



Loyalty: moving digital wallets
to the mainstream

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Going mainstream: mobile wallets and the loyalty “beachhead”

Back in the early 1990s a landmark book called *Crossing the Chasm* explored the challenges facing high-technology markets as they move from early adopters to mainstream acceptance. Mainstream users’ needs are radically different from those of early adopters (the technology enthusiasts and visionaries). What’s needed, the author argued, is a beachhead for exciting new technologies to gain traction in the mainstream market.



“The point of greatest peril in the development of a high-tech market lies in making the transition from an early market dominated by a few visionary customers to a mainstream market dominated by a large block of customers who are predominantly pragmatists in orientation”.

Geoffrey Moore,
Crossing the Chasm

History is filled with such occurrences. MP3 digital storage was introduced to the public in 1993, but it wasn’t until Napster in the late 1990s and iTunes in 2001 that the era of digitally-stored (and digitally-purchased) music began. File-sharing sites like Napster and downloading and storage sites like iTunes revolutionized how we listen to, purchase and share music.

The mobile wallet industry is at a similar tipping point. Early adopters have come on board, but they are struggling to gain popular acceptance. However, we believe that loyalty can be the enabling mechanism that fundamentally alters how consumers shop and transact and how merchants view payments.

The powerful reality is this: digital wallets are gaining traction but have yet to achieve mainstream appeal. The dollars just aren’t there yet. However, thanks to their ease-of-use and widespread popularity, loyalty programs are digital wallets’ ideal enabler to mainstream success.

Mobile wallets and loyalty programs could herald the ultimate technological union.

Loyalty programs: the cool kid on the block

We believe that loyalty programs will drive mobile wallets to the mainstream because of their ubiquity and the incredible consumer engagement that they have fostered. They are known quantities: time-tested customer engagement methods whose earliest iterations date back over a century. With nearly 3 billion US loyalty program members in 2012 (a 27% increase from 2010), the average American household belongs to 22 programs (Colloquy, 2012). In 2011, when the latest figures were released, the loyalty industry doled out \$48 billion in rewards currencies. Considering recent membership growth, this figure is likely even higher today.

A growing industry

Largely due to the pioneering efforts of American Airlines and its AAdvantage® frequent flyer program, the first of more than 130 FFPs with 150 million members, now almost every industry from travel to retail to financial services has its own card-based loyalty programs. And since 2006 all major sectors have recorded impressive membership growth.

YoY Increase, 2010 to 2012

Financial services	130%
Specialty Retail	109%
Hotels	73%
Airlines	46%

Source: Colloquy 2013 Loyalty Census

Earn behavior drives engagement

And this isn't just about using those points for redemption of free goods and service. Numerous studies have shown incredible engagement in the act of earning points. The accumulation of points can be exhilarating and genuinely fulfilling, a testament to rewards programs' game-like attributes. According to Points' own research:

73%

of consumers wish there were more ways to earn points and miles in their favorite programs

66%

of consumers report they'd like to earn points and miles faster

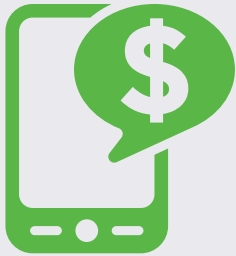
78%

of consumers said they'd be more likely to make a purchase if offered points or miles

Mobile wallets: a pioneering but challenged new technology

Compared to loyalty programs, mobile wallets aren't just the new kids on the block; they're infants in the digital cradle. That being said, the technology has come far since the earliest forms of mobile payment from over a decade ago.

The mobile wallet and mobile payment industries continue to evolve. According to market research firm Berg Insight:



- There were nearly **7.5 million** North American mobile wallet users by the end of 2012 using at least a single-merchant mobile payment systems like the Starbucks app (however, of that figure, only a few hundred thousand were using multi-merchant mobile wallets).
- This usage amounted to **\$500 million** in in-store spending.
- These figures are predicted to grow to **29 million** mobile wallet users and **\$44 billion** in transactions by 2017.
- NFC-enabled phone shipments surged 300% in 2012 and are forecast to grow to **1 billion units** within four years.

Forrester Research is even more optimistic. It predicts \$90 billion in US mobile payments by 2017, up from \$12 billion in 2012.

Despite the apparent growth, differentiating mobile wallets and mobile payments becomes a critical distinction.

Mobile payments (like buying a song through iTunes on your phone or donating to the Red Cross through SMS) are better understood and more accepted by the public partially due to their decades-long development. Mobile wallets, while related to mobile payments and single-merchant mobile apps, still remain foreign to many consumers and adoption challenges persist. Only 16% of respondents to a recent Chadwick Martin Bailey survey had used a mobile wallet in the last six months.

In their current format, mobile wallets face three critical challenges:



Technology standardization

Between QR codes, NFC or some kind of swipe-and-tap approach, defining what constitutes a mobile wallet transaction is difficult. Varying payment methods translate into merchant confusion. Which point-of-sale readers do merchants need and which make the most sense to invest in? Up to this point, with so many mobile wallet players vying for a piece of the action, the answer for many merchants has been not to invest at all.



Physical credit cards & loyalty programs are the best game in town

There's no getting around this challenge. Credit and loyalty cards work extremely well. Credit cards are universally accepted at any business with a card reader. Co-branded credit cards (credit cards with built in loyalty accrual) are just as ubiquitous, creating even more incentive for use. The technology will mature only when mobile wallets are as easy to use as today's physical wallets.



Security issues & big data abuse

Consumers fret about their personal data being hacked or stolen and fear too much sharing of data will result in cross-industry marketing bombardment. In addition, the latest ICM Research finds 51% of consumers would use a mobile wallet if such fears were mitigated. Even with advances like Apple's fingerprint smartphone lockout, concerns about having too many features built into one product persist. Lose your phone and you lose your wallet.

Despite these challenges, numerous studies indicate widespread support for the idea of mobile wallets even if relatively few merchants and consumers have actually embraced the technology. But due to a flood of competitors (there are dozens of mobile wallet developers), point-of-sale technology fragmentation and nagging data security issues, mobile wallets' would-be converts don't know where to begin or which platform to embrace. The industry is on the verge of greatness and the excitement is palpable, but payment alone isn't enough.

Solutions: crossing the mobile wallet chasm

Considering the challenges laid out in the previous section, it's clear that mobile wallets need to focus on customer engagement. This is where loyalty programs can be part of the solution.

Simply adding loyalty programs to a mobile wallet increases adoption rates by 12%, according to Chadwick Martin Bailey. Meanwhile, a 2013 Vibes study finds that 85% of consumers say they would receive at least some benefit from such wallets while 59% would have a more positive opinion of brands that offer mobile wallet content. In addition, 44% of mobile wallet non-users think the technology would enhance their shopping experience.

A report by Carlisle & Gallagher Consulting Group, *Mobile Wallet Reality Check: How Will You Stay Top of Wallet?* reflects similar sentiments:

65%

of survey respondents rated the ability to make better payment choices, like maximizing their loyalty programs, as the most valued mobile wallet service.



57%

said managing receipts and additional documentation was also important.



In short: the data proves that even non-transactional loyalty integration will drive engagement and adoption of mobile wallets.

Smart-phone enabled collecting

Mobile wallets provide a solution for loyalty — a simpler way to keep track and collect points. It solves a very real problem.

With the vast majority of consumers (80%, Points Research) keeping an eye out for opportunities to earn points wherever they turn, adopting mobile wallets that allow them to manage multiple currencies in one location at the tap of a screen isn't just prudent, it's intuitive.

The union of mobile wallets and loyalty programs also makes sense considering consumers' high smartphone adoption rates and their familiarity with the technology.

Consumers are already comfortable using their smartphones to perform loyalty and payment-focused tasks. Redemption of real-time location-based offers is one of the most popular smartphone uses and 60% of consumers use their phones to comparison shop (First Data, The Mobile Wallet: It's Not Just About Payments). Furthermore, over half of smartphone users, 56%, perform at least some banking transactions on their devices, according to First Data.

Loyalty programs in context: can they come to the rescue again?

First popularized by grocers in the 1890s, loyalty programs encouraged consumers to pay for their goods at the time of purchase and not carry a balance — balances which merchants were required to carry with no guarantee the bill would be paid.

By the 1930s S&H's Green Stamps program was already a hit as it was successfully incentivizing spending habits and driving loyalty. But it was more than that. Sticking stamps into redemption booklets became a common cross-generational practice. Grandparents, parents and children all took part in a process that inspired teamwork and collective achievement.

Loyalty programs have long proved themselves highly adept at reinvigorating entire industries. This is most evident in the credit card industry. While credit card use grew steadily throughout the latter half of the 20th century, it didn't become ubiquitous among North American consumers until the 1980s and '90s, coinciding with the rise of co-branded credit cards.



Thanks to widespread loyalty program linkage, millions of consumers make credit card purchases they wouldn't have dreamed of making just a few years ago. Co-branded and airline loyalty programs arguably deserve much credit for this customer engagement boost. Incentivized to travel on the cheap (and earn additional perks), consumers accumulated frequent flyer miles via credit card purchases. Today, three-quarters of Americans own at least one credit card and co-branded cards comprise 50% of all credit card spending. What's more, Americans with co-branded cards also tend to outspend single-brand card owners by approximately \$4,900 per year.

When will the mobile wallet chasm be crossed?

When it comes to the union of mobile wallets and loyalty programs, inevitability is a strong word. But when a wealth of cross-vertical data suggests widespread consumer and merchant interest even if adoption has lagged, it's only a matter of time until the industry realizes its maximum potential. Mobile wallets are helping map out the contours and use patterns of an entirely contactless payment and loyalty industry. It's the stuff of science fiction and it's exciting to see it actually happen.

And it really comes down to a few simple facts:

- The loyalty industry is well-established and extremely popular.
- Consumers and merchants are intrigued by mobile wallet potential yet adoption stumbling blocks remain.
- Smartphones, acting as the technological focal point, are the ideal medium to bring these two industries together.
- Loyalty integration will drive interest and adoption of digital wallets.

Ultimately, the mobile wallet is simply an extension of a cell phone's already formidable capabilities — they will broaden consumer engagement and create new value for brands.

In an increasingly complex and interconnected world, loyalty and currency-based mobile wallets have the potential to make our lives easier, filling them with rewards that add true value.



"We already know that consumers are fanatical about loyalty programs. They are exactly what mobile wallets need to encourage mainstream adoption and become the next major technology to impact our lives".

~Christopher Barnard, President

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