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How Effective Are Loyalty Reward Programs in Driving Share of Wallet?

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This study, set in a credit card context, examines the impact of loyalty programs on share of wallet and explores the moderating role of attitudinal loyalty on this relationship. The authors are particularly interested in two characteristics of reward programs: their perceived attractiveness and perceived switching costs between loyalty programs. Their findings suggest that perceived switching costs are highly effective in driving share of wallet at low rather than high levels of attitudinal loyalty, and only when combined with an attractive reward program. The attractiveness of a reward program, on the other hand, has a positive impact on share of wallet regardless of the level of psychological attachment to the company. These findings are particularly important for service providers in markets characterized by undifferentiated product offerings and low perceived switching costs between service providers.

Keywords: *customer loyalty; reward program; share of wallet; switching costs*

Many markets have become a battleground for a share of the customer's wallet. Loyalty reward programs are

important tools for driving customer retention in many industries, including airlines, credit card companies, and retail and hotel chains (Kivetz 2005; Kivetz and Simonson 2003; Kivetz, Urminsky, and Zheng 2006; Noordhoff, Pauwels, and Odekerken-Schröder 2004). The goal of such programs is to enhance customer relationships by offering high value to profitable market segments (Bolton, Kannan, and Bramlett 2000; Kumar and Shah 2004). Reward programs are also effective in increasing customers' perceptions of switching costs, thus further fostering customer retention (Bendapudi and Berry 1997; Guiltinan 1989). As many service firms suffer from undifferentiated offerings and low switching costs (Reinartz and Kumar 2000), loyalty reward programs might be an effective tool to relationship building.

This study investigates the relationship between reward programs and customer loyalty. Here, we focus on two dimensions of loyalty, namely attitudinal loyalty and share of wallet, and their relationship. Attitudinal loyalty reflects the consumer's psychological attachment toward a particular provider or brand (Butcher, Sparks, and O'Callaghan 2001; Oliver 1999), whereas share of wallet reflects the consumer's brand-level spending within a

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product category (Baumann, Burton, and Elliott 2005). A richer understanding of the attitudinal component of loyalty is crucial, as it has been shown to be linked to future usage (Liddy 2000), enhanced word-of-mouth recommendations (Reichheld 2003), and ultimately to customer profitability (Reinartz and Kumar 2002).

The primary objective of this study is to examine the combined effects of reward programs and attitudinal loyalty on share of wallet. Specifically, we examine the impact that attractiveness of reward programs and perceived switching costs between reward programs (not between the services themselves) have on share of wallet, and we propose that this relationship is moderated by attitudinal loyalty. The context of the study involves the credit card industry—a market characterized by undifferentiated offerings with virtually zero switching costs between different cards a customer has in the wallet. This study contributes to the services literature by focusing on share of wallet as opposed to purchase or switching intent as a proxy for behavioral loyalty. For many companies, customers shift their spending patterns rather than stop doing business with the company, and hence, managers are increasingly interested in share of wallet rather than customer retention rates (Perkins-Munn et al. 2005). Share of wallet reflects the consumer's brand-level spending in a given product category, and hence, it is one way to measure behavioral loyalty (Jones and Sasser 1995). Despite its importance, research on the topic is scarce (for notable exceptions, see Keiningham, Perkins-Munn, and Evans 2003; Magi 2003). Moreover, prior research on share of wallet has been limited to understanding the relationship between satisfaction, share of wallet, and customer retention (e.g., Perkins-Munn et al. 2005), whereas this study contributes to the literature by examining the relationship between loyalty reward programs and share of wallet.

CONCEPTUAL BACKGROUND AND HYPOTHESES

Relative Attractiveness of Loyalty Programs

Consumers typically participate in reward programs to obtain economic benefits (discounts), emotional benefits (sense of belonging), prestige or recognition, and/or access to an exclusive treatment or service (Gruen 1994; Yi and Jeon 2003). If the consumer views a particular loyalty reward program to be more attractive than competing programs, it seems reasonable to assume that he or she is more likely to participate in that program, even if that customer is a member of several loyalty reward programs. Most reward systems are based on volume (e.g., your 10th sandwich is free), thus inducing heavy users to remain loyal to the company (Shugan 2005). However, we propose

that an individual's psychological attachment to the brand might moderate the relationship between relative attractiveness of a reward program and share of wallet. Previous research suggests that reward programs tend to be more effective in enticing customers whose psychological attachment to the brand is relatively low (O'Malley 1998). Highly committed customers, on the other hand, are likely to be loyal to their brand or provider regardless of the benefits offered by the company's reward program. There are providers with some of the highest loyalty rates in their respective industries that do not offer reward programs. For example, Ritz Carlton or Four Seasons hotels do not offer points to enhance future patronage; instead, they focus on personalization of the service delivery and service excellence as a means to guest loyalty. Based on the above discussion, we put forth the following hypothesis:

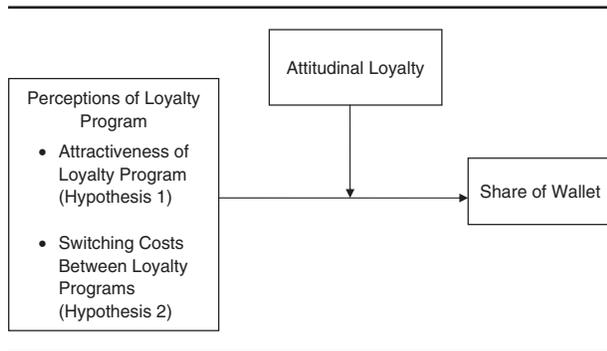
Hypothesis 1: At low levels of attitudinal loyalty, the relative attractiveness of a reward program will have a stronger positive effect on share of wallet than at high levels of attitudinal loyalty.

Perceived Switching Costs Between Reward Programs

In addition to the relative attractiveness of a reward program, perceived switching costs are linked to customer participation in the program. Switching costs can be defined as time, money, and effort associated with changing service providers (Burnham, Frels, and Mahajan 2003; Jones, Mothersbaugh, and Beatty 2000; Lam et al. 2004; Wirtz and Mattila 2003). When loyalty programs are involved, these costs increase. Switching may involve forgoing points (Dick and Basu 1994; Patterson and Smith 2001), expending effort and time in signing up for a new program and learning how to redeem rewards, customize PIN numbers, and so forth. Switching costs can also reflect psychological costs such as loss of sense of belonging, which can be related to a reward program (Dowling and Uncles 1997). As a result, firms can increase switching barriers by offering attractive loyalty programs.

In this article, we propose that attitudinal loyalty will moderate the impact of perceived switching costs on behavioral loyalty. Under conditions of low attitudinal loyalty, consumers are expected to exhibit low behavioral loyalty. However, high switching costs associated with a reward program encourage consumers to stick with a particular brand despite low attitudinal loyalty, leading to increased share of wallet. Conversely, at high levels of attitudinal loyalty, emotional bonding with the brand plays a bigger role in explaining behavior than switching costs associated with the reward program. Consequently, we put forth *Hypothesis 2*. Figure 1 summarizes our two research hypotheses.

FIGURE 1
Research Framework



Hypothesis 2: At low levels of attitudinal loyalty, the perceived switching costs associated with a reward program will have a stronger positive effect on share of wallet than at high levels of attitudinal loyalty.

METHOD

Research Setting and Data Collection

We used the credit card industry as a research context for two reasons. First, most consumers carry two or more credit cards, thus minimizing switching costs between those cards at the point of payment. Second, the products offered in the credit card industry are highly undifferentiated, making it an ideal context to study the impact of reward programs on customer's loyalty or share of wallet.

Data were gathered via door-to-door interviews in three different districts in Singapore, and the sample was stratified by housing type. Respondents who did not own at least two credit cards were screened out. The sample comprised 283 respondents, consisting of 60% males. In terms of age distribution, 36% of the respondents were in their 20s, and the rest of the sample comprised older adults (20% 30 to 39 years old, 20% 40 to 49 years old, and 24% 50 years old and older). The majority of the respondents (50%) had a personal income between \$30,000 and \$59,999, followed by 19% in the \$60,000 to \$89,999 income bracket (income given in Singapore dollars [S\$]; exchange rate as of January 22, 2007: US\$1 = S\$1.54).

Survey Design

Two versions of the survey were randomly administered to respondents. One version had the most preferred credit card carried by the respondent as the focal point of the interview, and the other was anchored at the respondent's

least preferred card (high and low attitudinal loyalty conditions). In the first section, respondents were asked to rank all the credit cards they owned in order of their preference and to estimate their total percentage usage of each card, followed by their past usage pattern of the focal card (share of wallet). The second section measured respondents' attitudes and feelings toward their focal card (manipulation check for attitudinal loyalty). The third section tapped into the perceived attractiveness of the focal card's reward program, and the fourth section measured the perceived switching costs related to switching away from that reward program. The last section captured demographics.

Measures

Attitudinal loyalty was manipulated by anchoring respondents to think of their most versus their least preferred credit card when answering the survey questions. We had a three-item manipulation check for attitudinal loyalty (see Table 1 for all scale items). Relative attractiveness of the loyalty program was measured using Lichtenstein, Burton, and Karson's (1991) relative attractiveness scale adapted to our context. Perceived switching cost between loyalty programs was adapted from Jones, Mothersbaugh, and Beatty (2000). The items tapped into overall perceived effort required when switching loyalty programs, potential rewards forgone, and/or points forgone because of switching. Share of wallet used a two-item self-reported scale. The first asked respondents to state what percentage of credit card purchases were made with the focal card. This percentage figure was then converted to a 7-point scale and combined with the second item that tapped into frequency of use of the focal card compared to other credit cards (adapted from Too, Souchon, and Thirkell 2001).

RESULTS

To ensure that our manipulations were effective, we first compared the means for our three-item attitudinal loyalty scale. As expected, participants in the most preferred card group exhibited higher levels of attitudinal loyalty than their counterparts in the least preferred card group ($M = 5.53$ and $M = 2.47$, respectively, $p < .001$).

We used a median split for relative attractiveness of the reward program and for perceived switching costs between programs. The means were significantly different for both splits at $M = 2.35$ and $M = 4.88$ ($p < .001$) for relative attractiveness and $M = 2.97$ and $M = 5.35$ ($p < .001$) for switching costs.

We used a three-way ANOVA for hypothesis testing (see Tables 2 and 3). All three main effects and two two-way interactions between relative attractiveness and attitudinal

TABLE 1
Scale Items

<i>Measurement Scale</i>	<i>Reliability and Source</i>
Relative attractiveness of reward program (RA) Using the following scales, indicate your attitude toward XYZ credit card's loyalty program compared to other loyalty programs (semantic differential scale anchored in) unfavorable/favorable unattractive/attractive poor/excellent	alpha = .96 Lichtenstein, Burton, and Karson (1991)
Perceived switching costs between reward program (PSC) In general it would be a hassle changing loyalty programs The costs in terms of rewards forgone is high when switching loyalty programs The costs in terms of points forgone is high when switching loyalty programs	alpha = .84 Jones, Mothersbaugh, and Beatty (2000)
Attitudinal loyalty (AL); manipulation check I consider myself a loyal customer of XYZ credit card I try to use XYZ credit card because it is the best choice for me I like using my XYZ credit card to make a purchase	alpha = .93 Pritchard et al. (1999)
Share of wallet (SOW) Estimate how often (%) you charge on each credit card Usually I use my XYZ card instead of other credit cards	$r = .74$ Rayner 1999 Too, Souchon, and Thirkell 2001

NOTE: All items were measured on a 7-point Likert-type scale, ranging from 1 = *strongly disagree* to 7 = *strongly agree* unless otherwise stated.

TABLE 2
ANOVAs With Share of Wallet as Dependent Variable

<i>Source</i>	<i>Type III Sum of Squares</i>	<i>df</i>	<i>Mean Square</i>	<i>F</i>	<i>p</i>	<i>Partial Eta Squared</i>
Three-way ANOVA						
Attitudinal loyalty (AL)	241.3	1	241.3	149.9	< .001	.36
Relative attractiveness (RA)	48.6	1	48.6	30.2	< .001	.10
Perceived switching costs (PSC)	16.6	1	16.6	10.3	.001	.04
AL * RA	8.8	1	8.8	5.4	.02	.02
AL * PSC	1.7	1	1.7	1.1	> .10	.00
PSC * RA	6.4	1	6.4	4.0	.05	.02
AL * PSC * RA	6.1	1	6.1	3.8	.05	.01
Error	426.5	265	1.6			
Total	860.4	272				
Two-way ANOVA – high attitudinal loyalty						
RA	8.5	1	8.5	5.5	.02	.04
PSC	4.0	1	4.0	2.6	> .10	.02
PSC * RA	0.0	1	0.0	0.0	> .10	.00
Error	222.4	144	1.5			
Total	244.9	147				
Two-way ANOVA – low attitudinal loyalty						
RA	46.8	1	46.8	27.8	< .001	.19
PSC	13.9	1	13.9	8.2	< .01	.06
PSC * RA	11.9	1	11.9	7.1	< .01	.06
Error	204.1	121	1.7			
Total	302.9	124				

loyalty ($F = 5.4, p = .02$) and between relative attractiveness and perceived switching costs ($F = 4.0, p = .05$) reached significance. However, these effects were qualified by a significant three-way interaction between attractiveness of the

loyalty program, perceived switching costs, and attitudinal loyalty ($F = 3.8, p = .05$). To simplify interpretation of this three-way interaction, we conducted two two-way ANOVAs controlling for attitudinal loyalty.

TABLE 3
Cell Means of Share of Wallet
by Independent Variables

	Attitudinal Loyalty	
	Low	High
Low switching costs		
Low relative attractiveness	1.99 (1.13)	4.34 (1.40)
High relative attractiveness	2.65 (1.45)	4.87 (1.20)
High switching costs		
Low relative attractiveness	2.04 (1.14)	4.70 (1.49)
High relative attractiveness	4.06 (1.49)	5.25 (1.04)

NOTE: Standard deviations are provided in parentheses.

High Attitudinal Loyalty

For high attitudinal loyalty, the perceived switching cost main effect did not reach significance ($F = 2.6, p > .10$), whereas the relative attractiveness main effect was significant ($F = 5.5, p = .02$). The means were in the expected direction, with $M = 4.44$ and $M = 5.15$ for low and high relative attractiveness, respectively.

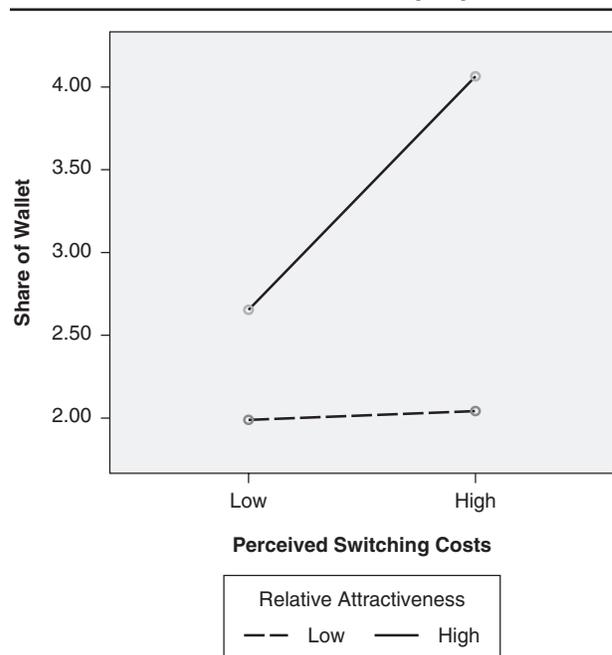
These findings imply that switching costs did not matter, perhaps because at high attitudinal loyalty, the intent of switching out of the loyalty program is low and therefore was not relevant for share of wallet behavior. However, an attractive loyalty program still resulted in increased share of wallet even at high attitudinal loyalty.

Low Attitudinal Loyalty

For low attitudinal loyalty, both the relative attractiveness and switching cost main effects were significant, but these effects were qualified by a significant two-way interaction ($F = 7.1, p < .01$). The means are plotted in Figure 2. Contrast effects comparing low and high relative attractiveness in the low switching cost condition ($M = 1.99$ vs. $M = 2.65, t = 2.09, p = .04$, for low and high relative attractiveness) and in the high switching costs condition ($M = 2.04$ vs. $M = 4.06, t = 4.93, p < .001$, for low and high relative attractiveness) show that relative attractiveness increased share of wallet significantly across both conditions of switching costs.

The plotted means show that switching costs mattered significantly more when an attractive loyalty program was offered than when not. A contrast test showed that at high levels of relative attractiveness, share of wallet increased significantly at higher switching costs ($M = 2.65$ to $M = 4.06, t = 3.46, p < .01$). Conversely, this effect did not reach significance for low levels of perceived attractiveness ($M = 1.99$ to $M = 2.04, t = .17, p = .87$). That is, for perceived switching costs to drive

FIGURE 2
Share of Wallet Cell Means
at Low Attitudinal Loyalty



share of wallet at low attitudinal loyalty required an attractive program.

Hypothesis Testing

We had predicted that the relative attractiveness of a loyalty program (*Hypothesis 1*) and the loyalty program-related switching costs (*Hypothesis 2*) have a stronger effect on share of wallet when customers have low attitudinal loyalty compared to when they have high attitudinal loyalty. Looking at our findings, we can conclude that effects of relative attractiveness and perceived switching costs showed the predicted effect only in conjunction (i.e., when both relative attractiveness and switching costs were high).

Perceived switching costs had no significant effect, except for the low attitudinal loyalty, high relative attractiveness condition. In contrast, relative attractiveness increased share of wallet significantly in all conditions—the mean differences across all cells were between .54 and .67 in the expected direction, except for our special condition of high relative attractiveness and high switching costs, where the mean difference jumped to 1.02.

In conclusion, our hypothesized two-way interactions were superseded by a significant three-way interaction, leading us to reject both our simpler hypotheses. The three-way interaction is intuitive and partially consistent with our hypotheses, indicating that the relationship

between our variables is more complex than initially expected.

DISCUSSION

Loyalty reward programs have become the central part of customer relationship management (Kivetz 2005; Kivetz and Simonson 2003; Kivetz, Urininsky, and Zheng 2006). With a large proportion of the marketing battle being carried out in the reward program arena (Kivetz and Simonson 2002; Noordhoff, Pauwels, and Odekerken-Schröder 2004; O'Malley 1998; Yi and Jeon 2003), this study provides empirical evidence of the effectiveness of reward programs in influencing share of wallet, a reasonable proxy for customer loyalty (Jones and Sasser 1995). To better understand the complex relationship between reward programs and customer loyalty, the present study differentiated between psychological attachment toward the brand (attitudinal loyalty) and credit card usage (share of wallet).

The findings of our study demonstrate that the relative attractiveness of a reward program has a positive impact on behavioral loyalty, and this finding was valid for all of our experimental conditions regardless of the level of attitudinal loyalty. In other words, the more attractive the loyalty program is perceived to be, the greater the perception of rewards gained from participation (Gruen 1994; Wright and Sparks 1999), which in turn seems to be effective in driving share of wallet.

Our findings also indicate that perceived switching costs associated with a reward program have a positive impact on share of wallet but only when low attitudinal loyalty is combined with an attractive reward program. Previous work has established that reward programs are effective in raising switching costs (de Ruyter and Wetzels 1997; Lee, Lee, and Feick 2001; Reinartz and Kumar 2000). Frequent usage is typically rewarded with accrual of points, rewards, or higher service levels that are forgone should the consumer switch to another provider (Dick and Basu 1994; Patterson and Smith 2001).

The findings of this study suggest that the impact of perceived switching costs on behavioral loyalty is moderated by the joint effects of attitudinal loyalty and relative attractiveness of a reward program. That is, perceived switching costs between attractive loyalty programs have a greater impact on share of wallet at low rather than high levels of attitudinal loyalty. With committed customers, switching costs seem to become less relevant in driving actual purchase behavior, perhaps because committed customers are unlikely to have switching intentions in the first place. Also, if a loyalty program is not seen as attractive, related switching costs seem to have minimal impact, probably because there is little to be gained from unattractive rewards.

Managerial Implications

The credit card industry is characterized by largely undifferentiated service offerings combined with multiple cards per customer. Hence, it is easy for customers to switch from one card to another at the point of usage. Under these circumstances, firms could consider implementing reward programs to differentiate themselves (or their offering) and/or raise switching costs at the point of usage. An important goal of any loyalty reward program is to provide customers with an incentive to remain with the company and to prevent competition from stealing share of wallet (Butcher, Sparks, and O'Callaghan 2001; Kivetz and Simonson 2003).

In the commoditized credit card industry, customers often lack psychological attachment to any particular credit card company. However, as our results indicate, offering an attractive loyalty reward program is likely to boost behavioral loyalty. Credit card companies can explore offering a mix of soft rewards (sense of belonging, special treatment, recognition, and appreciation), hard rewards (annual credit card fee waiver, discounts, and point accruals), and higher tier service levels and customization to increase their loyalty program's attractiveness (c.f. Lovelock and Wirtz 2007, p. 366). These same tactics can potentially raise perceived switching costs at the point of purchase, thus further enhancing card usage. It might be beneficial to let customers choose among several reward options to account for idiosyncratic preferences and to maximize customer utility from the rewards offered (Kivetz and Simonson 2003; Kumar and Shah 2004).

Further Research

Our research examined the role of reward programs in influencing behavioral loyalty. In the credit card industry, the context of this study, customer-firm relations are considered noncontractual at the point of usage. Thus, marketers face the difficulty of ensuring continual usage, as switching costs are close to zero when their customers carry several cards. Hence, future studies should investigate attitudinal and behavioral loyalty in services characterized by contractual settings (e.g., insurance companies or health clubs).

The scope of this study was limited to two characteristics of reward programs. Future investigations could explore different aspects of loyalty program-related switching costs (e.g., financial and psychological switching costs) to gain a richer understanding of the impact of reward programs on loyalty. Similarly, attractiveness of loyalty programs could be studied from several perspectives (e.g., the cumulative attractiveness of rewards vs. instant gratification).

Furthermore, future research on examining the attitudinal-behavioral loyalty relationship is warranted. We took the perspective that attitudinal loyalty moderates the effects of loyalty program features on behavioral loyalty. Yet one could argue that it is the loyalty program that moderates the attitudinal-behavioral loyalty link. Future work should explore the causal flow of these constructs.

Finally, we have to acknowledge that our data are correlational and rely on self-reported and perceived measures of the various constructs, including share of wallet. Future research could examine these constructs and their relationships using manipulations (e.g., field experiments) and behavioral measures (e.g., observed share of wallet).

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