CUSTOMER SATISFACTION AND SERVICE QUALITY: CONCEPTUAL AND APPLICATION IN BANKING INDUSTRY

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Abstract

Customer satisfaction is very important particularly for banking institutions which offer similar products and services. The competitive portfolio of services suggest banking institutions to make a significant effort to improve their service quality. This article discusses concepts of customer satisfaction and service quality within banking industry to draw attention to some conceptual and application challenges for Islamic banking institutions. This article is based on a critical review of literature in this area. This paper highlights the need for sufficient information regarding customer's expectation and satisfaction in order for banking institutions to sustain in the market. It is also found that customer culture is an important factor that has impact on service quality and has an influence on customer satisfaction in the banking sector.

Keywords: *Customer satisfaction,Service quality,Islamic banking*.

INTRODUCTION

Every profit-based organization or institution needs to have a specific marketing strategy to meet the needs of a group of customers who have similarities in certain usage patterns or behaviours to attract their attention in conducting purchasing or service transactions (Lai et al 2010). Consequently, decision makers in an institution could respond appropriately based on their customers' profile, needs and expectations. Banking institutions are key players in financial market operations so that the country's economy is in good shape. Along with the current developments leading to an integrated global banking environment, there are changes in the global banking industry involving regulatory, structural and technological changes. The banking industry is now expanding across borders, offering a diversified and competitive portfolio of services as well as restructuring their services to take advantage of rapid technological change to meet the ever-changing needs of customers. The changes also affect the decisions of banking institutions that involve investment as well as high costs to provide the best service for their customers. Therefore, banks need to have information on service quality and customer satisfaction to stay in the market (Elmayar 2011).

As banking customers are not homogeneous especially in markets with customers of various ethnicities and cultures, this challenges marketers to adapt a complete marketing framework so that banks can understand and capitalize on existing market opportunities (Muhamad and Alwi 2015). It is important to know the needs of different types of customers and what similarities and differences they have. This applies to all types of banks including Islamic banks. Market research is very important for organizations that aim to develop marketing strategies in multicultural markets and it starts with understanding the culture of the target group (Emslie et al. 2007). For the banking industry that is in the same market and offers similar products and services, the quality of service is very important because the most common reason for customers to switch banks is due to poor customer service (Pont and McQuilken 2005). In addition, bank managers will try to convince customers that they provide better services than their competitors because good service quality can be a competitive resource for the institution (Ltifi et al 2016). Therefore, bank management needs to understand customer behaviour, the factors that influence customers to switch to other banks, how to retain existing customers and promote long-term relationships (Clemes et al 2010).

Islamic Banking System in Malaysia

Malaysia is one of the first countries to implement a dual banking system that operates in parallel; where conventional and Islamic products are offered simultaneously (Khiyar 2012). Initially, the introduction of the Islamic banking system in Malaysia was to meet the needs and desires of Muslims so that their financial activities are in line with religious teachings. This dual banking system creates fierce competition among banks while customers could benefit from the multiple choices provided from both systems (Aris et al. 2013). In fact, the Malaysian government plays an important role in the development and growth of Islamic banking by financing Islamic financial services banks and creating the necessary legal framework (Nasser and Muhammed 2013). The performance of the Islamic banking system in Malaysia is good and exceeds the target of 20 percent set by the government in terms of market share of assets, deposits, and financing of the banking sector (Khiyar 2012). Furthermore, there is great support from the political leadership, Parliament and the Malaysian society in general which led to the success of the Islamic financial system introduced in Malaysia.

The introduction of the Central Bank of Malaysia Act in 2009 has recognized the existence of a dual financial system in the country (Ibrahim et al. 2012). The Government efforts and initiatives to become a leader in the Islamic world are tied to its colonial and postcolonial history, the integration of religion and ethnicity, which is reflected through its endeavour to promote the country as a global hub for Islamic finance (Rudnyckyj, 2013). This is because Islam as the national religion plays an important role in the identity of the Malays and therefore becomes a foundation in the politics and culture of Malaysia (Uddin Uddin and 2012). Islam played an essential

role in the strategy development of government whereby Islamic values were utilised as guidance for society and thus created a conducive environment for economic growth (Rudnyckyj, 2013).

Muslims represent the largest population in Malaysia and most of them are Malays. This is because all Malays in Malaysia are Muslim by legal definition. Article 3 (1) defines Islam as the official religion of the country while Article 11 of the constitution gives freedom to all religions practiced by various ethnic groups. The Islamization program also saw the emergence of Islamic finance in Malaysia. The great achievement of Tabung Haji led to the establishment of a national council in 1981 with experts being involved to study the idea of establishing Islamic financial institutions in the country (Nasser and Muhammed, 2013). Islamic banking in Malaysia was incepted with the introduction of the Islamic Banking Act 1983, which then led to the establishment of the nations first fully-fledged Islamic bank which is Bank Islam Malaysia Berhad (BIMB), to provide an alternative banking system initially for the Muslims in Malaysia, which operates according to Islamic law. Under the Islamic Banking Act 1983, Islamic banking business means banking business whose aims and operations do not involve any elements which are not approved by the Religion of Islam.

In 1993, Bank Negara Malaysia (BNM) introduced the Interest-Free Banking Scheme now known as the Islamic Banking Scheme (IBS), which allows conventional banks to offer Islamic banking products and services without having to apply for an Islamic banking license. This step was required to support the expansion of Islamic banking activities and to create more players in the Islamic financial system. In 2006, Malaysia International Islamic Financial Center (MIFC) was launched to promote and position Malaysia as an international Islamic financial hub.

There are three stages in the development of Islamic finance in Malaysia (Kadir, 2009). Firstly, the foundation stage which took place between 1983-1992. This period witnessed the enactment of dedicated Acts for Islamic banking, takaful and Shariah-compliant government funding. The establishment of the first Islamic bank and takaful company in the country also took place at this stage. Secondly, the intermediate stage (1993-2000) took place where the government increased the number of players in the market to stimulate competition in the market. In 1993, the concept of Islamic windows was introduced under IBS, which meant conventional banks could offer Islamic banking products and services. In addition, in the second stage of Islamic financial development in Malaysia, the National Shariah Advisory Council and the Islamic interbank money market were established. Furthermore, all Islamic banks have their own Shariah committees to guide and ensure that the banks are operating and functioning in accordance with Shariah law and customers are relying on the information provided to be assured of compliance (Ltifi et al., 2016).

Thirdly, the advanced stage in 2001-2010 indicated market liberalization by allowing the entry of foreign banks for the integration of the international Islamic finance sector (Kadir, 2009). Among the factors that contributed to the strong growth of Islamic banking in Malaysia are the wide range of Islamic financial products, large pool of talents for the industry, a comprehensive Islamic financial infrastructure and full support from the government (Md Nawi et al., 2013). Currently, there are 16 Islamic banking institutions comprising local and foreign Islamic banks offering products and services based on Islamic principles in Malaysia. The great number of Islamic banking institutions offering Islamic products and services in Malaysia reflect the highly competitive environment in the Islamic banking industry. Furthermore, Islamic banks are competing not only among themselves but with the conventional banks as well due to the similarity of products and services such as saving accounts, current accounts, credit cards and other products and services (Naser and Pendlebury, 1997; and Naser et al., 1999).

The existence of Islamic banking institutions from foreign countries also pressures local banks to compete as they serve the same market segmentation. Wilson (1995) asserts that Islamic banking is no longer seen as a business to fulfill religious obligations, but is significantly needed to win over customers as well as to retain them. Initially, Islamic banking customers in Malaysia were mainly Muslims although recently, non-Muslims have also become major users of Islamic banking products and services in some Islamic banks (Md Nawi, 2013).

Customer Satisfaction and Service Quality for Banking Institutions

Relationship marketing suggests that the main objective of a business entity is to establish relationships and engage in interactions with customers for the long term (Kassim et al. 2009). Kotler et al define relationship marketing as the process of establishing, maintaining and enhancing strong relationships, as well as having the value of relationships with customers and other stakeholders (1999). Therefore, companies and financial institutions try to build and maintain good relationships with their stakeholders especially customers to maximize profits. Most previous studies have shown that relationship marketing orientation has positive and significant results on business performance (Widana et al 2015). Moreover, in customer relationship management (Customer Relationship Management), the most significant variables are customer satisfaction, followed by employee commitment, customer trust and customer loyalty (Kassim et al. 2009). Empirical studies also show differences between the importance of some factors compared to other factors on consumer satisfaction or dissatisfaction.

Customer satisfaction has been recognized as one of the most important theoretical and practical issues for marketers and researchers especially in the subject of customer behaviour (Molina et al 2007). Customer satisfaction is considered the key to success in a competitive banking industry and one of the key outcomes in marketing

activities (Siddiqi 2011). The advantage of relationship marketing as a strategic idea for banks is the ability to maintain a good position in the market and maintain banking relationships and long-term profits with customers (Widana et al 2015).

Customer satisfaction is a key criterion for banking institutions to assess their relationship with the market, to be an important element in strengthening the reputation of the bank, as well as a basic guide to the operating process. It is argued that long-term customer satisfaction has the potential to improve and stabilize overall profits through customer loyalty and better market position. The profit is not automatic and passive, instead it is obtained from the choices that have been made by the bank through targeted marketing (Munari et al 2013). Wilton and Nicosia see customer satisfaction as a process of subjective experience that cannot be seen as a static or measurable variable (1986).

According to McDougall and Levesque, customer satisfaction is a cognitive or affective reaction that emerges in response to a single or prolonged set of service encounters. In addition, Johnson and Fornell state that satisfaction is usually achieved when the customer assumes the performance shown is greater than the customer's expectations (1991). If the customer considers the performance to be less than their expectations, the customer will experience dissatisfaction. Kotler and Armstrong also point out that customer satisfaction depends on perceived service performance compared to buyer expectations (2006). In other words, customers will be satisfied if the performance matches or exceeds their expectations. As a result, satisfied customers will repurchase and tell others about good things (Khafafa and Shafii 2013).

Oliver offers the following definition of satisfaction, which he claims has been consistent with theoretical and empirical evidence to date; satisfaction is the response of consumer fulfillment (1996). It is a consideration that the characteristics of the product or service itself, provide satisfaction or a level of fulfillment that is less or more than expected. In addition, satisfaction is an ongoing process that encompasses the overall user experience as well as being an indication of an important process that leads to customer satisfaction (Yi and Zeithaml 1990). In the context of retail banking services, Caruana states that customer satisfaction involves a post-purchase response process, when customers are questioned about the retail banking services offered by competitors (2002). In short, satisfaction refers to the specific goals or objectives that the customer wants to achieve (Molina et al. 2007).

Few researchers stated that the benefits gained by customers through the facilities and access provided by the bank are the factors that make customers feel comfortable dealing with the bank. The ability of a bank in providing and delivering these facilities continuously to their customers will affect the level of customer satisfaction. For example, some customers have a positive attitude towards the use of ATM machines based on the perception of facilities derived from its use. The

availability of ATM machines can be an indicator of the bank's achievements as well as contribute towards a positive organizational image. However, negative perceptions of ATM machines were also acknowledged. For banking institutions in Kuwait, bank customers show most of them are satisfied with the availability of ATM machines in some locations, security of funds, ease of use of ATMs and the quality of services offered (Alhemoud 2010). While the factors that lack customer satisfaction are such as interest rates for savings and loan accounts as well as ease of obtaining loans.

Customer dissatisfaction is acknowledged to be one of the main reasons customers turn to other banks. Customers may be dissatisfied with the services provided, financial products offered, less skilled bank staff, customer service, waiting times, technology and location. Customers who are satisfied with a product or service will give positive feedback and indirectly result in positive advertising. On the other hand, dissatisfied customers will have a negative impact (Gupta and Dev 2012).

Previous studies have shown many factors that influence customer satisfaction with a particular bank. Among them, empirical studies show that customer satisfaction is influenced by seven factors namely; employee responsive nature, physical appearance or convenience, social responsibility, service innovation, positive word of mouth advertising, efficiency, and reliability (Singh and Kaur 2011). Delivery and service facilities are among the common factors used to measure the level of customer satisfaction (Saad 2012). For the banking industry, the quality of products and services is usually considered as critical prerequisite for satisfying and retaining valued customers (Mohsan et al 2011; Hoq and Amin 2010). In addition, proposed improvements in service quality, service features and handling of customer complaints may affect customer satisfaction (Levesque and McDougall 1996). Customers who are satisfied with the services of a bank can reduce the cost of bank services as there are fewer complaints to handle (Ehigie 2006).

Measuring customer satisfaction levels is considered to be reliable feedback, provide effective customer priorities and experiences, provide value and objectives, and is ultimately seen as a baseline and standard of excellence that can be applied to any organization (Arokiasamy 2013). Customer satisfaction is able to influence the performance of banks in a highly competitive environment as these banks offer similar products and services. In the Islamic banking industry, customers place customer satisfaction criteria on the quality of service provided by their banks (Hoq and Amin 2010; Dusuki and Abdullah 2007), similar to conventional banking where the offering of services is also related to customer satisfaction. For example, the convenience and competitiveness of products and services can be expected to affect overall customer satisfaction and ongoing support for banks. In addition, customer benefits such as facilities, location and competitive interest rates can affect customer satisfaction (Levesque and McDougall 1996).

Most companies or organizations do a preliminary study to find out the level of customer satisfaction. Generally, all banks that conduct surveys on the level of customer satisfaction will systematically submit the report to management. Next, the results of the survey will be sent to the branch for further action. Most banks have specialized units to regulate their customer satisfaction level monitoring activities (Munari et al 2013). For instance, a research study by Saad looked at the level of customer satisfaction in Islamic and conventional banking institutions in Malaysia (2012). The research also examines the relationship between demographic variables and customer satisfaction. The results of the study show that most customers are satisfied with the quality of service including the efficiency, friendliness, and efficiency of the staff of both banking institutions (Islamic and conventional). However, customers are not satisfied with the public transport facilities to go to the bank, the physical facilities of the bank, and the parking space facilities. In addition, there are several important links between customer satisfaction and ethnicity, age, gender and level of customer education for Islamic banking institutions.

In addition, Alsoud and Abdallah also studied the level of customer satisfaction for Islamic banking in Kuwait (2013). The findings of the study show that the majority of customers are generally satisfied with the service from their bank. However, respondents were not satisfied with the parking facilities provided, advertising and information related to the new products and services provided. For research purposes, customer satisfaction is often assessed as overall customer satisfaction or dissatisfaction during meetings with banks at all times (Fornell et al. 1996; Amin et al. 2013).

The level of service quality is a formula to measure customer satisfaction which is crucial for every organization to ensure that the organization continues to survive in the market (Khafafa and Shafii 2013). Although the quality of services varies in the industry, organizations in the same market need to look at and review their own practices as well as competitors in order to attract and retain customers (Gilbert and Veloutsou 2006). Past service-related studies emphasize the importance of quality perception and the relationship between satisfaction and service quality (Cronin and Taylor 1992). Evidence from previous studies shows that service quality leads to customer satisfaction and helps to ensure retention of existing customers and attract new customers (Metawa and Almossawi 1998). Cronin and Taylor argue that service quality is the basis of customer satisfaction (1992). In addition, service quality is one of the most important components of the customer and illustrates the great implications for customer loyalty (Malai and Speece 2005).

The best step that banking institutions can take to increase the level of customer satisfaction is to take into account all the feedback and suggestions submitted and implement the recommendations if deemed appropriate and give added value to the bank (Gupta and Dev 2012). Banks will be in a bad situation if their customers feel uncomfortable, not confident and feel unsafe using the banking services. In retail

banking, the basis of customer satisfaction is formed by service quality assessment (Levesque and McDougall 1996).

Service quality is the basis of needs and important elements in the service industry including banking for corporate profit and maintaining existence in the industry (Othman & Owen 2001). In addition, the quality of service can also be the key to competitive advantage especially in the banking industry as it provides high customer satisfaction (Almossawi 2001). Most retail banks have similarities in terms of products to each other. Thus, providing the best service to customers can offer market differentiation (Naser et al 1999). Most researchers suggest that a high level of service needs to be delivered to achieve a high level of customer satisfaction, as quality of service is often viewed as a source of customer satisfaction (Shanka 2012). Shanka points out that empirical studies show that the quality of services offered has linked with overall customer satisfaction (2012). Moreover, previous studies have found that the relationship between service quality and customer satisfaction is significant (Othman and Owen 2001; Hoq and Amin 2010). For example, customer satisfaction in the banking industry in Pakistan is strongly influenced by the quality of services provided (Mohsan et al 2011).

Thus, the quality of service has received higher attention nowadays as a result of its relationship with cost, financial performance, customer satisfaction and retention (Shanka 2012). Providing high quality services to customers is an effective approach to ensure customers are loyal to the service provider. As a result, quality of service is recognized as an important requirement to ensure that customers are satisfied and maintain their relationship with the bank (Amin et al. 2008).

DISCUSSION

Parasuraman et al. stated service quality as the difference between customer expectations of service and customer perceptions of actual service (1988). Whereas according to Zeithaml, the quality of service is a judgment from the customer on the overall excellence of the product (1988). Another definition of service quality is the extent to which the services offered can meet consumer expectations (Kasper et al. 1999). In terms of service quality dimensions in the financial services industry, various dimensions have been introduced. The most widely used model is the model Parasuraman et al (1985). Ten service quality determinants have been identified namely reliability, communication, access, physical or tangible dimensions, responsiveness, efficiency, courtesy, credibility, security, and customer understanding and knowledge. These dimensions are then codified into five dimensions: tangible, responsive, reliability, assurance and empathy dimensions known as the SERVQUAL model (Parasuraman et al. 1988).

According to the SERVQUAL model, service quality can be measured by identifying the gap between customer expectations of the service to be provided and perceptions of the actual performance of the service. Therefore, this model consists of two parts namely customer expectations and customer perceptions. However, this model has been criticized by many researchers from the field of service quality. Cronin and Taylor concluded that future research should focus on measuring customer perceptions or actual bank performance, rather than using the SERVQUAL (1992) two-tool scale approach. The use of both expectations and perceptions also resulted in longer time taken by respondents to answer the questionnaire (Malai and Speece 2005). Alternatively, Cronin and Taylor introduced the SERVPERF model. The SERVPERF model measures service quality by simply using customer perceptions, without using customer expectations and feeling that it is sufficient (1992). They also suggest that in measuring service quality, SERVPERF is better. In addition, it is also acknowledged that the dimensions of service quality may vary according to sector, country and culture (Akhtar and Zaheer 2014).

In 2001, Othman and Owen proposed the CARTER model to measure the quality of service in Islamic banking institutions by modifying the SERVQUAL model. They introduced an additional new dimension other than that proposed by the Parasuraman model. The additional dimension is "compliance" which aims to determine the bank's ability to comply with Islamic law and conduct its operations in accordance with Islamic principles. The CARTER model involves six dimensions with 34 items. The six dimensions of this model are compliance, assurance, reliability, tangibility, empathy and responsiveness. In their findings, Othman and Owen identified the importance of service quality programs in Islamic banking institutions (2001).

The conceptualization of the CARTER model dimension provides a proposal framework to measure the quality of service in Islamic banking institutions. In addition, the study also emphasizes the importance of implementing quality service programs for Islamic banking institutions (Othman and Owen 2001). According to the study of Osman et al., the motivation of Malaysians to choose Islamic financial institutions is because its operations and services are in line with their religious values (2009). This shows that adherence to Islamic principles has an important influence in the decision of customers to choose Islamic banking. These results support the Othman and Owen study conducted in 2001. In particular, compliance is in the first place, while reliability, tangibility, assurance, responsiveness and empathy are ranked second, third, fourth and fifth respectively. The study also found that the quality of service, availability of services, religious perspective, social perspective and customer confidence in banks have a great influence on customer satisfaction of banks in Malaysia.

Research by Tsoukatos and Rand shows that service expectations are also influenced by cultural and cultural profiles determining the importance of service quality dimensions to customers (2007). In addition, this study implies that culture also influences customer satisfaction through the similar position between the relationship between customer satisfaction and service quality dimension and the importance of service quality dimension.

Past studies have also shown that customer culture is an important factor that has an impact on service quality and has an influence on customer satisfaction in the banking sector (Endara et al 2019). It is acknowledged that customer perceptions differ according to different cultures (Morales and Ladhari, 2011). For example, in a country that has a collectivist society, they have a close relationship and care for each other (Endara et al 2019). If members of the community are in trouble, other members of the community will help each other. Although Asian customers are more collectively perceived or have a lower perception of service quality compared to Western customers, the impact of service quality on loyalty is stronger among Asian customers (Malai and Speece 2005). On the other hand, stronger brand value among individual customers and maintaining a strong brand image has a greater impact on ensuring loyal customers.

Notably, among the things that can be emphasized by the bank management is to evaluate the customer-related policies that have been made as well as redesign the processes and rules based on the customer's cultural profile. For example, bank management can provide appropriate training programs to their staff so that better services can be provided to the customers. It is concluded in the literature that the attitude and behavior of staff is a very important factor in generating customer satisfaction. Improving the quality of service is associated with the willingness of staff of an institution to work together. This result can be achieved through increasing employee satisfaction regarding their employment status (Munari et al 2013). Customer satisfaction is one of the sources of information to formulate strategies in meeting customer’s needs. This allows the bank to understand customer perceptions, especially emphasizing critical aspects in their relationship with customers as well as identifying areas that can be improved.

CONCLUSION

Customer satisfaction is a very important element and should be given attention by the management of banking institutions. This is because previous studies have found that customer satisfaction has a strong connection and influence on the success and profitability of an institution. Customers who are satisfied with the services or products of a financial institution will give good feedback to the people around and vice versa. Customer dissatisfaction will result in the bank losing existing customers as well as possibly alienating their potential customers due to the rumoured

reputation. Furthermore, technological changes need to be taken into account by banks as customers expect the facility to streamline their transactions and financial activities. In addition, the culture and environment of the customer must also be taken into account so that the needs and wants of each group of target customers can be met. The results from previous studies have found that banking customers are not homogeneous, especially those in the market that have diversity in terms of ethnicity, culture, religion, education and so on. Therefore, bank management should re-evaluate their relationship marketing strategies in order to meet the diversities of their customers.

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