Introducing a new approach for turning reward points into a highly liquid, fungible and valuable currency

REWARD POINTS

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Airlines cultivate loyalty with frequent-flier miles. Hotels attract business travelers with free nights. Large online merchants and retail chains offer reward points. Even small businesses such as cafés, restaurants and other service businesses offer digital punch-cards that can reward frequent visitors with customizable offers.

Bank issuers bring all these together with credit and debit card offerings that allow customers to earn reward points that can be exchanged for airline miles, hotel nights, gift cards, or cash back.

Reward points are everywhere. Yet despite their ubiquity, reward programs have yet to reach their full potential.

Why are reward points issued monthly in a real-time economy?

Even within a real-time digital economy, most consumers still earn reward points only once per month at statement closing, and then may have to wait weeks for delivery of the underlying product or service.

The unwieldy and cumbersome process of reward redemption requires

customers to visit a separate third-party site where they have to figure out for themselves the best value among a limited menu of pre-approved merchants. Typically, third-party reward programs aggregate a collection of the most high-profile brands in each category, leaving out popular local favorites and the hottest new merchants.

Finally, once a reward has been selected, the customer may face a significant delay in delivery, such as waiting for a physical gift card to arrive in the mail.

The combination of slow accrual, an underwhelming selection, and lackluster fulfillment tends to reduce the excitement associated with a rewards purchase, and these challenges increase the risk of customer attrition.

In other words, reward points aren't worth much to someone who has to struggle to spend them. While the current system for reward points may work well for motivated points collectors who avidly comparison shop for the best deals on card offers and redemptions, a consistently high level of engagement and interest is simply not practical or desirable for most people.

The current system also has serious drawbacks for the card-issuing banks. Each issuer has to maintain expensive systems to track reward points, fulfill reward redemptions, and reconcile customer accounts across an extended settlement period. Furthermore, banks have to carry unused reward points as liabilities on their balance sheets, which can complicate financial results given changes in redemption rates or accounting rules.

It's axiomatic that reward points are a form of currency.

The core problem is that it's a highly illiquid currency that's only exchange-able into airline miles, other reward points, merchant-specific gift cards, or (at a significant discount) cash.

It's also a highly fragmented currency, with each bank issuing its own reward points that cannot be pooled with points from other issuers.

Moreover, each issuer is responsible for the expense of recordkeeping, accounting, and reconciliation of reward points. All but the largest banks outsource their points management to third-party vendors, who in turn offer largely undifferentiated services.

What if the banking industry could increase the liquidity, fungibility, and value of reward points, while also significantly improving operating efficiency for the bank and reducing barriers to participation for merchants?

Higher liquidity would involve real-time points accrual and redemption, allowing customers to spend rewards points at any card-accepting merchant.

Higher fungibility would allow customers to aggregate reward points from different issuers into a single pool, enabling faster accumulation of points for higher-value goods and services.

The result would be a higher-value currency that more closely approaches cash-back rewards, but with important advantages relative to cash:

1. Earned reward points would incentivize incremental spending on future purchases rather than being applied to past balances.
2. Unrestricted spending using reward points would provide valuable information as to what customers value most, i.e. what they consider "rewards" versus everyday transactional spending.
3. Real-time analytics based on patterns of real-time spending and rewards fulfillment would enable new kinds of rewards, special offers, and personalized product suggestions.

Benefits for card issuers:
- ■ Lower operating costs by switching from third-party systems to a shared ecosystem
- ■ Real-time data eliminates the need for reconciliation
- ■ Better utilization of Reward point balances, leading to healthier balance sheets
- ■ Simpler operational processes for points redemption

Benefits for card issuers and payment processors:
- ■ Higher operating efficiency from real-time settlement
- ■ Audit trail for a complete history of transactions
- ■ Better information from real-time view of transactions and balances

Introducing a new approach for the rewards ecosystem

A common currency for reward points would need to encompass the entire ecosystem, including card-issuing banks, credit card networks, merchant acquiring banks, payment gateway services, and merchants. The overall complexity of this undertaking explains why a common rewards currency hasn't been feasible – until now.

Blockchain technology now makes it possible to create distributed shared ledgers that are robust and scalable enough to support an entire ecosystem without the difficulty and expense involved with traditional database deployments.

With a private, permissioned blockchain, each participant in the ecosystem can perform verified updates on a single source of data.

Issuers will be able to locate their customers' accounts on the shared ledger and credit them with reward points immediately based on real-time spending.

Merchants and their acquiring banks will be able to debit reward points according to real-time customer instructions, whether delivered in-person or online. ■

Benefits for customers:
- Consolidates reward points across issuer relationships
- Improved ability to make higher-value purchases
- Flexibility in using reward points without restrictions
- Vastly superior customer experience

Benefits for merchants:
- Higher customer spending
- Easier acceptance of rewards points
- Custom offers and promotions