THE VALUE OF REWARDS IN A REFERRAL-BASED LOYALTY PROGRAM

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ABSTRACT

Loyalty and rewards programs provide incentives to customers in exchange for their membership. The presence of these programs is widespread in the marketplace and consumers are beginning to expect such programs to be available across many industries. However, the cost of operating these programs is significant.

This study analyzed a rewards program in which members of a health club are rewarded for referring other new members. The purpose of this study was twofold; identify who participated in the rewards program, and determine if members value rewards. Secondary data on member participation within the program was gathered, and a survey was distributed to members. The secondary data displayed that behaviors varied by age group, gender, and stage of membership tenure. The survey found that a majority of members value this firm's rewards program. Based on the data, suggestions for improving the program are provided.

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INTRODUCTION

Loyalty and rewards programs are everywhere in the marketplace, and in every type of business, including retail, transportation, financial services, and food service. Definitions of loyalty programs vary, but researchers are in general agreement on the nature of these programs. Loyalty is a commitment to repeat purchase behavior of the same product or brand (Furinto, Pawitra, & Balqiah, 2009). A loyalty program (LP) is an incentive program where members are rewarded for a single or multiple pre-determined behavior(s) (Fichter & Wisniewski, 2010). Because loyalty programs (LPs) reward members for taking designated actions, they are also referred to as rewards programs (Yi & Jeon, 2003). The terms loyalty program and rewards program are used interchangeably in the academic literature.

The purpose of this study was twofold. The study explored the demographic profiles of members of a health club who participated in a program where members are rewarded for referrals. Rewarding for member referrals was the only type of reward activity analyzed in this study. Second, the perceived value of this rewards program was assessed. Because the rewards themselves could encourage or discourage the desired referral behavior, specific improvements to the merchandising strategy are suggested.

Program background

A health club operating over 100 clubs in North America has developed a rewards program in which members are rewarded for membership referrals. Because this health club operates on month-to-month memberships, memberships are not contracted and therefore voluntary for each month of membership. Members who refer other new members are labeled as promoters, and promoters are considered to be the most valuable customers. The same currency used to reward members for referrals is also used by the company for other promotional purposes, such as incenting new members to sign up for a membership, and for various customer service-related gestures. However, the only action that is consistently rewarded and promoted is referring new members, which is why this was the single action evaluated in this study. The firm desired to explore ways in which they could increase participation and redemption rates of the program.

For investors, an important measure of the firm's success is the number of new members joining the health club, along with a low attrition rate, which is measured by the annual percentage of members who terminate their membership. Improving the merchandising strategy for the rewards program is essential in order to encourage the members to initiate referrals. This study will provide the firm with suggestions for improvement of their reward program by using the research data.

REVIEW OF LITERATURE

Over 1.3 billion loyalty program memberships existed in 2007, with each household averaging 12 programs, of which 4.7 were actively used (Ferguson & Hlavinka, 2007). Membership in these programs doubled from 2007 to 2012 to 2.65 billion, which equated to $50 billion in rewards in 2011 (Barry, 2013). The value of LPs and rewards programs are current topics of dispute because many LPs do not actually change consumer behavior but are rather an additional perk of purchasing with that particular retailer. Some researchers believe that LPs stimulate product or service usage, and in turn will increase purchases and revenue (Omar & Musa, 2008). However, because LPs are now a proliferated marketing scheme, the competition between LPs is now a topic of additional research. Rewards among LPs in related industries seem to be rather similar (Lara & Madariaga, 2007). Some research suggests that customers may be becoming wary of LPs and are more selective in which programs they join, known as the experience of loyalty fatigue (Wright & Sparks, 1999). Marketers are challenged to create broader and more creative rewards in order to meet the needs of many different groups of customers. Despite the trend of using LPs, 70% to 80% of apparel and grocery customers said they were not loyal to one particular retailer (Omar & Musa, 2008).

It is no doubt that LPs are expensive, and the return is often difficult to measure. Because buyer behavior is dependent on many things, it could be difficult to determine which consumer actions resulted from the involvement in a LP. As early as 2000, LPs were a notable expense of some of the world’s largest retailers. The top 16 retailers in Europe spent about $1 billion on LPs that year, and some large supermarket chains spent over $150 million on individual LPs (Omar

& Musa, 2008). Magi (2003) agreed that the results on the return of LPs are mixed, and also that they have become a basic marketing expenditure.

Research on LPs has been ambiguous, with some studies claiming the programs actually encourage the wrong attitude, or that some only attract those members who would already be loyal, despite the program (Daams, Gelderman, & Schijns, 2008). Shugen (2005) claimed that LPs do not foster loyalty because they produce liabilities versus assets. In markets where there is little expandability and demand is fixed, LPs seem to be developed as a defense mechanism. After most viable players incorporate a LP, all programs result in a zero-sum game. However, in markets with high expandability where demand is more flexible, LPs can be a good strategy for gaining market share (Liu & Yang, 2009; Singh, Jain, & Krishnan, 2008). In a business-to-business setting, Daams et al. (2008) suggest that a LP where rewards are earned through repeat purchase behavior does increase customer loyalty. They also deduce that customers who were previously considered loyal became more loyal after the program was introduced, and the members of the program who were originally less loyal became even less so. Despite the existence of the research negating the effectiveness of LPs, companies continue to build and promote their programs.

Loyalty programs in marketing

American Airlines started what is considered the first loyalty program in 1981, their frequent flyer program. The financial, hospitality, automobile, service, and retail sectors now commonly have rewards programs. Companies commonly introduce LPs to increase customer satisfaction and offer differentiation among competitors, especially since price and quality differentiation is difficult to execute (Farooqui & Rehmaan, 2010). Tesco was the first retailer to introduce a LP in the form of their "Club Card" in 1995. This was a revolutionary concept at the time, especially because Tesco found that Club Card vouchers generated a 51% redemption rate, which was significantly higher than the 3% to 5% typical Tesco promotion rate. NCH Marketing Services report that coupon redemption in the US averages between 1% and 2%; in the UK, this number is on the lower end of the scale. Loyalty programs are appealing to marketers because coupon or voucher redemption rates that are issued as a part of a LP are much higher than general coupons, at 47% in the UK (Smith & Sparks, 2009).

Loyalty programs were created to satisfy a variety of marketing and sales needs, primarily based on customer relationship marketing (CRM) (Omar & Musa, 2008). From 2000 to 2006, LP participants rose to over a third of all consumers, providing a large amount of consumer behavior data for companies to analyze (Liu & Yang, 2009). A LP gathers significant data about customer buying patterns, and allows marketers to segment and target their customers. Merchants also find the data helpful when profiling their target market, along with creating merchandising strategies that continue to appeal to current customers, while attracting new segments of the market. All of these actions result in building a relationship with customers and in turn, increase sales and positive perception of the firm (Farooqui & Rehmaan, 2010).

Farooqui & Rehmaan (2010) outlined different types of LPs:

- Appreciation programs, where LP members can use their reward currency toward that same company's products or services.
- Rewards programs, where members can redeem reward currency on unrelated products or services.

- Partnership programs are LPs where one company shares their loyalty database with another company, and the partner company can market to the database, and members can redeem rewards at either company.
- Rebate programs allow discounts or money back for the more a member purchases.
- Coalition programs involve a few to many companies that share a common company demographic, and customer databases are shared among all partner companies.

Loyalty program design

Firms can construct LPs in a variety of ways. Some actions that may be required to earn rewards in any given program are spending certain amounts of money, buying specified products or brands, purchasing at certain times and/or days, or frequenting the store a certain number of times. The design of the LP contributes to the attitudinal loyalty consumers have toward the program, which in turn impacts total consumer spending. Most LPs are constructed in a way in which the highest users or purchasers also receive the highest rewards (Omar & Musa, 2008). The design of a LP, specifically the required effort and potential reward, affect the likelihood of joining a program (Zhang & Breugelmans, 2012). Also, marketers must be cautious that their LP is not confused with their promotional strategy, which typically is created with the goal of increasing revenue rather than gaining true customer loyalty (Furinto, Pawitra, & Balqiah, 2009).

There are properties that LPs should define in order to adequately present the program to customers. Reward distance and step size are among these properties. Reward distance clearly shows how many points or rewards must be earned in order to redeem the points. Step size defines how many points each desired action earns (Bagchi & Li, 2011). For example, members of a health club may need 100 points to purchase a yoga mat (reward distance), and each new member they refer earns the referrer 50 points (step size). A lower "point threshold" is perceived as more easily achievable because the perceived effort it takes to get to the reward seems smaller. Zhang and Bruegelmans (2012) studied item-based loyalty programs (IBLP), where price discounts are replaced by reward point promotions. They found reduced customer attrition rate with the IBLP and increased positive feelings and attractiveness of the retailers because the LP is exclusive to only shopping with that one retailer and shopping elsewhere does not have the same reward. The cost of switching retailers is greater if one shops elsewhere. They call this the "lock in effect." Companies such as CVS Pharmacy used a combination of IBLP and promotional price discounts. IBLP can also be used for manufacturer/retailer collaboration, to promote certain products. One third of LPs are assumed to be multi-sponsored, and they can be used to establish relationships or rapport between customers of each sponsor (Lara & Madariaga, 2007).

Liu and Yang (2009) define the three elements of a LP's design as participation requirements, point structure, and rewards. Participation can be voluntary or automatic, and a firm can determine how much effort is required of the consumer to earn and/or redeem points. Point structure is the amount of reward points that are earned for various activities. This is where the thresholds for redemption and reward minimums are created. Effective LP structures guide the member to recognize purchases as a sequence of associated transactions, not individual purchases (Omar & Musa, 2008). And the closer members are to a reward threshold, the more effort they will exert to reach the reward (Bagchi & Li, 2011). Loyalty scheme design impacts the redemption rate. Ease of points collection, reward attainment, delay between collection and redemption (by the points threshold or other criteria), and time it takes to redeem all influence the effort to redeem rewards (Smith & Sparks, 2009).

Omar, Wel, Musa, and Nazri (2010) found program trust to be an essential piece of the program model because trust is an important component in building a relationship with the customer. Omar (et.al, 2010) defined trust as the level of confidence the member has that a set outcome will be achieved when the expected behaviors are completed. Trust can increase commitment and also is the foundation that is typically present before commitment is established. To encourage trust in a LP, the program construct must be well defined and communicated to the customer. The more ambiguous the members are to the reward structure, the more customers will rely on other aspects of the program (Bagchi & Li, 2011). Members are motivated to earn and burn rewards, and tiered programs allow for more opportunities to achieve a higher status. Dreze and Nunes (2008) found that the presence of two elite tiers (3 total) within a program is more appealing to consumers than a similar program with one or no elite tiers, even if they are not able to achieve elite status. These can be used to promote a feeling of exclusivity, which the travel and entertainment industries use most commonly, including programs built by Harrah's, Starwood Hotels, and Regent cruise lines.

Loyalty rewards

Determining which reward incentives are the most valuable to consumers is difficult because preferences vary based on consumer-related variables, including income, purchase volume, and socio-demographic profile. Therefore, there is not one ideal reward for a single program (Lara & Madariaga, 2007). Because of the factors that affect the extent to which members value rewards, it seems logical that only 25% of consumers think LP rewards meet their needs. If members understand the actual economic and time-saving value of a reward program relationship, they are more likely to continue pursuing the relationship, which is why focusing on the reward is one of the most important elements of a LP. Typically, the greater the incentive, the more money, effort, or obligation a member must provide (Daams, et al., 2008). Overall, LPs that seem attractive to consumers have economic, sociological, and psychological benefits (Zhang & Breugelmans, 2012).

There are many research studies based on the rewards offered in LPs. Studies have evaluated the type of rewards, cost of rewards, and how rewards relate to the brand hosting the LP. The results of the Omar, et al. (2010) study, along with the work done by Lara and Madariaga (2007) indicated that LP members who perceive program benefits as valuable are more likely to be engaged in the LP and are more likely to be satisfied with the program. In turn, satisfaction with the LP was shown to influence store loyalty, and these members are less likely to be price-sensitive. Therefore, retailers will likely see greater store loyalty when they implement a LP with high-value rewards. This can also be a competitive advantage for the retailer. When the LP's value does not increase future purchases, the customer will go elsewhere.

Program benefits are anything that a customer perceives value within as a result of being a member of the program. Loyalty reward research suggests that combinations of both hard and soft benefits are important to the program benefit mix. Hard benefits are rewards, and soft benefits are recognition (Dreze & Nunes, 2008). The rewards should depend on the goal of the program. For instance, short term buying behavior is influenced by tangible rewards, whereas relationships are built with intangible benefits and deferred incentives (Lara & Madariaga, 2007). If a firm offers special treatment rewards in their LP, their goal is likely to increase customer trust and confidence in the firm, and they result in the customer feeling cheerful and excited. If a company offers monetary rewards, the goal is likely to increase feelings of customer security and provide them with a utilitarian benefit that they value as useful. Furinto, Pawitra, and Balqiah (2009) cite two categories of rewards: monetary-based rewards and special treatment-based rewards. Monetary rewards clearly display economic benefits because being a member has a greater economic effect than not being a member. Liu and Yang (2009) have also found that brand-congruent rewards are more effective in terms of consumer involvement and promotional reactance than incongruent rewards. And, if members of a particular LP are price-conscious, cash is an effective reward offer, whereas if members are less price-conscious, they likely prefer product rewards.

One way in which retailers can keep LPs fresh and interesting is to change their mix of rewards. Research has found that a variety of rewards is a positive thing, along with the aspirational value of rewards (Liu & Yang, 2009). Customers also prefer immediate gratification and can sometimes become dissatisfied with delayed rewards, common in IBLP (Zhang & Breugelmans, 2012). Reward points, both collecting and redeeming, spur psychological benefits. "Point pleasure effect" happens when customers increase purchase behavior when they are closer to a reward threshold (Zhang & Breugelmans, 2012). Smith and Sparks (2009) found that the more effort it takes to redeem a reward, the more likely the member is to choose a luxury item, if they have the choice. Interestingly, Lara and Madariaga (2007) think rewards may even be more important to non-users than to members. Because substantial differences are present between the rewards the LP members versus non-members value, it could influence the choice to participate or not participate in the program.

Measuring effectiveness of loyalty programs

Omar and Musa (2008) conducted a study to look at how a LP impacted the purchase behavior of grocery store customers. They found that just over half of grocery store customers engaged in a LP, while in apparel retailing, just over 20% were enrolled in these programs. Within these groups of customers who were enrolled in LPs, half of the grocery store loyalists were influenced to spend more, and one fifth of apparel loyalists experienced this same effect. A separate source indicated that approximately 50% of LP members decided where to shop based on the LPs. Clearly, some case studies prove that LPs can have very impactful results. Because LPs are created by firms for different reasons, the measures of success each firm finds also vary. However, there are a few standardized measures that seem to be common key performance indicators among most LPs; these include purchase frequency, transaction size, share of consumer spend, overall store sales, and overall store traffic (Omar & Musa, 2008). Liu and Yang (2009) studied another measure of the effectiveness of LPs when using external factors, such as competing LPs, into consideration. This is why when considering the effectiveness of a LP, firms need to also consider the 'card portfolio' or other loyalty programs members are a part of, which may offer similar benefits. Furthermore, Liu and Yang (2009) also incorporate category expandability into their assessment of the effectiveness of loyalty programs, which some research suggests as a way to determine the practicality and advantage of implementing a LP.

Redemption rates are assumed to be a measure of success for a LP because they typically generate additional revenue and provide the retailer with additional consumer purchase knowledge, which is why program managers desire to find out why members don't redeem rewards (Smith & Sparks, 2009). Reasons for non-redemption are because rewards were not appealing, disinterest in the program, forgetfulness, and insufficient attainment of program currency. This again reiterates the importance of a specific merchandising strategy for rewards.

Additional measures of LP return on investment (ROI) were explored by Furinto, Pawitra, and Balqiah (2009): customer lifetime value and customer equity. Customer lifetime value (CLV) is the total customer spend with a particular company, less the cost of capital invested by the company. CLV can be used as a quantifiable measure in loyalty program analysis, and it is also a key performance indicator used by some investors because it has been linked to shareholder value. Farooqui and Rehmann (2010) tested the effectiveness of LPs based on the Net Promoter Score (NPS) method, proposed by F. F. Reichheld. NPS Score was published in the Harvard Business Review as the "the one number you need to grow" a retail business. This method works when comparing things, such as one retailer to another, or NPS scores of members versus non-members of a LP.

Due to the multiple ways used to measure the effectiveness of LPs, there are mixed opinions in the literature about the ROI of these programs. Because there is no standard ROI model used for LPs, there is room for researchers to explore the best way to test and measure the programs. Specifically for the firm studied here, ROI can be directly impacted because new members generate revenue, and the investment of this particular program is known. When a business provides a positive experience for customers, referrals may happen with or without a loyalty program. The objective of the firm for rewarding referrals was to ultimately gain incremental new memberships.

METHODOLOGY

There were two ways information for this study was collected. First, secondary information was provided by the company. This data provided the information on the demographics of the members, along with whether or not they participated in this rewards program. If they participated, information on how rewards were spent was also gathered. Secondly, a survey was distributed by the company to select members, and the results were studied. This survey provided information on how members perceived this rewards program.

The total population studied was 691,921 members of a health club who were active during the six-month period of January 1, 2013 through June 30, 2013. Data included a nine-digit member ID, age of the members, gender of the members, and the members' tenure. The data also indicated whether the member was eligible for rewards. If they were eligible for rewards, it was indicated if the members used rewards or did not use rewards. Members were split into groups based on this information. The groups included: 1) total population, 2) members who were eligible for rewards, 3) members who were eligible for and redeemed rewards. If rewards were redeemed, the product or service purchased and price were included in the data. Age, gender, and membership tenure were reported for each of the three groups. The objective of separating the members into the three groups described above was to identify points of comparison among the groups, so a better picture of active rewards program participants could be provided.

Because the unique, nine-digit ID number used for each member account was a random number assigned to each member, it did not provide identification of individual members. Also, over one million active member IDs exist in the company's database, making identification of purchasers nearly impossible. The request for this data was authorized by the firm, and was delivered by the company's information technology department. The file transfer occurred electronically and was not completed on-site. The data was stored in a password protected storage device and was only accessed through a device that conforms to NDSU IRB standards. The data will be permanently deleted from the storage device and computer in which it was analyzed after the final paper is submitted.

The firm also conducted a survey in order to determine how to improve their loyalty program and gauge the perceived value of their program. A link to the on-line survey was distributed to select members in an email. The sample was a purposive sample and was a subset of the total population. The reasons for this type of sample was because the company wanted to gather the opinions of newer members and because the company wanted to send the survey to a smaller group of members due to the high number of emails already being sent to members. The population to which the survey was distributed totaled 30,062 members who had joined within six months of the survey launch date and were also eligible for rewards at some point within the 6-month period. A copy of the survey questions is included in Appendix A. Answers to the questions in the survey specifically reference aspects of the program that were valuable to this study. Unfortunately, the firm did not request demographic data from the members completing the survey. Also, because members with a maximum of six months tenure were evaluated, it was not possible to cross reference survey responses with the secondary data gathered. Slightly more than 1,000 responses were received, which is a response rate of approximately 3%.

In order to build a merchandising strategy for the firm, historical purchase data was analyzed. The group of members who earned and used rewards was sub-divided into two groups: A) members who used rewards on services such as personal training or swimming lessons and B) members who used rewards on tangible products such as fitness apparel or accessories. The membership tenure, age, and gender of participants in each of the above groups were gathered. Along with finding patterns in how various demographic groups spent rewards, this information was used to identify shortfalls in specific item categories.

RESULTS

Reward program demographics

The first part of this study looked at the demographics of the total company and compared different reward participation groups through the use of secondary data gathered from the firm. The total population included in this data set was members active during the time period of January 1st, 2013 through June 30th, 2013 and totaled 691,921 members. Within this population, 47% were female, and 53% were male. Only 0.2 % of the total population did not choose to provide gender information. Within the various age groups, 27.5% were in the 35-44 age group and 24.1% were in the 45-54 age group. The 25-34 age group was the next largest in number at 22.4%. This was consistent with the business model and target market for this health club. Table 1 lists the breakout of gender and age group of the total population.

Table 1

Total Population

	Under Age 25	**Ages 25-34**	**Ages 35-44**	**Ages 45-54**	**Ages 55-64**	**Age 65+**	**Total**
Female	3.8%	10.4%	13.8%	11.7%	5.7%	1.8%	**47.2%**
Male	5.6%	12.0%	13.7%	12.4%	6.5%	2.5%	**52.6%**
Total	**9.4%**	**22.4%**	**27.5%**	**24.1%**	**12.3%**	**4.3%**	**100.0%**

Members who earned rewards

Members who referred a new member or multiple members to the health club in the six month time span of this study are shown in Table 2. The total count of approximately 62,000 members equals 9% of the total population at that time. The demographic makeup of members who were eligible for rewards was not consistent with the demographic makeup of the total population. For example, the total population was comprised of 12% more male members than female members. In comparison, there were 7% more female members than male members who earned rewards. In terms of age groups, it was clear that the younger age groups referred new members at a higher rate than the older age groups. For example, while members ages 55 and older made up 16.6% of the total population (see Table 1); these same age groups comprised only 8.5% of members that earned rewards (see Table 2). The age group with the highest disproportion was the age group of those ages 24 and younger, where there was a 9.9 percentage point difference between this group's portion of the total population and the same group's portion of those who earned rewards. This was followed by the age group of 45 to 54 year-olds, which made up only 16.9% of those who earned rewards but totaled 24.1% of the total population, a difference of seven percentage points.

Table 2

Members Who Earned Rewards

Demographics	Under Age 25	Ages 25-34	Ages 35-44	Ages 45-54	Ages 55-64	Ages 65+	**Total**
Female	8.1%	14.3%	15.0%	9.8%	3.7%	0.8%	**51.7%**
Male	11.1%	14.9%	11.0%	7.1%	3.1%	0.9%	**48.2%**
Total	**19.3%**	**29.2%**	**26.0%**	**16.9%**	**6.8%**	**1.7%**	**100.0%**

Those that earned rewards were then divided into two groups: those that earned but did not redeem rewards and those that earned and used rewards. Members who earned but did not use rewards within the timeframe of six months measured approximately 7% of the total population. In comparison, those that earned and used rewards in this time period made up 2% of the total population. Of those that earned rewards, 25% redeemed rewards within the 6-month period evaluated. These groups were compared with the total population, the total group of those who earned rewards, and the group that earned rewards and used rewards.

It is clear that females not only earn rewards at a higher rate than males, but they redeem rewards at an even higher rate. Females in this study made up 58.6% of the population who redeemed rewards (see Table 3), despite the fact that there were fewer female members than male in the total population. Overall, females had a 28% redemption rate, which was 33% higher than the 21% redemption rate of males. The age groups of 45 to 54, 55 to 64, and 65 and older were all fairly consistent in their reward redemption rates. Members who earned rewards in the 35 to 44 age group redeemed at a higher rate than average at 28%, however, this group also had 37% more females than males. Conversely, the group of age 24 and younger had 37% more males than females and redeemed rewards at a rate seven percentage points lower than average, with 18% redemption. Those included in the age group of 25-34 had a slightly higher than average redemption rate, at 28%.

Table 3

Members Who Earned and Used Rewards

Demographics	Under Age 25	Ages 25-34	Ages 35-44	Ages 45-54	Ages 55-64	Ages 65+	**Total**
Female	6.6%	18.2%	19.6%	9.7%	3.9%	0.7%	**58.6%**
Male	7.3%	15.1%	10.7%	5.3%	2.2%	0.8%	**41.3%**
Total	**13.9%**	**33.3%**	**30.3%**	**15.0%**	**6.1%**	**1.5%**	**100.0%**

Membership tenure and rewards program participation

Membership tenure is the length in which a member has consecutively paid membership dues. Although it is not a demographic indicator, it is an important factor to the firm because it allows them to better understand membership patterns. It is also not an indicator of club usage, and many members that have very low or no usage still pay membership dues. Of the total population studied, 38.7% had membership tenure of one to two years. The second largest group, membership tenure of over five years, comprised 24.0% of the membership population studied. Table 4 shows membership tenure by rewards participation group.

Overall, members who earned rewards were more highly saturated in the lower tenure groups, when compared to the entire population, and as tenure grew, the members who earned rewards grew smaller in comparison to the total population. Those that earned but did not spend rewards were the most concentrated in the earliest tenure groups, likely because these people terminated their membership prior to being able to use rewards. Eleven percent of members in their first six months of tenure earned rewards. For the group with seven to 11 months tenure, this number rose slightly to 13%. After one year of tenure, the percentage of those who earned rewards continued to drop, with 9% of those in the one to two year tenure group earning rewards, followed by 6% of those in the two to five year tenure group, and finally, 5% of those with membership tenure of five years.

Table 4

Membership Tenure by Participation Group

Participation Group	0-3 months	4-6 months	7-11 months	12-48 months	49-60 months	61 months	**Total**
Earned rewards	10.5%	13.5%	15.0%	40.9%	5.5%	14.6%	**9.0%**
Earned but did not use rewards	13.3%	16.2%	14.2%	36.3%	5.6%	14.5%	**6.8%**
Earned and used rewards	2.0%	5.5%	17.5%	55.1%	5.1%	14.9%	**2.2%**
Did not earn rewards	8.3%	10.4%	10.0%	38.5%	7.9%	24.9%	**91.0%**
Total	**8.5%**	**10.6%**	**10.4%**	**38.7%**	**7.7%**	**24.0%**	**100.0%**

The data evaluated during the study aided the researcher in determining which tenure groups were the most likely to redeem the rewards they earned. In this case, the general trend points toward higher redemption rates with longer tenure. Redemption is especially low for tenure less than six months, with redemption rates 70% lower than the average redemption rate of 25%. Redemption rates for the other tenure groups hovered around the average, with those with membership tenure of one to two years redeeming at a rate eight percentage points higher than average. See Table 5 for redemption rate by membership tenure.

Table 5

Redemption Rate by Membership Tenure

0-3 months	**4-6 months**	**7-11 months**	**12-48 months**	**49-60 months**	**61 months**
4.7%	9.9%	28.6%	33.0%	22.8%	25.0%

Purchase analysis

Analyzing purchasing behavior by demographic group is essential when a firm builds their merchandising strategy for a rewards program because the rewards themselves must be valuable to members to motivate participation in the program. In the rewards store studied, members could purchase fitness-related products or fitness services, and the data showed notable differences in the demographics of purchasers within the two categories. A product is a tangible item, and in this rewards store, there was an assortment of approximately 50 unique items at any given point in time. Examples of items included mid to high-end fitness apparel with the company logo, gym bags, and fitness accessories such as yoga mats, water bottles, and tennis racquets. Services are intangible purchases, and the members must take action to schedule an appointment to redeem their purchased service. The price or point value of the services and products was equal to market value.

A total of 39,323 items were purchased by 15,227 members within the time period of January 1st, 2013 through June 30th, 2013. Members could purchase both a service and a product within their transaction (if their rewards balance allowed), so some members were counted in both the product and service data sets. The objective of gathering this data was to create and compare profiles of members who made service purchases and those that made product purchases, followed by recommendations to enhance the merchandising strategy of this rewards program. Of the 7,742 members who purchased a service within the evaluated time period, 1,663 or 21% of the sample had terminated their membership when the data was collected. The average tenure of those who cancelled was 15 months compared with the average tenure of 26 months for those who did not cancel. Of the 9,385 members who purchased a product within the evaluated time period, 2,723 had terminated their membership by the time the data was collected. The average tenure of those who cancelled was 16 months compared with the average tenure of 32 months for those who did not cancel. The most important finding here is that purchasing a service makes a member 27% less likely to cancel their membership in the 6 months following the service purchase than if they had purchased a product. Those that did cancel stayed about one month longer when they purchased a product, even though this group left the health club at a higher rate.

Table 6

Product Purchases

Demographics	Ages <25	Ages 25-34	Ages 35-44	Ages 45-54	Ages 55-64	Ages 65+	**Total**
Female	8.1%	17.3%	13.1%	8.6%	3.4%	0.5%	**50.9%**
Male	10.7%	19.2%	10.2%	5.6%	2.5%	0.8%	**49.0%**
Total	**18.8%**	**36.5%**	**23.3%**	**14.3%**	**5.9%**	**1.3%**	**100.0%**

Table 7

Service Purchases

Demographics	Ages <25	Ages 25-34	Ages 35-44	Ages 45-54	Ages 55-64	Ages 65+	**Total**
Female	5.1%	20.5%	27.8%	11.1%	4.7%	1.0%	**70.3%**
Male	2.2%	9.4%	11.1%	4.5%	1.7%	0.7%	**29.7%**
Total	**7.3%**	**29.9%**	**39.0%**	**15.7%**	**6.4%**	**1.8%**	**100.0%**

Price point analysis

Price point can drive consumer behavior, depending on the consumer's goals. Members can feel as if they are getting more for their rewards if they purchase multiple items, rather than just one single item. Some members split their purchase into a combination of products and services. Although products and services were available to members at a range of price points, no relationship was found between price point and purchase behavior. Product purchases were by far the highest in the $41 to $60 price range. It is surprising that this purchase frequency is much higher than the $21 to $40 price point because the assortment is similar. A suggestion for the company would be to package lower price point products together in order to reach the higher price point and suggest to the member what items may work well together.

The purchased price points of services varied more than products and seemed to be more highly dependent on the service itself rather than the price point. For instance, swimming lessons and personal training sessions were overwhelmingly the most popular items for members to pay for with cash in the club, separate from the rewards store. But, they were also the most popular items in the rewards store. Swimming lessons are primarily within the $21 to $40 price range, and personal training sessions are within the $61 to $80 price point. It would be important for the firm to avoid over-pricing items to a point where members would not have enough rewards to redeem their favorite items, so it is more of a matter of price control rather than choosing assortments based on price point in the service section.

Table 8

Product Purchases by Price

Average price point: $45.69			
Price Point	**Purchases**	**Unique Items**	**Average Purchase per Item**
<=$20	4968	9	552
$21-40	5930	26	228
$41-60	10,063	24	419
$61-80	1250	9	139
$81-100	2561	9	284
$101+	190	1	190

Table 9

Service Purchases by Price

Average price point: $49.23			
Price Point	**Purchases**	**Unique Items**	**Average Purchase per Item**
<=$20	4112	13	316
$21-40	4211	30	140
$41-60	765	14	55
$61-80	3875	13	298
$81-100	341	10	34
$101+	1065	2	533

Rewards program survey data

The second part of this project included a survey distributed by the firm to gather insights on how members perceive rewards and how the program can be improved. Because this survey was distributed by the firm to members who were eligible for rewards within six months of the survey, the firm expected members' feelings toward the program to be relevant and recent. In the actual survey, the firm replaced the word "rewards" with the name of their rewards program. Due to confidentiality, this word was changed in the tables below. Select questions from the ten-question survey were omitted from this analysis because they were not relevant to the study. However, the firm had interest in the results of these questions. The total response rate was 1,153, or a 3% response rate.

This on-line survey was distributed to members who were believed to be eligible for rewards at some point in their membership. The expectation was that a majority of the responses would answer "yes" to the question "Have you ever received 'rewards?''. Eighty-seven percent of the responses did answer yes to this question. According to the firm, reasons why members would have answered "no," despite the fact that they were eligible were due to misinformation or forgetfulness. It is significant that most of the respondents received rewards because the follow-up questions are based on how the respondents used the rewards or why they did not use rewards. In follow up questions, respondents weren't required to answer every question.

Respondents who answered that they had received rewards were asked a follow up question on whether or not they spent their rewards. This particular company uses redemption rate as a performance measure of their rewards program, which is why it is important to uncover and evaluate reasons why rewards were not used or are not valued by member. According to the answers recorded in Table 10, reward expiration was the primary reason why members did not use rewards, answered by 21.5% of members. Eleven percent of members did not find value in rewards, and 9.1% of members didn't know what the rewards were. Seven percent of members did not spend rewards because they didn't find a product or service that they desired. This is referred to in Table 10 as “selection.” The same percentage of members did not spend rewards because of a club error, which would include issues such as receiving the incorrect information from the health club or not being able to schedule a service they desired. Fewer members (3.8%) had usability issues with the redemption vehicle, which is a website where members could shop products and services available for purchase with rewards. Only five members were not interested in the rewards.

Table 10

Survey Question: Why Did You Not Use Your Rewards?

I did not know what "rewards" are	Was not interested in finding out what "rewards" were	Did not Find Value in "rewards	Club Error	Expired	Selection	Usability	Total
9.1%	1.3%	11.4%	7.3%	21.5%	6.6%	3.8%	100.0%

All respondents answered the question rating how valuable this firm’s rewards were to them. The ratings were somewhat favorable for the firm, with 44.6% of members rating the value of rewards at four or five, on a scale of one to five, with one being extremely low and five being extremely high. There is room for improvement, especially with those members who answered neutrally, or at a rating of three. Slightly over a quarter (28.2%) of respondents did not find much value in rewards, scoring the value rating at a one or two.

Table 11

Survey Question: How Valuable Are Rewards to You?

How valuable are "rewards" to you on a scale from 1 to 5 (1 being Extremely Low and 5 being Extremely High):					
1	**2**	**3**	**4**	**5**	**Total**
15.8%	12.4%	19.3%	19.8%	24.8%	100.0%

Comparing the question in Table 11 to the question in Table 12 is important because it could be an indicator of how this rewards program rated in consumer's minds in comparison to how they feel about rewards programs in general. The question in Table 12 referred to rewards programs in general and not this specific firm's program, whereas the question in Table 11 referred to the rewards program belonging to the firm studied. A higher percentage of members (53.6%) rated rewards programs in general as high or extremely high, compared to members who rated this specific rewards program as high or extremely high in value (44.6%). This could indicate that members perceive other rewards programs as more valuable or appealing than this firm's rewards program.

Table 12

Survey Question: In General, How Appealing Are Rewards Programs to You?

In general, how appealing are rewards programs to you on a scale from 1 to 5 (1 being Extremely Low and 5 being Extremely High):					
1	**2**	**3**	**4**	**5**	**Total**
12.3%	9.2%	24.9%	23.0%	30.6%	100%

One way to identify points in the reward process where members experience difficulty is to compare it with other rewards programs the population perceives as valuable. Survey respondents identified rewards programs that they thought were useful. Starbucks topped the list, followed by airline and credit card companies, Best Buy, and Kohl's.

DISCUSSION

The findings of this study could be used by the health club in a variety of ways. The company could develop more targeted marketing efforts based on information provided by the top reward user groups or by those who are under using the program. Communicating with different types of members and user groups is an important aspect of truly connecting with members or customers. This connection can lead to loyalty, which is the objective of most rewards programs.

Demographic overview of reward program participation

Age group and gender were the primary demographics analyzed in this study. The age group distribution of members who earn rewards was not consistent with the age group distribution of the total population. Due to the nature of this rewards program being online, it is not surprising that the younger age groups had higher participation rates than the older age groups because they may be more familiar with the on-line technology used for this rewards program. Members ages 45 to 54 had especially low participation rates, meaning that they did not take the action to earn rewards. This is unfortunate because many of the fitness services which can be purchased with rewards, such as nutrition coaching or group training, are typically very appealing to this age group. The firm may need to simplify the process of earning rewards or change their marketing materials to better target this age group. Health clubs often use young adult models in their marketing materials, which can distance some members or prospective members, specifically when the target market or market share opportunity is within older age groups.

Also inconsistent with the total population distribution was the percentage of women versus men who earn rewards. Because more women are participating than men, the company may want to take a more active marketing approach toward men's items, such as men's apparel or men's nutritional supplements. One reason why women participate at a higher rate than men could be because group fitness is a more common practice among women than men. This is evident when reviewing enrollment in group fitness classes, where the great majority are female. Because men commonly do not work out together, they may be less likely to refer friends, and therefore do not earn or spend rewards gained from referrals as frequently as women.

Reward program participation and membership tenure

Knowing where members are in their membership lifecycle and what type of behaviors occur at each stage in the lifecycle are key to communicating relevant information to members at any given time. In the beginning of a membership, the enthusiasm of a member is typically highest, and it is the first time these new members have communicated to their networks of potential referrals. Because it is the first time these members reach out to their network, it is suspected that these members are most likely to refer other new members during this time. As members continue in their membership for a longer period of time, most of their network that would have also joined the health club has already done so. The firm should be marketing referrals heavily within the first year and communicate different revenue-generating initiatives to members who have over two years' tenure. Interestingly, despite earning rewards in earlier membership tenure, members with six months of tenure or less redeem at lower than average rates. This could be because they are less familiar with the rewards program and how it works.

Purchase behavior

Data from Tables 6 and 7 indicate that product purchases are preferred over services by most age groups, with the exception of members 35 to 44 and members 65 and older. Members ages 35 to 44 used rewards toward services 38% more often than products, while members age 65 and older chose services at a rate 15% more often than products. The opposite purchasing pattern occurred for members under age 35, who purchased products at a rate 80% more often than services. Members in these age groups may feel they do not need fitness services in order to reach their fitness goals or are generally healthier and therefore choose products. Another possibility could be that members younger than age 35 find products more appealing than service, perhaps due to the instant gratification received from the new product.

Interestingly, females chose services approximately 14% more often than products, but if this is analyzed further by age group, the females ages 35 and above chose services at a higher rate, while females ages 34 and younger chose products at a higher rate. The males chose products over services more often in each age group, although the gap becomes smaller after age 35. Reasons why these patterns occur must be explored individually, but a few speculations based on other data the company has gathered could be made. One idea is that a higher percentage of women are interested in weight loss and nutrition when compared with their male counterparts, therefore they may be more likely to choose a service which would help them with their goal. As mentioned previously, women also enjoy working out in groups, and men are more individualistic in their workouts. Thus, men may be less likely to work with a personal trainer or other fitness professional, and fitness services overall are less attractive to men.

The firm could improve the assortment that members can spend rewards on. Below are some ways the firm can improve their merchandising strategy based on the findings of this study. In order increase participation rates and redemption rates for some of the groups who were comparatively low in these areas, the firm could:

1. Add a greater presence of equipment and apparel targeted toward ages 55+ in order to increase rewards program engagement by these groups.
2. Highlight items for the 35 and younger male population that may drive them toward a service purchase.
3. All items must be fitness-related in order to inspire increased engagement in healthy living, including involvement in the health club.

In a previous study done by the firm, observation was completed in the club, along with interviewing fitness professionals, including a certified personal trainer who commonly partners with members ages 55 and over as an effort to select appropriate items for this group. Older populations need fitness items and activities that are not stressful on the body, such as those that focus on flexibility and low-impact exercise (Fitness, 2013). Also, the percentage of people ages 55 and over who are physically active and are spending money in the physical fitness sector has continued to rise since the 1980's, so it is prudent to develop a merchandising plan to accommodate this growth (Carpenter, 1999). Daniel Hove, Certified Personal Trainer for the firm studied, recommended a few low-cost items for clients in this age group, such as the foam roller and yoga mat, which both can be used at home as well as in the health club. Hove also recommended fitness tracking devices that are easy to use, such as pedometers with sleep tracking, where users can measure their activity during the day along with their sleeping patterns to improve overall health (Hove, 2013). Water exercise has been a popular choice among older generations due to lessened pressure on joints in the water, but now this segment is spreading toward younger age groups as well (Anderson, 2005). Because swimming and water exercise classes are still largely recommended for those with joint issues, including a swim kit with items such as kickboards, fins, and goggles in the merchandising strategy could be helpful.

In the past, the rewards store did not have a problem attracting men to products, but services are less likely to appeal to this gender group, specifically under age 35. For that reason, there are no suggestions to change the product assortment. Personal Trainer, Daniel Hove suggested contest-based services for this group because the competition would appeal to these members. Including club events such as weight lifting competitions, cycle or running races, along with triathlons are services that would appeal to this group (Hove, 2013).

Perceived value of the rewards program

Beyond evaluating demographic data and uncovering membership lifecycle patterns, asking members about themselves provides valuable insight into reward program behavior. The objective of our survey was to gather preliminary data on the perceived value of one firm's rewards program, from members who were recently eligible for rewards. It would be critical for the firm to further study the results received in order to find the "why" behind the actions. Because the members generally valued this rewards program less than their other rewards programs, the firm should evaluate other, highly respected programs and possibly use some of their successful strategies. Simply asking members to communicate why they did not redeem rewards is another way to uncover shortfalls in the rewards program. In this particular survey, there was a wide range of reasons why rewards were not redeemed. Many of the answers to this question are items the firm can easily identify and create action plans to fix, such as expiration, usability, selection, and club error. Members who did not redeem rewards because they did not find value in rewards should be explored on a deeper level in order to find out why the members did not find value in rewards.

LIMITATIONS AND OPPORTUNITIES FOR FURTHER RESEARCH

This study reviewed data for a six-month time period. Transactional data from the time period chosen may be seasonal, and purchase behavior may change from season to season. Reviewing data for a one-year timeframe or multiple timeframes would provide a more holistic view of reward program behavior. This rewards program distributes rewards based on referrals, an action that is not typically rewarded in most popular loyalty programs. However, many companies do reward consumers for referrals, outside of their loyalty program. Due to this, the comparison between the program evaluated and popular LPs may require slightly altered recommendations.

The survey conducted was only offered to members with membership tenure of a six months maximum, and demographic data was not included in the survey. Cross-referencing the survey data with demographic data would have been helpful to support or deny inferences made based on the demographic data and participation. In future studies, the firm would be wise to continue to compare the same variables over the time of one year or more in order to monitor the demographics more closely. This would be especially helpful after taking suggested actions toward specific demographic groups and would be an appropriate way to measure success of various marketing tactics. Gathering additional information from members through focus groups or user experience studies would also be helpful. This would allow the firm to learn why some members do not value the rewards program and provide suggestions for improving program participation and reward redemption.

CONCLUSION

The rewards program in this study had a fairly simple construct: members earn rewards by referring new members. This concept is easily understood by members, which is a benefit to any program (Bagchi & Li, 2011). Because the reward currency exists, along with an online platform where members can redeem rewards, this program could easily expand to include rewarding other loyalty-based actions. This study identifies the demographic portions of the membership base most actively participating in the program, which would be valuable information when expanding the program. Based on previous academic research, the firm could begin by adding tiers into the rewards program, which proved by Dreze and Nunes (2008) to appeal to a more members. Although these suggestions are straightforward, executing the marketing and operations behind each initiative requires a large amount of effort and planning on behalf of the firm. Measuring the ROI is essential to determining the success of the program, but because loyalty programs must be measured over months or even years, the resources required for small program tests are still noteworthy.

The results of this study also provide suggestions to improve the program without expanding on the current construct. Because the firm had never explored the aspects of the program included in this study, the opportunity for the company to improve is significant and easily measurable by using the same metrics studied in this report. This program is unique because eligible participants are already engaged in a subscription-based membership, which in itself infers loyalty to the company. However, because this company has already formed an initial relationship with its members, nurturing this relationship by rewarding continued loyalty could push this company's rewards program to be an identifiable competitive advantage in the low barrier-to-entry health club industry. The results of this study provide valuable insight into loyalty program rewards and referral programs.

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APPENDIX

Survey Questions

1. Have you ever received rewards?
2. How did you receive rewards?
3. Was it clear what you could use your rewards for?
4. What did you purchase with your rewards?
5. Why did you NOT use your rewards?
6. What, if anything, would you like to see added to the selections?
7. Do you know how you can earn rewards?
8. Please rate the following on a scale from 1 to 5 (1 being Extremely Low and 5 being Extremely High):
    a. In general, how appealing are rewards programs to you?
    b. How valuable are rewards to you?
9. If you think of a great rewards program, what company comes to mind? Why?
10. If you could change one thing to improve rewards, what would it be?