

# **BUILDING LOYALTY: CREATING VALUE THROUGH CUSTOMER EXPERIENCES**

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## **ABSTRACT**

A review of the academic and practitioner literature on customer relationship management indicates a general consensus that quality, value, and satisfaction are critical variables in explaining customer loyalty in tourism services, yet, although much is known about the relationship between the aforementioned variables and customer loyalty, they don't fully explain how customer loyalty is built. This paper argues that one critical variable has been excluded from consideration that impacts on customer loyalty, explicitly customer experiences. Therefore, the purpose of this paper is to rectify this significant gap in the literature and present a relatively new perspective of customer loyalty that recognises that the customer has to interact with the components of a service in order for the service to become 'real' (Echeverri 2005) and that the successful management of customer experiences leads to a differentiated competitive advantage (Smith and Wheeler 2002). Based on the literature reviewed, observations are drawn for future theoretical and empirical development in the field of customer loyalty.

## **INTRODUCTION**

Over the past decade, unprecedented economic growth has seen Ireland's GDP almost double in size. In line with this overall economic experience, the Irish tourism industry has become a major economic sector of enterprise and of national and regional wealth creation. Indeed, the industry at present constitutes approximately 16,000 tourism enterprises, generates €4 billion in revenue earnings, employs 140,000 people and is currently the largest, Irish-owned internationally traded sector within the economy. However, as The Tourism Policy Review Group (TPRG) 2003 notes, the landscape is changing and the tourism industry is at a significant turning point in its evolution: (1) due to unparalleled economic growth, the tourism industry has seen a "significant loss in competitiveness, which if not redressed, will undermine the capacity of the industry to benefit the strong economic growth envisaged in

international tourism in the years ahead” (2003: 40), (2) while the tourism industry has matured, it still is characterized by the dominance of individual, small to medium sized enterprises competing in an increasingly global international tourism marketplace. The consequence is that there is weak access to market and operational intelligence, a lack of management resources and market power and little or no financial institutional backing and (3) there is a tendency amongst small Irish tourism firms to adopt the ‘complacency syndrome’ where there is little flexibility and adaptability of products to the changing needs of customers. In recognition of these challenges, enhancing the tourist experience to build customer loyalty was identified as a key strategic success driver to create a stronger competitive capacity in Irish tourism companies (The Tourism Policy Review 2003). The tourism company operates in an extremely competitive industry, which is primarily characterised by continuous transformation (Wahab and Cooper, 2001). Therefore, the competitiveness of the tourism firm depends on their innovativeness in achieving customer loyalty through a service quality, satisfaction and customer oriented strategy (Wiljinson et al., 1998). Indeed, leading edge tourism companies such as the Four Seasons group and the Forte Hotel Group are increasingly recognizing the importance of building customer loyalty as a strategic business objective (Erstad, 2001). This rests on customer relationship management’s central premise that a firm’s overriding strategy should be the attraction and retention of profitable customers because loyal customers will, in the long-term, buy more and pay a premium for doing business with those they trust and like (Peppers and Rogers, 2004).

However, in spite of the considerable research efforts in many salient fields of enquiry, such as customer relationship management, consumer behaviour, marketing and business strategy, service management and human resources, no acceptable theory exists that fully explains how customer loyalty is built. The latter may, at least partially be attributed to the fact that most research on customer loyalty has tended to focus on the inter-relationships between customer satisfaction, service quality, and loyalty as an explanation (Cronin et al., 2000; Payne et al., 2000; Loveman and Heskett, 1999; Reichheld, 1996; Parasuraman et al., 1991; 1988; Cronin and Taylor, 1992; Reichheld and Sasser, 1990) - a perspective which has been heavily criticized (Berry & Carbone, 2007; Dube and Renaghan, 2000; Pine and Gilmore, 2000; 1999). Underpinning the central argument of this paper is that one critical variable has been

excluded from consideration that impacts on customer loyalty, explicitly customer experiences.

This article, therefore seeks to extend the conceptualization on building customer loyalty amongst tourism firms by identifying the conceptual deficiencies of past research. This paper also presents on customer loyalty that recognises that the customer has to interact with the components of a service in order for the service to become 'real' (Echeverri, 2005) and that the successful management of customer experiences leads to a differentiated competitive advantage (Smith and Wheeler 2002). As such the objectives of this article are to:

1. To synthesise and analyse the literature on customer loyalty in order to assess the research progress in the area;
2. To re-think the conceptualisation of building customer loyalty;
3. To provide insights for future theoretical and empirical development in the field of customer loyalty.

### **THE EXTANT CONCEPT OF BUILDING CUSTOMER LOYALTY**

According to Jacoby and Kyner, loyalty "is (1) biased (i.e. non random), (2) behavioral response (i.e. purchase), (3) expressed over time, (4) by some decision making unit, (5) with respect to one or more brands out of a set of such brands, and is function of psychological (decision making evaluative) processes" (1973: 2). Incorporating this concept of loyalty, several competing loyalty building models have been proposed: (1) some quality models argue that service quality only impacts loyalty via satisfaction and value (Patterson and Spreng, 1997; Woodruff, 1997), others maintain that quality has a direct impact (Zeithaml et al., 1996; Parasuraman et al., 1991; 1988), (2) drawing from the service literature, the value model maintains that value leads directly to the favorable outcome customer loyalty and that both service quality and satisfaction are precursors of value (Sweeney et al., 1999; Cronin et al., 1997; Gale, 1994), (3) the satisfaction model shows that customer loyalty is directly influenced by the variable satisfaction (Hallowell, 1996; Fornell et al., 1996; Anderson and Fornell, 1993), and (4) Oh (1999) proposed an integrative model of service quality, customer value and customer satisfaction. The model incorporates key variables such as perceptions, service quality, consumer satisfaction, customer value

and intentions to repurchase. The model suggests that customer value has a significant role in customer's post-purchase decision-making process. It indicates that value is an immediate antecedent to customer satisfaction and repurchases intentions. Although researchers hold differing conceptualisations of loyalty and the both the direct and indirect relationships of its major determinants, explicitly, value, satisfaction and quality, they all, nevertheless, agree that these three variables are important dimensions for building loyalty (Salegna and Goodwin, 2005; Cronin et al., 2000; Fornell et al., 1996; Cronin, 1992).

### *Service Quality*

Service quality is defined as the comparison customers make between their expectations about a service and their perceptions of the actual service performance (Parasuraman et al, 1994, 1988, 1985; Grönroos, 1984, Lewis and Boom, 1983). Research findings are mixed as to the relationship between quality and loyalty. In an investigation of four service providers, Zeithaml et al., (1996) observed a significant relationship existed between service quality and loyalty. Cronin and Taylor (1992) show divergent results and did not find a direct relationship between quality and loyalty. Indeed, they concluded that service quality had less of an impact on purchase intentions than did consumer satisfaction and that quality is an antecedent of the latter. For Cronin et al., (2000) this apparent contradiction is an indication that quality provides only a partial view of customer loyalty and that

“models of consumers’ evaluations of services that consider individual variables or direct effects are likely to result in incomplete assessments of the basis of these decisions. Thus, the services manager who only considers the likely effect of a service quality initiative on his or her customers’ behavioural intentions errs if he or she does not also consider the impact of such a strategy on the value and satisfaction attributed to his or her firms services” (210).

Collaborating evidence to support this logic was provided by Cronin et al., (2000) who found an indirect relationship between quality and loyalty through satisfaction and value independently of each other. This would indicate that quality has a link to the other variables in determining behavioural intentions and ultimately loyalty. In the loyalty building in figure it is proposed that quality has direct impact on customer loyalty and indeed a indirect impact via the value and satisfaction variables.

### ***Customer Value***

For Woodruff (1997) value is a “customer’s perceived preference for and evaluation of that product attributes, attribute performances, and consequences arising from use that facilitate (or block) achieving the customers goals and purposes in use situations” (176). Indeed, many marketing strategists and industrial organisational economists have stressed that the creation of customer value is one of the crucial variables involved in determining customer loyalty and ultimately ensuring a company’s success (Higgins, 1998; Kordupleski and Laitamaki, 1997; Reichheld, 1996; Gale, 1994). However, the relationship between customer value and loyalty still remains ambiguous within the literature. For instance, Sirdeshmukh, et al. (2002) found that value had a direct relationship with customer loyalty. In their study of assessing the effects of quality, value, and customer satisfaction on consumer behavioural intentions in service environments, Cronin et al (2000) found both direct and indirect effects of service value on behavioural intentions. These authors perceive that considering only value as an explanation for loyalty is likely to give an incomplete assessment as to the basis of loyalty. For Patterson and Spreng (1997), the positive relationship between value and loyalty is interceded by satisfaction, further indicating that value does not on its own fully explain the loyalty concept. Additionally convergent evidence suggests that service quality is a critical determinant of perceived value (Cronin et al., 2000; Bolton, 1991), which, in turn, impacts on satisfaction (Cronin et al., 2000; Day and Crask 2000; Patterson and Spreng, 1997; Woodruff, 1997) in determining behavioural intentions and loyalty (Cronin et al., 2000)

### ***Customer Satisfaction***

Customer satisfaction has received considerable attention due to its importance in the customer relationship management literature and its impact on customer loyalty (Cronin et al, 2000; Cronin and Taylor, 1992; Oliver 1980). Numerous studies show that a relationship exists between value and satisfaction. Satisfaction is perceived as being both an evaluative and emotional based response to the service encounter (Oliver, 1997) and is the result of a customers perception of the value received in a transaction or relationship – where value equals perceived service quality relative to

price and customer acquisition costs (Heskett et al., 1990) - relative to the value expected from transactions or relationships with competing vendors (Zeithaml et al., 1990). Loyalty behaviors such as relationship continuance, increased market share and recommendation (word-of-mouth) results from customer's beliefs that the quantity of value received from one supplier is greater than that available from other suppliers (Hallowell, 1996). Indeed, much of the literature on the influence of customer satisfaction on building customer loyalty has been positive and generally implies that satisfaction is one of the determinants of customer loyalty (Hoisington and Naumann, 2003; Cronin et al., 2000; Gronholdt et al., 2000; Anderson and Fornell, 1994; Heskett et al., 1990; Cronin and Taylor 1992; Reicheld and Sasser, 1990; Zeithaml et al. 1990; Oliver 1980).

However, others studies have found that satisfaction has a less of a significant impact on customer loyalty than is traditionally perceived in the literature (Khatibi et al., 2002; Bowen and Chen, 2001). Indeed, Reichheld (1996) argues that although satisfaction is one of the necessary components for building loyalty, it does not necessarily guarantee loyalty. Bennet and Rhundle-Thieles'(2004) analysis of 267 businesses found that high satisfaction does not necessarily result in high loyalty which further illustrates that although loyal customers need to be satisfied, satisfied customers are not necessarily loyal.

A review of the academic and practitioner literature on customer relationship management indicates a general consensus that quality, value, and satisfaction are critical variables in explaining customer loyalty, nevertheless, this extant concept of loyalty which has served the research needs of the scientific community for the past 40 years and has produced valuable insights into the process of building customer loyalty, is been criticised to a great extent (Salenga and Goodwin, 2005; Cronin, 2003; Smith and Wheeler, 2002; Dube & Renaghan, 2000; Cronin et al., 2000; Cronin and Taylor, 1992). The criticism relates mainly to the fact that it has become generally accepted amongst most loyalty researchers to assume that the variables quality, value, and satisfaction are sufficient to building loyalty, to the exclusion of any new constructs. It is our view that one critical variable has been excluded from consideration that impacts on customer loyalty, explicitly customer experiences. In

addition, we believe that the following arguments can be directed against the extant concept of customer loyalty:

1. The interrelationships between the variables of value, quality and satisfaction in building customer loyalty remain relatively unresolved and contradictory in the literature (Cronin et al., 2000). This knowledge deficit has implications for both practitioners and researchers. Without a clearer understanding by academics of how customer loyalty is built the existing gap between what academics are prescribing and what practitioners are practising will remain. Building customer loyalty without an understanding of how firms can achieve it can lead to a misapprehension of the importance of variables or even their omission from this process.
2. For Cronin (2003), there is a need to move away from the traditional quality → value → satisfaction → loyalty model to a new and more dynamic model for building customer loyalty, which incorporates new variables in order to enrich our understanding and bring a more holistic perspective to customer loyalty building. One such variable which has been identified in the customer relationships management literature is “customer experiences”. This variable has received limited research in terms of building customer loyalty. Indeed, it is perceived that customer experience is a highly relevant component involved in both customer relationship management and in building customer loyalty. With the exception of Dube and associates (Berry and Carbone, 2007; Dube and Renaghan, 2000; Pine and Gilmore, 2000; 1999) little research exists and none in the Irish context, which examines this relationship thus there is a considerable gap that exists in academic knowledge. Therefore, this paper suggests an alternative approach for the conceptualization of building customer loyalty - one that recognises the customer experience as a critical component in building customer loyalty.

## **RE-THINKING THE CONCEPTUALISATION OF CUSTOMER LOYALTY IN TOURISM TO INCLUDE THE CONCEPT OF EXPERIENCES**

In order to incorporate the experience concept as a critical component of building customer loyalty, it is first necessary to define what is meant by the term. According



to the Oxford English dictionary, the term experience is defined as the “actual observation of or practical acquaintance with facts or events” (Swannell, 1992: 369). Within the services literature, the depiction of *actual* and *practical acquaintance* is analogous to Echeverri’s (2005:3) definition of services “as something that becomes “real” when a customer interacts with some specific prerequisites – such as organisational structures, activities, people, and other customers. Customers will always have an actual experience when they engage with a service provider (Mascarenhas et al., 2006). For Berry et al. (2006), this service experience is actually “a series of discrete sub-experiences that is full of messages that impact how customers feel and tell a story about the service and company that provides it” (Berry et al., 2006:53). The experience becomes memorable when the company engages their customers in inherently personal ways (Mascarenhas et al., 2006; Anderson et al., 2006; Bendapudi and Bendapudi, 2005). However, for Pine and Gilmore (1999: 2), it is important to realise that actual experiences are distinct from services in that “when a person buys a service, he purchases a set of intangible activities carried out on his behalf. But when he buys an experience, he pays to spend time enjoying a series of memorable events that a company stages – as a theatrical play-to engage him in a personal way. This implies that creating customer’s experiences are embedded in the performance of a company’s ability to personalise specific prerequisites (Mascarenhas et al., 2006). For Berry et al. (2006: 43), these embedded experience prerequisites or clues allow customers to “form perceptions based on the technical performance of the service (functional clues), the tangibles associated with the service (mechanic clues), and the behaviour and appearance of service providers (humanic clues)”. It is these functional, mechanic and humanic clues that influence the customers’ rational and emotional perceptions of the quality of the service and creates the actual service experience (Berry and Bendapudi, 2003). Based on this perception of the concept, each one of these experience clues will now be discussed in turn.

## **FUNCTIONAL CLUES**

For Berry et al. (2006), functional clues are concerned with the technical quality of the service offering, specifically the reliability and competence of the actual service. Its presence or absence can have a serious impact on the creation of the customers’ experience. Indeed, the importance of getting this clue right the first time was clearly illustrated by Keaveney’s (1995) study on why customers switch service suppliers;

they found that 44 percent of customers attributed switching to a failure in the actual quality of the product/service. From the literature, a number of clues have been attributed to impinging on the actual products/services provided in the total customer experience. According to Tucker (1991), the speed of the service process and delivery is important and depends on both the accessibility and the location of the product or service. Convenience is also a vital clue to be considered and is reflected in how well the service matches the needs and expectations of the customer such as opening times range of services/products provided and the extent the product/service is customised (Tucker, 1991 ). For Rowley (1994), keeping up with technology has probably become one of the most important clues for all businesses to improve the core product/service provided.

Indeed, it is fundamental for the service experience that businesses evaluate and manage the functional clues of their core product/service effectively to meet their customers' service expectations (Berry et al., 2006). However, functional clues alone are not sufficient enough to exceed customer's expectations, as customers generally expect a business to know their core product/service and to provide this as promised (Berry and Carbone, 2007). Therefore two other sets of clues are also important, mechanic and humanic clues.

### **MECHANIC CLUES**

Mechanic clues are drawn from inanimate objects or environments and offer a physical representation of the service. For example, building design, equipment, furnishings, displays, colours, sounds, smells, lighting and other sensory clues visualise the service, communicating with customers without words (Haeckel et al., 2003). While a variety of terms have been utilized by scholars to explain this concept such as "the physical environment" (Baker, 1987), "atmospherics" (Kotler, 1973), "marketing environment" (Turley and Milliman, 2000), "service environment" (Cronin, 2003) and "servicescapes" (Booms and Bitner, 1981), there is, nevertheless, a common theme that the mechanic clues encompass "the environment in which the service is assembled and in which the seller and consumer interact, combined with tangible commodities that facilitate performance or communication of the service" (Booms and Bitner, 1981: 36). For this paper we will utilise the term "servicescapes" in an attempt to explain mechanic clues. Numerous studies provide collaborating

evidence that servicescapes has a strong impact on a customer's behavioural intentions and loyalty (Foxall and Yani-de- Soriano, 2005; Cronin, 2003; Foxall and Greenley, 1999) which leads them to either continue or discontinue doing business with a certain service provider (Tombs and McColl-Kennedy, 2003; Hoffman and Turley, 2002). Indeed Palmer, (2005) maintains that the servicescape must be efficient and effective in order for the customer to respond efficiently and effectively to the supplier indicating that customers respond to their environment as a whole, after assessing the effects of all clues present. There is general agreement in the literature that servicescapes are composed of three dimensions:

1. Ambient conditions include background characteristics of the environment such as temperature, lighting, noise, music, and scent.
2. Spatial layout and functionality refers to the physical surroundings of the service environment such as the positioning of equipment/furniture, the size, the shape and the spatial relationship between the objects. The functionality is the ability of these items to assist and support in the achievement of a customers' objectives and enjoyment.
3. Signs, symbols and artefacts are clues in the servicescape that communicate information and messages about the environment to the consumers. Items such as signage and décor are utilized to communicate and enhance a certain image or mood, or to direct customers to desired destinations (Bitner, 1992).

For Bitner a customer's environmental perception is affected by these three dimensions and "each dimension may affect the overall perception independently and/or through its interactions with other dimensions" (1992: 65). Clue congruency in both tangible and intangible dimensions is crucial to the servicescape concept and in the creation of the service experience (Hoffman and Turley, 2002, Bitner, 1992).

## **HUMANIC CLUES**

Humanic clues are concerned with the actions and appearance of employees and the service providers such as the choice of words, tone of voice, and level of enthusiasm, body language, neatness and appropriate dress (Berry et al., 2006). Human interaction provides a good opportunity in which to convey respect and high regard to the customers and, as a result, exceed their expectations and create an emotional involvement (Berry and Carbone, 2007).The extant literature has suggested that

employee performance and interaction is an important humanic clue in the creation of the actual customer experience (Berry and Carbone, 2007; Berry et al., 2006; Rowley, 1994; Bitner, 1992). The quality of the person-to-person interaction between an employee and a customer (known as a “service encounter,”) is an important basis for how a customer judges the service experience (Hennig-Thurau, 2004; Czepiel et al., 1985). Indeed, extensive service quality research has found that service employee’s behaviour affects the customer’s perception of the service (Zeithaml et al., 1996; Bitner , 1990; Parasuraman et al., 1985).

It is fundamental for companies to identify the mechanic clues of an employee’s behaviour and performance in order to meet and exceed customer’s expectations (Berry et al., 2006). Recent research conducted by Specht et al. (2007) discovered that perceived employee effort is more important for customer satisfaction than are perceived abilities, suggesting that managers should focus predominantly on effort, including performance elements that represent social competence. Similarly, in a study based on restaurant tipping, Lynn and Grassman (1990) discovered that both the number of courses ordered and bill size positively related to the amount of tip given and concluded that bill size and the number of courses both measured the server’s effort, hence customers were rewarding the server’s perceived efforts. This would further suggest that perceived effort leads to customer satisfaction. Subsequently, the employee performance is crucial to the humanic clue aspect of the actual customer (Berry et al., 2006).

### **THE LINK BETWEEN QUALITY, VALUE, SATISFACTION AND EXPERIENCES IN BUILDING LOYALTY**

Research has found that there is a link between quality and experience, for example, both Ing-san and Der-Jang (2005: 4) and Zeithamal and Bitner (2000) found that “the quality of service achieved relies entirely on the impression the customers have of the service person (employee) delivered during the course of providing service”. Moreover, Rowley (1999) maintains that a significant relationship exists between customer experience and service quality and argued that customer experience and satisfaction were inextricably linked with service quality. Indeed, some authors have proposed a link between the service attributes (physical facilities, people’s behaviour) and service quality (Dabholkar, 1996; Haywood-Farmer, 1988).

From a value perspective, Dube and Renaghan's (2000) research determined that loyalty in the hotel business is strongly influenced by customers experiencing 'visible value' everyday of their stay rather than meeting customers' expectations on the attributes that motivated their booking. Interestingly, they found that loyalty diminished considerably when customers did not obtain 'visible value' every day of their stay. Their research found that, for all guest types, the top three major drivers of 'visible value,' in order of importance, were: guest-room design, physical property (exterior, public space) and interpersonal service, however, interpersonal service was placed second by leisure and business-meeting guests. This suggests that the physical environments of the service as well as the individuals involved in delivering the service are major experience components. From a tourism context, the identified relationship between experience and customer value is critical considering that extant research has identified customer value as a key driver of success for tourism enterprises (TPRG). Indeed a dominant theme that continuously appears to emerge from supranational and national reports is that the future success of tourism enterprises relies on delivering a unique and 'complete holiday experience.' Yet, except for Dube (2000) little research exists (none in the Irish context) which examines the relationship between customer value, loyalty, and customer experiences, indicating a considerable gap exists in academic knowledge.

Moreover, Dahlsten (2003) has noted that academics agree that "customer satisfaction is a function of the relationship between customer expectations and experience, that it is dependent upon value and that it is formed continuously" (74). Indeed, Rowley (1999:303) who based her study on measuring the total customer experience in a museum maintained that customer satisfaction is determined by the total customer experience "from the moment that a customer seeks to park their car, make a connection through the telephone network, to the moment the customer leaves the museum with the appropriate information, or leisure experience". This indicates a strong connection with the customer experience and the level of customer satisfaction obtained. Based on the foregoing discussion, it is our contention that experience is an essential component for building loyalty and may even have a direct effect on loyalty. Nevertheless, it does not on its own fully explain the loyalty concept, value, satisfaction and quality are also important variables to consider.

## **CONCLUSION**

In summary, although much has been written about the relationships between customer satisfaction, service quality, and loyalty, researchers in this field have not been successful in totally explaining how loyalty is built. In recent times, a few researchers have turned their research lens on the relationship between loyalty, customer value, and customer experiences. What research has been completed on these three variables, specifically by Dube and associates, has indicated that customer experience has a substantial affect on building customer loyalty through creating customer value. Yet a multitude of questions remain unanswered. For instance: (1) what is known about the process and content of ‘experience’ especially in the Irish tourism context? (2) What is customer value? (3) What do customers value about their experiences? (4) Which experiences have the most impact on building customer value? (5) Which don’t? (6) How do these experiences differ between tourist segments and differing tourism contexts? (7) How can customer experiences be managed successfully?

On a theoretical level, this knowledge gap is significant in light of the extant literature which indicates that loyalty-building value is found in the customer’s experience with the product/service; hence a major key to building customer loyalty is the successful management of each customer’s service experience. The limited research shows that there is tremendous opportunity for theory building and empirical testing of new variables such the “customer experience variable” in building customer loyalty.

Finally, from a practice perspective, the lack of research on customer experiences is of particular concern to the tourism industry and policy makers especially in light of the TPRG’s definition of tourism as a total customer experience – a focus that is particularly evident in Fáilte Ireland’s current advertising (reflecting the TPRG report which states that customer experience is “of primary importance in the formulation of Ireland’s tourism policy and in shaping the competitive position for the industry” 2003: 36). As Schmitt (1999: 53) argues: “from now on, leading edge companies, whether they sell to consumers or businesses, will find that the next competitive

battlefield lies in staging experiences”. Unquestionably, consumers now desire experiences and, in order to fully capitalise on this, businesses must deliberately orchestrate engaging memorable experiences. The tourism and hospitality sectors cannot fall behind with regard to adopting such fundamental strategies in both their business operations and marketing activities. In recent times, the marketing of tourism and hospitality offerings, has “become increasingly complex, being associated not only with conveying an image of a place, but with attempting to sell an experience of a place” (Williams, 2006:482). Therefore, those businesses that design innovative experiences that meet and exceed their customer’s expectations will lead to the creation of value and ultimately loyalty.

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