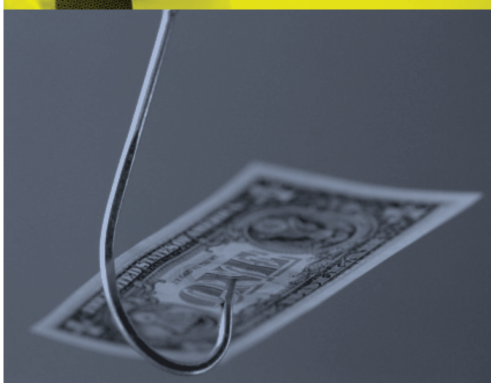

An EMI Industry
Intelligence Report

Expanding Rewards Impact While Maintaining Program ROI

By: Judy Cohen, Practice Leader

As many banks slow acquisition efforts to control costs and focus on maximizing current customer relationships, rewards programs remain a key — albeit expensive — strategy. However, with virtually every bank offering rewards, and with customers averaging 5 credit cards in wallet (more than 8, including store and gas cards[1]), simply offering rewards on credit and debit cards is no longer enough:

The market is saturated.

Rewards programs are increasingly look-alike.

Savvy consumers are continually cashing out for a better deal.

To win and retain your customers, find out how banking leaders are reinventing rewards strategies and focusing on smart marketing to ensure their messages are compelling and response-generating.

EMI Strategic Marketing

The Rewards Dilemma: Cost vs. Commoditization

The Saturated Rewards Market

- More than 60% of credit cards carry rewards[2]
- More than half of debit card issuers offer rewards programs[3]
- 75% of consumers participate in credit, debit, or ATM rewards programs[4]

Virtually every bank now offers debit or credit card rewards, or both, to attract new customers, retain current clients, and generate incremental interchange income from higher transaction volumes. But the push to market rewards programs has created serious dilemmas for industry marketers:

- **Programs are increasingly look-alike.**
  This is no great surprise since so many originate with the same providers — Visa, MasterCard, Maritz, and Carlson — and generally offer identical redemption options and brands from the same retailers. In 2007, 38% of banks with debit rewards used Visa Extras as their platform.[5] As of late 2008, Visa Extras was offered on credit or debit cards from Wells Fargo, Chase, National City, PNC, BB&T, and many other leading Visa-issuing banks.

- **Program differentiation comes at a high price.**

  To differentiate, some banks invest heavily to offer faster earn rates or impressive promotional bonuses, a broader range of redemption options, and best-in-class customer service — all with significant cost implications.

  - Capital One's 20,000 miles introductory offer for some cards is paid as 10,000 miles at the end of year one and 10,000 miles at the end of year two after $3,000 in annual purchases each year, to decrease attrition and stimulate ongoing usage over a longer period.
  - To promote ongoing spending and top-of-wallet behavior, Discover's Miles card awards 1,000 bonus miles for every month a purchase is made in the first year.
  - Sovereign Bank rewards its new small business customers for their "relationship" with up to $650. To earn the full amount, the business owner must open a business DDA ($150) and a personal DDA ($100), and actively use both debit cards; sign up for — and use — Merchant Services; and apply and be approved for a Sovereign Amex Gold Card, which can earn 5% cash back, up to $200.

- **Bank margins are increasingly squeezed.**
  The cost of rewards alone can be a drain on the marketing budget.

  - When American Express increased its assumed redemption rate for Membership Rewards points from 85% to 90% in 2007, it added a one-time accrued liability charge of $685MM. It reported spending a total of $4.8BN on cardmember rewards[6] that year, and only slightly less in 2008 ($4.4BN) as volume declined.
  - Discover's $160MM expense on cashback rewards in 2Q09 was higher than its $103MM spend on marketing and business development.

- **Cost-sharing through retail partnerships is now commonplace.**
  A growing number of online merchant malls offer banks' customers discounts and other promotional offers, from nearly all the same retailers. This relatively recent movement to motivate incremental spending on a specific bank card is losing some of its luster as a program differentiator since many of these offers involve the same participating merchant partners.

Leading Banks' Retail Partnerships

National and local retailers participate in these primarily online discount programs.

Partner	Bank	Program Name
The Database Group	American Express	Bonus Points Mall
	Bank of America	Add It Up and WorldPoints Mall
Access Development	Zions	Zions Cash Rewards
Mall Networks	Discover	ShopDiscover
	Wachovia	Earn More Mall
Vesdia	Citibank	ThankYou.com and Bonus Cash Center
	Citizens Bank	Citizens Bank Merchant Network
	SunTrust	SunTrust Rewards BonusBuy
Affinity Solutions	Regions	Regions CheckCard Rewards
	Sovereign	Sovereign Cash Rewards

- **Points-fatigued and ever-more pragmatic in today's tough economy, customers now prefer cash back, which doesn't engender loyalty.**
  61% of the respondents to EMI's 2008 Loyalty Study[4] told us that cash back rewards were their first choice, followed by only 21% who prefer merchandise or gift cards. Yet whenever a consumer receives a statement credit or check, he no longer has any "equity" in the program and becomes ripe for switching to the next best offer. In addition, with so many banks offering cash back today, the customer simply does the math and applies for the payment product with the highest earn rate.

With such commoditization, loyalty to a specific bank or reward program is becoming increasingly rare.

Creating a program that piques anyone's interest has become a real challenge.

Do Financial Institutions Need a Rewards Program?

Are rewards a necessity for success in acquisition and retention? Certainly banks can market themselves on other attributes that matter to customers: *Service, Location and Convenience, Product* and *Pricing*. But these attributes are both expensive and difficult to deliver on. It's almost impossible to unseat category leaders that offer:

- **An unbeatable level of customer service:**
  - American Express, at great expense, sets the bar for customer service — and is the clear leader in rewards.
  - Of the branch banks, Wachovia (now part of Wells Fargo) has placed first in the American Consumer Satisfaction Index every year since 2001. Customers love them — but this level of channel performance takes years to achieve, an enterprise-wide commitment and significant investment in a service culture.
  - In May 2009, Discover won the Brand Keys Customer Loyalty Award for the 12th consecutive year.
  - Chase's new Sapphire card heavily promotes 24/7 access to live, dedicated customer service advisors.
- **Convenience through presence, open branches and extensive product offerings:** It's hard to compete with Bank of America with its 6,109 branches and more than 11,000 ATMs; Wells Fargo/Wachovia with 6,668 branches and 12,000 ATMs; and Chase, with its expanded Washington Mutual footprint, which now has more than 5,203 branches and 14,000 ATMs. They have their markets covered: convenient ATMs everywhere and an extensive product line-up that suits all target audiences and provides "one stop" shopping. TD Banknorth, with its smaller footprint, provides a different spin on convenience — branch availability 7 days a week, which it is rolling out throughout its geography.
- **Best-in-market rates, yields and "free" products:** Online banks, as well as some community banks and non-profit credit unions with low-operating costs and preferential tax status, are price leaders and successful, even while offering some of the highest yields on deposits. However, pricing offers don't provide a sustainable competitive advantage since they're so easily copied, and they can only be offered by similar institutions with low cost structures.

Clearly rewards alone don't engender sustained customer loyalty. But they do contribute to loyalty when positioned in the context of the bank's commitment to enhancing customer relationships and satisfaction.

For banks that can't achieve or compete on these fronts, there's another answer:

Create a differentiated rewards program that spans your product set and market it skillfully.

Offering Rewards on a Single Product Is Not Enough

Incentives for single or first-product adoption produce limited customer engagement and no opportunity to amortize rewards program costs.

- **Credit card-only programs make it too easy for customers to be lured away.** In EMI's loyalty survey[4], 34% of a bank's customers said they adopted cards from institutions other than their primary bank because of a better rewards offering.
- **Debit card-only programs are at a disadvantage because of their financials.** Debit rewards alone have to be meager; low debit purchase interchange, both signature- and PIN-based, limits the return to the customer — and therefore the tie to the bank.

Conversely, multi-product rewards create opportunity to sell more product, strengthen customer relationships and drive profitability. The evolutionary first step from rewards on single products has been to enable customers to combine credit and debit card rewards. But a more important second step has been the expansion of rewards to cover DDA-related transactions.

Card-based Rewards Have Evolved and Now Include DDA Services

A checking account is rarely viewed as a single product. It's truly the gateway to moving customers to more cost-efficient products: direct deposit, debit cards, online banking and bill payment, and ATMs — all behaviors every bank wants to encourage. In addition, with lending criteria still tight, virtually all banks are focused on capturing deposits for balance sheet strength and market share growth.

Checking-Related Rewards Offers from Leading Banks

Relationship programs now reward much more than single account usage to drive cross-sell success.

Bank	*Signature Purchases*	*PIN Purchases*	*Ongoing Earn Activities*
Capital One	10 miles / transaction	10 miles / transaction	Withdrawals: 5 miles Electronic Bill Pay: 10 miles Account anniversary: 1,000 miles each year
Citibank	1 pt / $2	1 pt / $2	Checking account with two linked products: 25 to 1,200 pts Online bill payment: 20 pts per transaction
Citizens	1 pt / $1	1 pt / $2	Recurring payments: 2 pts / $1 Online bill payment: 20 pts per transaction
National City	2 pts / $1 (gas, grocery & drug store purchases) 1 pt / $1 (all other)	25 pts / transaction	Electronic Bill Pay: 25 pts per transaction Direct Deposit: 25 pts per transaction Preauthorized savings account transfer: 500 pts Business CheckCard: 2 pts/$1; 25 pts per direct debit *Note: Limit of 500 pts/month for points earned on checks, bill payment, PIN purchase and direct debit*

Further evolving, there are now essentially two very different categories of relationship rewards:

- Pure points-based enterprise-wide programs that allow customers to earn and pool rewards points based on usage of multiple bank products, and
- Preferential rates and discounts on individual products as rewards for multiple product ownership.

Citibank, National City and Capital One Bank have been refining and enhancing their enterprise-wide points programs to ensure they attract and retain customers.

A recent Citibank offer to affluent prospects was 43,500 points worth $425 in gift cards for opening three accounts: Citigold Checking, a money market account, and a Citi PremierPass credit card. While the qualifying usage requirements created a large enough hurdle to keep most prospects from adopting all three products – and Citibank from paying out more than 40,000 points – the offer raised consumer awareness that ThankYou Points extend across multiple products.

Selling in from a base of deposit accounts, "points from National City" has been successful because the bank rewards most core products and repeatedly markets that message. At times, the program itself receives as much or more marketing real estate in mail, print, and merchandising as do the bank products. National City has sequenced the right products, at the right time, and has grown "points" coverage to now reward credit, deposit, mortgage, and home equity products.

After adding the credit card division's No Hassle rewards as a feature of the Direct Bank's Money Market Accounts, Capital One added its "No Hassle" program to the local bank's consumer DDA services. Rewarding debit usage, check writing, withdrawals at ATMs and online bill payments, the local bank heavily promotes this multi-product relationship program throughout its physical branch network.

Other banks — such as Chase and Harris Bank — reward existing checking account customers with a series of preferential offers (discounts, special bonus offers, lower rates, more rewards points earning potential) on discrete products. While these programs do not take the totality of the customer's relationship with the bank into account, they typically require a lower level of cross-organizational coordination and systems development than the enterprise-wide points programs above.

Through a combination of broadcast media and its retail channel, Chase continues to heavily promote Chase Exclusives (launched June 2008). Leveraging the Chase Freedom credit card (now its most-promoted card), along with checking accounts and home equity lines, Chase informs customers that they can enjoy relationship rates on multiple products as well as increased points earning on Freedom cards – but only when they have checking accounts too. As of 2Q09, Chase had 25.3MM checking account customers and added two more offers for DDA customers: 1% cashback on mortgages, and 10% extra points and 10 bonus points for Chase Freedom credit card purchases.

Harris Bank's Extras program features bonuses on deposits, discounts on loans (25 bps on home equity, 50 bps on fixed-rate loans with AutoPay), and other benefits for all Harris personal checking account holders. It also has a Harris Extras for Business program.

Strong Marketing Can Drive Program Differentiation

With customer rewards and preferred rates now commonplace, marketing discipline becomes more important than ever. Messaging not only has to work hard to convince prospects that the program is different, but CRM campaigns must cost-effectively cross sell products and encourage ongoing usage.

Relationship rewards leaders leverage the breadth and strength of their programs to showcase the value of a broader relationship with the bank. They are overcoming siloed marketing and limited budgets to continuously sell their cross-enterprise rewards offers.

These bank leaders are investing in smart marketing to ensure they clearly communicate how customer benefits increase with greater product adoption and usage. After carefully sub-branding their programs and crafting a distinctive "look and feel," they ensure the programs are continuously visible at frequent customer touchpoints.

Rewards: Are They Worth the Cost?

With the financial crisis, banks have moved back to basics and are embracing relationship banking. And while rewards are expensive, they have become an integral element in building relationships.

To produce positive ROI, programs must motivate the desired behavior from the most-likely-to-be-profitable prospects. Recognizing this, banks need to apply sophisticated database technology and analytics to ensure the right offers reach their targeted segments. Outsourcing some of the systems required, an increasing number of banks are moving swiftly to:

- Customize rewards and earning opportunities to entice customers of high-potential demographics and psychographics
- Make it easy for customers to pool points, shop online, and redeem easily, so they experience the program benefits often and return to the bank's site frequently
- Increase awareness through fresh promotions and bonus offers, with carefully calculated frequency and measurement, and delivery by low-cost emails to customers

New technology enables narrowly-defined segmentation based on past customer behavior, so banks can now dynamically deliver appropriate offers to targeted niches. This new layer of one-to-one marketing and customer recognition will, over time, lower attrition rates and increase cross sell. Banks slow to embrace relationship pricing and rewards supported by technology and customized communications may find it increasingly difficult to win customers from their competition.

To learn how EMI can help you maximize your rewards program, call Judy Cohen at 617-226-4359.

Sources

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