Decision Support

Exploring two explanations of loyalty in application service provision

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A R T I C L E   I N F O

A B S T R A C T

While the application service provider (ASP) market continues to grow, it is fiercely competitive, and ASPs encounter difficulties in retaining customers and achieving long-term profitability. One stream of prior literature suggests that customer loyalty is driven by service quality, while another argues that loyalty is driven by partnerships between the firms. However, to date these competing explanations have not been tested together in the ASP context. This empirical study contributes to the literature by unifying these two previously separate streams of research on customer loyalty. Using a survey of 135 ASP clients, we find a significant relationship between the service quality perspective and the partnership perspective. We thus argue that service loyalty models ought to include both of these constructs in order to effectively explain service loyalty.

1. Introduction

Application service providers (ASPs) represent an important evolution of information technology (IT) outsourcing services. The ASP model differs from conventional IT service outsourcing in that services are delivered on demand (Liu, Methapatara, & Wynter, 2010). ASP services can be engaged and disengaged at short notice, thereby allowing customers from a range of industries to achieve capital and infrastructural savings in ownership of their software solutions (Benlian & Hess, 2011; Kern, Kreijger, & Willcocks, 2002). The application services market is hence more diverse and complex than the traditional service market, and firms are struggling to understand how best to manage these differences (Gartner Research, 2009). The contribution of ASP to small, medium and large companies is currently significant and further research into ASPs and the SME market is required (Bayrak, 2013; Demirkan & Cheng, 2008): the ASP market is forecast to reach $69.8 billion by 2015 (Global Industry Analysts, 2011), while the Asia–Pacific region has a projected growth of more than 18% over the period 2011–2015, as the demand for contractual IT services increases.

While this expected growth is a positive outcome for ASP as a business model, a closer look indicates a less than comfortable situation. Application service providers have encountered significant competition in retaining customers and achieving long-term profitability. International financial pressures mean that "clients are deferring project decisions, consolidating their vendor relationships, and starting to renegotiate prices with their existing providers" (Forrester Research, 2008, p. 1). Competition between ASPs is becoming more fierce: recent practitioner literature describes how "vendors will jockey to position themselves as thought leaders, strategic advisors, aggregators and implementers of architected solutions" (Gartner Research, 2011, p. 10). Contractual agreements are typically much shorter in the ASP context (Chang, Yen, Ng, & Chang, 2012; Susarla, Barua, & Whinston, 2009; Yao & Murphy, 2005), so customers need not remain with unsuitable providers. Retaining the loyalty of customers is thus a key challenge facing ASP managers.

The academic explanation for loyalty in the ASP context is not clear. One stream of research has argued that partnership builds trust, which leads to customer loyalty. More specifically, effective commercial partnerships enhance the trust, communication, cooperation, and functionality of the relationships that exist among parties, thus reducing conflict (Anderson & Narus, 1990). For example, Heart (2010) observed a positive relationship between trust and partnership in the SaaS context, while Rustagi, King, and Kirsch (2008) explored the use of control mechanisms to improve trust between partners in outsourcing relationships. Another stream of research has argued that service quality contributes to satisfaction, yielding long-term customer retention and loyalty (Heskett, Sasser,

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& Hart, 1990). For example, Ma, Pearson, and Tadisina (2005) examined how increases in service quality affected satisfaction among current and future ASP clients. Liu, Du, and Tsai (2009) also examined the relationship between service quality and satisfaction and its effects on service portal use.

However, in the context of loyalty, these two streams assume conflicting positions. On one hand, perceptions of service quality depend on explicit activity signals (Bhargava & Sun, 2008; Zeithaml, Parasuraman, & Malhotra, 2002). To improve service quality, managers must carefully assess and evaluate their customer needs (Fan, Kumar, & Whinston, 2009; Väyrynen & Kinnula, 2012). These explicit signals must be well documented, so that both parties have evidence of the other's requirements and behavior (Dabholkar, Shepherd, & Thorpe, 2000; Grönroos, 1984). However, the other stream assumes that loyalty is based on trust, which can exist *without* explicit signals. Reichheld and Schefter (2000, p. 107) state that "to gain the loyalty of customers, you must first gain their trust", Rosanas and Velilla (2003, p. 56) write that "loyalty and trust…represent the two sides of the same coin", and Uys (2008, p. 907) argues, "loyalty requires trust". Harris and Goode (2004) also claim that loyalty depends on trust. However, trust entails "a…level of faith in the intentions of the other party" (Rousseau, Sitkin, Burt, & Camerer, 1998, p. 400), and so formalized indicators and contractual mechanisms of behavior may be ineffective (Granovetter, 2008; Shapiro, 1987; Sitkin & Roth, 1993). Moreover, formal mechanisms "may not only fail to restore trust, but may lead to an escalating spiral of formality and distance that increases distrust" (Sitkin & Roth, 1993, p. 386). For this reason, Rosanas and Velilla (2003, p. 56) argue that "both trust and loyalty…cannot be expressed in the formal rules of an organization that specifies the results to be obtained".

Because one explanation of loyalty depends on trust (positive beliefs in the absence of evidence), and the other depends on explicit requirements (clear signals of service requirements), the two explanations are in conflict. These two perspectives thus need to be tested together in order to better understand this situation. We argue that the current understanding of trust in the outsourcing literature is incomplete: to resolve this incompleteness, we use an explanation from trust theory which posits that interdependent partnership among parties will motivate and build trusting behaviors (Rousseau et al., 1998). We apply the construct of partnership to a model of loyalty in the outsourcing context, using the wider service literature as a basis. We argue that these trust perceptions may not hold in the ASP context, where partners cannot easily monitor each other's behavior. In this case, service partners may lack the positive belief-based evidence that allow them to trust.

The focus of this study is thus to examine the relationships among partnership, service quality, and customer loyalty. Our objective is to unify the partnership-trust and service quality-satisfaction explanations of loyalty. Based on prior attitude-behavior research, we argue that the customer evaluations of the ASP's level of partnership and quality of service would influence their affective states (i.e., trust and customer satisfaction) which, in turn, affect customer loyalty (i.e., behaviors). Nevertheless, we also argue that customer loyalty is more influenced by customer satisfaction than trust. Furthermore, based on the existing literature, we anticipate that partnership would lead to a higher level of service quality perceptions by customers. The results of this study could provide the literature with new insights into how working partnerships and service quality affect customer loyalty (Anderson & Narus, 1990; Delone & McLean, 2003; Grover, Cheon, & Teng, 1996; Lee & Kim, 1999; Sharma & Gupta, 2002). This work also has implications for ASPs that are interested in establishing continuing partnerships. Our results help ASP firms understand how to retain custom-

ers in the highly dynamic application service market, thereby growing their businesses and obtain and maintain competitive advantage in the digital era. We especially contribute to calls for a better understanding of the SME response to ASP services (Altaf & Schuff, 2010; Bayrak, 2013; Jeong & Stylianou, 2010).

2. Theoretical context

Application service providers deliver business-to-business e-commerce services for small- and medium-sized enterprises (SMEs) that cannot otherwise afford to implement expensive and complicated information systems (IS) (Heart & Pliskin, 2002; Smith & Kumar, 2004). ASPs are thus an outsourcing solution for SMEs that offer a leasing arrangement rather than a purchasing decision (Dibbern, Goles, Hirschheim, & Jayatilaka, 2004). However, the use of ASPs differs from typical IT outsourcing in terms of adoption, use and consequences, in particular in relation to SMEs (Smith & Kumar, 2004). The ASP model has been attractive to firms because it appears less risky, with fewer barriers to investment than traditional IS outsourcing (Ekanayaka, Currie, & Seltsikas, 2002). For example, SMEs can switch to different ASPs when their services do not match business needs and expectations (Barthelemy, 2001; Bennett & Timbrell, 2000; Fulford & Love, 2004), and thus retaining customer loyalty is a major challenge faced by ASPs.

The general service literature provides a basis for examining these phenomena. In explaining customer loyalty, the marketing management and IS literatures have emphasized both service marketing (Jiang, Klein, & Carr, 2002; Susarla, Barua, & Whinston, 2003; Zeithaml, 2000) and relationship marketing (Sheth & Parvatiyar, 2002). For the most part, these two streams of studies have developed without much overlap (Berry, 2002; Fullerton, 2005a), even though some of the related studies both focus on the same customer loyalty-related dependent variables (Fullerton, 2005b; Morgan & Hunt, 1994).

One view, principally based in the marketing literature, holds that service quality leads to customer loyalty (Zeithaml, 2000). A number of mechanisms have been proposed to explain this relationship, reflecting the popularity of loyalty as a construct in prior service research (Bloemer, De Ruyter, & Wetzels, 1999; Han, Kwortnik, & Wang, 2008; Jones & Taylor, 2007). For example, higher service quality results in more of the service partner's needs being met in a cost-effective and timely manner. This relationship results in greater satisfaction, and a desire to continue it (Fullerton, 2005b). Higher service quality demonstrates a sensitivity to partner expectations (Brady & Cronin, 2001; Parasuraman & Grewal, 2000), and has been seen as a key factor in prior literature, whereby relational partners develop feelings of commitment (Allen & Meyer, 1990) because they enjoy dealing with the partner on an ongoing basis (Morgan & Hunt, 1994). This enjoyment reinforces satisfaction between partners, and raises the perceived switching costs involved in finding alternative partners (Fullerton, 2003), resulting in greater loyalty. Higher service quality also means that the relationship partners are more likely to accept price increases (Anderson, 1996; Zeithaml, Berry, & Parasuraman, 1996), be willing to act as a reference customer for promotional purposes (Anderson, 1998; Zeithaml et al., 1996), and to spread positive news of the relationship to others by word of mouth (Zeithaml, 2000).

Another view of loyalty is based on the effects of interrelated partnership in the service relationship, and this has largely been examined separately from the service quality perspective discussed above (Fullerton, 2005b). It holds that loyalty is driven by mutual trust between the partners, which, in turn, is motivated