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# **Enhancing Customer Loyalty: Critical Switching Cost Factors**

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## **Structured Abstract**

**Purpose** - This paper aims to simultaneously examine the moderator effects of switching costs, classified by type (relational, procedural, and financial) and direction (positive and negative), on the relationships between customer-perceived value, trust, and loyalty.

**Design** - This study reports on quantitative data from a survey of two service contexts which vary in their degree of customer-employee contact and customization. Three hundred and sixty usable questionnaires were collected, and the data was analysed using multi-group structural equation modelling.

**Findings** - The results demonstrate that switching costs moderate, in different ways, the relationships between customer loyalty, trust, and perceived value. Moreover, the strength of the moderator effects vary according to service type.

**Research limitations/implications** - This study provides new insights into understanding the moderating role of switching costs; thus, it reduces inconsistencies about the direction and the strength of the moderator effect of switching costs in loyalty frameworks.

**Practical implications** - This study helps managers choose the most effective loyalty strategy for specific service industries and perceptions of switching costs, and to look beyond their service boundaries in order to cross-fertilize strategies for handling switching costs.

**Originality/value** - No empirical study to date has simultaneously examined the moderator effect of switching costs, classified by type and direction, on the relationships between customer-perceived value, trust, and customer loyalty across two different service contexts in a single framework.

**Keywords** switching costs, customer loyalty, trust, perceived value, moderator effects, services.

**Article classification** Research paper.

## **Enhancing Customer Loyalty: Critical Switching Cost Factors**

### **Introduction**

Understanding why, how, and under what conditions customer loyalty is developed remains an important and interesting issue (Ha and Park, 2013). A growing body of evidence indicates that customer satisfaction is a necessary but insufficient condition for loyalty enhancement (e.g., Agustin and Singh, 2005). As a result, focus has shifted onto other important determinants and/or moderators, such as switching costs (Burnham *et al.*, 2003). Switching costs have been found to act as a quasi-moderator in loyalty frameworks (Sharma, 2003) and to have a profound explanatory effect on customer loyalty. Burnham *et al.* (2003) found that switching costs predict 16% and 30% of customer loyalty in credit cards and long distance telecommunications while Tsai *et al.* (2006) found that switching costs predict 59% of loyalty in e-retailing. Further, switching costs can provide a competitive advantage that deters customers' switching behavior (Klemperer, 1995). Certain service industries are highly customized, personalized, and geographically dispersed, which can affect customers' perceptions of switching costs (Jones *et al.*, 2000). The strength of customers' perceptions of switching costs/losses, relative to the benefits offered by competitors, determines customers' switching behavior (Yang and Peterson, 2004).

A review of literature on the moderating role of switching costs in loyalty frameworks revealed three main issues. First, it was found that research examining switching costs as a multi-dimensional construct is very limited when switching costs are classified by type (relational, financial, and procedural) and direction (positive and negative). Viewing switching costs as a multi-dimensional construct enhances the explanatory power of the construct (Whitten and Wakefield, 2006), clarifies important theoretical and managerial implications across switching costs types (Jones *et al.*, 2002; Jones *et al.*, 2007), and

adequately assesses the relationship between switching costs and other related constructs (Barroso and Picón, 2012). Second, the research findings are inconsistent regarding both the moderating role of switching costs and the strength of specific type(s) of switching costs in specific service type(s). For example, Burnham *et al.* (2003) assert that financial switching costs have the weakest impact on loyalty in credit cards and long distance telecommunications. In contrast, Jones *et al.* (2002) argue that lost performance costs exert the strongest impact on loyalty intentions in hairstylists and banks. Similarly, Patterson and Smith (2003) argue that the loss of special treatment benefits is a more powerful predictor of customers' propensity to stay in medical and travel services.

This paper argues that these inconsistencies in previous research findings are due to researchers overlooking the interaction between switching costs type (i.e., relational, financial, and procedural), switching costs direction (positive and negative), and service type (i.e., high versus low customer-employee contact and customization). Understanding industry-related switching costs (e.g., service type), in addition to firm- and customer-related switching costs, provides a better understanding of the boundary conditions of switching costs' effects (Barroso and Picón, 2012). Crucially, no empirical study to date has simultaneously examined the moderator effect of switching costs classified by type and direction on the relationships between customer-perceived value, trust, and customer loyalty in a single framework.

In line with Agustin and Singh (2005), this study focuses on trust (e.g., Harris and Goode, 2004) and customer-perceived value (e.g., Chen, 2001; Yang and Peterson, 2004) in addition to switching costs (Burnham *et al.*, 2003). These factors are critical in helping firms to maintain and enhance customer loyalty.

The purpose of this paper is to address these issues in order to make four important contributions. The first theoretical contribution is providing a more sophisticated

understanding of the interdependencies between switching costs, customer-perceived value, trust, and loyalty (MacKinnon and Luecken, 2013). The second theoretical contribution is reducing inconsistencies about the moderating role of switching costs (Holloway, 2003), particularly in terms of relevance, direction, and strength. The paper's empirical contribution is improving the generalizability of the results (Wang, 2010) by assessing whether they hold across similar service contexts (high vs. low employee-customer contact and high vs. low degree of customization). Finally, this paper's managerial contribution comes in the form of helping service managers to look beyond their service boundaries in order to cross-fertilize strategies for handling switching costs (Lovelock, 1984). Moreover, it also helps managers to decide which loyalty strategy is the most effective for specific service industries and perceptions of switching costs.

The paper is organized as follows. The first section presents a critical literature review of previous research on customer loyalty, trust, customer-perceived value, and switching costs. Subsequently, a conceptual model specifying the moderating effects of different types of switching costs on the relationships identified is developed. The second section explains the research design and outlines the data collection procedure. The third section presents the results of both exploratory and confirmatory factor analyses, and is followed by a discussion of the findings and an elaboration of the theoretical and managerial implications. The paper concludes by addressing the limitations of the study and making suggestions for future research.

## **Literature Review and Hypotheses Development**

### *Customer Loyalty: Views*

Customer loyalty conceptualization research can be divided into three main streams. The first of these is the behavioral loyalty stream, evidenced, for example, by Tucker's (1964, p. 32) statement, that "no consideration should be given to what the subject thinks nor what goes on

in his/her central nervous system, his/her behavior is the full statement of what brand loyalty is". The second is the attitudinal loyalty stream, evidenced, for example, by Pritchard (1991) referring to attitudinal loyalty as a psychological attachment to a brand and by Yang and Peterson (2004) viewing it in terms of behavioral-intention. Finally, there is the composite stream, which is evidenced by Oliver (1999) referring to two elements of loyalty; attitudinal loyalty reflecting behavioral intentions, and behavioral loyalty reflecting actual behavior. Despite there being a lack of agreement on how to conceptualize customer loyalty, the majority of seminal research papers in the field (e.g., Agustin and Singh, 2005; Mattila, 2004; Zeithaml, *et al.*, 1996) tend to view customer loyalty as intended behavior. Thus, this paper adopts the view of customer loyalty intentions as being a common proxy for customer loyalty behavior (Wang, 2010).

#### *Customer Loyalty: Importance*

The importance of customer loyalty is well documented in services literature. A 1 percent increase in customer loyalty has almost five times more impact on a firm's value than a 1 percent change in discount rate or cost of capital (Gupta *et al.*, 2004; Roos and Gustafsson, 2007). Moreover, loyal customers are likely to buy more (e.g., Lam and Burton, 2006; Meyer-Waarden, 2007), generate more profit (Reichheld, 1996), forgive infrequent service failure (Yi and La, 2004), resist competitive offerings (Narayandas, 2005), and cost less to retain (Ganesh *et al.*, 2000).

#### *Customer Trust: Views*

The literature on customer trust reveals key differences in the way that trust is defined, with researchers defining trust as a belief, as a confidence benefit, and even as a psychological state. Specifically, trust has been conceptualized as a belief that the other party will fulfil a set of obligations such as integrity, benevolence, and competence (Luran and Lin, 2003). Some researchers have viewed trust as a perceived confidence benefit, which reduces anxiety

and increases comfort as a result of customers knowing what to expect from a service provider (e.g., Henning-Thurau *et al.*, 2002; Morgan and Hunt, 1994; Singh and Sirdeshmukh, 2000). In contrast, other researchers have viewed trust as a psychological state comprising beliefs and conative connotation (e.g., Agustin and Singh, 2005; Moorman *et al.*, 1993) or comprising beliefs, affect, and conative connotation (Johnson and Grayson, 2005). Additionally, previous studies have urged researchers to examine trust within its nomological net and to distinguish between trusting beliefs and trusting intentions. Specifically, McKnight and Chervany (2002) argue that trusting beliefs refer to the characteristics of service providers (e.g., ability, integrity, and benevolence), while trusting intentions refer to customers' behavioral intentions (e.g., willingness to depend on the service provider). Therefore, this paper supports the view of trust as being related to customer's beliefs. Such a view captures the characteristics of the service provider, including confidence benefit, while maintaining the causal distinction between trusting beliefs and trusting intentions.

#### *The Relationship between Trust and Customer Loyalty*

Previous studies have referred to the important role of trust in enhancing customer loyalty by using various terms that seem conceptually similar. Specifically, trust has been referred to as being a fundamental building block (Wilson, 1995), a central attribute (Sirdeshmukh *et al.*, 2002), and a relationship quality feature/determinant/glue (e.g., Dwyer *et al.*, 1987; Moorman *et al.*, 1993; Singh and Sirdeshmukh, 2000). Consumers act as trustworthy or interactive agents in the loyalty chain (Roger-Monzó *et al.* (2015) as trust creates an ongoing process of developing and maintaining an important relationship (Thompson, *et al.* 2014). The important role of trust in developing customer loyalty intentions is further enhanced in service industries (El-Manstrly and Harrison, 2013). Services are characterized as being more intangible, heterogenous, perishable, and inseparable in comparison to manufactured goods. Thus, service customers tend to rely on trust in order to reduce the perceived risk and

uncertainty associated with service offerings (Chaudhuri and Holbrook, 2001; Han *et al.*, 2008). In accordance with previous discussions, it is expected that:

H1: Trust has a positive influence on customer loyalty

#### *Customer-perceived Value: Views*

Customer-perceived value is defined as the “consumer’s overall assessment of the utility of a product (or service) based on perceptions of what is received and what is given” (Zeithaml, 1988, p.14). According to Sweeney and Soutar (2001), this utility can be divided into emotional (i.e., an offering capacity to enhance customers’ sensations or affective responses), social (i.e., an offering capacity to enhance customers’ social self-concept), and functional components (i.e., an offering capacity to decrease short term and enduring costs). In line with the majority of studies in the field, this study adopts an economic-based view of customer-perceived value (e.g., Agarwal and Teas, 2002; Dodds, 1991).

#### *The Relationship between Customer-perceived Value and Loyalty*

Customer-perceived value has been viewed as a fundamental issue in every marketing activity (Holbrook, 1999), as a source of providing a competitive advantage (Parasuraman and Grewal, 2000), and as a strategic tool for reducing defection and increasing retention rates (Woodruff, 1997; Zeithaml, 1988). Customers are more likely to stay loyal to a service firm if they feel that they are receiving superior value to that offered by competitors (Lam *et al.*, 2004; Gruen *et al.*, 2007; Sirdeshmukh *et al.*, 2002). Further, customer-perceived value prompts customers to buy more, spend more, and pay premium prices at a particular service provider (Palmatier *et al.*, 2007). In support, Floh *et al.* (2014) suggest that higher levels of perceived value are associated with higher levels of loyalty intentions. This important role of customer-perceived value has been supported empirically across various service settings, such as telecommunications, airline travel, and retailing (Yang and Peterson, 2004). In light of the preceding discussion and findings, it is expected that:



H2: Perceived value has a positive influence on customer loyalty

### *The Relationship between Customer-perceived Value and Trust*

Sirdeshmukh *et al.* (2002) argue that trust creates perceived value by providing relational benefits and reducing the uncertainty associated with a relational exchange. In support, Walter and Ritter (2003) argue that trust eases the learning processes in service encounters as both parties are more open, thus enhancing perceived value. Further, previous research has found that trust increases perceived value by reducing perceived non-monetary costs, such as the time and effort required to select an appropriate service provider (Ponte *et al.* 2015). In this regard, the following hypothesis is proposed:

H3: Trust has a positive influence on perceived value

Our understanding of the simultaneous impact of customer-perceived value and trust on customer loyalty, however, is incomplete. What is lacking is an understanding of the moderating role of switching costs on these crucial interrelationships (i.e., when these interrelationships are stronger or weaker for a specific type and direction of switching costs).

### *Switching Costs*

The literature on switching costs can be organized into four main groups in terms of conceptualization, categorization, direction, and levels of modeling.

### *Switching Costs: Views*

In terms of conceptualization, researchers view switching costs either at a very broad or a specific level. For example, broad views include real or perceived costs (Gremler, 1995), objective/economic costs and subjective/non-economic costs (Molina-Castillo *et al.*, 2011), and monetary and non-monetary expenses (Lam *et al.*, 2004). In contrast, specific views include transaction costs, learning costs, and artificial switching costs (Klemperer, 1995); search costs, customer discounts, customer habit, emotional cost, cognitive effort, and

financial, social, and psychological risks (Fornell, 1992); and monetary, behavioral, search, and learning-related costs (Yang and Peterson, 2004).

The switching costs construct has also been used interchangeably with the switching barriers construct. For example, Jones *et al.* (2002, p. 441) state that “switching costs can be thought of as barriers that hold customers in service relationships”. Similarly, Fornell (1992) refers to switching barriers as being all the costs associated with deserting one supplier in favor of another (e.g., financial, psychological, learning, search costs, etc.). However, Goode and Harris (2007) argue that there are subtle differences between perceived switching costs and perceived switching barriers constructs. They argue that switching barriers refer to any factors that make it costly or difficult to change, including the lack of attractive alternatives, whereas switching costs refer to losses that are only incurred upon switching. Therefore, in line with Goode and Harris (2007), this paper adopts the term ‘perceived switching costs’ for reasons of parsimony.

#### *Switching Costs: Categorization*

In terms of categorization, Barroso and Picón (2012) extend switching costs literature to include three categories of switching costs. Customer-related costs refer to habit, effort, time, commitment, expertise, and psychological risks; firm-related costs refer to monetary, search, and learning costs; and industry-related costs refer to competition, alternative attractiveness, and service type. In terms of direction, switching costs can be classified as positive and negative. According to Jones *et al.* (2007), positive switching costs refer to relational and financial switching costs derived from positive losses that add value to customers (e.g., losing a relational bond or benefits), whereas negative switching costs refer to procedural switching costs derived primarily from negative losses that add no value or benefit to customers (e.g., losing time and expending effort).

### *Switching Costs: Level of Modeling*

In terms of levels of modeling, Jones *et al.* (2002) identified three higher order factors (namely continuity, learning, and sunk costs) to reflect six lower order factors of switching costs. Continuity costs include lost performance costs and uncertainty costs, which refer to the extent and likelihood of losing performance benefits and perquisites secured via continued patronage of a given provider. Learning costs include pre-switching search and evaluation costs, post-switching behavioral and cognitive costs, and set up costs, which refer to the time and effort spent on information acquisition, exchange, and evaluation. Sunk costs refer to the economically irrelevant but psychologically important prior investments made in the exchange relationship (e.g., non-recoupable time and effort).

In attempting to provide a more comprehensive typology of switching costs, Burnham *et al.* (2003) developed and validated three higher order factors of switching costs to reflect eight lower order factors of switching costs. These include relational switching costs (personal relationship loss costs and brand relationship loss costs); financial switching costs (benefits loss and monetary-loss costs); and procedural switching costs (economic risk, evaluation, learning, and setup costs). Relational switching costs refer to psychological or emotional losses/discomfort (e.g., loss of identity and breaking of bonds). Financial switching costs refer to economic losses (e.g., penalties and economic benefits accumulated over the years). Procedural switching costs refer to time and effort losses (e.g., search, learning, and setup). This paper argues that Jones *et al.*'s (2002) typology reflects both the procedural and financial types of switching costs, whereas Burnham *et al.*'s (2003) typology reflects the financial, procedural, and relational types of switching costs. Therefore, this paper adopts Burnham *et al.*'s (2003) view of switching costs, as it is more likely to adequately capture the richness of the construct (Bagozzi and Edwards, 1998; El-Manstrly, 2014).

*The Moderating Role of Switching Costs on the relationships between trust, customer-perceived value, and loyalty*

Previous research has tended to provide mixed results (e.g., positive, negative, or no effect) regarding the moderator role of switching costs in loyalty frameworks (see Table 1).

Insert Table 1 here

In terms of positive moderator effects, Patterson and Smith (2001) argue that switching costs (e.g., having a friendly and comfortable relationship; being recognized by service personnel; being treated as more than just another customer; and enjoying the social aspects of interpersonal interactions) can provide a source of satisfaction (a construct highly correlated with customer value (Wang, 2010)) and act as incentives to strengthen the satisfaction-loyalty relationship. In support, Lam *et al.* (2004) argue that switching costs strengthen the relationship between satisfaction and word-of-mouth. This is due to the fact that, under high conditions of perceived switching costs, dissatisfied customers feel trapped and forced to stay with a service provider. This, in turn, can increase their tendency to bad-mouth the service provider. Similarly, based on social exchange theory, Woisetschläger *et al.* (2011), found that satisfied customers are more likely to recommend the service provider when social ties are strong. This results from the fact that social ties offer more opportunities to engage in WOM, due to the anticipated benefits of reputational gains and influence on others. Further, a recent meta-analysis by Blut *et al.* (2015) found a significant positive moderating effect of financial switching costs on the relationship between satisfaction and repurchase intentions/behavior. Finally, Sharma and Patterson (2000) found that switching costs strengthen the relationship between trust and customer commitment (which reflects lower order attitudinal loyalty (DeWitt *et al.*, 2008)). In support, Li *et al.* (2015) argue that switching costs create ties between suppliers and customers which strengthen the relationship between supplier trust and customer involvement in the development of new products.

Some researchers, however, argue that the moderator effect of switching costs on the relationships between loyalty and its antecedents is contingent on the level of the independent variable. For example, Yang and Peterson (2004) found a statistically significant positive moderator effect of switching costs on the customer satisfaction-loyalty link and customer value-loyalty link when customer value and customer satisfaction are above average. In line with Jones *et al.*'s (2007) distinction between positive and negative switching costs and Herzberg *et al.*'s (1959) two-factor model, this paper argues that if perceived trust/value levels are above average and switching costs are positive, customers are more likely to view switching costs as motivating factors and sources of incentives. This, in turn, strengthens value-loyalty and trust-loyalty relationships. Therefore, this paper proposes the following hypotheses:

H4: Financial switching costs positively moderate the relationship between trust and customer loyalty.

H5: Financial switching costs positively moderate the relationship between customer value and customer loyalty.

H6: Relational switching costs positively moderate the relationship between trust and customer loyalty.

H7: Relational switching costs positively moderate the relationship between customer value and customer loyalty.

In terms of negative moderator effects, based on side-bet theory, Colwell, Zyphur, and Schminke (2011) argue that switching costs negatively moderate the relationship between supplier-enforced ethical codes of practice and commitment. Customers view switching costs as relationship investments and thus their decision to remain in a relationship is more likely to be a function of avoiding losses that may outweigh the benefits of supplier-enforced ethical codes of conduct. In support, Vasudevan, Gaur, and Shinde (2006) argue

that, as suggested by reactance theory, constrained freedom of choice for the customer reduces the effect of low levels of satisfaction on commitment. Similarly, other researchers (e.g., Shin and Kim, 2008; Wang, 2010) argue that the relationships between customer loyalty/switching intentions and psychological evaluations (e.g., perceived value and satisfaction) are weaker when switching costs/barriers are high rather than low. Further, this paper argues that if trust/value levels are above average and switching costs are negative (i.e., procedural switching costs), customers are more likely to view switching costs as hygiene factors and a source of disincentives, which in turn weaken the trust/value-loyalty link. Therefore, this paper proposes the following hypotheses:

H8: Procedural switching costs negatively moderate the relationship between trust and customer loyalty.

H9: Procedural switching costs negatively moderate the relationship between customer value and customer loyalty.

### *The Impact of Service Type*

Previous research suggests that the perceived importance of switching costs is contingent on service type. Specifically, Patterson and Smith (2001) argue that strong customer relationships (i.e., relational switching costs) are especially important in high customer-employee contact and customized services. Moreover, Patterson and Smith (2003) found that the loss of a friendly interpersonal relationship and special treatment benefits (i.e., relational and financial switching costs) were perceived as being more important in hairdressers and medical services (high contact services), while the loss of special treatment benefits and the need to explain preferences (i.e., financial and procedural switching costs) were perceived as being more important in travel services (medium/low contact services). In contrast, Jones *et al.* (2002) found that perceptions of setup costs, and pre-switching search and evaluation costs (i.e., procedural costs), were higher for hairstylists than banks. Thus, one could argue

that although customers' perceptions of the importance of procedural and relational costs may vary across service type, the perceived importance of financial switching costs seems to be consistent across high vs. low customer-employee contact and high vs. low customized services.

Based on two-factor theory (Herzberg *et al.*, 1959) and involvement theory (Sherif *et al.*, 1965), this study suggests that in high customer-employee contact and customized services (i.e., those reflecting a high degree of customer involvement), relational and financial switching costs (i.e., motivators) are more likely to positively moderate the relationships between customer-perceived value, trust, and loyalty.

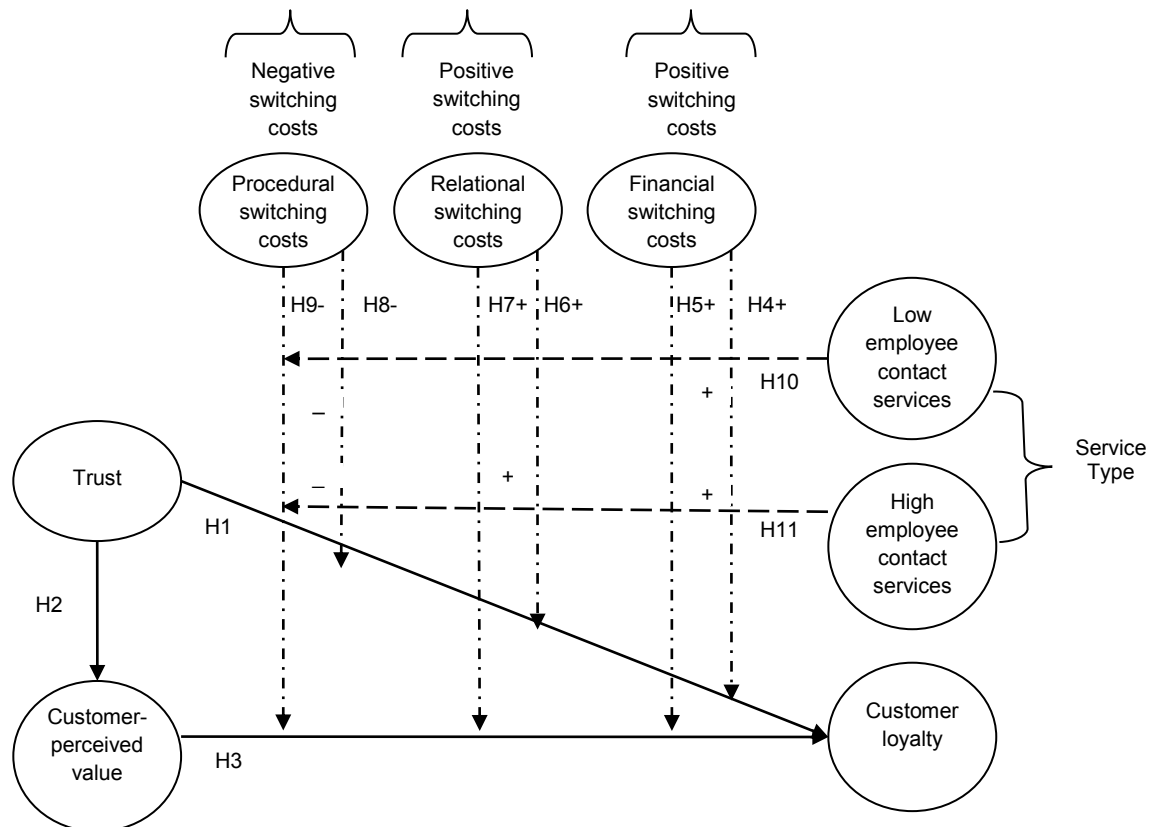
With regard to procedural switching costs (i.e., hygiene factors), this study posits that they are more likely to negatively moderate the relationship between customer-perceived value, trust, and loyalty. In contrast, in medium/low customer-employee contact and standardized services (i.e., those reflecting medium/low degrees of customer involvement), financial switching costs are more likely to positively moderate the relationships between customer-perceived value, trust, and loyalty. Thereby, relational switching costs (i.e., irrelevant motivators) are less likely to moderate the relationships between customer-perceived value, trust, and loyalty, while procedural switching costs are more likely to negatively moderate the relationships between customer-perceived value, trust, and loyalty.

H10a-c: In low contact and standardized services, the relationships between customer loyalty, perceived value, and trust are positively moderated by financial switching costs (a), not moderated by relational switching costs (b), and negatively moderated by procedural switching costs (c).

H11a-c: In high contact and standardized services, the relationships between customer loyalty, perceived value, and trust are positively moderated by financial switching

costs (a) and relational switching costs (b), while being negatively moderated by procedural switching costs (c).

The proposed conceptual framework (see Figure 1) examines the moderator effects of switching costs dimensions on the interrelationships between customer-perceived value, trust, and loyalty.



**Figure 1.** Conceptual model.

## Research Design and Method

A survey design was used to test the conceptual framework across two service contexts. The following section explains in detail the procedure followed.

### Measures

Latent constructs were measured using scales adapted from previous research. Customer-perceived value was measured using four items adapted from Dodds, Monroe, and Grewal (1991), and trust was measured using six items adapted from Morgan and Hunt (1994). Customer loyalty was measured using six items adapted from Zeithaml, Berry, and



Parasurman (1996) in order to reflect behavioral intentions. Relational, procedural, and financial switching costs were measured using three items, each adapted from Burnham *et al.* (2003).

Adding new/additional constructs to the conceptual model was deemed inappropriate, due to the fact that the aim of this study is explanatory (Royston and Asauerbrei, 2008). Moreover, such additions would also increase the complexity of the conceptual model and the statistical analysis. All scales employed a 7-point Likert type scale, anchored by 1 (strongly disagree) and 7 (strongly agree). Prior to the questionnaire's distribution, five academic experts in services marketing were asked to examine face validity (Hair *et al.*, 2006). In addition, a random sample of 40 retail service customers similar to the study population were asked to complete an initial draft of two versions of the questionnaire (one for hairdressers and one for fast-food restaurants). All items demonstrated face validity based on the results from the panel experts and pre-test.

#### *Context, Data Collection, and Sample*

Respondents were asked to answer the questions with their most frequently visited hairdresser and fast-food restaurant in mind. Hairdressers and fast-food restaurant services were selected for both theoretical and practical reasons. First, they reflect two contrasting service characteristics in Bowen's (1990) service taxonomy (high vs. low customer-employee contact and high vs. low degree of customization), allowing for a stronger test of the generalizability of the conceptual model. Second, the necessary conditions for testing the role of trust and switching costs in customer loyalty development are satisfied in these two service contexts (high vs. low perceived risk and high vs. low perceived switching costs). Finally, the preliminary exploratory stage indicated that these two service contexts were best suited to the study's aims. When intercepted in a shopping mall setting, respondents talked freely and easily when asked questions about these particular service contexts.

Data was collected using the mall intercept survey method. Many studies in retailing use mall intercept survey methods (e.g., Sharma *et al.*, 2014; Sharma, 2015), as it is “a relatively inexpensive method of collecting high quality, accurate data in a face-to-face manner” (Bush and Hair, 1985, p. 166). In line with Bush and Hair’s (1985) recommendations, data was collected at various times of the day and on different days of the week in the biggest regional shopping center in Scotland. The chosen regional shopping center comprises “one million square feet of prime retail and leisure space” (Daily Record, 2007) and the journey to the center by car took between 20 and 30 minutes.

Trained undergraduate business students enrolled in marketing courses at one of Scotland’s largest universities were placed at, and rotated around, major stores and they intercepted shoppers as they walked into the mall’s common area. Four hundred questionnaires — 200 for each service industry — were collected over a period of four weeks during the month of February. Collecting data at such a time, when neither promotions nor festival activities were taking place, ensured that the average shopper was represented in the data collected (Sharma *et al.*, 2014).

Three hundred and seventy questionnaires were collected. Ten were excluded due to incomplete responses, which resulted in three hundred and sixty usable questionnaires (90% response rate). Thus, checking for non-response bias was not required (Salant and Dillman, 1994). The sample characteristics were broadly representative of the Scottish population in terms of gender and age (Scotland’s Census, 2011). In the study of fast-food restaurant services, 41.7% of respondents were male and 58.3% were female. For hairdresser services, 47.8% of respondents were male and 52.2% were female. For respondents in both service contexts, the median age was 35-43 years old, and the median household income was £35,000-£55,000. The median age of the sample’s respondents is representative of the Scottish population in terms of age, as the largest age group identified in Scotland’s Census

(2001) was the one comprising 30-44 year olds. The descriptive statistics of all scale items for each construct are shown in Table 2.

Insert Table 2 here

## Results

### *Measurement model results*

Data was analyzed using Analysis of Moment Structure (AMOS 22). Common-method variance was not an issue, as the first factor failed to comprise a majority of the variance and there was no general factor in the un-rotated factor structure (Podsakoff and Organ, 1986). Anderson and Gerbing's (1988) two-step structural equation modeling approach was followed. Thus, the following section reports the results of assessing measurement model validity, followed by assessing structural model validity for fast-food restaurant and hairdresser services. Fit indices including CFIs > 0.90, SRMRs < 0.09, RMSEAs < 0.1,  $\chi^2 / df < 0.3$  (Hair, *et al.*, 2006; Kline, 2005; Hu and Bentler, 1995) indicated adequate model fit.

Model fit. The results for fast-food restaurant services provide adequate fit ( $\chi^2 = 175.32$ ,  $df = 96$ ,  $p = 0.00$ ,  $\chi^2 / df = 1.83$ , CFI = 0.95, RMSEA = 0.07, 90% CI = (0.05 - 0.08), SRMR = 0.05). For hairdresser services, model fit also suggests adequate fit ( $\chi^2 = 204.99$ ,  $df = 96$ ,  $p = 0.00$ ,  $\chi^2 / df = 2.14$ , CFI = 0.96, RMSEA = 0.08, 90% CI = (0.06 - 0.08), SRMR = 0.04). Simultaneous estimation of SEM model fit for both services also suggests a good fit ( $\chi^2 = 380.31$ ,  $df = 192$ ,  $p = 0.00$ ,  $\chi^2 / df = 1.98$ , CFI = 0.96, RMSEA = 0.05, 90% CI = (0.04 - 0.06), SRMR = 0.05). Therefore, the results support the measurement model across the two service contexts.

Convergent validity was assessed using factor loadings, reliability, and variance extracted. As shown in Table 2, for fast-food restaurant services (except two items) and for hairdresser services, all factor loadings are statistically significant and are equal to, or higher than, the 0.7 standard (Hair *et al.*, 2006). Construct reliabilities range from 0.85 to 0.90 and

0.85 to 0.94 for fast-food restaurant and hairdresser services respectively, suggesting adequate reliability (Nunnally, 1967). The VE estimates per construct (see Table 3) range from 0.50 percent to 0.66 and 0.52 percent to 0.73 for fast-food restaurant and hairdresser services respectively, providing support for convergent validity (Bagozzi and Yi, 1988).

Insert Table 3 here

Discriminant validity is evident (see Table 3) in both service contexts because the AVE of each construct is higher than the squared correlations between each pair of constructs (Fornell and Larcker, 1981). Discriminant validity is also supported, as the CFA model does not contain any cross-loadings, either among the measured variables or among the error terms (Hair *et al.*, 2006).

Nomological validity is also evident (see Table 3) for both fast-food restaurant and hairdresser services, as most constructs are positively correlated to one another (Peter, 1981). More specifically, customer loyalty is positively correlated with customer-perceived value, trust, and procedural switching costs. Relational, financial, and procedural switching costs are also positively interrelated. Four correlations are inconsistent with the hypotheses. For fast-food restaurant and hairdresser services, the correlation between customer loyalty and financial switching costs is positive, but statistically insignificant (0.12 and 0.06, respectively). Similarly, for fast-food and hairdresser services, the correlation between customer loyalty and relational switching costs is positive, but statistically insignificant (0.00 and 0.03, respectively). A possible explanation is that financial and relational switching costs may have an indirect effect on loyalty. Interestingly, customer-perceived value is positively correlated with relational switching costs in fast-food services and negatively correlated with relational switching costs in hairdresser services. This may be due to the fact that in low versus high employee contact and customized services, opportunities to enhance customers'

perceived value by building relational switching costs are quite low, due to the transactional nature of the exchange.

Overall, considering the convergent, discriminant, and nomological validity results, the measurement model for fast-food restaurant and hairdresser services appears to satisfy all psychometric requirements.

#### *Structural model results*

Model fit. The results for fast-food restaurant services provide adequate fit ( $\chi^2 = 175.32$ ,  $df = 96$ ,  $p = 0.00$ ,  $\chi^2 / df = 1.83$ ,  $CFI = 0.95$ ,  $RMSEA = 0.07$ ,  $90\% CI = (0.05 - 0.08)$ ,  $SRMR = 0.05$ ). For hairdresser services, model fit also suggests adequate fit ( $\chi^2 = 204.99$ ,  $df = 96$ ,  $p = 0.00$ ,  $\chi^2 / df = 2.14$ ,  $CFI = 0.96$ ,  $RMSEA = 0.08$ ,  $90\% CI = (0.06 - 0.08)$ ,  $SRMR = 0.04$ ). Simultaneous estimation of SEM model fit for both services also suggests a good fit ( $\chi^2 = 380.31$ ,  $df = 192$ ,  $p = 0.00$ ,  $\chi^2 / df = 1.98$ ,  $CFI = 0.96$ ,  $RMSEA = 0.05$ ,  $90\% CI = (0.04 - 0.06)$ ,  $SRMR = 0.05$ ). Therefore, these results support the structural model across the two service contexts.

Direct effects. Hypotheses testing revealed that, as expected, for fast-food restaurant services and hairdresser services the effects of trust on customer perceived value ( $b = 0.54$  and  $b = 0.87$ , respectively) and customer loyalty ( $b = 0.48$  and  $b = 0.64$ , respectively) were statistically significant. Further, the effects of customer-perceived value on loyalty were also statistically significant for fast-food restaurant services and hairdresser services ( $b = 0.32$ , and  $b = 0.29$ , respectively). The next step was to test for the moderator effects of switching costs dimensions, in order to gain deeper insights into the relationships between trust, customer-perceived value, and loyalty.

Moderation effects. Multi-group structural equation modeling was considered an appropriate method because the analysis considered relationships between latent constructs. Switching costs dimensions were divided into high and low groups using median split (Baron

and Kenny, 1986). The null hypothesis that switching costs dimensions have no moderating effect on the relationships between trust, customer-perceived value, and loyalty was tested by conducting an overall chi-square difference test to compare a restricted model (RM) with a non-restricted model (NRM). If the change in chi-square value between the two models is statistically significant, and if the effect is in the hypothesized direction, a moderator effect is supported in general. For fast-food restaurant services, with two more degrees of freedom, the restricted model exhibits a statistically significant chi-square difference (at  $p < .05$ ) for financial switching costs (Table 4), but not for procedural and relational switching costs. In contrast, for hairdresser services, with two more degrees of freedom, the restricted model exhibits a statistically significant chi-square difference (at  $p < .05$ ) for financial and procedural switching costs (Table 4), but not for relational switching costs. The findings show that financial and procedural switching costs, in general, are relevant moderators in the context of the relationships between trust, customer-perceived value, and loyalty.

Insert Table 4 here

To test for specific moderating effects, the change in chi-square between the restricted model (RM) and two models, for which one path at a time is allowed to vary freely across the two groups, was then compared for each of the three moderators. As shown in Table 4, the change in chi-square with 1 degree of freedom indicates four statistically significant relationships. More specifically, the results suggest that for both fast-food restaurant and hairdresser services, perceived financial switching costs (i.e., high versus low) positively moderate the relationships between trust and customer loyalty ( $p < .00$  and  $p < .05$ , respectively). Financial switching costs positively moderate the relationship between customer-perceived value and loyalty for hairdresser services but not for fast-food restaurant services ( $p > .05$ ). Perceived relational switching costs have a statistically insignificant moderator effect on the relationship between trust, customer-perceived value and loyalty for

both fast-food restaurant and hairdresser services ( $p > .05$ ). Perceived procedural switching costs have a statistically insignificant moderator effect on the relationship between trust and customer loyalty for both services ( $p > .05$ ). In contrast, procedural switching costs positively moderate the relationship between customer-perceived value and customer loyalty for hairdresser services only ( $p < .05$ ).

### **Discussion and Implications**

The results of this study highlight the differential moderator effects of switching costs and service type on the interrelationships between customer-perceived value, trust, and loyalty. While trust and customer-perceived value continue to be important determinants of customer loyalty, their effects are strengthened or weakened based on customers' perceptions of specific types and directions of switching costs. Moreover, the strength of the moderator effect is contingent on service type. Financial switching costs play more of a general moderating role (applicable across various service characteristics), procedural switching costs play a more specific moderating role (applicable across specific service characteristics), and relational switching costs playing no moderating role (not applicable across various service characteristics).

Interestingly, the results indicate that financial switching costs positively moderate the relationship between trust and customer loyalty for both low customer-employee contact and standardized services and high customer-employee contact and customized services. In other words, the relationship between trust and loyalty is stronger when customers perceive high financial switching costs. Therefore, H4 is supported. The results suggest that trust is the most effective loyalty enhancement strategy across various service types when customers perceive high financial switching costs. This indicates that positive losses (e.g., losing monetary benefits, special treatment, and recognition) can be viewed as incentives to remain loyal as they increase customers' perception of benefits and reduce their perceived anxiety.

This, in turn, strengthens the relationship between trust and customer loyalty. These results are consistent with previous research findings (e.g., Jones *et al.*, 2002; Patterson and Smith, 2003), which found that lost performance costs and the loss of special treatment benefits (financial switching costs) have a strong impact on loyalty.

Financial switching costs positively moderate the relationship between customer-perceived value and customer loyalty only for high customer-employee contact and customized services. In other words, the relationship between customer-perceived value and customer loyalty is stronger when customers of this type of service perceive high financial switching costs. Therefore, H5 is partially supported.

The results suggest that customer-perceived value is the most effective strategy for maintaining customer loyalty for this specific type of service characteristic and when customers' perceive high financial switching costs. A plausible explanation for this finding is that, for high customer-employee contact and customized services, the decision to remain loyal is determined by customers' perception of overall utility (i.e., the tradeoff between costs and benefits), which is further enhanced by customers' desire to avoid losing monetary and/or non-monetary benefits (e.g., recognition and discounts). In contrast, for low customer-employee contact and standardized services, consumers' perceptions of perceived value are above average due to high competition and service standardization. Therefore, customers' decisions to stay are more likely to be influenced by their perception of value, rather than the loss of benefits (e.g., losing discounts). This result is inconsistent with Woisetschläger *et al.*'s (2011) finding of a negative moderating effect of economic switching barriers on the relationship between satisfaction (a closely related construct to perceived value) and loyalty intentions in the newspaper subscription context. A possible explanation, within the aforementioned contractual context, is that when customer satisfaction is below average, a



customer's decision to remain loyal is determined by their perception of losing benefits, rather than satisfaction.

As expected, the results indicate that relational switching costs have no moderator effect on the relationship between trust and customer loyalty in low customer-employee contact and standardized services. Surprisingly, although the impact of trust on customer loyalty increases when customers perceive high relational switching costs in high customer-employee contact and customized services, the impact is statistically insignificant at the 0.05 level. Therefore, hypothesis 6 is partially supported. A plausible explanation is that, in low customer-employee contact and standardized service industries, consumers' chances of perceiving personal losses are low. Therefore, customers' decisions to remain loyal are more likely to be a function of their perceived trust or confidence benefit. Here, recourse to Jones *et al.*'s (2000) view of the contingent moderator effect of switching costs on the level of the independent variable is useful. A possible explanation for the lack of a statistically significant moderating effect of relational switching costs in high customer-employee contact and customized services is that customers' perceived trust is above average. Therefore, customers' decisions to stay are more likely to be determined by perceived confidence benefits in the service provider rather than by perceived positive losses (e.g., relational bonds). In other words, relational switching costs can only affect customers' loyalty intentions if their perceived level of trust is below average.

Similarly, the results indicate that relational switching costs have no moderator effect on the relationship between customer-perceived value and customer loyalty in either service context, thus providing partial support for H7. Therefore, customers' decisions to remain in these service contexts are more likely to be influenced by their perception of value. However, customers in high customer-employee contact and customized services may consider relational losses as an incentive to remain if perceived value is below average. This finding is

consistent with Burnham *et al.*'s (2003) findings of there being no moderating effect on relational switching costs in the relationship between customer-perceived value and customer loyalty. The lack of consistency with Woisetschläger *et al.*'s (2011) findings of a negative moderation effect of social ties on the satisfaction-loyalty intentions link could be due to the nature of contractual transactions (e.g., newspaper subscriptions), which may lead to the development of stronger relational bonds.

Procedural switching costs have no statistically significant moderator effect on the relationship between trust and customer loyalty in both service contexts. Therefore, H8 is not supported. This is consistent with Yang and Peterson (2004), who found that the moderating effect of switching costs on customer loyalty are not always statistically significant, in addition to being contingent on situational variables (e.g., types of customers). A possible explanation may be that due to increased customer literacy and advancements in technology and deregulation, switching between alternative service providers is becoming easier. Thus, the direct and indirect effect of procedural switching costs on loyalty is likely to be reduced. Further, the lack of moderating effect may be explained by the conflicting roles of procedural switching costs (negative motivation to stay) and trust (positive motivation to stay). These opposing forces, therefore, could lead to the lack of a statistically significant interaction effect (Yang and Peterson 2004).

Procedural switching costs negatively moderate the relationship between customer-perceived value and customer loyalty only for high customer-employee contact and customized services ( $p < .05$ ). Therefore, H9 is partially supported. One could argue that due to the high degree of customization in these service industries, customer perceived losses of switching (e.g., the need to explain preferences, recognition, and perceived risk) are likely to be high. While these can motivate customers to remain loyal, they in turn weaken the relationship between value and customer loyalty. In contrast, the lack of moderating effect in

low customer-employee contact and standardized services may be explained by the fact that consumers' chances of perceiving high procedural costs (e.g., losing time and effort) in finding alternative service providers are likely to be low due to high competition and service standardization. Therefore, customers' decisions to remain loyal are likely to be influenced by perceived value, rather than perceived negative losses. This finding is consistent with Wang's (2010) finding of a statistically significant moderating effect of procedural costs on the perceived value-loyalty link in hairdresser services. It is also consistent with Jones *et al.*'s (2002) finding of there being higher perceptions of procedural costs in hairdresser services than banks.

In terms of theoretical implications, this study advocates that a more complex view of switching costs (classified by type and direction) provides a more sophisticated understanding of the moderating role of switching costs in loyalty frameworks. The findings empirically confirm the importance of differentiating between positive and negative switching costs. Additionally, they indicate that a uni-dimensional view may be too simplistic, thereby potentially obscuring important theoretical and managerial implications. Consequently, this study shifts academic interest away from a focus on understanding the interrelationships between trust, perceived value, and customer loyalty to a focus on understanding the boundary conditions of these interrelationships. Further, the inclusion of service type in the conceptual model provides a more detailed assessment of how customer loyalty intentions are not only influenced by firm and customer-related switching costs, but also by industry-related switching costs.

This sophisticated understanding is required in order to explain, for instance, why specific groups of customers remain loyal to specific service industries with specific types of switching costs. Any analysis that fails to consider the simultaneous moderating effect of switching costs classified by type, direction, and service type on the interrelationships

between trust, perceived value, and loyalty intentions is likely to provide not only an incomplete understanding, but to add to existing inconclusive results.

This paper is unique in carrying out a simultaneous examination of three different types, and two distinct directions, of switching costs across two contrasting service categories. The paper also has important practical implications. The findings suggest that managers can still rely on customer-perceived value and trust as loyalty building and enhancement strategies, but that the effectiveness of these strategies varies. Specifically, managers must decide whether customer-perceived value or trust is the most effective loyalty strategy in specific service industries with specific types of perceived switching costs. For example, managers across various service types should invest in building financial switching costs but avoid investing in relational switching costs, as they seem to have no impact on enhancing loyalty. In contrast, service managers in high employee contact and customized services should invest in building procedural switching costs in order to enhance customer loyalty. The conventional wisdom among service managers is that the higher the switching costs are, the higher customer loyalty and profitability will be. Paradoxically, the present findings suggest that spending a substantial amount of money on interpersonal marketing programs in order to retain customers (Chiu, *et al.* 2005) may not be the most effective strategy. Customers' loyalty decisions across various service categories are less likely to be determined by a desire to avoid losing strong social bonds with a service provider.

Managers in high customer-employee contact and customized services (such as dentists, legal services, and real estate agencies) should concentrate on building financial and procedural types of switching costs in order to increase loyalty intentions. Specifically, managers should focus on offering monetary and non-monetary benefits (e.g., special treatment, customized services, discounts, and recognition benefits) not only to increase customers' perception of intrinsic value, privileges, and confidence benefits but to reduce

customer anxiety in the service exchange. Further, managers in this service category should also offer convenient, co-created, and well-explained services in order to increase customers' perception of both risk and the time and effort involved in switching. In contrast, managers in low customer-employee contact and standardized services (such as cafeterias, theme parks, and budget airlines) should devote their resources to building only financial switching costs (e.g., competitive prices and efficient, easy to use services) in order to motivate their customers to remain loyal. Customers' decisions to remain loyal in these service industries are less likely to be determined by the creation of psychological and relational constraints. Table 5 provides more detailed suggestions that managers can cross-fertilize across similar service contexts.

Insert Table 5 here

Managers should also expend effort in identifying customer groups with stronger/weaker relationships. Specifically, for customer groups with a stronger relationship between perceived trust and customer loyalty, managers should use their limited resources to train service employees to demonstrate competence, a better understanding of customer needs, and to deliver reliable services. For customer groups with a stronger relationship between perceived value and loyalty, managers should focus on enhancing the economic value of the exchange by offering competitive service pricing and efficient, good quality services. In contrast, for customers with a weaker relationship between perceived value, trust, and customer loyalty, managers need to focus on creating procedural switching costs (e.g., explaining medical/legal preferences, co-creating the service, and increasing the perceived risk of switching to alternative provider) in order to make it difficult for this group of customers to switch.

It should be noted that building negative switching costs is only appropriate for firms offering good value and trustworthy services who may need to develop a defense mechanism

against inevitable changes in customers' evaluations. If customers feel that they are trapped in a service exchange, this may lead to the development of spurious loyalty or adverse behavioral outcomes.

### **Future Research Directions and Limitations**

This study concludes by noting some limitations, and by making recommendations for future research directions. First, customer loyalty, trust, and perceived value may consist of multiple dimensions (Oliver, 1999; Sweeny and Soutar, 2001). Thus, further studies could consider a multi-dimensional view in order to verify the results. Second, to better assess causality, future research could assess the current model using an experimental or longitudinal design. For example, trust and customer-perceived value could be manipulated while switching costs are measured. Third, customers in only two service industries have been investigated; thus, the results must be validated in other service industries before generalizations can be made. In line with Homburg and Giering (2001), only the moderating impact of switching costs on the strength of the relationships between customer-perceived value, trust, and loyalty was investigated. Hence, there was no analysis of whether these moderators also affect the functional form of the relationships between trust, customer-perceived value, and loyalty. The findings also highlight the need for more comprehensive models of the relationships between customer-perceived value, trust and loyalty.

As the current model focuses on selected types of moderators (i.e., switching costs), future research should examine other types of moderators that may affect the strength of the relationships between trust, customer-perceived value, and loyalty, such as channel type, expertise, and alternative attractiveness. Future research, therefore, should build upon these findings and attempt to provide further insight into the nature of the relationships between customer-perceived value, trust, and loyalty under different boundary conditions.

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