SERVICE QUALITY AND CUSTOMER LOYALTY: THE MEDIATOR EFFECT OF CUSTOMER SATISFACTION

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ABSTRACT

Currently, the banking world is experiencing a rapid development, which leads to a fierceand tight climate of competition. With the increasing competition, maintaining customer loyalty has become increasingly difficult. Banks have to implement numerous measures including, among others, improving the quality of their services to foster customer loyalty. The objective of the study is to find out how the quality of bank services is affecting customer loyalty through customer satisfaction. A total of 316 randomly selected respondents were involved in this study. The result of the study shows that customer satisfaction acts as a mediator to the quality of bank services that will lead to customer loyalty.

INTRODUCTION

The banking industry is part of a country’s economy. In building the country’s economy, the banks are expected to take an active role in supporting the country’s development both nationally and regionally. In fulfilling its role, they need access to a number of assets, including those obtained from the country’s central bank and from their own customer or third party funds. To collect funds from a third party, the banks obviously need to put some efforts, so their customers will be willing to entrust their money to them and to foster loyalty toward the bank. Each bank will implement its innovative measures that in turn will make the competition even fiercer.

A study by Mc Kinsey Asia PSF Survey on banking and customer behavior in China shows that bank customers in China are becoming less loyal to their banks due to the offer of better products or services made by competing banks. Customers will be willing to try new products or services offered if they feel better than their main bank (Lam, K., Shu, J., & Huang, E., 2015). The study shows the importance of maintaining customer loyalty in order to win the competition.

In the service industry, service quality rendered is a crucial factor, because it is a component of the strategy that will attract new customers, retain the existing ones, and prevent customer turn over, and create a specific advantage (Parasuraman, 2002). In other words, to increase customer loyalty, an institution needs to improve the quality of its services continuously. A number of previous studies have shown that service quality definitely has an effect on customer loyalty (Jariah, 2013; Malik, Naeem, Arif, 2011; Ali, Leifu, & Rehman, 2014). To be more critical, some researchers even argue that service quality is believed, albeit indirectly, to be responsible for increasing customer loyalty.

The quality of service rendered must be able to generate customer satisfaction before it can create customer loyalty. Service quality starts by fulfilling the need of a customer and ends with shaping the customer perception (Kotler, 2005). It means that the perception of good quality will not be based on the perspective or perception of the bank, but it will be based on the customer perspective or perception. Furthermore, Tim (2002) states that one aspect of customer loyalty is the overall customer satisfaction. Based on these considerations, this study will endeavor to examine the role of customer satisfaction with respect to the quality of bank services that will lead to customer loyalty.

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Key Words:
Service quality, customer loyalty,
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Literature Review
Loyalty
Kotler (2005) defines customer loyalty as an act of repeat purchases made by a customer because of his/her commitment.
to a specific brand or bank. Whereas Caruana (2002) argue that a bank customer loyalty is a buying behavior, which is based on past experiences. These past experiences are affecting customer loyalty toward a specific bank.

Customer loyalty is quite important for banks because of the need to maintain a continuity of their business activities. In the opinion of Griffin (2005), aspects associated with customer loyalty can be grouped as follows: (1) Repeat buyer; wherein a customer is making repeated purchases of a specific product, (2) Purchasing across product and service lines; wherein the customer is not only purchasing the primary products or services, but customer also buying other products or services of the same bank, (3) Recommending to others; wherein the customer is communicating by word of mouth aspects of the product. Old customers will be talking about the superiority and advantages of the products or services to other customers, (4) Demonstrating immunity to the full of competitions; wherein the customers refuse to use alternative products or services offered by the competitors; moreover, the customers even refuse to acknowledge the existence of competing products or services.

**Customer Satisfaction**

Olsen & Johnson (2003) state that customer satisfaction is the result of delivering products or services that meet or exceed the customer’s needs. According to Kotler & Keller (2012), customer satisfaction is a feeling of satisfaction or disappointment that surfaces after comparing the performance (results) of a specific product that exceeds or falls below a previously held expectation.

According to Reichheld (2006), satisfied customers are more likely to recommend a particular bank to other prospective customers, thereby reducing the cost that must be shouldered by that bank to provide services due to fewer complaints. Studies have shown that the level of satisfaction experienced by customers regarding a bank’s products or services will affect their decision whether they will remain as customers (Amin, Isa, and Fontaine, 2011).

Wilkie (1994) states that there are five aspects of customer satisfaction; they are: (1) Expectation; i.e. when the buying process is carried out, the customer expects that the products or services that he/she receive will match his/her expectations, wishes and values. In this respect, customer satisfaction is heavily dependent on his/her previous perception and expectation, (2) Performance; wherein the customer experiences the actual performance of the products or services during its use without being affected by his/her own expectation, (3) Comparison; after utilizing the said products or services, the customer will compare the expected performance of the products or services before purchasing them with the actual performances of the products or services, (4) Confirmation; customer expectations are influenced by his/her experiences in using other products or services from a different brand or from the experiences of other customers who use a different brand as well as communication from the bank and other customer. (5) Discrepancy; it is to indicate the discrepancy between the actual performance and expectation. A negative disconfirmation occurs when the actual performance falls below the level of expectation; a wider gap may lead to a higher level of dissatisfaction. On the other hand, a positive disconfirmation occurs when the actual performance goes above the level of expectation.

**Service Quality**

In the current global competitive environment, providing quality services is considered an important strategy for the success and survival of a bank (Zeithaml, Bitner, and Gremler, 2012). Kotler and Keller (2012) define service quality as the overall characteristics and nature of a product or service, which affects its ability to satisfy some expressed or implied needs. While Grönroos (2001) defines service quality as a process that consists of a series of service activities for the customers that take place during the interactions between employees of the institution and its customers, in which the service activities are provided as a solution to customer problems.

Lee and Moghavvemi (2015) identified six aspects of service quality that are suitable for the banking industry. These aspects are used to capture customer perceptions on service quality. They are as follows: (1) Tangibles, which assess the physical/material surroundings (material, in this case includes physical facilities, equipment, and communication) and objects (e.g. bank appearance); (2) Empathy, which assesses the bank’s ability and capacity to meet the needs of each customer; (3) Reliability and Security, which measure the bank’s ability to provide accurate and secure services; (4) Price, which measures the shipping costs; (5) Online Banking, which assesses how easy it is to use the bank’s online services; and (6) Convenience, which assesses the bank’s ATM facilities, branch locations, and bank’s parking facilities.

**Framework**

Service quality is a very important component in the marketing of bank services; it will determine the success of the marketing efforts. The bank’s customers are the service users in the banking business. Customer satisfaction can only be achieved when the expected quality of the services matches service quality provided by the bank.

The banks must always strive to provide services that match the customer’s wants and needs by taking into account the various service attributes that are considered important by their customers and regularly improving the services to satisfy the customers so they will become the bank’s loyal customers. This is what H Siew-Peng Lee and Sedigheh Moghavvemi (2015) assert in their work that when a bank embeds an aspect of high quality into its services, it will reap the benefits of increased customer loyalty. Several other studies have also delved into the direct linkage between service quality and customer loyalty and found that service quality has a direct bearing on loyalty (Ainun Jariah, 2013; Malik, Naeem, Zoune Arif, 2011; Ali, Leifu, and Rehman, 2014).

**Hypothesis 1. Service quality influences customer loyalty**

Customer satisfaction can be created through service quality provided by the banks to their customers. The better service quality, the higher customer satisfaction will be towards the banks. If we were to refer to the results of some previous studies, we would see that banks, which provide good quality services, would reap the benefits of increased customer loyalty (Kheng et al., 2010; Bloemer, 1988; Yusnaint, 2010).
Hypothesis 2. Service quality has an effect on customer satisfaction

Satisfied customers are more likely to recommend a bank to other prospective customers, thereby reducing the cost that must be shouldered by that bank to provide services due to fewer complaints (Reichheld, 2006). Research has shown that the level of satisfaction experienced by customers with respect to the bank’s services would influence their decision to remain as a customer of the bank (Amin, Isa, & Fontaine, 2011). Other studies also found that the level of satisfaction has a bearing on loyalty (Chocholakova et al., 2015; Mosahab, Mahamad, Ramayah, 2010).

Hypothesis 3. Customer satisfaction affects customer loyalty

When the high quality of service has been achieved, a high level of customer trust will ensue, thus customer satisfaction will increase and lead to a high level of customer loyalty. If we were to refer to the results of the research by Akbar and Parvez (2009), we would see a positive relationship between satisfaction, trust, and customer satisfaction to customer loyalty. Among them, customer satisfaction is the most effective mediator between the service quality and customer loyalty. This research is the same as the research findings conducted by Caruana (2002) which found that customer satisfaction is the mediator variable influencing service quality on loyalty.

Hypothesis 4. Service quality influences customer loyalty through customer satisfaction

METHODOLOGY

In keeping with the objective of the study, i.e., to examine the effect of each variable, which has been classified into four hypotheses, this study will use a structural equation modeling (SEM). The 316 randomly selected respondents in the study were customers of different public banks in Indonesia, which consisted of 141 men and 175 women. The study utilizes a psychological-scale instrument, which was specifically developed by the researchers. The quality tests of the three psychological instruments yield loading factors above 0.5 and good construct reliability with the following results: bank’s service quality = 0.86, customer satisfaction = 0.90, and customer loyalty = 0.87.

RESULTS

Based on the analysis of the data research using a structural equation modeling, the following results are obtained.

Based on Figures 1 and 2, all of the manifest variables have a loading factor > 0.5 for the latent variables, and the obtained reliability of the construct for each variable is greater than 0.7. Therefore, the variables in this study have good validity and reliability.

The result of the data analysis in hypotheses 1 test shows that the service quality has a positive and significant effect on customer loyalty ($\gamma = 0.22; t > 1.96$), which means the better the quality of the bank’s services, the higher the customer loyalty will be. The result of the test on hypothesis 2 shows that service quality has a positive and significant effect on customer satisfaction ($\gamma = 0.44; t > 1.96$), which means better service quality will further enhance customer satisfaction. The result of the test on hypothesis 3 shows that customer satisfaction has a positive and significant effect on customer loyalty ($\gamma = 0.72; t > 1.96$). Then to test hypothesis 4, we will examine the result of the goodness of fit statistics that shows the following RMSEA < 0.08, NFI > 0.90, CFI > 0.90, IIF > 0.90 and GFI > 0.90; therefore, the model fits the empirical data.

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*Significant at the level of 0.05

Even though service quality has a significant direct effect, the analysis results in Table 1 show that the indirect effect is greater than the direct effect. Therefore, it can be concluded that service quality has an effect on customer loyalty through customer satisfaction.

DISCUSSION

The bank’s service quality has a positive and significant effect either directly or indirectly to customer loyalty. The degree of service quality direct influence on customer loyalty is 0.22, whereas its indirect influence is 0.32, which means the better the quality of bank’s services, the higher the customer loyalty will be. Because the direct effect of service quality on customer loyalty is lower than the indirect effect on customer loyalty through customer satisfaction; therefore, customer satisfaction in this study acts as a good mediating variable for service quality and customer loyalty variables.

The dimension that highly reflects the bank’s service quality is the online banking facilities, as indicated by how easy a customer can see the transactions histories of his/her account, whereas the dimension that most reflects the customer loyalty...
is indicated by a commitment to use Permata bank credit cards continuously. This study is in line with the research conducted by Caruana (2002) that shows how customer satisfaction plays a mediating role that influences service quality that leads to customer loyalty. The current study is also in line with the study by Respati, Yulianto and Kusumawati (2016) found that the physical condition had a significant impact on the number of people who were also pregnant, then it was significantly affected by the disease. Thus, this finding reinforces the proof of previous studies on the importance of service quality to create customer satisfaction that will have an impact on customer loyalty.

References


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