To Refund or Not to Refund?

2020 saw unprecedented swathes of holiday cancellations. The year COVID-19 hit was a tough one for hospitality and tourism firms, who were forced to make swift decisions about changes to their refund policies. However, no one could clearly envisage how those crisis-induced changes would impact customer loyalty and trust. In the first study of its kind, Dr Daniel Leung and Ms Christine Seah from the SHTM looked at customer reactions to generous or self-serving refund policy changes, and whether these are shaped further by the magnitude of changes and the format in which refunds are offered. This inspiring work will help industry practitioners to optimise refund policy strategies in the future.

The Refund Rush

Without question, the COVID-19 pandemic was a brutal shock to the hotel industry. Confronted with unimaginable numbers of cancellation requests and refund claims, for the main part the industry reacted sympathetically to customers. Some hotels, such as Hilton and Premier Inn, started allowing refunds on previously non-refundable purchases during the crisis, and Expedia and Travelodge offered customers cash or vouchers to be used on future bookings. "Helping consumers in need during crises is considered to be an altruistic behaviour, even though the changes may result in financial losses", say the researchers.

However, a few companies took a more selfish path. EasyJet and British Airways, for instance, breached cancellation promises and denied their customers any refunds during the pandemic period. Negatively changing refund policies from fully refundable to partially or non-refundable might go some way to limit a firm's financial losses in the short term, but it is a rude violation of the initial promises made to customers. According to the researchers, these actions are "likely to reduce consumers' trust of the company and even their intention to repurchase products from that same company in the future".

How did these two strategically distinct crisis-induced reactions affect customer behaviours and attitudes? Until now, the effect of the "polarity" of change, that is, whether refund policy changes are positive or negative for consumers, has been left unmapped. The researchers reasoned that "if one hotel behaves egoistically and changes a policy to benefit themselves only, consumers would perceive that policy change as an unfair business practice". They predicted that this "opportunistic" behaviour would decrease consumers' trust and lower their intention to repurchase products from that company. Conversely, positive changes should increase trust and repurchase intentions.

Big and Small, Cash and Credit

Imagine your feelings on learning that you are to receive a refund, only to then find out that the refund is small, or that it comes in the format of a voucher that can only be used within the next two months. Would that token gesture be satisfactory? Previous work has considered refund policy as a "one-off" or "static" event, without fully considering the detailed characteristics of changes. "Another objective of this study was to examine the effects of the interplay of the polarity of change in refund policy, the magnitude of change in refund policy, and refund format on consumers' trust of the company and repurchase intention", explain the researchers.

Larger price reductions can boost consumers' purchase intention. After all, who wouldn't prefer a 30% over a 15% discount? Indeed, larger magnitude changes can be exponentially beneficial for companies. "One study shows that consumer spending in a store with a larger magnitude of change increases by 12%, while the corresponding figure in a store with a smaller magnitude of change increases by just 1%", report the researchers. This magnitude-of-change effect might also translate to a refund policy context. Meanwhile, refund format can also affect customer responses, whereby cash refunds are generally preferred over credit refunds. "This research complements existing literature by demonstrating how consumers react differently when a company changes its refund policy in various forms", say the researchers.

Clues from past work indicate that a large magnitude of change causes a strong "contrast effect" that drives the intensity of customer responses, be it in a positive or negative direction, whilst a small magnitude of change results in an "assimilation effect" that dampens customer responses. For companies that implement a negative change in refund policy, the researchers hypothesised that a large magnitude of change would decrease consumer trust and intention to repurchase products more than a small change. "If a company changes its refund policy positively", specify the authors, "and the magnitude of change is high (low), consumers' trust in that company and intention to repurchase products from the same company will be significantly higher (lower)".

Two Scenario Studies

In two elegant studies, participants were asked to imagine that they had made holiday plans to visit New York but were obliged to cancel their hotel reservation due to a health crisis. In study 1, the researchers looked at the effect of the polarity and magnitude of changes in refund policy. For this, 144 participants read a set of emails that were carefully constructed to reflect either a positive or negative policy change, and either a large (100%) or small (50%) magnitude of change. For example, a negative change of large magnitude was reflected by an initial booking email explaining that a refund would be possible, followed by a cancellation email stating that no refund was offered due to the crisis. In study 2, 319 participants were shown emails that reflected either a positive or negative change, as well as whether the 50% refund that was offered would be in the form of cash or credit. In both studies, trust in the company and repurchase intention were assessed using a questionnaire.

Trust and Loyalty

As expected, positive changes to refund policies resulted in higher levels of consumer trust and repurchase intentions, whilst negative changes decreased trust and loyalty. "The execution of self-beneficial actions during crises reduces consumers' trust of a company and their intention to repurchase products from that same company in the future", report the researchers. This means that hospitality practitioners should expect consumers' brand evaluation and future behaviour to deteriorate when they change their refund policies negatively in response to a health crisis.

For companies that made a negative policy change that was large in magnitude, the detrimental impacts of negative change in refund policy on consumers' trust and loyalty were magnified. This means that companies who enact negative changes should be careful to do so gently, at modest levels. "In contrast, when a refund policy is changed positively and mildly, the degree of gain becomes less evident", say the researchers. In other words, if companies are prepared to bear financial losses to favour consumers during crises, they should make sure that those positive changes are large in magnitude.

Finally, refund format impacted the influence of polarity of change in refund policy. For both negative and positive policy changes, cash refunds amplified the impact of the polarity of change in refund policy. Namely, when companies that negatively changed their policy offered cash refunds, trust and repurchase intention were lower than when credit was offered. When companies that positively changed their policy offered cash refunds, trust and repurchase intentions were higher than when credit was offered. Hence, to mitigate losses, companies that negatively change their refund policy should offer credit refunds, whereas companies that make positive changes should offer cash rather than credit refunds. "This will further enhance consumers' trust, as well as customers' intention to repurchase products from the same company in the future", explain the researchers.

Mitigating Losses

Whilst refund policies are widely embraced by hospitality and tourism business, research in this area has been lacking. This long-awaited investigation casts light on what practitioners can expect to see when they make strategic changes to refund policies. As well as keeping their heads above water, companies must strive to retain customer trust and loyalty in times of crisis. This fascinating work shows how consumers process and react to policy change, and could therefore prove to be immeasurably useful in strategic decision making about refund policy. "This research generates insights into how to adequately change refund policies in order to mitigate additional losses in the future", conclude the authors.

POINTS TO NOTE

- Changes to refund policy during a large-scale crisis significantly impact consumer trust.
- Changes that are positive for consumers, e.g. allowing refunds in a crisis, only have an effect when large in magnitude.
- Negative changes should be small to avoid reputational damage and customer loss.
- The impacts of refund policy changes on consumer trust are smaller when credit rather than cash is involved.

Leung, Daniel and Seah, Christine (2022). The Impact of Crisis-induced Changes in Refund Policy on Consumers' Brand Trust and Repurchase Intention. *International Journal of Hospitality Management,* Vol. 105, 103272.