LITERATURE REVIEW OF SERVICE QUALITY IMPROVEMENT IN THE RETAIL BANKING INDUSTRY

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ABSTRACT

Banks offer similar kinds of services, but they could provide differences in terms of service quality. This paper analyzes past studies regarding service quality improvement in the retail banking industry. The continuing trend to a model of service quality improvement, from personnel counter services to electronic services, is demonstrated. Improved service quality should be adopted to maintain the core competence and this paper contributes knowledge and background for banks to apply these findings to better shape and focus their positions in the market and also to provide service quality to customers.

1. Introduction

It is commonplace that all people are involved with all kinds of services, for example, in educational institutions, fitness centers, and transportation, as well as in banking in their everyday life (Rose, 1999). In today's highly competitive business environment, service has increasingly played a critical role in banks' operations (Payne, 1993).

Banks offer services, and they usually experience difficulties in managing them. Thus, service quality has emerged as a key strategy adopted to offer quality service to customers. In consequence, in the retail banking industry, where many similar products are available, banking practitioners have to pay close attention to superior service provision. This is because service quality does not impact only on the customer decision-making process, but also influences customer satisfaction, purchase retention, loyalty and business survival as shown in many studies (Adebanjo, 2001; Berry et al., 1994; Li *et al.,* 2001; Lim & Tang, 2000; Newman & Cowling, 1996; Youssef *et al.,* 1996).

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2. Objectives

This paper's objective is to review the literature regarding service quality improvement in the retail banking industry, from various kinds of studies and sources. It will lead to understandings of aspects of service quality improvement. The past studies examined are mainly about service quality improvement in the personnel counter services. Few studies are emerging to examine service quality in the electronic-service aspects. In addition, the available studies examined do not present the relationship between service quality in personnel counter services and electronic services. This research will seek to close the gap in this field of study.

3. Problem identification

The major problems for this paper are to explore the body knowledge of improve service quality improvement, and the continuing trend of service quality improvement in the retail banking industry.

4. Retail banking industry and its major changes

The significance of retail banking roles and the everyday involvement of banking services in people's lives has been recognised (Hughes, 2002). Starting with the purchase of goods and services, individual consumers can use credit or debit cards as well as cash withdrawn from Automatic Teller Machines (ATMs) as methods of making payments. Banks are where people can go when they need a loan to purchase a new house, tuition fees for their study, financial advice for investments, or a credit line for starting a newly owned business (Rose, 1999). Thus, banks are providers of the widest ranges of financial products and services, labeled as a "financial department store" (Rose, 1999, p.6).

However, banks face great changes in their business environment where adjustments and improvements are needed. Major changes in banking environment include the following:

First of all, in the past banking business had previously been an un-competitive environment due to the entrance limitation from strict regulations; however, about two decades ago in the United States financial deregulation began and expanded widely around the world (Rose, 1999). Banks around the world are experiencing intense competition from both local and overseas banks as well as new entrants (Bloemer *et al.*, 1998, Griffiths *et al.*, 2001; Hemple & Simonson, 1998) as a result of globalization and deregulation (Cheron *et al.*, 1999; Mishkin & Eakins, 1997; Lowe & Kuusisto,1999), which leads to the decrease in profit margins.

Secondly, customer expectations and needs for services have substantially increased (Li *et al.*, 2001; Lockwood, 1995; Meyer *et al.,* 1999; Wrennall, 2000). As customers become better educated, they demand new products, better and more reliable delivery, as well as more responsive services. As a consequence, to improve competitiveness, banks have to understand customer needs and expectations (Parasuraman, 1991) and satisfy their customers by providing better products and services.

Moreover, the economic crises, especially the Asian crisis, have greatly impacted on banking profit margins and also on customers' confidence in banking institutions. Specifically, in Hong Kong, the domestic recession since the second half of 1997 resulted in banks no longer having highly profitable returns. Bad debt surged significantly in both 1998 and 1999 and the number of licensed banks in 1999 has dropped by approximately 17% compared with 1997. As a result, banking customers have not felt confident with local financial institutions and have moved their deposits and transacted their financial business with reputable institutions from overseas (Li *et al*., 2001).

Finally, other factors including demographic and social changes, technology and laws and regulations (Jayawardhena & Foley, 2000; Lockwood, 1995; Angur *et al*.,1999) lead to changes to the banking industry as well. In the future, there may be new target groups that banks need to focus on and the regulations, especially for electronic banking services, may increase their important roles in defining and shaping banks' performance.

5. Need for service quality

Those changes mentioned have profoundly transformed the nature of banking business (Rose, 1999). Today, bank marketing strategy applied in the market is easy to imitate over a short period of time. One obvious evidence is that banking products and services offered in the market are the same or very similar (Li *et al.,* 2001; Lim & Tang 2000; Lockwood, 1995; Levesque & McDougall, 1996; Coskun & Frohlich, 1992; Alfansi & Sargeant, 2000). In addition, price reduction should not be used because it will lead to a larger decrease in profit margins and finally a price war among banking providers. Further, distribution channel management is another strategy in which branch expansion, as an example, is costly and should be available to a certain optimal level to deliver appropriate customer services. Last, but not least, promotional campaigns are expensive and easy for competitors to copy. Thus, the 4Ps (product, price, place and promotion) of the marketing mix (Kotler, 1997) cannot be prolonged and banks have to specifically focus on the long-term core strategy known as 'service quality' (Allred & Addams, 1999; Galloway & Blanchard, 1996; Johnson, 1997; Joseph *et al.,* 1999; Li *et al.,* 2001; Kunst & Lemmink, 2000; Newman *et al.,* 1998; Lim & Tang 2000; Lockwood, 1995; Lloyd-Walker & Cheung, 1998; ; Soteriou & Stavrinides, 2000; Stafford, 1996; Siu & Cheng, 2001; Wong

& Perry, 1991, Yavas *et al.*, 1997), which competitors will strenuously imitate (Reichheld & Sasser, 1990; Ennew & Binks, 1996; Devlin, 1998).

Service quality will sustain the customers' confidence in a service provider's service delivery, attract more new customers, increase business with existing clients, reduce dissatisfied customers with fewer mistakes, maximise a company's profits and increase customer satisfaction (Berry *et al.*, 1994; Lee *et al.*, 2000). However, quality costs are expensive, usually about 30–50 per cent of sales revenues (Newman & Cowling, 1996), and time consuming to realise the benefits. Whoever implements them first will gain advantages before others. Hence, service quality will be an important business catalyst driving the retail banking business and ultimately will reflect in corporate performance.

6. Service quality and its determinants

Service quality has been defined as customers' overall impressions of an organisation's services in terms of relative superiority or inferiority (Johnston, 1995). Further, service quality is considered to not only meet but to exceed customer expectations, and should include a continuous improvement process (Lloyd-Walker & Cheung, 1998). Customers evaluate banks' performance mainly on the process of their interpersonal contacts and interactions (Grönroos, 1990). Service quality arises from a comparison of the difference between service expectations developed before an encounter with banks and the performance perceptions gained from the service delivery based on the service quality dimensions (Bloemer *et al.*, 1998). Berry *et al.* (1985) and Zeithaml and Bitner (1996) indicated that service quality consisted of five dimensions. The definition for each is explained as follows:

1. Tangibles: appearance of physical facilities, equipment, personnel and written materials.
2. Reliability: ability to perform the promised service dependably and accurately.
3. Responsiveness: willingness to help customers and provide prompt service.
4. Assurance: knowledge and courtesy of employee and their ability to inspire trust and confidence.
5. Empathy: caring, individualised attention the firm provides its customers.

In the study by Berry *et al.* (1994) with more than 1,900 customers of five large famous US corporations, they found that thirty-two out of 100 placed emphasis on reliability, followed by responsiveness (22%), assurance (19%), empathy (16%) and tangibles (11%). Thus, reliability is considered the essential core of service quality. In addition, other dimensions will matter to customers only if a service is reliable, as those dimensions — for example, responsiveness and empathy from service staff — cannot compensate for unreliable service delivery. Further, they found that more companies were deficient in reliability than in other service dimensions, but their best performance was on the least essential dimension of tangibles.

7. Service quality and its impact

The relationship between service quality and its impact on banking providers will be explored in terms of both qualitative and quantitative benefits. Regarding qualitative benefits, customer satisfaction and loyalty were major concerns as Oliver (1993) and Newman et al., (1998) found that quality was an antecedent to satisfaction, and Cronin and Taylor (1992) discovered that perceived service quality brought about satisfaction or vice versa. In addition, Grönroos (1990) suggested that the mutual exchange and promise fulfillment between customers and service providers was a core construct to obtaining customer satisfaction and loyalty during the process of service delivery. Besides, the study by Zairi (2000) emphasised that customer satisfaction had greatly affected business, its corporate image, and obtaining new customer bases through direct recommendations.

With respect to the quantitative benefits, a study was conducted in 1988 of a particular US bank regarding the impact of service quality improvement on performance. Before the quality had been improved, the bank had to pay for the cost of failures and corrections. However, after the bank prevented errors and mistakes in serving customers or, in other words, improved its service quality, the cost of services systematically decreased while profit margins and earnings finally increased. Accordingly, there was an increase in return on assets (ROA) from 1.05 per cent before improvement to 1.38 per cent after improvement and also a return on equity (ROE) from 16.10 per cent to 21.22 per cent respectively as shown in the following table (Harvey, 1996):

Table 1: Impact of quality improvement

Bank Performance	Before Improvement	After Improvement
ROA	1.05 %	1.38 %
ROE	16.10 %	21.22 %

(Source: Harvey, T. 1996, *The Banking Revolution: Positioning Your Bank in the New Financial Services Marketplace*, Irwin Professional Publishing, USA, p. 11)

In addition, Zairi (2000) finds that satisfied customers possibly share their experiences with five or six people while dissatisfied clients might inform another ten. It costs 25 per cent more to recruit new customers than to maintain existing customers. Further, Naumann (1995) and Dawes and Swailes (1999) presented that retaining an existing customer costed about five times less in money, time and corporate resources compared with attracting a new customer while Newman *et al.*, (1998) indicated that an increase in only five per cent in customer loyalty would grow in profitability about 25–85 per cent.

In contrast, poor service will result in a lot of consequent costs and damage, including low customer satisfaction, relatively high customer defection, loss of business sales opportunities, and a decrease in customer retention and excessive costs due to having to attract new customers and overcome a damaged corporate image (Stuart & Tax, 1996). Specifically, about two-thirds of customers generally stop having business with a particular organization as a result of poor customer service (Julian & Ramaseshan, 1994).

8. Move from personnel counter services to electronic services

The areas of past researches in retail banking services in many countries such as Jordan (Nazer, *et al.*,1999), Finland (Holstius & Kaynak, 1995), Australia (Kaynak & Whiteley, 1999; Nielsen *et al.,* 1998), Poland (Kennington *et al.*,1996), Ghana (Owusu-frimpong 1999), Sweden (Zineldin 1996), USA (Boyd, *et al.,* 1994) and Malaysia (Haron, *et al.,* 1994), were mainly about services at branches and high technology services were not considered as a significant choice. This indicates that service quality improvement started from personnel counter services.

Recently, there has been an increasing trend of studies regarding a new distribution channel of banking services, electronic banking (Delvin, 1995; Joseph *et al*., 1999; Jayawardhena & Foley, 2000; Mols, 1998; Mols, 1999; Mols, 2000; Birch & Young 1997; Daniel, 1994; Prendergast & Marr, 1994; Sathye, 1999). Accordingly, these studies show the transition of service quality improvement from the personnel counter services to electronic services. In this section, some past studies will be examined to identify this transforming trend.

8.1 Personnel counter services

In this section, the study by Kaynak and Whiteley (1999) will be employed as an example. After examining the bank's customers a total of 245 respondents in Western Australia, the authors found that the importance of bank selection determinants was ranked and categorised as follows:

Table 2: Importance of bank selection factors by percentage

Selection Factors	Very Important/Important (%)
1. Friendliness of bank personnel	93
2. Fast and efficient service	93
3. Location near home/work	87
4. Lower service charges	87
5. Perceived confidentiality of bank	85
6. Loan with favorable terms	85
7. Bank reputation and its image	84
8. Lower loans interest rate charges	84
9. Higher interest payments, savings	83
10. Confidence in bank manager	72

(Source: Adapted and shortened from Kaynak, E. and Whiteley, A. (1999), 'Retail bank marketing in Western Australia', *International Journal of Bank Marketing*, Vol. 17 No. 5, p.227)

From table 2, to determine the selection factors for the traditional way of service, 'friendliness of bank personnel' and 'fast and efficient service' were among first items ranked in importance for consumers to be clients of specific banks. The reasons are that the respondents basically require a human and friendly approach and staff' ability when conducting their financial transactions. Thus, interpersonal skills and work ability are very valued aspects for the banking experience (Kaynak & Whiteley, 1999). Remarkably, it indicates that there is no concern about a factor of technology advancement in this study.

8.2 Electronic services

Electronic banking was first introduced in the UK in the early 1980s (Daniel, 1994, p.73) and its availability was the result of pressure from the increasingly competitive business environment and customers' demands (Mols, 2000). It was expected that electronic banking would have a significant influence on the banking market (Daniel, 1994) and substantially change the distribution channel of retail banking business (Mols, 1999).

There have been a number of delivery platforms of electronic banking services, which are categorised as: ATMs, telephone banking, PC (home) banking, Internet banking, managed network, public access kiosk and TV-based service (Daniel, 1994; Liao *et al.* 1999: Mols, 1998; Mols *et al*., 1999; Mols, 2000; Ramsay & Smith, 1999). In this paper, Internet banking is the main channel of distribution to be explored due to the increase in its popularity.

Sathye's study (1999) stated that six major determinant factors for adoption or rejection of an Internet banking service in Australia were: the availability of infrastructure; resistance to change; ease of use; reasonable price; awareness of service and its benefits;

and security concerns. The results from the study demonstrated that security concerns and lack of awareness about Internet banking and its benefits played the most important role as the obstacles to non-adoption for Internet banking.

As well, another study from 300 usable questionnaires by Joseph *et al*. (1999) examined the factors for high quality electronic banking services. The five important factors were categorised as: convenience/accuracy; feedback/complaint management; efficiency; queue management; accessibility; and customisation. The results of this study illustrated that banks have to maintain the standard of their convenience/accuracy and efficiency. In addition, they need to improve their customisation, feedback/complaints and queue management by reallocating their resources. One point of interest, though, was that although the performance of the electronic banking service was not accepted as being of a high standard, 52.9 per cent of respondents were satisfied with it.

In addition, the other important characteristics of consumer behaviour in using an e-banking service are that customers tend to be more satisfied with their banks, provide more positive word-of-mouth recommendations, possibly switch less to other banks and are price-conscious (Mols, 1999). Further, the reality regarding banking services is that the personnel counter services will decrease and the high-tech touch services will increase (Mols, 1999; Rose, 1999). However, a substantial proportion of bank clients still prefer bank staff to consult for a wide range of banking matters (Rose, 1999).

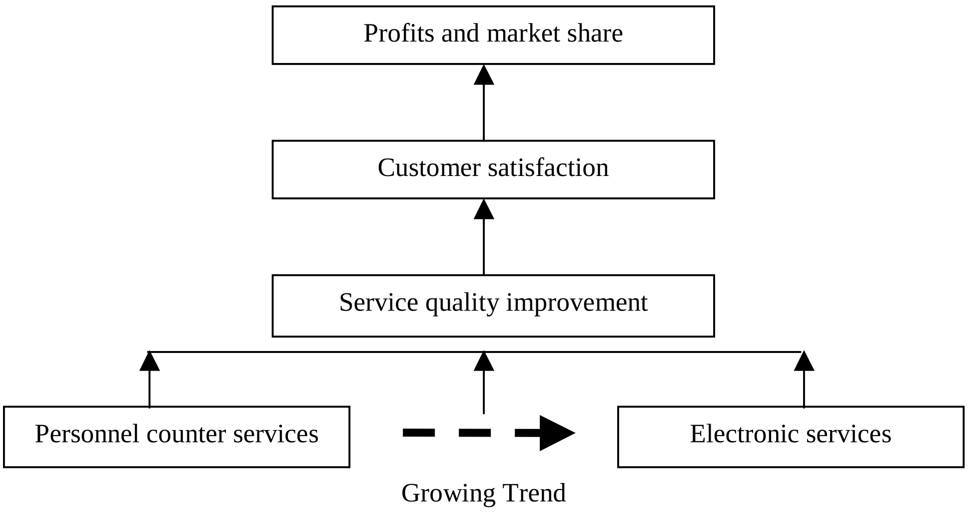
Recently, banking industry in different countries has shown their interest transition in improving service quality from traditional branches to electronic channels. Accordingly, many of them have tended to close or relocate their branches to be sited closely to customers' places for customers' conveniences, and they have relied more on electronic banking services with significant growth in electronic facilities such as Internet, computer, ATMs, telephone and mobile phones. Such trend happened in many countries, for example, in Australia, Japan, Singapore, Korea, Hong Kong, India, Indonesia. Particularly, in Australia, branch penetration (branches per million population) in 1999 decreased about 4.6 percent compared with 1998, ATMs penetration (ATMs per million population) in 1999 showed an increase in 6.5 percent compared with 1998, and Internet penetration (Internet per million population) in 1999 significantly increased 28.2 percent compared with 1998 (The Asian Banker, 2000, pp.17-19).

Similarly, in some countries, such as China, although banks in 1999 showed the minimal increase in number of branches approximately 2.7 percent compared with 1998, the increase in investment in electronic banking facilities, the substitute area to be focused, was about 32 percent for ATMs compared with 1998, and about 200 percent for Internet compared with 1998 (The Asian Banker, 2000, p.17-19). This proliferation of electronic banking facilities leaded to banks' attempt to migrate their customers from personnel counter services to electronic banking services (The Asian Banker, 2000).

9. Model proposition

As mentioned above, the growing trend of service quality improvement is transformed from personnel counter service to electronic service with the ultimate goal of organisation survival in terms of profits and market share through developing customer satisfaction as shown in the model below:

Figure 1: Model of growing trend from personnel counter services to electronic services



(Source: Developed for this study)

Hence, banks should consider the findings and pay attention to electronic banking services as new alternative distribution channels emerging in this century, due to their increased popularity and benefits. They should decide on which service area to increasingly focus, between personnel counter services and electronic banking services, or both. Then banks will be able to allocate their resources to improve their service quality strategically. Nevertheless, the fundamental fact for banks to focus on in any kind of service is that one of the successful banking traits depends on being an innovative provider to offer value-added services (Kaynak & Whiteley 1999; Groth & Dye 1999). Further, to focus either personnel counter services or electronic banking services, or both, banks have to improve their services delivered to customers. The achievement of service quality improvement is to create customer satisfaction, which will finally leads to corporate profits and market share.

10. Contribution of knowledge

This research provides information on retail banking characteristics as well as service quality improvements. Hence, bankers can apply knowledge, findings and a model of service quality improvement for their banks to build or improve a competitive edge, increase customer satisfaction and maintain long-term profits.

11. Conclusion

Nowadays, banks are in a fluctuating business environment as they experience an increase in competition and in customer demand, and a decrease in profit margins. Thus, it is critical for banking practitioners to focus on a differentiated strategy, known as service quality improvement, to strengthen their core competitive edge, and urgently make a decision to focus on either the area of personnel counter services or electronic services or both, to be able to allocate limited resources to serve that decision. This strategy, to focus on either personnel counter services or electronic services or both, will be successful if there is commitment from bank management and involvement from all employees to develop an exact understanding of the customers' needs. Remember that, "consumers will seek out those financial products and suppliers which offer the best value for money and they are educated about it" (Sathye, 1999, p.325). Thus, if a bank is able to position itself favorably within a specific market, relative to competitors, high profits will be earned as a result (Davies *et al.*, 1995).

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