Money

Staying Power. New ways companies are getting us to stick with lousy service

By Bill Saporito

MY CABLE BILL ARRIVED THE OTHER DAY with an unexpected $20-a-month increase for the same package I've been getting for years. A cheery customer-service representative explained that my discount for bundled services had expired and, although she would truly like to, she couldn't restore it. When I mouthed off about hoofing it to another provider, her response fell into the category of "Good luck with that."

If she figured I wasn't going anywhere, she was right. Although I wasn't facing any exit fees, the idea of setting up a new account elsewhere—which involves not only waiting for the cable guy to swap out three cable boxes but also learning a different remote control and repopulating my DVR—proved too big a burden, despite the prospective savings of $240 a year.

I had become trapped by what economists call switching costs—the barriers, financial and otherwise, that prevent a customer from getting rid of an underperforming product or service provider. Given the rising volume of advertising for insurance, mobile phones, cable service and credit cards, it seems companies must be winning and losing customers as the struggle to grow revenue intensifies. They aren't. They're just tightening their grip on us. Verizon spent 21% more in the last quarter trying to reel in new subscribers and keep existing ones, even though fewer than 1% of its customers jumped ship. And that low churn rate is not unusual. Cell-phone industry consultant Chetan Sharma says that annually only 2% of U.S. subscribers change providers.

"The longer you stay with something, the less likely you are to switch," says marketing professor Vijay Mahajan of the University of Texas, who sorts switching costs into three buckets: financial, procedural and relational.

The first one is straightforward. Breaking a cell-phone contract, for instance, costs money. It's in the other two categories that companies have really been working hard to jack up switching costs in various ways. Bundling has raised the ante procedurally, in part by adding complexity to the equation. To switch Internet-service providers, you won't just need to get a different cable box; you'll need a new modem, and you'll have to adapt to a new system after having spent the time to master your current one. Going up the learning curve of a new provider is yet another switching cost. The reason cell-phone companies spend so much on advertising, says Sharma, is not necessarily to lure new customers but to upsell old ones from feature phones to smart phones to tablets, from a single data plan to multiple—leaving them tangled in a web of technology and family plans.

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And the more deeply invested you are in a brand relationship, the higher the so-called relational cost of leaving it. If you break with Allstate, as some of its current advertising suggests, you risk getting lousy service somewhere else. So go ahead—put your loved ones at risk for a few bucks. It's a neat bit of marketing psychology, says Peter Fader, a marketing professor at the University of Pennsylvania's Wharton School: "The company is saying, 'We're not trying to hold you hostage.' Instead, you hold yourself hostage."

He thinks companies should spend more money on raising switching costs and less on marketing that raises customers' expectations. "For every dollar spent on switching costs, $10,000 is spent on unicorns and rainbows," he says. The risk is that they overpromise fantabulous service and then underdeliver—which, in theory, should make it easier for us to switch to another company.

But service sellers have a way of compensating for overpromising too: hooking us on loyalty programs. "We overplay the value of the points and the chance that we will use them," says Fader, who gets paid to advise companies about such things. And we are headed for even more switching costs with the onset of coalition loyalty programs that unite restaurants, shops and other unrelated companies around one frequent-buyer program. It is more common in Europe but is starting to take root in the U.S. via mobile-payment platforms like LevelUp. There are benefits to be had, but we risk becoming loyal to a fault. ■

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