Building Customer Loyalty for Company Profitability

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Abstract – This paper aims to review several possible ways of building customer loyalty in business and investigate the correlation between company profitability and customer loyalty. For this purpose, a comprehensive literature review on several marketing approaches utilizing foundations of customer loyalty was performed with a focus on real company cases. A marketing model with four main factors, namely building customer-firm/staff relationship, establishing brand affinity, offering loyalty programs, and avoiding customer demotion was developed depending on those marketing approaches. Findings obtained from this marketing model show that customer loyalty generated through four main factors enhances company profitability based on the empirical data presented in this paper. The proposed marketing model would be helpful for business owners to better understand the customer behaviors and to build loyal relationships with them. The study also indicates how marketing approaches contribute to the customer loyalty and how do these techniques can be utilized by company owners to promote their businesses’ profitability.

Keywords: Customer Loyalty, Brand Affinity, Loyalty Programs, Customer Demotion, Customer Relationship

INTRODUCTION

The foundations of contemporary marketing first emerged in late 1960s, as the driving force for profit has switched from selling methods to needs and wants of the customers in early 1970s [2, 3]. In one of the early works of Kotler, he and his colleague makes an abrupt definition as “Marketing is a pervasive societal activity that goes considerably beyond selling of toothpaste, soap, and steel” and highlights the fact that “it involves product development, pricing, distribution, communication, and continuous attention to the changing needs of customers” [4]. Within the evolutionary framework of marketing and in today’s general terms, marketing can be defined as “a social and managerial process by which individuals and groups obtain what they need and want through creating and exchanging products and value with others.” [5].

From our perspective, marketing has evolved in an unprecedented way as consumer demands and the need trends have changed overtime. In order to keep up, companies need to involve multidisciplinary approaches such as arts, sciences, technology, and engineering. This change in the way marketing described is partly due to the availability of more consumer goods supplied by a variety of competitive companies, the increased perception of knowledge and the demand for the highest quality products among consumers. Regardless, it is inevitable for companies to adopt this evolutionary change by utilizing advanced design and technology tools to promote their products, while understanding both of their existing and potential customer profiles through social science and engineering. From where contemporary marketing stands today, these are the bare essentials for a company to survive. However, it should be noted that as every attempt made to optimize a company’s marketing approach, comes with additional

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risks and costs. Therefore, it is utmost importance for companies to keep everything under control while the constantly changing world of the marketing is adopted. If the required research, knowledge and technology transfer is not fully completed, the company will end up loosing their traditional revenues and market shares prior to the changes made in marketing strategy. Capon and others acknowledges and highlights the importance of consumer trends research and knowledge transfer to adopt new marketing trends while keeping the costs optimal [6-9]. As a result, attracting new customers by offering superior value and keeping current customers by making them satisfied are established purposes of contemporary marketing. Yet, it is easier to increase the retention of current customers than to acquire new customers in competitive environments, as this process requires less budget and effort. Therefore, customer loyalty has recently gained significance and started to spread along with the development of various strategies to make customers loyal.

The simplest definition of customer loyalty can be described as “the willingness to purchase the same brand or product again and repeat business for a company.” [10]; while the importance of customer loyalty can be emphasized with these words: “Loyal customers are backbone of every company; rewarding that loyalty should be the focus of everyone’s resources.” [10]. This concept has been also linked with customer satisfaction and theorized as “customer satisfaction is related to customer loyalty, which in turn is related to profitability” [11]. It is also believed that “the loyalty-centered business approach focuses on developing and managing the customer value package – the combination of factors that create what the customer perceives as a superior value in the relationship with the seller.” [12]. In this paper, three factors that generate the customer value package are examined since building customer loyalty entails a comprehensive understanding of each component of the value package. Also, it is aimed to address the ways of turning a factor, which has a negative impact on building customer loyalty, into a factor that can be considered as one of the customer value package components. These factors are customer-firm/staff relationship, brand affinity, loyalty programs, and customer demotion.

**RESEARCH METHOD**

Review-centric research theory helps to examine the four independent factors’ impact on building customer loyalty by providing a theoretical and empirical knowledge about each approach [13]. It builds on the principal that customer perception tends to be related to four factors including customer-firm/staff relationship, brand affinity, loyalty programs, and customer demotion. On the other hand, the case study theory helps to establish a relation between the customer loyalty and the firm’s profitability by allowing us to observe the customer perception through multiple case study analysis [14]. In other words, discussions and information obtained from review-centric theory and the case study theory are used in this paper to anticipate that the customer loyalty can be built by many different strategies and result in with substantial increases of the company’s sales.

**WHAT IS CUSTOMER LOYALTY?**

Before examining the marketing model and factors that affect customer loyalty, it is important to understand the exact meaning of loyalty. There are various broad definitions for customer loyalty. However, within the concept of this paper, it can be described as “a positive belief in the value that a company provides, leading to increased purchases over time.” [15]. Even though there is a strong connection between the customer loyalty and customer satisfaction [11, 16], they cannot be considered as the same notion. Loyalty can be built on satisfaction, so it means that companies can satisfy their customers without establishing loyal relationships. Therefore, customer loyalty should be conceived different from customer satisfaction in terms of its requirements.
The model above aims to review independent factors that each has some sort of impact on building customer loyalty. Hypotheses developed state that building customer-firm/staff relationship, creating brand affinity, and delivering loyalty programs are factors that positively affect loyalty intentions. On the other hand, customer demotion is a factor which negatively affect loyalty intentions. However, we believe that avoiding customer demotion can be considered as another positive factor, which will also be hypothesized in this paper. It is also intended to review the correlation between customer loyalty and company profitability.

**HOW TO BUILD CUSTOMER LOYALTY**

The key to build customer loyalty can be considered as treating people how they want to be treated. Creating strong emotional bonds with the customer, delivering incentives and benefits, establishing positive affiliation with the community, and avoiding customer demotion are some of the key factors that have positive impact on customer loyalty. To build strong customer loyalty, these factors should be assessed first. It should also be decided that each factor to what extent affects the customer loyalty by measuring the value from customer’s point of view.

**Building Loyal Relationships**

In recent years’ reduced spending and increased competitive environment, "relationship marketing" is one of the most widely used terms within the marketing literature as it enhances customer loyalty. The relationship marketing can be defined as “all marketing activities directed toward establishing, developing, and maintaining successful relational exchanges” [17]. Companies can gain invaluable information on how to serve customers in the best possible way and how to increase their repetitive buying behaviors by building strong firm/staff-customer relationships. It should be noted that the customer–employee relations turn into the customer–firm relationships over time. It is emphasized that “Customers who have strong relationships with service staff commit to the firm, which strengthens the customer–firm relationship.” [18]. However, it is also believed that “the challenge of building customer loyalty through staff excellence goes beyond wages and benefits” [19]. Therefore, companies should train their employees in the way of building relationships with their customers. In addition, building strong customer relationships generates mutual benefits for both the company and the customer. Moreover, companies can obtain quality sources of marketing intelligence for better planning of their marketing strategy by implementing relationship marketing to their business. The importance of loyal relationships can be emphasized with these words “Perhaps firms fail to build strong customer loyalty because they are unable to create strong emotional bonds with their customers.” [20]. There are many ways of establishing loyal relationships such as creating personal interaction with the customer, keeping the customer informed, and deciding the right attitude and customer liaison.
In consumer world, it is a rule of thumb that everyone wants to feel special. Therefore, it is important for employees to treat every single customer as, not their only customer, but also their most important customer. For example, remembering some important details about customer is one of the factors that contribute to build loyal relationships because customers think that they will get more benefits like discounts or rewards when they are remembered by the vendors. This feeling makes customers more willing to buy from the same store again and again by establishing a circle of trust between the customer and the firm.

It is also suggested that “One of the simplest ways to keep customers feeling special and make them feel important to you and your organization is to keep them informed.” [21]. Hence, keeping customers informed about potential problems, changes, and coming up events makes the company more connected with its clients. These can be done by phone calls, e-mails, letters, face-to-face interactions, advertising, posters, and/or magazines. However, it is important to get permission from customer before sending information about something in particular. Also, the content of the information should be chosen carefully. For example, informing customers about something that does not related to their needs can be resulted with withdrawal of those customers.

Deciding right attitude and customer liaison include both verbal and non-verbal behaviors. It is emphasized that “People would rather buy from a friendly and enthusiastic trainee than an indifferent expert.” [22]. Hence, it is very crucial for employees to be positive, enthusiastic, and helpful in critical times. For example, using negative and simple expressions like “There is nothing I can do” or “You have come through to the wrong extension” can be considered as ‘push factors’ from the perspective of a customer. Thus, it is essential for employees to communicate with the customers by using positive expressions all the time.

When a customer has a problem, employee should try to understand the customer and find a way to solve it. If there is no way to solve that issue, employee should comprehensively explain the reasons and his/her authorities on this issue to the customer. In this kind of situation, using jargon words makes the situation more complex, so it has always better for employees to choose simple and clear words while communicating with the customers.

\[ H_1: \] Customer-firm/staff relationship has a positive influence on building customer loyalty.

Creating Brand Affinity

It is possible for firms to build customer loyalty by establishing a brand’s “psychic” value through positive affinity or affiliation with a community. However, brand affinity should be conceived different than the brand loyalty because it goes beyond loyalty. Marketers do not have to put any effort to convince customers to buy something, but they have to help their customers to create personal connection with the brand by providing meaningful information (including particular interest and lifestyle) through engaging with online social communities. In other words, companies help customers to generate positive feelings toward their brands by taking advantage of community’s power. Hence, customer’s emotional connection with a brand can be considered as “brand affinity”. Since most of these consumer feelings are real and strong but not always logical, brand affinity can be conceived as a very powerful term for companies while building customer loyalty. For example, “Apple and Harley Davidson are the brands known with well-understood attributes such as innovation, and freedom of personal expression. People often buy these brands because they are identified with them and want them to be part of that shared identity. They perceive the brand as representing or complementing some highly personal aspect of their personality, social class or their values – or sometimes they believe that being associated with these brands makes them more cool.” [23].

\[ H_2: \] Creating brand affinity has a positive influence on building customer loyalty.

Delivering Loyalty Programs

In every purchase made, consumers give either voluntarily or unconsciously some of their information to the companies which perform loyalty programs. By using this data, companies offer their customers rewards and incentives that increase the frequency of purchasing or patronage which creates tangible motivation for customers to come back to the same store. Today, every company has some sort of loyalty program because loyalty programs are one of the well-known marketing strategies to build and promote customer loyalty and thereby increase the company’s long-term profitability [24]. Customers’ participation in loyalty programs has also grown steadily during the past decade depending on the application of those programs to various sectors such as airlines, banking, store...
retailing, and hotel chains [25-27]. It is indicated that “Companies in the United States spend more than $1.2 billion on customer loyalty programs per year, and the average household belongs to 12 of such programs.” [28]. Even though some of these programs are not worth the time, money or effort required to get any real benefit, it is fact that a properly executed loyalty program enables companies to obtain detailed customer information, to improve retention rates, to differentiate its products and services as well as brand equity, and to improve company profitability. For example, Starbucks’ reward cards allow its customers to receive free drinks on their birthdays. Customers also earn a free drink at the end of every 15 purchases. The most important thing is that the Starbucks delivers completely personalized reward programs. The company provides its customers special offers and coupons based on what they purchase the most. So, this innovative loyalty program of Starbucks created loyal customers for the company and it directly affected the company’s total net revenues at a rate of 84% during fiscal 2010 [29, 30]. Since loyalty programs are usually based on altering customer behavior by providing them incentives and benefits, it is necessary for the company to design and manage relationships between different incentives. Most common incentive areas can be hierarchical/bonus and reward-oriented programs, and promotions.

Customers need to be given a reason to increase their purchases with a particular company, so bonuses offered for reaching a higher-level status can be considered as the best incentives in this manner. Bonus and reward-oriented programs are also known as hierarchical loyalty programs. These types of programs can be defined as programs which “award preferred customer status, providing exclusive benefits to consumers who have exceeded a certain spending level” [28]. All of the clients are treated the same within the scope of these incentives as everyone receive the same amount of bonus or reward from any particular purchase. However, high level spending is required in order to maintain the elevated status. The various types of rewards include accrual rewards (where the member receives something for making a purchase or completing an action), redemption awards (where the member receives discounts or even free products or services, generally by redeeming points or using a voucher), and service awards (where the member receives specialized services) [15].

On the other hand, promotions are used by firms in order to provide additional incentives for customers who fulfill the desired behavior within a specific time frame. Therefore, promotions usually require some criteria such as the products must be purchased, the channel must be used, and the actions must be done within a given time frame [15]. It is also possible for companies to provide more than one promotion for customers who meet those specified criteria.

**H1: Delivering loyalty programs has a positive influence on building customer loyalty.**

**Avoiding Customer Demotion**

Hierarchical loyalty programs, which have been implemented in various service sectors for many years, promote customer status of consumers who exceed the specific spending level within a given time frame. Since loyalty programs are directly related to the customers’ spending levels, it is inevitable for companies to lower customer status within a program once the spending level diminishes [31]. This process is basically known as customer demotion and withdrawal of desired customer status and the advantages associated with it [28]. It was verified by many researchers that customer demotion triggers the occurrence of negative emotions within the person whose status is degraded when the subject is transaction [32, 33]. Since “emotions play a key role in the evolution of consciousness and the operations of all mental processes” [34], they should be considered by companies while building customer loyalty. Because, any potential status reduction can adversely affects the customer’s purchasing behavior by awakening a sense of being treated as a second-class customer. Thus, it can be concluded that negative emotions reduce the company’s loyalty intentions by causing the formation of a weak relationship between the vendor and customer. Depending on these factors, a significant decrease on the company’s transactions and revenues may occur. In order to avoid customer demotion, companies should keep their customer elevation periods longer than one year because sometimes such brief time periods can be inadequate to make reliable evaluations about customers’ contributions to the firm’s profit [35]. Also, it is a fact that most of the customers usually tend to make a purchase in case of losing their elevated status because hierarchical loyalty programs offer them an opportunity to get some benefits given in Figure 2 with their names and definitions. Therefore, sending warning notifications to the customers who are about to be demoted can be another method to encourage them for an immediate spending. Through these marketing strategies, it is possible for companies to transform customer demotion into a factor.
influencing loyalty intentions in a positive manner without damaging the existing relationship with their customers.

\[ H_4: \text{Customer demotion has a negative influence on building customer loyalty.} \]

\[ H_{4a}: \text{Avoiding customer demotion has a positive influence on building customer loyalty.} \]

Figure 2: Perceived Benefits from Loyalty Programs

<table>
<thead>
<tr>
<th>Dimensions of benefits</th>
<th>Sub dimensions of benefits</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Utilitarian</td>
<td>Monetary savings</td>
<td>To spend less and save money</td>
</tr>
<tr>
<td></td>
<td>Convenience</td>
<td>To reduce choice, and save time and effort</td>
</tr>
<tr>
<td>Hedonic</td>
<td>Exploration</td>
<td>To discover and try new products sold by the company</td>
</tr>
<tr>
<td></td>
<td>Entertainment</td>
<td>To enjoy collecting and redeeming points</td>
</tr>
<tr>
<td>Symbolic</td>
<td>Recognition</td>
<td>To have a special status, to feel distinguished and treated better</td>
</tr>
<tr>
<td>Social</td>
<td></td>
<td>To belong to a group that shares the same values</td>
</tr>
</tbody>
</table>

(Source: Mimouni-Chaabane & Volle, 2010) [1]

LINKING CUSTOMER LOYALTY AND COMPANY PROFITABILITY

Customer loyalty is an important determinant of a company’s long-term operational efficiency. To maximize the profit, companies have to look for the ways of building and maintaining customer loyalty. As customer loyalty and lifetime value creation are inextricably linked to each other, high customer retention offers companies countless benefits. First of all, as it is mentioned before, acquiring new customers requires more efforts and budget. Therefore, keeping existing customers with high retention rates helps companies to shrink their costs at a significant level. Reduced costs, repeat sales, and referrals accelerate the growth of company revenues and market share. Profitable growth leads companies to be more committed to provide high quality product or service and to make innovations. Reinforced customer retention and better customer service enhances employees’ job pride and satisfaction so that employee retention increases as well. It was confirmed, “The companies with the highest retention rates, also earn the best profits.” [36]. For example, Lexus is one of the companies that approve the importance of customer loyalty. Thus, the company established a system which allows it to monitor the loyalty levels of both auto sales and post-sales services. Through this approach, the company has attained the capability of taking immediate action in case of low retention rate by analyzing the differences between the dealers who earn superior customer loyalty and those who do not. According to the J.D. Power and Associates’ customer service index study conducted among luxury car
brands operating in the United States, it was verified that the Lexus attained the highest repurchase rate with the overall score of 861 out of 900 [37]. It was also reported that this high customer retention rate of Lexus increased the company profits at a rate of 33% [37-39].

CONCLUSION

Although establishing a steady customer base is neglected most of the times by enterprises, it should be highlighted that the large amount of a company’s profit comes from its customer chain. Since the cost of attracting new customers is significantly higher than the cost of maintaining existing relationships, the company efforts should be focused on to build customer loyalty while trying to boost the revenues. Also, it should be noted that the customer loyalty means more business, more profitability, and thereby greater rewards for all employees who create success every day. Traditionally, competitive advantage comes from access to low-cost raw materials, energy sources, or financial capital, and an ability to invest in physical capital to achieve economies of scale and scope. In recent years, this belief has completely changed. Today, having loyal and profitable customers is the key of creating a lifetime value for a company. Therefore, today's most innovative firms have started to look for the ways that turn the loyal customer into an essential extension of the company's sales, marketing, and product development teams.

REFERENCES


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