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SERVICE QUALITY AS A PROFIT STRATEGY IN MARKETING:
THE SERVICE-PROFIT CHAIN MODEL

Abstract

Service quality in marketing of goods or services is getting more important day by day. Because competition in every sector is becoming more severe in a global world market. High service quality is one of the key elements to increase customer satisfaction and loyalty. At the same time it is one of the main factors in profitability, development, and sustainability of businesses. In this article, it is emphasized the importance of service quality in customer satisfaction and loyalty. Service-profit chain model is examined. As the case study, some research findings from academical and managerial perspectives are summarized. And some proposals are made to promote high quality services as an important aspect of successful marketing management.

Keywords: Service quality, Service-Profit Chain Model, Customer satisfaction, Customer Loyalty

Introduction

Services marketing concepts and strategies have developed in response to the tremendous growth of service industries resulting in their increased importance of

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the world economies (Zeithaml and Bitner, 1996 cited in Bitner et al., 1997). As it is stated in the Memorandum of Understanding which has been signed between Gulf Organization for Industrial Consulting (GOIC) and the Geneva-based International Services Trade Information Agency (ISTIA) in Doha Qatar (2007) “In the new millennium, services are instrumental components of industrial activities; previously, services and industrial business activities were viewed as distinct and separate. The modern global economy views services and industrial activity as symbiotic and integrated for two principal reasons. Firstly, because businesses require efficient services sectors such as transportation and communications for domestic or import/export commercial operations. Secondly, modern business models no longer view companies as strictly services-only or industrial-only”. Meanwhile, because of increasing of competition, especially after liberalisation of the economies and globalization, now more than ever, customers patronize the institutions that best serve their needs. The better the service, the greater the number of customers. The greater the number of customers, the better a company’s financial performance. As many industry sectors mature, competitive advantage through high quality service is an increasingly important weapon in business survival. The tourism industry has certainly not been exempted from increased competition or rising consumer expectations of quality (Fen and Lian, 2010, p. 60). Service is a key component of value that drives any company’s success. To the customer, value is the benefits received for the burdens endured – such as price, an inconvenient location, unfriendly employees, or an unattractive service facility. Quality service helps a company maximize benefits and minimize non-price burdens for its customers (Berry, Parasuraman and Zeithaml 1994 p. 32).

Quality and service quality

There are many researchers who have defined quality and service quality in different ways. A modern definition of quality derives from Juran’s “fitness for intended use”. This definition basically says that quality is “meeting or exceeding customer expectations” (SHSU, 2011). The British Standards Institute definition of quality, which is identical to the ISO and the EN standards, is “the totality of features and characteristics of a product or service that bear on its ability to satisfy a stated or implied needs” (Johnson and Winchell, 1988; Businessdictionary, 2012).
On the other hand, service quality is often conceptualised as the comparison of service expectations with actual performance perceptions (Zeithaml and Bitner, 2003). From this perspective, Mackay and Crompton (1990) as cited in Prabaharan, Arulraj and Rajagopal (2008) defined service quality as “the relationship between what customer’s desires from a service and what they perceive that they receive”. According to Chakrabarti, Whitten and Green (2007–2008, p. 3) service quality can be defined as the conformance to customer requirements in the delivery of a service. Service quality refers to a number of inter-related factors including the way in which individuals are treated by providers, the scope of services and contraceptives available to clients, the quality of the information provided to the clients and quality of the counseling skills, the promotion of individual choice, the technical competence of providers, and the accessibility and continuity of services (Erc.msh, 2010). Service quality is an intangible, but crucial, area of interest to travel service providers (Prabaharan, Arulraj and Rajagopal, 2008).

Increasing importance of service quality

Backman and Veldkamp (1995) as cited in Prabaharan, Arulraj and Rajagopal (2008) stated that quality of service is an essential factor involved in a service provider’s ability to attract more customers. The quality of a product or service is the main characteristic when it comes to selling. There are many and diversified factors that determine the success of the sale. They include market conditions, type of product/service, the image created by advertising, socio-cultural peculiarities of customers etc. But the major factor that ensures the marketability of a product/service is its quality as it was approved by the customers (Dragolea and Todoran, 2009). Delivering excellent service is a winning strategy. Quality service sustains customers’ confidence and is essential for a competitive advantage. Excellent service is a profit strategy because it results in more new customers, more business with existing customers, fewer lost customers, more insulation from price competition, and fewer mistakes requiring the reperformance of services. Excellent service can also be energizing because it requires the building of an organizational culture in which people are challenged to perform to their potential and are recognized and rewarded when they do. Service is a key component of value that drives any company’s success. To the customer, value is the benefits received for the burdens endured – such as price, an inconvenient location, unfriendly
employees, or an unattractive service facility. Quality service helps a company maximize benefits and minimize non-price burdens for its customers (Berry, Parasuraman and Zeithaml, 1994). All businesses whose service depend on building long term relationship need to concentrate on maintaining customer’s loyalty. In this respect, loyalty is greatly influenced by service quality. As such, hotels often invest in managing their relationships with customers and maintaining quality to ensure that customers whose loyalty is in the short term will continue to be loyal in the long term (Al-Rousan and Mohamed, 2010).

Quality is what makes the difference between a service and another, between one provider and another. Quality services can provide access to international markets; quality reduction may be compromising, is very expensive, and can be harmful and sometimes impossible to recover. A quality service brings immediate and lasting satisfaction to the clients, tourists and also to the provider (Dragolea and Todoran, 2009). Service quality has been shown to result in significant benefits, such as profit level increases, cost savings, and increased market share, to firms (Parasuraman, Zeithaml, and Berry, 1988). Competition through service quality enables the organization to develop a competitive edge without the loss of revenue (Carper, 1992 cited in Lashley and McGoldrick, 1994, p. 28). Simply stated, customer satisfaction is essential for corporate survival. Several studies have found that it costs about five times as much in time, money and resources to attract a new customer as it does to retain an existing customer (Naumann, 1995 cited in Pizam and Ellis, 1999, p. 326). Improved service quality results in greater customer satisfaction and loyalty, which, in turn, creates repeat business and opportunities to cross-sell, both of which are natural revenue enhancing activities (Harvey, 1995). Satisfaction of customers also happens to be the cheapest means of promotion (Pizam and Ellis, 1999 p. 326).

The components of service quality

As the world’s largest service sector in tourism, service quality comprises 10 dimensions, namely core-tourism experience, information, hospitality, fairness of price, hygiene, amenities, value for money, logistics, food and security (Profit-strategies, 2010). Webster’s marketing culture scale (1990) as cited in Luk (1997), this “service quality” dimension is composed of eight values:

- a succinct definition of excellent service,
— strong commitment to quality service of top management,
— systematic, regular measurement and monitoring of employees' performance,
— clear focus on customer needs,
— a strong linkage between employees' behaviour and the firm's image.
— the desire to meeting the firm's expectations on quality service,
— emphasis on communication skills,
— employees' attention to detail in their work.

In their study, Berry, Parasuraman and Zeithaml (1994) focus on the question of what could organizations do to improve service quality? And their answer is presenting lessons learned that we believe are essential for improving service quality. These lessons in headlines are Listening, Reliability, Basic Service, Service Design, Surprising Customers, Fair Play, Teamwork, Employee Research, Servant Leadership. Berry, Parasuraman and Zeithaml (1994) have constructed in Fig. 1 a service quality ring to capture these interrelationships. Listening is positioned on the outer ring because listening has an impact on all the other lessons. Identifying the basics of service, improving service system design, recovering from service shortfalls – these and other essentials of service quality involve listening behavior. Reliability is pictured in the center, because reliability

Fig. 1. A Service Quality Ring

is the core of service quality. Little else matters to customers when the service is unreliable.

The link among service quality, customer satisfaction and customer loyalty

Customer satisfaction is critical to any business. A happy customer is likely to give repeat business, provide word-of-mouth advertising, send referrals, and pay for services without dispute or delay. Anything one can do to improve customer satisfaction will pay dividends to the business in both the short and long term (Profitstrategies, 2010). Liljander and Strandvik (1994) cited in Storbacka, Strandvik and Grönroos (1994) have suggested that perceived service quality can be seen as an outsider perspective, a cognitive judgment of a service. It needs not even be experienced, it can be based on knowledge about a service provider through word-of-mouth or advertising. It is, however, usually also based on experiences with the service. Customer’s own experiences of a service where the outcome has been evaluated in terms of what value was received, in other words what the customer had to give to get something.

For a service-based business the “sale” is the service performed, which means making sure the service provided is to the customer’s liking. According to a recent Pricewaterhouse-Cooipers (2010) “Trendsetter Barometer”, four-fifths of America’s fastest growing companies have initiated important new programs aimed at customer expansion, customer retention, and customer profitability. A significant percentage of these are service-based businesses. The attitude, appearance, skill and professionalism of service staff is a vital element in effective service delivery. Therefore, the manner in which service industries recruit, train and manage their staff has a direct impact on customer satisfaction (Fuller, Hanlan and Wilde, 2006).

Many studies have investigated the relationship between service quality and customer loyalty. Shoemaker and Lewis (1999) argue that customer loyalty is built by focussing on three concepts: the overall service process, the use of effective database management and value creation either through added value or value recovery. Relationship marketing is widely accepted as the most successful way to build customer loyalty and competitive advantage in a mature, competitive market (Hotel Mule, 2010). Improved service quality results in greater customer satisfaction and loyalty, which, in turn, creates repeat business and opportunities
to cross-sell, both of which are natural revenue enhancing activities. This is quite the opposite of continually raising fees or cutting costs across the board (Harvey, 1995). The basic assumption is that customer satisfaction drives profitability (Grönroos, 1990 cited in Storbacka, Strandvik and Grönroos, 1994). The assumption is based on the idea that by improving the quality of the provider’s service, customers’ satisfaction is improved. A satisfied customer creates a strong relationship with the provider and this leads to relationship longevity (or customer retention – customer loyalty). Retention again generates steady revenues and by adding the revenues over time customer relationship profitability is improved. Thus the firm can utilize potential customer relationship economic opportunities in a favourable way (Storbacka, Strandvik and Grönroos, 1994, p. 23).

The service-profit chain model

The service-profit chain is a powerful phenomenon that stresses the importance of people – both employees and customers – and how linking them can leverage corporate performance. The service-profit chain is an equation that establishes the relationship between corporate policies, employee satisfaction, value creation, customer loyalty, and profitability (Fig. 2).

![Service Profit Chain Diagram](image-url)

**Leveraging Your Corporate Performance**

- **Employee satisfaction**
  - Results from high quality support services and policies that enable employees to serve customers well
- **Value**
  - Created by satisfied, loyal and productive employees
- **Customer satisfaction**
  - Created by the value of services provided to customers
- **Customer loyalty**
  - Results from customer satisfaction
- **Profit & Growth**
  - Stimulated primarily by customer loyalty

Fig. 2. Service profit chain: linking employees and customers

Marriott who was the founder of the homonymous American hotel chain stated "you can't make happy guests with unhappy employees" who promoted the role of empowerment in driving customer satisfaction. Satisfied employees stay with the company for longer and therefore give a much better return on any investment (recruitment; training; pay-rises; package of benefits) put into them. The higher rate of return may stem from a prolonged use of company specific tacit knowledge that gets lost when employees leave the organization, and from the increased trust that customers will put in the organization if a stable staff represents it (Xu and Goedegebuure, 2005 pp. 56–57).

According to Heskett et al. (2008) the service profit chain establishes relationships between profitability, customer loyalty, and employee satisfaction, loyalty, and productivity. The links in the chain (which should be regarded as propositions) are as follows: Profit and growth are stimulated primarily by customer loyalty. Loyalty is a direct result of customer satisfaction. Satisfaction is largely influenced by the value of services provided to customers. Value is created by satisfied, loyal, and productive employees. Employee satisfaction, in turn, results primarily from high-quality support services and policies that enable employees to deliver results to customers (Fig. 3).

The overall objective of the service profit chain is to link initiatives of retention, referrals and related sales with the other links within the chain. These include satisfaction, loyalty, value and long-term growth (Maritz, 2005, p. 150).

Lashley and McGoldrick (1994) ideas developed and expressed in their article originate from their recognition that an increasing number of firms are considering employee empowerment as part of their human resource strategy for competitive advantage through hospitality service quality. Unlike the quality of a product, it is more difficult to define, to judge or express in quantitative terms, the quality of services is more as the service has little physical dimensions such as performance, operational characteristics and maintenance costs, which could be used to comparison or measurement. The human element in the production and consumption of services prevents the service provider from standardising production outcomes as is possible in a manufacturing environment. This lack of standardisation further increases the importance of service delivery processes and effective people management as integral elements of the marketing mix (Fuller, Hanlan and Wilde, 2006).
Research findings from academical and managerial perspectives

Several studies involving empirical analysis of some of the links in the service-profit chain have been undertaken. For example, In his study Maritz (2005) found that, despite a few associations being inadequate within the defined franchise system, service profit chain initiatives were positively associated with service quality.

As a result of their surveys Heskett et all (2008) conclude that a growing number of companies that includes Banc One. Intuit, Southwest Airlines, ServiceMaster, USAA, Taco Bell, and MCI know that when they make employees and customers paramount, a radical shift occurs in the way they manage and measure success. The new economics of service requires innovative measurement techniques. These techniques calibrate the impact of employee satisfaction, loyalty, and productivity on the value of products and services delivered so that managers can build customer satisfaction and loyalty and assess the corresponding impact on profitability and growth. In fact, the lifetime value of a loyal customer can be astronomical, especially when referrals are added to the economics of customer retention and repeat purchases of related products. For example, the lifetime revenue stream from a loyal pizza eater can be $8,000, a Cadillac owner $332,000, and a corporate purchaser of commercial aircraft literally billions of dollars.
Furthermore Heskett, Sasser, and Wheeler (2008) add that highly successful companies like Bouygues Telecom in France (the third largest in its markets in 2008 within ten years since its founding) and ING DIRECT (the 17th largest bank in the U.S. in 2008 after just seven years) have been created since then, based on service-profit chain (SPC) relationships. Others, such as Rackspace Hosting (engaged in Web site design and management), Westpac (one of Australia’s leading banks), CEMEX (one of the world’s largest cement companies, based in Mexico), Harrah’s Entertainment (a leader in branded casino entertainment, based in Reno, Nevada), and Baptist Health Care (a not-for-profit health care organization centered in northwest Florida and southern Alabama), have been revitalized through actions suggested by SPC relationships. Other companies, such as Circuit City, provide examples of what happens when organizations manage themselves into a “doom loop” of negative SPC relationships. In March 2007, Circuit City announced that it would replace 3,400 of its more experienced, higher-paid salespeople with new, lower-paid hires. In so doing, it damaged customer satisfaction and ultimately suffered the financial consequences.

ROI resource Center (2013) indicates that, the service-profit chain stresses the importance of people – both employees and customers – and how linking them can leverage corporate performance. This circular relationship between employees, customers and shareholders contributed to the well known Sear’s model in the mid-90: a 5% increase in employee attitude leads to a 1.3% increase in customer satisfaction which leads to a 0.5% increase in revenue growth. Led by CEO Arthur Martinez, a group of more than 100 top level Sears executives spent the better part of three years rebuilding the company around its customers and in the process changed its culture. The company tracked success from management behaviour through employee attitudes to customer satisfaction and financial performance.

In their survey, based on the case study of a UK home improvement store chain, measuring of each of the variables in the service profit chain Pritchard and Silvestro (2005) found that although analysis of the performance relationships revealed many interesting correlations, the data lent little support for some of the expected linkages; in particular, the “satisfaction mirror” effect between employee and customer satisfaction and loyalty, and the link between customer loyalty and financial performance. The possible asymmetries and non-linearity of certain performance relationships may also have added to the difficulty in applying the model to this organisation. Furthermore, the study revealed many performance linkages between variables which are not aligned in the service profit chain model.
Reichheld and Sasser Jr. (1990) observed that Charles Cawley, president of MBNA America, a Delaware-based credit card company, knows well how customer defections can focus a company’s attention on exactly the things customers value. Frustrated by letters from unhappy customers, he assembled all 300 MBNA employees and announced his determination that the company satisfy and keep each and every customer. The company started gathering feedback from defecting customers. And it acted on the information, adjusting products and processes regularly. As quality improved, fewer customers had reason to leave. Eight years later, MBNA’s defection rate is one of the lowest in its industry. Some 5% of its customers leave each year – half the average rate for the rest of the industry. That may seem like a small difference, but it translates into huge earnings. Without making any acquisitions, MBNA’s industry ranking went from 38 to 4, and profits have increased sixteenfold within eight years.

In their survey, realized with Orange Mobile call center employees and subscribers, Al-Tamimi, Hasoneh and Rezqallah (2009) reached the following conclusion:

A 1 degree increase in call center employees’ satisfaction represents approximately a 5% increase in achieving the company a competitive advantage among its competitors, which is sequenced as the following:

- a 1 degree increase in call center employees’ satisfaction represents approximately a 23% increase in customers experience and about 37% in customers’ satisfaction,
- such increase in customers experience and satisfaction represents nearly 17% increase in their advocacy,
- such increase in customer’s advocacy represents approximately a 8% increase in their loyalty to the brand,
- such increase in brand loyalty represents almost a 5% increase in achieving the company a competitive advantage among its competitors.

Finally, this research presented various recommendations that are applied to Orange Mobile top management; call center management and for further studies to be conducted.

The most important recommendations are:

- to adopt a philosophy of “putting people first” that applies to employees and customers, and this philosophy shall be reflected in the organization mission,
- to develop and maintain a corporate culture that is employee – customer centric.
- to adopt a comprehensive strategy aiming to achieve a competitive advantage among competitors through linking employees, customers and the financial performance of the organization.

In the case study concentrated on Health & Safety training of First Aid and CPR (cardiopulmonary resuscitation) courses, Pasupathy (2006) found that for each unit of increase in service quality, the level of satisfaction would increase by 0.69, the latent Brand Recognition will influence satisfaction by 0.22 while the perception of branch availability will influence the evaluation of level of satisfaction by 0.16, and so forth.

A study conducted by Stodnick (2005) reflecting a service profit chain perspective, realized in one large retail chain within the women’s specialty apparel industry. The study shows that employee satisfaction and loyalty can be increased by creating a positive internal working environment. Rather than reducing frontline service jobs to mundane, repetitive tasks, organizations can achieve competitive advantage by broadening job descriptions and developing their employees through commitment enhancing human resource practices. The best way to increase customer satisfaction is to provide a superior total retail experience. As previous research has indicated, customers who are extremely satisfied with their retail experience are less likely to search for alternatives decreasing the firm’s overall cost of serving their customer base, increasing store profitability. Moreover, satisfied and loyal customers are more likely to recommend the store to others and purchase secondary, ancillary products, increasing market share.

Xu and Goedegebure (2005) showed in their survey made among Chinese securities firms, employee satisfaction is positively correlated with customer satisfaction. Employee satisfaction and customer satisfaction have a positive impact on profitability. Customers perceive the positive energy and the willingness of satisfied employees to provide good services in terms of higher quality of services received. In turn, they become more satisfied and loyal to the company.

A research was conducted in the service industry of Hong Kong by Yee (2007). The results showed that the relationships among employee satisfaction, service quality, customer satisfaction, and firm profitability are significant, suggesting that employee satisfaction is an important determinant of operational performance in service organizations.
Conclusions

The ultimate goals of any business are to generate profit, to increase market share, and to be in the market for years. Customer satisfaction and loyalty are critical to succeed these goals. Excellent service quality is one of the key elements for customer satisfaction and loyalty. A happy customer is likely to give you repeat business, provide you word-of-mouth advertising, send you referrals. On the other hand, the achievement of service excellence and productivity standards is ensured by integrated and comprehensive human resource management practices, including effective recruitment techniques; training and development programmes; appraisals, incentive and reward schemes, job enlargement and other employee satisfaction systems. Effective human resource management practices are crucial to the achievement of service quality standards, productivity improvements, and thus profitability in businesses.

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