

Mediating effect of Program Loyalty on the relationships between Value Perception and Relationship Investment on Customer Loyalty

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Abstract

This research examined the mediating effect of program loyalty on the relationships between value perception and relationship investment on customer loyalty in the context of a services retailer. We found that program loyalty mediates the relationship between the predictor variables and customer loyalty, suggesting that implementing loyalty programs is useful for encouraging customer loyalty. Our results also empirically support the positive relationship between the value perception of a loyalty program and customer loyalty.

Introduction

Customer loyalty has a powerful influence on companies' performance (Lam, Shankar, Erramilli and Murthy, 2004). The significant benefits of customer loyalty have led many firms to implement relationship marketing instruments such as loyalty programs (reward schemes), in an attempt to build closer relationships with customers, stimulate product and service usage, and retain customers (Verhoef, 2003; Kivetz and Simonson, 2003). Much of the existing literature on relationship marketing investigates loyalty programs' effectiveness purely from the firm's perspective (Bolton et al., 2000; Lewis, 2004). To justify allocation of resources to a loyalty program rather than alternate marketing devices, our research investigates the 'understanding of customers' evaluations of loyalty programs and the various moderators and determinants of the success or failure of such efforts' (Kivetz & Simonson, 2002). For a loyalty program to be successful, it must be both profitable and effective at inducing customer loyalty within program participants.

In the existing research relating to the antecedents of customer loyalty, there has been little attention given to perceived customer value and perceived relationship investment. Ramaseshan and Johnston (2007) investigated the effects of perceived customer value and perceived relationship investment in the context of a product retailer. These days many firms, in particular service firms implement customer loyalty building strategies that fail to provide customers with any real value, or fail to entice them to reciprocate investments made by the firm. For a long-term relationship to be successful, both the firm and the customer must benefit. Therefore, this research was aimed to examine the effects of program loyalty, value perception and relationship investment on customer loyalty in the context of service retailer.

Literature

To date there have been limited attempts to investigate the antecedents of customer loyalty (Lam et al., 2004). Those who have attempted to delve further into the construct have suggested potential antecedents may include customer satisfaction, switching costs, trust, perceived customer value, and perceived relationship investment. Several authors agree that perceived value plays a key strategic role in determining customer loyalty (Dowling and Uncles, 1997; Patterson and Spreng, 1997; Yi and Jeon, 2003; Harris and Goode, 2004).

Value perception is considered a central tenet in relationship marketing, because consumers who perceive they are receiving value and feel valued, tend to spend more money with the firm on a year-to-year basis, and stay with the firm for a longer duration. Yi and Jeon (2003) investigated how reward schemes of a loyalty program influence perceived value of the program, and how value perception of the loyalty program affects customer loyalty. Harris and Goode (2004) found overwhelming support for the positive influence of perceived value on customer loyalty, as moderated by trust.

Treating customer loyalty as a two-dimensional construct (patronage and recommendation), Lam et. al. (2004) investigated the effect of customer value on customer loyalty, as mediated by customer satisfaction. The authors found that it was customer satisfaction that mediates the relationship on the recommend dimension, and partially on the patronage dimension and suggest that customers consider their affect state (satisfaction) when recommending the service to another. When considering patronage however, the consumer is influenced by both their affect (satisfaction) and cognitive state (customer value). The above studies suggest that perceived customer value has a positive effect on customer loyalty. However, they fail to define customer loyalty consistently. Yi and Jeon (2003) use the term brand loyalty and customer loyalty interchangeably, and measure it in terms of customer share. Harris and Goode (2004) as well as Evanschitzky and Wunderlich (2006) apply Oliver's (1997, 1999) framework, evaluating loyalty in terms of the four components (cognitive, affective, conative and action loyalty).

Perceived relationship investment is defined as 'a consumers' perception of the extent to which a retailer devotes resources, efforts, and attention aimed at maintaining or enhancing relationships with regular customers that do not have outside value and cannot be recovered if these relationships are terminated' (Smith, 1998). Perceived relationship investment is based on the notion of reciprocity, which implies that when organisations invest certain resources in their customers, the customers tend to feel the need to contribute equitably in return in some way (Smith and Barclay, 1997). Perceived relationship investment therefore differs from customer perceived value in that it implies that a consumer reciprocates a retailer's actions.

Morais, Dorsch and Backman (2004) found that 'customers' perceptions of investments made by the provider result in equitable investments made by the customer, and that those customer investments in the provider lead to increased loyalty. They found that investments of love, status, and information are more strongly related to customer loyalty than investments of money (i.e. discounts, free gifts). In addition, they also suggest that these investments (i.e. love, information, money) may result in different types of loyalty (i.e. behavioural or affective).

In examining the potential antecedents of customer loyalty in the context of loyalty programs, it is imperative to investigate potential variables which may mediate this relationship. One such mediator may include program loyalty (Yi and Jeon, 2003). In considering whether loyalty programs do in fact generate customer loyalty, program loyalty provides an indication of whether the consumer is truly a loyal customer or whether they are more deal-prone (Rothschild and Gaidis, 1981). With the plethora of loyalty programs in existence today and consumers holding multiple memberships, investigation into this construct will provide some insight into the psychological attachment of program participants. Are they a loyalty program participant because they truly want a long-term relationship with the provider – or are they simply acting opportunistically?

Yi and Jeon (2003) investigated the role of program loyalty as a mediator of the value perception of a loyalty program – loyalty relationship, as moderated by involvement. The authors discovered that value perception of a loyalty program predicts loyalty both directly and indirectly via program loyalty under conditions of high involvement. Under low involvement however, loyalty was only achieved indirectly via program loyalty. Therefore, their results indicate that customers may desire long-term relationships with unlikely products such as detergent or soap – so long as the loyalty program provides them with some value.

Theoretical Framework and Hypotheses

For a loyalty program to be successful, it should be perceived as valuable to the customer (O'Brien and Jones, 2000; Yi and Jeon, 2003). There is agreement that perceived value plays a key strategic role in determining customer loyalty (O'Brien and Jones, 2000; Yi and Jeon, 2003; Harris and Goode, 2004), and/or attractiveness of the loyalty program (Kivetz and Simonson, 2003). Harris and Goode (2004) and Lam, Shankar, Erranilli and Murthy (2004) provided empirical support for the positive effect of value perception on loyalty. Thus, it is hypothesised that: *H₁: Perceived value of a loyalty program has a positive effect on customer loyalty.*

Based upon the notion of reciprocity, perceived relationship investment implies that when organisations invest certain resources in their customers, the customers tend to feel the need to contribute equitably in return in some form (Smith and Barclay, 1997). Morais, Dorsch and Backman (2004) found that 'customers' perceptions of investments made by the provider result in equitable investments made by the customer, and that those customer investments in the provider lead to increased loyalty'. Thus, it is hypothesised that: *H₂: Customers' perceptions of investments made by the provider positively influence customer loyalty.*

The mediating variable of interest in our research is program loyalty. Our research argues that customer loyalty can be influenced by the presence of program loyalty. This suggests that consumer's may become loyal to the retailer/brand because initially they were drawn in by the program. Empirical support for program loyalty acting as a mediator between independent variable's predicting customer loyalties is evident in the work of Yi and Jeon (2003). Thus, it is hypothesised that: *H_{3a}: Program Loyalty mediates the relationship between value perception of the loyalty program and customer loyalty; and H_{3b}: Program Loyalty mediates the relationship between perceived relationship investment and customer loyalty.*

Method

The sampling frame of this study includes 842 participants of loyalty program of a service retailer - café franchise. The café retailer's loyalty program was launched during 2000 and currently has an active membership of approximately 1,432. They currently operate four franchises. To become a member, customers must purchase five coffees within one month. Members receive a free coffee voucher (valued at \$3.20) for every \$20 spent and points do not expire. Upon joining the club, members receive a swipe card key ring. Members are entitled access to an exclusive section on their website devoted to company news, coffee and food tips, exclusive competitions and community discussions. Members also receive a quarterly newsletter full of coffee news, new café openings, competitions and prize draws, up-to-date information about what is happening at the café's and the latest reward offerings. A

self-administered mail survey was used for data collection. The scales to measure the variables included in the study were adapted from prior literature.

Results

The Cronbach Alpha value for the variables “customer loyalty”, “value perception”, “perceived relationship investment”, and “program loyalty are .913, .773, .894, and .845, respectively. Results of multiple regression indicate that 33.5% of the variance (R-square) in customer loyalty has been significantly explained by the two variables value perception and perceived relationship investment and statistically significant. Of the predictor variables, perceived relationship investment has the highest standardized beta (0.331), significant at the .01 level, indicating that it has the most influence in predicting customer loyalty. The other variable, value perception, is also significant at .01 (Beta = .295). Furthermore, as hypothesized, perceived value of the loyalty program and perceived relationship investment have a positive effect upon customer loyalty – supporting H1 and H2. The results are presented in Table 1.

Table 1: Results of Regression Analysis

	Unstandardized Beta	Std. Error	Standardized Beta	t-value	Sig.
Constant	2.764	0.412		6.703	0.000
Perceived Relationship Investment	0.250	0.087	0.331	2.855	0.005
Value Perception	0.263	0.103	0.295	2.545	0.012

H3a and H3b were tested using standard multiple regression and the three step approach recommended by Peccei and Rosenthal (2001). Results from the first equation concerning the mediator and the predictors indicate that the value perception and perceived relationship investment explained 84.6% of the variance (R-square) in program loyalty, significant at .0001. Examination of the Beta values demonstrates that value perception had the highest standardized Beta (0.787), significant at .0001, making it the strongest predictor of program loyalty. Perceived relationship investment had a standardized beta of 0.181, also significant at .0001. The next equation indicates that the predictor variables explain 33.5% (R-square) of the variance in customer loyalty, significant at the .0001 level. Value perception was the strongest predictor with a standardized Beta value of 0.263, significant at .01. Perceived relationship investment had a standardized Beta of 0.250, significant at .01. The last equation indicates that the mediating variable and the predictor variable explain 39.9% of the variance in customer loyalty, significant at .0001. This last equation explains 6.4% more than the equation without the mediating variable. Furthermore, program loyalty – the mediating variable – has the highest Beta (0.556) and is the only significant variable, significant at .001.

These results support program loyalty mediating the relationships between the predictor variables and customer loyalty (H3a, H3b). However, the individual coefficients were not all in the predicted direction, with value perception displaying a negative relationship with the dependent variable in the third equation. Therefore, there is partial empirical support for the full mediation model.

Discussion and Managerial Implications

The results suggest that the two independent variables - value perception and perceived relationship investment explained 33.5% of the variance in customer loyalty. Both variables were significant with value perception being the strongest. The results supported program loyalty mediating the relationships between the predictor variables and customer loyalty. However, the individual coefficients were not all in the predicted direction, with value perception displaying a negative relationship with the dependent variable in the third equation. Therefore, there is partial empirical support for the full mediation model. Overall, this analysis provides empirical support for the mediating effect of program loyalty upon the predictor-dependent relationships. These results suggest that the full mediation model is preferable to the partial mediation model – whereby the predictor variables directly influence customer loyalty as well. These findings provide critical insights into loyalty program literature as they suggest that loyalty to the program is crucial for customer loyalty and that loyalty programs may be suitable for increasing a customer's loyalty to the firm.

The study provides several ideas for managers. Firstly, the findings suggest that managers should invest in relationship prone consumers, as they more likely to reciprocate the relationship. In accordance with De Wulf, Odekerken-Schroder and Iacobucci's (2001) recommendations, a few simple questions on the registration form for a stores loyalty card can measure the consumer's intrinsic disposition to engage in relationships and therefore provide some guidelines to their value as a loyalty program participant. Secondly, this research demonstrated that program loyalty is a pivotal force in influencing customer loyalty. This research advocates the full mediation model, rather than a partial one, suggesting that managers may aim for program loyalty as a suitable target for program success. Therefore, making program loyalty a suitable target for some firms – especially those with typically low involved product's, is a reasonable strategy. Thirdly, the final significant finding of this research was the positive effect of value perception of the loyalty program on customer loyalty suggesting that managers should focus on making the loyalty program appear as valuable to the consumer to improve loyalty levels.

The limitations of this study include: (i) conducted among the customers of one service organization as such caution must be exercised while generalising the study findings to other industries and (ii) based on attitudinal data. Future research could focus on replicating the study to other industries, use actual behaviour data as dependent variable, consider longitudinal data to assess cause-and-effect structures and test the model in a situation in which the customer is a member of multiple loyalty programs.

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