A NEGLECTED STRATEGY OF PARTIAL SERVICE TERMINATION AND ITS IMPACT ON CUSTOMERS' PATRONAGE

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Abstract:

This research introduces the strategy of *partial service termination* (PST) and its consequences on customers' patronage. PST is a company's strategy where the company decides to stop providing a service while maintaining the relationship with the customer; it represents an in-between strategy between other investigated strategies, like service demotion and service termination. Using longitudinal and archival data from 26,464 clients of a large French insurance company, from 2014 to 2019, results show that PST exerts a negative effect on customers' patronage. Build on justice theory, we explain that customers tend to restore justice after a PST by terminating their other contracts with the company, in the vein of "an eye of an eye and a tooth for a tooth." Moreover, we find relationship length to play a protective effect here, as customers reduce less their patronage after a PST as their relationship is longer.

Keywords: partial service termination; unprofitable customer management; patronage reduction.

Track: Relationship marketing

1. Introduction

While customers' decisions to stop a relationship is well-documented in the marketing literature (e.g. Morgeson et al., 2020; Van Vaerenbergh et al., 2019), research about companies' decision to devaluate or stop their relationships with their customers is scarcer (Haenlein et al., 2006). However, unprofitable customers are a prevalent phenomenon and most firms use some demarketing strategies to avoid losing much money on this significant proportion of customers (Haenlein and Kaplan, 2012 ; Mittal and Sarkees, 2006). In the banking sector, unprofitable customers account for up to 50% of total customers (Ang and Taylor, 2005). Academic literature investigates two main strategies for companies in order to deal with these unprofitable customers: relationship termination when companies decide to completely stop doing business with their customers (Haenlein and Kaplan, 2012), and relationship demotion when the company devalue the service (i.e., higher price, lower value) without ending the relationship (Haenel et al., 2019). However, empirical evidence suggests an in-between situation where companies stop providing a service without ending the relationship. For instance, an insurance company might decide to stop insuring a customer for her/his car without stopping her/his other insurances; in this case, the company stops providing a service (the car insurance) but the relationship with the customer continues (because s/he still has some other insurance contracts); a phenomenon that we entitled as *Partial Service Termination* (PST) and defined as a situation when an existing service contract with a customer is abandoned by a service provider but the customer still provided the service on other contracts. However, marketing literature is unable to provide some insights to managers about the potential detrimental consequences of such actions.

Here, justice theory informs that customers usually retaliate from companies' negative actions (Grégoire et al., 2018). In regards to unprofitable customer management (UCM) strategies, previous research informs that customers usually bad-mouthed against companies that stop the entire relationship with them (Nazifi 2021), in the vein of "an eye of an eye and a tooth for a tooth." However, there is no research investigating customers' reactions to a smoother strategy like PST. Indeed, when companies apply for PST, they expect the customers' relationship to continue. However, in line with the aforementioned justice theory, there is high risks that customers might interpret this company's strategy as unfair and decide to completely end the relationship on their own. Precisely, the purpose of this research is to investigate customers' patronage after a PST.

To do so, we use longitudinal archival data from 26,464 clients of a major French insurance company, on a five years period (2014-2019). By doing so, this research provides two main contributions to the literature. First of all, our results show that PST negatively impacts the future of the relationship, as we find that customers who experienced a PST reduce more their patronage in comparison to a control group of customers who did not experience any demarketing strategy. Second of all, we examine the moderating role of relationship length (Jap and Anderson, 2007). Previous research informs that this variable plays an important role on customers' reactions to negative events (e.g., Béal et al., 2019; Khamitov et al., 2020) but it has been surprisingly under-investigated in the case of UCM. Here, our results show that customers with long-term relationship are less sensitive to PST, and long relationship acts as a "safety cushion" because it slows customers' patronage reduction after a PST.

2. Theoretical framework

Relationship marketing management is based on the philosophy that companies build relationship with profitable customers. The twin of this logic is that firms must apply UCM strategies and dismiss unprofitable customers. The literature usually names this phenomenon as "customer demarketing" (Bradley and Blythe, 2014), "customer abandonment" (Haenlein, Kaplan and Schoder, 2006), or "customer divestment" (Haenel et al., 2019 ; Mittal and Sarkees, 2006), all referring to UCM strategies (Feng et al., 2020), meaning firm-initiated actions with respect to customers who provide insufficient value to the firm (Haenlein et al., 2006 ; Mittal et al., 2008). Indeed, a substantial proportion of most firms' customers are unprofitable, creating a significant performance drag (Mittal and Sarkees, 2006). As a result, it has been argued that firms should selectively "demarket" to or even "fire" such unprofitable customers (Lepthien et al., 2017).

Today's literature on UCM strategies considers two main strategies: direct and indirect UCM. In a *direct UCM strategy*, the firm takes specific actions to openly terminate its relationship with targeted low value customers without giving them an option to stay (Mittal and Sarkees, 2006), a strategy also called service termination (Haenlein and Kaplan, 2012). Customers often get even of firms adopting such strategy, by spreading negative word-of-mouth as a way to restore justice (Haenel et al. in press, Lepthien et al., 2017). In contrast, firms using *an indirect UCM strategy* seek to improve low value customers' profitability or to divest them without sending explicit termination messages to affected customers or by providing them with options to continue the relationship (Haenlein et al., 2006). Examples of indirect UCM strategies could be a price increase for the same service or lower benefits on a service. Problem is that this strategy also generates negative outcomes such as customer revenge (Haenel et al., 2019), boycott and exit (Haelein and Kaplan, 2011). Generally, Nazifi and his colleagues (2021) show that UCM strategies lead to negative words or mouth and patronage reduction.

Our research investigates an in-between UCM strategy that has been largely ignored by previous research: PST. PST can be classified as both *direct* and *indirect UCM strategies* as it refers to a situation where the company is somehow ending a part of the relationship with the client (by stopping providing one or several contracts), though it maintains the relationship with one or several other contracts. Thus, companies might decide to stop providing some services to some customers because they are not profitable on this specific service, though they consider the relationship to be sufficiently valuable to not fire the customers entirely. Put it differently, we assume that managers adopt PST when they consider a direct UCM strategy to be too extreme because the overall relationship is still sufficiently profitable to maintain. However, we hypothesize that such approach will also exhibit negative reactions from customers with detrimental consequences on the future of the relationship. Precisely, previous research argues that customers usually restore justice by destroying the company's reputation with negative word-of-mouth. In the case of PST, customers still have other contracts and we hypothesize that they will reciprocate and restore justice after PST, by ending their other contracts and bringing their businesses to competitors. Hence, we assume that customers are more prone to reduce their patronage after a PST:

H1: *PST has a positive impact on patronage reduction, in the sense that customers reduce more their patronage after a PST.*

This research also explores the moderating role of relationship length, meaning the duration in years of a firm-customer relationship (Verhoef et al., 2001). Relationship variables play a significant role on customers' reactions to negative events (Khamitov et al., 2020) and especially relationship length. The effects of relationship variables on customers' reactions are quite unpredictable as some studies demonstrate that these variables often protect the firm while some others tend to demonstrate the opposite. In regards to relationship length, there are several signs that tend to confirm for a protective effect. On the one hand, a recent study shows that long-term customers tend to react more positively after a poor company's actions like a dissatisfying service recovery (Béal et al., 2019). Moreover, other studies show that relationship length is often associated to inertia behaviors, in the sense that long-term customers are less reactive and have lower ability to adjust their behaviors due to inertia (Chintagunta, 1998). Accordingly, in this research, we hypothesize that relationship length should protect the firm from the negative consequences associated to PST. We believe that long-term relationships are characterized by habits and inertia, which makes these customers less reactive to PST, in terms of their ability to reduce their patronage:

H2: *Relationship length negatively moderates the positive effect of PST on patronage reduction, in such a way that the effect of PST on patronage reduction is stronger (vs. weaker) as the relationship is getting shorter (vs. longer).*

3. Method and results

Database from a large insurance company, which operates on the French market, is used to test our hypotheses. The data comes from a prospect/customer repository connected to all the company's sales tools, that gives an overview of the purchasing behavior of customers. It allows to obtain very rich information at the individual level, whether it is socio-demographic determinants or business activity (contracts subscribed and terminated). As a result, this database provides indicators to understand the purchase pattern of customers, and more precisely to monitor the evolution of the number of insurance contracts held. Historical customers' data are available from 2014 to 2019, what we call the reference period. After cleaning the database, we compare two samples: a sample of customers who have experienced a PST and a randomly selected sample of customers who did not experience any such incident[1].

Both sample contains 13,232 observations, which represents a final sample of 26,464 customers (28% female; M_{Age} = 43,14 years old, SD = 12,91). The average relationship length with the insurer is 4 years and 9 months. For purchases, the mean contract at the beginning of the observation period (2014 to 2019) was of 2 contracts and of 0.85 contracts at the end of the period. We characterize as a purchase reduction for customers whom the number of contracts at the end of the observation period is lower than the number of contracts at the beginning of the observation period. Overall, during the observation period, 39,26% customers reduce their

[1] We have reweighted control group in order to have similar distribution for main variables. Margin calibration methods are commonly used to weight data: they perform the calculation of weight for each observation in order to respect known variable distributions. We have used Icarius package, available for R software, developed by the French National Institute for Statistics and Economic Analysis (INSEE). Three variables have been used (age, gender and length of the relation).

patronage and 60,76% customers increase their patronage or have the same number of contracts at the end of the reference period.

First, Table 1 shows that during the reference period, customers who have experienced a PST are more likely to close remaining contracts than clients from the control group. More precisely, if 46.32% of customers who experience a PST chose to reduce their purchases in the reference period, this proportion dropped to 32.23% in the control group ($p < .001$). Second, we hypothesis that this effect is moderated by the length of the relationship. That means the length of the relationship at the beginning of the reference period could play an important role in the client decision to reduce its purchases.

However, the real impact of each factor – and their evolution over time – on the probability to reduce purchases can only be accurately evaluated on an "all other things being equal" basis, by means of econometric models. Using disaggregate data, we estimate multivariate models in order to explore the possible determinants of this behaviour. In our analysis, the dependent variable is a dichotomous variable, indicating whether the customer has reduced its purchases or not during the reference period. The econometric model is estimated on the pooled sample and a dichotomous variable allows to identify customers who have experienced PST from the other. Interaction term between the length of the relationship and this dichotomous variable is introduced in the model, to determine whether the impact of PST on the likelihood of reducing purchases is moderated by relationship length. More specifically, for customers who have experienced a PST, if the associated interaction term with relationship length is not statistically significant, this means that the effect of this variable on purchase reduction remained constant between both samples (with and without PST). If the interaction term is statistically significant and of the same sign as the main effect of the dichotomous PST variable, then it could be concluded that relationship length has increased this effect. Conversely, if the interaction term was significant but of opposite sign to the dichotomous PST variable, then it could be concluded that relationship length decreased the impact of PST on patronage reduction.

We first estimate a logistic regression, which explains the probability for a customer to reduce its purchases between 2014 and 2019:

$$PR_i = \begin{cases} 1 & if\ PR_i^* = X_i\alpha + u_i > 0 \\ 0 & \text{otherwise} \end{cases}, \quad (1)$$

where PR_i is the binary variable indicating if the customer i has reduced its purchases, PR_i^* a latent variable, X_i the vector of covariates, including interaction term, and u_i a random term error following a logistic regression. The coefficients α associated with covariates are estimated by maximizing the following likelihood:

$$L(\alpha|X_i) = \prod_{i=1}^{N} \left[\frac{\exp(X_i\alpha)}{1+\exp(X_i\alpha)}\right]^{PR_i} \cdot \left[1 - \frac{\exp(X_i\alpha)}{1+\exp(X_i\alpha)}\right]^{(1-PR_i)}, \quad (2)$$

Table 2 presents the detailed results of the logistic regression. Results show that experiencing a PST significantly increases the probability of reducing purchases, compared to customers who haven't experienced any such event (b = 1.74, p < .001), which is consistent with the logic exposed in H1. Moreover, we also find a significant interaction effect between experiencing a PST and relationship length, in the sense that the longer the relationship (in months) is, the less consumers are likely to reduce their purchases (b = –6.55e-04, p < .001), consistent with H2.

Above all, the factor that seems most likely to explain the probability of patronage reduction is PST. Indeed, for customers who experience a PST, the likelihood of reducing purchases is in average 11 percentage points higher than in the control group, with other equivalent characteristics[2]. However, the impact of PST on patronage reduction is moderated by relationship strength in such a way that the higher the relationship strength is, the less consumer will reduce its purchases (the coefficient of the variable "length of the relationship" is negative for customers who experience a PST: -3.54e-04). Finally, the coefficients associated with the socio-demographic variables, gender and age, are not significant. There is therefore no effect of gender or age on the probability of reducing purchases.

4. Discussion and implications

This research provides two core contributions to theory and practice. First, we contribute to the marketing literature on demarketing and UCM strategies (e.g. Feng et al., 2020 ; Haenel et al., 2019) by empirically investigating a new phenomenon called PST and its implications on customer-firm relationship. To date, UCM literature focusses only on extreme strategies where the company either directly entirely end the relationship (i.e., service termination) nor indirectly devalue one service (i.e., service demotion). The PST strategy represents an in-between alternative situation in which the company stops providing one service to the clients although their relationships continue because they had multiple services from this provider. We assume that companies adopt such approach because customers might be

[2] This figure corresponds to the marginal effect of the variable "Partial service termination", calculated at the average point from the logistic regression.

unprofitable in regards to one service but their overall relationships might be too much valued for applying an extreme strategy like service termination. Thus, companies adopt PST because they expect relationships with these customers to continue without some unprofitable specific services. Built upon the justice theory (Grégoire et al., 2018), we use longitudinal archival data to demonstrate that this strategy pertains some negative consequences, as customers who experienced a PST tend to reduce their patronage in the months and years that follow. This result is consistent with past research on the effect of demarking strategies on customers' negative reactions (Haenel et al., 2019 ; Nazifi et al., 2021), although this research is the first to show this effect using archival data. In that sense, PST exert a backfire effect on company profitability. Thus, managers who deal with unprofitable customers have to consider the fact to use a PST strategy when they want to "get ride" of unprofitable clients. Indeed, if the company retains some contracts because they expect to keep these customers who remain profitable on other contracts, there are risks that the clients themselves cut down the remaining contracts and progressively end the relationship.

Second, this research demonstrates the role of relationship length on the link between PST and patronage reduction. Relationship variables like relationship length, plays a major role in customers' reactions to negative events (see Béal et al., 2019; Khamitov et al., 2020), although their role is ignored for negative events like UCM strategies. Findings highlight that relationship length moderates the effect of PST on patronage reduction in such a way that the longer the relationship between the company and the client, the lower s/he reduces her/his purchases with the company after the PST. Overall, this result shows that relationship length tends to protect firms from the negative consequences associated with PST and we recommend managers to apply such strategy on long-term unprofitable customers because they will be less prone to close their other contracts compared to short-term customers.

5. Limitations and research avenues

This research presents several limitations and avenues for further research. First, we investigate the insurance sector, a decision based on the strong presence of UCM strategies in this sector. However, it might limit the external validity of our findings. If our results should be similar in other closed sectors, such as the banking sector, further research should replicate our findings in other sectors such as telecommunications. Second, further research could compare PST with other UCM strategies, such as service termination or demotion, to compare their effects on patronage reduction. Third, this research only investigates the consequences of PST on behaviors; however, it would be interested to investigate the psychological mechanisms at stake, in order to better understand what drives customers to leave after a PST. Finally, as PST has a detrimental effect on consumers' responses, further research could investigate which recovery tactics would be the most efficient to appease the negative effect of PST.

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Appendix

Table 1. Descriptive statistics

	Customers with partial service termination	Customers with no partial service termination
Observations	13 232	13 232
% ind. with patronage reduction	46,32%	32,23%
% ind. without patronage reduction	53,68%	67,77%
Women	28,03%	28,03%
Men	71,97%	71,97%
Average age in 2014 (years)	43,14 (SD = 12,91)	43,14 (SD = 12,91)
Average length of the relation (years)	4,76	4,76

Table 2. Logistic regression

	Coefficients	P-values
Intercept	-1.65	<0,001***
Gender_male	-2.36e-02	0.412
Age	-5.79e-04	0.533
Partial service termination (PST)_yes	1.74	<0,001***
Lenght of the relationship	3.01e-04	<0,001***
Initial number of contracts	1.70e-01	<0,001***
PST_yes* Lenght of the relationship	-6.55e-04	<0,001***