THE LINKAGES BETWEEN SERVICE QUALITY, CUSTOMER SATISFACTION, CUSTOMER LOYALTY IN MALAYSIAN ISLAMIC BANKS

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Abstract
This study attempts to examine the linkages of service quality, customer satisfaction and customer loyalty in the Malaysian Islamic banking industry. In this study, respondents are the customers (Muslim and non-Muslim customers) visiting the banks counters and have an account with one of the full-fledged Islamic banks and dual-window banks. A total of 660 questionnaires were distributed, and 440 were returned. The finding showed that the linkage between service quality and customer satisfaction is significant. The result revealed that customer satisfaction is the most important driver to enhance customer loyalty.

Keywords: Service quality; Customer satisfaction; Customer loyalty; Islam; Banks; Malaysia.

JEL Classification Codes: M31, M54.

1. Introduction
The first Malaysian Islamic bank was established in 1983 under the Banking Act 1983, which created Bank Islam Malaysia Berhad, a full-fledged commercial bank. Today, there are twelve full-fledged Islamic banks and eight dual-window banks offering products and services based on Islamic principles in Malaysia (Bank Negara Malaysia, 2008). In Malaysia, conventional banks were allowed to offer Islamic banking products and services, a bank could thus have two windows under the same roof, one for conventional banking operations and the other for interest-free transactions (dual-window banking). For example, foreign banks such as the HSBC have established Islamic banking subsidiaries that offer Islamic products through the use of Islamic windows.

Thus, Islamic banking is not merely of interest to Muslim customers but clearly non-Muslims customers see benefits from such a system. There are two full-fledged foreign Islamic banks operating in Malaysia alongside the local full-fledged Islamic banks and local and foreign dual-window banks. Consequently, the existence of foreign players in the Islamic banking industry pressures the local banks to be more innovative in order to compete aggressively in the development of products and services in the same market segmentation. As the competition increased banks began to offer products and services that differed from one another. Although, there is a difference between Islamic banks and conventional banks, they are nonetheless competing in the same market in terms of offering complementary products and services (Naser & Moutinho, 1997). In order to compete, Islamic banks probably need to develop effective marketing strategies, upgrade their technological capabilities and develop their human resources. In particular, there is a need for Islamic banks to develop and maintain better service quality, customer satisfaction, and customer loyalty.

Although previous research has attempted to examine the link between customer satisfaction and customer loyalty in the banking industry, there are still unresolved issues concerning the concepts of how to measure service quality, customer satisfaction and customer loyalty, and the relationships, especially in the Islamic banking context. Therefore, this study attempts to examine the relationship between service quality, customer satisfaction and customer loyalty for Muslim and non-Muslim customers in the Malaysian Islamic banking industry. Unfortunately, no previous research has included an empirical study related to the consumers behavioural decisions in the Malaysian Islamic banking sector, especially for Muslim and non-

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Muslim customers. This study is intended to provide the Malaysian Islamic banking sector with valuable insights for enhancing customer loyalty and thereby gain an advantage in competing in the highly competitive market of global banking.

2. Service quality, customer satisfaction and customer loyalty

The relationship between service quality and customer satisfaction has received an attention in previous study (Bolton and Drew, 1994). Although, in the literature indicate that is not very clear about distinction between service quality and customer satisfaction (Anderson and Fornell, 1994). According to Parasuraman, et. al. (1985), service quality as a comparison differentiation between the customer perception and expectation of the service and the actual performance of service received by the customer that provided by the company at the certain period time. Meanwhile, Iacobucci, et. al. (1995) concluded that the key difference between service quality and customer satisfaction is that quality relates to managerial delivery of the service while satisfaction reflects customers’ experiences with that services.

In the services literature, strong emphasis is placed on the importance of service quality perceptions and the relationship between service quality and customer satisfaction (Cronin & Taylor, 1992; Taylor & Baker, 1994). Some researchers and academics described that customer satisfaction is an antecedent of service quality (Parasuraman, et. al., 1988, 1991, Carman, 1990; Bitner, 1990), and others have counterargued that the service quality as an antecedent of customer satisfaction (Cronin and Taylor, 1992, 1994; Bolton and Drew, 1991; Anderson and Sullivan, 1993), and that service quality is not equivalent to satisfaction (Oliver, 1980). In the banking industry, bank service quality is commonly noted as a critical prerequisite for satisfying and retaining valued customers. Current research from the retail banking sector indicates that service quality dimensions appear to be linked to customer satisfaction (Jamal and Nasser, 2002, Arasl, et al. 2005a, 2005b; Al-Tamimi and Al-Amiri, 2003; Avkiran, 1994; LeBlanc and Nguyen, 1998).

In a recent study, Levesque & McDougall (1996) found that the performance of the service provider on core and relational dimensions of services was an important driver for customer satisfaction in retail banking. According to Bitner, et. al. (1994) and Anderson, et. al. (1994) also point to this link by suggesting that improved service quality will provide significant impact of customer satisfaction. The causal relationship between service quality and customer satisfaction is the subject of great academic debated and no consensus has been reached (Bahia, et. al, 2000). Nevertheless, from a theoretical point of view the researchers and academics have established the conceptual definition of customer satisfaction. Then, we develop a set of hypothesis, service quality are positively related to customer satisfaction.

In the banking market, the length of the relationship between a bank and its customers is a common feature. Customers frequently develop an attitude towards purchasing behaviour based on a prior service experience that leads to satisfaction or dissatisfaction. This attitude is a significant factor influencing customer intention to engage in positive or negative behaviour decisions. Consequently, satisfaction is a necessary prerequisite for building long term customer relationships and likely to increase loyalty (Athanassopoulos, et al. 2001; Bloemer and Ruyter, 1998). However, several studies have examined the association between customer satisfaction on customers’ behavioural intentions across all industries (Cronin & Taylor, 1992; Oliver, 1997; Fornel, 1992; Caruana, 2002; Beerli, et al. 2004; Zeithaml, et al. 1996; Boulding, et al. 1993).

Additionally, Bontis, et al. (2007) examined the causal construct between customer satisfaction and customer loyalty in the North American banking industry. The results found that the link between customer satisfaction and customer loyalty was supported. In addition, the other reasons behind customer behavioural intentions concerning loyalty and switching were strongly influenced by service quality (Zeithaml, et al. 1996; Rust and Zahorik, 1993), and service failures (Gerrard and Cunningham, 2004). According to Rust and Zahorik (1993), service quality is only one of many other variables (e.g. price, advertising and image) that influence a customer’s decision to consume the service. In this way, customers who remain loyal to service providers are likely to engage in favorable or unfavorable behavioral responses. This implies that customer satisfaction and customer loyalty are highly related. Therefore we posit that customer satisfaction has positive relationship on customer loyalty.
3. Conceptual model and hypothesis

The objective of this study is to examine the linkage of service quality, customer satisfaction and customer loyalty in the Malaysian Islamic banking context. The conceptual model is demonstrated and tested as per Figure 1. This model starts with the hypothesis that service quality has positive relationship with customer satisfaction, and customer satisfactions leads to customer loyalty. Although our literature review provides support for a direct relationship between customer satisfaction and customer loyalty there is no such claim of a direct link between service quality and customer loyalty.

![Figure 1: Hypothesis research model](image)

3.1 Research Method

Questionnaire design

The five dimensions of SERVQUAL instruments as proposed by Parasuraman, et.al (1988), Othman & Owen (2001, 2002), and Jahnoun and Al-Tamimi (2003) were adapted and modified in this study. In addition to the original SERVQUAL scale, relevant items from Islamic banking service quality scale (Othman and Owen, 2001, and Jahnoun and Al-Tamimi, 2003) are also adapted and incorporated. For example, compliance items one, two, three, and four are items from compliance aspects of the Islamic banking service quality scale (Othman and Owen, 2001). Subsequently, empathy items one, two, and three from the empathy dimension of commercial bank service quality are also incorporated in the current scale (Jahnoun and Al-Tamimi, 2003). Customer loyalty was measured by adapting scale items from Zeithaml, et al. (1996). A seven-point Likert scale was used to measure the level of service quality and customer loyalty ranging from “strongly disagree” (1) to “strongly agree (7)”. Customer satisfaction was measured by adapting scales developed from Fornell, et al. (1996), and Levesque & McDougall, 1996. In addition, to measure the customer satisfaction a seven-point scale was used ranging from “1 = very unsatisfied” to “7 = very satisfied”.

Sample

The quota sampling technique was used for this study. To develop these quotas, the researcher lists relevant control characteristics and determines the distribution of these characteristics in the target population. The relevant control of the demographic characteristics for the quota sample was determined based on the characteristics of Malaysian banking customers – 18 years old and above, male/female, Muslim/non-Muslim, education, and occupation. The sample elements within each quota were selected based on convenience sampling. In this study, respondents are customers visiting the counters of banks and have an account with one of the full-fledged Islamic banks and dual-banking systems. There are two leading full-fledged Islamic banks (Bank Islam Malaysia Berhad and Bank Muamalat Malaysia Berhad) and two dual-window banking systems (Maybank and Public Bank) involved in this study, located in eight different states of Peninsula Malaysia. Two branches in each state for the two full-fledged Islamic banks, and two branches in each state for the two dual-window banks. The respondents were from four branches in each state for each of the eight states (32 branches).

A total of 660 questionnaires were distributed, and 440 were returned (66.7 percent customer response rate). The sample characteristic includes 214 customers of full-fledged Islamic banks and 226 customers of dual-banking systems. Females comprise 46.6 and males 53.4 percent of the customers of both full-fledged Islamic banks and dual-window banks. Muslims comprise 71.1 and non-Muslim 28.9 percent of the customers of both full-fledged Islamic banks and dual-window banking systems. According to Anderson and Gerbing (1988) and Hair, et al. (2006), this sample size should be sufficient to obtain a converged and proper AMOS solution for models with three or more indicators per factor.
4. Analysis and findings

Measurement model
To assess the measurement model, two analyses were conducted. First, a first-order CFA model was conducted to examine the measurement model using AMOS 5. The purpose of a measurement model is to describe how well the observed indicators serve as a measurement instrument for the latent variables. Second, the squared multiple correlation was conducted to measure each indicator and how well an item measures a construct (al-Hawari and Ward, 2006; Holmes-Smith, 2001). The first run of squared multiple correlation showed that the majority of the measurement items indicated greater than 0.5, which indicated a good reliability level (Holmes-Smith, 2001). However five items has R² values less than 0.4. By checking the squared multiple correlations for each measurement items, there were five items have been dropped as the R² values were less than 0.4. The effect of high of R² values were indicated to acceptance of model fit. As result of this procedure, the measurement model retained of twenty one observed indicators from the original twenty six were derived to estimate the model fit.

To test the reliability of the Malaysian Islamic banking service quality instruments, the Cronbach’s alpha coefficient was computed. The coefficient alpha exceeded the minimum standard of 0.70 (Nunnally & Bernstein, 1994) indicated providing good estimates of internal consistency reliability. The coefficient alpha obtained are greatly exceeded the minimum acceptable values which are 0.75, 0.79, 0.82, 0.84, 0.83, 0.77, respectively (tangibles, reliability, responsiveness, assurance, empathy, and compliance with Syariah). The estimates of standardize factor loadings were used to the determine validity of the SERVQUAL dimensions. The factor loadings in the confirmatory factor analysis ranged from 0.56 to 0.89 for the SERVQUAL dimensions. Because each factor loading on each dimension is more than 0.50, the convergent validity for each dimension of the SERVQUAL scale was established and providing evidence of construct validity (Hair, et. al, 2006).

A re-run CFA was conducted, and the results of measurement model shown were the goodness-of-fit was satisfied. Although, the GFI value of 0.89 did not meet the threshold of 0.90, but the value was very close to the threshold recommended level. The RMSEA value of 0.07 and CFI value of 0.92, and the values were above the threshold level of 0.08 and 0.90. The results of model fit indicated that the twenty one indicators of first-order CFA model of Islamic banking service quality were fit to the sample data.

Structural equation modelling
A structure model of Islamic banking causal relationships between service quality, customer satisfaction and customer loyalty were conducted to estimate the parameters. In this model, there were six models from the measurement model constructs (tangible, reliability, responsiveness, assurance, empathy, and compliance), and three second-order construct (service quality, customer satisfaction and customer loyalty).

According to our hypothesis (see Figure 1), results of the research model indicate that the acceptable goodness-of-fit models (Table 1). The chi-square is significant (χ² = 1059.823, χ² / degree of freedom (χ² / df)) ratio 2.888, ρ = 0.000, which is expected given the sample size. Although, the GFI value of 0.85 and AGFI value of 0.82 did not meet the threshold of 0.90, their values were in range the recommended levels. The model had a CFI of 0.92 and NFI of 0.89 indicated that the model is parsimonious, since the value of close to 0.90. According to Bentler (1990) and Hair, et. al, (2006) suggested that both CFI and NFI should be the index of choice, and these were consistent in suggesting that the hypothesized model represented an adequate fit to the data. Even if the model fits the data, it is not necessary the correct model. Many equivalent models can fit the data equally well as judged from any goodness-of-fit measure (Anderson and Gerbing, 1988).

Meanwhile, the model had a RMSEA of 0.06, which were below range level and considered a good absolute fit of the model. Overall, the values were close to the threshold and thus they represented an acceptable model fit and hypothesis was supported. The model indicated that each dimension of perception Islamic banking service quality had a positive relationship with Islamic banking service quality. It means that SERVQUAL model is still an acceptable and useful instrument to measure service quality in Malaysia’s Islamic banking industry.
Table 1: Goodness-of-fit statistics for modified and initial model

<table>
<thead>
<tr>
<th>Variables</th>
<th>GFI</th>
<th>CFI</th>
<th>$\chi^2$ / df</th>
<th>RMSEA</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Measurement model</td>
<td>.89</td>
<td>.92</td>
<td>3.274</td>
<td>.07</td>
<td>.000</td>
</tr>
<tr>
<td>Structured model</td>
<td>.85</td>
<td>.92</td>
<td>2.888</td>
<td>.06</td>
<td>.000</td>
</tr>
</tbody>
</table>

Notes: Measurement model = 21 items., Structure model = 29 items

Table: 2. Standardized regression weights for the research model

<table>
<thead>
<tr>
<th>Description</th>
<th>Estimate</th>
<th>p-values</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tangible ← Service Quality</td>
<td>.931</td>
<td>0.000</td>
</tr>
<tr>
<td>Reliability ← Service Quality</td>
<td>.998</td>
<td>0.000</td>
</tr>
<tr>
<td>Responsiveness ← Service Quality</td>
<td>.914</td>
<td>0.000</td>
</tr>
<tr>
<td>Assurance ← Service Quality</td>
<td>.897</td>
<td>0.000</td>
</tr>
<tr>
<td>Empathy ← Service Quality</td>
<td>.966</td>
<td>0.000</td>
</tr>
<tr>
<td>Compliance ← Service Quality</td>
<td>.245</td>
<td>0.000</td>
</tr>
<tr>
<td>CS ← Service Quality</td>
<td>.806</td>
<td>0.000</td>
</tr>
<tr>
<td>CL ← CS</td>
<td>.721</td>
<td>0.000</td>
</tr>
</tbody>
</table>

Notes: (CS=Customer Satisfaction), (CL= Customer Loyalty), Significance at the 0.01 level

The standardized parameter estimates and significant values for the hypothesis relationships are presented in Table 2. The findings suggest that the standard model of Islamic banking service quality dimensions is good determinants of customer satisfaction and customer loyalty. The standardized regression weight of Islamic banking service quality to customer satisfaction and customer loyalty were significant ($p=0.000$, $\alpha=0.01$) with parameter estimates (0.806, 0.721). These regression weights explain the degree of association between the construct and the manifesting variables. In other word, if service quality increased by 1 standard deviation, the standard deviation of customer satisfaction and customer loyalty would have increased by 0.806 and 0.721.

5. Discussions and conclusions

The findings of this study indicate that for the establishment of higher levels of service quality will leads for customer has a high level of satisfaction. As a result, these indicate that service quality is positively associated with customer satisfaction in Malaysian Islamic banking. Furthermore, these relationships showed that the indicators were used in this study able to explain the concept of customer satisfaction. In addition, the findings of this study is consistent with previous studied by Othman and Owen (2001) stated that there was strong link between service quality and customer satisfaction in Islamic banking. Arasli, et. al, (2005a, 2005b) found was service quality to be significant predictors of customer satisfaction in Turkey banking industry. In China banking industry foud that service quality leads to customer satisfaction (Zho, 2004).

With respect to the direction of the relationship between customer satisfaction and customer loyalty, our model demonstrates that there is a positive and statistically significant relationship in this link, and that the hypothesis was supported. These links indicate that factors such as customer intention to say positive things about Islamic banks to other people; willingness to recommend family and relatives; recommend Islamic banks to someone who seeks advice; and do more business with Islamic banks emerged as the most significant predictors of customer loyalty. Interestingly, results of the study clearly demonstrated that Muslim and non-Muslim customers loyalty to Islamic banks was influenced by the customer satisfaction dimension. This results consistent with previous study conducted in banking industries (Caruana, 2002; Yavas, et. al, 2004; Bloemer dan Ruyter, 1998; Fornell, 1992; Zeithaml, et. al, 1996). In banking context, although there was recognised that service quality and customer satisfaction playing important role in enhancing long term relationship between customers and banking, but the customer dimension showed the better predictors to customer loyalty (Fornell, 1992; Nguyen dan LeBlanc, 1998; Bontis, et. al, 2007; Yavas, et. al, 2004).

6. Implication and future research

The results of the study explain that Islamic banking customers are loyal customers, but the propensity of customers to switch to other banks is always available. If customers become dissatisfied due to more than one incident, they may have a stronger desire to switch, even if there are high switching costs (Gerrard and
Cunningham, 2004). However, Islamic banks must recognize that customers’ tendency to switch to competitors may be caused by dissatisfaction or the attractiveness of programmes offered by competitors in providing better quality services or product varieties as well as for seeking high profit. Therefore, Islamic banks should create extended strategy relationships with identifiable customer’s that offer special benefits to both parties. This might be a good strategy to prevent customers from switching to competitors. The current study adds to previous findings and clearly shows that poorer relationships lead to increased potential for switching (Chakravarty, et al. 2003), and in retail banking, customer dissatisfaction with their banks leads to low loyalty and defection (Holmlund and Kock, 1996). In addition, the management of Islamic banks should be aware that the strength of customer relationships may vary over time as customers become more experienced with their bank. Therefore, Islamic banks have to respond proactively and listen to customer concerns to overcome customers’ wants and needs. The process starts by identifying and targeting the right customers, where customers often differ widely in terms of needs and values.

This study is being conducted based on the confirmatory factor analysis instruments that the instruments of service quality may differ from exploratory study. Further research should be considered to conduct exploratory study to gather more information regarding the service quality, customer’s satisfaction and customer loyalty dimensions in context of Malaysian Islamic banking industry. The potential of the inaccurate data collection exists due to the questionnaires that were distributed through the branch managers. For further research, the researchers need to increase the number of banks involved in the research study, the number of respondent, and the research should represent the whole Malaysia.

References


