalty programs do appear capable of insulating a proportion of a brand's customers from the 'temptations' of competitor promotions. This raises the issue of whether or not loyalty programs bring about increases in differentiation loyalty (decreases in vulnerability) perhaps even when they do not cause increases in purchase loyalty. This research was not designed to address this issue, which is an important limitation of this thesis and an opportunity for future research.

1 Though the panels did not really run for sufficient time to assess this properly.
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