



# An investigation of service quality, customer satisfaction and loyalty in China's airline market



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## ABSTRACT

Customer loyalty is a source of competitive advantage and an important intangible asset to any organisations, but empirical evidence from China's airline market regarding the determinants of passenger satisfaction and loyalty is lacking. This paper investigates the service quality of four major airlines in China's domestic market and explores the links between their service quality and customer satisfaction, as well as the conditions under which airlines can retain existing passengers. In line with previous studies, service quality variables are significant factors influencing customer satisfaction levels. However, satisfactory service was not found to result in higher customer loyalty among business travellers. In comparison to Hainan Airlines, passengers who travelled with Air China, China Southern and China Eastern were more likely to switch to an alternate carrier, indicating lower levels of brand loyalty. In addition, the frequent flyer programs (FFPs) have been largely a failure for the four major airlines in terms of increasing customer loyalty, as revealed in this study. It is necessary to draw distinctions between business and leisure travellers when studying the determinants of customer satisfaction and customer loyalty. Ticket pricing had a positive and significant effect on passengers' overall satisfaction and in turn strengthened customer loyalty among leisure travellers, but achieved no impact on the satisfaction and loyalty of business passengers. Some demographic variables such as gender, income and education are statistically significant for one group of passengers but not for another in the probit models estimated. It is suggested that different marketing strategies may be used to target different market segments to improve customer loyalty.

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## 1. Introduction

China has been the second largest aviation market in the world in terms of the volumes of passengers and air cargo moved in its domestic market since 2007. In 2014 the whole industry handled 392 million passengers and 5.9 million tonnes of air cargo, a 10.7% and 5.9% increase from the previous year, respectively (Civil Aviation Administration of China, 2015). China's airline market is a growing market underpinned by a huge population and rapid economic growth. IATA (2014) forecasts that China will overtake US as the largest air passenger market by around 2030 as measured by traffic to, from and within a country.

However, until the late 1990s most Chinese airlines, which

emerged from the monolithic Chinese government-owned carrier CAAC,<sup>1</sup> had failed to establish brand images and develop favourable reputations among consumers. With more and more foreign airlines flying to China in the 1990s, Chinese consumers had begun to question why the state-owned Chinese airlines could not provide services similar to their foreign counterparts, especially in the events of flight delays and cancellations. As a result, Chinese airlines were forced to make strides in many service aspects since the late 1990s. For example, the introduction of telephone and internet booking services, issuing of guidelines on handling flight delays and cancellation, and the monitoring and regular review of queue times at the check-in counter and boarding gate. Air China was the first

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<sup>1</sup> CAAC (Civil Aviation Administration of China) was an airline operator and a government regulatory body. It now refers to the General Administration of Civil Aviation of China, a government regulatory agency responsible for the oversight and administration of the civil aviation industry.

Chinese carrier that introduced the frequent flyer program (FFP) in 1994 in order to retain customers and differentiate their services from competitors, followed by China Eastern and China Southern in 1998. Other airlines quickly followed suit and almost all the airlines had their FFPs in place in the early 2000s. Despite these efforts, it has been found in a survey conducted in 2006 that Chinese travellers were not significantly influenced by airline brands when making a travel decision (Zhang, 2012).

There have been a series of airline mergers and consolidations since the early 2000s, resulting in four dominant airline groups in China's domestic market, namely, Air China, China Southern Airlines, China Eastern Airlines, and Hainan Airlines. Together they maintained a market share of about 90% in the following decade in terms of the goods and people carried. Chow (2014) claimed that the competitive environment of China's airline industry has changed significantly since the mid-2000s. The domestic airlines compete against each other not only by offering competitive prices, but also service quality aiming to improve customer satisfaction and increase customer loyalty. In fact, high quality customer service has become another significant differentiating factor between an airline and its competitors, especially in a deregulated operating environment. Although much literature has been devoted to air transport service quality and passenger satisfaction, little is known about what makes a passenger loyal (Dolnicar et al., 2011). An excellent work by Vlachos and Lin (2014) examined the determinants of business traveller loyalty towards full-service airlines in China. They found that reputation, in-flight service, FFP, and aircraft type had significant impacts on airline loyalty. However, the factors driving leisure traveller loyalty were not examined by this study. In addition, Vlachos and Lin (2014) argued that there is no consensus in terms of the definition customer loyalty and passenger loyalty in their study was measured with three separate variables: overall satisfaction, recommendation intention, and repurchase intention. Nevertheless, many studies have treated the two as different variables. Although the vast majority the literature suggests a direct, positive relationship between customer satisfaction and customer loyalty (Wang, 2014; Hussain et al., 2015), a key finding in Dolnicar et al. (2011) is that an attempt to improve customers' satisfaction has not proven to have a big impact on loyalty. Chen (2012) noted that past empirical evidence has shown the existence of difference in the strength of the relation between customer satisfaction and loyalty.

This research aims to examine the impacts of service quality, airline brand, and passenger demographics on customer satisfaction. We will also explore the relationship between customer satisfaction and customer loyalty as well as the roles of service quality and demographic variables in explaining customer loyalty in China's airline industry, a topic that has been rarely studied in previous literature as far as we can understand. This study makes two main contributions. First, it adds to the very limited research on China's airline services, customer satisfaction and loyalty, and provides empirical evidence for the relationship between customer satisfaction and customer loyalty in the Chinese context. Lai et al. (2009) pointed out that cultural factors influence the ways in which customers become loyal and thus it is important to assess loyalty formation in different cultures. Second, the findings of this research will not only provide airline management with useful information on how to develop non-price competition strategies to retain customers, but also reveal the highly valued service items appreciated by passengers, which will help airlines in deciding how to allocate their scarce resources. The next section will review relevant literature and briefly describe the profiles of Air China, China Southern, China Eastern and Hainan Airlines whose service quality will be examined in this study. Section 3 will discuss the data collection and methodology. Section 4 presents the results and findings. Section 5 concludes this article.

## 2. Literature review and research background

Quality is one of the key factors influencing a customer's purchasing decisions (Anderson and Zeithaml, 1984). Szwarc (2005) notes that service quality increases customer satisfaction, which enforces customer loyalty and in turn leads to increased corporate profits. Han and Ryu (2009) claimed that tangible physical environment and perceived price are essential elements that determine the level of customer satisfaction, and play a role in enhancing customer loyalty. There has been a growing amount of literature focusing on the relationship between service quality and customer satisfaction and loyalty in the airline industry context including Ostrowski et al. (1993), Curry and Gao (2012), Chen and Hu (2013), and Namukasa (2013), to name a few. However, research in the airline service quality issue within the specific context of China remains sparse and studies on customer satisfaction and loyalty in the second largest aviation market are lacking. The limited studies on China's airline service quality and passenger satisfaction include Zhang (2012), and Chow (2014, 2015). Using stated preference data, Zhang (2012) examined how attributes such as prices, punctuality, schedule delay and the size of network of an airline influenced a passenger's travel decisions on the Shanghai-Guangzhou route. Chow (2014) studied the relationship between customer complaints and the service quality of Chinese carriers. The factor of customer expectation was included by Chow (2015), who found that an improvement in expected on-time performance levels significantly raised passenger complaints.

It is necessary to understand what consumers really want in defining and delivering high-quality service (Zeithaml et al., 1990). Liou et al. (2011) argued that there is no universal definition of service quality, which may take on a different meaning in different industries. The authors pointed out that the concept of service quality is context-dependent and its measurements should reflect the operational circumstances under consideration. Chen and Chang (2005) noted that airlines service is a chain of services in which the entire service delivery can be divided into two stages: ground services and in-flight services. Gourdin (1988) classified airline quality into three aspects: price, safety and timeliness. Ostrowski et al. (1993) considered both ground and in-flight services as well as carrier image. Quite a few studies investigated airline service dimensions that mattered most to passengers including safety, frequency, punctuality, penalty for ticket changes, cabin service and in-flight seat comfortability (Mason, 2001; Gilbert and Wong, 2003; Chen and Chang, 2005; Liou and Tzeng, 2007; Liou et al., 2011; Martin et al., 2011). Airlines that provide better services than their competitors are able to build a solid foundation for customer loyalty (Curry and Gao, 2012).

Satisfaction has been defined as the feeling of pleasure or disappointment when a customer compares a product's perceived performance with his or her prior expectations (Oliver, 1981; Tse and Wilton, 1988). Clearly customer satisfaction is a post-decision experience. Service quality and customer satisfaction are closely related but not interchangeable, although both concepts involve a comparison of expectations of quality and the actual service received. The FFP that was first introduced by American Airlines was a loyalty program with an aim to maintain loyalty among those who travel frequently by rewarding them with free upgrades, free tickets, additional baggage allowances and business lounge access, etc. (Martin et al., 2011). These days the FFP also includes other partners such as banks, hotels and supermarkets. Seelhorst and Liu (2015) found that the FFP membership played a strong role in airline choice, especially for passengers with elite membership. Numerous studies have shown that the quality of pre-flight, in-flight, and post-flight services had a significant effect on customer satisfaction, which as a mediating variable, had a positive effect on

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