



UNLEASH POTENTIAL THROUGH EFFECTIVE SERVICE QUALITY DETERMINANTS

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ABSTRACT

This article is based on a recent research conducted in the Sri Lankan banking sector and it discusses how the results of the study can be used to unleash potential of the banking industry. Presently the use of multiple banks and switching is a common feature among the retail banking customers. Products and services offered by banks are similar, but the differentiator is the service quality and how customers perceive it. The article highlights the degrees of impact of human related factors and non-human related factors of perceived service quality on customer satisfaction. In this study over 230 retail banking customers has been used from two local private commercial banks and their branches in the metropolitan area. Findings revealed that the human related factors of perceived service quality have a greater impact on customer satisfaction than that of non-human related factors. Out of the five main service quality factors i.e Reliability, Responsiveness, Assurance, Empathy and Tangibles, this study revealed that Reliability and Responsiveness are the most influential factors on customer satisfaction in retail banking. Further analysis on the above two quality factors i.e Reliability and Responsiveness, established that their determinants, 'providing service at the promised time' and 'employee willingness to help', are the most sensitive determinants on customer satisfaction in retail banking. In addition, the above empirical investigation revealed many insights to the bankers. Therefore, this new knowledge can be used to unleash the potential in the Sri Lankan banking industry.

1 Introduction

A business cannot function without customers. The financial loss and damage to reputation that causes a business due to losing customers can be severely detrimental. Assessing the lifetime value of a customer gives an insight as to why customers matter a lot to a business, although this value varies from industry to industry. The cost of gaining a new customer is five times higher than keeping an existing one, and apart from this financial aspect, the impact of negative word-of-mouth can very often be devastating. An unsatisfied customer will in general informs at least ten people of the bad experience and is willing to talk about it to anybody who is willing to listen (Bazan, 1998). Customer satisfaction is the feeling a customer experiences when the customer's expectations are met (Chaston, 1993). Customer satisfaction demands an



objective of complete focus on satisfying the customers from all angles of the business. With the above insights on customer satisfaction, the present study is focused on the perceived service quality and customer satisfaction in the Sri Lankan retail banking sector.

There is a rapid growth and intense competition in the Sri Lankan banking industry. The products and services offered by banks are very similar in the industry, but the differentiator is the level of service quality and how the customers perceive it. Perceived service quality is the customers' overall impression of the relative inferiority or superiority of the organization and its services. Customers in the present banking environment are knowledgeable and highly demanding, due to rapidly developing information technology and advanced communication channels. The present competitive business environment facilitates customers to switch banks easily seeking better options for higher levels of satisfaction. This is a major challenge to the banks. The preliminary investigations conducted through interviews with a few senior bank managers too supported this view. It was revealed that due to stiff competition, the use of multiple banks and incidents of switching are high among the retail banking customers, and it is a common feature in the industry.

2 Service Quality and Customer Satisfaction in the Banking Industry

The potential in the banking industry can be released through high quality customer service, as per the results of this empirical investigation. The literature survey revealed that many previous studies have been conducted in Sri Lanka to explore the importance of service quality on customer satisfaction in retail banking (Wijetunga, 2003, Mallawarachchi, 2004, Wanninayaka and Dissanayake, 2007). However, no study has been conducted yet to identify the degrees of impact of the two key types of perceived service quality factors: Human Related Factors of perceived service quality and Non-human Related Factors of perceived service quality on customer satisfaction. Therefore, a knowledge gap exists in the Sri Lankan retail banking industry in the area of service quality. Such knowledge gap expose banks to the risk of not addressing their customers' issues on time effectively and efficiently. As a result, the potential of the banks are not totally dissatisfied customers switch to competitors and this affects the banks' profitability, market share, growth and stability in the long-run. Therefore, identifying the degrees of impact of key service quality determinants on customer satisfaction is vital and a timely need in the local retail banking sector. The present study bridges this knowledge gap, considering the financial and economic value of the industry in the country's economic growth.

At present, banks spend millions under their annual marketing budgets for product/service development, promotional activities, image building programs including upgrading of physical features of products, banks/branches, staff appearance etc. How effective are these measures in the long-run? Are there any better and cost-efficient approaches to achieve this goal? This paper will provide answers to these vital questions through the empirical findings of the study. It will provide insights through recommendations to the senior managers of banks, to formulate effective strategic marketing plans to gain competitive edge in the market, by increasing customer satisfaction and loyalty. Finally, the above findings will bridge a knowledge gap in the Sri Lankan retail banking sector.



3 What is Customer Satisfaction ?

According to Kotler (2006), customer satisfaction is the extent to which a product's perceived performance matches a buyer's expectations. He further argues, customer satisfaction depends on the product's perceived performance relative to a buyer's expectations. If the product's performance falls short of expectations, the customer is dissatisfied. If performance matches expectations, the customer is satisfied and if performance exceeds expectations, the customer is highly satisfied or delighted. Highly satisfied customers make repeat purchases and tell others about their positive experience with the product or services.

Oliver (1997) defines customer satisfaction as the customers' evaluation of a product/service in terms of whether that product/service has met their needs and expectations. If it fails to do so, dissatisfaction with the product/service occur. Further, 'satisfaction' is a feeling, which is a short-term attitude that can readily change in given circumstances. It is different from observable behaviors, such as product choice, complaining, and repurchase and it resides in the user's mind. Satisfaction commonly has thresholds at a lower level (under fulfillment) and at a upper level (over-fulfillment). A consumer's satisfaction may drop if he "gets too much of a good thing". Many people focus upon the lower threshold and neglect the potential for an upper threshold. Outcomes of satisfaction feelings may involve intent to repurchase, word-of-mouth and complaints. These outcomes are also moderated by other variables such as extreme dissatisfaction, where it will not necessarily generate complaint behavior, especially if the consumer believes complaining will be of no use.

4 What is Service Loyalty ?

Since the preliminary investigations of this study highlighted a management issue, i.e. customers switching banks or sign of decreasing customer loyalty in the banking industry, it is appropriate to discuss the relationship between customer satisfaction and loyalty. A strong positive relationship exists between customer satisfaction and loyalty, where the degree of influence depends on the level of customer satisfaction. That is, higher the customer satisfaction higher the loyalty and vice versa, which is a vital factor in getting the best out of the banks.

According to Gronroos (2000), it is important not to exceed the satisfaction level too much, since if it exceeds the customers' expectations, it will be even higher the next time. This will result in an up going spiral, where the risk of service failure increases. Therefore, it is important that the customer satisfaction level is increased by small steps, to avoid the risk of dissatisfied customers in the future. Later Kotler (2006) supported this view by stating that, 'smart' companies aim to delight customers by promising only what they can deliver, then deliver more than they promise. However, although customer-centric firms attempt to deliver high customer satisfaction than their competitors, they do not try to maximize customer satisfaction. Further, when it comes to service quality, efficiency and reliability are the important drivers of loyalty. Reliability is strongly correlated to satisfaction, therefore it is crucial for banks to increase customer loyalty. They further



stated, factors such as good customer contacts, being society-driven and showing empathy has indirect effect on loyalty via satisfaction and service quality.

5 What is Perceived Service Quality ?

Zeithaml and Bitner (2003) stated that, satisfaction is generally viewed as a broader concept, whereas service quality assessment focuses specifically on dimensions of service. Based on the above view, perceived service quality is a component of customer satisfaction.

Figure 1 below illustrates the distinctions between the above two concepts.

Figure 1: Perception of Quality and Satisfaction



As in above Figure 1, service quality is a focused evaluation that reflects the customer's perception of elements of service such as interaction quality, physical environment quality and outcome quality. Further, customer satisfaction is influenced by perception of service quality, product quality and price and also by situational factors and personal factors such as emotional responses, their attributions, and their perceptions of equity.

6 Importance of the Relational Quality

How customers perceive the quality of service of an organization is very much impacted by how they are approached and treated by their front-line/customer-contact employees, at different encounters with the organization. As Chaston (1993) found out, customers are reluctant to approach their banks for discussions of financial needs, because they have experienced bad relationships in less welcoming atmosphere. Personal relationships with banks are the most important factors for retail banking customers at an abstract level and the need for personal relationship increases proportionally, with the complexity of a situation.



According to Bazan (1998), there are specific events in the relationship where negative experiences often tend to occur as : Employee attitude, employee ability, lack of empathy, rules and policies, and perceptions of dishonesty. Actions to be taken against the negative factors stated above, and employee must focus on having 100% satisfied customers. Only after implementing these in a correct manner, the company could gain competitive advantage in customer relationship quality.

Service Quality - Since Marketers have recognized intense competition, they are more customer focused than ever before and continue to develop and implement marketing strategies that differentiate themselves from the competitors. 'Service quality' is one effective area for differentiation in a customer-focused, competitive environment. Parasuraman et al., (1985, 1988) defines 'service quality' as the difference between customer perceptions of the current service being provided by a given organization and customer expectations of excellent service within that given industry.

Gronroos (2000) defines 'quality' as whatever the customer perceive it to be. He points out, when it comes to service quality it is not the actual level of quality, but the level of quality the customer expects. Hence, service quality depends on the strategy of the organization, how it wants to be perceived. A customers' perceived service quality is very much impacted by how the customers are approached by, and treated by the bank's front-line, and support-employees at different encounters with the organization. The same can be applied to the banking industry. Customers perceive services in terms of quality of the service and of the overall satisfaction with their experience. Thus, companies today recognize that they can compete more effectively by distinguishing themselves with respect to service quality and improved customer satisfaction.

7 Perceived Service Quality Model

Gronroos (2000) presents the Perceived Service Quality Model for managers to understand quality through consumer behavior and the effects from comparing expectations about a positive experience of it and later evaluating it. This Model is illustrated in Figure 2 below.



Source : *Customer Loyalty and Satisfaction*



Figure 2: Perceived Service Quality Model

According to above model, experience is made up of the accumulated prior experiences of the client, and this can be split into two different dimensions : (i) Technical (outcome) dimension and (ii) Functional (process-related) dimension. In other words, technical dimension is the objective dimension or “what” customers actually receive in the interaction with the service provider and the product/service they are left with, once the interaction is completed. Functional dimension is “how” is the manner in which the product/service is delivered to the customer. Functional quality of the process is subjective since it is based on encounters with the service provider. The third step in the above model is the Image (Corporate and/or Local). This is how customers will see the organization and its methods of operation and is a major element of quality perception. Further, if the company has a good image, minor mistakes will not change customers’ perception of the company, but if the company has a bad image, mistakes will yield that customers perceive quality as bad.

The firm can either choose to focus on a technical dimension or functional dimension strategy. The former is useful when the company needs to find a technical solution to problems that competitors are not able to match. He suggests a company must not focus merely on one strategy and forget the other. Company should strike a balance between the two dimensions, since one cannot exclude the other, in order to increase perceived service quality. However, it is most common to have slightly more focus on functional quality according to Gronroos, 2000. The present study was focused on the above model and the functional dimension of the perceived service quality, since the writer was interested in finding strategies to improve the functional dimension of the perceived service quality in the local banking sector.

8 How to measure Service Quality in the Banking Industry ?

There are a number of different models to measure service quality in an organization. Service Quality Measurement Model (SERVQUAL) developed by Parasuraman et al., (1988), is a popular, multi-item scale used to measure customer perceptions of service quality in service and retail business. While there have been many different approaches or methods for measuring service quality, SERVQUAL instrument seems to have the greatest potential for applicability in different industries and sectors. SERVQUAL Model refers to five dimensions of service quality. (i) Reliability – ability to perform service dependably and accurately; (ii) Responsiveness – willingness to help and respond to customer need and provide prompt service; (iii) Assurance – ability of staff to inspire confidence and trust; (iv) Empathy – the extent to which caring individualized service is given and (v) Tangibles – physical facilities, equipment, staff appearance, etc. The above five dimensions were measured with 22 items, on a 7-point Likert scale.

The view of focusing on the functional dimension of service quality is considered as the American perspective by the scholars. According to Kotler and Armstrong (2006), there is more attention on the functional quality dimension than the technical quality dimension, particularly in the more developed economies. Kotler and Armstrong (2006) suggests that market differentiation

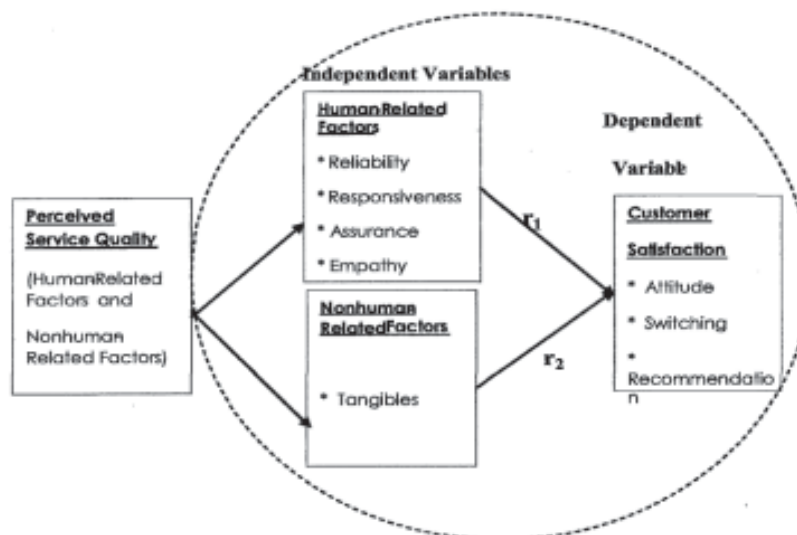


can be obtained through the way products/services are delivered; creating satisfying customer experiences about the company, employees and the delivery process; but this may not create the necessary competitive advantage for growth. They further argue that even in business environments where the competition is at the highest product level, it would be important to know the relative strengths of industry specific aspects of “what is offered?” versus “how it is offered ?” Therefore, SERVQUAL is an appropriate, widely used instrument to measure customer satisfaction through perception and expectations of service quality. The data collection instrument used in the present study was based on the above SERVQUAL instrument, since the study was focused on the functional dimension of service quality.

9 The Conceptual Model of the Study

Guided by the literature survey and the requirement of the study, the following Conceptual Model was developed. The Dependent Variable (Customer Satisfaction) and two Independent variables (Human Related Factors of Perceived Service Quality and Non-human Related Factors of Perceived Service Quality) of the study has been conceptualized based on the empirical findings of previous studies.

The Figure 3 illustrates the Conceptual Model of the study.



Formulated by the researcher, based on Zeithaml, A., and Bitner, M.J., (2003) p. 85

Figure 3 : Conceptual Model



The degree of perception and the nature (positive/negative) of the two independent variables were assumed to determine the level of dependent variable. Further, in the Conceptual Model, two correlations were assumed: (i) the correlation between Human related factors and Customer satisfaction (r_1) and (ii) the correlation between Non-human related factors and Customer Satisfaction (r_2). The study investigated the nature of these two correlations and their impact in the retail banking sector.

The sample was 230 retail banking customers from two established, private sector commercial banks/branches in the metropolitan area. Over 230 questionnaires were distributed to collect the data. The sample comprised of professionals maintaining Current Accounts or Personal Loan Accounts with the above two Banks. They were in the age group of 25 to 50 years, with an individual monthly income between Rs. 25,000/- to Rs. 150,000/-. Geographically, the sample was limited to the Metropolitan and sub-urban branches of the said banks, due to time and practical constraints in data collection. Primary data from individual customers were collected through a self-administered, structured questionnaire, consisting of 33 multiple choice questions and two open-ended questions.

10 Key Findings of the Study

- The analysis of quantitative and qualitative data of the study revealed the following key findings and that there is an issue of 'customer switch' in the retail banking sector.
- The human related factors of perceived service quality (i.e. reliability, responsiveness, assurance and empathy) have a greater impact on customer satisfaction than that of non human related factors of perceived service quality (i.e. tangibles).
- Variance in Customer Satisfaction is significantly (37.20%) explained by the functional dimension, under the above five factors: reliability, responsiveness, empathy, assurance and tangibles.
- The unexplained variance (62.80%) in Customer Satisfaction may be due to factors under Technical and Image dimensions, such as product quality, service features, price, situational factors and personal factors, which were not considered in this study.
- Reliability and Responsiveness have the greatest impact on Customer Satisfaction in retail banking.
- 'Providing service at the promised time' and 'employee willingness to help' are the most sensitive and crucial factors on Customer Satisfaction in retail banking.
- Above two determinants are also the most influential/sensitive items on CS-attitude, CS-recommend and CS-Switch in retail banking



- Only 21.71% of the total responses indicated that they were 'totally satisfied'. Responses from both banks indicated similar patterns. Majority of the responses were at 'somewhat satisfied' level (51.32%), out of which 41% belong to the age group of 31 to 40 years.
- It is important to note that 33% of the sample indicated that 'they will definitely switch' and 42% stated that 'they might switch'. These two groups accounted for 75% of the sample. Further 20% have stated they are undecided, whether to switch or not. Above results established the facts revealed at the preliminary investigations about customers switching banks.
- Similar response patterns were displayed by both banks. Out of the total valid responses, only 21.71% were totally satisfied.

However, the following limitations were identified in the above study.

- Only the functional dimension of service quality was explored, instead of all three, technical, functional and image dimensions (Gronroos,2000).
- The present study under functional dimension explained only 37.2% of the variance in Customer Satisfaction. Further 62.80% of the variance is unexplained, which needed further research.
- Sample was limited to 230 respondents and was not 100% homogeneous. Hence, can not be generalized to the entire industry.
- The study was conducted using only two local, private sector commercial banks, out of the total 23 licensed commercial banks in Sri Lanka.

11 Recommendations to Banks

Based on above key findings, the following recommendations are made to the Retail Banking sector.

1. To enhance customer satisfaction in retail banking high managerial attention should be focused on improving human related factors of perceived service quality i.e. reliability, responsiveness, assurance and empathy, than on non-human related factors of perceived service quality i.e tangibles.
2. To focus attention mainly on reliability and responsiveness, since they are the most influential factors on customer satisfaction in retail banking.
3. Priority should be given to the improvement of quality determinants, (i) 'To provide service at the promised time' and (ii) 'Employee willingness to help', since these are the



most sensitive quality determinants that have a greater impact on customer satisfaction.

4. Banks should not neglect the other quality factors, i.e. assurance, empathy and tangibles, since they too influence Customer Satisfaction in retail banking.
5. Banks should pay high attention to enhance the satisfaction level of the age group of 31 to 40 years. This group comprise of professionals and other high-ranking managers who are very influential with powerful word-of-mouth. Increasing the satisfaction level of this age group will prevent negative word-of-mouth, switching to competitors and increased cross-selling in banks.
6. In addition to functional dimension investigated above, there are two other dimensions in service quality: (i) Technical and (ii) Image quality, which influence customer satisfaction. Therefore, banks should encourage further study to investigate the influence of Technical and Image dimensions on customer satisfaction in retail banking.

12 Conclusion

Based on the above study it was empirically established that the human related factors of perceived service quality (reliability, responsiveness, assurance and empathy), has a greater impact on customer satisfaction than that of the non-human related factors of perceived service quality (tangibles) on Customer Satisfaction. It was further established that Reliability and Responsiveness are the most influential determinants on customer satisfaction in retail banking. The previous studies in retail banking has not explore the degrees of impact of the two types: human related factors and non-human related factors of perceived service quality on customer satisfaction. Therefore, the present study added new knowledge which can be practically used in managerial decisions in retail banking. Further it added many insights to the retail banking sector to increase customer satisfaction and addressed a knowledge gap in the sector. Finally it contributed to increasing the economic and financial value of the banking industry, thereby contributing to the economic growth of the country.

The banking industry is highly competitive and is very sensitive to the external changes. It is presently experiencing the financial turbulence more than ever before, due to the effects of globalization, demographic trends, regulatory shifts, modern technologies and new communication modes. The banks cannot release their full potential, unless they are aware of their customers' needs and wants. The above new knowledge on perceived service quality determinants will help the retail banking sector to unleash potential in the industry.

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