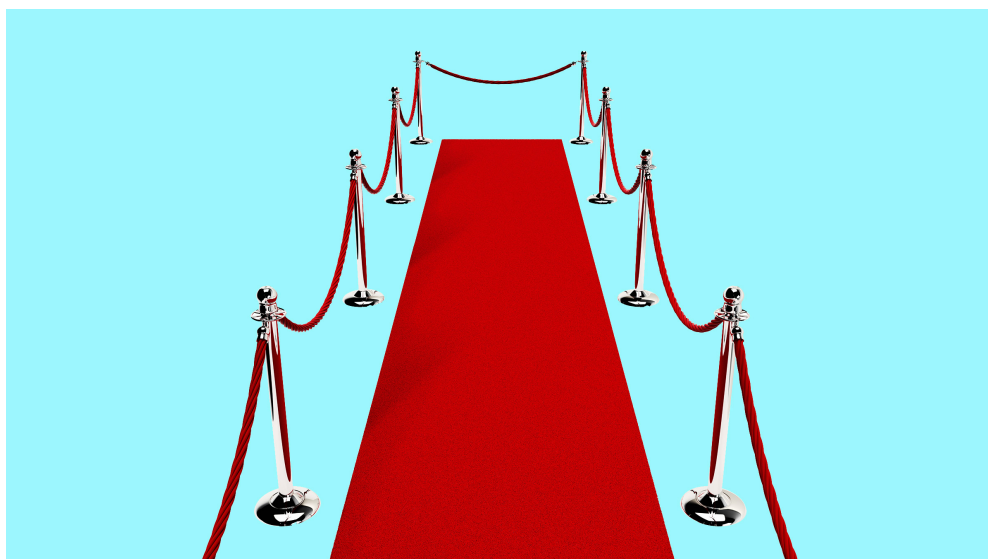




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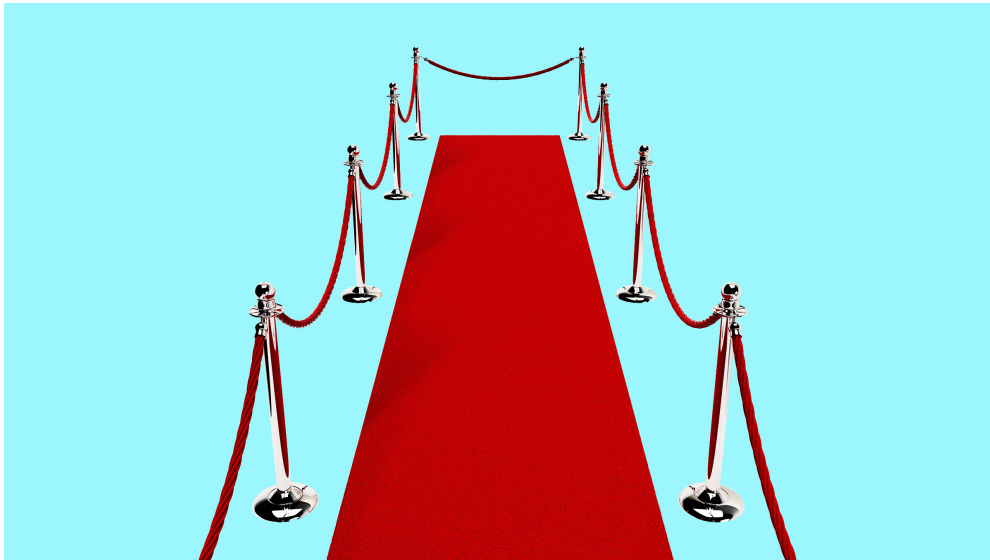
When — and How — to Build Hurdles into a Loyalty Program

by Yacheng Sun, Jonathan Z. Zhang, and Dan Zhang

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Have you ever signed up for a rewards program, only to discover several months later that your points expired before you had a chance to use them? If so, you're not alone. Research shows that loyalty program members lose up to a third of the savings they could have earned from these programs due to *redemption hurdles*: policies such as expiration dates, spending minimums, and other requirements that hinder customers from actually reaping the benefits of membership.

These redemption hurdles are extremely common. In fact, we conducted a [survey](#) with the top 100 U.S. retailers and found that 85% of the rewards programs these firms offered included some form of hurdle. For example, many [airlines and hotel chains](#) stipulate the minimum number of points required for a free plane ticket or night of stay, and they forfeit members' miles and reward points after a period of inactivity. These sorts of policies may incentivize customers to spend more — but they have also [been cited](#) as a major source of frustration for customers, and may even push some to cancel their memberships. Is it possible for businesses to reap the benefits of incorporating redemption hurdles into their rewards programs without alienating customers?

To explore this question, we built an [economic model](#) to determine how redemption hurdles impact customers' purchase and reward redemption decisions. We also analyzed key features of the top 100 U.S. retailers' reward programs and conducted a series of in-depth interviews with senior executives in order to better understand how real-world companies are implementing these programs, what tends to work, and what doesn't. These analyses demonstrated that redemption hurdles can in fact be a win-win for both companies and their customers — but only when they're set up the right way.

Redemption hurdles enable effective price segmentation.

Specifically, we found that redemption hurdles can provide a mechanism for retailers to effectively price segment their customers in contexts where actually listing different prices is infeasible, ultimately enabling a closer match between company offerings and customer needs. To do this, firms can use past purchase histories, survey results, or other market research data to determine their customers' *willingness to pay* (i.e., how much they are willing to spend) and *purchase frequency* (i.e., how often they are likely to make a purchase). Once the firm has a sense for the ranges of these two key metrics, it can create redemption

hurdles that split customers according to their frequency and amount of spending, meaning that these different customer groups will be charged different effective prices.

For example, if a coffee shop rewards members with a free cup of coffee for every four cups purchased within a certain date range, the effective price per cup paid by a customer who makes use of the reward will be about 20% lower than that of a customer whose reward points expire before they reach four cups. The redemption hurdle allows the firm to offer a lower effective price to low-willingness-to-pay customers who make frequent purchases, while still charging a higher price to high-willingness-to-pay, less-frequent purchasers.

Conversely, if the shop chooses not to use an expiration date, it will be effectively setting the same price for all customers — which means either pricing out low-willingness-to-pay customers, or leaving money on the table by failing to charge as much as high-willingness-to-pay customers would be willing to pay.

Of course, this only works if you set the right redemption hurdles — and the optimal thresholds will depend on both your industry and your specific customer base. In general, the more frequently customers buy your product, the shorter the expiration term should be. For example, most people buy groceries every week, but they only fly a few times a year, explaining why grocery stores tend to set much shorter expiration terms than airlines. Indeed, this is borne out in our data: Among the top 100 U.S. retailers, the average expiration term for grocery store reward points is about a week, while specialty stores such as GameStop and Dick's Sporting Goods give you up to a year to use your points.

But it's not just about average purchase frequency. Our analysis also demonstrated that if customers vary widely in their purchase

frequencies, then firms will benefit from a shorter expiration term, while if customers have similar purchase frequencies, a longer expiration term is more advantageous. This is because it's harder to segment customers when their purchase frequencies are more similar, and as such a longer expiration term is needed to effectively separate them into meaningful groups.

Redemption hurdles can be a win-win — but only if they're set up right.

To be sure, there are still potential risks associated with redemption hurdles. First, our analysis demonstrated that they can be mutually beneficial if set up correctly — but they can also backfire if expiration terms or other thresholds aren't optimized to meet customer needs. For example, when rideshare platform Didi [launched](#) a new rewards system in which drivers had to complete more than 30 trips per week to unlock benefits associated with a top-tier status, many complained that this reduced take-home pay and incentivized unsafe driving practices, ultimately pushing drivers to competitors' apps.

Second, as with any customer segmentation strategy, your ability to design effective redemption hurdles will hinge on your access to data regarding individual customers' prior behavior. That said, we found that hurdles can be effective even with minimal insight into customer preferences, and some firms have been able to achieve success with programs based purely on an analysis of the general composition of their market, without individual-level information regarding their customers' actual purchase frequencies or willingness-to-pay. While many personalization efforts require extensive personal data, redemption hurdles can essentially offer a shortcut, providing firms with many of the same advantages without the need for costly investment into collecting and protecting customer data.

And finally, even if the program is designed well, poor communication can be a major stumbling block. To avoid frustrating customers, firms should explain reward program structures clearly and transparently, and avoid jargon, complicated rules, or fine print. For example, Old Navy's reward program recently came under fire for being unnecessarily complex, confusing and angering loyal customers.

Similarly, firms should ensure that members are fully aware of expiration terms, and that they are given sufficient reminders before their points expire. For instance, many of the hotel chains in our data had 24-month expiration terms, but they would begin sending monthly reminders at 12 months, and then increase to weekly notifications during the last two months (these reminders not only reduce the risk of surprising customers with lost rewards, but also boost the chances that they will make a purchase, again creating a win-win). Some chains would also offer customers options to redeem their points some other way if they weren't going to need a hotel room before their points expired, such as purchasing merchandise or gift cards, making a donation, or extending the expiration date, further bolstering customers' trust and satisfaction levels.

Ultimately, there's no perfect design for a rewards program. But with an intentional, data-driven approach, firms can build redemption hurdles that are a true win-win, creating substantial value for both companies and their customers.



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