



## The effects of Justice Oriented Service Recovery on Customer Satisfaction and Loyalty in Retail Banks in Ethiopia

**Efrem Sisay Assefa**

Debre Berhan University, Debre Berhan, Ethiopia, | email: [efremsisay@gmail.com](mailto:efremsisay@gmail.com)

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### Abstract

The principal objective of this study is to investigate the effects of justice oriented service recovery on customer satisfaction in retail banks in Ethiopia. It also attempts to assess how recovery satisfaction in turn affects customer loyalty. In order to realize the research objectives, data were collected through survey questionnaire from a total of 400 customers who have experienced service failures and recovered by the banks during the past one year. The study utilizes the instrument developed by Tax et al. (1998). Findings reveal that, perceived justice namely procedural justice, interactional justice and distributive justice were found to be positively related to recovery satisfaction. Recovery satisfaction is also positively related with customer loyalty.

**Keywords:** Perceived Justice; Service Recovery; Recovery Satisfaction; Customer Loyalty; Retail Banks



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## 1. Introduction

Service organizations endeavor towards ‘a zero defect’ service or to the ability ‘to get things right the first time’ [1, 2]. However, in all contexts, whether customer service, consumer services, or business-to-business services, service failure is inevitable [3]. Failure is inevitable as a result of the unique characteristics of the service itself i.e. specially, co-production and the inseparability of production and consumption makes it impossible to ensure 100 percent error-free services [4]. Failures happen even to the best of firms with the best intentions and even to those with world-class service system [5]. Such failures can be costly for firms, as customers often to switch to other service providers after such dissatisfactory experiences [6].

Though it is unlikely that service firms can eliminate all service failures, they can learn to effectively respond to failures once they do occur. This response is often referred to as service recovery and is defined as the process by which a firm attempts to rectify a service delivery failure [7]. A good service recovery strategy has several positive impacts. Studies have demonstrated strong links between effective service recoveries and customer satisfaction, customer loyalty, repurchase intentions, and long-term relationships [2, 6, 8].

However, developing a successful service recovery is the most difficult task for service organizations, especially when it comes to the banking industry. Data from technical assistant research programs revealed that 63 percent of customers who complained were dissatisfied

with the banks recovery efforts [9]. Similarly, [10] discovered that 61 percent of customers who complained were not pleased with the banks’ recovery efforts because they were not treated fairly and the recovery efforts were far away from adequate justice.

The above arguments reveal a general consensus in the literatures regarding the inevitability of service failures and the difficulty of developing successful justice oriented recovery strategy.

The lack of academic interest in the field of service recovery is also depicted on the limited empirical studies that have been conducted over the issue. [11, p. 15] confirmed "given the acknowledged importance of service recovery, it is surprising that so few large-scale field studies have focused on this topic." Similarly, [12, p. 121] stated, "...limited attention is given to recovery, little is known about how customers evaluates recovery efforts, what constitutes successful recovery and the potential (and limit) of recovery to convert customer dissatisfaction to satisfaction". Furthermore, [13] have suggested few empirical studies have focused on service recovery and customer loyalty. Bearing this in mind, this paper endeavors to contribute to this neglected field by investigating the effects of justice oriented recovery on customer satisfaction and loyalty in retail banks in Ethiopia. In particular, how the three dimensions of perceived justice affects customers’ recovery satisfaction and how recovery satisfaction in turn affects customer loyalty will be examined.

Based on the above argument the objectives of this research are the following;

- to examine how justice oriented recovery efforts affect customer satisfaction in retail banks in Ethiopia,
- to examine how recovery satisfaction in turn affects customers’ loyalty in retail banks in Ethiopia..

This paper is organized as follows; first, a comprehensive review of the existing literature on service recovery, justice theory, recovery satisfaction and customer

loyalty. Second, the research methodology used is provided. Third, the data analysis, hypotheses testing and the discussion of results are presented, while, finally, the conclusions along with the basic implications of the main findings of the study, its limitations and the directions of future research are offered.

## 2. Literature Review

### 2.1. Service Recovery

The necessity of service recovery is brought about by the inevitability of service failure. Service failure is inevitable due to the unique features of the service itself [3]. To effectively handle failures, organizations should develop effective service recovery programs. Service recovery is defined as the action taken by the service provider to address a customer complaint regarding a perceived service failure [14], and to pacify dissatisfied customers through appropriate actions in order to reduce potential damage to customer relationship caused by service failures [15].

### 2.2. Justice Theory

Service recovery related literature attributes the social exchange and equity theory for providing the theoretical frame work for studies exploring customers' evaluation of service recovery efforts [16]. [16] proposed that in every exchange that takes place, people weigh the inputs (the perceived contributions) against the outcomes (the perceived rewards received) and compare them with others in similar situations. In the case of service recovery, customers input could be the costs associated with a service failure such as economy, time, energy, physiological costs and physical costs [17]. The outcomes could include specific recovery tactics used such as cash refund, apology, and replacement and so on. The outcomes must be perceived to be fair or just by the customers in order for them to be satisfied with the service recovery. In the event

that there is an equal balance between the inputs and the outputs, the exchange is considered as 'fair', but if the outcomes do not meet with the person's expectations, then the result is inequity. Consequentially, Inequity is expected to result in both dissatisfaction and disloyalty.

Thus, customers often use the perceived justice component of equity theory to evaluate the service recovery effort. It will let customers determine whether a recovery attempt was fair or not. The perceived justice has three dimensions which are proposed by [18]. Its dimensions are:

- ❖ procedural justice (extent to which the policies and procedures used to achieve the final outcome are perceived as fair),
- ❖ interactional justice (extent to which one's personal interactions with a firm's employees are perceived as fair) and
- ❖ distributive justice (the extent to which the final outcome is perceived as fair).

### 2.3. Dimensions of Perceived Justice

Procedural justice focuses on the process that is undertaken to arrive at the final outcome [19]. [20] refer to procedural justice as the perceived fairness of policies, procedures and criteria used by decision makers in arriving at the outcomes of a dispute or negotiation. [18] described five elements of procedural justice including process control, decision control, accessibility, timing/speed, and flexibility. Fair procedures are consistent, unbiased and impartial representative of all parties' interest and are based on accurate information and ethical standards. Prompt strategies were much more likely to be associated with higher satisfaction and customer retention rate than their delayed counterpart. It has also been found that procedural justice is important in service recovery as consumers who might be satisfied with the type of recovery strategy offered but still could be unhappy if the process endured to seek redress were unsatisfactory [18]. However, [20] found that in a retailing setting, procedural justice (timeliness) did not

have a significant effect on customers' repatronage intentions nor their negative word-of-mouth intentions.

The second dimension of perceived justice, Interactional justice, is defined by [18, p. 62] as "dealing with interpersonal behavior in the enactment of procedures and the delivery of outcomes". Hence, interactional justice refers the manner in which the recovery process is operationalized and recovery outcomes presented. Interactional justice has been operationalized as courtesy and politeness as exhibited by personnel, empathy, effort observed in resolving the situation, and the firms willingness to provide an explanation why the situation occurred. This component of the perceived justice is essential as [20] found that people might view the procedure and outcome to be fair and yet felt being unfairly treated as a result of interactional factors. Other research has shown that the manners in which managers and employees communicate with customers [21] and efforts taken to resolve conflicts [22] affected customer satisfaction. For instance, when employees apologized for their mistakes, customers often ended up feeling more satisfied. [23] also confirmed that display of empathy, being polite and willingness to listen to customers were critical elements in service encounters. [20] also discovered that interactional justice had the strongest effect on subjects' repatronage and negative word of- mouth intentions in their experimental study.

Distributive justice, the third component of perceived justice, focuses on the specific outcome of the firm's recovery effort. In other words, what specifically did the offending firm offer the customer to recover from the service failure, and did this outcome (output) offset the costs (inputs) of the service failure [24]? Some often-quoted distributive outcomes include compensation in the form of discounts, coupons, refund, free- gift, replacement, apologies and so on [17, 18, 20]. The assessment of whether the compensation is fair may be also affected by the customer's prior experience with the firm, knowledge about how other customers were treated in similar situations and perception of the magnitude of his or her own loss [18]. [20] found that in a retail setting,

distributive justice had a significant effect on customers' satisfaction and loyalty.

## 2.4. Loyalty

[25] Oliver (1997) describes loyalty as "a deeply held commitment to rebuy or repatronage a preferred product or service consistently in the future, thereby causing repetitive same-brand or same-brand set purchasing, despite situational influences and marketing efforts having the potential to cause switching behavior" (p. 392). A service organization's long-term success in a market is essentially determined by its ability to expand and maintain a large and loyal customer base [26]. Customer loyalty has definite financial benefits since the cost to attract a new customer is significantly higher than retaining an existing one [3]. [1] also reported that a service company could boost profits by 100 percent just by increasing customer retention rate by 5 percent. Retention is believed to be a function of existing customers' level of satisfaction. Other studies have also shown that an important variable that contributes to customer and employee commitment is satisfaction [13, 27]. When a firm develops a good system of resolving customer complaints, it leads to greater customer loyalty [28]. On the other hand, [18] discovered that as dissatisfaction with complaint handling increases, commitment would decrease. Similarly, [29] also affirmed that satisfaction with service recovery had a strong impact on customer loyalty.

## 3. Research Model and Hypotheses

Based on the preceding literature review, a model linking the key variables in this study is presented in **Figure 1**. Two main categories of variables are examined in this model. Variables that affect customers' recovery satisfaction, and recovery satisfaction and loyalty

### 3.1. The Three Dimensions of Perceived Justice and Recovery Satisfaction

Previous studies have suggested that perceived justice has positive impact on customer satisfaction. [18] argue that procedural justice, interactional justice, distributive justice strongly affect customers evaluation of service recovery, and [30] also found that positive perception of procedural justice, interactional justice, distributive justice are all significantly related with service recovery satisfaction. Based on the above discussion this study proposes the following hypotheses:

**Hypothesis 1:** Procedural justice oriented recovery has positive relationship with customers' recovery satisfaction in retail banks in Ethiopia

**Hypothesis 2:** Interactional justice oriented recovery has positive relationship with customers' recovery satisfaction in retail banks in Ethiopia

**Hypothesis 3:** Distributive justice oriented recovery has positive relationship with customers' recovery satisfaction in retail banks in Ethiopia

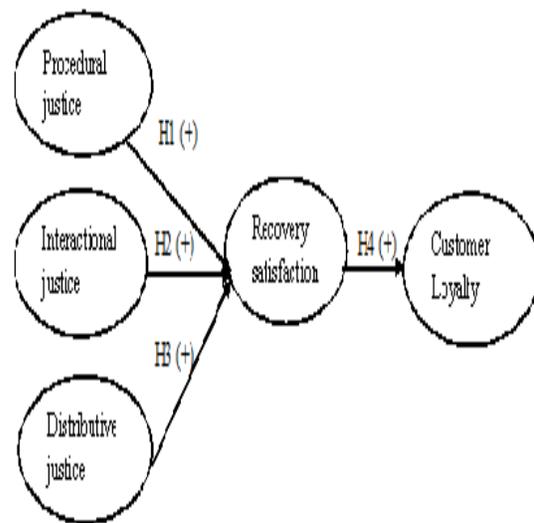
### 3.2. Relationship between Recovery Satisfaction and Customer Loyalty

It has been shown that recovery satisfaction is an important antecedent of customer loyalty. According to [30] word of mouth and purchase intentions are the result of recovery satisfaction showing that better service recovery has a significant effect on customer loyalty. [29] confirmed that effective service recovery ensures the long-term loyalty of complaining customer. Therefore, it is believed that recovery satisfaction has a significant relation

with customer loyalty, and this study proposes this hypothesis:

**Hypothesis 4:** Recovery satisfaction has positive relationship with customers' loyalty in retail banks in Ethiopia.

Figure 1: The Research Model



## 4. Research Methodology

### 4.1. Sample and Data Collection

Data were collected from customers of retail banks located in Addis Ababa, Ethiopia. The only condition for the inclusion of respondents was that they must have experienced service failure and recovered by the banks during the past one year. The respondents were approached at different branches of retail banks by 20 undergraduate students of Addis Ababa University from June to July 2012, while they were waiting for their services. The instrument used in this study was adopted from [18], and translated in to a local language – Amharic. Four linguistic professionals (i.e. two from English department and two from Amharic department) were involved in the translation

process. To make sure, whether the translation is reliable or not, back translation (translation - re - translation) was conducted and the same meaning was obtained. A total of 400 questionnaires were collected from the customers of 19 retail banks in Addis Ababa, Ethiopia.

#### 4.2. Measures

The questionnaire has five parts. The initial part of the questionnaire requested respondents to provide their background information. The second part was intended to measure the three dimensions of perceived justice using a seven point Likert scale starting from (1) “strongly disagree” to (7) “strongly agree”. The third part examined customers’ satisfaction with the bank’s recovery efforts. Customers rated their satisfaction from (1) “very dissatisfied” to (7) “very satisfied”. Finally, customers’ decision whether to stay with the bank or to switch to competitors was evaluated in the fourth part of the questionnaire on a seven point Likert scale, from (1) “strongly disagree” to (7) “strongly agree”. A total of 37 items used to capture the five constructs.

#### 4.3. Validity and Reliability

The validity and reliability of the instrument was tested using Cronbach’s alpha and the coefficient values which was at 0.910, 0.90, 0.898, 0.96 and 0.97 for procedural justice, interactional justice, distributive justice, recovery satisfaction and loyalty respectively. The instrument is considered as very valid, reliable and acceptable as the values are greater than 0.7 [31].

### 5. The Main Findings

#### 5.1. Descriptive Statistics

**Respondents’ demographics:** The total population was composed of 69.2% males and 30.8% females. The age of the majority group represented was 30-35 (29.8%). The second largest group was 36-40

(28.8%). The least respondent group was 18 – 25 (2.9%). The highest frequency monthly income was 1441 – 2300 (35.6). The lowest frequency of monthly income was less than 500 (7.7 %). For educational level, the highest number of respondents had obtained university degrees and above (55.8%), whereas only 17.3 % of respondents had an educational level of high school and below. This means that most respondents in this study were well educated. For occupation, about 29.8 % of the respondents were merchants, while only 15.4 % of the respondents were teachers.

#### 5.2. Perceived Justice and Recovery Satisfaction

Multiple regression analyses were used to establish the relationship between perceived justice and recovery satisfaction. This was followed by an examination of how satisfaction in turn could have affected customer loyalty. Specifically, all the three dimensions of perceived justice (procedural justice, interactional justice, and distributive justice) were regressed on satisfaction with service recovery. Subsequently, the impact of satisfaction on customer loyalty would be established. The complete results are tabulated in **Table I**.

The coefficient of determination ( $R^2$ ) of the first regression model was 0.837, suggesting a very good fit of the model. This confirms that, recovery satisfaction was significantly affected by the three dimensions of perceived justice (procedural justice, interactional justice, and distributive justice). In other words 83.7% of the variation on recovery satisfaction is explained by the three dimensions of the perceived justice and the remaining 16.3 % of the variance on recovery satisfaction was due to unidentified factors. The  $t$  – values were respectively, 20.509, 22.116, 17.275. These values suggest that each dimension of the perceived justice independently affect recovery satisfaction ( $t > 2$ ) [30]. The value of VIF (Variance Inflated Factors) for all dimensions was 1.000 indicating the non-existence of co-linearity. The standard beta coefficients were respectively, 0.897, 0.910, and

0.863. These confirm that interactional justice makes the strongest contribution while distributive justice contributes less.

### 5.3. Recovery Satisfaction and Customer Loyalty

Consequently, how recovery satisfaction could have affected customer loyalty was examined. The regression analysis result indicates that recovery satisfaction affects customer loyalty. The R<sup>2</sup> value was 0.237 indicating recovery satisfactions was able to explain 23.7% of the variance. This confirms that, its effect is not strong because 76.3% of the variation on loyalty explained by other factors. The t - value was 5.627. This indicates that customer satisfaction independently affects customer loyalty (t >2) [31]. The value of VIF is 1.000, implied the non-existence of co-linearity.

Table 1: model testing using multiple regression

Dependent variable	Independent variables	Beta	t	VIF	R	R 2	Sig.
Regression 1 Recovery satisfaction	Procedural justice	.897	20.509	1.000	.915*	.837	.000
	Interactional justice	.910	22.116	1.000			
	Distributive justice	.863	17.275	1.000			
Regression 2 Customer loyalty	Recovery satisfaction	.487	5.625	1.000	.487*	.237	.000

Source: summary of multiple regression analysis

### 6. Hypotheses Testing

**Hypothesis 1:** predicted procedural justice has positive relationship with recovery satisfaction in retail banks in Ethiopia. Findings of the regression analysis show that procedural justice has significant and positive relationship

with recovery satisfaction ( $\beta = 0.897, p < 0.01$ ). Hence, H1 is supported.

**Hypothesis 2:** predicted interactional justice has positive relationship with recovery satisfaction in retail banks in Ethiopia. Findings of the regression analysis show that interactional justice has significant and positive relationship with recovery satisfaction ( $\beta = 0.910, p < 0.01$ ). Thus, H2 is supported.

**Hypothesis 3:** predicted distributive justice has positive relationship with recovery satisfaction in retail banks in Ethiopia. Findings of regression analysis suggest that distributive justice is also positively related to recovery satisfaction ( $\beta = 0.863, P < 0.01$ ). Hence, H3 is supported.

**Hypothesis 4:** predicted recovery satisfaction positively related with customer loyalty in retail banks in Ethiopia. Analysis of the data also indicated that service recovery satisfaction positively related to customer loyalty ( $\beta = 0.487, P < 0.01$ ). Hence, H4 is supported. However, as it is shown in **Table 1** above recovery satisfaction has not strong positive relationship with customer loyalty, ( $R^2 = 0.237$ ) implied, only 23.7 % of the variation on loyalty explained by recovery satisfaction.

### 7. Discussions and Conclusions

The findings of this study confirm that interactional justice has significant and positive relationship

with recovery satisfaction. Compared to other dimensions of perceived justice, interactional justice has the biggest effect on satisfaction implying that customers view empathy, politeness, effort, explanation during the interaction with the service provider in the provision of financial services to be the most important component. This finding is consistent with results of previous studies suggesting that recovery satisfaction increase when higher level of interactional justice is experienced; e.g., [32] reported that customers were more satisfied when service providers were friendly and polite.

Procedural justice and distributive justice are also significantly and positively related to satisfaction with recovery satisfaction. This finding is consistent with that reported by different prior researchers where procedural and distributive justices were found to be positively related to recovery satisfaction. For instance, [10] found that hotel guests who perceived the hotel's recovery procedures to be fair were more likely to be satisfied with the outcomes of the recovery. [30] found distributive justice is significantly and positively related to satisfaction with service recovery and customers view fairness of outcome in the provision of mobile phone service to be the most important component. Similarly, [2,10] had come up with similar findings.

Findings also indicated that satisfaction with recovery is positively related to loyalty. [30] affirmed that the extent of the impact of recovery satisfaction on customer loyalty is not strong. In contrast, [32] found that satisfaction with service recovery had strong impact on

customer loyalty. The finding of this study is similar with that discovered by [30]. This study reveals that, recovery satisfaction has moderate positive relationship with customer loyalty. This is due to the perceived risk involved in the consumer decision-making process. Because services are intangible and non-standard, more risk would appear to be involved in the purchase of service than the purchase of goods [3]. Due to this reason, not all dissatisfied customer defect to competitors.

## 8. Implications

Several important managerial implications emerge from this study. First, the importance of justice oriented service recovery cannot be disregarded. In the case of the provision of financial services, it is noted that in the case of service recovery, customers are more particular of the interaction although they also care for procedural and distributive justice. Some of the interactions looked out by the respondents "very concerned employees to my problem", "polite employees", "a reasonable explanation as to why the original problem occurred", and so on. Similarly, retail banks should train their employees, specially, frontline employees to effectively handle customers complaints because front line employees (tellers) are easy to access and customers can voice their complaints with a minimum effort.

Second, although, satisfaction with service recovery positively related to loyalty, it is not strong. This implies

that retail banks should explore and implement other factors that could have strong impact on customer loyalty.

### 9. Limitations and Future Research

Although the research findings add something on the existing stock of knowledge, especially, on how justice oriented service recovery affects recovery satisfaction and loyalty in retail banks, this study just like other studies suffers from several limitations. The study is conducted based on the data obtained from a single source (i.e. customers). However, it would be better if multiple sources (i.e. both customers and managers) were used. This study is conducted on only one industry (the retail banking industry), it would be better to investigate if customers of other services would display the same behavior.

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