Business and Entrepreneurial Review, October 2005, page 35-40
ISSN 0853-9189
Vol. 5, No. 1

Switching Cost to Customer Loyalty: Operation and Business Relationship

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Accepted on March 30th 2005, Approved on August 7th 2005

Abstract: Many business customers today consolidate their supply basis and implementing preferred supplier programs. Consequently suppliers forced to gain a key supplier status from their customers whereas a collaborative buyer-seller relationship represents a source of competitive advance. The vendors sometimes inflict switching costs on their customers, to prevent them from defecting to new suppliers. In a competitive setting where competition dominated by a price war, the potential switching costs might be an exit barrier and a binding factor of customer loyalty. In efforts to address that issue this research examines the moderating effects of switching costs on customer loyalty through both satisfaction and perceived-value measures. The research investigates opportunities for differentiation through value creation in business to business (B2B) relationship.

Keywords: Switching cost, customer loyalty, business to business relationship

INTRODUCTION

In modern marketing concept with more focus on management of customer relationship, it is required a creation and delivery of *superior customer values* (Kotler dan Keller, 2006). *Customer* becomes a main focus to be maintained and developed as the most important partner in achieving long term goal of the company and the stakeholder.

Many aspects can change customer satisfaction from time to time. The key is company should become a customer oriented– refer to the customer needs and all of their activities (SWA magazine, 2006). Not only quality and services that need attention, but also design, speed and customization to win customers heart (Marketing magazine, 2007). The market leader has to search and find new attributes as a unique factor to make them become more superior to competitor.

Customer loyalty is very dynamic because there are many factors tempting customers to shift to other brands – begin with customer satisfaction, price, product availability, existence of more interesting competitor, to other various offers from competitors (SWA magazine, 2005).

Apparently to satisfy the customer wasn't enough. In a hypercompetitive era as today, a successful marketer need to establish and maintain customer loyalty. Firms with no competitive advantage will be easily knocked out by competitors. Marketplace provides various choice of products and services, which enable buyers to assume the role as a decision maker to choose product or service that fit their desires and needs. Value offered by a product may be in a 'context' or content' format. Content is related to what is delivered and context related to how it was delivered (McDougall & Levesque, 2000). Product and service with low quality and without a competitive advantage will hardly survive in this tight competition. Only those who are able to establish customer loyalty and to develop competitive advance in long term, will be succeeded and win the market share (Jarvis and Moyo in Luarn and Lin, 2003) and (Kotler and Singh, Luarn and Lin, 2003).

Creating superior customer values is a key to company success and long term existence (Slater and Woodruff in Ulaga & Eggert, 2006). In business market, *customer value* is considered as a *'Cornerstone'* of the marketing management process (Anderson and Narus in Ulaga & Eggert, 2006). Experiences proved that *retaining customer* is more effective than efforts to get new customers.

Customer switching costs play important role in the organization's ability to maintain customers and achieving competitive advantage (Hess & Ricart, 2002). The main idea of Strategic Management is focus on how the organization can create and lengthen their competitive advantage. A review of strategy, economic and marketing indicates that one of important strategic elements was an effort known as *customer switching cost* (Porter, Klemperer, Kotler, Shapiro and Hax in Hess & Ricart, 2002). *Customer switching costs* are costs created to hinder customer from switching to other service or product. The costs include customer's time, efforts and knowledge implanted on the products, services or relations. Recent study has showed that *switching cost* is not only considered important in achieving competitive advantage, but also has become a strategy in more advanced network environment. (Arthur, Economides, Yoffie, Bakos, Butler Evans, Shapiro, Hax in Hess & Ricart, 2002).

In 'B2B' or business to business (supplier – buyer) relation context, the involving of mutual partnership has a key role in preserving both side's business in the future. Partnership is a source of competitive advantage (Ulaga & Eggert, 2006) and strategic assets (Jackson, Webster, in Ulaga & Eggert, 2006). Becoming a "preferred supplier" for customers could also increase market share and business profitability. This strategy needs to be established strongly by suppliers to gain business sustainability in long term. A strong relationship will be considered as an effort to minimize customers' desire to switch to other supplier.

METHODS

This research is focus on business to business relation in market segmentation of food service bakery and confectionary industry. In this research, we analysed whether the customer-perceived value created by supplier will satisfy its customer, and whether customer satisfaction produced could promote a creation of a loyal customer. In addition, we reviewed the role of switching cost related to accepted rate of satisfaction and the value given to customer in obtaining their loyalty. Thus, this research investigated the effect of switching cost to customer loyalty through customer satisfaction and customer perceived value.

E-commerce and B2B are two different segment and have the possibility to produce something different. By focusing to business to business relation, the questions raised in this research are as follows: (1) Do core offering values which comprise of product quality and delivery performance affect customer satisfaction and customer loyalty? (2) Do sourcing process values which comprise of Service Support and Personal Interaction affect customer satisfaction and customer loyalty? (3) Do Customer Operation Values which comprise of Supplier know-how and Time to market affect customer satisfaction and customer loyalty? (4) Do Costumer Satisfaction could mediate the effect of costumer perceived value to customer loyalty? (5) Do Switching costs affect Customer loyalty through core offering, sourcing process, customer operation and customer satisfaction? (6) Do switching costs affect price loyalty through core offering, sourcing process, customer operation and customer satisfaction?

Variables and measurement. This research adopt previous research by Yang and Peterson that proved the character of switching costs were related to customer perceived value – satisfaction and loyalty. Customer perceived value in theory comprises of three variables, that is core offering, sourcing process, and customer operation. Customer loyalty comprises of three sub variables; future purchase intentions, price loyalty and recommendation giving.

In this research, there are six variables that will be analysed: Core offering, Sourcing process, Customer Operation, Customer Satisfaction, Customer Loyalty and Switching Cost.

Customer perceived value act as independent variable, and customer loyalty as dependent variable. Customer satisfaction act as independent variable to customer loyalty and as dependent variable to customer perceived value. Switching cost act as moderating variable that give some strengh or weakness factor to influence relation between customer perceived value variable to customer loyalty and customer satisfaction to customer loyalty.

Sample and data collection. In this research, selection of sample is conducted in accordance with certain characteristic considered having connection with population which has been noticed before (hair, et al. 2006). The sample chosen as respondent are costumers that still having business to business relationship with supplier of bakery-ingredients (PT. ZI) and representing every market segment of PT. ZI. Most of them live in Jabodetabek area.

Data was collected through questionnaires comprise of written questions distributed to be answered by respondent who are representing institutions or firms that having business relation with the supplier (PT. ZI). The questionnaire used close type of questions with all answers provided. Before the questionnaire is distributed or used as instrument, a test to measure validity and reliability of the instrument had conducted.

Calculation of targeted sample size using margin of error 5% with confidence level of 95%. Minimum sample size is determine refer to Walpole, Myers and Myers (1998), which is planned to be n = $\frac{Z\alpha_{\frac{2}{2}}}{4e^2}$. Where $Z\alpha_2$ is a value on table figure, with confidence level of a, and e is error rate. In this research, the planned minimum respondent sample size, which is the level of confidence is 95 percent or the value of table figure of z distribution for the level confidence is a or Za21,96 (from table z) and error rate (e) is= 0.10.

So $n = \frac{Z\alpha_2^2}{4e^2} = \frac{(1{,}96)_2}{4(0{,}10)_2} = 96.04$ respondent. So the amount of minimum respondent is 96.

Further, 190 questionnaires were distributed to ZI customers through sales visit, demo event, gathering and direct delivery to customers in Jakarta. Out of 190 questionnaires, 120 (63%) were returned, but only 115 (61%) could be analysed further, the rest were excluded from data processing and analysis due to incompleteness.

Research Design. This research is referring to previous research conducted by Yang and Peterson (2004) on *e-commerce* respondent. Using the same framework, this research in conducted on B2B relation, the relationship between *supplier* and *buyer/ customer*. Some variables and instrument used are referred to some researches based on business to business relationship. (Ulaga & Eggert, Babakus, et.al. 2004, Foster & Cadogan, 2000).

This research is a quantitative study based on survey to test the hypotheses about the influence of *switching cost* in business to business relationship to *customer loyalty* through *customer satisfaction* and *customer perceived value.*

The test using multiple regression statistic method to test *dependent / criterion variable* which is metric measurement scaled (*interval/ratio),* which estimated could be predicted by independent variable with metric measurement scaled. *(interval/ratio)* (Hermawan, 2006).

Sample and data collection. Sampling method used in this research is *Non-probability sampling* based on consideration with certain criteria or *purposive sampling.*

Variable and measurement. This research adopted Yang and Peterson (2004)'s research testing *switching costs* role on the relationship of *customer perceived value-satisfaction* and *loyalty.* The research is conducted on the business to business relationship measured by variable using the work of Ulaga and Eggert (2006), Babakus et al (2004), and Foster & Cadogan (2000). *Customer perceived value* as a construct comprise of three variables, which are *core offering, sourcing process,* and *customer operation.*

Customer Loyalty comprises of three sub-variables, which are *future purchase intentions, price loyalty,* and *recommendation giving.*

RESULTS AND DISCUSSION

This chapter discusses descriptive statistic with result of data processing giving by the checked variables, and then conduct a test against research hypothesis.

Table 1 showed the descriptive statistic processing result according to analyzed questionnaire.

Table 1. Descriptive Statistic

N = 115		Value			
Variable	Sub-variable (dimension)	**Min**	**Max**	**Mean**	**SD**
Core offering	Product quality	1.0	7.0	6.4630	0.72064
	Delivery performance	1.0	7.0	6.2174	1.00464
Sourcing Process	Service support	4.0	7.0	6.2783	0.77625
	Personal interaction	4.0	7.0	6.3130	0.81446
Customer Operation	Supplier know-how	1.0	7.0	6.3333	0.90004
	Time to market	2.0	7.0	6.2638	0.83700
Customer statisfaction		4.0	7.0	6.4145	0.55439
	Purchase intention	2.0	7.0	6.1217	0.98961
Customer Loyalty	Price Loyalty	2.0	7.0	5.8565	1.04121
	Recommendation	1.0	7.0	6.2377	0.80426
Switching costs		1.0	7.0	5.7710	1.03012

The above table showed the value of mean and standard deviation for each measured variables. Mean value is the average of respondent valuation to the questions asked, and standard deviation is the value of deviation against average value.

Standard deviation, showed that distribution of respondent's answer disparity against average answer, is ranged from 0.55 to 1.03. It shows that the relative disparity is quite wide or respondent's answer is relatively varied.

From the above result, each measured variables showed mean value more than 5, meaning that respondent give valuation above normal answer or nearly very agreed; although with a relatively heterogeneous answer. The highest scale given by respondent was 7 and the lowest was 1. Respondent valuation is using 7 point Likert Scale where 1 meant very disagree and 7 meant very agree to the statement of each indicator being measured. The highest mean value of measured parameter just as shown in table 4, is achieved by Product quality (mean = 6.46), and the lowest mean value is achieved by switching cost (mean = 5.77)

The smallest deviation rate in on *customer satisfaction* variable (= 0.554), and the highest is on *switching costs* (= 1.030). It showed that respondent's answers about *customer satisfaction* are quite similar, whereas the answer on *switching costs* are vary on wide range of answer.

Table 2. Regression Testing Result of the effect of Core offering, Sourcing process and Customer operation to Customer Satisfaction

Variable N = 115	β	t	Sig	Model R2	F	Sig
Dependent Variable : Customer Satisfaction						
Independent variable						
• Core Offering	0.486	5.909	0.000	0.236	34.913	0.000
• Sourcing Process	0.487	5.932	0.000	0.237	35.189	0.000
• Customer Operation	0.470	5.662	0.000	0.221	32.061	0.000
Customer Perceived Values	0.548	6.966	0.000	0.300	48.518	0.000

Table 2 showed that core offering, sourcing process, and customer operation variables are significant as predictors to customer satisfaction. The significant value of 0.000 which is below p of 0.01 ($p < 0.01$) or error tolerance is below 1%. As such, this research is managed to accept Ha where there are effects of core offering, sourcing process and customer operation to customer satisfaction. So the hypotheses H1A, H1B, and H1C are proven.

From the result, it seems that core offering and sourcing process have nearly equal effect to customer satisfaction. Value of core offering and sourcing process relatively stronger compared to customer operation.

CONCLUSION

Customer loyalty can be achieved through customer satisfaction improvement and high value product or service offering. From the research result based on business to business (B2B) relationship, it shows that *Customer perceived value* and *Satisfaction* became a quite powerful predictor to create *customer loyalty*. *Key values drivers* to create customer satisfaction and loyalty can be achieved through superior values delivery in *product quality, delivery performance, service support, personal interaction, know-how* and *time to market.* Customer will be loyal if supplier create and deliver superior values according to their satisfaction and needs. The superior values are able to create *switching costs* in hindering customer from switching to competitor.

Value sourcing process comprised of *service support* and *personal interactions are* also having quite strong contribution to *customer satisfaction* and *customer loyalty*. The most important part of *service support* is mainly determined by "baker" technical services, information needed by customers, and immediate response from supplier. *Personal interaction* is formed by a strong business to business relationship between *supplier - customer,* response to complaint and opportunity for discussion.

Value Customer operations is not less important in creating influence to a strong customer satisfaction and loyalty. The *Value* is determined by the thing related to *supplier know-how* and *time to market.* The thing related to *supplier know-how* is educational services, product improvement services, and a knowledge that inspire new product development. Action in term of *time to market* is related to product innovation development and how fast to market.

Customer loyalty in this research is showed by *purchase intention, price loyalty,* and *recommendation giving.* Customers show their loyalty by keep using supplier's products in quite a long time and not switching to other supplier who offer a lower price. *Price loyalty* indicates customer's loyalty by keep buying supplier's product although there are possibilities that the product more expensive in term of price.

The result strengthened the evidence that *customer loyalty* can be achieved through *customer satisfaction improvement* and superior product or service value offering (Yang & Peterson, 2004). In this term, *superior customer perceived values* in business to business relationship are *product quality,* *delivery performance, service support, personal interaction, time to market* for product and business development, and *know-how* that must be well managed by supplier.

Modernization effect of *switching costs* on *customer loyalty* through *customer satisfaction* and *perceived value* depend on customer satisfaction rate and their *perceived value.* In this term, *switching costs* contributes a mediate role when an organization reaches *customer satisfaction* and *perceived value* performance above average.

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