

MARKETING OF FINANCIAL SERVICES

Lecture Eleven

Customer Relationships, Retention, and Loyalty in Financial Services Marketing

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WEEK ELEVEN

11.1 Introduction

Welcome to week eleven lecture! We are almost coming to the end of this series of lecture. It is my hope that you have gained a lot of insight on how to market financial services. In this lecture we want to focus on how financial institutions build relationship with their customers, how they turn them to become loyal customers and retain them. This is a major area of focus given the current level of competition in the marketplace prompted by growth in technology.

11.2 Intended Learning Outcomes

At the end of this lesson, you will be able to

- a) Discuss relationship marketing in the context of financial service marketing
- b) Evaluate strategies of customer retention applied by financial institutions
- c) Examine ways of maintaining customer loyalty

11.3 Relationship Marketing in Financial Services Context

Building customer relationship has gained a lot of interest in the recent past in marketing of goods and services. This is because of the realization that building long term customer relationships offers a way of reducing defection rates, reducing costs and increasing revenues (Tina, 2000). Financial institutions are endeavoring to build this as a philosophy in all their undertakings to ensure that all staff work towards this goal. But what is relationship marketing and how does it work?

Various authors have defined relationship marketing in different ways. For instance, Berry and Parasuraman (1991) propose that relationship marketing concerns attracting, developing, and retaining customer relationships. On their side, Morgan and Shelby (1994,) state that “Relationship marketing refers to all marketing activities directed toward establishing, developing, and maintaining successful relational exchanges”. Contributing to this subject, Bruce de (1988) viewed relationship marketing as the process of attracting, maintaining, and enhancing relationships with key people. From this definition we note that relationship marketing is concerned with all activities directed towards establishing, developing, and maintaining successful exchanges with customers and other constituents. This is informed by realization that loyal customers are far more profitable and maintaining strong relationships with customers secures important and durable advantages that are hard for competitors to understand. Tina (2000) views relationship marketing as one that includes all activities of attracting, maintaining and enhancing customer relationships with an organization taking into account both offensive and defensive marketing strategies while at the same time incorporating a customer service element.

From these definitions we recognize that relationship building is a deliberate activity undertaken by financial institution to attract, develop, maintain and enhance beneficial relationship with various clients. This strategy offers the firm a variety of benefits, but it also comes with challenges

that will be considered in this lesson. The rationale for relationship building is the realization that increased competition in the financial sector is exerting pressure on financial institutions' abilities to retain profitability levels coupled with the fact that these firms need to consider why it is necessary to build relationships with customers.

11.4 Advantages of Building Relationship with Customers

There are many benefits that accrue to a firm because of building relationship with a customer. First, the financial institution is likely to sell more products and services to the customers that they have developed relationship with. This is because they have already built trust in them and would find it easy to transact with the institution, they know than one they don't. Second, we find that the cost of serving a well-known customer is low and this has effect on increasing overall profitability of the firm. New customers are often unprofitable to the firm but as the relationship grows the firm is likely to benefit from them in the long run. Third, we note that when customers are satisfied with the firm, they are likely to spread a positive word of mouth which is key in increasing customer base of the firm. This is also considered as free advertising and is sure to increase firms' revenue in the long run. Referred customers are also of higher quality and tend to be more loyal to the firm. The other advantage is that employee's retention rate is likely to be higher as anyone would want to work in a place where customers are happy and loyal.

To the financial customer, there are also benefits that arise from having a good relationship with the firm. It is known that customers initially experience some degree of anxiety in identifying and dealing with a financial service provider for they are not sure of what to expect. However, when they build relationship, they develop a feeling of trust or confidence in the provider, along with a sense of reduced anxiety and comfort in knowing what to expect. This benefit will make the customer to always want to deal with this service provider. We also note that over the years the customers tend to familiarize with the financial institution and even build a social relationship. This relationship is incremental in ensuring that they don't want to join competitors whom they may be familiar with, the social relationship may be extended into the customers family and their networks and thus benefits them a lot. Often the customers get special treatment due to the relationship they have with the financial institution.

Other benefits of building relationship include the understanding that it takes time to make money from customers; that sales, marketing, and setup costs amortized over a longer customer lifetime that repeat customers often cost less to service and that relationship allows cross selling opportunities that leads to customer spending in the institution over time. Another benefit is that relationship allows for intergenerational relationships coupled with the fact that satisfied customers provide referrals and may be willing to pay a price premium.

11.5 Drawbacks of Relationship Marketing

Though relationship marketing is hailed for its contribution to increasing business performance, there are also demerits to this business strategy. First there is danger of an institution ignoring new

customers and focusing only on the old ones. This may deny the financial institution numerical growth in terms of customers. The second drawback is the understanding that most customers today are not focused on long term gratifications. Many of them are not concerned about long term relationship, and this makes it difficult to effectively utilize this theory. Based on this understanding that not all customers want to develop relationship, marketers have an uphill task to determine whom to develop relationship with and the ones not to. Relationship takes time and resources to build, and this may not be easy especially with new and small financial institutions. It also emerges that sometimes customers and financial institutions form very close relationship which may not work very well for the business. Sometimes there is need to change value proposition and the relationship marketing may not augur very well as customers may not appreciate change in some instances. It becomes even harder to apply relationship marketing when there is need for cultural change. Finally, we find that the customers who develop relationship may raise too many demands which the financial institutions may not be able to meet, and this may affect relationship there in.

11.6 The Process of Relationship Development

The process of relationship development has been defined as consisting of eight distinct stages (Stone and Woodcock,1995).

- (i) **Recruitment:** in this stage the marketer identifies the clients he would want to develop relationship with. Not all clients are directly profitable and therefore the marketer must ensure he segments the market and chooses the specific clients to develop relationship with.
- (ii) **Welcoming:** in this stage the marketer welcomes the potential client and makes his intent of wanting to develop a relation with the customer clear. At this point the client has also to decide whether he would want to be in a deeper relationship with the financial institution.
- (iii) **Getting acquainted:** it is in this stage that the marketer seeks to know the goals, aspirations, needs and wants of his client. They will agree on how the financial institution will support the client in meeting his objectives and also the price client will pay for these services. Both parties want to develop a mutually relationship where all players benefit a lot.
- (iv) **Account Management:** this is the stage of running the accounts where the client does his side of the contract and likewise the marketer. Both parties are working to ensure the relationship works and incase of any difference they try to resolve the problem. The willingness of parties to remain in the relationship is what makes the contract hold or get dismissed.
- (v) **Intensive Care:** this occurs when the parities have a very serious difference that has the potential to cripple or even terminate the relationship. The marketer must do everything to try and salvage the relationship unless the demands made by the client are not possible within the financial institution or contravenes the law.

- (vi) Potential divorce: occurs when the differences between the parties cannot be resolved. The parties negotiate terms of ending the relationship. Though still hopeful that the relationship can be salvaged both parties regret that they have come to this level and are seeking ways of reuniting.
- (vii) Divorce: this stage is arrived at when the parties have to part ways. Divorce is painful but sometimes is the only solution especially when one party is not willing to give up some of its demands. Divorce must be done in such a way that there is room for coming back together and continue the business.
- (viii) Win back: this is the final stage where the marketer tries to win back the lost customer. As they say in politics, there are no permanent enemies in business, and all must work to ensure they meet their interest.

In the recent past we have seen financial institution work closely with their customers even in promotion. We have seen customers give testimonials of how their relationship with financial institutions have made them grow and how they have benefited from the relationship. The marketer must always seek ways of renewing relationship as it is the basis for his success.

11.7 Customer Retention

A well-built relationship often leads to customer retention. It is difficult to regain lost customers and therefore financial institution must do everything to minimize defections. Retention is the ability of financial institution to maintain its customers for a long period of time. It also implies increased business for the financial institution from the current customers.

There are many reasons why a financial client would want to remain in a financial institution or leave. Tina (2000) notes that clients would want to remain because of the rewards achieved, discounts given and the purchase of additional products from the financial institution. Financial institution also works with other firms to offer a package of benefits to customers free travel insurance, free legal expense insurance, free card loss insurance, free banking, and a year's warranty on household goods etc. Financial customers may also opt to leave a financial institution due to more attractive alternative elsewhere.

Customer's defection is very costly to a financial institution and must be addressed to reduce or even eliminate it. For us to be able to address it effectively, we need to understand the defection process well. Stewart (1998) identified the following stages of customer's defection process.

- a) *The problem*- customer's defection begins with a customer encountering a challenge in process delivery by financial institution. The problem could be related to service facilities, information sent to customer, breach of confidentiality or mishandling by financial institution staff.
- b) *Effort*- upon experiencing the problem, the customers will seek means of resolving it within the shortest time possible. The customer will contact the financial institution and if the institution does little to resolve the problem, the customer will proceed to the next step of defection.

- c) *Emotion*- upon realization that nothing much has been done to resolve the problem, the customer will become emotional not necessary because of the problem but the fact that nothing much is being done about it. The customers will become angry, disappointed, and frustrated.
- d) *Evaluation*- emotional stage is followed by evaluation where the customers reconsider his relationship with the financial institution. The customer will also consider alternative providers of the service and find out whether he is better of dealing with them.
- e) *Exit*: the customers will result to exit if he finds the problem was not well resolved and that a better alternative exist. For a financial institution, the customer will close the account or avoid doing any transaction through that account.
- f) *Post-exit evaluation*- this is consideration on the new service provider. The customer will keep on evaluation this relationship to see if it meets his expectation. He might also reconsider going back to the first service provider especially if they reach out to him.

With this understanding, it is evident that listening to customer at the point of complaint is key to resolving the matter. The marketer must provide the best options to the customers and where necessary apologize for poor service delivery. The marketer must try to empathize and guarantee the customer that the problem will not occur again.

In order that customers may be retained, financial institutions need to develop a retention strategy. DeSouza (1992) outlines a simple four-stage plan to foil defectors and boost retention rates:

1. *Measure customer retention*: the starting point of addressing retention problems is determining the retention rate. Depending on how serious the problem is the marketer will come up with appropriate measures. Retention rate is measured as a proportion of those who have been doing business and how many remain within a certain period.
2. *Ascertain defection motive*: the financial service provider must seek to understand why certain accounts have been closed. Understanding the motive helps the firm to retain others by addressing the reason behind movement.
3. *Analyze complaint and marketing research data*: this would help the firm to understand real cause of the problem of defection and how it can be resolved. Encouraging customers to air their concerns is critical if the firm will succeed in addressing defection problems
4. *Identify and erect switching barriers*. The financial institution must develop positive switching barriers to stop customers from leaving. Positive barriers can lead to better service, superior products, and technological innovation, thus eliminating several common reasons for defection.

11.8 Customer Loyalty

Let us now turn our attention to customer loyalty. Loyalty will be enjoyed if customers are satisfied and are willing to remain with current financial services provider. Loyal customers are an asset to financial institution and must be kept at all costs. They add a lot of value to the financial institution

and enough effort must be expended to keep them. The level of customer satisfaction leads to certain level of loyalty. Schiffman and Kanuk (2004) identified the following categories of customers because of loyalty. The level of customer satisfaction can result in several types of customers:

- Loyalist- are completely satisfied customers who keep on purchasing,
- Apostles: who provide very positive word of mouth about the company to others,
- Defectors: who feel neutral or merely satisfied and are likely to stop doing business with the company
- Terrorist: who have had negative experiences with the company and spread negative word of the mouth,
- Hostages: those who are unhappy but stay with the company because of monopolistic environment:
- Mercenaries: customers who are very satisfied customers but have no real loyalty to the company and may defect because of lower prices elsewhere.

On his side, Griffin (1995) noted that the attachment an individual has to a company, or its products/ services is shaped by two dimensions: degree of preference and degree of perceived product differentiation. Combining behavioral and attitudinal differences results in segments that exhibit varying degrees of loyalty, which include:

- True loyalty: this is indicated by high repeat patronage and a high relative attitude toward the company. Financial institution would desire this kind of loyalty and would develop loyalty schemes for the same.
- No loyalty: low repeat purchase combined with a low relative attitude towards the company signifies the absence of loyalty. The financial institution would want to avoid this situation
- Latent loyalty: low repeat patronage but a high relative attitude signifies latent loyalty. Thus, the customer is favorably disposed toward the financial institution and its product and services but is not a heavy user of them.
- False loyalty: despite a relatively low attitude toward the financial institution the customer continues to patronize it. From a purely behavioral perspective, these customers appear to be extremely loyal. Several factors can generate false loyalty or make customer to be deeply loyal when they are not. These include government regulation that limits competition, a logistical infrastructure which essentially holds the customer hostage to the bank by increasing the barriers to switching, or proprietary technology that limits alternatives. All of these have contributed to a certain degree of false loyalty among financial services consumers.

11.9 Review questions

1. Critically evaluate the various definitions of relationship marketing and come up with your own in the context of financial services marketing
2. Citing relevant examples from your country, describe how financial institution apply relationship marketing in building their brand
3. Discuss merits and demerits of relationship building in marketing of financial services
4. Why is it necessary for financial institutions to retain their customers?
5. Do customers always want relationship with financial institution? Justify your response
6. Most of financial institution customers are always loyal to them. Discuss

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