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Restaurant membership fee and customer choice: The effects of sunk cost and feelings of regret

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Abstract

Membership marketing is highly prevalent in today's restaurant industry. The purpose of the study was to examine the joint effects of membership fees and competition on customer choice, willingness to join other programs and feelings of regret in a restaurant setting. Using a $2 \times 2 \times 2$ experimental design, the study found that the effect of sunk cost and mental accounting do exist. Moreover, high levels of regret were detected when a higher membership fee was paid and when the competition provided superior service or a lower membership fee. However, when the membership fee was low, customers were more reluctant to go to another restaurant that offered a membership program. Marketing implications for restaurateurs are discussed.

Keywords: Sunk cost effect; Membership marketing; Mental accounting; Regret; Restaurant

1. Introduction

Membership marketing is gaining popularity in the United States. In its early days, membership marketing was limited to prestigious offerings such as exclusive country clubs. Yet, today membership marketing is common in various settings such as warehouse clubs, athletic facilities, and video rentals (Dick and Lord, 1998). In addition, many restaurant operators offer low fee or free membership programs. For example, Warren's Lobster

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House membership requires a $10 annual fee (http://www.lobsterhouse.com/frequent.html); Levy's preferred membership is free (http://www.levyrestaurants.com/levy/other/levy+preferred+information+levy+restaurants.html); and Chicago based LEYE membership requires a one-time $25 enrollment fee (Ragone, 2005).

Consumers sign up for membership in hope for preferential treatment and cost benefits. From the operator's perspective, a well-crafted membership program translates into favorable consumer attitudes and loyalty behaviors (Dick and Lord, 1998). Moreover, some companies (e.g., warehouse clubs) launch membership programs in order to increase their market share (Friedman, 2003). Despite its wide application in the restaurant industry, some people remain skeptical about the effectiveness of membership marketing (Stauss et al., 2005; Skogland and Siguaw, 2004). For instance, membership fees might have a negative impact on consumers' willingness to try a new restaurant. On the other hand, offering low cost or no-fee based memberships can be risky as such efforts minimize switching barriers. The primary purpose of this study is to examine the impact of membership marketing on consumer choices in a restaurant setting. Moreover, we want to investigate the role of membership fees in influencing feelings of regret via the notion of sunk costs.

2. Literature review

2.1. Sunk cost effect

Sunk cost is a cost that has been incurred and cannot be reversed. It also referred to as "stranded cost" (http://financial-dictionary.thefreedictionary.com/Sunk+Cost). Translated into our context, the initial membership fee represents a sunk cost. If we consider utility maximizing behaviors, consumers' purchase decisions should rely only on the marginal costs and benefits of alternatives (Dick and Lord, 1998). Therefore, the membership fee should not influence subsequent purchasing decisions or consumer attitudes. Yet, previous research clearly shows that sunk costs are not ignored in consumers' decision making processes (e.g., Arkes, 1996; Arkes and Blumer, 1985; Arkes and Hutzel, 2000; Dick and Lord, 1998; Kahneman and Tversky, 1984).

Arkes and Blumer (1985) were among the first to examine the sunk cost effect. Once an investment in money, effort, or time has been made, consumers become committed to their choices. In their ski scenario experiment, respondents had to choose between two ski resorts, one located in Michigan and the other in Wisconsin. The Michigan resort had a higher cost and lower level of expected utilities than the Wisconsin facility. Fees for both resorts were already paid and non-refundable. Following the argument for utility maximization, no rational human being would choose the Michigan resort. Yet, in reality a greater number of respondents chose the Michigan resort over its more attractive Wisconsin offer. In other words, sunk costs translated into commitment to prior choices. Similarly, Dick and Lord (1998) found that membership fees, as sunk costs, have a positive impact on consumer attitudes and purchase behaviors. In their study, members justified their decisions (paid membership dues) and exhibited a stronger attitudinal preference for their store than non-members.

Thaler (1980) proposed that Kahneman and Tversky's prospect theory could provide a theoretical explanation for the sunk cost effect. Kahneman and Tversky (1979) showed that the aggravation of experiencing losing a sum of money is greater than the pleasure