

2023

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Lynn, Kennedy, "The Influence of Loyalty Programs on Hotels" (2023). *Hospitality Graduate Student Scholarship*. 33.

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The Influence of Loyalty Programs on Hotels

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HOSP 6059

Professor Paul Howe

October 7th, 2023

Abstract

This study aims to create a working paper on the best practices of different ways loyalty programs can influence the hospitality industry, specifically in hotels. The hospitality industry is evolving daily, highly competitive, and customers seek more than genuine experiences. To differentiate themselves from competitors, hotel companies are developing unique ways to reward customers for repeat purchases and have relied heavily on loyalty programs to keep up with this trend. The study discussion indicates the best practices of a loyalty program used by various hotel companies.

In any business, customer loyalty is a factor that drives the overall success of a company. Capturing customer loyalty can be challenging because many factors affect how and what a customer is loyal to. Hotel firms that have developed a robust loyalty program can expect improved customer relationships and brand loyalty through the loyalty program, which positively impacts a hotel's long-term financials. Also, a customer's perception of the value of the loyalty program and the switching cost also impact customer loyalty to a brand.

History of Loyalty Programs

According to Ta-Yao, Loyalty programs began in the late 1700s as some U.S. merchants gave their customers copper tokens to redeem in future purchases. This idea stuck and became the foundation of the Spend and Get customer loyalty model (Ta-Yao, 2020). This concept rewarded customers for their purchasing decisions, which turned out to be attractive to customers and businesses. This concept started customer loyalty programs and paved the way for modern companies to innovate and create value within their business. In the 1980s, loyalty programs focused more on rewarding customers and were designed to acquire customer data, especially for the airline industry (Ta-Yao). American Airlines introduced the first modern loyalty program, a frequent flier program. This frequent flier program provided customers with new flight experiences and is recognized for its innovation. Today, all airline companies have their frequent flier programs. Most have agreed to share air miles to attract more customers and retain the current ones (Ta-Yao, 2020). This modern customer loyalty program has been applied in many industries, such as hotels, hospitality, and car rental (Ta-Yao, 2020).

Hoteliers were mainly partners of airline companies in the beginning (Laškarin, 2013). Once they saw the benefits of loyalty programs to the customer and the business, hoteliers began designing loyalty programs that fit their businesses. The idea is to balance what guests want and what they are offered as a reward while finding other programs whose services guests will use too (Laškarin, 2013). Hotels rely more on loyalty programs than airlines to keep customers returning because hotels have different business models compared to airlines.

Introduction

Inspired by the airlines' success after launching the modern loyalty program, hotel chains took the time to develop successful loyalty programs for their companies. With increasingly intense competition among hotels, this was a strategic way for hotels to ensure the guest was put first. This allowed companies to identify guests' needs and wants. Many customers voiced that their favorite go-to places are the ones that offer incentives (citation). ARTICLE defines loyalty programs as a structured marketing effort that rewards and encourages loyal behavior, hopefully benefiting the firm. To establish positive customer relationships, businesses must manage marketing strategies effectively to satisfy customer needs and build customer loyalty (citation). Outside of building customer relationships, loyalty programs have influenced brand loyalty, customer perception value of the brand, switching costs, and financials.

Literature Review

Loyalty Programs can be used as a CRM strategy. This strategy can enhance customer loyalty and increase a firm's long-term profitability (Gandomi & Zolfaghari, 2013). This study (Gandomi & Zolfaghari, 2013). developed an analytical model to analyze the effect of customers' valuation and post-purchase satisfaction level on a loyalty program's profitability. The collected solutions provide valuable insights into customer satisfaction's effects on loyalty programs' profitability. The results from this study revealed how customer satisfaction plays a critical role in the profitability of loyalty programs. If a firm maintains customer satisfaction, offering a loyalty program can become optional.

Loyalty Program Designs

According to Siddiqui (2022), there are four types of loyalty programs: tiered loyalty programs and subscription, value, or points based. The information below is cited from (Siddiqui, 2022).

- Tiered loyalty programs offer benefits to customers based on the tier they reach. The higher the tier, the more the reward or perks. Some programs are titled silver, gold, platinum, and diamond tiers to encourage customers to spend more.
- Subscription-based loyalty programs are when customers pay an initial, ongoing, or yearly fee to join this program. Businesses seeking customers for a set time use this type of program.
- Value-based loyalty programs are the kind of programs that do not offer customers prizes like discounts or other advantages. Instead, this program promotes the company's values and, ideally, corresponds with the intended target audience. This loyalty program promises to provide a portion of business earnings to one or more charities, letting customers select the group that closely matches their values.
- A point-based loyalty program gives customers points every time they spend. Customers can choose to redeem their points for merchandise or discounts after they reach a particular amount.

Areas of Influence

Brand Loyalty

As reported by Harvard Business Review (2020), companies with high scores on two market research metrics, brand and customer loyalty, grow revenue 2.5 times faster than their competitors (Markey, 2020). Brand loyalty is a long-term commitment from a customer to repeat purchases of a particular brand, not depending on price. The main difference between brand and customer loyalty is that customer loyalty is money-based. When customers choose to be loyal to a specific brand, they believe that this particular brand produces both higher quality and better service than its competitors. For hotels to flourish in such a competitive market and maintain brand loyalty, marketing departments must utilize tactics such as monitoring buying trends, analyzing spending data, and designing advertising campaigns targeting existing customers that are loyal and attract customers to become loyal. A loyalty program is a strategy that hotels can use to create and maintain a brand-loyal customer base that can take businesses to the next level. As stated before, establishing an LP is a way to reward existing customers for their business, which is the direct way to build brand loyalty (Markey, 2020). Investing in the retention and loyalty of existing customers can be less expensive than marketing to new customers. Especially for premium-priced brands, an exclusive discount for LP members can be the right incentive to choose the pricey brand over a less expensive option.

Perceived Value

An empirical study (citation) has identified the critical role of the perceived value of a loyalty program in building customer loyalty. Koo et al. (2020) proposed that customer value

perception is necessary for developing brand loyalty through the LP. Perceived value is “a customer's overall assessment of the utility of a product (or service) based on perceptions of what is received and what is given (Koo et al., 2020).” According to Koo et al. (2020), perceived value has been measured primarily in multiple-item scales such as functional, psychological, and external values. Functional value can be defined as “the value derived from accomplishing some pre-determined instrumental purpose” (Koo et al., 2020). The functional value is marked as the critical factor of consumer decision, which contains the convenient use of an LP and flexibility of terms and conditions. Psychological value involves intangible benefits (citation), such as an emotionally attached recognition to members, which is essential for hotels to increase customer purchases and the overall perception of values that conduct business with that hotel. External value includes benefits delivered through external parties in the partnership and point pooling that permits members to transfer points to other programs, such as frequent flier miles. These three values have proven to be prerequisites to explain how the perceived LP values can impact loyalty (Koo et al., 2020). Customers usually want to accumulate points to redeem with the same program, so hotels must understand how customers perceive the value of each LP to create a successful LP. Koo et al. (2020) verified that there is a relationship between the perceived value of a loyalty program and customer loyalty within hotels.

Switching Barriers

Researchers have claimed that loyalty programs can create loyalty for the hotel brand by increasing customers' perception of switching difficulties (Koo et al., 2020). Switching barriers can be defined as the consumer's assessment of the resources and opportunities needed to perform the switching act or the constraints that prevent the switching act (Koo et al., 2020).

Recently, research has shown that switching barriers are a crucial factor in consumer switching and the success of a business. The barriers that act as switching barriers are switching costs are relational investment and alternative attractiveness (Koo et al., 2020). Switching costs arise when customers perceive a psychological or financial burden related to leaving a particular hotel. According to Koo et al. (2020), switching costs can increase operational profits by securing loyal guests through the loyalty program.

Customer Relationships

Customers now seeking more than genuine experiences from hotels have changed the hotel industry companies, causing them to reassess what customer loyalty means and how to obtain it. Before COVID-19, most loyalty programs worked similarly by rewarding customers and spending more, but things have changed. Today, hotels have had to become more strategic and are developing loyalty programs to motivate customer relationships. To encourage these relationships, hotels use customer retention, not purchase frequency, as the key metric to optimize (Wertz, 2022). Hotels began to recognize the importance of building dynamic relationships that extend far beyond a transaction. When brands focus on creating deeper connections with customers beyond simply offering genuine service, research shows that 74% of consumers are more likely to buy from that brand (Wertz, 2022). Another benefit of these newly developed loyalty programs is that they can be used to create personalized communication **How?** (Wertz, 2022). Companies track the data recorded through loyalty programs and add it to their marketing mix. This enables hotels to create customer databases to use loyalty programs as a critical customer relationship management tool marketers use to identify, award, and retain customers (Wertz, 2022).

Financials

Research from Gandomi & Zolfaghari, (2013) has shown that customer satisfaction plays a significant role in the profitability of loyalty programs. A new way hotel has enhanced their loyalty programs and increased profitability is through co-branded credit cards. Co-branded credit cards cross between a store card and a rewards card, backed by a major card issuer (Gravier, 2020). These cards can be used as regular credit cards and accumulate points at the same time. An example is the Hilton Honors American Express Aspire card. This has been reviewed as a grand hotel card for someone who visits Hilton Hotels regularly and wants to maximize the benefits of their Hilton Honors program.

Research Methodology

The research method that would be most appropriate is a working paper, secondary research, and a subjective analysis to present best practices. There is a plethora of research on loyalty programs, but there needs to be more direct influences a program can have on a hotel or the factors that support this influence.

Research Findings

The findings showed that loyalty programs are beneficial to hotels in many ways. There is a trend that customers expect more than hotel experiences and are now seeking rewards, which

is precisely where loyalty programs come in. The most common design loyalty programs hotels use is tier-based. Tier-based hotel loyalty programs (THLPs) are broadly used to encourage consumption and develop customer-firm relationships (Yu et al., 2022). Many hotels give their loyalty program members quick feedback via mobile apps to update members' progress toward keeping their membership level. Research has identified two broad feedback formats THLP uses: looking-back feedback, which records the number of hotel stays that a loyalty program member has accumulated, and looking-forward feedback, which reports the number of hotels stays needed to retain current tier-level (Yu et al., 2022).

However, it has yet to be proven which feedback format is more effective in appealing to high-and-low-tier members to retain their tier level. For members who actively pursue various tiers or goals, the looking-back feedback is more motivating for low-tier members to retain their level. Those members tend to put in less effort and are less committed to maintaining their current tier level. The looking-forward vs. looking-back feedback motivates higher-tier members to retain their levels because they have made more effort to go through the tiers. Other findings show that if the LP is perceived positively, it can affect customer loyalty. Also, there is a psychological value that explains the extent of emotional attachment to the program and validates the substantial impact on loyalty (Koo et al., 2020).

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