The ROI Of Customer Loyalty
Business Case: The Customer Loyalty Playbook
by Emily Collins and Reggie Lau
June 1, 2017

Why Read This Report
Loyalty programs help companies identify and collect rich data about their best customers in order to reward, recognize, and retain them. This report helps B2C marketing professionals make the case for investment in a loyalty program. It provides a return on investment (ROI) model for loyalty program expenditures using Forrester’s Total Economic Impact™ (TEI) framework.

Key Takeaways
B2C Marketers Struggle To Make The Case For Long-Term Investments In Loyalty
Companies still invest more in customer acquisition than customer retention. To change this model, B2C marketers must take a thoughtful look at the costs and benefits of loyalty and explain how it will drive incremental value.

Forrester’s TEI Framework Helps Marketers Develop A Business Case
We present a model for capturing ROI that balances the complexity of loyalty investments. It breaks down benefit and cost components while factoring in risk and efficiencies.

Customize The Model To Fit Your Unique Program Requirements
The model is an interactive workbook that readers can change to fit specific technology costs, program components, and objectives.
Promising Long-Term Loyalty Isn’t Enough To Secure Program Funding

B2C marketers tell us that increasing customer loyalty is a top strategic priority, but year after year our data shows that marketers still spend more on acquisition than retention.¹ Companies across industries leverage loyalty programs to identify their most engaged customers, collect behavioral and preference data, and incentivize incremental purchases.² But these programs come at a cost: The platforms that power them can be big investments and require integration with existing marketing systems to be fully effective. In addition, it can take months to get these systems up and running. When justifying the time and cost to implement loyalty programs, marketers must:

› Quantify all potential contributions of a loyalty program. Increasing customer loyalty is an enterprise-wide responsibility — not one that just falls onto marketing. Best-in-class loyalty strategies require input and participation from all customer-facing departments in the organization — including customer service and customer experience — to be truly effective.³ These related customer initiatives also yield loyalty outcomes like retention, enrichment, and advocacy. To argue convincingly for the investment, B2C marketers must explain how it will fit into the existing marketing ecosystem and integrate with other customer-facing initiatives to drive incremental value.

› Account for all costs and benefits. The costs of a loyalty program, including design and implementation, marketing, and rewards, are easily accounted for. But the benefits of a loyalty program, especially since it’s a long-term strategy, can be harder to discern. This is especially true when businesses are under pressure to deliver short-term results to shareholders and investors, or firms are relying on the emotional benefits, which are difficult to measure.⁴ Since loyalty is a long-term investment, it’s important to take a balanced and thoughtful look at both the costs and benefits when making decisions about allocating budget. One consumer packaged goods (CPG) company made the case for loyalty by assessing its impact on overall marketing and program lifetime value starting at the point of program launch.
 › **Assess risk.** Marketers must think beyond direct costs and benefits when considering investments in loyalty programs. How long will implementation take? What happens if implementation slips? Will the organization take full advantage of the solution and the insights generated? How will the organization manage points liability? Incorporating these internal and external risks makes the model more realistic.

**Use Forrester’s TEI Framework To Make The Business Case**

B2C marketers face organizational and cultural challenges when making investments in customer loyalty. They can use Forrester’s Total Economic Impact methodology to overcome those challenges by demonstrating the tangible value of loyalty programs for marketing and beyond. Key elements of this business case methodology include communicating a business problem, proposing a solution that meets objectives, and supporting that choice with financial analysis (see Figure 1). The methodology helps B2C marketers quantify operational gains and incremental performance lift and subtract technology costs. Additionally, it incorporates risk factors and deferred future benefits (see Figure 2). Use the associated interactive workbook to create the financial analysis for your business case. Forrester has provided an example of what an investment in a customer loyalty program could look like (see Figure 3).
FIGURE 1 Key Elements Of The Business Technology Business Case

<table>
<thead>
<tr>
<th>Category</th>
<th>Description</th>
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</thead>
<tbody>
<tr>
<td>Executive summary</td>
<td>Should stand on its own</td>
</tr>
<tr>
<td>Problem description</td>
<td>Is the why of the project</td>
</tr>
<tr>
<td>Current practices</td>
<td>Describe current state</td>
</tr>
<tr>
<td>Best practices</td>
<td>Describe ideal state</td>
</tr>
<tr>
<td>Gap analysis</td>
<td>Is the difference between the current and the ideal</td>
</tr>
<tr>
<td>Solution description</td>
<td>Is the what of the project</td>
</tr>
<tr>
<td>Solution overview</td>
<td>Is how problems will be addressed</td>
</tr>
<tr>
<td>Resource requirements</td>
<td>Include both project resources and those that are required to support</td>
</tr>
<tr>
<td></td>
<td>resulting business changes</td>
</tr>
<tr>
<td>Considered alternatives</td>
<td>Add credibility to the recommendation</td>
</tr>
<tr>
<td>Project timeline</td>
<td>Shows scope and scale of effort</td>
</tr>
<tr>
<td>Risk analysis</td>
<td>Describes areas of uncertainty</td>
</tr>
<tr>
<td>Key goals and metrics</td>
<td>Include success metrics, baselines, and projections</td>
</tr>
<tr>
<td>Financial analysis</td>
<td>Translates the project into business value</td>
</tr>
</tbody>
</table>

FIGURE 2 Forrester’s Total Economic Impact Framework Examines Benefits, Costs, Flexibility, And Risk

- People
- Process
- Technology
- Quantified value
- Defined metrics
  - New opportunities created for the future

Benefits (impact on business)

Costs (impact on budget)

Flexibility (options)

Risk

Total Economic Impact™ (TEI)

Uncertainty

impact of assumptions
These tables provide a summary of the costs, benefits, ROI, and payback period over a three-year time horizon. The first table contains the totals based on the inputs on the cost and benefit tabs. The second table applies the risk levels, set on the risk tabs for both benefits and costs. As assumptions are changed on the later tabs, these totals will update. The spreadsheet associated with this figure contains details about this model.

### Discount rate

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#### Original estimates

<table>
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<th>Initial</th>
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<th>Year 2</th>
<th>Year 3</th>
<th>Total</th>
<th>Present value</th>
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<tr>
<td>Costs</td>
<td>$1,506,458</td>
<td>$23,574,697</td>
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<td>$24,979,946</td>
<td>$74,328,039</td>
<td>$61,761,125</td>
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<td>$40,170,000</td>
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<td>$29,821,907</td>
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</table>

#### Risk-adjusted estimates

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<th>Initial</th>
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<th>Year 2</th>
<th>Year 3</th>
<th>Total</th>
<th>Present value</th>
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<tr>
<td>Cumulative</td>
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<td>$9,878,748</td>
<td>$21,751,066</td>
<td>$33,995,803</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### ROI

<table>
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<tr>
<th></th>
<th>61%</th>
<th>42%</th>
</tr>
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### Payback period (years)

<table>
<thead>
<tr>
<th></th>
<th>Within 1 year</th>
<th>Within 1 year</th>
</tr>
</thead>
</table>

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Determine Revenue From Retained And Incremental Earnings

Forrester’s TEI framework includes top-line revenue gains derived from anticipated increased marketing effectiveness. The components of the model that focus on loyalty marketing performance:

› **Account for retained revenue benefits.** Since B2C marketers tell us the primary objective of their loyalty initiatives is customer retention, the model accounts for retained earnings as a result of reducing membership attrition, churn, or idleness. Different organizations set diverse goals and objectives for customer loyalty programs ranging from customer retention and profitability to increased wallet share; marketers can tailor this model according to their organization’s specific goals.

› **Represent incremental improvements to sales and customer value.** The model also takes into account improvements in customer value. Specifically, incremental earnings measure the value differential between a nonmember and a member through metrics like average order value, visit frequency, purchase frequency, or spend. The companies we interviewed for this report noted the importance of using incremental revenue as the basis of their loyalty business case, since there may already be marketing initiatives in play — such as email programs — that aim to drive sales and revenue as well. For instance, a retailer saw a 34% year-over-year boost in incremental spend for returning customers due to its loyalty program.

Add Savings From Operational Efficiency

In addition to incremental and retained earnings, customer loyalty programs may also create efficiencies in other areas of the business. Forrester’s TEI framework splits them into two primary groups, capturing benefits that:

› **Identify savings based on marketing efficiency.** The first group of efficiencies compares the cost and return of the customer loyalty program with the cost and return of all other marketing activities including advertising and events. If applied correctly, the customer insights gleaned from loyalty data can help companies earn a greater return on the dollars they spend. As the purpose of advertising, events, and other marketing activities can vary widely and serve a different purpose than customer loyalty, it isn’t likely that any cost effectiveness would be reallocated or recouped as a tangible benefit. This area simply provides a comparison of the highest return on investment if an organization could only invest in one item for a singular purpose.

› **Tie savings to driving desired member behaviors.** The second group of efficiencies uses customer loyalty programs, in particular those with points, to generate specific member behaviors that the organization desires. These can include offering points to members to use paperless billing, provide product reviews, or follow an organization’s social account. The behaviors can then be valued or lead to quantifiable metrics.
Subtract The Costs Of Technology And Related Services

Once you’ve quantified the performance enhancements and operational benefits that come from investing in the loyalty program, subtract the costs to arrive at your TEI estimates. The model accounts for execution costs that:

› **You incur upfront during adoption, testing, and implementation.** The model accounts for costs associated with initiating the program and includes all expenses up to the rollout and operation of the program including design and development and employee training. This model gives users the ability to select costs associated with either an external partner or an internal build. When making the decision whether to work with an external partner or develop internally, organizations must closely assess budget, availability of internal talent, and challenges in systems integration.

› **You realize on a recurring basis for ongoing operations and maintenance.** The model captures ongoing costs monthly. These include the costs of the loyalty currency, discounts and promotions, internal staff, and professional services. For a customer loyalty program, the largest component of recurring costs is typically the rewards that it offers to members. This includes points that have a tangible cost (i.e., $1 per point) as well as conveniences or experiential benefits like credit score checks, accelerated customer service, in-store events, or free alterations on purchased clothing. These costs may be distributed or absorbed by other departments.

Adjust Benefits And Costs Based On Risk

Forrester’s TEI framework takes into account calculated risks that may increase costs or decrease projected benefits. The model quantifies risk calculated based on time, cost overruns, and missed goals. To increase its accuracy, the TEI model factors in these risks and applies probabilities for achieving stated goals. Events accounted for here can include delays caused by integration hiccups, sluggish enrollment rates, or a lower-than-expected impact on customer behavior.

Recommendations

Tweak The Model’s Assumptions To Meet Your Business Needs

Forrester’s TEI methodology uses assumptions to simplify the financial analysis without jeopardizing its scope. B2C marketers can customize the assumptions within the framework to better fit their business goals and unique loyalty strategies. This is important because:

› **Costs and benefits aren’t the same for every kind of loyalty program.** The structure and goals of the program and how you plan to manage it will make these factors vary. Review the model and customize it according to your specific use cases. For instance, in retail, programs are largely designed to move the needle on traditional recency, frequency, and monetary value (RFM) metrics, while CPG companies look to loyalty programs as a way to collect customer data and increase engagement with the brand.
Recoupment periods will differ by organization and consumer behavior. Marketers shouldn’t expect there to be some industry benchmark or generally accepted time for recoupment of loyalty program costs because each organization’s needs and expectations of the investment are different. The five firms that we spoke with for this report told us that the benefits from loyalty investments outpaced their spend within two years.

Risks will vary. Marketers must anticipate and adjust risk assumptions in their business case, or they might face unexpected bumps in the road that jeopardize expected outcomes, exposing themselves to time and cost overruns. Specifically, they must consider their approach to loyalty, program benefit structure, and talent and resource availability. For example, a marketer that is planning to launch a loyalty program in an industry where program maturity is generally low might find implementing a program riskier than a marketer that is launching or revamping a program in an industry where programs are widespread and well adopted.

Your customized model can help you assess performance after implementation. Don’t treat the business case justification and TEI framework as a one-time effort prior to program implementation. Your program strategy must evolve with customers’ expectations in order to continue to earn their loyalty. For example, Regal Entertainment Group used the results of its customer feedback surveys and focus groups to tweak and refine the program before launch. The model provides you with two useful capabilities after your program is in market: 1) You can validate your assumptions to sharpen future models, and 2) you can use the metrics embedded in your model to determine if your program is keeping pace with customers and with competitors’ programs.
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Supplemental Material

**Online Resource**
The online version of Figure 3 is an interactive tool to take a deep dive into Forrester’s assessment of the ROI of customer loyalty. Use this model to view Forrester’s analysis and customize the assumptions, costs, and benefits to meet the characteristics of your organization.

**Companies Interviewed For This Report**
We would like to thank the individuals from the following companies who generously gave their time during the research for this report.

Brierley+Partners
HelloWorld
Citi
Regal Entertainment Group
GameStop
Endnotes

1 B2C marketing decision makers indicate that 37% of their marketing program budget is spent on new customer acquisition (both predetermined and unnamed prospects) whereas only 20% of marketing budget is spent on driving retention/upsell to existing customers. Source: Forrester Data Global Business Technographics® Marketing Survey, 2016.

2 Members of traditional retail loyalty programs spent an average of $183.50 over a typical three-month period, compared with $141.20 spent by nonmembers. Source: Forrester Data Customer Experience Index Online Survey, US Consumers 2016.

Forrester further compared members with nonmembers across four industries — airlines, car rental providers, hotels, and retailers in a brief. See the Forrester report “Brief: Loyalty Program Members Give Brands Higher Customer Experience Index Scores.”

3 To ensure the consistent development and execution of the loyalty strategy, companies need to streamline efforts across multiple teams: marketing, business technology (BT), customer experience, customer service, customer insights, finance, and market insights. See the Forrester report “Get All Hands On Deck To Reinforce Customer Loyalty.”

4 See the Forrester report “Five Keys To Unlock Additional Funding For Customer Loyalty.”

5 See the Forrester report “The State Of Loyalty Strategies 2016.”
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