The card game that calls for high stakes

With Nectar under the spotlight, Michele Witthaus explores whether retailers' outlay for loyalty might prove too costly

Loyalty card schemes have now been a feature of UK grocery for a decade, ever since Tesco secured first-move advantage with Clubcard back in 1995. But despite their ubiquity, doubts have persisted over whether they deliver genuine benefits to the shopper or adequate returns to retailers on the significant investments involved.

Last week, Nectar's major sponsor, Sainsbury, denied it was thinking of pulling out of the scheme on the grounds that it was too expensive (The Grocer, news p5, February 12). So do they really pay their way?

Retailers refuse to disclose their level of investment in such schemes, preferring to draw attention to figures showing the benefits cardholders enjoy. However, by Sainsbury chief executive Justin King's own admission, running costs for Nectar equate to half the chain's marketing budget. Meanwhile one loyalty specialist says of Clubcard: "You don't get much change from £300m a year." Indeed, some operators admit to having shaved back rewards because of the cost involved.

Another big challenge is measuring the return on that investment, says Merlin Stone, business research leader, IBM Business Consulting Services. "Sometimes the return represents promotional spend switched into the scheme instead of less-targeted forms of sales promotion. Figures are normally very confidential, sometimes because companies are not sure what they are."

Some analysts also question how much value individual Nectar sponsors get out of their relationship with others in the group. Research by customer intelligence company Wegener DM Results into the target markets of the four major Nectar sponsors suggests a negligible overlap between the different brands, says MD Roy Barker.

But, says Brian Sinclair, client services director of Nectar operator Loyalty Management UK, the Christmas 2004 Nectar points update mailing alone generated over £40m incremental sales for sponsors. "Our sponsors are attracted to the economies of scale we can offer them," he says. "They can share the cost of mailings, and the average UK household can now collect Nectar points on over 40% of their total spend."

One thing they can be sure of is the popularity of loyalty schemes with shoppers. Research undertaken for The Grocer by HI Europe last month revealed that four-fifths of shoppers use loyalty cards for their grocery shopping (see news). Tesco Clubcard was the most widely held and frequently used card among those surveyed, followed by Nectar. Boots Advantage took third place with more than half of all loyalty card users claiming to use the card.

HI Europe senior researcher, Caroline North, says she is not surprised that Clubcard now has 11 million active users and an 80%-plus rededemption rate on quarterly vouchers issued to cardholders: "Tesco has really caught the market and as a consequence has the biggest share of loyalty," she says. "Bearing in mind that half of 16 to 24-year-olds said they were influenced about where to shop by their cards, this could play a vital part in future loyalty."

Nectar, launched with Sainsbury, Barclaycard, Debenhams and BP in 2002, still has work to do to optimise loyalty levels, she suggests. But there is no doubting its potential pull. At the moment, 17 companies share the costs and benefits of the scheme and points are available at 6,000 locations, making it the UK's biggest loyalty programme with the participation of more than 50% of all households. It recently took on its first online sponsor (Ebookers) and poached Beefeater from Tesco. To date Nectar has given back more than £340m worth of rewards to collectors.

The data it provides also allows a better understanding of customers and more targeted offers than possible with its previous scheme, argues Leigh Rengger, Nectar marketing manager at Sainsbury. "Through direct marketing, we can tailor offers and communication directly to the people who will benefit most. With Nectar we have 75% more mailable customers than under Reward."

And Nigel Lawrence, loyalty and communications expert with Lawrence Pritchard, points out that Sainsbury will think long and hard before dropping the scheme. "The results of its loss of Air Miles to Tesco were clear," he says.

While Nectar is the biggest Boots has arguably taken loyalty a step further with Advantage Card, the most used scheme in the country with 15 million cardholders. It has worked hard to protect its share of consumer spend against competition from the major supermarkets. It has also tested the limits of customer trust by including an optional organ donor registration element. This takes it into the realm of a lifestyle statement with value beyond just shopping for points.

Changes can be made to a scheme without jeopardising customer loyalty. The Co-operative Group's Dividend scheme, launched in 1998, originally offered a 5% reward on own-label products only, but changed in 2002 to offer 3% on all own brand and fresh food and 1% on branded products.

"We conducted exhaustive trials before changing our rewards," says Ged Carter, general manager for marketing in the Co-operative Group. "These demonstrated that we could increase customer participation in the scheme, without increasing the level of reward paid to the average cardholder."

Of course, you don't need a loyalty scheme to build loyalty, points out Nick Gladding, senior analyst at Verdict. "Asda dropped its scheme yet has managed to maintain market share growth and has a good understanding of its customers."

But the consenus is that despite the high cost of running these schemes, they can generate real loyalty – the challenge is how to optimise it. G