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Truly Loyal Customers Do Not Have to Be Bought

Customers who stay for rewards leave for rewards.

by [Matt Hasan](#)
Monday, November 15, 2004

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Myth: Companies should do the most for their most loyal customers.

Many companies in a wide variety of industries have what are known as "loyalty programs." This practice, which is based on rewarding frequent buyers, started with the airline industry almost two decades ago, was then adopted by other members of the travel industry like hotels and rental cars companies, and has now spread to industries ranging from telecommunications to retail trade. Although each industry's program has its nuances, the basic structure is common to all of them: award miles or points to customers based on their "spend." Almost all of them allow customers to earn rewards at a higher rate by achieving higher levels such as silver and gold or premier and elite, etc.

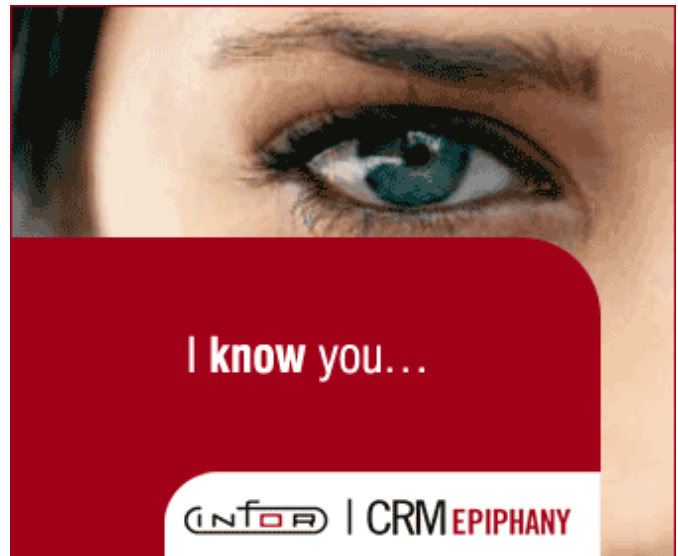
The foundation for these programs is the myth that providers should do the most for their most loyal customers.

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The key issue that needs to be looked at is that the myth implies that customers have to be rewarded at increasing rates to keep them loyal to the company. This contradicts the meaning of the word loyalty, which is "an unconditional and unwavering allegiance to something." In plain language, if it has to be bought, it is not loyalty.

Some might say that the issue is one of semantics. For example, when providers make statements like "we value and reward our loyal customers," they are trying to convey to the customer that loyalty is a



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positive trait which deserves to be rewarded.

On the face of it this would be fine if it was simply an issue of semantics with no repercussions for making effective business decisions. Unfortunately, that is not the case. Companies are allocating substantial resources to reward "loyalty" from customers, which is actually incenting the opposite behavior. Customers who stay for rewards also leave for rewards. The ante keeps rising.

What companies need to do is to establish win-win relationships with each customer based on an understanding of their internal loyalty intensity. In this approach the most loyal customers are the ones with the highest inherent propensity to stay with their current provider. Research, including my own, has shown that this internal loyalty intensity can be measured via the application of appropriate statistical and neural methods on carefully defined and compiled customer attribute data consisting of psycho-economic-demographic characteristics for consumers and culture-tradition-history-structure characteristics for businesses. The complex interrelationships between these characteristics determine the implicit cost of switching for any given customer. The higher the implicit switching cost the more likely it is that that customer will continue to do business with the current provider. From this it follows that customers who are intrinsically most loyal need the least amount of rewards or incentives to stay with a provider.

So, the reality is that companies have to do the least for their most loyal customers.

For loyalty programs to be truly effective companies should determine the inherent loyalty propensity of each customer and allocate rewards to them on the basis of their true worth, which can be calculated from their loyalty intensity score, lifetime-revenue stream, and all direct and indirect costs incurred in serving them.

About the Author

Matt Hasan, Ph.D., is a vice president in the CRM practice at Capgemini, a global consulting, technology, and outsourcing firm with more than 55,000 employees. Prior to Capgemini he led CRM practices at IBM Global Services, Deloitte Consulting, A.T. Kearney, and Sigillum Corporation. For more information on the above and related topics, he can be reached via email: matt.hasan@capgemini.com

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