Enhancing Total-Value Creation through Loyalty in Customer-Seller Relationships

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***Abstract: - Customers* and sellers enter a business relationship over a period of time. Relationships are assumed to grow, deteriorate, and dissolve as a consequence of many interactions. Loyalty develops in the relationship owing to number of repeated transactions. Today, concept of loyalty is a key factor in business relationship. This paper tries to presents brief idea of loyalty in customer seller relationship. It focuses on what exactly loyalty is in customer seller relationship. It presents an economic perspective of loyalty. This is an attempt to contribute to a better understanding of how loyalty in customer seller relationship emerges, reasons for it and under what conditions, customer and seller move away from loyalty. Present paper firstly proposes an economic perspective of loyalty in customer seller relationship, then dynamics of loyalty is discussed followed by a virtuous cycle of customer value enhancement through loyalty then thresholds of loyalty and at the end it state reasons for moving away from loyalty.**

Keywords: Loyalty, customer-seller relationship, captured value, willingness to pay, total value creation.

I. INTRODUCTION

In the current competitive world, business firms have been seeking for the most effective ways to acquire and retain customers. Importance to creating a loyal customer arises from that it costs more to create a new customer than to retain an existing one. Making a customer loyal towards a company product is not an easy job. The cost of creating a new customer is five times more than that of retaining an existing customer (Reichheld, 1996). A loyal customer is less price sensitive and refers the company's products to other people (Kotler, 1999). To achieve these goals, the loyalty program has been used as a vital tool for building, developing, and retaining relationship with customers (Lacey, 2009). Once revolutionary, loyalty programs designed to differentiate products quickly became commoditized. And yet, billions of dollars are still spent every year on programs that are doomed to fail. These programs, it turns out, don't inspire long-term loyalty. Once a better deal comes along, customers will gladly defect (Pahariya, 2013) . Thus there is a situation of disloyal customers. Hence there arises a question how an organization can enhance customer loyalty. Thus there is a need to find out what exactly loyalty is, what governs it, what are the reasons for moving away from it and how it can be improved in customer seller relationship for seeking mutually beneficial relationships. Thus this paper tries to enhance the idea of loyalty in customer seller relationship. It proposes an economic perspective of loyalty.

II. THEOROTICAL BACKGROUND

A. Loyalty:

(Dick & Basu, 1994)define loyalty as a combination of strong relative attitude and high repeat patronage.(Oliver, 1999)defines consumer loyalty as' a deeply held commitment to rebuy or repatronise a preferred product/service consistently in the future', thereby causing repetitive same brand (store) or same brand set purchasing, despite situational influences and marketing efforts having the potential to cause switching behavior. (Reichheld, 2003)defines loyalty as ―willingness of someone – a customer, an employee, a friend - to make an investment or personal sacrifice in order to strengthen a relationship. Loyalty is a multi dimensional construct and needs to be viewed as an attitude that leads to relationship with the brand/store, outcome in terms of revealed behavior, relational in terms of advocacy, word of mouth communication and buying is moderated by the individual's characteristics, circumstances and /or the purchase situations (Vyas & Sinha, 2008). Two main approaches to loyalty have evolved in the literature: behavioral and attitudinal approaches. While the behavioral approach defines loyal customers as their intent to stay with an organization, or whether they have repurchased its offerings, the attitudinal approach recognizes not only the behavioral dimension, but also the attitudinal dimension of loyalty (Bodet & Bernache- Assollant, 2011; Brunner, St¨ocklin, & Opwis, 2006). Thus loyalty is conceptualized as a customer's expected propensity to stay with a particular seller. Thus there are various definitions of the term loyalty given by various authors and there are different views about the concept of loyalty.

B. Customer-Seller Relationship

Sellers and customers not just exchange services and money but also often create ongoing, and even trusting, relationships of mutual benefit as suggested in the marketing relationship approach (Johnson & Selnes, 2004; Mohr, Fisher,&Nevin 1996; Mohr&Nevin, 1990; Morgan & Hunt, 1994; Palmatier, 2008; Sheth & Parvatiyar, 1995; Vargo & Lusch, 2004; Ward & Dagger, 2007). Marketing researchers seem to agree that (a) relationship marketing focuses on the individual customer–seller relationship; (b) both parties in a relationship must benefit for the relationship to continue; (c) the relationship is often longitudinal in nature; (d) the focus of relationship marketing is to retain customers (Bejou, 1997; Cox & Walker, 1997; Gronroos, 1994; Hunt, Arnett, & Madhavaram, 2006; Peterson, 1995). (Johnson & Selnes, 2004) suggesting that satisfaction and loyalty constitute main competitive advantages that may be gained from developing relationships with customers. By maintaining that "consumers enter into relational exchanges with firms when they believe that the benefits derived from such relational exchanges exceed the costs" (Hunt, Arnett, & Madhavaram, 2006, p. 76), marketing relationship theory basically takes a value-approach to marketing. Gaining value will improve customer satisfaction and stimulate repurchasing (or loyalty).

III. LOYALTY: AN ECONOMIC PERSPECTIVE

A. Value Creation:

A customer is the recipient of a good, service, product, or idea, obtained from a seller, vendor, or supplier for a monetary or other valuable consideration. A seller is an individual or entity that exchanges any type of good or service in return for payment. A seller performs different activities. These activities do not just generate cost. They also make customers willing to pay for the product or service. A seller adds all its cost and a desired profit margin and thus he decides a certain price for the product (Whether a good or a service, hereafter we will call it as product). A seller decides a price below which he will not sell the product.

B. Willingness to Pay:

Similarly if we consider a customer, he wants to buy a product but, the customer has his own idea about the price of a product he wants to buy. The customer decides a certain maximum amount i.e. price beyond which he will not be ready to pay; this is customer's willingness to pay for a product.

C. Value line:

The scenario is, there are two parties and two prices for a particular product one is seller's price below which he will not sell the product and the customer's price beyond which he will not pay for the product. Thus there is price range consisting of seller's minimum price (S_{min}) and customer's maximum (C_{max}) price. The transaction will take place if price of the product lies in this range.

D. Bargaining Power:

A seller tries to push the price towards the customer and wants to capture the maximum value. On the other hand, a customer tries to pull down the price and tries to capture the maximum value. This phenomenon is called as the bargaining power of seller and the customer respectively.

E. *Fairness in captured value:*

Thus there must be fair values for both the parties in the deal. Rather we can say that there must be perceived fair value in the transaction. When both the players agree on a certain price, a transaction takes place. When number of transactions takes place between two players, we can say that they enter in a business relationship where both the players trying to capture the maximum value.

F. Enhancing Total-Value Creation & Emergence of Loyalty:

As the transactions are repeated and a relationship develops over a period of time, there develops flexibility in the desire to capture maximum value from a transaction. For example, from customers' point of view, when a customer is ready to pay more price for a product than his earlier willingness to pay i.e. there comes flexibility in willingness to pay. This flexibility in willingness to pay is nothing but loyalty from economics point of view. Here the customer doesn't try to capture maximum value and is ready to forgo some benefits. Now, from sellers' point of view, when a seller is ready to reduce the price for the product below which he was not ready to sell the product earlier and he is ready to forgo some benefits and accepts the lower price. Hence there is an enhancement in the total value created in the transaction for both the players and thus there develops flexibility in the desired price and that is nothing but the loyalty in relationship.

IV. DYNAMICS OF LOYALTY

A seller wants to capture more value; so he increases price of the product. A customer has his own perceived maximum price (C_{max}) i.e. his maximum willingness to pay for the product. With the new price demanded by the seller, the customer will now think about whether to pay the new price or not. Customer may accept the new price at once. But in long run he will try to find an alternative i.e. a new seller.

Situation 1: Marginal Increase in Price:

If new price (N_p) of the product is marginally above C_{max}, then the customer will try to search a new seller but with low intensity and low urgency. But if the difference between N_p and C_{max} is considerably higher, then the customer will try to find the new seller with more intensity and more urgency. Thus the loyalty of a customer towards the seller is dependent on a certain setting. It is a relative term and may be transformed from loyalty to disloyalty. Suppose a customer is thinking of changing a seller then he will have to consider many aspects. Finding a new seller may not be so difficult but the new seller may or may not be as trustworthy as the older one. There is no certainty of timely and prompt service. More time is to be consumed in order to build a new good relationship. Thus in an effort to minimize the new prize, there is an uncertainty of many factors. There is a switching cost and risk involved in it. Hence the customer may not go for changing a seller and loyalty towards the older seller is not broken and the customer accepts the new increased price by considering the long term perspective.

Situation 2: Considerable Increase in Price:

In another scenario, if the new price proposed by the seller is far higher than the old price, then the customer tries to find a new seller with more intensity and urgency. There are also many uncertainties as mentioned above regarding trustworthiness, promptness of service, quality, etc but as the new prize is much higher than the older prize, and then there are more chances of taking a risk by opting a new seller. Thus if the customer goes for opting for a new seller, relationship with the older one breaks and thus a loyal customer becomes disloyal. Hence we can say that there is no absolute loyalty. Loyalty in a relationship is relative. Loyalty exists with certain predefined setting and is strongly associated with the economic perspective which plays an important role in the existence of loyalty in a relationship between a seller and a customer.

V. CUSTOMER VALUE ENHANCEMENT THROUGH LOYALTY: A VIRTUOUS CYCLE

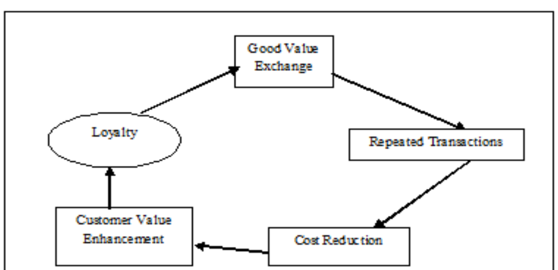

Fig: Customer Value Enhancement through Loyalty: A Virtuous Cycle

If we see the situation from a seller's perspective, a seller will try to increase price of the product. He tries to push more cost towards the customer. Now suppose a customer is loyal to a particular seller. He is willing to continue with the current seller despite an increase in the price. It becomes relatively easy to serve a regular customer. He knows exactly what he wants. He is completely aware of the products and services provided by the seller. He knows from which department to get what. In case any problem arise, he knows what exactly to be done and to contact whom with the seller, where and how to register a compliant , what is the exact procedure to do it, what is the time period required to for the processing of complaint, etc. Hence transaction cost of the seller gets minimized at each encounter with a loyal customer. Thus cost associated with a customer becomes less. Now, with a minimized cost, a seller can offer a discount to the customer. Price paid by the customer becomes less. Customer gets more benefit. Intensity of a customer to be loyal towards a particular seller increases and vice-versa.

Hence there is a shift in the value captured by the seller. The value line becomes flexible. Thus loyalty emerges and a win- win, mutually beneficial situation prevails over a longer time. Loyalty is nothing but the acceptance of more cost to be beard and flexibility in the value to be captured. It is a virtuous cycle starting with selling a product to a customer with a good value, customer gets a good value, customer continues with the seller, there is reduction in cost of seller, seller offers more value, customer continues with the seller, a strong relationship develops, more flexibility in the value captured, more repeated transactions and the cycle continues.

VI. THRESHOLDS OF LOYALTY

As discussed above, a sustainable relationship over a period of time is necessary for loyalty. When this sustainability gets disturbed, loyalty ceases. When a seller increases the price for the product, a customer has his certain willingness to pay, C_{max} and beyond this he will not pay and will not accept the deal, the price beyond which a customer is not ready to pay is said to be the threshold of loyalty for the customer. When a buyer pushes more cost towards the seller and bargains for more discounts and the price to be reduced, but the seller will not accept the deal below a certain minimum price S_{min} , this price is the threshold price for the seller. Thus, when one of the two players try to capture more value or there is a perception of one player that another player is trying to capture more value then loyalty comes to an end and a new relationship starts with some other player.

VII. REASONS FOR MOVING AWAY FROM LOYALTY

A Customer's Point of View:

We have seen how loyalty emerges and prevails in the customer seller relationship, what a virtuous cycle of loyalty is and how it works. Now, what are the reasons for moving away from loyalty? When a seller wants to increase price of a product, and tries to capture more value from the transaction, the customer may pay for it at once but if the price increase continues over further transactions, customer may go for finding new seller. And if he gets a new seller with desired price and value then the loyalty towards older seller breaks.

A Seller's Point of View:

When a customer tries to capture more value from the transaction by applying more bargaining power, the transaction may happen at once but over a period of time, the seller may not be willing to transact with the customer with the bargained price and tries to find other customers with desired value to be captured and tries to concentrate on them. Thus loyalty in the relationship breaks. A new value line with a new customer is formed and relationship develops leading to loyalty. Thus sustainability is required over a period of time for loyalty to exist in a relationship. When a player tries to provide a value in the relationship, loyalty exists and when a player tries to capture more value or there is a perception of it, loyalty ceases in the relationship.

VIII. CONCLUSION

As loyalty is a complex concept. This paper provides an economic perspective of loyalty in customer- seller relationship. It gives a distinguished angle of loyalty in a business relationship. Importance of good and mutually acceptable value exchange has been underlined if a seller wants to build a long term relationship with a customer. It is a virtuous cycle of loyalty which starts from a good value exchange leading to repeated transactions which results in cost reduction for the seller leading to availability of more value to be shared and this leads to loyalty and the cycle continues. Thus a virtuous cycle of loyalty has been explained which recommends a seller and a customer to be in sustainable and mutually beneficial relationship for the development of loyalty over a period of time. When a player tries to capture more benefit from the transaction and it continues over a period of time, other player tries to find a new partner and if he gets a suitable one, loyalty towards the older one ceases. Sustainability over a period of time is required for the loyalty to exist. Thresholds and reasons for moving away from loyalty has been stated here so that both customers as well as sellers can follow and can have better and more relationships for the overall development.

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