

Why Not Switch? Switching Costs and Switching Likelihood

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ABSTRACT

Although many bank customers report being unhappy with their current bank, few take the step of actually changing to a new bank. This is referred to as customer inertia, and is recognised as an issue in banking. The standard explanation for this low rate of churn, i.e. customers switching between banks, focuses on switching costs, comprising all the financial and non-financial factors that discourage customers from changing banks. This is an important issue for banks in markets with a relatively low proportion of unbanked in the population, such as New Zealand, for whom the main source of new customers must therefore be existing customers of other banks.

This paper reports findings in respect of the effect of switching costs on the relationship between a person's desire to switch banks and the likelihood that they will actually do so. This is part of a broader study completed recently that sought to provide better understanding of switching costs in banking. A mail survey was distributed to 2983 people whose names were drawn at random from the New Zealand electoral roll, with a final response rate of 34% being achieved.

We find that switching costs overall reduce the correlation between desire to switch and the likelihood of switching. Nine categories of switching costs were used in the study and the same result is found in respect of seven of the nine categories. This supports the argument that switching costs discourage customers from changing banks.

INTRODUCTION

While the numbers of customers claiming to dislike their bank¹ is substantial, the level of churn² is relatively low. For example, Sheeran (2003) reported research from the University of Auckland that had shown over a number of years that while 15-20% of residential customers thought of changing banks, only 3-5% actually moved. So if customers are unhappy with their bank, why do they not change to another bank?

The usual explanation for this low churn rate centres around switching costs, a term used to encompass all the factors that can discourage customers from changing banks, including both financial costs and non-financial factors. The inclusion of non-financial issues, such as finding a new bank and the customer's relationship with the existing bank's staff, is critical. The importance of switching costs lies in their impact on the operation of the market, and they are blamed for allocative inefficiency, monopolistic profits and barriers to entry, among other things. These problems arise because switching costs affect customer behaviour, with customers becoming locked in to a particular bank and therefore unwilling to switch to a different bank. Acknowledgement of the existence of switching costs in banking leads to consequent arguments about the need for regulatory intervention to overcome the switching costs and improve competition.

Many customers express a desire to switch to a new bank; for example, a survey by the University of Auckland in 2005 (reported in Steeman, 2005) found 20% of customers were likely or very likely to switch banks, although one author noted such intentions were not usually acted upon due to switching costs. The situation is similar in other countries. Fujitsu Australia found 80% of respondents in a study of 26,000 customers expressed a willingness to change their financial services provider (Rogers, 2007), while a recent US survey found 10% of respondents "were very dissatisfied and said they would switch their financial institution if it were easier to do so" ("Customers prefer their local branch", 2004, p. 7).

This desire to switch does not translate into comparable rates of switching, and low churn rates are the norm in New Zealand. About 180,000 New Zealanders change their financial institution each year, representing about 4.4% of the total population (Carlisle & De Freitas,

¹ In this paper the term 'bank' is used in its more generic sense to incorporate all financial institutions with which one may have a banking relationship. Where reference is intended to the narrower sense of registered banks, being the only entities in New Zealand entitled to refer to themselves as a bank, the term 'registered bank' will be used.

² Churn refers to the rate of turnover of customers moving from one financial institution to another.

2004). More recent data from Roy Morgan for the six months to December 2007 showed that 7.8% of those aged 14 years and older had switched banks in the previous twelve months , (Rogers, 2008). Despite media reports at the time of the closure of the last bank branch in two Northland town that *many* customers intended to change banks, only 13% did so (Matthews, 2000). Similar results are found in other countries (see for example, Wood, 2002; Cruickshank, 2000; Carrick, 2006).

This reluctance to switch despite dissatisfaction with the current banking relationship is known as customer inertia, and has some benefits for the banks. The main banks in Australia have “relied on the reluctance of customers to move” (James, 2005, p. 69) and it is alleged that customers are easily retained. Planned fee increases by St George Bank in Australia could be expected to generate customer complaints, but not cause customers to actually change their bank, according to Rogers (2006).

The low rate of churn in the New Zealand retail banking market is not due to a lack of alternatives. As at 31st May 2008, there were 17 registered banks³ in the New Zealand market, with six dominating the retail banking market: ANZ National Bank Limited (ANZ National), ASB Bank Limited (ASB), Bank of New Zealand (BNZ), Kiwibank Limited (Kiwibank), TSB Bank Limited (TSB) and Westpac New Zealand Limited (Westpac NZ). Two of these banks operate dual brands under the same registration: ANZ National operates the two distinct and major brands of ANZ and The National Bank (National); while ASB operates a major brand under that name as well as the minor internet-only brand of BankDirect. There are also two smaller, retail banking oriented registered banks: Kookmin Bank (Kookmin) focusses on meeting the needs of expatriate Koreans living in New Zealand; and, Rabobank New Zealand Limited (Rabobank NZ) which currently limits its offerings to deposit products. There are also non-bank financial institutions operating. The two most significant are Southland Building Society (SBS) and PSIS, both of which are mutual, co-operative organisations and substantially smaller than the banks. Other small financial institutions in the New Zealand retail banking market include other building societies and a number of credit unions⁴ offering products and services across the range of retail banking

³ The full list of currently registered banks is available on the website of the Reserve Bank of New Zealand at <http://www.rbnz.govt.nz/nzbanks/0091622.html>

⁴ Both the building society and credit union sectors are currently going through a period of rationalisation, with consequent reductions in the number of institutions in each sector from time to time. As at 1st February 2008 there were nine building societies (including SBS), 33 credit unions under the umbrella of New Zealand Credit Unions representing about 85% of credit union members in New Zealand, and about 10 other credit unions.

products, as well as financial institutions focussed on the retail lending market, such as finance companies primarily interested in the consumer/personal lending sector, and mortgage lenders primarily providing housing finance.

A recent study looked at switching costs in the New Zealand banking market. This paper reports on part of that study, relating to the effect of switching costs on the relationship between the desire to change banks and the likelihood of actually doing so. The next section considers prior research on switching costs, and is followed by a section that outlines the methodology of the study. The fourth section reports the results, and the final section concludes.

PRIOR RESEARCH

Switching costs have become more recognised and been the subject of substantial work in the last 20 years or so, although earlier related work exists. Nevertheless there is no accepted standard definition of what switching costs are. A useful definition of switching costs as “the onetime costs that customers associate with the process of switching from one provider to another” was used by Burnham, Frels, & Mahajan (2003) p. 110. They also made the useful points that switching costs “need not be incurred immediately upon switching” (p. 110), nor that they are limited to objective or economic costs. This last point is important because the use of the word ‘costs’ immediately creates a perception of a dollar amount.

Another view is offered by Jones, Mothersbaugh, & Beatty (2002) who suggested “switching costs can be thought of as barriers that hold customers in service relationships” (p. 441). In a similar vein switching costs are “a hurdle separating incumbent suppliers ... from would-be suppliers” according to Shapiro & Varian (1999, p. 159), who noted firms benefit from their own customers’ switching costs while having to find ways to overcome the switching costs of competitors’ customers. These two definitions are useful for incorporating the effect of switching costs, for customers and for markets.

In simple terms, switching costs in banking represent the range of costs bank customers face if they wish to transfer their banking relationship, in part or in full, from one financial institution to another. As this description makes clear, switching costs is a plural term encompassing a range of individual costs, but to date no real consensus has been reached on

the best categorisation to use. Determining an appropriate categorisation of switching costs is helped by understanding how switching costs arise. Chen & Hitt (2002) noted that factors from which switching costs can arise include “the general nature of the product, the characteristics of the customers that firms attract, or deliberate strategies and investments by product and service providers” (p. 256). Kim, Kliger and Vale (2001) suggested a variety of economic and psychological reasons for switching costs to arise, and other possible causes include information (Gabrielsen & Vagstad, 2003, and Evans & Wurster, 1997) and the customer’s investment in relationship specific assets (Sengupta, Krapfel, & Pusateri (1997)).

Klemperer (1995) described four different types of switching costs: Physical investment, in equipment or a relationship; Information investment, in the use of a product or its characteristics; Artificial investment, created by loyalty schemes; and Psychological investment, preference created by use and experience. In earlier work, Guiltinan's (1989) typology used four classes of switching costs: contractual costs, set-up costs, psychological commitment costs and continuity costs, while Fornell's (1992) switching barriers included “search costs, transaction costs, learning costs, loyal customer discounts, customer habit, emotional cost, and cognitive effort, coupled with financial, social and psychological risks on the part of the buyer” (p.10).

Burnham et al. (2003) used a more extensive, and arguably more complete, list of eight switching costs, comprising: Economic risk costs, the potential for a negative outcome; Evaluation costs, associated with the search for and analysis of alternatives; Learning costs, gaining the knowledge to be able to use the new product/service; Set-up costs, initiating the relationship; Benefit loss costs, including discounts and other rewards for ‘loyalty’; Monetary loss costs, initial financial outlays; Personal relationship loss costs, breaking the bonds of interaction; and Brand relationship loss costs, breaking bonds of identification with brand or company. They consolidated this list of eight costs into three higher order types of: ‘Procedural switching costs’ representing the expenditure of time and effort; ‘Financial switching costs’ representing the loss of financially quantifiable resources; and ‘Relational switching costs’ representing psychological and emotional discomfort.

The Cruickshank Report on the UK banking market is one of the few places that specifically identifies the hassle of switching, and it explains that “switching accounts can be tiresome and time consuming, not helped by the larger banks’ reluctance to develop technical solutions to the problem” (Cruickshank, 2000, p. 18). Other authors have recognised this issue, but have

incorporated the actual process of changing supplier within their other categories, rather than keeping it as a separate category. The approach of the Cruickshank report appears more appropriate as the hassle of changing is frequently mentioned by customers when discussing the possibility of changing banks.

Switching costs are argued to be greater for services than goods (Gremler and Brown (1996) in de Ruyter & Wetzels, 1998), suggesting they are more important in a service industry such as banking. There is general agreement that switching costs play a particularly substantial role in banking, and as a result, there is a body of literature that explores switching costs specifically in the banking industry. In 1998, the UK government instigated a review of banking in the UK and the resultant report provided support for the existence and influence of switching costs in banking, specifically in the UK. The report commented that “barriers to switching accounts are perceived to be high” (Cruickshank (2000), p. ix), and found it was unusual for consumers to switch between lenders unless they were moving property.

Kim et al. (2001), in a Norwegian study, supported the existence and influence of switching costs in banking and found that “switching costs in the market for bank loans are quite substantial and constitute a significant portion of the value of a marginal customer to the average firm” (p. 30). Where a line of credit is provided “the cost of switching to a new bank can involve substantial transaction costs associated with developing new agreements and lender relationships” (Phillips, 1993, p. 309).

In a study of U.S. bank retail deposit rates Sharpe (1997) concluded that “customer loyalty associated with switching costs and concentration behave as substitute sources of market power” (p. 94). Zephirin (1994) found that depositors can develop switching costs in banking markets where savings behaviour is conditioned by uncertainty and poor information, which encourages collusive pricing by banks.

The credit card market has attracted particular attention in the discussion of switching costs, which Stango (2000) suggested is due to it appearing to be non-competitive despite having a market structure that would seem to be a good fit of the competitive paradigm. He reported that as credit card solicitations in the US grew “firms began to offer increasingly varied and substantial inducements for consumers to switch cards” (p. 500), including beginning “to offer “switching checks” to make transferring balance from another card easier” (p. 501). A popular approach for many credit card issuers currently is to encourage cardholders to switch

provider by promoting a special low rate, or honeymoon rate, on balances transferred from a card issued by a different issuer, usually for a specified period of time, such as six months.

Stango (2002) found a relationship between switching costs and default rates, and suggested that a consequence is that “extending credit to risky consumers ... may be profitable because these customers have high switching costs” (p. 489). As an example he noted that credit cards that offer inducements for repeat purchases “can use the opportunity cost of switching cards incurred by the repeat purchase plan to extract higher annual fees” (p. 501). Calem & Mester (1995) argued that one reason switching costs arise in the credit card market is due to adverse selection issues, and that this explained the high interest rates in this market. Revisiting this issue, Calem, Gordy, & Mester (2006) found “switching costs and adverse selection may continue to afford market power to lenders with well-established relationships” (p.1685), despite technological advances having lowered search costs and improved credit assessment.

Banking is an information-based industry, and relationships enable banks to collect private information on the creditworthiness of small firms”, which is important as there is likely to be little public information available on such firms (Strahan and Weston, 1998, p. 824). Kim, Kliger, & Vale (2003) noted that banking is one “sector in the economy in which switching costs seem to be prevalent due to information asymmetry” (p. 27), a view supported by Cruickshank (2000) and Sharpe (1990). There is a rational anticipation by both borrowers and lenders that the borrower will be ‘informationally captured’ for the future once a loan has been made, leading to a discount being offered by the lender on the initial finance, in the expectation of a mark-up on future provision of finance (von Thadden, 2001).

The importance of switching costs lies in their effect on market operation. Klemperer (1987) found that “switching costs cause an allocative inefficiency” (p. 390). Berger & Hannan (1998) suggested that whether increased concentration and market power reduce cost effectiveness is of particular relevance in the banking industry. An underlying factor is the fact that switching costs shift the basis of competition by firms, from considering the needs of one consumer in one period to considering those needs over time, or multiple periods (Farrell & Klemperer, 2006). Fornell (1992) perceived switching barriers as a form of defensive strategy to reduce customer exit and switching.

Farrell & Klemperer (2006) caution that “one must not jump from the fact that buyers become locked-in to the conclusion that there is an overall competitive problem” (p. 41). Evidence

has been found that switching costs can generate monopolistic profits for participating firms. However, Anderson & Kaplan (1995) noted that the extent of a firm's monopoly power will depend upon the way in which consumers react to those switching costs. Moutinho & Smith (2000) suggested that a reduction in customer switching costs is one factor that has led to an intensified level of competition and increased pressure on profit margins for UK financial service providers.

An early reference to switching costs, albeit not using that term, noted that a seller might have a group of buyers who will deal with him rather than his competitors despite a difference in price (Hotelling, 1929). Hotelling suggested that the existence of these groups "may be said to make every entrepreneur a monopolist within a limited class and region" (p. 44), and he went on to find that where it was possible to discriminate between customers on the basis of price, a monopoly profit could be collected from some consumers while fierce competition favoured others.

The model of perfect competition used by economists assumes away switching costs for consumers, but Kerin (2006) noted that in the real world switching costs are pervasive and companies can gain if they manage them carefully and innovatively. Barriers to switching are a recurrent theme in the Cruickshank report, which noted that this issue is important because new entrants in a market will not spur more effective competition unless customers are willing and able to switch to a better deal (Cruickshank, 2000). A new supplier seeking new customers has to overcome customer inertia and the lock-in of existing customers (Shapiro & Varian, 1999). Stewart (1998) suggested that the maturing of the retail banking market means "the prospects for growth will rest on attracting customers away from competitors" (p. 12). The existence of switching costs therefore has the potential to be significant, because they will make it more difficult to persuade customers to actually move their business from competitors.

Bendapudi & Berry (1997) suggested that "relationships are profitable only when they last long enough for the firm to recoup its costs and reap the benefits" (p. 17), and switching costs offer a means by which firms can retain customers long enough for their relationship to become profitable. Ahmad (2005) argued that being able to attract and retain profitable customers "is likely to be the linchpin of the success of retail banking in the UK in the new millennium" (p. 320). In line with arguments advanced by others, he suggested that strong bonds, which can also be seen as switching costs, can act as barriers to customer switching.

Gerrard & Cunningham (2004) suggested that “banks could possibly set out to develop wide-ranging relationships with their customers in an attempt to make the switching process more onerous” (p. 220), although they did go on to suggest this is not a good way for banks to seek to preserve their customer base.

Different types of switching costs can have different effects. Nilssen (1992) distinguished between transaction costs, incurred every time a consumer switches supplier, and learning costs, incurred if the switch is to a supplier not previously used by the consumer, and considered their different impacts. He found “an increase in transaction costs, relative to learning costs, increases the price offered to loyal consumers” and leads to a decrease in welfare (p. 579). Search costs were found to be an important part of the explanation for the existence of large differences in price for relatively standardized products (Pratt, Wise, & Zeckhauser, 1979).

Julander & Söderlund (2003) argued it is important to distinguish between positive and negative switching barriers, which relate to wanting to be versus having to be in a relationship respectively. They classified switching costs as a negative switching barrier, i.e. switching costs lead to customers maintaining a relationship with a supplier that they would prefer not to have. Pae & Hyun (2002) agreed but suggested that “switching costs create dependence and inertia” (p. 376). Similarly, a key finding of Sengupta et al. (1997) was that “the net result of switching costs is that they produce inertia for the customer to remain in the relationship with the current supplier” (p. 10).

Zauberman (2003) claimed that lock-in is driven by consumers having a preference for minimizing immediate costs and underweighing the impact of future switching costs, which he attributed to consumers’ short-term focus and their failure to anticipate the impact of future switching costs. He claimed that “the cost of switching seems smaller the farther away it is in time, potentially leading consumers to choose options that are attractive in the short-run because they do not fully anticipate how painful it will feel to shift later” (p. 406).

Bansal & Taylor (1999) found that a customer’s attitude towards switching was an important determination of their intention to switch, and that switching costs also affected switching intentions. However, neither the attitude nor switching costs were found to have a significant direct effect on actual switching behaviour.

RESEARCH METHODOLOGY AND DATA

Although previous studies have identified several different switching cost categories, limited work has been done to understand how the different types of switching costs affect the likelihood of switching and switching behaviour. This paper explores the proposition that attitudes towards switching costs affect the relationship between the desire to change banks and the likelihood of actually switching.

Previous studies have found switching costs have the effect of locking in customers, so switching costs should have no effect on customer desire to switch but would be expected to reduce the likelihood of the switch being made. More specifically, switching costs are expected to impact on the relationship between the desire to switch and the likelihood of doing so, such that customers are less likely to switch despite wanting to do so when switching costs are higher. This should apply for switching costs overall, but may also apply for one or more individual categories of switching cost. This leads to the hypotheses to be tested in this paper.

H1: That the likelihood of switching is less positively correlated with the desire to switch when switching costs are perceived to be high.

H2: That the likelihood of switching is less positively correlated with the desire to switch when each category of switching cost is perceived to be high.

The hypotheses propose some form of correlation between variables. Spearman's correlation coefficient is one of the two principal measures of correlation and was used as it is designed for use with variables measured using ordinal scales as in this study.

The questionnaire took the form of an A5-sized booklet, designed in line with the university's current branding guidelines. It was pre-tested on a user-panel of family and friends, before the revised questionnaire was piloted on a sub-sample of 100 people. The questionnaire was structured and formatted in line with the principles advocated by Dillman (2000) to enhance the response rate.

A number of questions were asked where respondents were asked to signify the extent of their agreement, or disagreement, with a given statement, using a Likert scale. For this study, a seven-point scale was used because it was considered important to have a neutral option (Neither agree nor disagree) available as that could enhance the response rate, while three items on each side of the scale allows finer differentiation between attitudes. The descriptors

chosen were “strongly agree/disagree”, “mostly agree/disagree” and “slightly agree/disagree”. The use of seven response categories is supported by the findings of Preston & Colman (2000) that the most reliable scales had 7-10 categories with a 7-point scale being the third most preferred, after 10 and 9 point scales. Similarly, Cox (1980) found that seven plus or minus two offered “a reasonable range for the optimal number of response alternatives” (p. 420). For other questions where the extent of agreement or disagreement was not an appropriate response, a seven-point scale continued to be used, in most cases, for consistency but with alternate appropriate descriptors.

The questionnaire comprised 70 questions in four sections. The first section asked about the respondent’s banking relationships and is not relevant to the part of the study reported in this paper. The second section was of most relevance to this study, including questions about switching likelihood and the desire to switch. In addition, there were questions about the perceived ease of switching and actual past switching experiences. The third section of the questionnaire was also important, exploring respondents’ attitudes towards switching costs. The final section of the questionnaire sought information about the respondent’s demographic characteristics.

Nine categories of switching costs were used in the study, based largely on the Burnham et al (2003) approach; however, some names were changed, and hassle was added as a separate category. The categories were: **Learning Costs**, including familiarisation with the new bank, its products and its systems; **Search Costs** to find out about other financial institutions then evaluate them to decide the most suitable to switch to; **Uncertainty**, or the risk that the new bank may be no better, or even worse, than the current bank; **Benefit Loss** being the loss of accumulated benefits, in the form of reward schemes, discounts and other privileges; **Monetary Loss** in the form of fees for terminating the old relationship and those incurred establishing the new relationship; the **Hassle** or Inconvenience of actually making the change from one bank to another; the loss of the **Brand Relationship** as the switcher is no longer a customer of Bank X, which may have affected their self-image because of the bank’s reputation and/or market standing; the loss of the **Personal Relationship** the switcher has with the bank staff with whom they dealt on a regular basis; and **Service Disruption** such as the possibility that an automatic payment may be missed or a direct credit not received on time, for example, during the actual switch over phase. The switching cost variables were measured using 3-5 statements per category, with agreement/disagreement sought on a 7-

point Likert scale for each statement. The statements used were drawn from the existing literature, although some were reworded to ensure consistency of style.

The first and third mailings comprised a full set of survey material, with the information sheet in the third mailing amended to reinforce the request for participation. The second mailing was a one-page letter encouraging participation. The second and third mailings were sent only to non-respondents at the time of posting, identified via number coding on the questionnaire.

A total of 955 valid responses were received, while 135 were returned undelivered, from the sample of 2983. In addition there were 37 cases where the recipient was reported to be ineligible to participate and 130 questionnaires were returned by people who indicated a refusal to participate. The final response rate for the survey was 33.5% after allowing for the undelivered questionnaires and the ineligible recipients.

The sample population for the survey was drawn from the New Zealand electoral rolls, using a simple random selection process. The key characteristics of the respondent population are shown in Table 1 below. Clearly there are some differences between the respondents and the New Zealand population, which represent differences between respondents and non-respondents, and therefore there is potential for non-response bias. The respondent group is dominated by females to a greater extent than is the New Zealand population, which is in line with the assertion by Hair, Bush and Ortinau (2006) that mail survey respondents are more likely to be female. There is a reasonable distribution of respondents across the age groups, although the respondent group is older than the New Zealand population. Furthermore, a higher proportion of the respondents identified as New Zealand European than in the general population. Newell, Rosenfeld, Harris, & Hindelang (2004) reported that other research had found demographic differences between those who do and those who don't complete surveys, including education, gender and age. Similarly, Green (1996) reported survey respondents are likely to be more educated and to be female.

Table 1: Respondent population characteristics

Characteristic	Category	No	Proportion	New Zealand ⁵
Gender	Female	527	57.0%	51.2%
	Male	397	43.0%	48.8%
Age	<20 ⁶	11	1.2%	9.7%
	20-29	85	9.3%	16.5%
	30-39	158	17.3%	18.6%
	40-49	206	22.6%	19.6%
	50-59	177	19.4%	15.7%
	60-69	168	18.4%	10.6%
	70+	108	11.8%	9.4%
Ethnicity ⁷	NZ European	716	75.0%	64.8%
	NZ Maori	62	6.5%	14.0%
	Pacific Islander	19	2.0%	6.6%
	Other ⁸	152	15.9%	24.5%
Education	No qualification	159	17.2%	22.4%
	Secondary school	303	32.9%	n.c. ⁹
	Vocational	222	24.1%	n.c.
	Bachelor degree	152	16.5%	10.0%
	Higher degree	86	9.3%	4.2%

Data collected from a representative sample is of value because it can be used to make generalizations about the larger population from which the sample was drawn (Burkell, 2003). However, when only some of the sample respond to the invitation to participate in the survey or other research, as is usually the case, questions arise as to the extent to which this generalization can occur. This leads to the issue of non-response bias, which refers to the possible difference in views between those who do respond to a survey and those who don't. The Armstrong and Overton (1977) methodology was used to explore the existence of non-response bias in this study. The interest hypothesis approach used assumes "that people who are more interested in the subject of a questionnaire respond more readily" (Armstrong & Overton, 1977, p. 397). No evidence of non-response bias was found.

⁵ New Zealand figures are from the 2006 census data available from Statistics New Zealand (www.statistics.govt.nz).

⁶ The comparison with the New Zealand population is not direct as the <20 age group for New Zealand is for 15-19 years, while it is 18-19 for the sample.

⁷ Some respondents chose more than one response for ethnicity so the categories are not exclusive.

⁸ The "Other" Category includes 39 respondents who identified themselves as Kiwis or New Zealanders.

⁹ n.c. = directly comparable data for New Zealand not available

Hair et al. (2006) note that every study has limitations, and common limitations include sampling bias and systematic errors. The electoral roll was used to draw the sample, and not all New Zealanders over 18 are registered despite a legal requirement to do so, while some choose to have their details withheld from any production of the roll. Although the numbers are believed to be small, it means the electoral roll does not represent the complete listing of the population of interest, as required to limit the extent of sampling bias.

A non-parametric chi-square test was used to explore the differences between the sample and the New Zealand population in respect of gender and age. These tests found a significant difference, which indicates that generalizing the findings of this research to the general population must be done with care. A range of possible non-sampling errors can arise, most of which are dealt with in the design of the questionnaire and the process undertaken. Errors apparent in the responses received, have been corrected or removed. Some non-sampling errors may remain, primarily response errors such as deliberate falsification or unconscious misrepresentation, as they are unable to be identified and eliminated. These are not expected to be significant.

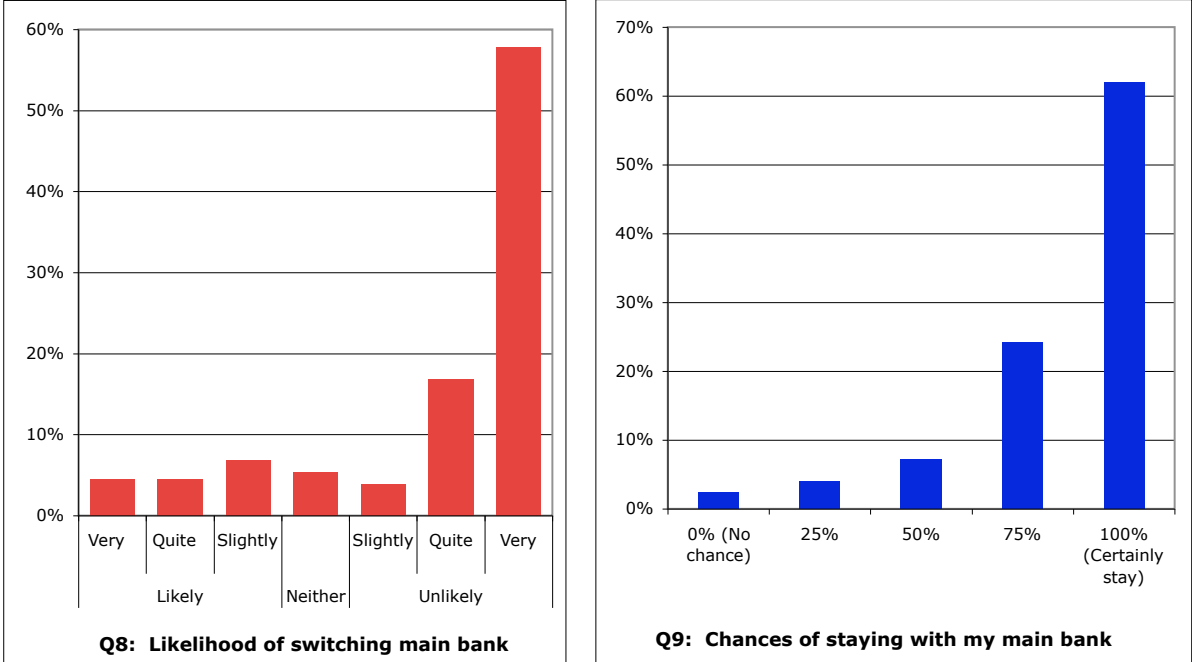
RESULTS

We begin with the respondents' expected future switching behaviour, or more specifically the likelihood that they will switch in the future. Respondents' likelihood of switching was captured using two separate questions. The first (Q8) asked "How likely are you to switch to a competing financial institution as your main bank during the next twelve months?", while the second (Q9) asked "What are the chances that you will stay with your bank for the next year?"

The distribution of responses for these questions is shown in Figure 1. It is clear the majority had no intention of changing banks in the next twelve months. The mean response for Q8 was 5.8, close to the response of 'Quite unlikely' (given a value of 6) and for Q9 it was 4.4, just over the response of '75%' (given a value of 4). For both questions the median response was the final option, or 'Very unlikely' and '100%' respectively. A minority of respondents did indicate a future intention to change their main bank, with 16.0% of respondents indicating

some likelihood of switching, but only 6.4% reported a less than 50% chance of staying with their current bank.

Figure 1: Likelihood of future switching



These questions were expected to generate similar responses, and this was tested with a Spearman’s correlation test. A correlation of 0.74 was found between responses to the two questions, which was significant at the 1% level indicating a strong correlation. The subsequent analysis on likelihood of future switching used a single variable, *Switching Likelihood*, measured as the mean of questions 8 and 9; however, as there were a different number of items in the response scale for Q9, the response options were adjusted to give equivalent values in a range of 1-7.

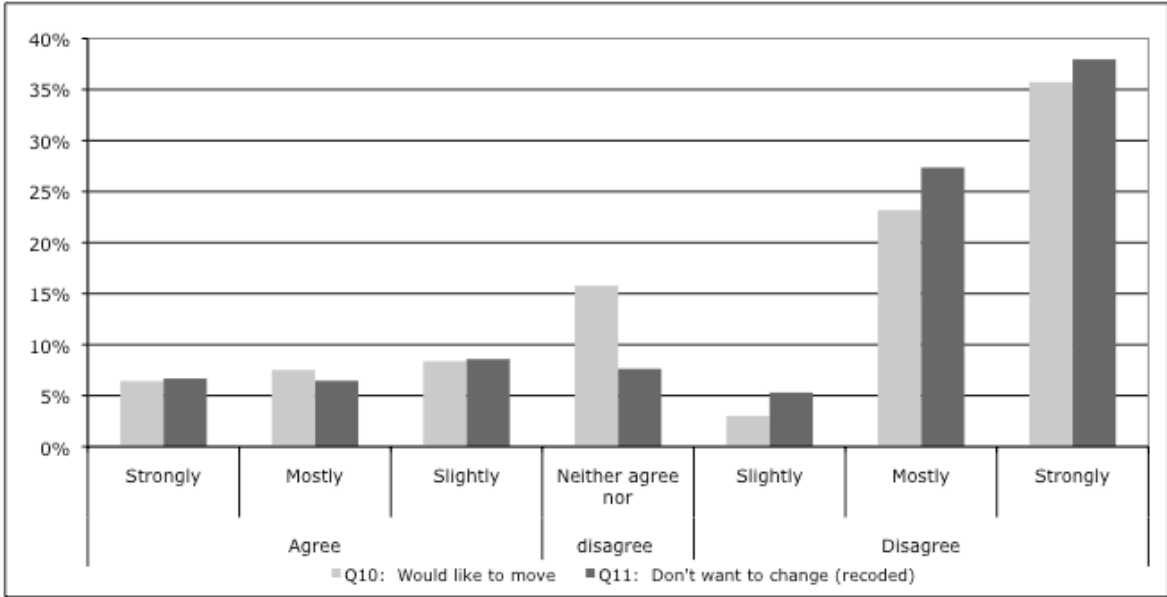
This reported lack of intention to change banks by most people could indicate that they were happy with their current banking arrangements, but it could also mean they felt locked in and unable to change. Two questions were used to capture the respondents’ desire to switch, to assist in a better understanding of whether the lack of intention to switch indicated satisfaction or a feeling of being locked in. The two questions sought the extent of the respondent’s agreement or disagreement with statements about their desire to change bank. The first statement (Q10) was “In an ideal world, i.e. ignoring any possible difficulties, I would like to move from my existing main bank to another bank”, and the second statement (Q11) was “I

am happy with my main bank and don't want to change". For analysis purposes the responses to the second question were inversely recoded.

The distribution of responses for these questions about desire to switch is shown in Figure 2, and we find most respondents had no desire to switch. The responses to the two questions were very similar, as Figure 2 shows, although there were more neutral responses for Q10 and more respondents who indicated they did not want to switch for Q11. The correlation between these two questions was tested using Spearman's correlation, with a correlation of 0.60 found, significant at the 1% level. The subsequent analysis related to the desire to switch uses the mean response for these two questions, using the recoded responses to Q11, as the measure for *Switching Desire*.

It is interesting to note that around one-fifth of respondents (22.3% for Q10 and 21.7% for Q11) indicated some desire to change banks compared to 16.0% and 6.4% who indicated some intention of actually switching banks in the subsequent 12 months. The relationship between these two variables is the key to the research question.

Figure 2: Desire to switch



The conflict between wanting to switch banks but being unlikely to do so was reflected in respondents' comments, such as:

Many times in the Past we thought about changing, but never did. Due to being busy with every day life and the inconvenience of it.

Would like to change banks, but the legal costs of switching the mortgage, isn't worth any savings we would make.

I would happily change Banks in a flash. Westpac Trust is the worst bank & I advise people not to go with them. ... I work from 5.30am – 5.00pm & don't have time to go & change my bank so I just put up with it.

These comments indicated that while these respondents would like to change banks, they were unlikely to do so because of the hassle and monetary costs involved. So switching costs would seem to be preventing desire becoming intention.

Before exploring the effect of perceived switching costs, it is useful to consider the basic correlation between desire and likelihood. The correlation between these two variables was found to be significant at the 1% level, with a Spearman's correlation coefficient of 0.54. This indicates a strong positive correlation between desire to switch and likelihood of switching. The fact that the correlation is not stronger suggests that while a person may wish to switch there is some factor that means they are unlikely to do so in practice, and it seems reasonable to suggest that switching costs may be such a factor. This is supported by the respondents' comments noted above. Other comments also indicated that switching costs were deterring people from changing banks despite a desire to do so. For one respondent it was the time and learning costs:

I want to change banks with lower fees but I don't really have the time to do that and learn a new system

For another it was simply the hassle involved:

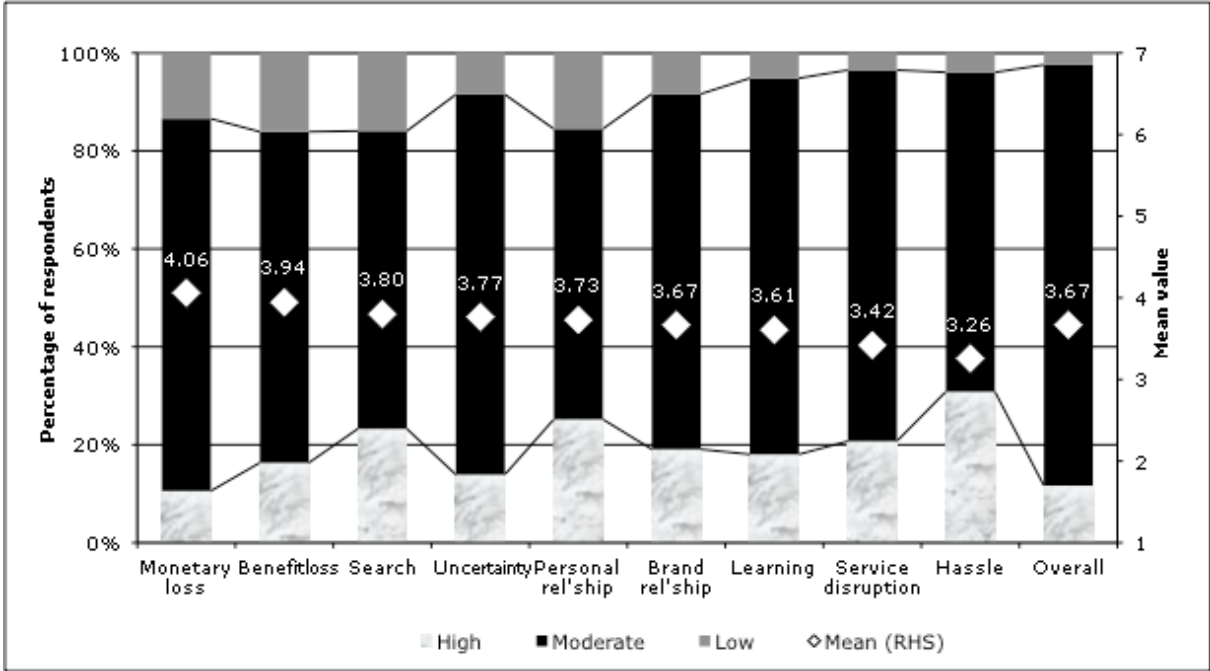
We did at one point consider changing banks due to mortgage interest rates, credit card interest rates etc. Got as far as completing the forms but too much hassle in the end compared to the service we get from our bank.

For a third the monetary costs were the issue:

I know I am not making the most from the way I am paying my mortgage and would like to change back to a bank I have previously used, but having valuations done, paying lawyers, and all the interest that I have already paid and starting all over again is very daunting.

To test both hypotheses the respondents were broken into three groups, comprising those who considered switching costs were high, moderate and low. Where the mean rating for the category, or overall switching costs, was less than 2.75 the respondent was judged to perceive that category of (or overall) switching costs as high. Respondents were considered to have a perception that switching costs are low where the mean was greater than 5.25. A mean value between 2.75 and 5.25 inclusive was considered to indicate a perception that switching costs are moderate. The cut-offs were chosen to be at a level such that the respondent appeared to have a reasonably strong view if included in the high or low groups. The proportion of respondents in each of the three groups for each category of switching costs is shown in Figure 3, along with the mean for each category.

Figure 3: Perceiving switching costs



The first hypothesis (H1) was that the likelihood of switching is less positively correlated with the desire to switch when switching costs are perceived to be high. Likelihood of switching was measured using the *Switching Likelihood* variable, and the desire to switch was measured using the *Switching Desire* variable. As Table 2 shows the correlation between *Switching Likelihood* and *Switching Desire* was positive for all three groups, and it was clearly less where perceived switching costs were high, thereby supporting the hypothesis. The highest correlation was found where switching costs were perceived to be low, although the difference between the moderate and low groups is small. Accordingly, the first hypothesis was supported.

Table 2: Correlation between desire to switch and likelihood of switching for different levels of overall switching costs

Switching costs are perceived to be		
High (N=110)	Moderate (N=802)	Low (N=23)
rs=0.37***	rs=0.56***	rs=0.59***

***= significant at the 1% level

The second hypothesis (H2) was in respect of the same relationship, but considered the effect for each of the nine switching cost categories individually. The results appear in Table 3. The final column indicates where the predicted relationship held, i.e. that the correlation between *Switching Likelihood* and *Switching Desire* increased as the perception of the switching cost category fell; no account is taken of the magnitude of the increase in the correlation.

For seven switching cost categories the results were clear, and the hypothesised relationship held, with a positive correlation that increased from the High group to the Low group. In the case of *Learning Costs* the correlation was greater for both the Moderate and Low groups compared to the High group, but the correlation was smaller for the Low group than the Moderate group. It can be argued that in this case the hypothesis is supported, but only partially. For *Uncertainty* the correlation was smallest for the Low group, although it was higher for the Moderate group compared to the High group. Nevertheless, the hypothesis should be rejected for this category.

The relative differences in the level of correlation were not analysed. However, it is of interest to note that the greatest range between high and low are found for *Benefit Loss* (0.29), *Personal Relationship* (0.28), and *Monetary Loss* (0.21). This suggests that these three categories of switching costs have a greater impact on deterring people from switching when they would like to do so. The smallest differences (for the categories where the hypothesis is fully supported) are found for *Search* (0.04) and *Service Disruption* (0.07). This suggests these two categories are limited in their impact on deterring people from switching if they have a desire to do so.

Table 3: Correlation between desire to switch and likelihood of switching for different levels of each switching cost category

Switching cost category	Switching costs are perceived to be			Correlation increases
	High	Moderate	Low	
Learning	rs=0.49*** (N=163)	rs=0.58*** (N=694)	rs=0.55*** (N=46)	No
Search	rs=0.53*** (N=213)	rs=0.55*** (N=553)	rs=0.57*** (N=144)	Yes
Uncertainty	rs=0.50*** (N=126)	rs=0.57*** (N=698)	rs=0.46*** (N=77)	No
Benefit Loss	rs=0.41*** (N=148)	rs=0.50*** (N=608)	rs=0.70*** (N=145)	Yes
Monetary Loss	rs=0.39*** (N=96)	rs=0.57*** (N=685)	rs=0.60*** (N=121)	Yes
Hassle	rs=0.50*** (N=280)	rs=0.57*** (N=587)	rs=0.60*** (N=36)	Yes
Brand Relationship	rs=0.43*** (N=170)	rs=0.50*** (N=654)	rs=0.52*** (N=76)	Yes
Personal Relationship	rs=0.30*** (N=227)	rs=0.53*** (N=534)	rs=0.58*** (N=141)	Yes
Service Disruption	rs=0.51*** (N=188)	rs=0.55*** (N=685)	rs=0.58*** (N=32)	Yes

***= significant at the 1% level

CONCLUSION

The findings in respect of the hypotheses are summarised in Table 4. Overall, the results were supportive of the proposition that the relationship between desire to change bank and the likelihood of actually doing so is affected by perceived switching costs. More specifically, someone who would like to change their bank is unlikely to do so if they have a perception that switching costs are high. The finding that seven of the nine switching cost categories reduce the correlation between *Switching Desire* and *Switching Likelihood* is important in terms of its implication in the banking market. It means that banks must address a range of issues, not just one, if they are to turn a potential switcher into an actual switcher.

Table 4: Results for hypotheses

H1	That the likelihood of switching is less positively correlated with the desire to switch when switching costs are perceived to be high.	Supported
H2	That the likelihood of switching is less positively correlated with the desire to switch when each category of switching costs is perceived to be high	
	<ul style="list-style-type: none"> • Learning • Search • Uncertainty • Benefit Loss • Monetary Loss • Hassle • Brand Relationship • Personal Relationship • Service Disruption 	Partial support Supported Rejected Supported Supported Supported Supported Supported Supported

Further investigation of the impact of switching costs on the relationship between customers' desire to switch and their actual intention to change banks would be useful. In particular, a better understanding of how switching costs affect the relationship would be of value. The relative importance of the different categories of switching costs would also be of interest, in order to identify which issues banks should direct more resources to.

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