Drivers of Service Quality and Customer Satisfaction in Kathmandu Valley

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Abstracts

Customer satisfaction is essential for businesses to encourage them to share positive responses in buying products. It stands as a crucial factor in determining long-term success of any organization reflecting the extent to which their offerings satisfy customer expectations. The economic progress and business success rely on customer satisfaction affected by the empathy, assurance, responsiveness, tangibility, reliability etc. especially in banking sector. Therefore, this study examines how bank customers perceive service quality and impact on their satisfaction. It utilizes a descriptive and causality research design to explore the relationship between drivers of service quality and customer satisfaction based on primary survey data from Kathmandu valley. This paper concludes reliability, assurance, tangibility, empathy, and responsiveness as service quality drivers play a significant role in shaping customer satisfaction within the banking sector. Notably, tangibility, assurance, and empathy stand out as key influential drivers in determining customer satisfaction level in commercial banks within Kathmandu valley. The significance of this research lies in its relevance to policymakers in the banking sector, urging them to develop and execute diverse bank policies aiming to enhance customer satisfaction, thereby fostering the business and economic success of commercial banks in Nepal.
Introduction

In today's fiercely competitive and globalized business landscape, achieving high levels of customer satisfaction in the service sector presents a significant challenge. As noted by Patterson and Spreng (1997), satisfaction plays a pivotal role in attracting customers. Mittal and Kamakura (2001) observed customer satisfaction is a crucial determinant for customers to make purchases, and satisfied customers are more inclined to share positive feedback. Leveraging knowledge about customer satisfaction, Kumar and Reinartz (2006) argued customer satisfaction is essential for establishing and sustaining long-term relationships with customers and ensuring competitiveness.

Customer satisfaction serves as a barometer for evaluating whether a firm's products and services meet customer expectations (Boonlertvanich, 2011). It also serves as an indicator of whether customers are likely to make repeat purchases and exhibit loyalty. Given the paramount importance of customer satisfaction, banks must diligently analyze and nurture robust relationships with customers to ensure their satisfaction.

In the investigation of service quality and customer satisfaction, Parasuraman et al. (1988) analyzed five key dimensions namely tangibility, reliability, responsiveness, assurance, and empathy of service quality in the banking sector to assess customer satisfaction and revealed positive insights of these drivers in customer satisfaction. Among these dimensions, Johnston (1997) underscores the significance of responsiveness in ensuring customer satisfaction and loyalty. Customer satisfaction serves as a mediator that links the drivers of service quality to customer loyalty (Caruana, 2002). A positive relationship is observed among the service quality drivers, loyalty and customer satisfaction in the banking industry (Veloutsou et al., 2004).

Customer satisfaction has a measurable impact on various aspects of a firm's performance mostly in the financial performance (Chalmeta, 2006), purchase intention of customers (Carter, 2010), customer retention (Voss & Voss, 2008), as well as competitive dynamics, incentive offerings, product innovation, and the adoption of technology (Mohammad, 2015).
In today's contemporary business landscape, the desires, needs, and expectations of customers evolve rapidly. Without a clear understanding of customers' expectations, banks cannot deliver superior service. Customer expectations can be discerned by assessing their satisfaction levels (Jham & Khan, 2009). Various factors influence the degree of customer satisfaction, necessitating identification and analysis for effective customer satisfaction.

The economic progress and development of any nation are heavily influenced by the advancement of financial markets as well as financial institutions. In Nepal, most of economic and financial activities are impacted by the evolution and expansion of modern banking system. Retail banking offers a diverse range of services to customers. Over the past three decades, Nepal has experienced rapid expansion, reforms, and growth in its banking system, driven by government policies promoting liberalization and privatization. However, challenges such as unfair competition, technological advancements, governmental instability, policy changes, customer demands, and environmental shifts pose economic uncertainties and obstacles for the Nepalese banking sector. In response, Nepalese banks must develop robust plans, policies, and strategies to provide high-quality services to customers, fostering loyalty by addressing the key service quality drivers of customer satisfaction.

Previous researches regarding this issue have predominantly focused on developed countries, but, limited attention is given to similar studies in developing nations. While some research has explored the drivers of service quality and customer satisfaction in developing countries, scope remains minimal. Nepalese firms, like many others in developing nations, confront significant challenges stemming from dynamic and globalized environmental factors, impacting their survival, expansion, and performance. Despite the wealth of both theoretical and empirical studies about the service quality drivers and customer satisfaction in both the developing and developed economies, there remains a prominent gap of similar researches in under-developed country like Nepal. Consequently, this paper seeks to address this gap by examining the influence of service quality drivers on customer satisfaction to investigate the explaining power of these service quality drivers to predict customer satisfaction in Nepalese banks within Kathmandu valley.
The primary aim of this study is to assess the service quality drivers influencing customer satisfaction in bank sector. Specific objectives of the research are: (a) to describe the service quality drivers and customer satisfaction in commercial banks; and (b) to investigate how service quality drivers such as empathy, assurance, responsiveness, tangibility, reliability impact on customer satisfaction of commercial banks in Kathmandu valley.

The rest of the paper is structured into four parts. The second section provides a brief overview of relevant literature exploring how service quality influences customer satisfaction. Section three outlines the methodology employed in this study. In section four, the results and discussion of the research are presented. Finally, section five offers conclusion and implication based on the results presented in this paper.

Literature Review

The enhancing service quality makes customer more loyal and satisfaction that is crucial for the success of service-related industries. Parasuraman et al. (1988) utilized multifaceted scale to assess the perceptions of service quality and observed banking industry emphasizes customer satisfaction for organizational effectiveness and success. The finding suggests drivers of service quality are significant factors in enhancing customer satisfaction in the banking sector. Andreassen (1994) investigated customer loyalty, satisfaction, and reputation, particularly emphasizing customer orientation and suggested customers’ loyalty stems by reputation and image leads more customer satisfaction that accelerates financial performance in service sector. Heskett et al. (1994) introduced Service Profit Chain model. This model explores relations among customer satisfaction, loyalty, profit, growth, and values through job satisfaction, loyalty, and productivity of organizational employees. Finally, result confirms service quality leads to customer satisfaction and subsequently increases their loyalty toward organizations.

In investing the moderating impact of customer characteristics, Mittal and Kamakura (2001) employed a conceptual framework for assessing satisfaction ratings and repurchase behavior in a comprehensive study and highlighted that customer satisfaction plays a pivotal role in influencing customers' intentions for future purchases and satisfied customers are inclined to share their positive experiences with others. Ravichandran et al. (2010) employed descriptive method
utilizing SERVQUAL framework, to examine the influencing power of service quality to explain customer satisfaction and revealed customer satisfaction holds significant role specially in service sectors like banking industry because there is direct association of customer satisfaction with loyalty and firm's goodwill.

Customer satisfaction serves as a metric to gauge whether the products and services provided by a company meet or surpass customer expectations. It acts as an indicator of whether customers are likely to make repeat purchases and exhibit loyalty (Boonlertvanich, 2011) and the finding concludes that the sense of contentment derived from fulfilling customers' goals contributes to enhancing customer satisfaction.

In the investigation of the drivers of service quality, Wilson et al. (2012) developed a theoretical framework that integrates service quality, customer satisfaction, and loyalty into a cohesive structure. This model reveals service quality drivers (such as reliability, responsiveness, assurance, empathy, and tangibility) collectively contribute to overall service quality. The finding concludes personal as well as situational factors, product attributes and price influence customer satisfaction.

In today's competitive landscape, it is crucial for various service sectors to effectively address customer needs, leading many service providers to shift their focus from products to customers (Badara et al., 2013). Lau et al. (2013) utilized the SERVQUAL framework to evaluate the factors influencing service quality in banking sector, encompassing reliability, assurance, tangibility, empathy, and responsiveness. Their findings highlighted the significance of responsiveness, particularly in providing assistance to the customers promptly and accurately. Results show that many banks endeavor to tailor their services according to each customer's needs and personalize services, which in turn enhances customer satisfaction. Customers seek assurance from banks. Therefore, staffs of banks must thoroughly explain all products and services to customers to ensure their comfort with banking services. Ultimately, the study concludes that bank employees should treat each customer individually to demonstrate empathy, recognizing the uniqueness of each customer.
Virima and Sandada (2019) applied multiple regression technique to examine the impact of drivers of service quality such as empathy, tangibility, responsiveness, reliability, price, location etc. on customer satisfaction and revealed that responsiveness, price and reliability have positive and significant effect on customer satisfaction. On the contrary, tangibility, empathy and location have statistically insignificant influence on customer satisfaction.

In the investigation of service quality and customer satisfaction, Nguyen et al. (2020) applied multivariate regression technique and revealed all service quality drivers have positive relationship with customer service. Regression results show that tangibility and service capacity have significant positive impact on customer satisfaction which indicates with the improvement capacity and tangibility that banks intend to satisfy their customers more. The insights of results confirm that customer satisfaction leads to make customer more loyal which results customers not only continue with the bank but, they also recommend other people to use the same bank.

In the investigation of service quality drivers and customer satisfaction, Dandis et al. (2021) applied CARTER technique and observed compliance, responsiveness, tangibility, empathy, and assurance are positively linked with loyalty intentions, quality of service is directly associated with customer loyalty intentions and satisfactions. Result of the study suggested that bank managers should focus on improving service quality through training and development programs for their human resources to make more customer satisfaction in Jordan.

In the investigation of service quality and customer satisfaction based on SERVQUAL structure, Anh and Thanh (2022) examined effect of responsiveness, assurance, tangibility, empathy and reliability on customer satisfaction in banking sector and reported that all five drivers (dimensions) of service quality have significant role in making customer satisfaction in bank industry.

In the investigation of service quality drivers and customer satisfaction, Gonu et al. (2023) explored that service quality influences to the customer satisfaction and accelerates business success in banking industry. The PLS-SEM results of the study show that customer orientation plays a key role in predicting customer satisfaction. Finding concludes that policy makers need to formulate comprehensive policies and bank management should focus on orientation
programs to the customers to increase the service quality driver which intends to increase customer satisfaction in banking sector. Islam et al. (2023) examined relationship between e-service quality drivers and customer satisfaction in banking sector based on online survey and observed that e-service quality drivers have a significant influencing role for the customer satisfaction. Result suggests that the management of banks should focus on utilization e-service quality drivers such as perceive of security risk, ease of use, responsiveness, website quality etc. to make more customer satisfaction.

Both theoretical and empirical literature confirms sufficient studies about service quality drivers and customer satisfaction have been made both in developing and developed economies; however, there remains a prominent gap of similar researches in under-developed economy like Nepal. Therefore, this paper aims to address this gap by examining the role of service quality drivers to predict and explain customer satisfaction in Nepalese banks within Kathmandu valley.

**Research Methodology**

This paper has applied both descriptive and causal research methodologies. The descriptive research design is used to assess the status of respondent profile and descriptive statistics (mean, variation, minimum and maximum values). Causal research design is employed for examining impact of different drivers of service quality on consumer satisfaction. Within the framework of SERVQUAL model, these approaches have been applied to assess how bank customers in Kathmandu valley perceive various service quality drivers and their influence on overall customer satisfaction in the Nepalese banking sector within Kathmandu valley.

This research is grounded in primary data collection methods aimed at understanding and analyzing the perspectives regarding service quality drivers and their effect on customer satisfaction. To achieve the purpose, questionnaire survey was made among customers of Nepalese commercial banks. The questionnaire included a total of twelve questions. Five questions were directed towards gathering demographic information about the respondents. The remaining six questions were structured using a five-point Likert scale to gauge agreement or disagreement with statements related to customer satisfaction and reliability, assurance, tangibility, empathy, and responsiveness as drivers influencing
customer satisfaction. Finally, an open-ended question was included to capture written comments concerning the influence of service quality drivers in determining customer satisfaction in Kathmandu valley.

In this study, the population consists of individual bank customers holding accounts with various commercial banks licensed by Nepal Rastra Bank until mid-July 2023. Specifically, the focus is on customers with bank accounts within the Kathmandu valley. For data collection, 500 sets of questionnaires were distributed and collected only 405 sets in usable form. Therefore, sample size of this paper is 405 customers from commercial banks, and sample was selected using convenience sampling technique.

This research paper has processed and analyzed collected data utilizing SPSS software version 24 and MS-Excel. Descriptive statistics and regression analysis along with t-tests, F-test, and Adjusted R$^2$ have been employed to evaluate and assess the drivers of service quality to predict and analyze the level of customer satisfaction within the banking sector in Kathmandu. This study has applied F-statistics for the validity of the model, Adjusted R$^2$ for the validation of explanatory power of service quality drivers in explaining level of customer satisfaction and Cronbach’s alpha for the test of reliability of data and variables.

Customer satisfaction is regarded as the independent variable. Previous theoretical and empirical research has identified various service quality factors that influence customer satisfaction. In this paper, the reliability, assurance, tangibility, empathy, and responsiveness (RATER) of banks towards their customers are regarded as explanatory variables. These explanatory factors are collectively referred as RATER.

This study employs multiple regression models to analyze how service quality drivers influence customer satisfaction. Equation (1) in the regression model is specifically utilized to scrutinize how these factors affect customer satisfaction within the banking sector in Kathmandu valley of Nepal.

Customer satisfaction ($Y$) = $\beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \epsilon_1$ ... (1)

$X_1$ stands for empathy, $X_2$ represents assurance, $X_3$ indicates responsiveness, $X_4$ symbolizes for tangibility, $X_5$ is reliability, $\beta_0$ represents the constant coefficient, while $\beta_1$, $\beta_2$, $\beta_3$, $\beta_4$, and $\beta_5$ signify the coefficients of the explanatory variables, with $\epsilon_1$ representing the error term.
Results and Discussion

Analysis of Profile of Respondents

This section of the paper aims to describe survey results concerning respondents’ profile of bank customers. The major insights relating respondents’ profile of bank customers influencing drivers of service quality and customer satisfaction delve into the viewpoints, impressions, and attributes of the respondents. Results of respondents’ profile shows that majority (76.05%) of bank customers are male, and most of bank clients (51.11%) are the age of 40 to 50 years which indicates the mainstreams of bank customers. Additionally, result reveals that the majority (54.07%) of bank customers have academic qualification of bachelor degree or above. Furthermore, this paper explores that occupation of bank customers is in various sectors such as service (26.17%), business (33.83%), self-employed (16.5%) and remaining (23.5%) in other sectors. Finally, survey result confirms majority (61.48%) of bank customers have monthly income of Rs. 30,000 to Rs. 50,000.

Descriptive Statistics

The paper utilizes descriptive statistics to outline the drivers of service quality that impact customer satisfaction. Table 1 provides a summary of these statistics, encompassing customer satisfaction and its associated explanatory variables.

Table 1

Descriptive Statistics of Variables

<table>
<thead>
<tr>
<th>Variables</th>
<th>Y</th>
<th>X1</th>
<th>X2</th>
<th>X3</th>
<th>X4</th>
<th>X5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>3.53</td>
<td>3.89</td>
<td>3.92</td>
<td>3.65</td>
<td>4.23</td>
<td>3.19</td>
</tr>
<tr>
<td>Standard Deviations</td>
<td>24.78</td>
<td>42.36</td>
<td>33.95</td>
<td>25.47</td>
<td>36.79</td>
<td>20.82</td>
</tr>
<tr>
<td>Minimum</td>
<td>2.66</td>
<td>2.96</td>
<td>3.07</td>
<td>2.85</td>
<td>3.30</td>
<td>2.52</td>
</tr>
<tr>
<td>Maximum</td>
<td>3.61</td>
<td>4.27</td>
<td>4.25</td>
<td>3.42</td>
<td>4.56</td>
<td>3.42</td>
</tr>
<tr>
<td>Number of observations</td>
<td>405</td>
<td>405</td>
<td>405</td>
<td>405</td>
<td>405</td>
<td>405</td>
</tr>
<tr>
<td>Cronbach’s alpha</td>
<td>0.85</td>
<td>0.86</td>
<td>0.87</td>
<td>0.83</td>
<td>0.91</td>
<td>0.81</td>
</tr>
</tbody>
</table>

*Note:* Estimated results based on data of Field Survey 2023. Y represents customer satisfaction, X1 stands for empathy, X2 represents assurance, X3 indicates responsiveness, X4 symbolizes for tangibility, and X5 is reliability.

Table 1 displays the descriptive statistics outcomes for all variables. Customer satisfaction (Y), empathy (X1), assurance (X2), responsiveness (X3), tangibility (X4), and reliability (X5) exhibit a positive mean (composite average values). The maximum score of customer satisfaction is 3.61, while the lowest is
2.66, with an average composite mean score of 3.53 indicates bank customers' satisfaction levels surpass the average. The composite mean values for the empathy, assurance, responsiveness, tangibility and reliability are 3.89, 3.92, 3.65, 4.23, and 3.19 respectively. Composite mean values exceeding 3 suggest that customers agree that all service quality drivers (X₁, X₂, X₃, X₄, & X₅) influence customer satisfaction levels. Customers attribute the highest importance to tangibles, followed by assurance, and so forth, with reliability being of least importance. Additionally, Table 1 provides both minimum and maximum composite mean (average score values) for each of variables. Lastly, descriptive results reveal the value of standard deviations of each variable which measures the variations of bank customers' prioritization in service quality drivers affecting customer satisfaction. The Cronbach’s alphas (α >0.80) of each variables show the good reliability of data, variables and results of this paper.

**Analysis of Impact Drivers of Service Quality on Customer Satisfaction**

This study has employed regression models to scrutinize the connection of explanatory variables with customer satisfaction in bank sector. Table 2 demonstrates regression outcomes based on multivariate models, as per the previously specified equations, aiming to assess the impact of service quality drivers on customer satisfaction of commercial banks in Kathmandu valley.

**Table 2**

*Regression Results of Customer Satisfaction and Service Quality Drivers*

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficient (β)</th>
<th>Standard errors</th>
<th>t-statistics</th>
<th>p-values</th>
</tr>
</thead>
<tbody>
<tr>
<td>X₁</td>
<td>0.964</td>
<td>0.267</td>
<td>3.610</td>
<td>0.000</td>
</tr>
<tr>
<td>X₂</td>
<td>1.434</td>
<td>0.392</td>
<td>3.658</td>
<td>0.000</td>
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<tr>
<td>X₃</td>
<td>0.357</td>
<td>0.125</td>
<td>2.856</td>
<td>0.003</td>
</tr>
<tr>
<td>X₄</td>
<td>0.403</td>
<td>0.168</td>
<td>2.399</td>
<td>0.005</td>
</tr>
<tr>
<td>X₅</td>
<td>0.597</td>
<td>0.276</td>
<td>2.163</td>
<td>0.037</td>
</tr>
<tr>
<td>Constant</td>
<td>2.381</td>
<td>0.593</td>
<td>4.015</td>
<td>0.006</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>F-statistics</th>
<th>17.962</th>
<th>Adjusted R²</th>
<th>0.594</th>
</tr>
</thead>
<tbody>
<tr>
<td>p-value</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Note:* Estimated results are based on Field Survey data 2023. The numbers observations is 405. Customer satisfaction is dependent variable, and service quality drivers X₁, X₂, X₃, X₄ and X₅ are explanatory variables. P-values<0.01 indicate significance at 1% level, P-values<0.05 represent statistical significance at 5% level. Also reported are the Adjusted R² and F-statistics.
Table 2 displays the outcomes of multiple regression analyses aimed at assessing how various quality service drivers (explanatory variables) collectively impact on customer satisfaction in banking sector. The regression coefficients demonstrate a positive association of empathy, assurance, responsiveness, tangibility and reliability with customer satisfaction. Specifically, the estimated results show that $X_1$, $X_2$, $X_3$, and $X_4$ positively impact on customer satisfaction ($Y$) and are statistically significant at the 1% level ($P$-values < 0.01), whereas reliability ($X_5$) also has a positive impact but achieves significance only at the 5% level ($P$-value < 0.05).

The positive impact of empathy on customer satisfaction of this study is consistent with prior findings of Parasuraman (1988), Wilson et al. (2012), Lau et al (2013), Dandis et al. (2021), Anh and Thanh (2022) and inconsistent with results of Virima and Sandada (2019). In addition, this study reveals significant positive influence of assurance as driver of service quality on customer service which supports to the prior findings of Parasuraman (1988), Wilson et al. (2012), Lau et al (2013), Dandis et al. (2021), Anh and Thanh (2022) that service quality has positive role in making customer satisfaction. Furthermore, this paper explores a significant positive impact of responsiveness in making customer satisfaction in the field of commercial banks in Kathmandu valley which supports for the prior results of Johnston (1997), Parasuraman (1988), Wilson et al. (2012), Lau et al (2013), Anh and Thanh (2022). Moreover, this research reports a significant effect of tangibility on customer satisfaction in bank industry which result in consistent with prior findings of Parasuraman (1988), Wilson et al. (2012), Nguyen (2020), Dandis et al. (2021), Anh and Thanh (2022) and inconsistent with results of Virima and Sandada (2019). Finally, finding of this paper shows a positive influence of reliability as service quality driver on customer satisfaction which supports to the prior findings of Parasuraman (1988), Wilson et al. (2012), Virima and Sandada (2019), Anh and Thanh (2022).

The coefficients of determination of the multiple regression models indicate predictive as well as explanatory strength of the explanatory variables. The adjusted $R^2$ value of the model stands at 0.594, suggesting that the multiple regression models can predict approximately 59.4% of the variance in customer satisfaction based on their explanatory variables (drivers of service quality). Furthermore, the F-statistics (17.952) of the models are statistically significant at
the 1% level (P-values < 0.01) that implies all the regression models employed in this study are statistically meaningful. The outcome suggests that regression models utilized in estimating customer satisfaction levels with their explanatory variables adequately fit the overall models.

**Conclusion and Implication**

Satisfaction plays a crucial role in inviting customers to openly express their positive sentiments and consider purchasing products. Customer satisfaction stands as a cornerstone for the enduring success of any organization, serving as a measure to determine whether a firm's products and services meet customer expectations. The prosperity of business endeavors and overall economic advancement centered upon customer satisfaction. The drivers such as empathy, assurance, responsiveness, tangibility, and reliability comprise dimensions of service quality that determine the level of customer satisfaction specially in banking sector. The descriptive and regression analysis of survey tends for examining influence of drivers of service quality for determining customer satisfaction of commercial banks in Kathmandu valley.

This survey reveals a favorable link between quality drivers and customer satisfaction. This paper explores Nepalese bank customers assert all service quality drivers such as empathy, assurance, responsiveness, tangibility, and reliability significantly influence customer satisfaction in banking sector. Findings of this study indicate these service quality drivers exert a prominent impact on customer satisfaction. Therefore, service quality drivers collectively have a substantial explaining power influencing customer satisfaction in Nepalese commercial banks within Kathmandu valley. Drivers of service quality play a crucial role in enhancing the customer satisfaction in banking sector in Nepal. Hence, result of this paper is more important for policymakers, executives, regulatory bodies, bank customers and academics to recognize the drivers of service quality and their influence on customer satisfaction. Policymakers ought to prioritize in providing better service qualities for bank customers to provide them more satisfaction. This study is limited only in commercial banks inside Kathmandu valley; further such studies are suggested to make covering other financial institutions and industries with consideration of other techniques (SEM, PLS-SEM etc.) incorporating additional explanatory variables such as purchase intentions, compliances, adoption of technology etc. in Nepal.
References


