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**Bachelor's Thesis:**

**Customer Retention in a Health Club**

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# 1 INTRODUCTION

The health and fitness industry is a growing service industry that requires continued customer patronage to assure its ongoing success. (Hurley 2004) Also in Finland the growth has been fast in the past years. (Suomen Kuntourheiluliitto 2003; Kansallinen Liikuntatutkimus 2005-2006) Many big foreign chains have realized the potential in Finnish market, and many of the biggest clubs in Finland nowadays are in foreign possession. (Arola 2007) A study called The National Exercise Research (Kansallinen Liikuntatutkimus 2005-2006) suggests that the amount of people visiting health clubs regularly in Finland has grown 46 percent between the years 2001 and 2006, being the most growing past time activity. The study was conducted with audience between 19 to 65 years of age.

Besides big health club chains there are also many smaller privately owned health clubs in the scene. An interesting question is how are the small privately owned health clubs managing to stay alive? How can a small health club compete with big chains and stay profitable? One thing certainly is that the company has to keep their acquired customers loyal. To make this possible a company has to have a working customer retention program. (Reichheld and Kenny 1990; Rust and Zahorik 1993)

## 1.1 Research Problem and Objectives

The topic of this study is “Customer Retention in a Health Club -Case Olarium Fitness Club”. The objective is to resolve how a health club can retain their existing customers. Furthermore, it has to be resolved why there is a need for customer retention in general, and what the constructs leading to retention are. In addition, the relationship between customer satisfaction and customer retention is studied and discussed. The research problem for the study is the following:

- What can a health club do to retain their existing customers?

In order to answer the research problem, the following supportive questions have to be answered:

- Why is there a need for customer retention programs?
- What are the elements of customer retention in health club industry?
- How to implement retention theories and build a successful retention program for a health club?

1.2 Theoretical Framework

To understand the development of building a working customer retention program in the health and fitness club industry, we have to understand the constructs that lead to customer retention. There has been little empirical research that investigates these constructs. Others studies have focused, according to Cohen *et al*. (2006), on developing measures of customer value, customer satisfaction and customer loyalty, without specifically looking into other potential important constructs. An exception in this field is a study by Cohen *et al*. (2006), about customer satisfaction and retention in banking industry in New Zealand. The constructs used in the study were competitive advantage, customer satisfaction, switching barriers, corporate image, and bank services characteristics. These constructs can be, with few modifications, used to fit the health and fitness club industry, and they will form the basis of the current investigation.

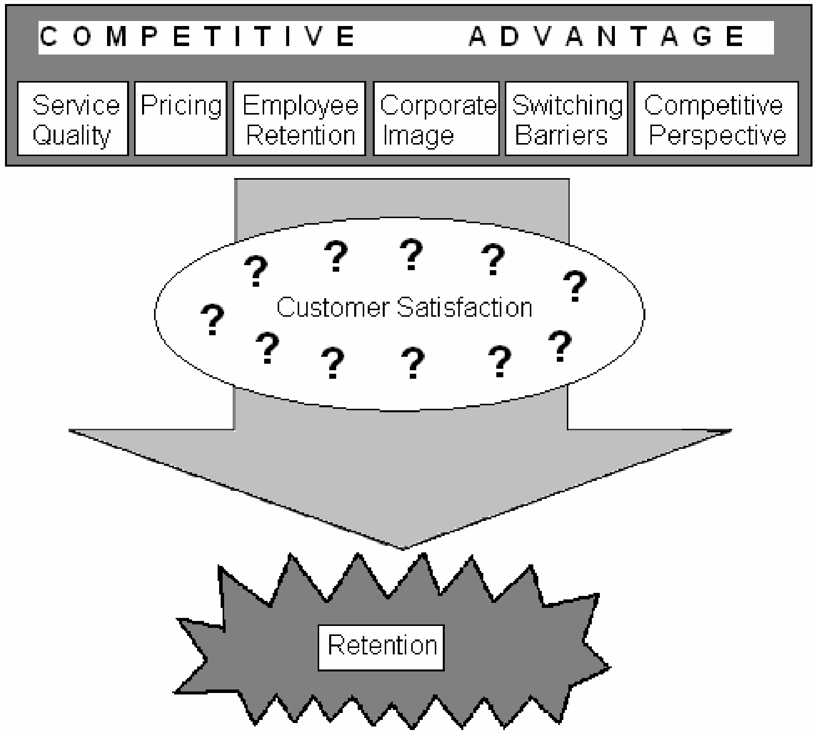


Figure 1. Theoretical Framework of the constructs leading to customer retention (adapted partly from Cohen et al. 2006)

## 1.3 Previous Studies and Literature

There is a limited amount of studies made concerning customer retention in the health and fitness club industry. There are virtually none specifically about the means for a small health club to retain their customers. Many of the studies made in the field of customer retention in the health and fitness club industry do not meet the standards of proper academic study. Still, there are some comprehensive studies made in the area, such as Hurley's (2004) study about the managerial view of health club retention in the Irish Health club industry. Literature about customer retention and loyalty, on the other hand, is plenty. (Barnett et al. 2007; Reichheld and Kenny 1990; Hennig-Thurau and Klee 1997) The importance of customer satisfaction has also been studied comprehensively. Customer satisfaction and prior experiences of service quality have been shown to be key antecedents of customer retention in some literature (Zeithaml et al. 1996; Bolton 1998; Hennig-Thurau and Klee 1997).

## 1.4 Limitations and Structure of Study

The first part of this study presents customer retention, and an explanation of the importance for a small health club to have a working retention program. The second part is limited to explore the elements influencing customer retention in a service industry company. The study covers those areas that are considered to be crucial in the retaining of customers in the health club industry. This work is limited to exclude the segmentation and acquiring of customers, and for the most part the financial aspect related to customer retention. The empirical part examines the existing customer loyalty program of Olarium Fitness club, and the means for further development of the program, based on the customer retention theory and other related literature. Conclusions and recommendations for future research are described in the end of the paper.

## 1.5 Research Method and Definitions

The empirical data for this paper was collected by using qualitative research methods, more precisely an interview. Qualitative research is an integral way to collect data. Furthermore, the information is collected in a natural environment. The primary instrument in qualitative research is the researchers own perception based on collected data. Qualitative research is a good method for resolving the meaning and the context of behavior. Qualitative research brings out the interviewee’s perception about situations, and creates a possibility to observe the factors related to the interviewee’s past and development. (Hirsjärvi and Hurme 2001, 27) The interview questions were designed to reciprocate the theory of customer loyalty, and are presented in appendix 1. The interview was conducted in Olarium Fitness Club, and the person interviewed is the General Manager of Olarium Fitness Club, Katri Kylmälä.

Important definitions:

**Customer retention/loyalty** = Loyal customers are those who hold favorable attitudes toward an organization, recommend the organization to other consumers and exhibit repurchase behavior (Dimitriades 2006).

**Customer satisfaction** = Customer's cognitive and affective evaluation based on the personal experience across all service episodes within the relationship (Storbacka et al. 1994).

**A loyalty program** = A marketing program that is designed to build customer loyalty by providing incentives to profitable customers (Yi and Jeon 2003).

**Competitive advantage** = Adding value by differentiation while increasing margins through higher prices. (Cohen et al. 2006)

**Perceived service quality** = Customer's cognitive evaluation of the service across episodes, compared with some explicit or implicit comparison standard (Storbacka et al. 1994).

**Switching barriers** = Factors that make it difficult or costly for consumers to change providers/ Measure of the extent to which the customer has to remain in a relationship. (Julander and Söderlund 2003)

## 2 CUSTOMER RETENTION

Customer retention is a part of Customer Relationship Management, or CRM. According to Payne (2006, 4), CRM is a business approach that seeks to create and develop relationships with carefully targeted customers in order to improve customer value and corporate profitability and thereby maximize shareholder value. Hennig-Thurau and Hansen (2000) argue that relationship marketing has become one of the most prosperous branches of marketing theory in recent times, as well as one of the most important management issues for the business community.

The argument for customer retention is relatively straightforward; it is more economical to keep existing customers than to acquire new ones. According to some studies, acquiring new customers is calculated as being five times more costly than the expenses of retaining existing customers. The costs of obtaining customers to replace those who have been lost are high, because the expense of acquiring customers is incurred only in the beginning stages of the commercial relationship. (Reichheld and Kenny 1990; Hurley 2004) In addition, long term customers buy more, and if satisfied, may generate positive word-of-mouth promotion for the company. Finally, long term customers take less of the company's time, and are less sensitive to price changes (Healy 1999).

Although many companies recognize the value and importance of customer retention in general, relatively few understand the economics of retention in their own business. (Kotler 2003, 73; Payne 2006, 143) Companies can clearly benefit from increasing the lifetime spending of customers. Most companies, however, concentrate a significant amount of resources on attracting and acquiring new customers, instead of keeping the existing ones. It is generally thought that once a customer is acquired, keeping the customer is simple through superior products and services. (Payne 2006, 2)

In the literature the concepts customer retention and customer loyalty are usually treated as the same. However, in their study of customer satisfaction in New Zealand, Cohen *et al*. (2006) argue that there is a difference between these concepts. Consumer inertia implies that some customers are only being retained, rather than expressing loyalty. Truly loyal customers are described as being less price-sensitive and more inclined to increase the number of purchases.

Moreover, satisfaction with a company's services also plays a role in generating loyalty that might be absent in the retention situation. Customer loyalty is therefore not the same as customer retention, as loyalty is distinct from simple repurchase behavior. Loyalty is considered to be only a valid concept in situations where customers can choose other providers. (Cohen et al. 2006) In this study, loyalty and retention are both treated as synonyms for a strong feeling of support and allegiance from the customer's side towards an organization.

## 2.1 Customer Satisfaction

Customer satisfaction is originated from a comparison between customer's expectations and experiences. Customer satisfaction means positive reaction to a service experience. If the customer's perceived experience matches the expectations, the customer is assumed to be satisfied. If the preceding expectations were higher than the gain of the service, the customer is considered to be disappointed and dissatisfied. (Ylikoski 2000, 109) At a theoretical level, satisfaction is a concept that has many definitions which tend to differ from each other. In the most recent definitions, there is recognition of a dual nature of satisfaction. In other words, a cognitive and an affective character, as well as a relative nature are found to exist. (Anton et al. 2007) In this study it is considered that satisfaction is achieved when consumer's expectations about the performance of the service are met or exceeded.

Customer satisfaction and prior experiences of service quality have been shown to be the key antecedents of customer retention. (Bolton 1998; Rust and Zahorik 1993; Zeithaml et al. 1996) Satisfaction has been treated as the main element for customer retention in numerous publications, and has therefore moved to the forefront of relational marketing approaches. (Rust and Zahorik 1993) Consequently, customer satisfaction has developed extensively as a basic concept for monitoring and controlling activities in the area of relationship marketing. Customer satisfaction has traditionally been regarded as a fundamental determinant of long term consumer behavior. The more satisfied customers are the greater is their retention. (Anderson and Sullivan 1993) On the other hand, there are studies and publications where the relationship between satisfaction and retention has been noted not to be this straightforward. (Hennig-Thurau and Klee 1997) In some industries, customer satisfaction scores tend to correlate with retention. In other industries there is little or no correlation. (Lowenstein 1995, 11-12)

## 2.2 The Ambiguous Relationship between Satisfaction and Retention

Kotler (2003, 73) states that companies should measure satisfaction regularly, because the key to customer retention is customer satisfaction. Highly satisfied customers stay loyal longer, buy more from the company, talk favorably, pay less attention to competing brands, are less sensitive to price, offer ideas to the company, and cost less to serve than new customers, because transactions are routine. Customers will be lost if they are very dissatisfied, dissatisfied, or even indifferent. Thus, companies have to regularly survey their customers' level of satisfaction and aim to create very satisfied customers, because they are most likely to stay loyal to the company. According to Bolton (1998), the level of satisfaction explains a significant portion of explained variance in the duration of service provider – customer relationship, comparable to the effect of price. In addition, Bolton states it to be a common misconception that organizations which focus on satisfaction are failing to manage customer retention. Furthermore, managers and researchers may have underestimated the importance between customer satisfaction and retention, because of the complexity of the relationship between these factors.

In a study by Ranaweera and Prabhu (2003), it is argued that while satisfaction may be an important driver for retention, it alone does not ensure service loyalty. Trust, switching barriers, and emotional response such as inertia and indifference are also likely to influence retention. In their study Ranaweera and Prabhu (2003) adopted a holistic approach to examine the combined effects of satisfaction, trust, and switching barriers in a continuous purchasing setting. The empirical study was based on a postal survey of telephone users in the United Kingdom. The findings implied that customer satisfaction and trust have strong positive effects on customer retention, although the effect of trust on retention is weaker than that of satisfaction. Results also indicated that switching barriers have a significant effect on customer retention. According to the study, it is clear that satisfaction is the main driver of retention as a direct determinant. However, if trust is absent, satisfaction will have less impact on retention.

## 2.3 Arguments for Negative Correlation between Satisfaction and Retention

The linkage between satisfaction and customer retention is not always as simple and straightforward as stated earlier. In an article by Reichheld *et al*. (2000), a concept called “the satisfaction trap” is represented: “while it may seem intuitive that increasing customer satisfaction will increase retention and therefore profits, the facts are contrary. Between 60 percent and 80 percent of customers who defect say they were satisfied or very satisfied with their former supplier. In the auto industry, satisfaction scores average 85 percent to 95 percent, while repurchase rates average 40 percent.” According to Storbacka *et al*. (1994), customer satisfaction is only one dimension in increasing relationship strength. Strong relationships can be dependent or perceived of contextual bonds that function as exit barriers. It is vital to understand that contextual barriers can generate latent dissatisfaction which emerges as the importance of the contextual bonds decreases. The article concludes arguing that the relationship varies significantly between different individual consumers. Others may be very committed to the relationship and for them the perceived satisfaction with the relationship is very important. Others may find the relationship unimportant, and for these customers the satisfaction component is not as significant.

In an article by Hennig-Thurau and Klee (1997), it is argued that satisfaction with a company’s products or services is often seen as the key to a company’s success and long term competitiveness. However, the few empirical investigations in this area indicate that a direct relationship between these constructs is weak or even nonexistent. The link between satisfaction and the long term retention of customers is typically generated by marketing practitioners and scholars in a rather categorical way, and is therefore treated as the starting point, rather than the core question of the analysis.

The potential intervening variables in the relationship quality– retention relation can be grouped into intra psychological, contextual, and situational factors, with the latter ones being specific intra psychological or contextual factors that only have a temporary impact in one particular buying situation. One major variable among the intra-psychological variables is the customer’s predisposition to variety seeking which can play an important role in repeat-purchase behavior. The customer’s need for diversity with a product or service may then evoke brand switching behavior despite a perception of high quality. (Hennig-Thurau and Klee 1997)

The second category, contextual factors, encompasses a variety of different factors, such as the social context. In consumer markets it is the influence of parents, colleagues, or spouses that can impose buying norms on the consumer which override the individual decision based on the quality appraisal. A situation may occur, when the buyer’s and the decider’s individual decisions are contradictory, and the latter’s higher formal status plays the deciding role in making the final decision. Finally, situational variables can also erode customer retention. Examples of these potentially relevant factors are time pressure, temporary budget restrictions, exceptional shopping situations like vacations, or lack of availability of the desired product or service. These and other situational variables may also lead to the purchase of a product or service other than the one that ranks highest in terms of quality perception. (Hennig-Thurau and Klee 1997)

Mattila (2004) has studied the impact of service failures on customer loyalty. More specifically, she studied the moderating role of affective commitment on post-failure attitudes and loyalty intentions under two service failure conditions: a successful and poor service recovery. The findings imply that even dissatisfied customers can be retained at some occasions. Customers with high affective commitment tend to have low levels of tolerance for service failures. Hence, service organizations might develop customized service recovery strategies for this group of consumers. Employees need to be trained to take customer problems as their own, and to get personally involved in the recovery process. The goal is to exploit the personal connection between the customer and the service provider. According to Mattila, the majority of customers are dissatisfied with companies' service recovery efforts. Still, service organizations are left with little guidance of how to deal with these customers.

Condensing the results from these studies, skepticism seems to be well founded as to the widespread conceptual view of a strong satisfaction–retention relationship. Different authors have different opinions about the matter, and different kinds of results have been reached based on empirical studies. The relationship between satisfaction and retention, in many instances, is moderated by other factors. The strength of the relationship can be lower or higher, given the influence of other variables. Specifically, the relationship between satisfaction and loyalty has been found to be moderated by personal characteristics, such as demographics.

## 2.4 Satisfaction Measurement

Companies tend to think they are receiving reliable information about customer satisfaction by tallying customer complaints. However, about 96 percent of customers who are dissatisfied do not complain. (Kotler 2003, 73; Lowenstein 1995, 16) Hence, from the company's perspective it would be recommended to make it easy for the customer to complain. This could be accomplished by using suggestion forms, toll-free numbers, and e-mail addresses. (Kotler 2003, 73) Customer satisfaction surveys do not always give reliable answers about the state of satisfaction. There are examples from the car industry, where some companies got high satisfaction scores by calling their customers immediately after they have bought the car. In these cases the customer feedback is often ignored as the main purpose is just to get high customer satisfaction scores. (Reichheld et al. 2000)

However, there are occasions when, even with the right intentions, the scores of customer satisfaction surveys do not reflect reality. Satisfaction surveys in general are not always considered as a good way to measure satisfaction. Researches has shown, as stated before in this article, that 60 - 80 percent of customers who defect from a company say that they were satisfied or very satisfied. Some companies have responded to this problem by refining their measures for satisfaction. Still, only 45 percent of their customers return when more than 90 percent say they are satisfied. (Reichheld et al. 2000) Lowenstein (1995, 23-30) proposes six failures and five cures for customer service performance measurement. The six failures are measurement programs that:

1. Follow rather than lead customers
2. Consider only registered complaints and ignore latent ones
3. Measure only global attributes, not operational elements
4. Ignore customer expectations
5. Ignore customer-provider gaps
6. Have a measurement goal of satisfaction, not loyalty or attrition

According to Lowenstein (1995, 30-33), the way to have a more effective customer service performance measurement system is closely related with pro-activity. The five suggested cures for customer service performance measurement are:

1. Gather latent and registered complaints
2. Identify and measure critical incidents and transactions
3. Include customer expectations
4. Pay attention to customer-provider gaps
5. Develop models for customer retention

# 3 COMPETITIVE ADVANTAGE

A firm's relative position within its industry determines whether a firm's profitability is above or below the industry average. The basis of above average profitability in the long run is sustainable competitive advantage. There are two basic types of competitive advantage that a firm can have; low cost or differentiation. The two basic types of competitive advantage, combined with the activities for which a firm seeks to achieve them, lead to three generic strategies for achieving above average performance in an industry. These are cost leadership, differentiation, and focus. The focus strategy has two variants, cost focus and differentiation focus. (Porter 1985, 11-15)

1. *Cost leadership*. In cost leadership a firm sets out to become the low cost producer in its industry. The sources of cost advantage are varied and depend on the structure of the industry.
2. *Differentiation*. In a differentiation strategy a firm seeks to be unique in its industry along with dimensions that are widely valued by buyers. It selects attributes that many buyers in an industry perceive as important and positions itself to meet those needs. It is often rewarded for its uniqueness with a premium price.
3. *Focus*. The generic strategy of focus rests on the choice of a narrow competitive scope within an industry. The focuser selects a segment or a group of segments in the industry and tailors its strategy to serving them to the exclusion of others.
    *a.* *Cost focus*. In cost focus a firm seeks a cost advantage in its target segment.
    *b.* *Differentiation focus*. In a differentiation focus a firm seeks differentiation in its target segment.

No company can be good at everything. Companies have limited funds and they have the problem of concentrating them. Choosing to be good at one thing can cause the company to be less good at some other thing. Companies need to go beyond broad positioning to express more concrete reasons to buy. A concept called a single major benefit positioning is suggested by many companies. It could be formed from the following: (Kotler 1999, 55-57)

- Best quality
- Best performance
- Most reliable
- Most durable
- Safest
- Fastest
- Best value for money
- Least expensive
- Most prestigious
- Easiest to use
- Most convenient

According to Kotler (1999, 58), companies must avoid certain errors when positioning themselves. The first error is under-positioning, which means failing to present a strong central benefit for customers to use the companies services. The second error is over-positioning; adopting such a narrow positioning that some potential customers may overlook the image. The third error, confused positioning, means claiming many benefits that contradict each other. The fourth error is irrelevant positioning, which means claiming a benefit that only few prospects care about. The final error is doubtful positioning, which means claiming a benefit that people will doubt the company can actually deliver.

## 3.1 Loyalty Programs

A loyalty program is a marketing program that is designed to build customer loyalty by providing incentives to profitable customers. A loyalty program is often based on propositions as the following: (Yi and Jeon 2003)

- Customers may want more involving relationship with products or service that they purchase.
- A proportion of these customers show a tendency to be loyal
- They are a profitable group
- It is possible to reinforce these customers' loyalty through a loyalty program.

Wendlandt and Schrader (2007) interpret loyalty programs as combinations of bonding potentials. A customer that offers personal contact to other members, and a price discount, represents a mixture of socio-psychological and economic bonds. According to Storbacka *et al*. (1994), there are all together ten different types of bonds between the customer and the provider. There are legal bonds, economical bonds, technological bonds, geographical bonds, time bonds, knowledge bonds, social bonds, cultural bonds, ideological bonds, and psychological bonds. The first five bonds are argued to constitute effective exit barriers for consumers. They can be seen as contextual factors that cannot easily be influenced by customers but can be managed by the service provider. These five bonds can also prevent, to some extent, the customers from switching even if they are dissatisfied with the service. The other five bonds are difficult to measure and manage by the firm. These bonds can result in the customer accepting a lower level of service and not switch to the competitor, even with the prospect of getting better service elsewhere.

Wendlandt and Schrader (2007) argue that loyalty programs like customer cards can arouse psychological reactance. Moreover, companies should use these elements with caution and check the acceptance of the program before the implementation. The level of reactance is influenced by the disposition of customers towards reactance in general and the importance of autonomous buying behavior. This suggests that some customers can be convinced to participate more easily than others. Reactance against loyalty programs can lead to a number of negative consequences from the company's perspective; it has the potential to reduce the willingness to participate in the program, it can enhance negative word-of-mouth, and it can even decrease the repurchase intention.

## 3.2 Service Quality

Berry and Parasuraman (1991, 5) define service quality as the foundation for services marketing, because the core product being marketed is a performance. Moreover, the performance is the product, and it is what customers buy. Hence, companies can gain from strong service concepts giving them the opportunity to compete for customers. A strong performance of the service concept builds competitiveness by earning customers' confidence and reinforcing branding, selling, and pricing. According to studies, reliability seems to be the foremost criterion customers consider in evaluating a company's quality of service. Five general dimensions that influence customers' assessment of service quality are suggested in the literature. From these, reliability has repeatedly emerged as the most crucial. The dimensions are: (Berry and Parasuraman 1991, 16)

- *Reliability*. The ability to perform the promised service dependably and accurately.
- *Tangibles*. The appearance of physical facilities, equipment, personnel and communications materials.

- *Responsiveness*. The willingness to help customers and to provide prompt service.
- *Assurance*. The knowledge and courtesy of employees and their ability to convey trust and confidence.
- *Empathy*. The provision of caring, individualized attention to customers.

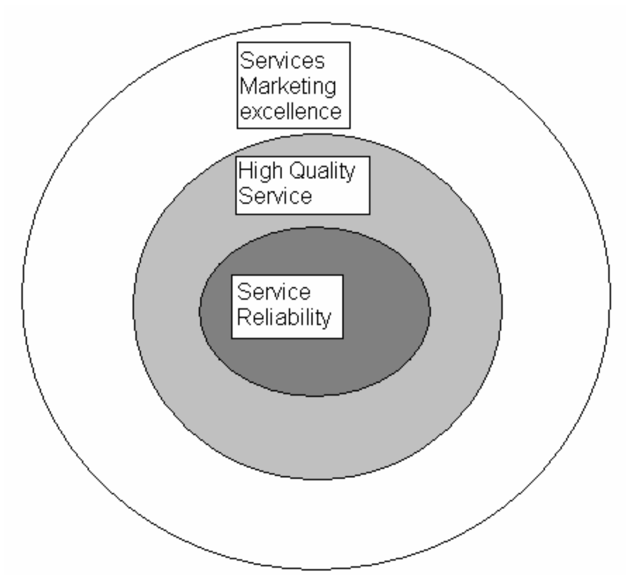


Figure 2. The Foundation for Services Marketing Excellence (Berry and Parasuraman 1991, 17)

According to Ranaweera and Neely (2003), service quality is an important driver of customer retention. However, service quality does not seem to be the only concern of the customer. High service quality, at the expense of a reasonable price, also appeared to be unacceptable for the more price sensitive segments of customers. Where the perception of price is low and there is potential for improving service quality, improvements in service quality can lead to a significant increase in the retention rate. However, if negative price perception is associated with high service quality perception, service quality alone will be inadequate to retain customers.

## 3.3 Pricing

Price is an important marketing tool. (Lowenstein 1995, 81; Kotler 2003, 471; Gupta and Lehmann 2006, 122) When setting the price policy, companies must follow a six-step procedure. First, they select their pricing objectives. Second, they estimate the demand curve. Third, they estimate how costs vary at different levels of output, at different levels of accumulated production experience, and for differentiated marketing offers. Fourth, they examine competitors' costs, prices, and offers. Fifth, they select the final price. (Kotler 2003, 499) Different methods of pricing products and services are: (Ylikoski 2000, 263-264; Kotler 2003, 481-485)

- *Markup Pricing*. The most elementary way of pricing is to add a standard markup to the costs.
- *Going-Rate Pricing*. The firm bases its prices largely on competitor's prices. The company might charge the less, same, or more than the main competitors.
- *Perceived Value Pricing*. An increasing number of companies base their price on the customer's perceived value. This is not the easiest way to price services, since the value of the service can differ with different individuals. The price, using this method, should be the consequence of the benefits for the customer, such as for example timely and psychological costs.

Furthermore, there are additional factors that the company should consider, before selecting the final price: (Marketing Teacher ltd)

- *Psychological Pricing*. This approach is used when the marketer wants the consumer to respond on an emotional, rather than rational basis.
- *Product/Service Line Pricing*. Where there is a range of product or services, the pricing reflect the benefits of parts of the range.
- *Bundle Pricing*. Sellers combine several services in the same package.
- *Promotional Pricing*. Pricing to promote a service is a very common application.

- *Value Pricing*. This approach is used where external factors such as recession or increased competition force companies to provide “value” products and services to retain sales.

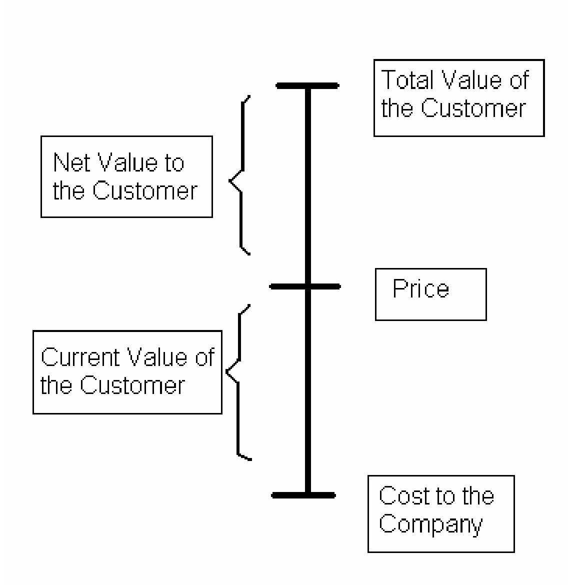


Figure 3. The impact of price on value and value of the customer (Gupta and Lehmann 2006, 124)

Figure 4 describes how lower prices provide higher value to the customer, but decrease the value of the customer to the firm. Optimal pricing involves a delicate balance between the two sides of customer value. (Gupta and Lehmann 2006, 124)

## 3.4 Employee Retention

For most industries high employee turnover can damage factors such as quality and customer service. The financial cost of defecting staff can be high. The cost of recruiting new staff can be up to 50 percent higher than the annual salary of key staff. In addition to financial costs there is the loss of skills, knowledge, experience, and the investment in training. (Curtis and Wright 2001) Organizations are increasingly recognizing the significant value their employees contribute to the business. Employees are instrumental in implementing customer service policy, improving process efficiencies, and nurturing customer confidence. Employees provide the mechanism for promoting customer satisfaction, improving productivity, assuring quality control, and reducing costs. (Payne 2006, 373-374) According to Mullen (2007), staff retention is crucial for establishing customer loyalty. The challenge of building customer loyalty through staff excellence, according to Mullen, is in hiring upper level staffers with sufficient emotional intelligence.

The relationship between customer retention and employee loyalty works in both directions. Satisfied employees mean satisfied customers, and according to Reichheld and Kenny (1990), satisfied customers can in turn mean satisfied employees. It is easier for employees to deal with customers who are pleased than it is with those who are dissatisfied. The ability to retain employees for longer periods of time confers multiple benefits. Hiring costs, value of training, and development investments are proportional to employee longevity. Also long term employees are more likely to form bonds with customers, which can lead to additional customer retention.

## 3.5 Corporate Image

Today's consumers have more choices for their needs than ever before. Technology, globalization, increased competition, and increased consumer mobility have dramatically changed the way people think (Harwood, 2002). Bharadwaj *et al*. (1993) argue that services are highly intangible, and therefore are high in experience and credence qualities. As a consequence, brand reputation or corporate image is important as a potential competitive advantage. Corporate image constructs, according to Andreassen (1999), from four items. The items are opinion of the company, company's profile, perception of the company being customer oriented, and company related word of mouth. These items were derived at after a pretest among 400 respondents concerning banking and charter services, and applied in a study. According to Dowling (1988), corporate image is a construct similar to the construct of self-concept in psychology. Both terms refer to a set of thoughts and feelings having reference to an object.

A Norwegian Customer Satisfaction Barometer confirmed the importance of corporate image on customer satisfaction. A positive correlation between corporate image and customer satisfaction was found in all of the investigated industries, and customer satisfaction was positively correlated with customer loyalty in eight industries. Interestingly, in the service industry a positive correlation existed between corporate image and customer loyalty. Moreover, corporate image plays an active role in the formation of customer loyalty among existing customers. In the case of dissatisfaction with services, a good corporate image may function as moderator on future intent, and thus reduce incentives to exit from the market or change patronage. (Andreassen 1999)

## 3.6 Switching Barriers

Switching barriers have been used as marketing strategies to make it costly for customers to switch to another organization and create “customer lock-in” (Bonanni et al. 1998). In their article Storbacka *et al*. (1994) represent reasons for a customer to stay loyal to a company. They claim that even dissatisfied customers can be retained through switching barriers. Establishing a new relationship represents some sort of investment or effort, for example time and/or money, which constitute a barrier for the customer against taking action when dissatisfied. According to Fornell (1992), switching barriers include search costs, transaction costs, learning costs, loyal customer discounts and emotional costs. These barriers provide disincentives for the customer to leave the current organization. According to Ranaweera and Prabhu (2003), switching barriers have both a significant positive effect on customer retention, as well as a moderating effect on the relationship between satisfaction and retention. While service providers may be able to retain even dissatisfied customers who perceive high switching barriers, firms should aim at a combined strategy that makes switching barriers act as a complement to satisfaction.

Julander and Söderlund (2003) suggest a distinction between negative and positive switching barriers. The results show that these two variables have different effects on repurchase intentions. These two types of switching barriers also have different effects on customer satisfaction. An example of positive switching barriers is a customer maintaining a relationship with a company because of a perception that the supplier is superior in services and products. Examples of negative switching barriers are expensiveness for a customer to leave the supplier, or a monopoly on the market.

## 3.7 Competition

Most good marketing plans have a detailed section on competitive activity. Companies of any size can learn from the competition and plan accordingly. (Lowenstein 1995, 73) There are basically four ways a company can get closer to customers and position its delivery strategy relative to competition: (Ries and Trout 1986; Kotler 2003, 255-260)

1. *Defense*. Companies with market dominance should defend against competitors. They can create market entry barriers, create exclusive distribution contracts, or use patent protection.
2. *Offence*. Companies that are strong but not market leaders can mount offensive approaches designed to challenge the market leader. Companies can use intensive advertising or try to develop new superior services. It can also try to wear the competition down by imitating the competitor's services and products, or by expanding the market niches that surround the target competitor's market. An offensive strategy aims at getting the other company's customers to become your own.
3. *Flanking*. A surprise move which requires both competitive information and customer need determination and market insight to identify segments or niches where opportunity exists. Flanking involves competing in a market segment that the competitor does not consider critical, using subtle advertising campaigns and other discrete promotional measures.
4. *Guerrilla warfare*. The development of many tactical advantages that especially small companies can use to keep constant pressure on competitors. A company can do targeted legal attacks on the competition by using product comparison advertising, executive raiding, short term alliances, selective price cuts, or orchestrating negative publicity for a competitor.

According to Kotler (2003, 274), if a company aims to prepare an effective marketing strategy, it must study its competitors as well as its customers. Companies need to identify competitors' strategies, objectives, strengths, weaknesses and reaction patterns, and collect competitive intelligence intensively. In addition, companies need to know how to prepare an affective competitive intelligence system. A company should pay attention to latent competitors, who may offer new ways to satisfy customers' needs. As a conclusion Kotler states that as important as a competitive orientation is in today's markets, companies should not overdo the emphasis on competitors, but maintain a good balance of consumer and competitor monitoring.

# 4 EMPIRICAL RESEARCH

As mentioned earlier, the empirical data for this study was collected using qualitative research in the form of an interview. In qualitative research there are no formal rules or methods concerning the form of conclusions for a study. Still, the analysis, interpretation, and the argumentation of a material should be conducted with great care. The procedure should be based on research objectives and theory. (Alasuutari et al. 2005, 229–233) An interview is a flexible research method which can be used for many purposes. Moreover, an interview makes it possible to maneuver the acquiring of information into specific direction, and also makes it possible to establish a better overall comprehension about the answers, due to non-verbal elements. Also, the motives behind the answers are easier to notice. (Hirsjärvi and Hurme 2001, 34)

The interview in this study was designed to be a half-structured "theme-interview". The concept was designed by Hirsjärvi and Hurme (2001, 47), and the basic idea is that the interview advances in pre-determined themes.  The main advantage of this interview type is that it brings out the interviewee's perception of matters. This study also aims at developing suggestions for Olarium Fitness Club to strengthen and improve their customer retention. In that sense this study is considered to be a normative study.

## 4.1 Olarium Fitness Club

Olarium Fitness Club was established about 12 years ago. It has been known throughout its existence as a youthful gym, and a place for hard training. In December 2005 Olarium Fitness Club experienced a change of ownership. The new owner was a family of six from Espoo. The eldest daughter, Katri Kylmälä, had been working at the club for five years as an aerobics and gym instructor, when the possibility of becoming the new manager for Olarium Fitness Club came to her knowledge. She immediately expressed her interest, and that is how the present day Olarium Fitness Club became to exist. (Kylmälä 2007; Olarium Fitness Club)

## 4.2 Results of the Interview

Katri Kylmälä became the General Manager of Olarium Fitness Club in December 2005. Besides working as a manager, she is also working on a master's degree in Sport and Health Sciences. Her work in Olarium Fitness Club involves administrating tasks and human resource management; paying the salaries, recruiting new personnel and training the new personnel. In addition, she is working as an instructor and a personal trainer.

According to Kylmälä, Olarium has always had a reputation as being youthful and inexpensive club, and a place for an intensive work out. Service quality is considered very important by Kylmälä. Because Olarium Fitness Club is a small business compared to many competitors, it is challenging for it to be competitive in for example the amount of room space or the number of services. Thus, service quality becomes very important. Competitive advantage is being created by concentrating on top quality, professional health club business, with the emphasis on not requiring long term bonds. In addition, flexibility plays an important role in the business; individual customer needs are taken into consideration as much as possible when required by customers' life situation.

Moreover, competitive advantage is being created by trying to make it easy for the customer to enter the club. Customers are not being startled from the beginning by trying to force them to sign long term contracts. In fact, Olarium does not offer 12 month contracts at all. Still, the club wants to maintain a variety of other membership card possibilities; there is a card for 10 visits, for one month, for three months, and for six months. The card for 10 visits is valid for three months, and there is a possibility, if the customer prefers so, to temporarily freeze the three and six-month cards.

An article by Barnett-White *et al*. (2007) introduces a concept called “Customer’s Future Usage Uncertainty”, or FUU. The results of the article offer insights into how service organizations can manage their customer retention activities more effectively. According to the text, FUU is a common state in many companies in the health club business. The text suggests that marketers can increase customer retention by influencing the way consumers frame the repurchase decision. Consumers seem to act in accordance with a prospect theory, with increases in FUU decreasing repurchase intent. Moreover, firms can reduce customer perceptions of downside risk by focusing on customer flexibility to defer the drop decision. By highlighting the customer’s ability to leave, marketers may actually convince customers to stay.

This is, in a way, the case in Olarium Fitness Club. In today’s Health club business the concentration seems to be in retaining customers as intensively as possible right from the beginning. Many clubs have a “joining fee” policy which is a fee that one has to pay right away before he/she can decide the length of the contract. Olarium Fitness Club has a different approach on the matter. It wants to appeal to those customers who are uncertain of the period of time they are willing to be financially retained to a health club. This way of gaining competitive advantage is according to the differentiation strategy introduced in the theoretical part. In the differentiation strategy, the firm seeks to be unique in its industry. In some cases, the company is rewarded for its uniqueness with a premium price. However, this is not the aim for Olarium Fitness Club. In the health and fitness club industry the competition is hard, and in Olarium Fitness Club’s case the barriers for switching are not significant. Thus, it would be hard for the company to be competitive using high prices.

Olarium Fitness Club prices its services mainly according to the prices the previous owner had. In general, Olarium is very competitive with its prices. For example, one visit to the club costs seven euro's, six for students and unemployed. A big rival chain asks 20 euro's for the same, 15 euro's, if you visit together with a club member. According to the pricing strategy the long term contracts are cheaper than short term contracts. A normal three month card costs 120 euro's (80 euro's per month) as a card for six months costs 215 euro's (35, 8 euro's per month). In contrast, many rival chains use a strategy where every month costs the same no matter how long the contract is.

Unger (2004) suggests that success in retaining customers often follows from building a customer database that identifies and characterizes loyal customers and collects their individual attributes and needs. Also using this information to segment customers based on high, medium and low value, is important. In addition, Unger states that loyalty programs should include elements that focus on recognizing and retaining high value customers, growing medium value customers, and either growing or disengaging low value customers.

Olarium Fitness Club has sold, according to Kylmälä, over 2 500 member cards so far. The problem is that just a fraction of these customers are constant visitors. Olarium has a database of its customers' names, birthdays, addresses, phone numbers, e-mail addresses (optional), and the visiting histories to the club. When asked about how the club keeps contact with the customers, Kylmälä states that contact is being kept mainly by replying to feedback and questions. People nowadays are not eager to provide e-mail addresses for commercial purposes Thus, it difficult to target retention efforts through direct marketing. Customer satisfaction in Olarium has been measured with a survey once so far in. Kylmälä says that the customer feedback is mainly conducted through the Internet, and that she often personally reads the feedback and acts accordingly. In many cases customers also give verbal feedback for people working at the counter. According to Kylmälä, besides the internet, Olarium Fitness Club does not use any other specific forms for gathering customer feedback. However, Kylmälä often personally talks with the customers and gathers data and opinions that way.

As an answer to a question about employee retaining, Kylmälä ensures that the working climate in Olarium is good, and the wages are competitive. Also, there are bonuses for a well done work, and the management aims at being flexible when it comes to working schedules etc. Furthermore, the turnover of employees is being considered average. The only problem the club has experienced regarding staffing, according to Kylmälä, was finding and retaining the appropriate cleaning staff that could keep up with the expected level of work. Nowadays the club has outsourced the cleaning of the gym.

The family orientation is strongly present in the atmosphere of Olarium Fitness Club. New acquisitions, renovations and redecorations are made continuously; the gym and the equipment are being kept clean at all times, and just recently the club invested 20 000 euro's in general improvements. The previous owner of the club had some legal issues which might have had a negative effect on the company's image. The objective is to change that image in the eyes of the customer. Moreover, Olarium Fitness Club wants to signal that the company is trustworthy, and it does not operate the same way as it might have done with the previous owner. This is attempted to accomplish by showing that the owners care deeply about the club and the customers.

As for recreational activities, Olarium hosts an annual Christmas party for its members. Also on some other occasions there are different kinds of events and discounts aimed for the members. The club tries to maintain a pace of hosting one event every autumn and spring. Some of the programs during these events include discounts for massages and solariums, product offerings, and different kinds of activities for children. According to Kylmälä, these events are too time taking and wearisome to organize more than a few times a year.

In general, Olarium Fitness Club tries to differentiate its profile from its competitors. It tries to create an image of a cozy "second living room", where everybody is welcomed warmly as themselves. According to Kylmälä, Olarium does not have a specific loyalty program strategy. The idea is to promote longer time memberships when possible, but over extensive promotion could hurt the image the club wants to signal. Kylmälä thinks the development of customer retention is very important, although it is hard while trying to maintain the image of a place where customers specifically do not feel obligated to form lifelong memberships. As a conclusion, Kylmälä states that the club is doing well at the time. The customer base and the net revenue has grown steadily throughout the couple of years that Kylmälä has been managing the company. This is good news for the company, especially considering the fact that last year the club invested only 300 euro's on its marketing.

# 5 CONCLUSIONS AND RECOMMENDATIONS

The conclusions of this study will be made in the next chapters. First, the major findings will be summarized from the theoretical and empirical part. Furthermore, some points will be given out that might help the developing of customer retention in Olarium Fitness Club. Finally, there will be some recommendations for further research.

## 5.1 Summary of Major Findings

Customer retention has been gaining a lot of popularity in Customer Relationship Marketing in the past years. Many companies have realized the economical advantage of keeping existing customers against acquiring new ones. Customer satisfaction has been traditionally seen as the antecedent for customer retention. However, when studying thoroughly what has been written about the relationship between the factors, it becomes quite hard to come up with a specific opinion on the matter. It seems that both positive and negative opinions about the correlation between the factors arise throughout the period of which the subject has been studied. Moreover, it seems that the opinions on the matter are depended on the way the researchers have studied the matter. Still, if one would have to take a stand based on the literature, one would probably lean towards the assumption that customer satisfaction has an asymmetric effect on retention. Although loyal consumers are most typically satisfied, satisfaction does not universally translate into loyalty.

The competition is hard in today's health club business. Consumers have lots of different options from which to choose from when choosing a place to train.

Furthermore, lots of health clubs offer same kind of programs and services, and differentiation in the industry is hard. Especially small companies face this when doing business because customers today are demanding and quite aware of different offerings.

Olarium Fitness Club has decided to aim at creating an image of a warm, family oriented health club, with reasonable prices and good service quality. The General Manager of Olarium Fitness Club wants to emphasize that the club does not force customers into long term memberships. Olarium Fitness Club seems to be doing well at the time, but systematically upgrading the customer retention strategy could further enhance the company's competitive abilities. This should be done with care and by using discreet methods, so that Olarium Fitness Club's image does not suffer. However, when discussing the means for Olarium Fitness Club to enhance their customer retention, one has to remember that Olarium Fitness Club is a relatively small company.  Hence, the club cannot necessarily implement extensive retention programs or strategies without wearing down a substantial proportion of its financial, mental, and/or timely capital in the process.

## 5.2 Managerial Implications

Olarium Fitness Club wants to differentiate itself by not emphasizing on long term memberships. In practice, this means not offering 12 month membership cards. On the other hand, it could be argued that adding the 12 month membership to the club's offerings could interest the active members of the club, and create additional stability and financial insurance for the club, without necessarily startling the potential customers away. At least, Olarium could conduct a survey inquiring people's opinions on the matter. Also, Olarium should constantly survey customers to maintain understanding of the level of satisfaction, and the need for further development of the business. In addition, the company should try to develop means for evaluating the satisfaction-retention ratio. This could enlighten the extent the company needs to please the customers.

Customer comments, complaints, and questions provide critical information needed to anticipate areas of potential dissatisfaction. Olarium Fitness Club should try to emphasize on making it as easy as possible for the customer to provide feedback. Customer feedback forms at the main counter could be used to encourage people to give suggestions and comments. Even though the feedback is not always constructive and useful, it is still argued to be generally better to get feedback as much as possible than not to get it at all. Also, problems should be seen as opportunities, and this way of thinking should be also understood by the employees. However, the company should be prepared to respond to the feedback, because the quickest way to disengage any customer is to ask for input and then ignore it. Used correctly, however, customer input can be used to develop customer retention in the club.

It would be useful for Olarium Fitness Club to try to identify the specific customers that it wants to retain. Furthermore, understanding what types of services customers value, and determine what incentive motivational programs will work best with those customers is also important. Building a customer database that identifies and characterizes loyal customers, and collects their individual attributes and needs, could help the company tremendously in developing their retention strategy. This information could be then used to segment customers based on high, medium, and lower value. This could lead to increased efficiency and better understanding of the customer type desired to retain.

Using the mail, telephone or e-mail to keep in contact with the customer has proven to be effective when retaining customers. Remembering customers’ birthdays and other important days creates warm feelings towards a company. On the other hand, there seems to be resistance from the customer’s side towards providing their e-mail addresses. Therefore, effort to build trust should be made by the staff for getting customers to agree on receiving ongoing marketing and special offers. This could be established by giving customers incentives to allow their purchases to be tracked.

In general, Olarium should try to keep in touch with their customers as much as they can. The club should seek opportunities for keeping customers informed of their fine service, make them aware of new products and services, and offer information to help them get more for their money. Many companies invest heavily in market research, but they often overlook critical listening points. Customers should be interviewed both at the time of arrival, when they become customers, and at the time they defect. Non attending members are less likely to renew memberships, so companies should be curious about the reasons for defection. Contacting departing customers and listening to them earnestly, could recapture a significant percentage of departing customers. Tracking non attending members and initiating reactivation programs could decrease customer defection thus increasing the profits for the club.

Customer service is often seen as the key competitive advantage in the future. Thus, Olarium Fitness Club should try to develop a unique relationship with the customers, and treat each one as someone special. The more customization the club is able to build into customer relationships the better. The company should try to increase the number of points of contact with the customer, and encourage social interaction between employees and customers. Also, the company should aim at developing other relational norms such as commitment, trust and support, open communication, adaptability, shared responsibility for conflict resolution, cooperation, and solidarity among participants. These factors can increase psychological loyalty towards the organization and enhance retention. Management and employees can contribute greatly to the improvement of customer service elements. As a result of properly executed customer service policy, greater distribution of guest invitations, referral incentives, and customer referrals may follow, thereby increasing the lifetime and financial value of loyal members.

In addition to preceding retaining suggestions, Olarium Fitness Club should remember that members visit health clubs for social reasons as much as to exercise. According to studies, as much as 90 percent of people prefer to exercise in groups than by themselves. Moreover, someone who works out with a friend is 50 percent more likely to stay with their exercise program than someone who exercises on their own. The first 60 days are crucial in making people feel like a part of a group and form social bonds. The introduction of training partners, group induction programs, and social activities are efficient ways to encourage people to meet each other and form bonds. There should always be emphasis on providing more social activities, discounts, and seasonal offers since these are great ways to create additional value for the company, and enhance retention. In general, Olarium Fitness Club should go the extra mile for the customers and show them just how dedicated they are to making sure that they feel good about doing business with them.

## 5.3 Suggestions for Further Research

There is not much academic research about the means for a health club to retain customers. The competition in the health and fitness club industry is hard, and customer retaining has already, according to many studies, proved its importance in today's business life. For many clubs, especially the smaller ones, the information on how to efficiently retain customers would be of greatest importance. These companies need the information to stay in business, and more academic research should indeed be conducted in this field. The relationship between customer satisfaction and retention, on the other hand, has been a target of many studies. Still, the relationship is quite ambiguous, and more research on the matter should be conducted. In particular, the effect satisfaction has on retention in a health club industry should be examined thoroughly, since many health clubs measure their customer retention by satisfaction polls assuming there is a strong correlation between the factors.

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*Interviews*

Kylmälä, Katri (2007), General Manager, Olarium Fitness Club, Espoo, Finland, November 20, 2007.

Appendix 1. The Interview

1. *Taustatiedot*

- *Nimi?*
- *Ikä?*
- *Asema yrityksessä?*
- *Koulutus?*

2. *Nykyinen työ*

- *Milloin aloititte työssänne?*
- *Millainen on työkuvanne?(työn sisältö ja tehtävät)*

3. *Olarium Fitness Club*

- *Millainen on Olarium Fitness Clubin historia?*
- *Millainen on Olarium Fitness Clubin toiminta-ajatus?*

4. *Asiakastietokanta*

- *Pidättekö asiakastietokantaa? Millaista tietoa se pitää sisällään?*

5. *Asiakastyytyväisyys*

- *Millä tavoin mittaatte asiakastyytyväisyyttä?*
- *Millä tavalla asiakaspalautteen antaminen on järjestetty?*
- *Otatteko yhteyttä asiakkaisiin, jotka eivät ole käyneet yrityksessänne tiettyyn aikaan? Yritättekö selvittää syyn käymättömyyteen?*

6. *Kilpailuetu*

- *Millä tavoin Olarium Fitness Club pyrkii saavuttamaan kilpailuetua?*
- *Millaisena pidätte palvelun laadun asemaa liiketoiminnassanne?*
- *Minkälainen on hinnoittelustrategianne?*
- *Millä tavoin pyritte sitouttamaan henkilökuntanne?*
- *Kuinka suuri vaihtuvuus teillä on henkilökunnan suhteen?*
- *Kuinka usein ja miten pidätte huolta yleisistä tiloista ja laitteista?*

- *Millaisen yrityskuvan/imagon Olarium Fitness Club pyrkii viestittämään asiakkailleen?*
- *Millä tavoin suhtaudutte kilpailijoihin?*

*7. Sitouttaminen*

- *Minkälainen on nykyinen sitouttamisohjelmanne?*
- *Millaisia alennuskampanjoita pidätte?*
- *Millaisia sosiaalisia tapahtumia pidätte?*
- *Kuinka tärkeänä pidätte asiakassitouttamisen kehittämistä kuntosalialalla?*
- *Millä tavoin pyritte itse kehittämään sitouttamista yrityksessänne?*