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Loyalty program rewards and their impact on perceived justice, customer satisfaction, and repatronize intentions

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ABSTRACT

This study examines three types of rewards in a retail loyalty program context (under-reward, equity-reward, and over-reward) and their impact on perceived distributive justice, customer satisfaction, and repatronize intentions. The results from a between-subjects experiment showed that equity-reward produced higher levels of perceived distributive justice than both under-reward and over-reward. Moreover, equity-reward and over-reward produced higher levels of both customer satisfaction and repatronize intentions than did under-reward. Yet there were no differences in satisfaction and repatronize intentions for equity-reward and over-reward. These outcomes suggest that loyalty programs have the potential of not boosting members' loyalty, at the same time as they may reduce loyalty among non-members.

1. Introduction

Loyalty programs have become common in many service and retail industries (Melancon et al., 2011), and some empirical studies suggest that they may have a positive impact on customer loyalty (Leenheer et al., 2007; Liu, 2007; Meyer-Waarden, 2007). These programs typically provide the member with preferential treatment, in the sense that members receive a better deal than non-members. Moreover, researchers have identified a positive association between receiving preferential treatment and variables such as customer satisfaction, customer commitment, increased purchases, positive word-of-mouth, and customer share (Gwinner et al., 1998; Lacey, 2007), thus suggesting that preferential treatment produces benefits for both (a) the customer who receives this treatment and (b) the firm providing the customer with the treatment.

However, and as a main thesis in this paper, we believe that existing research on the effects of rewards from loyalty programs, and on preferential treatment effects, has overlooked the possibility for inter-customer comparisons. Given that we humans are hardwired to make comparisons in resource allocation situations, we assume that loyalty programs designed in the typical way (i.e., members are given preferential treatment) induce comparisons. We also assume that this is particularly likely when loyalty rewards are distributed to members in social settings in which members and non-members can see – and compare – the distribution of the rewards vis-à-vis each other. Moreover, we believe that the rapid development of social media, in which customers often share purchase-related information, are making customer-to-customer comparisons increasingly common. In relation to many previous studies of loyalty programs, in which the customer is depicted as a socially isolated individual, we are thus explicitly concerned with the potential for inter-personal comparison opportunities to influence the effects of loyalty program rewards.

The purpose of this paper, then, is to examine the effects of preferential treatment stemming from a loyalty program in a situation explicitly allowing for inter-customer comparisons of rewards. Three effect variables are included: perceived justice, customer satisfaction, and repatronize intentions. We assume that inter-customer comparison is particularly likely to evoke justice perceptions. In general, this variable has to do with the extent to which individuals perceive that the exchange of resources between themselves and another party is fair (Maxham and Netemeyer, 2003), and it should be seen as one of several parts of the individual's overall framework for assessing moral aspects of exchange (Carlson and Kacmar, 1997; Ferrell and Gresham, 1985). Our focus is on one specific perceived justice type, distributive justice, which has to do with individuals' perceptions of justice in terms of the distribution of tangible outputs from resource exchange activities (Cohen-Charash and Spector, 2001; Maxham and Netemeyer, 2002; Tax et al. 1998). In overall moral terms, then, we focus on consequential aspects rather than deontological aspects.

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In our case, the output is the price offered to a focal customer in relation to the price offered to another customer. More specifically, we examine three outcomes derived from equity theory and in a setting in which exchange takes place between a retailer, a focal customer and another customer: (1) the focal customer (a non-member of a loyalty program) does not receive a lower price while the other customer (a member) receives it (*under-reward*), (2) the focal customer (a non-member) does not receive a lower price and the other customer (also a non-member) does not receive it (*equity-reward*), and (3) the focal customer (a member) receives a lower price while the other customer (a non-member) does not receive it (*over-reward*).

In an experiment in a retail environment, in which customers were able to compare outcomes, we show that both the customers who received over-rewards and the customers who received under-rewards viewed the outcome as less just than the customers who received the same treatment as other customers (equity-reward). We also show that customer satisfaction and repatronize intentions were affected. More specifically, being under-rewarded significantly reduced satisfaction and repatronize intentions in relation to equity-reward and over-reward, thus indicating that the causal potency of the rewards was highest in the under-reward condition. An additional and important result is that over-reward did not produce higher levels of satisfaction and repatronize intentions than equity-reward. In other words, given the opportunity for inter-customer comparisons, we show that a loyalty program has the potential of (a) reducing satisfaction and repatronize intentions among non-members and (b) *not* boosting satisfaction and repatronize intentions among members. This potential means that one may question the effectiveness from a loyalty-building point of view.

2. Theoretical framework and hypotheses

In the following sections, we develop arguments and hypotheses regarding the consequences for customers of receiving versus not receiving preferential treatment stemming from a loyalty program. The effect variables are perceived distributive justice, customer satisfaction, and loyalty in terms of repatronize intentions.

2.1. Loyalty programs and preferential treatment

Since the end of the 1980s, many firms (and many researchers) believe that customer loyalty is positively associated with profitability. Therefore, it is not surprising that many firms strive to improve customer loyalty, and one of the most popular ways to do so is by creating loyalty programs. Such programs have indeed proliferated and many contemporary consumers in Western countries are members in loyalty programs (Berman, 2006; Melancon et al., 2011; Zhang and Breugelmans, 2012). The general idea is that rewards to members would make them more loyal, an idea that has received some empirical support (Leenheer et al., 2007; Liu, 2007; Meyer-Waarden, 2007). Typically, loyalty programs are designed so that members receive preferential treatment in relation to non-members (often, they are also designed so that different levels of membership are subject to different treatment).

It should be noted that few authors dealing with loyalty programs have discussed the possibility that different treatment of different customers may elicit justice perceptions. Presumably, one reason is that preferential treatment can be seen as an expression of the traditional (and seldom questioned) marketing idea that markets comprise different segments—and that different segments should be subject to different offerings. Indeed, given an increasingly fragmented marketplace, it would appear somewhat odd to question the need for segmentation. Nevertheless, some authors have noted that there is an increasing awareness in firms that all customers are not equally profitable, and that this is often followed by attempts to treat the most profitable customers better (Mayser and von Wangenheim, 2012; Schudson, 1993). Similarly, O'Brien and Jones (1995) argue that the firm considering a loyalty program needs to accept that not all customers are equal. Shugan (2005) is even more explicit from a justice point of view when he argues that loyalty programs providing frequent customers with preferential treatment exercise de facto discrimination against infrequent customers. Similar views are expressed by Brady (2000), who argues that markets are evolving towards a state of "consumer apartheid", and by Drèze and Nunes (2009), who claim that loyalty programs serve to segregate customers. Less attention, longer waiting time, fewer "extras", and higher prices are what can be expected for customers who are non-members. Not every customer, then, is "king" in the contemporary marketplace (Laczniak and Murphy, 2006). Therefore, we believe that preferential treatment of some customers, within the frame of a loyalty program, is a sterling example of a situation in which justice perceptions can be elicited.

2.2. Perceived distributive justice effects

Human beings are programmed to make comparisons with others when the possibility to do so exists (cf. Drèze and Nunes, 2009; Moschis, 1976), and we assume that preferential treatment is likely to result in such comparisons. We also assume that a main outcome of such comparisons is an assessment of moral issues. Several bases exist for moral assessments, and justice is generally considered to be one of them (Carlson and Kacmar 1997; Shultz and Brender-Ilan, 2004). Moreover, several types of justice may be evoked by a comparison (Aggarwal and Larrick, 2012; Maxham and Netemeyer, 2003; Tax et al., 1998), but we assume that distributive justice perceptions are particularly likely to be evoked, because they are related to the (often highly visible) consequences (i.e., the output) of resource allocation. In overall moral terms, then, our output focus can be seen as dealing with consequential aspects of moral assessments as opposed to deontological assessments (cf. Ferrell and Gresham, 1985), which represents a limitation we return to later on.

In any event, studies of resource allocation in prehistoric society show that our ancestors took the size of the output very seriously and used elaborated rules for food sharing (Flannery and Marcus, 2012). Moreover, several primates, particularly chimpanzees, have been shown to have a sense of justice, thus suggesting evolutionary benefits of fair allocations—particularly in terms of fostering cooperative interaction between individuals (Brosnan, 2006; Price and Brosnan, 2012). Justice perceptions are particularly likely to be evoked, and to have an impact on other variables, in social settings characterized by long-term relations between members (cf. Aggarwal and Larrick, 2012). Yet we assume that justice perceptions are easily evoked also in situations in which strangers make comparisons of resource allocation outcomes—such as in service encounters occurring in the presence of other customers (cf. Söderlund et al., 2014).

The notion of distributive justice perceptions used here is derived from equity theory, in which inter-personal comparisons of outcomes is a crucial point of departure. Equity theory states that a resource allocation involving several individuals would result in that a person P compares his/her ratio of rewards to inputs against that of another individual O (Adams, 1963; Ajzen, 1982; Alwin, 1987; Konow, 2003; Pritchard, 1969). Three main outcomes of this comparison are covered by equity theory. If P perceives O's reward/input ratio to be equal his or her own, then P will perceive that justice is at hand. This is called *equity-reward*. If P perceives