

## Loyalty Schemes in food retail

## Loyalty schemes – our views (i)

### Our view on loyalty schemes

Loyalty schemes in food retail are a controversial issue: their costs and potential benefits need to be carefully assessed

<p>Loyalty schemes cannot substitute a good value proposal</p>	<ul style="list-style-type: none"> <li>▪ Consumer's <b>loyalty has to be earned and cannot be bought by granting a few points</b> on a card.</li> <li>▪ <b>Retailers earn loyalty fundamentally through the excellence of their value proposition:</b> assortment, price, quality and service.</li> </ul>
<p>Main goal of the loyalty card is to gather information</p>	<ul style="list-style-type: none"> <li>▪ The primary role of a <b>loyalty scheme is to gather information about customer's behavior and preferences.</b></li> <li>▪ <b>Reward systems are necessary to encourage the use of the card</b> and ensure a <b>high penetration on total sales.</b></li> </ul>
<p>The use of the information is the key</p>	<ul style="list-style-type: none"> <li>▪ The ultimate goal of a loyalty scheme is to <b>extract value from the customer's information which can be used in a variety of actions:</b> <ul style="list-style-type: none"> <li>▪ <b>Direct marketing</b> to differentiated customer's segments.</li> <li>▪ <b>Tailor-made promotions</b>, cross-selling campaigns.</li> <li>▪ Life-cycle management: <b>desertion prevention and recovery.</b></li> <li>▪ <b>Substitution of traditional marketing</b> and advertising.</li> <li>▪ Collaboration and <b>information-sharing with manufacturers</b> and other third parties.</li> </ul> </li> </ul>
<p>Cost-benefit trade-off: the key issue</p>	<ul style="list-style-type: none"> <li>▪ While <b>loyalty systems are costly</b> (rewards, IT systems, CRM departments, communication with customers, etc.), the <b>benefits are difficult to calculate</b>, especially when compared to the 'traditional' marketing and promotional tools that are more straightforward, measurable and usually funded by suppliers.</li> </ul>

# Loyalty schemes – our views (ii)

## Our view on loyalty schemes in food retail

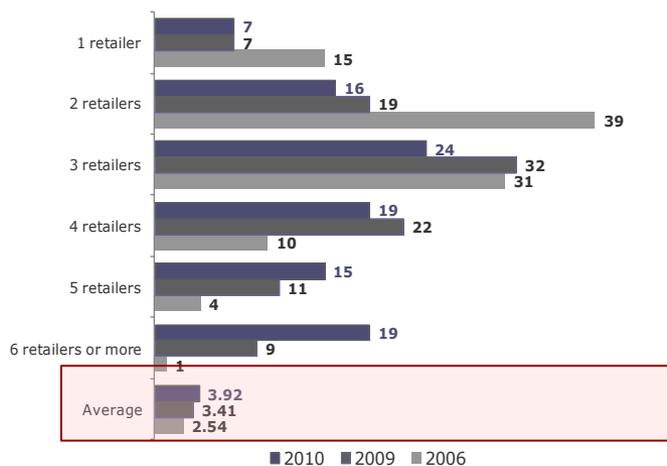
Food retail segment presents some characteristics which make difficult and condition the adoption of successful loyalty systems

Loyalty is low in the food retail market

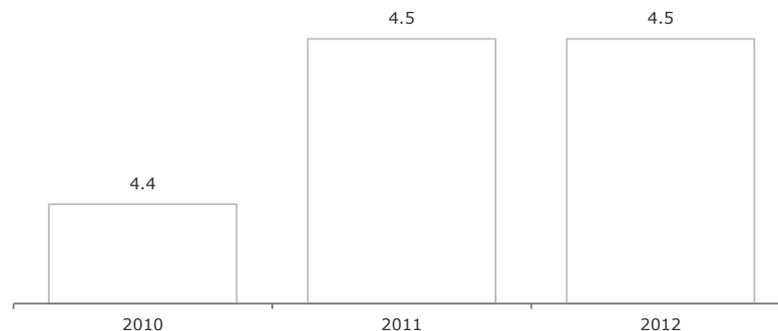
- The **food retail market is a sector with an overall very low loyalty** due to:
  - High competitiveness
  - 'Commoditization' of a good part of the value proposals
  - Proximity as the main reason for shopping
  - Increasing price sensitiveness of customers
  - Limited differentiation drivers in the sector

## The examples of Slovenia and Spain

Number of food retailers visited - Slovenia



Number of food retailers visited - Spain



## Loyalty schemes – our views (iii)

<b>Commoditization of the loyalty programs</b>	<ul style="list-style-type: none"> <li>When most players adopt loyalty programs, <b>the impact and the differentiation value of these systems considerably diminish</b> (it is not unusual that a good number of customers have cards from several retailers).</li> </ul>
<b>Entry barrier for new customers</b>	<ul style="list-style-type: none"> <li><b>'Aggressive' loyalty systems</b> (with too much emphasis in rewarding loyal customers and penalizing occasional buyers) <b>discourage new clients.</b></li> <li>Since the loyalty in food retail is 'weak', <b>penalizing occasional buyers can undermine the future customer base of the Company.</b></li> </ul>
<b>Low potential rewards</b>	<ul style="list-style-type: none"> <li>Given the <b>low margins in food retail, the potential rewards for customers</b> (as a percentage of their purchases) are <b>mandatorily low.</b></li> </ul>
<b>Costs (...and benefits?)</b>	<ul style="list-style-type: none"> <li><b>Loyalty systems have high operational costs</b> (especially those <b>based on points</b> accumulation and redemption and those using direct mailings for communication), while the <b>benefits compared to traditional promotional systems are unclear</b> and not <b>easy to measure.</b></li> </ul>
<b>The KEY: information</b>	<ul style="list-style-type: none"> <li><b>Most retailers fail to find a real use for the information</b> obtained:             <ul style="list-style-type: none"> <li>The complexity of customer's behavior is a barrier to achieve <b>practical conclusions to be effectively and successfully implemented.</b></li> <li><b>An in-depth customer's segmentation is radically opposed to the standardization</b> of systems and operations that is the base of the productivity in simple and industrial retail formats.</li> <li><b>The information sharing with suppliers</b> is limited (privacy, confidentiality, negotiation tactics, etc).</li> </ul> </li> </ul>
<ul style="list-style-type: none"> <li>Loyalty systems can be a <b>good promotional tool and source of information but not the pillar of the value proposal</b> of a food retailer.</li> <li><b>Simple, direct and almost zero cost systems can work and provide useful information about consumers. The rest only adds unnecessary complications and do not increase loyalty.</b></li> </ul>	

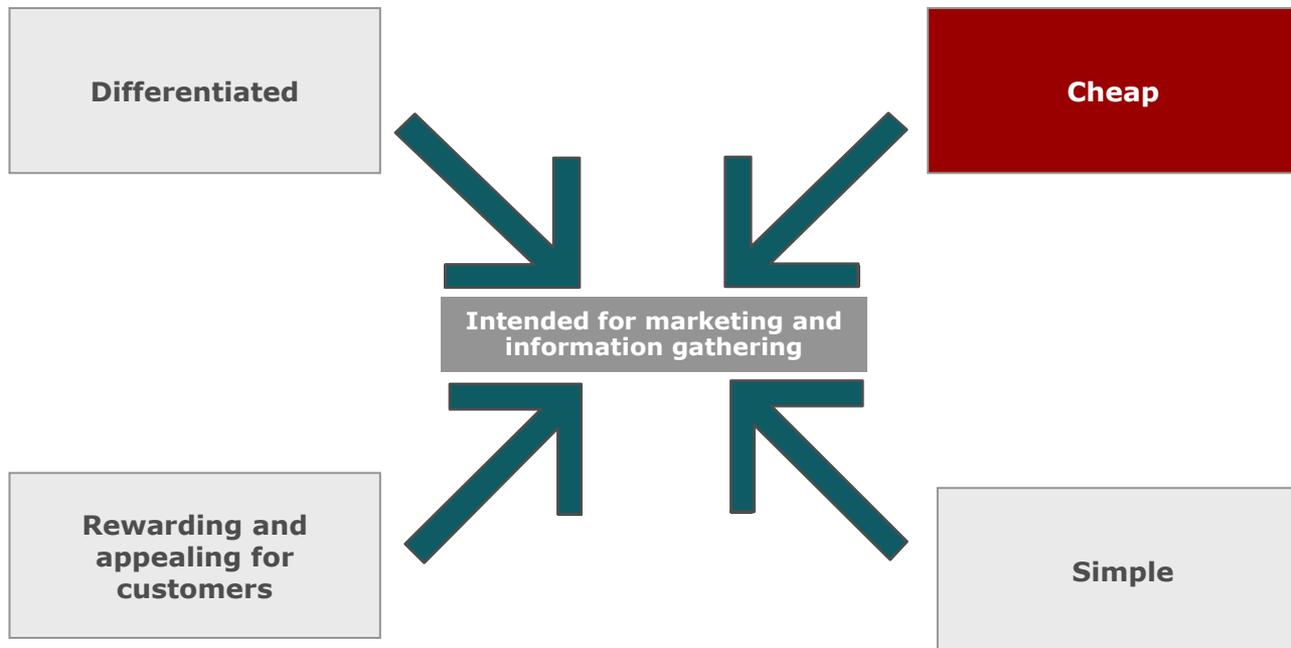
## Case study – current loyalty systems in Russia

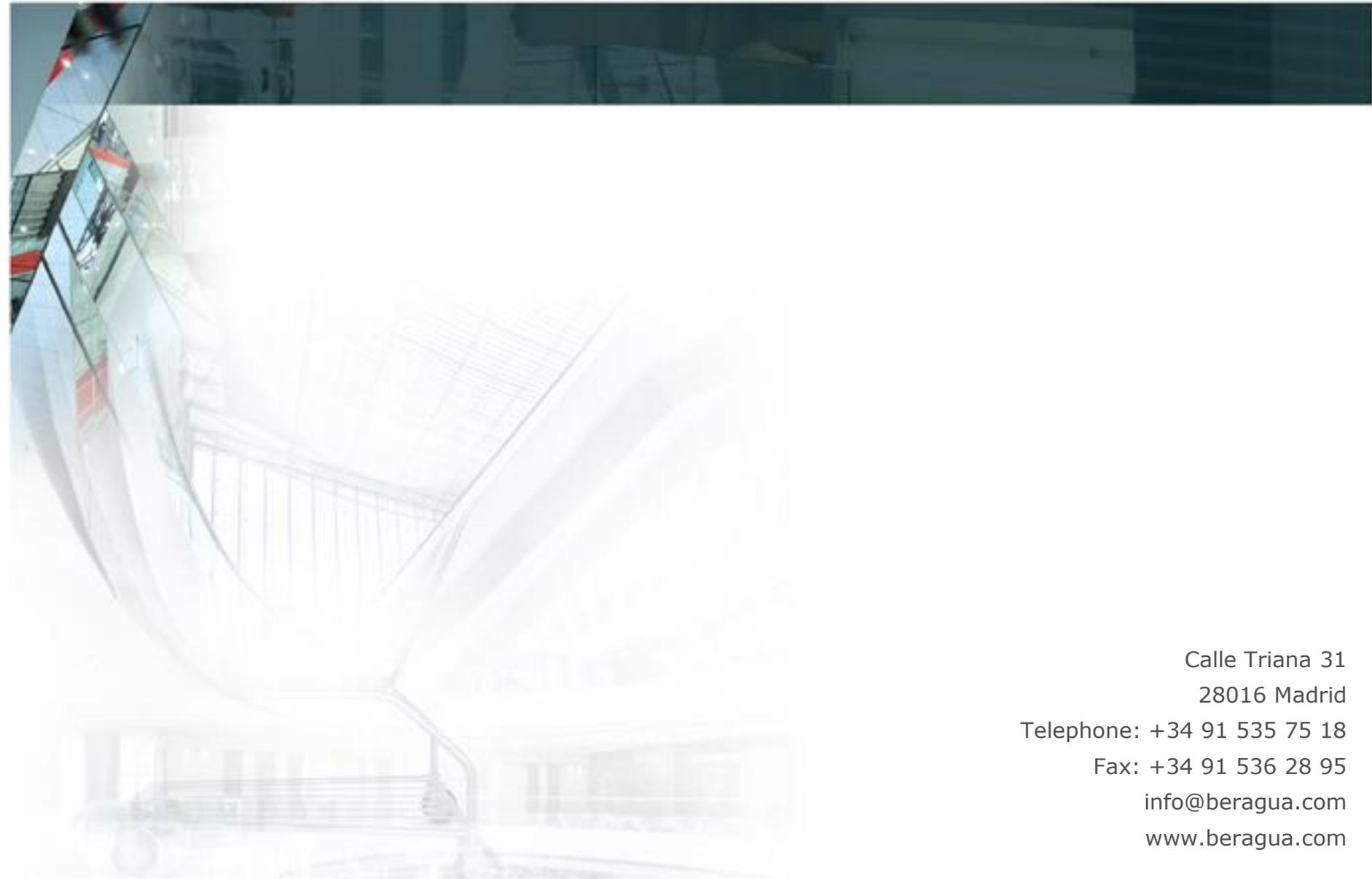
		<ul style="list-style-type: none"> <li>▪ <b>Points: 1 point for each RUR10.</b> Special promotions to receive more points and promo catalogue every 2 weeks. <b>Redemption</b> at Perekrestok (<b>10 points=1RUB</b>) or with partners. Credit (or debit) bank card with loyalty program. <b>COST: RUR49.</b></li> </ul>	<p><b>1% of upfront investment + expensive operative</b></p>
		<ul style="list-style-type: none"> <li>▪ <b>Points: 1 point for every RUB10 spent.</b> Ticket RUB2,000- RUB5,000 - 5 points for every RUB10. Ticket more than 5,000 - 10 points for every RUB10. You can use Perekrestok program in both Perekrestok and Perekrestok Green. <b>10 points=1RUB</b></li> </ul>	<p><b>+1% of upfront investment + expensive operative</b></p>
		<ul style="list-style-type: none"> <li>▪ <b>Discount: 10% discount on c.300 SKUs.</b> COST RUR40. Pyaterochka cancelled its loyalty cards in 2008. In 2012 started again just in North-West Region. Company plans to introduce it in all Pyaterochka stores</li> </ul>	<p><b>Simple and direct discounts</b></p>
		<ul style="list-style-type: none"> <li>▪ <b>Discount: discounts on certain items depending on the amount purchased:</b> &lt;RUR30,000 - 5% and up to 10% buying more than RUR130,000. Need to buy RUR5,000 to get the card.</li> </ul>	<p><b>Expensive system</b></p>
		<ul style="list-style-type: none"> <li>▪ <b>Discount: discount+gift lottery, promo catalogue (discount up to 50%, 300 SKUs every 2 weeks).</b> Some ready made products with 20% discount during the week. Cost: RUR55.</li> </ul>	<p><b>Direct discounts</b></p>
		<ul style="list-style-type: none"> <li>▪ <b>Discount: weekly promo actions, catalogue with discount up to 30%, seasonal offers with discount up to 70%. Special groups (pensioners, large families) have an additional discount 3%-8% on around 60 basic SKUs.</b> COST: RUR200.</li> </ul>	<p><b>Direct discounts. High entry price</b></p>

- **Russian peculiarity: most retailers charge for their loyalty cards** (something totally unusual in other countries).
- **In general low differentiated programs (points or discounts) with low personalization and expensive** (especially those based on points and the system of Advuka).

# Loyalty schemes – requisites of a successful system

We believe a potential loyalty program needs to be based on the following premises





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