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Hirschman's original idea

New-formula Coca-Cola

In 1985 Coca-Cola introduced a new version of its trademark brand of soft drink. Unofficially called 'New Coke' until it was rebranded officially as Coca-Cola II in 1992, the new brand proved controversial. On its introduction the company stopped production of the original formula. Three months later, however, following protests and falling sales, Coca-Cola reintroduced the original brand under a new name, Coca-Cola Classic. What had gone wrong?

The company had seemingly done its homework. Blind tastings amongst focus groups had shown most people preferred the new formula to the old and also to its rival Pepsi. (It was that rivalry that had led to Coca-Cola's innovation, in an effort to regain customers from Pepsi.) Why did New Coke fail when it was preferred by a majority of people? The early focus group research might give some indication, for those groups often contained a vocal minority who preferred the old formula. And that vocal minority could sometimes turn focus groups away from the new drink. That is what happened nationally. Whilst sales of New Coke at first held up, there were vociferous groups of people who campaigned against it. Gary Mullins formed a pressure group 'Coca-Cola Drinkers of America' to lobby the company to reintroduce the old formula or to sell it to a new company. In the Deep South there were some street protests; bottling companies became worried and also lobbied Coca-Cola. Finally Coca-Cola announced that it would reintroduce the old formula, calling it Coca-Cola Classic, alongside the New Coke. What seemed to have happened is that some people were so upset about the new version of their favourite drink that they campaigned against it, managing to turn others against it too. This behaviour is an example of what Hirschman calls 'voice'. What really mattered to Coca-Cola of course were not the voices against their new soft drink but falling sales. Consumers stopped buying Coca-Cola and shifted to Pepsi or other soft drinks. Moving away from a brand is what Hirschman calls 'exit'. Furthermore, the story might also reveal something about the role of what Hirschman calls 'loyalty'. At the press conference announcing the reintroduction of Classic Coke, Coca-Cola stated 'the simple fact is that all the time and money and skill poured into market research on the new Coca-Cola could not measure the deep and abiding emotional attachment to original Coca-Cola felt by so many people'. It seems loyalty to the old product was an important determinant of the failure of the new one. So in one example there are all the key Hirschman concepts: exit, voice and loyalty. This book examines how they might play out in different contexts.

Exit, voice and loyalty

In 1970 the development economist Albert O. Hirschman published a short book entitled *Exit, Voice and Loyalty: Responses to Decline in Firms, Organizations and States*. The book had an immediate impact upon academia in various disciplines including political science, management and social psychology. It reached the status of a classic almost on publication (Barry 1974) and has since then been massively cited and utilized in the academy.[1]

The argument of the book is simple. When there is a decline in the quality of the production of a firm – or any organization including the state – there are two general ways in which consumers or citizens might react. They might exit from the product or they might complain about its decline. For example, imagine one likes to pop into a local bakery a few mornings a week to buy a particular cake they sell. Then one day one's regular order has changed in some way. Perhaps the owner has started baking it in a larger size, which is more than one wants with one's morning coffee. Or perhaps the price has suddenly doubled. Or maybe the cake looks the same at the regular price, but the baker has changed the mix slightly and it just doesn't taste quite the same anymore. As a consumer one might remark to the baker that you are not so keen on the new cake. You might inquire about the new mix and say you preferred the old version and ask if they are going to go back to the original recipe. Or complain that the cake is a little too much for morning coffee or that whilst you still love

[1] Inputting 'exit, voice and loyalty' to Google Scholar gives 'about 13,600' hits (May 11, 2011).

it the price is beyond your budget now. In other words, by some friendly remark or complaint, you have signalled that in your opinion the quality of the cake has declined (in taste, size or in terms of value-for-money). The point of such remarks is to suggest to the baker that she returns to the original recipe, size or price. Making the complaint might be difficult, especially if the baker has become a friend over the years, but is certainly possible. And given that one is a regular customer, especially in a small bakery, one's comment might well have an effect. The baker will want to keep customers happy.

Alternatively one might simply stop buying cakes from that bakery. If one's favourite cake is no longer on sale, or not so much to one's taste, one might try different cakes from a different bakery or shop nearby. One might choose a different type of product for the morning snack – a bar of chocolate or a jam tart – or save money by skipping sweet food with morning coffee. These are different exit options. The exit option is to withdraw one's custom from the bakery. And indeed, perhaps the voice option could only really be effective if the exit option is available as an implied threat. If the bakery is the only place that sells cakes locally, then short of stopping eating cakes altogether, one might be forced to carry on buying the less favoured cake. The baker might well prefer to keep her customers happy, but if they are willing to go on buying the new cakes she has less of an incentive to go back to the old recipe or price – especially if she makes more money than before. So voice might not be an effective option without the threat of exit, even if that threat is only an implied one.

Of course, the two responses are not direct competitors. One might try complaining first and only if the baker does not respond would one then take one's business elsewhere. Indeed if the customer has a friendly long-term relationship with a local bakery that is the most likely response. If the customer purchases his cakes in a busy supermarket where the checkout operators change frequently and so there is no personal relationship then he might be much less likely to signal his dissatisfaction through voice. If one does not have a personal relationship, then making a complaint might be more difficult, or more pertinently, making a complaint might be much less effective. Complaining at a checkout that one's favourite cakes are no longer available might receive a sympathetic response, but the checkout operator can do nothing about it. Unlike the baker, checkout operators have no control over the products on sale at the supermarket. To complain about the changed buying policy of a given supermarket the customer would have to speak to the supermarket manager; even then the local manager might have little control over the products on the shelves. Multinational supermarkets often make buying decisions at the regional level or even, for big policy decisions, at the headquarters in another country. To take one's suggestion to such a high level requires a great deal more effort than merely mentioning one's disquiet over the counter as one might do in a local bakery. And if one does make that effort with the big company one might expect a less helpful response. A local baker is highly likely to be interested in the views of one of their customers; the cake-buyer supreme of a multinational supermarket corporation is less likely to be influenced by one complaint. As the cost of voice goes up and the expected benefits go down, the exit response to quality decline becomes more likely. In these cases voice just does not seem worthwhile.

We might note also that the implied threat of exit is much greater for the local bakery than for the supermarket. A local bakery might notice the impact of one of their regular customers taking their business elsewhere; a large supermarket chain would not. Though both businesses must take the general threat of exit equally seriously – since in either case too many customers exiting could seriously jeopardize their business – the size of the customer base affects the efficacy of each individual voice or exit to change policy. Exit in the general sense, however, is the universal motor of competitive markets. The importance of this element in the Coca-Cola story is that Gary Mullins organized a campaign and the effect of his campaign snowballing into a broad movement caused the multinational company to respond.

Hirschman complicates his story by suggesting that a third variable, 'loyalty', might mediate in some manner between the two possible responses to the decline he identifies. Essentially if one is loyal to a firm, organization or state then one might be less prepared to exit than if one felt no such loyalty. So if the customer felt some loyalty to the baker, say the baker and customer had built up a friendship over the years, he might be less inclined to exit. To suddenly stop going into the baker's might be noticed, and that would affect the friendship. The customer might find himself continuing to buy cakes there even though he does not like them as much, or has discovered nicer or better-value ones in a new delicatessen nearby. Loyalty might lock one into a particular organization, even though one can see that one might be better off if one took one's custom elsewhere.

The fact that loyalty might make exit more difficult also might entail that it makes voice more likely. One might simply remain loyal to the local bakery and continue to buy cakes there (especially if it is run, say, by one's sister-in-law). Indeed, making a complaint about a business matter to a friend can be more difficult than making that same complaint to a stranger. Out of loyalty one might simply suffer in silence. Silence and non-exit, of course, are also possible responses to quality decline, and loyalty might also make these more likely than either exit or voice. It might depend on the nature of the loyalty and the nature of the product decline. The important issue for Hirschman, however, is that if the exit option seems too costly or impossible, and if the decline in quality is marked, one might get up the nerve to say something. However gently one might explore the issue, the customer notes the cakes are not the same as they once were and whilst nice, one prefers the old recipe or size. Or that one cannot buy the cakes as often as the price is a bit beyond one's means. The customer might find some other excuse for shopping elsewhere, or might simply exit. Hirschman hypothesized, reasonably enough, that loyalty makes exit less likely, and given that voice is the only other positive response possible, loyalty, on average, tends to make voice more likely. In the supermarket case the only reasonable response (given the high cost of voice) is either to suffer the change in silence or to exit. In the bakery case, exit remains an option, but voicing complaint is a real option that might work. For Gary Mullins, exiting from new-formula Coca-Cola to Pepsi did not satisfy him. Remaining loyal to old-formula Coca-Cola, he had to voice in order to try to get it reinstated.

Hirschman argues that exiting is the standard economic response to quality decline. Firms tend to respond to signals given to them by their customers. If custom drops off because their clientele chooses to purchase products from rival firms, the company must respond to those signals. They might have to reduce price if custom drops rapidly after a price hike, or return to an original size or recipe if custom falls just after an alteration in the product. In pointing out the potential signals of voice activity Hirschman was directing economists' attention to consumer response outside of the general market equilibrium models, albeit a response well known to manufacturers themselves who often pilot new brands and product changes carefully taking account of consumer feedback, and who conduct regular market research into the opinions of their customer base. Though – as the Coca-Cola example demonstrates – not always successfully.

Whilst exit and voice are two possible responses to a decline in quality in some regard, they can be used in different ways. The important element in Hirschman's book, however, is that the two responses – exit and voice – can be the result of a decline in quality, but they can be mediated or affected by the third psychological variable, loyalty, which makes exit less likely. Loyalty can be seen simply in cost terms. In this sense one's loyalty is simply a measure of how likely it is that one will exit, given the relative objective costs and benefits of voicing and exiting. We might explain the amount of loyalty we find in such a calculation of the relative costs and benefits of voice and exit by a variety of means, as we see later in this book. However, the amount of loyalty a person has might be from relative cost–benefit calculations over exit or voice behaviour. It can also be conceptualized theoretically to appear in some circumstances rather than others.

Hirschman drew a number of implications from these simple reflections on exit and voice that we will briefly consider in this opening chapter. We then turn to various applications of the argument and some problems that have been noted in the literature. First however, we consider Hirschman's own original application of his exit, voice and loyalty framework.[2]

Hirschman's puzzle

Ideas, concepts, models and frameworks in the social sciences are usually developed in order to help solve a puzzle noted by the originator. In that sense they are problem-solving devices. It is often useful or important to remember the original puzzle that motivated the creator since ideas get taken up by others and put into contexts that do not always quite fit the original puzzle. Modifications occur to ideas and concepts and they end up being used quite differently from how the creator envisaged them. As we shall see, this has happened to Hirschman's exit, voice and loyalty idea. So what was his original puzzle?

Hirschman uses the exit, voice and loyalty framework to consider the issue of introducing competition into a system of public services. In that sense, though the book was published over forty years ago its resonance is very contemporary. He wrote the book in order to defend an observation he had made about the efficiency of the Nigerian railway system he had discussed in his previous book (Hirschman 1967), which he felt could be extended to a whole realm of public services. What we refer to as his 'exit, voice and loyalty framework' was devoted to explaining a puzzle, a puzzle that is particularly pertinent to economics and the idea that competition improves the efficiency of services through the standard exit response. Hirschman noted that the Nigerian public railway system deteriorated at just the time that competition with other forms of transport was increasing. He argues that it was the availability of ready alternatives to rail transport that facilitated that decline in quality. He suggests that where there is a state monopoly in some service, such as transport or education, then, in a free and democratic society, declining quality will lead their customers

[2] We describe Hirschman's account as a framework. We take it that hypotheses can be logically drawn (and subsequently tested) from formally specified models. Hirschman's framework is not a model in that formal sense (and we examine attempts to formally model the framework in Chapter 2). However, he does draw some important hypotheses from his argument that we attempt to examine and test in this book. We term such a non-formal model a framework (Morton 1999).

to complain and these complaints will put pressure on government to ensure that the service improves. In that sense voice is the standard political response to decline in quality. However, if there are alternatives that people can choose to use instead then they are less likely to put pressure on government. So when the services of the Nigerian railway declined, their passengers did not pressurize government to do something about it; rather, many of them chose the cheaper and more immediately effective response of departing from the rail system altogether by using buses or private cars.

Without the signal of complaints the government did nothing to improve the state monopoly rail service, and as the rail service was not a private company it did not have strong incentives to respond to the exit signals. Rather, as its customer base eroded the quality of its services declined further. The general idea that underlies this account of the Nigerian railway system in the 1960s is that providing an exit option, or more generally making exit easier, might have the effect of driving out voice. If voice is a relatively ineffective process for arresting quality decline, increasing the propensity to exit will not necessarily be a bad thing; indeed it might increase efficiency gains in a given product market. However, if voice responses do have qualities missing from the exit signals then driving out voice might have an overall deleterious effect on quality by increasing exit opportunities. Hirschman notes this particularly with regard to the state-run railway systems and to state education. He suggests that those who can afford private cars are more likely to move from the railway system than those who cannot afford them. Those able to shift to cars are likely to be richer and more educated and so also those who could lobby government most effectively. Similarly, if the state education system declines, then those who are most likely to remove their children from state-funded schools are the middle and upper classes. Again, on average, it is these people who are most able to effectively vocalize their complaints to teachers and administrators within the school system. Their voice and votes are also likely to be important within the democratic system. Once those voices are lost within the state school system there are fewer incentives for teachers, administrators and politicians to arrest the decline in quality. Exit, hypothesizes Hirschman, drives out voice.

One of Hirschman's major theses in his book is that making exit easier causes voice to decline, possibly leaving behind a class of people who have no practical exit option, and are unable to voice effectively. Thus if state welfare systems – whether in transport or education, or health or whatever – start to decline causing exit they will continue to do so. This is an important implication to which we will return both theoretically and empirically in this book. Its pertinence to modern debates about ways of improving public services should be obvious, as new public management (Dunleavy and Hood 1994; Ferlie 1996; Barzeley 2001; McLaughlin *et al.* 2002), entrepreneurial government (Osborne and Gaebler 1992; Wood and Waterman 1994), public value management (Moore 1995; Stoker 2006) and choice in public services (Le Grand 2007) are pushed throughout both the developed and the developing world. He also noted various conceptual features of voice, exit and loyalty, and we will take each of these in turn, keeping in mind his primary hypothesis about exit driving out voice with regard to state-monopoly public services.

Elements of the three elements

Exit

Exit only performs the function of signalling deteriorating quality if those consumers who exit are not replaced with incoming ones. For example, the bakery's new cake might not be to the taste of the regular customer who takes his business elsewhere. But if it is preferred by other customers the bakery might not notice the departure, or if it does notice it, the loss is worthwhile for the extra gains in business. Of course, if it is truly the case that the problem is a *decline* in quality, then gaining some replacement consumers for those exiting might seem unlikely. However, our bakery example does not necessarily entail a decline. Rather the baker is offering a slightly different product, and whilst some regular customers might not like the new variant, others might prefer it. The issue of decline versus change is an important one to which we return when considering the relationships of voice and exit in empirical examples.

In order for exit to perform the signalling function that the firm can respond to, the speed of exit is important. If all consumers exited immediately and completely from a company's products then the firm might go out of business before it could respond. So the customer base needs to erode more slowly if the company is to take note, find out what the problem is and respond. Hirschman writes about the different types of consumers, whom he calls the alert and inert, and suggests both are needed for efficient signalling. An organization needs some consumers who respond fast to quality decline, some who respond more slowly and others that perhaps do not respond at all. He suggests that the exit mechanism works most efficiently with the right mix of alert and inert consumers.

The exit signal can also be difficult to interpret. For complex products like computers or cars, for example, quite why consumers stop buying one model and choose another is not obvious. Similarly, as we see in the public sector, if the exit option is used geographically by households who move from one local authority jurisdiction to another, how far these geographic exits are related to specific services on offer, or ones on offer in other areas, or whether they are the result of other considerations entirely might not be obvious to the authorities. In other words the exit signal can be very indistinct and unclear. In fact so crude is the exit signal, that when companies realize they are losing customers, often their first response is to find out the cause of the dissatisfaction. They commission voice through customer or public surveys to try to find out what the problem is. Thus exit is a dramatic signal to which competitive firms must respond, but it is not necessarily a clear one. The nuances of the problem need voice. The indistinctness of exit signals in the public sector might be even greater and whilst public authorities also commission surveys to gain greater information through voice, we argue below that these voice signals can be even more unclear in the public context.

Voice

Exit might seem to be a fairly straightforward response (though in Chapter 2 we distinguish between different types of exit). Voice is less straightforward, however. Hirschman (1970, p. 3) defines voice as 'any attempt to change, rather than escape from, an objectionable state of affairs, whether through individual or collective petition to the management directly in charge, through appeal to higher authority with the intentions of forcing a change in management, or through various types of action and protests, including those that are meant to mobilize public opinions'. We see therefore that voice is a multiform and complex response to quality decline. Again in Chapter 2 we unpack voice somewhat to distinguish different elements and forms in which it might be realized. However, we can see immediately that there could be a form of private voice – our customer complaining directly to the baker – or a more collective voice where consumers might organize a complaint to the regulatory authorities over, say, the amount of a chemical used in the baking of cakes. Hirschman somewhat privileges the latter, as he makes a direct comparison between exit as an economic response and voice as a political one. He seems to see voice very much as an interest articulation rather than as a simple complaint. However, both are important and might interact in different ways to potential ways of exiting. We explore these issues later in this book.

Exit tends to be a binary response. If one is dissatisfied one can either leave or not. Voice is more nuanced and one can not only demonstrate dissatisfaction (or indeed satisfaction) but also the degree of dissatisfaction and state what the organization can change to increase satisfaction.

Hirschman (1970, p. 31) argues that there might be negative returns to voice particularly in the political sphere. If people harass government, the state might not only not comply but become more determined not to give in to protest. Hirschman again argues that the right mix of alert and inert citizens is needed at the political level to ensure that government receives signals and that apathy does not suddenly burst forth with too much vigour. Like exit, to be effective voice must provide the signal and then allow the organization time to respond before escalating.

Voice can be a residual of exit; that is, voice becomes the only option when exit is simply impossible for, say, a monopoly supply of necessities. The degree of voice might depend upon inelastic demand or the lack of opportunity for exit. So the amount of voice would increase as the opportunity for exit decreases up to the point where exit is impossible. What should we expect to happen where exit is impossible? On the one hand, voice is the only option for change. On the other hand, if exit is impossible firms might have no incentive to respond to voice and if firms have no incentive to respond to voice then consumers have little incentive to use it in the first place. This might be the situation in non-democratic authoritarian societies. Citizens are dissatisfied, exit is almost impossible with closed borders, but government has little incentive to respond to voice demands. So the citizens suffer in silence. Of course, protest is possible even under the most authoritarian regimes, but the costs of such protest can be immense (Clark *et al.* 2007; Wright 2007). When considering the feasibility of exit and voice strategies we must always bear in mind the likely costs and benefits. We might see an example of the changing costs of voice with the opening up of Eastern Europe. Voice had been costly and so sparingly used despite great dissatisfaction with the communist regimes. With the break-up of the Soviet Union and perceived relaxation of control in communist Europe, voice flowered with many protests and eventual regime change (Hirschman 1995; Blanz *et al.* 1998; Pfaff and Kim 2003; Pfaff 2006).

Hirschman generally views voice as a complement to exit rather than as an alternative. As the implied threat of exit generally needs to underlie voice for the latter to be effective the two are not strict alternatives. Voice rather can act as an early signal for organizations to respond to before exit kicks in. But voice might be an alternative in the sense that once someone has exited then they do not have an effective voice. Voice needs to be the alternative used first, with exit as the final option (Hirschman 1970, p. 37). Table 1.1 shows a two-by-two table of the possibilities.

Category 1 occurs when the product has declined in quality and shows no sign of improving despite the consumers' voicing complaint. Exiting silently is the response of the individual who does not discern any point in