Loyalty programs in the function of customer relationship strategy

Програми лојалности у функцији стратегије везивања купаца

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Abstract: The aim of this paper is to analyse the loyalty program in the function of selecting the most adequate customer relationship strategy in the retail sector. Strengthening retailers' competitiveness on the market is realized on the basis of development and creation of an interactive and long-term relationship with customers (CRM) within which the most efficient ways of meeting the demands of modern customers are systemically identified. In this context, the basic characteristics of CRMand relational assessment are defined in the paper, the significance of the concept of loyalty as the basis of the CRM strategyis analysed and diverse ways of bonding customers based on different types of loyalty programs in retail are presented. The conducted research can serve the management of retailers as a guideline for developing, designing and implementing a successful loyalty program and building a long-term relationship with customers. Suggestions for future research are listed in the paper.

Keywords: loyalty programs, retail, customers, CRM.

Сажетак: Циљ овог рада јесте анализа програма лојалности у функцији избора најадекватније стратегије везивања купаца у малопродајном сектору. Јачање конкурентности малопродаваца на тржишту реализује се управо на основу развоја и изградње интерактивног и дугорочног односа с купима (CRM), у оквиру којег се системски идентификују и проналазе најефикаснији начин и задовољавања захтева савремених купаца. У том контексту у раду су дефинисане основне карактеристике CRM-а, анализи раније значај концепта лојалности као упоришта CRM стратегије и презентовани су начини везивања купаца на бази различитих типова програма лојалности у малопродаји. Спроведено истраживање може послужити менаџменту малопродајних објеката као смерница за развијање, пројектовање и спровођење успешног програма лојалности и изградњу дугорочног односа с купима. Предлози и сугестије за будућа истраживања наведени су у раду.

Кључне речи: програми лојалности, малопродаја, купци, CRM

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Introduction

In literature (Lovreta et al., 2010; Mayer-Waarden, 2007; Aspinall et al., 2002), retaining customers (or those that are good customers) is one of the most important topics in customer relationship management (CRM) in the retail sector. Aspinall et al. (2002) conclude that some customers are obviously "loyal" and/or "obligated", others buy products from certain companies, but they are simply not loyal to them and easilyswitch to other companies, while others think they should not buy products from just one retailer but continually change them. A special group of customers does not make purchases, but they feel some kind of loyalty to the specific retailer. Obstacles, such as prices, access, range of products, etc., can prevent the purchase. However, when they are removed, a loyal customer can show his/her loyalty by specificbehaviour.

According to Lovreta et al. (2010), satisfaction and retention of customers, as well as improvement of their experience during the realization of sales should be the main goal and task of CRM. By realizing the business in this way, the majority of customers will switch to the first category - loyal customers- and itis indirectly reflected on the financial indicators and the market share of the retailers. As the biggest obstacles to building a long-term relationship with customers, Plazibat (2016) and Stone & Woods (2002) consider incorrectly recorded transactions, inaccurate discounts, unequal individual interests of sellers and customers, lines at the "peak visit times", omissions in the range of products, etc.The task of CRM is actually minimizing the above mentioned omissions and putting the customer at the centre of business activities based on well-conceived loyalty programs (Filipe et al. (2017); Alina Elena, (2016).

It is exactly the loyalty programs in the retail sector that need to create a strong link between trading enterprises and final customers (Loreta, Končar, & Petković, 2013). Dowling & Uncles (1997) divided the expected outcomes of the loyalty program into three parts: a) maintain sales levels, margins and profits (a defensive outcome to protect the existing customer base); b) increase the loyalty and potential value of existing customers (an offensive outcome to provide increases in sales, margins and profits); and c) induce cross-product buying by existing customers. This achieves the basic goals of CRM with retailers: a) toincrease profits and market share, b) to create a database, acquire new customers and improve communication with existing customers, and c) to increase the frequency of visits and the frequency of using or improving the product, brand, and image of a trading company.

Bearing in mind the presented aspects, *the subject of this research* is the analysis of the advantages of building long-term relationships with customers (CRM) based on loyalty programs in the retail sector. *The aim of the research* is to define the appropriate program of loyalty based on the size of the retailer, reward structure and type of sponsorship. In this context, the paper comprises three sections. Introductory

considerations are followed by the definition of the basic characteristicsof CRM andrelational assessment, and their effects and significance for long-term customer bonding. In the second section, the concept of loyalty is analysed, the matrix of loyalty is defined and an analysis of the value of customers for trading enterprises is carried out. In the final section, a comparative analysis of the different types of loyalty programis made compared to the size of the retailer, the loyalty program's instruments, the type ofrewards and the types of sponsorship. The concluding observations summarize the most important results of the conducted research and provide guidelines for future CRM research in the retail sector.

1. CRM and relationship assessment

The specificity of customer demands that are typical for modern market conditions have made it possible in economic theory and practice to develop a systemic approach in identifying and finding ways to meet the requirements of a modern customer. Swift (2000) defines such approach as Customer Relationship Management (CRM) that includes the company's endeavours to direct the whole business activity to a more accurate and better understanding of the behaviour of customers and the possibility of influencing them through various forms of meaningful (two-way) communication, aimed at the continuous improvement of the ability to attract new and retain existing customers, and to raise the level of their loyalty and usefulness. According to Foss, Stoneand Komolafe (20002) managing long-term relationships with clients is a methodology that implies a comprehensive approach to business reorganization, whose primary goal is to recognize specific habits, behaviours and preferences of customers with the ultimate task of building a high level of loyalty. Similar to this viewpoint, Bradshaw and Brash (2001) define CRM as a managerial approach that includes identifying, attracting, developing and maintaining relationships with customers, in order to increase the retention of profitable customers. Therefore, CRM is actually a business strategy that should maintain and improve the relationship with profitable customers, while minimizing business costs with less profitable customers (Rodrigues & Stone, 2002).

In the retail sector, CRM includes activities such as: sales staff recognition and remembering customers' attitudes, behaviour and names, keeping track of their habits and buying preferences, rating the satisfaction with the purchase, recording other essential information about the customer and/or his/her family members, etc. Collected information is used to improve existing products, i.e. services, create and promote new ones, or customize their own business models (Lovreta et al., 2010).

In fact, this is an old business practice that has long been used for improving the sales of leading retailers. When establishing CRM, according to Lovreta et al. (2010, p. 60),the following key elements are especially evident: customers and their needs make a starting point in retail; the individual goals of the sellers and customers influence

their mutual relations; exchange, which is a central point in long-term marketing relations, includes a constant battle for equalizing the forces; there are various means of establishing long-term relationships between sellers and customers; promises must be made to maintain long-term relationships; mutual trust is the main factor in long-term relationships, etc.

In order to achieve the goal, i.e. identify and acquire loyal customers of value, a starting point should be to assess the customer portfolio of the retailer through the analysis of the main characteristics of its relationship with customers. It assumes the thorough exanimation of constructs such as satisfaction and strength of the relationship, mutual power, trust and commitment.

In the framework of CRM, the concept of satisfaction is regarded as a complex construct with specific characteristics. It is seen as a dynamic evaluative, emotional and partly behavioural response of the buyer that is manifested in a certain moment and regarding a certain reason (Georgieva et al., 2008). Although in literature it is commonly considered at transactional or product levels, it can also be analysed at a broader relational level (Storbacka et al., 1994). Satisfaction, together with trust and commitment, are key elements of quality relationships. Trust is related to the belief in the reliability and the competence of the partner (i.e. the retailer). Morgan and Hunt (1994) build a model where it is seen as a result from the sharing of values, proper communications and the lack of opportunistic behaviour. Relational commitment on the other handis defined as a conviction that the relationship is important and an intention to keep it, these being provoked by the existence oftermination costs, relational advantages, shared values and trust.

The strength of the relationship is another construct that is often analysed regarding the seller-buyer dyad. Shi et al. (2009) develop a scale for its measurement which comprises the following three dimensions: (1) affective strength, based on emotions, (2) cognitive strength, based on rationality and (3) conative strength, based on will. According to Storbacka et al. (1994) the relational strength results from the satisfaction and the commitment of the customer as well as from his binding with bonds at different levels. In this context the created bonds act as barriers for termination of the relationship. They can be juridical, economical, technological, geographical, temporal, informational, social, cultural, ideological and psychological. Liljander and Strandvik (1995) argue that the first half are easy to manage but have a more negative connotation to the customer as they express some sort of coercion. The second half constitute of factors of perception, which are difficult to measure and manage by the organization but regarding their positive character, should be developed.

In the context of analyzing the characteristics of the relationships between the two parties it is also important to understand their typology. The following table (Table 1) presents a matrix of types of relationships between the seller and the customer,

which are conditioned by factors that determine the value of their mutual relations and the associated interests arising from the given relationships.

Table 1: Types of relationship between seller and customer

Partner	Friend	High
Rival	Acquaintance	Low

Associated interest

High   Low

Value of relationship

Source: Adapted to Walter, Ritter & Gemunden, 2001

According to the presented matrix *long-term relationship (partner)* between seller and customer occurs when the value of their mutual relations correlates with the associated common interests. Then the exchange of goods and services is intensive and takes a significant share in the total sales of the seller and in the overall purchasing of the buyer. *Friendly relationship* occurs where the value of the current mutual exchange relationships is low and when the seller realizes at the same time that there are chances of joining their individual interests. *Rivalry* appears in the case of high value of the current mutual exchange relationships, but also when there are small opportunities for the association of their individual interests, and*Acquaintance* occurs in the case of low value of the current exchange relationship and when there is a little need for the association of individual interests. Most commonly, those are routine procedures for the sale of standardized products and services.

The natural tendency of each participant in the exchange process is to maximize their individual goals and interests. The power of the participants has a central role in the exchange process.Higher levels of associated interests and a higher value of mutual relations reduce the need and relativize the use of power in regulating the relationship between seller and buyer (Končar, 2015). By crossing power and dependency, it is possible to obtain a matrix with different relationship management models (CRMs) between the seller and the customer (Table 2).

Table 2: Models of relationship management between the seller and the customer

Adjustment	Cooperation	Guidance	High
Submission	Negotiation	Domination	Low
Weak	Balanced	Strong	

Associated interest

Perceived power of the seller

Source: Adapted from Walter, Ritter & Gemunden, 2001

The matrix above shows six possible CRM models for the relationship between the seller and the customer. The first three models of guidance, co-operation and adjustment are appropriate when there is a partnership or friendly relationship between the seller and the customer. When the forces are fairly balanced the most efficient model is cooperation, as then there is a high level of joint interest between the seller and the customer, and both sides have a common interest to establish long-term relations of cooperation. The next three models of domination, negotiation and submission are in rival relationship or poor acquaintance between the seller and the customer and they are obstacles to the implementation of CRM. Therefore, in order to develop long-term relationships with customers, it is crucial that each customer is understood and viewed as a special individual, with whom a direct contact is being established.

The effects of introducing CRM can be multiple. The most important effect is certainly reflected in long-term customer loyalty retention. In this way, higher levels of customer satisfaction, higher growth rates of revenues and increase of competitive position and advantages in the market are achieved. By creating and developing long-term relationships with customers, value is generated, by which the CRM concept creates a competitive advantage for the retailer as well as for customers. This is why CRM is positioned highly on the list of priorities of today's corporate agenda, and the most commonly used tool for CRM implementation are loyalty programs. They are used in all sectors of the economy, especially in retail through special credit and other loyalty cards.

2. The concept of loyalty in retail

In the retail sector, the concept of loyalty usually appears as a means of reducing the buyer's time and effort invested in research when buying a product (Aspinall et al., 2002). Živković (2011, p. 195) emphasizes that the concept of loyalty is based on the creation of satisfied customers who return to the company and its products, positive oral propaganda by which they influence the acquisition of new satisfied customers and, most important of all, help the company to maximize its target function – to increase profits. A number of authors (Lovreta et al., 2010; Aspinall et al., 2002) define

loyalty as a two-dimensional construct made by behaviour and attitudes. Based on such observations, the company *Lidl* developed a matrix (Table 3) which can be used to classify loyalty.

Table 3: Matrix for loyalty classification

High	Spurious	High
Latent	Low	Low

High   Low

Attitudinal loyalty

Behavioural loyalty

Source: Aspinall et al, 2002, p. 264

From the matrix, it is concluded that loyalty is binary and that every retailer should strive towards the first quadrant, i.e. to establish true loyalty both in the attitude and the behaviour of the customer. In that context, Gordon (1998) proposes seven strategies for achieving the first quadrant based on strengthening the relationship by binding existing and potential customers: 1) structural bonding – the possibility of continuous ordering of the product (24h x 7 days); 2) information and control bonding – allows customers to monitor the execution of their orders; 3) brand equity bonding; 4) attitudinal bonding– requires the development of a corporate culture with a retailer that will be adjusted to customers, as well as full commitment of employees; 5) personal bonding –bonding to the personality of the seller; 6) value bonding– loyalty card-based bonding, and 7) zero option bonding. Consequently, the concept of loyalty in retail can be explained as a formalized bonding of customers that meet the conditions set by the retailer in a way to increase the amount and frequency of the purchase through rewarding returning customers, rewarding for combined purchases within the same brand for the amount of purchase, etc. (Kelligan, Moradi & Romppanen, 2007).

Kumar and Reinartz (2006) suggest that the dialogue between the retailer and the customer should take a central place in defining a loyalty program and that CRM building in retail should include the following seven guidelines (Figure 1).

Figure 1: Guidelines for developing, designing and implementing a successful loyalty program
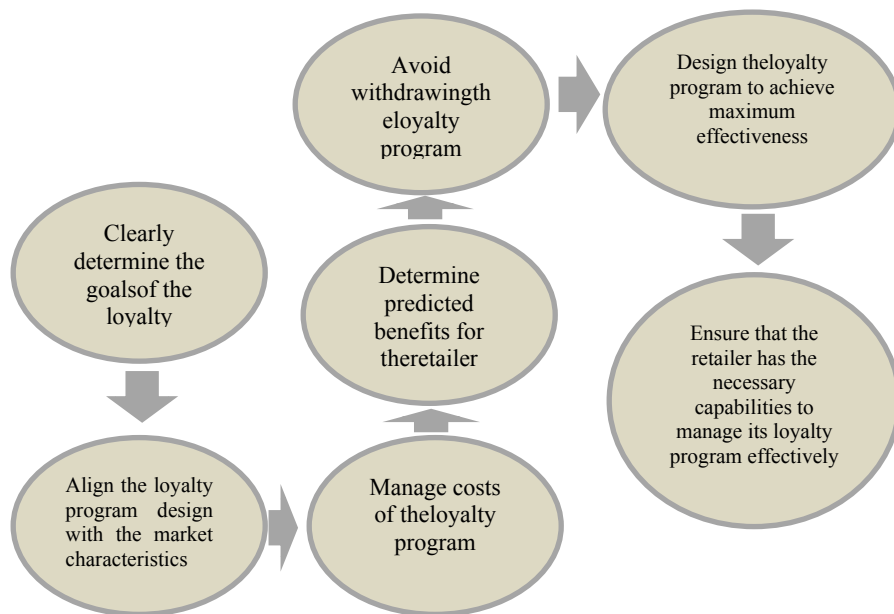
Source: Kumar & Reinartz, 2006, p.186.

The provided figure illustrates the guidelines for developing, designing and implementing successful loyalty programs in the retail sector. The loyalty program for trading enterprises should be based on a precise definition of the goal of loyalty and alignment of the program and the goal of loyalty with the characteristics of customers in a given market segment (Guidelines 1 and 2). The task of the management of trading companies (Guidelines 3, 4 and 5) is to precisely predict the costs of implementing the given program and the benefitsfor the retailer, as well as to avoid the withdrawal of the loyalty program in case the customer is not interestedin the beginning. After these steps, the loyalty program should be designed (Guideline 6) so that it enables maximal customer satisfaction and maximal efficiency of the retailers. The last guideline (Guideline 7) concerns the ability of the management to possess the infrastructure, capabilities and knowledge for successful implementation of the program.

There are a number of modalities for creating a loyalty program in the retail sector, and a retailer in accordance with the proposed guidelines, i.e.by own abilities, capabilities and predicted effects, should formulate a true program that will allow rewarding loyal customers, accelerate sales, increase the satisfaction of existing ones and attract new customers. It is therefore necessary to categorize the loyalty program.

3. Types of loyalty programs as the core of CRM strategy

The goal of every trading company is to achieve top loyalty in a critical mass of customers (Lovreta et al., 2010). In 1996, Frederick (1996, p. 12) classified the loyalty programs in the retail sector into three groups: 1) connection building programs that focus on strengthening relationships between customers and trading companies based on the provision of additional services; 2) programs to encourage more frequent contact between customers and retailers by stimulating repetition of purchases with various types of rewards for purchases that are performed regularly and frequently, and 3) membership programs including the organization of customers in groups or clubs, and the provision of such groups with special (privileged) purchasing conditions. Berman (2006) distinguishes four types of membership in loyalty programs: 1) first type - Membership is open to all customers and rewards are obtained only by using a membership card. Data is not collected and the retailer can not apply targeted marketing, 2) second type - discounts on the amount on which customers receive some free products after reaching a certain level of consumption, 3) third type - requires a database because rewards are based on cumulative purchases. Once the customer achieves a certain amount of purchase, the program offers a reward that will encourage the customer to continue to consume, and 4) fourth type - records demographic characteristics and history of purchases in databases, and compares them with each other. Such information is subsequently used for segmentation and individual marketing.

The many types of existing loyalty programs are proofs of a large number of dimensions and types of rewards within the program itself. Reinartz (2010, p. 400) describes the choice of the optimal loyalty program through the following two dimensions: reward structure and type of sponsorship. Within the reward structure, a long-term relationship with customers is based on the benefits that customers receive in the form of rewards generated by transactions during their purchase. Retailers should choose the most suitable system of rewarding in accordance with the types of rewards valorising loyalty, as well as according to the time aspect of rewarding, viewed through the prism of continuity and linearity of rewards and potential customers' requests (Table 4).

Table 4: Structure and types of rewards in loyalty programs

Types of rewards	Description of loyalty program
Hard and soft rewards	Financial rewards (hard) are distinguished from those based on psychological or emotional benefits (soft). Hard rewards include a range of price reductions, discounts, promotions, etc. Soft rewards are usually associated with a special relationship with a customer. When a customer recognizes the product as important, soft rewards usually become more important than hard ones, such as: vehicle testing, promotional gifts, gift tickets, tasting, receptions, etc.
Product proposition support (choice of rewards)	Rewards in the loyalty program can be directly related to the retailer's offer or completely unrelated. However, other loyalty programs may allow members to buy points for products that are totally unrelated to the retailer's offer.
Aspirational value of reward	Aspirational products are those whose consumption is associated with pleasure and fun. Customers feel better when enjoying luxury goods, while the retailer organizes all activities that allow saving time, money and energy for a higher level of satisfaction when buying and choosing aspirational products.
Rate of rewards	It refers to the ratio of reward value over transaction volume. It corresponds to the percentage the customer is getting in return for concentrating his or her purchases with that retailer. The customer prefers the loyalty program that brings a higher rate of reward.
Tiering of rewards	It depends on cumulative spending. There are two forms: 1) in the first case, the customer receives the same number of assets, regardless of his/her cumulative spending, and 2) inthe second case, the customer receives more assets as his/her level of spending grows.
Timing of Rewards	Retailers prefer to create redemption rules that favour long accumulation periods, which later reflect customer retention. This is called "lock-in" effect. However, customers favour a scenario with immediate reward redemption or a short accumulation period. The reward timing should be determined by the minimum redemption rules, the type of reward and the rate of reward. If the redemption time becomes too long, customers either lose interest in the program or even refuse to get involved.

Source: Adapted from Reinartz, 2010, p. 409

In his research, Liu (2007) shows that it is always necessary to consider each individual's thinking about loyalty programs. For example, there are three groups of customers: difficult ones, which gradually increase purchase and easy ones. Those customers who initially were difficult buyers were most likely to demand rewards, but the program did not encourage them to change their purchasing habits. In contrast, customers who were initially less buying or who were gradually buying more became more and more loyal to a retailer. The loyalty program has expanded the relationship between easy customers with a retailer to all other business areas.

Another key dimension of building CRM that describes loyalty programs is sponsorship. Reinartz (2010, p. 409) distinguishes three types of sponsorship within a

loyalty program: single or multiple retailers, within the sector or across sectors, and ownership. These types have some disadvantages such as loss of customer relationships and limited impact on the loyalty program strategy (Table 5).

Table 5: Types of sponsorships in loyalty programs

Type of sponsorship	Description of the loyalty program
Single or multiple retailers	Retailers can design loyalty programs that only relate to transactions with their own customers, but they can also allow their members to accumulate assets that are associated with a specific retailer. A potential disadvantage of such partnership is that loyalty programs of a specific retailer can lose significance and lose ties with customers if they include many partners. However, loyalty programs with multiple retailers are necessary when a single category does not cover sufficient capabilities for accumulation of assets.
Within sector or over sector	This loyalty program is designed so that customers can benefit and accumulate assets within a single sector (e.g., only stores of that specific retailer) or multiple sectors. For example, on the Serbian market, customers can use the loyalty program super-card in the stores of Merkator S, Idea, Mediana, Intersport, as well as at the NIS petrol stations.
Ownership	In the case of a loyalty program designed by several retailers, the ownership dimension shows who owns the loyalty program within the retailer's network. While joining a network like this makes it easier to overcome the critical stages, this membership also means that the retailer has a limited impact on the loyalty program strategy, such as positioning, branding, or selection of members.

Source: Adapted from Reinartz, 2010, p. 409

Based on the implemented rewards and sponsorship system analysis, it can be concluded that the creation of a loyalty program for long-term customer bonding in the retail sector implies the following typology: 1) type 1 - any customer receives a discount on a particular item when using his/her membership card, regardless of the history of previous purchases, in the stores of a specific retailer or stores associated with a specific retailer, 2) type 2 - it is based on giving hard (additional discounts) and soft (free products) rewards for any purchase that is higher than the usual. One of the variants of this program is, for example, rewarding each customer with one free item, after ten purchased items at full price, while the other variant enables customers to make a certain number of points, buying within (across) sectors and thus acquiring certain benefits, 3) type 3 - requires appropriate databases to track purchases and points of program members, the rate and ranking of the rewards depends on the level and scope of the purchase, and 4) type 4 - this type represents a massive customisation that is based only on points collected by customers (they can even buy them), whereby the retailers have the opportunity to send special offers, information or notifications on the basis of such collected points and individually to their members, whereby ownership is precisely defined. The prerequisite for applying such loyalty programs is the ability to

develop and maintain complex databases and efficiently manage communication and reward programs.

Conclusion

The need to research loyalty programsas a CRM strategy core in the retail sector has emerged from the increasing importance of finding adequate customer bonding strategies. A fierce rivalry and a large number of participants in the retail sector point to the need for retailers to organize all business activities through loyalty programs, thus the competition between trade companies regarding products, services and prices, is broadened to the conditions and possibilities of loyalty programs.

Conducted research has shown types of loyalty programs based on rewards, sponsorships, etc., and how retailers should design their CRM strategy, according to each type of program individually. The management of trading companies must be familiar with the characteristics of all types of programs, as well as their advantages and disadvantages in order to perform and optimize the most adequate program, fully adapted to the target segment of their existing and potential customers.

As a proposal for future research, empirical research among customers should be conducted on the practical significance of each of the offered types of loyalty programs in the retail sector of the Republic of Serbia. On the basis of the obtained results, a comparative analysis with the results of research from developed EU member states is necessary. In addition, the sample could be divided into types and conditions of loyalty programs offered by majority-owned foreign companies, domestic companies, etc. In this way, the efficiency and practical importance of the loyalty program for the establishment of CRM in the sector of the Republic of Serbia would be completely presented.

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Summary

The need to research loyalty programs as a CRM strategy core in the retail sector has emerged from the increasing importance of finding adequate customer bonding strategies. A fierce rivalry and a large number of participants in the retail sector point to the need for retailers to organize all business activities through loyalty programs. The aim of this paper is to analyse the loyalty program in the function of selecting the most adequate customer relationship strategy in the retail sector. Strengthening retailers' competitiveness on the market is realized on the basis of development and creation of an interactive and long-term relationship with customers (CRM) within which the most efficient ways of meeting the demands of modern customers are systemically identified. In this context, the basic characteristics of CRM and relational assessment are defined in the paper, the significance of the concept of loyalty as the basis of the CRM strategy is analysed and diverse ways of bonding customers based on different types of loyalty programs in retail are presented. Conducted research has shown types of loyalty programs based on rewards, sponsorships, etc., and how retailers should design their CRM strategy, according to each type of program individually. The management of trading companies must be familiar with the characteristics of all types of programs, as well as their advantages and disadvantages in order to perform and optimize the most adequate program, fully adapted to the target segment of their existing and potential customers.