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Recommended Citation

Carter, Michelle; Klein, Richard; Thatcher, Jason B.; and Wright, Ryan, "Switching Costs and Loyalty: Understanding How Trust Moderates Online Consumers' Ties to Merchants" (2009). *SIGHCI 2009 Proceedings*. 2.

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Switching Costs and Loyalty: Understanding How Trust Moderates Online Consumers' Ties to Merchants

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ABSTRACT

Information technology has transformed how travelers interact with travel service providers. Due to fierce competition in the online air travel industry, e-ticketing services have focused attention on fostering customer loyalty. This is an important strategy because, in general, initial transactions with new customers are less profitable than transactions with existing customers. Drawing on research on customer loyalty, switching costs, and trust, this study develops, and proposes an empirical test, for a model incorporating trust as a moderator of the relationship between switching costs and online customer loyalty. We propose that in the presence of high customer trust, e-businesses should have less need to rely on switching costs as a driver of customer loyalty. If supported, this proposition will extend understanding of customer loyalty, switching costs, and trust in e-commerce environments and provide practical, theory-driven, guidelines to e-businesses seeking to develop customer loyalty programs.

Keywords

Customer loyalty, trust, switching costs, e-commerce, e-business strategies.

INTRODUCTION

Information technology has transformed how travelers interact with service providers. E-ticketing services have lead to many travelers abandoning relationships with traditional bricks-and-mortar travel agents in favor of purchasing tickets and associated travel services from e-ticketing providers. Airline carriers (i.e. direct suppliers) and online travel agents (OTAs) are the primary sources of e-tickets. Direct supplier Web sites include features such as online check-in capabilities and frequent flier pricing offers (Jupitermedia, 2004). OTAs make it possible to view travel itineraries and pricing offers from multiple carriers (Mead, 2002).

Due to fierce competition in online markets, e-ticketing services have focused on building customer loyalty. This is an important strategy because loyal customers are more likely to disregard information about offers from other providers and tend to decline invitations to switch providers (Thatcher and George, 2004). Two strategies aimed at fostering customer loyalty are considered particularly important in the online context: 1) the ability of e-ticketing providers to create costs that dissuade customers from switching from the incumbent provider (Lin et al., 2006) (called switching costs); and 2) the ability to build customer trust (Reichheld and Scheffer, 2000). In this work-in-progress, our objective is to investigate the relationship of these important strategies with customer loyalty, within the context of the online air travel industry.

The constructs and relationships described in this paper have implications for theory and practice. From a practice perspective, a better understanding of the antecedents of customer loyalty will help e-ticketing providers develop effective e-business strategies. From a theoretical perspective, the model and empirical approach proposed by this study will further understanding of customer loyalty by explicating the relationship between overall switching costs and trust.

Next, we present our theoretical development and hypotheses. In the section that follows we discuss our proposed empirical methodology.

THEORETICAL DEVELOPMENT

Following Gefen (2002), we refer to customer retention as customer loyalty. Customer loyalty is an important concept in e-commerce because the cost of attracting new customers is high relative to the cost of retaining and doing business with loyal customers (Oliver, 1999). Given the costs involved in customer acquisition and the ease with which online customers can find competing products and services, there is growing interest in

understanding the drivers of customer loyalty in online environments (Jones et al., 2000, Srinivasan et al., 2002).

The assumption that customer satisfaction translated into customer retention served as basis for much early customer loyalty research (Oliver, 1999). Weaknesses in this assumption lead to calls for researchers to include “factors beyond satisfaction in models of customer loyalty and extend existing theories of retention to incorporate contingency relationships” (Jones et al., 2000, pg. 267). One such factor is the concept of switching costs, defined in the marketing literature as the “onetime costs that customers associate with the process of switching from one provider to another” (Burnham et al., 2003). In a study investigating the influence of service satisfaction and switching costs on repurchase intentions, Jones, Mothersbaugh et al (2000) found that the presence of high switching costs attenuated the influence of satisfaction on customer loyalty. Another factor, trust, has been identified as central to understanding individual decision making in e-commerce environments (Gefen et al., 2003b). Recent studies have suggested that beyond initial purchase decisions, trust may also influence online customer retention (Qureshi et al., 2009, Kim et al., 2009). However, the precise relationship between trust and customer loyalty is not yet known, prompting calls for research to consider the “moderating effects of trust” in the context of online purchasing (Kim et al., 2009, p. 253).

To advance research on customer loyalty, switching costs and trust, this study develops and proposes an empirical test for a theoretical model that incorporates trust as a moderator of the relationship between switching costs and customer loyalty. We propose that in the presence of high customer trust, e-businesses should have less need to rely on switching costs as a driver of customer loyalty. If supported, this proposition will extend understanding of customer loyalty in e-commerce environments and provide practical, theory-driven, guidelines to e-businesses seeking to develop customer loyalty programs.

Switching Costs and Customer Loyalty

Switching costs are an important driver of customer loyalty. Customers will not switch providers if the onetime, as distinct from ongoing, costs associated with the process are viewed as prohibitively high. In a study that developed a typology of switching costs, Burnham, Frels et al. (2003) identified three switching costs that collectively dissuade customers from changing providers: procedural, relational, and financial. A fuller description of these constructs and their relationship to loyalty is provided next.

Procedural switching costs are primarily concerned with the time and effort involved in switching providers (Burnham et al., 2003). Burnham, Frels et al. identify four distinct facets of procedural switching costs, which are relevant to the online air travel industry, namely economic risk, evaluation, set-up, and learning costs.

Economic risk costs are costs of accepting financial risk, performance risk, and convenience risk when switching provider, while evaluation costs include costs associated with searching for, and evaluating, information about alternative providers. Set-up costs are those costs associated with initiating a relationship with a new provider (e.g. creating a user profile, configuring software, etc.), and finally, learning costs comprise the costs involved in acquiring the skills necessary to use a new service or product (e.g. learning to create travel itineraries using a different online interface).

Relational switching costs consist of personal- and brand- relationship loss costs (Burnham et al., 2003). Personal relationship loss costs arise when customers experience a loss of comfort as a result of breaking bonds with familiar providers. Brand relationship loss costs occur when customers break bonds with a provider whose brand, or corporate public image, they identify with. For example, in transitioning to the online environment for their travel needs, some customers may have chosen to transact directly with familiar airline carriers. For these customers, the relational costs associated with switching to OTAs with multiple pricing offers (e.g. loss of direct interaction with airline employees and loss of identification with a familiar brand) may outweigh any potential price benefits of making the switch.

Financial switching costs relate to loss of accrued benefits (i.e. benefit loss costs) and/or financial charges or consequences (i.e. monetary loss costs) involved in switching to another provider. Benefit loss costs arise when customers lose accumulated points, benefits, or discounts by switching to an alternative provider. Monetary loss costs are “onetime financial outlays that are incurred in switching providers other than those used to purchase the new product itself” (Burnham et al., 2003, pg. 111). Financial switching costs associated with online air travel include loss of frequent flier miles, access to executive lounges, membership fees, and membership coupon rewards.

In sum, switching costs can be conceptualized as being made up of onetime procedural, relational, and financial costs that the customer associates with the process of changing service providers. These switching costs types are, in turn, multifaceted. Consistent with Burnham, Frels et al’s (2003) typology, we propose that customers who perceive switching costs as prohibitively high should be more likely to stay with an incumbent provider. Formally stated:

H1: Switching costs will positively influence customer loyalty toward the incumbent e-ticketing provider.

Trust and Customer Loyalty

Trust has been defined as “the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to

monitor or control that other party” (Mayer et al., 1995, pg. 712). Trust has particular significance specific to e-commerce transactions, which are characterized by uncertainty and risk due to geographical dispersion and an absence of face-to-face contact among the social parties involved (Kim et al., 2009). Within the information systems (IS) literature, empirical studies have found that trust in specific Internet vendors directly influences Web customers’ attitudes (Gefen et al., 2003b, Kim, 2008), purchase intentions (McKnight et al., 2002), actual purchase behaviors (Lim et al., 2006), and loyalty intentions toward an online vendor (Kim et al., 2009).

Trust can be conceptualized as a second-order concept reflecting an individual’s cognitive beliefs about another party’s benevolence, ability, and integrity (Mayer et al., 1995). From this perspective, a higher level of trust in another party should increase an individual’s willingness to make themselves vulnerable to the actions of that party. Thus, in the online air travel industry, a high level of trust in an e-ticketing provider should increase the likelihood that the individual will purchase airline tickets from that provider.

Benevolence is the extent to which one party (the trustee) is genuinely interested in the other party’s (the trustor’s) welfare, beyond trustee profit motives (Bhattacharjee, 2002, Doney and Cannon, 1997). Benevolent providers (1) demonstrate receptivity and empathy toward customer needs and concerns, and (2) proactively make good-faith efforts to resolve customer concerns (Bhattacharjee, 2002). Customers who perceive their e-ticketing providers as benevolent are less inclined to guard against opportunistic behaviors.

Ability (also referred to as competence) refers to customer perceptions about provider capability to conduct transactions effectively and reliably (Doney and Cannon, 1997). Such perceptions may be based on prior experience or institutional endorsements (Gefen et al., 2003a, McKnight et al., 2002, Kim and Benbasat, 2006, Pavlou, 2002). Prior experience arises from first-hand engagement with the e-ticketing provider, while institutional endorsements are provider-specific, third-party claims about provider capabilities.

Integrity implies volitional will on the part of the provider and refers to customer perceptions that the provider will adhere to an acceptable set of principles or exchange policies during and after the transaction (Mayer et al., 1995, Crosby et al., 1990, Jarvenpaa et al., 2000). In the e-commerce context, exchange policies may include customer service policies and terms of use relating to exchange of private customer information (Bhattacharjee, 2002). E-ticketing providers may encourage customer perceptions of integrity and consequently trust formation by including policy statements on their Web sites, keeping customers informed of changes in policy, and by abiding by self-reported and self-imposed rules of behavior. Self-reported policies help build trust by reducing customer

perceptions of uncertainty and transaction risk within the online environment (Gefen, 2002).

The absence of face-to-face contact in e-commerce transactions is considered an impediment to initial trust formation in online settings (Ba and Pavlou, 2002, Lim et al., 2006). Given these difficulties, we suggest that once formed, trust reflecting cognitive beliefs about the benevolence, ability, and integrity of a specific e-ticketing provider will cause the customer to develop a favorable attitude toward the provider that will result in repeat purchasing behavior. Moreover, customers who have formed trust in a specific online provider should be less likely to switch providers because of difficulties associated with establishing new trusting relationships in a context characterized by uncertainty and risk. Formally stated:

H2: Trust, reflecting cognitive beliefs about the benevolence, ability, and integrity of the incumbent e-ticketing provider, will positively influence customer loyalty toward that provider.

Trust as a Moderator

In addition to its direct influence on customer loyalty, we posit trust moderates the relationship between switching costs and customer loyalty. Research has shown that attitudes and behaviors are positively affected when trust is high (Pennington et al., 2003). Thus, a customer who trusts his e-ticketing provider is likely to have developed a favorable attitude toward the relationship that makes it appear more attractive than reasonable alternatives (Whitten and Leidner, 2006) and leads to greater commitment to the relationship (Morgan and Hunt, 1994). This commitment should strengthen individual resolve to persist in a relationship with an incumbent provider and mean less reliance on switching costs as a driver of customer loyalty. Therefore, we expect that for the same level of switching costs, individuals who trust their e-ticketing provider will demonstrate a greater degree of customer loyalty than individuals who do not trust the provider. Formally stated:

H3: The relationship between switching costs and customer loyalty will be stronger (weaker) when trust is high (low).

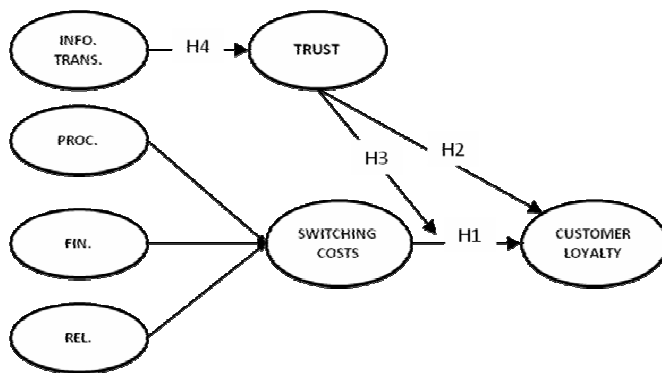
Information Transparency and Trust

Web customers form trusting judgments about e-ticketing providers based on available information. Information may be obtained through first-hand engagement with the e-ticketing provider, third-party recommendations, or self-reported policy statements. Given the lack of interpersonal interactions in online transactions, incomplete or obscure information makes it difficult to form cognitive judgments about a provider and therefore acts as an impediment to formation of trusting beliefs. Consequently, *information transparency*, defined as “the degree of visibility and accessibility of information” (Zhu,

2002, pg. 93), should influence customer cognitive judgments in three key ways that promote trust formation (Nicolaou and McKnight, 2006). First, the provision of reliable and accurate information positively influences beliefs relating to provider ability to complete transactions. Second, when the provider is responsive and offers timely information, the customer develops beliefs about the company benevolence. Third and finally, truthful and credible information influences trusting beliefs about provider integrity. Formally stated:

H4: Information transparency will positively influence trust in the incumbent e-ticketing provider.

Our theoretical model is presented in Figure 1.



INFO. TRANS.=information transparency; PROC.=procedural switching costs; FIN.=financial switching costs; REL.=relational switching costs.

Figure 1. Theoretical Model

METHOD

Survey data, collected from a representative sample of online repeat purchasers of airline tickets, will be used to test the proposed relationships. The survey will capture customer perceptions with respect to six e-ticketing providers, including four online travel agents—Expedia.com; Orbitz.com; Priceline.com, and Hotwire.com—and two airline carriers—Delta Airlines and American Airlines. Capturing customer perceptions of multiple e-ticketing providers will help explain why individuals develop loyalty intentions toward a specific provider and not toward others.

Measures. Measures of core constructs are adapted from prior research. Each measurement item is measured using a 7-point Likert-type scale (e.g. 1=strongly disagree, 7=strongly agree). *Customer Loyalty* is adapted from Gefen and Straub (2002). Consistent with the conceptualization of switching costs as a multi-dimensional concept (Burnham et al., 2003), this study operationalizes procedural, relational, and financial costs as indicators of *switching costs* as a third-order, multi-dimensional, construct. Switching costs measures are adapted from Burnham, Frels et al (2003). Similarly, *trust* is operationalized as a second-order construct reflected in

the three first-order dimensions of benevolence, ability, and integrity. Trust measures are adapted from Bhattacharjee (2002). *Perceived risk* is adapted from Gefen (2002). *Information Transparency* is adapted from Devaraj, Fan et al. (2002). In addition to the core constructs, we will collect data on transaction frequency, prior Internet experience, relative price comparison, and level of exclusiveness to control for their effects on customer loyalty intentions.

Analytical Procedure. This study employs Partial Least Squares (PLS) path modeling, which allows for modeling higher-order constructs in a hierarchical construct model. Partial least squares (PLS), is used because it is considered a less restrictive approach than covariance-based structural equation modeling (SEM) for assessing complex hierarchical models, including models with moderation effects (Wetzels et al., 2009).

CONCLUSION

Fostering customer loyalty is important for e-ticketing providers operating in a highly competitive environment. To this end, the current research-in-progress makes three primary contributions to theory and practice. First, from a theoretical perspective, although well developed in the economics literature, few empirical analyses have examined the influence of overall switching costs as drivers of customer retention (Burnham et al., 2003; Elzinga and Mills, 1998). By explicitly modeling switching costs as a higher-order, multi-dimensional, construct this study augments existing switching costs research. Second, while many studies have investigated the relationship between trust and initial purchasing decisions in the e-commerce context, relatively little is known about the relationship between trust and customer loyalty (Qureshi et al., 2009). In proposing a theoretical model that incorporates a direct relationship between trust in an incumbent provider and customer loyalty, as well as moderating effects of trust on the relationship between switching costs and customer loyalty, we aim to further understanding of the influence of trust on retention of online customers. Third, from a practice perspective, we anticipate that if empirical analysis of the model described in this paper supports our propositions, findings from this research will help e-ticketing providers develop better e-business strategies.

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