The effect of incentives on customer evaluations of service bundles

Melinda L. Andrews a,⁎, Ray L. Benedicktus b,1, Michael K. Brady c,2

a College of Business, University of Southern Mississippi, Hattiesburg, MS 39406, United States
b College of Business and Economics, California State University - Fullerton, 800 North State College Boulevard, Fullerton, CA 92834-6848, United States
c College of Business, Florida State University, Tallahassee, FL 32306, United States

⁎ Corresponding author. Tel.: +1 601 266 4629; fax: +1 601 266 4630.
E-mail addresses: melinda.andrews@usm.edu (M.L. Andrews), rbenedicktus@fullerton.edu (R.L. Benedicktus), mbrady@cob.fsu.edu (M.K. Brady).
1 Tel.: +1 714 278 7117.
2 Tel.: +1 850 644 7853; fax: +1 850 644 4098.

ABSTRACT

Effects of service bundle incentives on perceived value, search intentions, and switching intentions are assessed in two independent studies. The first study demonstrates that service bundling influences switching and search intentions through perceived value. Results related to bundle incentives support the salience of the convenience associated with consolidating charges onto one bill. Further analysis reveals that explicit valuation of savings creates higher perceived value than convenience alone; however, search and switching intentions are unaffected by incentives or valuation thereof beyond the convenience effect. A second study replicates key parts of these results. Research and practical implications are discussed.© 2009 Elsevier Inc. All rights reserved.

1. Introduction

Service bundling is the practice of marketing two or more services in a single package (Guiltinan, 1987). For example, Comcast’s Triple Play package includes phone services, high-speed Internet, and digital television. Marketers spend billions of dollars each year to promote service bundles by emphasizing incentives such as savings discounts, convenient billing options, and/or free gifts (e.g., technical upgrades, gift cards, etc.; Higgins, 2004; Sharma, 2005). Given the vast investment in service bundle promotional tactics, it is essential that service managers have information on how to design and communicate bundle incentives in a way that maximizes value for consumers and minimizes cost for the firm. This study examines the effects of bundle incentives (i.e., one-bill convenience, cost savings, and service upgrades) on consumers’ value perceptions, intentions to search for and compare alternative service providers, and willingness to switch to a competitor. Given the frequency of bundled offers in the multi-billion dollar telecommunications industry (Teal, 2007), the domain of this research centers upon telecommunication services (Agarwal, 2002).

Prior research about the topic of bundling (e.g., Harlam et al., 1995; Kaicker et al., 1995; Simonin and Ruth, 1995) does not focus on bundles of services. Thus, this research fills a gap by addressing several important questions in regards to service bundles. First, what role does value play in influencing consumer perceptions and decisions about service bundles? Second, is there a differential impact of cost savings and/or premium upgrade incentives above and beyond the convenience of one bill? Third, do consumer reactions to bundle incentives depend on the presentation (i.e., message framing) of the offer? The results of two independent experiments address these questions while offering important managerial insights for designing bundle offers.

2. Research questions

The role of a bundling strategy is to encourage multi-item purchases in buyer groups that would normally purchase fewer products than those included in the bundle (Finney et al., 2008; Yadav, 1994). Bundles can adopt one of three strategic forms: pure, mixed, and unbundled (Adams and Yellen, 1976). The present research focuses on mixed bundles, which unlike pure bundles, may involve services that are also commonly purchased individually. Mixed bundling strategies are suggested to be more profitable than pure bundling strategies, provided the price of the bundle and its components are carefully chosen (Venkatesh and Mahajan, 1993).

Prior research documents the success of both pricing and promotions in stimulating immediate sales response (Blattberg et al., 1995; Guadagni and Little, 1983; Neslin et al., 1985). For example, Dodson et al. (1978) indicate that the probability of positive purchase outcomes is greater when a deal is involved, and this probability increases as the magnitude of the incentive associated with the deal increases. Thus, offers with high economic value are expected to have greater utility and induce positive behaviors more than offers having lower economic value.
The role of incentives in value creation is particularly important to the success of service bundle offers. Perceived value is the consumer’s overall assessment of the utility of a product based on perceptions of what is received versus what is given (Ruiz et al., 2008; Zeithaml, 1988). The importance of perceived value is illustrated in previous studies that suggest value perceptions exercise a direct influence on satisfaction (Lai et al., 2008), purchase intentions (Bolton and Drew, 1991; Hightower et al., 2002), loyalty (Brodie et al., 2009), and willingness to buy (Dodds et al., 1991). Moreover, value may enhance switching intentions and/or reduce search because the added benefit of additional search is reduced when a need-satisfying, goal-relevant deal is identified (i.e., consumers seek value and thus may search less before choosing to switch when value is high). These relationships suggest that value perceptions play an important role in determining consumers’ switching and search intentions.

The first two research questions are related to the role of value perceptions in service bundles. The aforementioned bundling literature, economic utility theory, and the established role of value in affecting purchase decisions suggest that bundling services adds value to a service offer. The source of value can be tied to either side of the “receive versus give” value equation. On the receive side, service bundles may add to the utility of the offer through billing convenience, as consumers are in business with only one firm rather than several firms and they can pay for all of the services at one time. On the give side, price discounts and free upgrades offered as incentives to purchase the bundled offer may reduce what consumers have to give up to receive the bundle of services. Drawing from prior work on the economic utility of incentives (e.g., Dodson et al., 1978), we expect perceived value will increase as the perceived magnitude of bundle incentives increases.

**H1.** Perceived value will be higher for bundled services than for unbundled offers.

**H2.** Bundles with incentives elicit higher perceived value than convenience alone.

The third hypothesis mandates investigation of whether value-relevant information can be made more salient to consumers via message framing. Message-framing effects are well established in the literature as a determinant of consumer purchase decisions (Chandrashekaran and Grewal, 2006; Puto, 1987). Framing effects occur when a superficial variation in the description of an offer leads consumers to make additional positive or negative associations about the product (Darke and Chung, 2005). For example, consumers can underestimate the true value of an offer when its value is not explicitly stated, thereby limiting the overall perceived value of the offer (Raghubir, 2004).

It is important to provide consumers with desirable incentives and clearly communicate the value of the incentive within an advertisement or offer (Darke and Chung, 2005). Financial bundle incentives that are presented with the benefit of an explicit monetary value (i.e., positive framing) may lead customers to perceive added value of the offer over billing convenience alone. Specifically, because explicit information requires less cognitive processing effort, consumers may readily identify the added value and be more likely to consider this value in purchase deliberations. Thus, if the inclusion of incentives is not sufficient to increase value perceptions beyond convenience, it is possible that explicit valuation of these incentives will increase incentive salience to the extent that:

**H3.** Perceived value will be higher for bundled service offers that equate financial incentives to a specific monetary value than for bundles noting only one-bill convenience.

The majority of promotional sales come from customers switching from existing service providers (Gupta, 1988; Totten and Block, 1987). This research focuses on decisions associated with a switch to a competitor’s service bundle and explores the impact of common switching incentives. Due to the large number of available bundling options within and across brands, the complexity of comparing bundles with different attributes, and differences in quality and price, consumers are likely to engage in extended search when evaluating bundle offers (Clarke and Belk, 1978). Consumers’ search typically declines as the marginal benefit of seeking additional offers is reduced (Bettman et al., 1988; Hauser and Wernerfelt, 1990). This paper is among the first to examine the effects of specific bundle incentives that would induce consumers to switch from an existing service provider.

**H4.** Consumers will have (a) higher switching intentions and (b) lower search intentions when presented with bundle offers equating incentives to a specific monetary value than for offers noting only one-bill convenience.

### 3. Study 1

#### 3.1. Method

Trained student recruiters collected data from 293 consumers as part of an assignment for an undergraduate marketing course.

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**Fig. 1.** Monthly valuated savings manipulation.
Students received course credit for collecting data from non-student, non-faculty acquaintances, over the age of 25. Recruiters emailed a request for participation, developed by the authors, to potential respondents that included a description of the study and a link to the online experiment. The Study 1 sample contained 53.4% women and 46.6% men with an average age of 45.3 years. Cell sizes ranged from 26 to 46.

Upon accessing the study, respondents were told an established telecommunications company was expanding its service to their area, and they must decide whether to switch services or remain with their current provider. Eight conditions were created based on offers common in the telecommunications industry. Subjects receiving the unbundled condition considered a situation wherein they received ads from several service providers, but no bundled offers. A second advertisement cited only “the convenience of having one bill” as an incentive for switching. Two other bundle ads noted both one-off convenience and either “a free high-speed Internet upgrade,” or “savings of at least 10% off the costs of existing services.” The 10% incentive was selected based on the results of prior research that suggested the effect of 10% savings was similar to larger (20%) savings incentives (Hermann et al., 1997). Pre-testing with a separate sample indicated the effect of 10% savings was similar to larger (20%) savings incentives (Hermann et al., 1997).

Pre-tests indicated that the average telecommunications bill for the services in the ad was about $178 per month. Thus, the 10% savings amount was valued as an “average savings of $18 per month” or “an average $216 annual savings.” Valuation of the high-speed Internet upgrade was based on regional market prices for the service upgrade. Subjects in the valued upgrade condition received an ad noting the upgrade represented “a $9.95 monthly savings” or “a $120 annual savings” over not having to pay for the service upgrade.

3.2. Measures

All scale items were measured with 7-point Likert scales anchored by 1 = Very Low or Strongly Disagree and 7 = Very High or Strongly Agree. A nine-item scale captured subjects’ value perceptions (Burton and Lichtenstein, 1988; Lichtenstein and Bearden, 1989). Subjects indicated their switching intentions on a four-item scale (Dodd et al., 1991) and their search intentions on a three-item scale (Grewal et al., 1988). The presentation of incentives can deteriorate quality perceptions and thus could have affected the perceived value of the bundles. For example, Darke and Chung (2005) show that negative quality inferences limit the extent to which discount frames are capable of increasing perceptions of value. Thus, the study included a check to ensure that the incentives in the ads affected value perceptions independent of resulting quality inferences.

3.3. Preliminary analysis

The psychometric properties of the measures were assessed using confirmatory factor analysis (CFA). All scales were simultaneously tested, with each item being allowed to load only on its respective factor. CFA results indicate that the measurement model fit the data well ($\chi^2 = 848.8; df = 314; CFI = .98; TLI = .97; SRMR = .053$). Construct reliabilities ranged from .84 to .97 and all variables exhibited convergent and discriminant validity based on Fornell and Larcker’s (1981) criteria. Additionally, preliminary analyses indicate that the data did not violate the assumptions of the general linear model. The experimental condition was accurately recalled by 92.1% of subjects. Also, perceived benefit was equal across conditions that valued the savings and upgrade incentives ($p > .45$) and subjects perceived more savings in the convenience/valued incentive conditions than for convenience alone (all $p < .05$). Valuation of incentives did not deteriorate quality, as perceptions of quality were similar across all conditions [$F_{7,201} = 0.945, p = .472$]. Thought listings were checked to determine whether the valued incentive conditions eased processing requirements (Petty and Cacioppo, 1986). As expected, results

### Table 1

<table>
<thead>
<tr>
<th>Dependent variables</th>
<th>Switching intentions</th>
<th>Additional search</th>
<th>Perceived value</th>
<th>Mediation testing value as covariate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$F$</td>
<td>$\eta^2$</td>
<td>$F$</td>
<td>$\eta^2$</td>
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<tr>
<td>Study 1 — bundle type</td>
<td></td>
<td></td>
<td>Study 1 results</td>
<td></td>
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<td></td>
<td></td>
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<td>Study 2 results</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unbundled</td>
<td>2.05*</td>
<td>.253</td>
<td>6.31*</td>
<td>.208</td>
</tr>
<tr>
<td>Bundled — convenience only</td>
<td>2.78</td>
<td>.208</td>
<td>5.75</td>
<td>.171</td>
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<tr>
<td>10% Savings discount</td>
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<td>.221</td>
<td>5.42</td>
<td>.181</td>
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<tr>
<td>Free service upgrade</td>
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<td>.234</td>
<td>5.41</td>
<td>.192</td>
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<tr>
<td>Savings — monthly valuation</td>
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<td>.201</td>
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<td>.165</td>
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<td>Savings — annual valuation</td>
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<td>Study 2 results</td>
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<td></td>
</tr>
<tr>
<td>Unbundled</td>
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<td>.206</td>
<td>5.73*</td>
<td>.173</td>
</tr>
<tr>
<td>Bundled — convenience only</td>
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<td>5.20</td>
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<td>4.84</td>
<td>.165</td>
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<tr>
<td>Free service upgrade</td>
<td>5.26</td>
<td>.197</td>
<td>4.76</td>
<td>.165</td>
</tr>
</tbody>
</table>

Notes: $\eta^2$ = partial eta-square. * $p < .05$, ** $p < .01$. 


revealed that subjects receiving valued incentives had significantly fewer thoughts (Mean_valuated = 1.62) when processing the incentive information than subjects in the non-valuated groups (Mean_non-valuated = 2.48, p < .001). Additionally, there were no differences in the number of support arguments [F(3, 263) = 0.93, p = 0.422] or counterarguments [F(3, 263) = 1.27, p = 0.283] across any of the bundled conditions, suggesting that the information processing results are independent of the valence of respondent’s thoughts.

3.4. Results

ANOVA results (see Table 1) revealed a significant effect of bundling on perceived value [F2.292 = 3.47, p < .01, partial η2 = .08], switching intentions [F2.292 = 2.16, p < .05, partial η2 = .05], and additional search [F2.292 = 2.45, p < .05, partial η2 = .06]. Consistent with H1, LSD contrasts revealed that perceived value of all bundled offers was significantly greater than the unbundled offer. In fact, the bundled conditions showed significant improvement over the unbundled condition for all dependent variables (all ps < .05). The effect of one-bill convenience accounted for the increased perceived value among the non-valuated bundles; merely offering incentives without explicit valuation yielded value perceptions equal to the convenience-only condition (all ps > .05). This is not consistent with H2.

Regarding the effect of incentive valuation on perceived value (H3), mean responses to bundles valuating the Internet upgrade (M_upgrade monthly = 3.41, M_upgrade annually = 3.56) were statistically equivalent to responses for the convenience only ad (M_convenience only = 3.37; p > .41). However, group means for both valuated 10% savings conditions (M_valuation = 3.86, M_non-valuation = 3.85) were significantly greater than the convenience only condition, (ps < .05). These results partially support H3. The period over which the incentives were valuated (i.e., monthly versus annually) had no effect on these results (ps > .61).

H4 refers to the effect of incentive valuation on search and switching intentions. Results displayed in Table 1 reveal a pattern similar to the findings observed for perceived value: the effects of the non-valuated incentives on switching and search intentions were insignificant beyond billing convenience alone (all ps > .05). Unlike the value results, however, valuation of the savings incentive did not significantly affect switching intentions (all ps > .23) or search intentions (all ps > .41) beyond the convenience only effect.

3.5. Mediation

This paper also suggests that perceived value is a mechanism by which bundling enhances switching intentions and reduces additional search. The following mediation tests support this reasoning. The initial requirements for mediation are supported by previous analyses showing that bundling affected the three dependent factors (Baron and Kenny, 1986). Two ANCOVAs were employed to complete formal mediation testing, wherein switching intentions and additional search intentions were dependent factors and value was included as a covariate. Results showed that perceived value was a significant predictor of switching intentions [F = 351.141, p < .001, partial η2 = .532] and search intentions [F = 5.832, p < .05]. Lastly, inclusion of value as a covariate in the switching intentions model reduced the effects of bundling on switching intentions [F = 0.701, p = .67] and search intentions [F = 1.962, p = .06] to insignificance. These findings indicate that perceived value mediates the effects of bundling on both switching intentions and search intentions.

3.6. Discussion

Study 1 suggests that value perceptions are the mechanism by which bundling induces switching and reduces search intentions. Moreover, results indicate that switching intentions are higher for bundled offers than unbundled offers and that bundling services can reduce additional search effort. Study 1 also sought to investigate the effects of various incentives commonly used to provoke switching. Results pertaining to the incentives are somewhat surprising. The findings suggest that combinations of convenience and cost savings or upgrades offer no advantage with respect to switching and search intentions over the mere convenience of consolidating services onto one bill. Although no improvement in switching or search intentions can be attributed to valuation of the incentives, the valuation of savings in specific monetary terms can improve perceptions of value, which is a key concern for consumers when searching for additional choice alternatives. Given the unexpected results regarding the incentives, replication of the incentive effects is the focus of Study 2. In order to give more credence to some of the null findings of Study 1, this study employs a more internally valid sample, a different method, and a new covariate. Moreover, we modify the design to ease potential concerns that switching barriers common in the telecommunications industry may influence the results.

4. Study 2

4.1. Method

Three bundle conditions (convenience-only, convenience plus cost savings, convenience plus free premium upgrade) and one unbundled condition (separate service offers) were developed for the between subjects experimental design. Questionnaires including one of four purchase scenarios were distributed randomly to 166 undergraduate marketing students at a large southeastern university in the United States. Students were removed from the sample if they indicated that they were not responsible for payment of their telecommunications bills, resulting in a final sample size of 135. Cell sizes ranged from 32 to 35.

Scenarios included either an offer for unbundled services or a bundled service package that included the switching incentives (convenience, 10% cost savings, Internet upgrade). Subjects were asked to consider a scenario in which they were subletting an apartment for the next academic term. The scenario indicated that telephone, cable, and Internet services were already established. Thus, their decision concerned an inclination to switch service providers, which may ease concerns over the possible influence of switching barriers. Subjects were asked to respond to items measuring switching and search intentions using the same items that appeared in Study 1. Frugality, a covariate relating to value-seeking tendencies, was also measured using four items (Lastovicka et al., 1999).

4.2. Preliminary results

Confirmatory factor analysis results indicated that the measurement model fit the data well (χ2 = 572.4, df = 41, CFI = .98, TLI = .97, SRMR = .075). The construct reliabilities of the switching intentions, additional search, and frugality scales were .94, .86, and .78, respectively. Moreover, the factors again exhibited both convergent and discriminant validity per Fornell and Larcker's (1981) criteria. The assumptions of the general linear model held and analysis showed that the covariate effect of frugality on the dependent measures was not significant (both ps > .22) and therefore the variable was removed from the final ANOVA models.

Checks were performed to determine the appropriateness of the manipulations. Responses indicated that each of the service bundles communicated higher savings than the unbundled group (all ps < .001), and both incentive conditions were perceived to offer more savings than the convenience only condition (ps < .05). These findings are consistent with the perceived value results observed in the first study.
4.3. Results

One-Way ANOVAs were computed for both dependant variables. Results indicated a significant difference in means for the switching intentions variable \((F_{3,134} = 22.12, p < .001, \text{partial } \eta^2 = .336)\). Results of LSD contrasts for switching intentions indicate that subjects presented with bundled service offers \((M_{\text{convenience}} = 5.48, M_{10\%\text{ savings}} = 5.20, M_{\text{upgrade}} = 5.26)\) were more inclined to switch \((\text{all } p < .001)\) than subjects receiving offers to switch to separate providers \((M_{\text{unbundled}} = 3.41)\). This result is consistent with Study 1. Regarding the effects of incentives, contrasts again showed that differences in switching intentions were not significantly higher for convenience/ savings and convenience/Internet upgrade than for convenience alone \((p > .33)\).

Regarding search intentions, ANOVA results also indicated a significant difference in means for the additional search intentions variable \((F_{3,135} = 6.78, p < .001, \text{partial } \eta^2 = .134)\). Specifically, means for subjects in bundled service conditions \((M_{\text{convenience}} = 4.98, M_{10\%\text{ savings}} = 4.84, M_{\text{upgrade}} = 4.76)\) were lower \((\text{all } p < .05)\) than subjects receiving offers to switch to separate service providers \((M_{\text{unbundled}} = 5.73)\). However, neither the additional savings nor the Internet upgrade yielded a reduction in search intentions beyond the convenience of one bill \((p > .372)\).

Overall, bundles elicited lower additional search intentions than unbundled service offers, suggesting that consumers are less likely to search for a better deal and more inclined to switch service providers for a bundle of services than for unbundled services. In both studies, there was directional support for inclusion and/or valuation of incentives, but in most cases, the results were not statistically significant beyond the convenience benefit of the bundled offers.

5. General discussion

The results of two studies provide information about the effectiveness of service bundling as a promotional tool. Specific attention is given to the nature of incentives offered to induce switching behavior and attenuate search for additional offers. Results of two independent studies suggest that bundling is an effective form of promotion for service products. Additionally, the convenience of a single bill is a powerful incentive that generates switching intentions that appear to be comparable to free upgrades and discount incentives. As a result, marketers should carefully weigh their options when promoting service products so as not to offer unnecessarily expensive incentives. Moreover, framing the offer as a valued incentive is important for impacting value perceptions but not for switching or search intentions. Thus, managers should be cautious with respect to the incentives offered and be cognizant that alternative presentations of the incentives may impact the perceived value of the deal.

The two studies presented in this research answer important questions with respect to service bundling strategies. An interesting finding in both studies was that no significant difference in switching intentions or search was identified beyond the convenience of a single invoice. At first glance, this implies that service providers can entice consumers to switch service providers by simply touting the convenience of having bundled services billed on a single statement. This finding, however, is qualified by the results of Study 1; providing an explicit valuation of the cost savings incentive increases the perceived value of the deal.

Results provide some insight into the important attributes of a services bundle. Specifically, when searching for and comparing alternatives, subjects are likely to be primarily concerned with factors directly related to perceived value. For example, they may pay close attention to the value of incentives and information regarding quality. The core value derived from bundling may be tied to the simplicity of having all of the services on one bill (i.e., the billing service). In addition, explicit valuation of the savings should be provided to enhance perceptions of deal value.

6. Managerial implications

As competition has intensified in many service industries, bundling has become an important means to increase sales, build brand loyalty, and retain customers (Owens, 2001). Bundling provides customer convenience, combines complementary services, and creates efficiencies for consumers by reducing the number of service providers with which they must do business. However, the inappropriate or unnecessary use of bundling incentives can lower firm profits (Paun, 1993). Based on the results of these studies, service firms should carefully consider the incentives offered in the promotion of bundled offers in order to maximize return.

Overall, communicating value is important when consumers are considering switching service providers. Competitors may offer service bundles to encourage switching. Thus, firms must communicate value beyond convenience and make value-relevant information easily recognizable for consumers. When consumers seek more information following a bundling promotion, information about relative prices, service quality, and the brand in general should be available.

Another important implication of this study involves the framing of the incentives. Both studies suggest that there is no difference in switching intentions garnered by savings and service upgrade offers when presented without explicit savings information. However, the study reveals that explicit valuation of savings incentives can lead to higher perceptions of deal value and that value-related information is critical to consumers’ switching decisions. It is therefore important for managers to consider how bundle incentives are framed in their offers.

7. Limitations and directions for future research

This research is limited to the domain of telecommunications services. The results may not generalize to all service industries. Also, follow-up investigations should be conducted to assess the effects of competition with comparable offers. The effects of incentives may change when consumers consider offers from several companies simultaneously. For example, if two companies offer similar bundled service packages, but one firm offers an incentive and the other offers none, there is likely to be more notable variation in switching intentions.

A study assessing consumer reactions to incentives compared to those offered to other consumers would also be a logical extension to this research. For example, a 10% discount may be perceived in a more positive light when consumers know that other customers were offered only 5%. Additionally, the impact of branding on evaluation of bundle offers should be considered. For example, if a firm offers a bundled package and consumers associate that firm with poor service, consumers may be less likely to switch regardless of any incentive offered. The value of purchasing from firms with high brand equity might also affect the marginal utility that consumers perceive from certain incentives.

The present study examined switching costs to a limited degree. However, future studies should focus on the role of switching costs in bundle decisions. In addition, similar to the examination of frugality as a covariate in the current study, future studies should examine other consumer groups, such as convenience- or variety-seekers.

8. Conclusion

Firms that exploit opportunities offered by bundling enjoy increases in market share and profits (Stremersch and Tellis, 2002). After all, the fundamental objectives for both goods and services bundling are to increase shareholder value, attract new customers, and develop stronger relationships with existing customers (Legarreta and Miguel, 2004). Along these lines, Verizon recently announced a
record low 1.3% customer churn rate and the firm added 7.5 million net customers over the previous year, which is more than any other carrier in the industry. Verizon acknowledged that its Verizon Freedom packages were instrumental to this and other recent successes (Verizon 2nd Quarter Highlights. Verizon reports continued strong quarterly results [Internet], 2006). However, misuse and poor representation of incentives can detract from overall profit maximization. This study provides a better understanding of how to present service bundle incentives while preserving the benefits of such programs.

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