



State of the LOYALTY INDUSTRY™

powered by Loyalty 360

October 05, 2009

How Loyalty in Eastern Europe Compares to the US

By Sarah Phelps
Principal, First Annapolis

First Annapolis conducted a survey of points-based loyalty programs in the United Kingdom, France and Germany in cooperation with its European office in Amsterdam. The study was focused on programs sponsored by financial institutions, travel companies and retailers with the objective of identifying differences in program benefits and value propositions compared to what is available to consumers in the US. Three key findings emerged: first, value propositions are tied to the same fundamentals; second, the biggest differences can be explained, at least in part, by interchange levels and scale economies; third, incentive marketing is still alive on both sides of the pond.



Fundamental Ties

One major difference between the US and three European countries reviewed is that proprietary financial institution rewards programs, that is stand-alone or single-sponsor programs associated with banks like WorldPoints™ or Membership Rewards™ in the US are far less prevalent.¹ In fact, we only observed proprietary bank programs in the UK and in these cases, cash-back is far more common than points-based.

Programs offered in partnership with a travel or retail partner, however, are as common as they are in the US with nearly all banks co-sponsoring programs in both the retail and travel categories. Coalition programs; such as Nectar or Airmiles, are far more pervasive in Europe than in the US.

¹ **Note that Central and Eastern Europe as well as certain markets in Southern Europe (for example markets such as Greece and Turkey), the nature of loyalty and supporting card behaviors and economics are quite different than in Western & Northern Europe. In some of these markets, proprietary loyalty programs are highly prevalent; even more so than in the U.S.*

Two central drivers of these differences are the sharp contrast in the utilization of credit and debit cards by European consumers and the associated acceptance revenues and costs. First, unlike the US, Europeans are far more likely to use debit over credit cards. In markets like Germany and The Netherlands, debit cards account for 90% of all card volumes. Debit cards provide lower interchange revenue and less potential for other sources of revenue.

This difference in transaction economics explains, to some extent, why single-sponsored programs are uncommon in Europe. Programs that leverage partner assets to provide customer incentives, however, are more feasible. Based on our research, the differences in interchange levels between the US and Europe and within the European countries surveyed, are roughly proportionate to the variance in customer value propositions.

Coalition programs that pool the interests and assets of a network of merchants, travel companies and other sponsors, are able to offer consumers a richer value propositions in this context. In Germany and the UK for example, value propositions offered by coalitions are nearly twice as robust as bank-sponsored programs. Surprisingly, a high level review of the value of bank sponsored programs in the three countries surveyed indicated that, as a proportion of transaction revenue (e.g., interchange), value to the consumer is roughly proportionate to US programs at a little less than half, on average.

Scale Economies

Another potential driver of the differences is the simple economies of scale that exist in the US. Scale economies have the potential to impact the administrative costs of a rewards program in addition to the cost of the underlying value proposition. Consider the impact of rewards program maintenance, such as a website with robust redemption options, and the potential savings generated by incorporation of merchandise along with travel and gift. Scale programs have far more potential to benefit from the infrastructure across a broader customer base and the inclusion of low cost alternatives in the range of redemption options.

Because the size of the portfolios of the each of the three leading US card issuers in terms of cardholders is roughly equivalent to the entire population of the three countries surveyed. As such, any one bank would essentially have to issue cards to the entire population within that geography to achieve the scale that these US financial institutions have and the markets within these regions a quite fragmented.

Several of the larger banks in Europe have a presence in multiple geographies and, as such, attempt to leverage scale in this fashion. Coordination within pan-European multi-national banks is however, early stage, for the most part. Moreover, regulation, and at times culture, each have the potential to act as natural barriers to centralizing and standardizing program design and operations across Europe.

The addition of a co-brand partner tends to simplify operations for the bank. For starters, the redemption experience, including the program website and processing are all handled by the partner and, in many cases, also leverages the partner's platform and servicing infrastructure. This is all in addition to the ways in which the partner can subsidize redemption in the spirit of driving enrollees back to their doorstep to bolster the brand.

Coalition

So, given certain fundamental economic disadvantages relative to the U.S. market, what are the ways in which loyalty stays alive and well in Europe? One way is by pooling interests and costs via coalitions. We define coalition as a program in which multiple sponsors contribute to the customer value proposition on both the earn and the burn side. Each of the three countries has several versions of coalitions, some of which boast a customer base that closely replicates the total population within that country, a wide range of merchant partners across industry verticals, and offer program members the option of applying for a credit card to accelerate earnings. AirMiles in the UK, for example, can be tied to an American Express card which enables cardholders to earn miles for purchases outside of the coalition of merchants.

The prevalence of coalitions in Europe is in sharp contrast to the US. While coalition programs exist in the U.S., they tend to be smaller in scale and tied to alternative revenue streams. UPromise, for example, is about as close as we come to coalition however, the business of managing the associated 529 savings account balances is as much a part of that business as the rewards program. Similarly, Rewards Network employs a discount model with the restaurants participating in the iDine network. Both programs have been successful in attracting both members and sponsors with the underlying concept of coalition, but their success has been equally dependant upon the associated service.

Merchant-funded networks, a close cousin of coalition, have rapidly spread throughout US loyalty program in all three sizeable loyalty verticals: financial institution, airline and hotel. While many of these programs offer discounts to program members, accelerated earn structures are also common. The key difference in these programs relative to European coalition is that extent to which they embrace the coalition's unique brand in terms of signage at the point of sale.

Headlines have abounded over the course of the economic crisis relative to the dilution of customer value propositions as financial institutions go through a series of belt tightenings and as consumers shift away from credit and into debit card products. While the US programs will continue to have the advantage of scale, but participation in coalition to leverage partners for program contributions will become increasingly attractive to program sponsors.