Losing Loyalty: The Consumer Defection Dilemma™

A Milestone Study On CPG Brand Loyalty & Defection Among American Shoppers

POINTER MEDIA NETWORK™
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About The Study

Losing Loyalty: The Consumer Defection Dilemma™ is the second in a series of milestone studies on US shopper purchasing dynamics conducted by Catalina Marketing's Pointer Media Network in conjunction with the Chief Marketing Officer (CMO) Council. Our studies are designed to test the assumptions of CPG brand marketers and retailers and assist in the development of new strategies and approaches for growing brand equity, volume and value based on the realities of today's consumer. This latest report was developed to shed light on the global dynamic of loyalty and to assist in the development of new loyalty approaches.

This new study, through analysis of household-level consumer shopping behavior, exposes the high level of loyalty churn that is impacting today's leading CPG brands. The truth about brand loyalty, and its frequently transient nature, may surprise many seasoned brand marketers and retailers.

This study is unique in the breadth and depth of consumer data used in developing insights. The findings are based on an analysis of the individual buying patterns of more than 32 million consumers in 2007 and 2008 across 685 leading CPG brands. All consumer purchase data confidentially studied were consistent shoppers, meaning that they shopped at least two times in every eight-week interval during the two-year study period within the retail chains.

For the purposes of our study, loyalty was measured as a percentage of category sales using standard CPG categories defined by Information Resources Incorporated (IRI). Our study measures loyalty only for individual product brands, not for master brands as a whole. In some cases, the defection of a consumer from one product brand may well have coincided with that consumer purchasing another product brand within the same master brand.

High-loyal consumers were defined as those consumers who made 70% or more of their category purchases with a single brand during a 12-month period. Switchers were defined as formerly high-loyal shoppers who continued purchasing the brand, but reduced those purchases below 70% of all category buying. Defectors are those formerly high-loyal shoppers who have stopped buying the brand altogether, but are still purchasing in the category.

The findings demonstrate that there is an unexpectedly high level of churn across most product brands. In fact, for the average CPG brand in this study, only 48% of high loyal consumers in 2007 remained highly loyal in 2008. Approximately one-third of all high loyals completely defected from the average brand in 2008.

The research was conducted using Catalina Marketing's vast database of household-level purchase data. Through partnerships with more than 200 major retail grocery, mass merchant and pharmacy chains across the United States, Pointer Media Network and Catalina Marketing continuously track the purchases of more than 150 million individual shopper IDs, with a multi-year history of purchasing for an estimated 76% of American households.

The world's largest addressable media, Pointer Media Network has the ability to deliver highly customized advertising and offers to these individuals based on actual purchase history. These color communications are delivered at point-of-sale at more than 24,000 retail locations throughout the United States. Using advanced analytic techniques and predictive modeling, Pointer Media Network helps CPG manufacturers and retailers reach the right consumer with the right messages to drive new product trial, enhanced loyalty, increase consumption, and reduce brand defection.

STUDY HIGHLIGHTS:

- Loyalty erosion and consumer defection are pervasive and costly problems for CPG brands, and their impact is increasing dramatically in the current economy.
- For the average brand in this study, 52% of highly loyal consumers in 2007 either reduced loyalty or completely defected from the brand in 2008.
- Only four out of ten brands retained 50% or more of their highly loyal consumers from year to year.
- For the average brand, approximately one-third of all highly loyal consumers in 2007 completely defected to another brand in the same category in 2008.
- The current economic downturn is having a significant impact on brand loyalty. Many leading brands experienced a drop in the total number of highly loyal consumers between 2007 and 2008.
- Loyalty and consumer churn have a huge impact on brand revenue and value. Some major brands could have increased overall revenues by more than 20% in 2008 if they had eliminated churn among high loyal consumers.
- Precision marketing strategies for engaging loyal and high volume brand buyers are now playing a major role in improving consumer loyalty and value.
- Pointer Media Network and Catalina Marketing are working with CPG manufacturers and retailers to build programs that significantly improve customer loyalty, purchasing and brand performance.

Losing Loyalty: The Consumer Defection Dilemma™

For the average brand, **33% of highly loyal consumers** in 2007 completely **defected the brand** in 2008...

THE LOYALTY CHALLENGE

Loyal consumers are the bedrock of your brand. Without them, building profitable growth and brand equity would be as difficult as filling a porous bucket. Yet, for CPG manufacturers and brand managers, the truth about consumer loyalty is often hidden. Periodic consumer panel reports may, in good times, provide a sense of satisfaction about your brand's continued strength in share of category requirements. Yet, they can also mask a high level of defection and churn beneath the placid surface.

In today's tough economy and highly competitive consumer marketplace, concerns about brand loyalty and defection have become top of mind for marketers and retailers alike. The wishful thought that "my loyals will stay my loyals"– that highly loyal consumers, by and large, remain loyal from year-to-year – is no longer a comfortable assumption.

The truth is that consumer churn and defection are consistent problems in today's CPG marketplace, even while the economy is significantly accelerating and aggravating the problem. We believe the findings of this study, which reveal dramatic levels of defection and loyalty erosion across most CPG brands, may surprise many seasoned marketers.

Conducted by Catalina Marketing's Pointer Media Network, in conjunction with the CMO Council, **Losing Loyalty: The Consumer Defection Dilemma**, uncovers new insights into CPG brand loyalty among US consumers. Pointer Media Network's unique ability to look inside the shopping baskets of consumers to see exactly which brands they are buying and how often, provided the rich census-level data required to develop this study. Its findings have significant implications for the way brand marketers communicate and engage with their most valuable and loyal consumers.

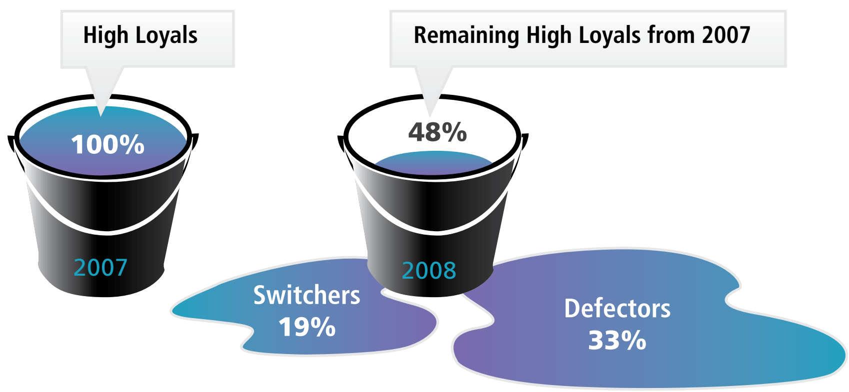
Our discovery: For the average brand, more than half of all loyal consumers in 2007 did not remain loyal in 2008. Just as worrisome for marketers, the overall level of consumer loyalty appears to be declining year over year for many brands in the current recession, not only because of churn, but because new loyals are not being added fast enough to replace these switchers and defectors.

The study analyzes shopping patterns and preferences of 32 million US consumers over a two-year period across 685 leading brands. Our findings show that, for the average brand, only 48% of highly loyal consumers in 2007 remained highly loyal in 2008. (See Chart 1) A large percentage of this churn was characterized by a total defection from the brand. For the average brand, 33% of highly loyal consumers in 2007 completely defected from the brand in 2008, even though they continued to buy within the category. In fact, 82% of all brands experienced a total defection of more than 20% of their highly loyal consumers.

The wishful thought that "my loyals will stay my loyals"... is **no longer a comfortable assumption.**

52% of high loyal consumers in 2007 had either **reduced their loyalty** or **completely defected from the brand** in 2008.

Chart 1. WHERE DID ALL MY LOYALS GO?



For the average CPG brand in this study, 52% of consumers who were highly loyal to the brand in 2007 either reduced their loyalty and became switchers or completely defected from the brand.

Chart 2. CHURN & DEFECTION AMONG LEADING BRANDS

CATEGORY LEADERS*	Remain Highly Loyal	Reduced Loyalty	Not Buying Brand
Canned Tomatoes	34.5%	30.6%	34.9%
Canned Tuna	49.5%	21.3%	29.3%
Cereal	34.6%	37.1%	28.2%
Cola	75.3%	16.6%	8.1%
English Muffins	76.3%	14.4%	9.3%
Ground Coffee	60.7%	20.8%	18.5%
Household Cleaner	41.8%	20.9%	37.3%
Pain Reliever	34.9%	20.6%	44.6%
Peanut Butter	48.8%	23.7%	27.5%
Steak Sauce	49.8%	22.0%	28.2%
Toothpaste	41.2%	21.2%	37.3%

* All categories referenced consist of the brand leaders in this space.

Loyalty varies by category and brand, but **switching and defection is a consistent issue**, even for major brands.

Consumer churn and loyalty defection are surprisingly high even among the industry's most respected and well-funded brands. One of America's top cola brands, for example, performed far better than the vast majority of brands analyzed in this study. Yet, approximately one-fourth of of this brand's highly loyal brand consumers in 2007 did not remain so in 2008. A market-leading toothpaste brand lost loyalty in 2008 among 59% of its 2007 high loyals.

The findings make it abundantly clear that the issues of customer loyalty and retention represent some of the most critical factors impacting brand success, perhaps more so today than ever.

THE ECONOMY'S IMPACT: A DOWNTURN IN LOYALTY

CPG executives and brand managers across the industry are acutely concerned about the current recession and its impact on consumer retention and brand loyalty. Many believe that financial strains and economic worries are driving once loyal consumers away from their brands. Indeed, coupon redemption rates, after several years of decline, are now increasing again, indicating consumers have become more cost and value conscious in the current economic downturn. Likewise, purchases of private label brands are increasing in many categories. According to a consumer survey by IRI, published in January of 2009, some 40% of consumers who earn less than $55,000 a year, a group that represents 60% of the population, report they are having difficulty buying the groceries they need.

"There is some trade-down; there's obvious pocketbook pressure,"
P&G's Chief Executive, A.G. Lafely, recently told financial analysts.

Marketers, however, are not just worried about lost revenue in the downturn due to temporary financial strains. The concern is that consumers who switch will build new brand rituals and allegiances that endure far beyond the recession. Indeed, Pointer Media Network's own experiences in working with CPG brands indicate that it is far easier to retain loyal consumers who are in the early stages of switching brands than after they have completely defected.

The concern is that **consumers who switch will build new brand rituals and allegiances** that endure far beyond the recession.

Data analyzed in this study suggests that the recession is having a significantly negative impact on consumer brand loyalty. Many CPG brands are experiencing an overall decline in loyalty. Chart 3 shows 12 leading brands, blinded for the purposes of this report, and the rise or fall in overall loyalty between the first half of 2007 and the first half of 2008. Only three brands experienced increases in their number of loyals. Nine others experienced declines ranging from 2% to 9%.

This erosion is not just the result of consumer churn. Loyalty defection rates were high throughout the study period, indicating that churn is a consistent problem that must be addressed by brand managers in good economic times as well as bad. An even more grim statistic for these brands was a significant drop in the rate at which new loyals joined the brand to replace defectors.

These findings underscore the critical need for marketers to protect their loyals, while also developing effective strategies for identifying and engaging with consumers who have a high potential to become loyal, high-value brand buyers.

Chart 3. LOYALTY DECLINES IN THE DOWNTURN

CATEGORY LEADERS*	Change in Total High Loyals	Change in Total Brand Buyers	No Longer Highly Loyal
All Purpose Cleaner	-2% ↓	-1% ↓	62%
Canned Tomatoes	15% ↑	15% ↑	65%
Cereal	6% ↑	4%↑	65%
Deluxe Bagels	-3% ↓	0%	52%
Frozen Pizza	-6% ↓	-9% ↓	34%
Frozen Vegetable	-9% ↓	-7% ↓	51%
Granulated Sugar	2% ↑	6% ↑	37%
Ketchup	-4% ↓	-3% ↓	19%
Pain Reliever	-7% ↓	-5% ↓	56%
Paper Towel	-9% ↓	-7% ↓	34%
Peanut Butter	-7% ↓	-8% ↓	36%
Refrigerated OJ	-6% ↓	-8% ↓	41%

This table shows the % change in the total number of high loyals and brand buyers between 2007 and 2008, as well as the percentage of 2007 highly loyal consumers who remained high loyals in 2008. Replenishing loyal consumers is becoming more difficult in the economic downturn.

* All categories referenced consist of the brand leaders in this space.

THE HIGH COST OF CHURN

Consumer defection and churn have major financial implications for CPG manufacturers. An analysis of leading brands underscores the heavy economic toll of loyalty churn. (See Chart 4, 5, 6 and 7) For example, in the case of one premium orange juice brand, 64.8% of highly loyal 2007 consumers either reduced loyalty or completely defected from the brand in 2008, even while they continued to purchase within the category. Cumulatively, these consumers spent 34% fewer dollars on this brand in 2008. This represented an 8% decline in potential overall revenue for the orange juice brand in 2008.

Those who **reduce churn rates** and retain greater consumer loyalty can **significantly improve revenue and brand value.**

Using the same formula, another premium orange juice experienced a 25% reduction in 2008 spending among consumers who had been highly loyal in 2007, representing a 12% decline in overall observable revenue for the brand. A leading cola, a brand with very high loyalty from 2007 to 2008, saw an 8% decline in spending among highly loyal 2007 consumers in 2008. Yet that drop represented a very significant 6% decline in overall revenues in 2008. Loyalty churn and defection resulted in a 7% decline in overall revenues for a competing cola brand, and a 25% decline in overall revenues for one leading laundry detergent brand.

For brand marketers, the message is clear. Those brands that reduce churn rates and retain greater consumer loyalty can significantly improve revenue and brand value. Those which do not must climb a steeper hill just to keep pace with the rate of consumer defection. The issue, however, is how to identify, reach and engage with these consumers.

Chart 4. THE COST TO COLA BRANDS

BRAND*	Change in Spending Due to Loyalty Erosion	Impact on Overall Observable Revenue
Cola brand A	-8%	-6%
Cola brand B	-10%	-7%
Caffeine Free Cola	-19%	-9%

Chart 5. THE COST TO BREAKFAST CEREAL BRANDS

BRAND*	Change in Spending Due to Loyalty Erosion	Impact on Overall Observable Revenue
Non-sweetened cereal	-42%	-6%
Sweetened cereal brand A	-59%	-5%
Sweetened cereal brand B	-46%	-4%
Sweetened cereal brand C	-73%	-4%

Chart 6. THE COST TO LAUNDRY DETERGENT BRANDS

BRAND*	Change in Spending Due to Loyalty Erosion	Impact on Overall Observable Revenue
Detergent brand A	-29%	-19%
Detergent brand B	-6%	-5%
Detergent brand C	-38%	-25%

Chart 7. THE COST TO REFRIGERATED OJ BRANDS

BRAND*	Change in Spending Due to Loyalty Erosion	Impact on Overall Observable Revenue
Premium OJ brand A	-34%	-8%
Premium OJ brand B	-25%	-12%
Premium OJ brand C	-16%	-8%
Premium OJ brand D	-14%	-9%

The charts above underscore the heavy financial cost of loyalty churn on major brands. The column on the left shows the percentage decline in spending among highly loyal consumers due to reduced loyalty in 2008. The decline is based on 2008 category spending by these consumers. The column on the right shows the impact of this spending reduction on overall observable revenue in this study for each brand.

* All brands referenced were among the leaders in their category.

ALL LOYALS ARE NOT CREATED EQUAL

Loyalty, of course, is not the only critical determinant of a consumer's present value to your brand. Some consumers are highly loyal, but not major category buyers. It is the high-volume brand buyer that really drives revenue.

In December of 2008, Catalina Marketing and Pointer Media Network, in conjunction with the CMO Council, released a major report entitled, **Discovering the Pivotal Point Consumer.** The study introduced into marketing lexicon the "Pivotal Point Consumer"– the high volume brand buyer who along with her or his peers accounts for 80% of your brand's sales. This breakthrough research showed that a surprisingly small number of consumers – just 2.5% of shoppers for the average brand – make up 80% of brand sales.

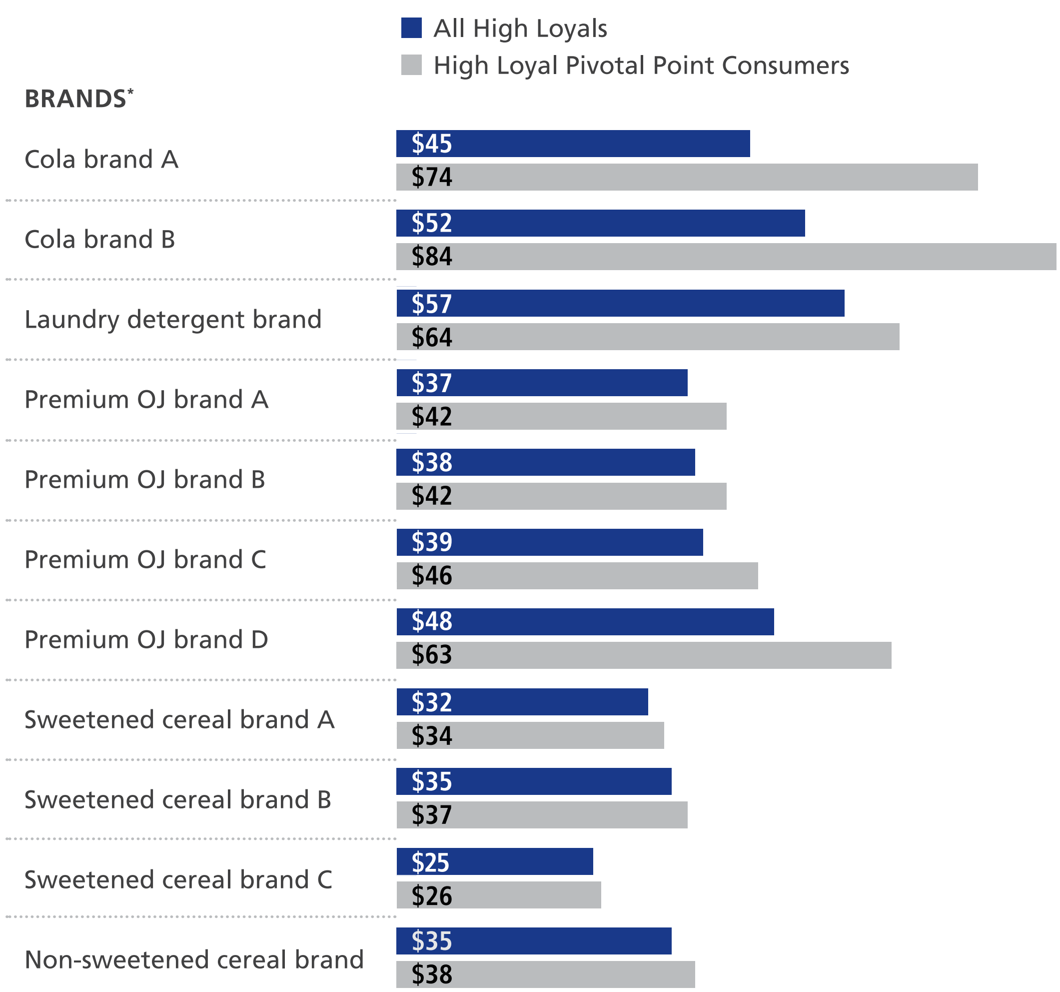
The ability to target the high volume brand buyer is an important lever in driving brand value and revenue.

Chart 8 shows the difference in value between the average highly loyal consumer and the average highly loyal Pivotal Point consumer to a variety of leading brands.

For CPG manufacturers, the good news is that the Pivotal Point Consumer tends to remain more consistently loyal year-over-year than other highly loyal consumers. However, the reality is that loyalty churn among Pivotal Point Consumers is also surprisingly high, and the dollar impact of that churn is very significant.

The ability to target the high-volume brand buyer in order maintain and grow loyalty is an important lever in driving brand value and revenue.

Chart 8. THE VALUE OF HIGH LOYAL PIVOTAL POINT CONSUMER



* All brands referenced were among the leaders in their category.

PROTECTING AND OPTIMIZING YOUR LOYAL BASE

The rate of loyalty churn for CPG brands is dramatically higher than many of us may have thought, and the current economic environment has only intensified the challenge. In response, savvy marketers have a major opportunity to significantly grow brand revenues and value by effectively addressing the issue of loyalty. Strategies and programs that reduce customer churn, win over new loyal consumers, and increase category consumption and purchasing among these consumers will pay both immediate and long-term benefits to your brand.

The challenge, however, is identifying your most valuable consumers, understanding their relationships with your brand and taking the appropriate steps to protect, sustain and build those relationships. Mass media and demographically targeted advertising, or even generalized coupon incentives, do not ensure that you are reaching the right consumers with the right message or offer when those consumers are actually wavering in their loyalty to your brand. An on-package or FSI coupon often reduces the profitability of consumers who have no intention or predisposition to switch brands, and even reduces the perceived value of your brand. On the other hand, if a loyal, high-value consumer is exhibiting signs of defection, well-timed, targeted and relevant ad messaging and incentives can be very effective in sustaining the brand relationship.

Based on research for numerous CPG brands, Catalina Marketing's Pointer Media Network has identified a variety of leading indicators that can predict impending defection, allowing marketers to take effective action to reduce churn. An increase in purchases of alternative brands in your category is a powerful early warning sign. However, there are also numerous, more subtle cross-category indicators. For example, a consumer's use of coupons or value-based defection from brands in other product categories significantly increases the likelihood that she or he will also consider switching in your category. Pointer Media Network is also conducting research into other cross-category indicators, including defections based on characteristics such as "organic", "heart-healthy" or "family-size".

Catalina's Pointer Media Network has identified a variety of leading indicators that **can predict impending defection.**

Using these insights, Pointer Media Network is working with clients to build predictive models that analyze household buying patterns across 200,000 individual brands and a variety of factors, including recency, frequency, unit purchases, spending and tenure. These models, analyzing millions of variables, have proven to be powerful tools for identifying and retaining high value consumers who might otherwise switch.

For example, predictive modeling, combined with a targeted coupon offer, helped a leading brand in feminine care significantly reduce churn rates. The predictive model identified consumers, based on category and cross-category analytics, who were likely to switch brands. Pointer Media Network then set up a control group, to compare behavior, delivering a single coupon to all at-risk brand buyers outside of the control group. Based on a comparison in defection rates between the two groups, delivering that single coupon to at-risk consumers resulted in a 2% improvement in category share purchases compared to what would have occurred without the intervention of precision marketing. This positive result continued to hold up six months after the coupon was delivered at point of sale via the Pointer Media Network.

Predictive modeling is also being used to win new loyal consumers. Hundreds of CPG brands have worked with Pointer Media Network to find likely loyal buyers and drive trials of new products through cross-category analytics. Delivering relevant advertising, followed by coupons, to specific households who did not already purchase brands after receiving the ads, has proven highly effective in building purchases and loyalty for new products ranging from ready-to-serve soups and frozen dinners, to cereal and wine and spirits. Increasing consumption and purchasing among loyal consumers is also a proven precision marketing strategy. For example, a leading CPG manufacturer in food products worked with Pointer Media Network to identify brand consumers who had recently purchased several product brands in its portfolio. Leveraging the growing trend toward eat-at-home, the company targeted these consumers with recipes that include products already in the consumers' pantries, as well as other ingredient brands from the manufacturer's portfolio.

TARGETING LOYALTY FOR RETAILERS

Many major grocery, drug and mass merchant retailers have substantial insights into the issues of loyalty and customer turnover via their own loyalty programs. Loyalty programs allow retailers to understand customer shopping basket size, store trips and other key metrics. In addition, they enable the retailers and their CPG partners to serve up relevant offers, incentives and advertising messages that can drive increased purchasing and loyalty. Retailers who do not operate card-based programs have far less ability to uncover customer turnover, and even less capacity to take measured action to improve customer value and reduce defections to competitive retailers.

Catalina Marketing and Pointer Media Network, for example, are working with many leading CPG retailers to increase loyalty and value through effective, precision marketing campaigns that reach specific consumers with relevant incentives and messaging based on their shopping purchases and preferences. These customer value campaigns serve up a series of household-specific offers and communications via the Pointer Media Network over a period of 13 weeks or longer with tremendous results in terms of consumer retention and increased purchasing over time. Based on comparisons with control groups, these campaigns consistently drive a 2-3% lift in sales within the intended customer base and provide a sales return on investment of 6 to 1.

Catalina Marketing and Pointer Media Network are also designing new predictive models to help retailers identify specific consumers who are showing signs of defection and reduced loyalty. As with CPG brand attrition models, these programs compare consumers' actions against a variety of leading indicators that can predict impending defection, allowing retailers to take fast and effective action to re-engage with these at-risk shoppers.

Conclusion

Customer churn and defection are consistent issues facing CPG brands and retailers. Indeed, for the average brand in this study, only 48% of highly loyal consumers in 2007 remained highly loyal in 2008. Perhaps even more remarkable, some 33% of highly loyal consumers actually left the brand altogether, even though they continued to buy in the category. The financial impact of this consumer churn is significant. If major brands tracked in this study had retained their high loyals from 2007, their 2008 observable revenues would have increased five, seven, 12 and even 25%.

The impact of consumer brand defection is even more severe in the current recession. Not only are churn rates high, but brands are experiencing increased difficulty replacing lapsed loyals with new brand buyers. The result is an overall decline in the volume of loyal consumers for many major brands.

Both CPG manufacturers and retailers are well advised to take direct and forceful action to increase loyalty, retention and customer value as a core marketing and business strategy – both in the current economic downturn and beyond. To do so, they should increase the relevance of their communications and offers to high value customers. By identifying real purchasing preferences and shopping behavior and reaching their best customers with meaningful and tailored advertising, messaging, incentives and rewards, marketers will have a significant impact on loyalty and customer value. Predictive modeling, combined with addressable marketing and media techniques, can help both retailers and CPG brands reduce churn and drive revenue improvements. These same strategies can help win over new consumers to your brand and increase consumption and loyalty levels among existing customers.

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ABOUT POINTER MEDIA NETWORK

Pointer Media Network (**www.pointermedianetwork.com**), a service of Catalina Marketing, is one of the largest, most advanced, addressable media outlets in the world. Pointer Media enables advertisers, media buyers, creative agencies, brand managers and marketers to leverage the network's sophisticated database of 250 million weekly shopping transactions to develop, manage, and measure direct-to-consumer media campaigns and engagement opportunities. The on-demand media channel provides an extensive infrastructure of 24,000 retail distribution channels, 25-years of actionable insight development and expertise, and unique communication exchanges with nearly 80 percent of US households.

ABOUT THE CMO COUNCIL

The Chief Marketing Officer (CMO) Council is dedicated to high-level knowledge exchange, thought leadership and personal relationship building among senior corporate marketing leaders and brand decision-makers across a wide-range of global industries. The CMO Council's 4,500 members control more than $125 billion in aggregated annual marketing expenditures and run complex, distributed marketing and sales operations worldwide. In total, the CMO Council and its strategic interest communities include over 17,000 global executives across nearly 100 countries in multiple industries, segments and markets. Regional chapters and advisory boards are active in the Americas, Europe, Asia Pacific, Middle East and Africa. The Council's strategic interest groups include the Coalition to Leverage and Optimize Sales Effectiveness (CLOSE), Customer Experience Board, Marketing Supply Chain Institute, and the Forum to Advance the Mobile Experience (FAME). More information on the CMO Council is available at **www.cmocouncil.org.**