An Overview of Factors Affecting Customer Loyalty in Retail Banking Sector

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Abstract

Banking sector in India have seen major changes in past few years, globalisation of competition, segmentation of markets, and development of information technology have enhanced customer awareness and created a situation where the achievement of long-term success is not possible without building a loyal customer base for bank. The present paper will throw light on the concept of customer loyalty with a special reference to retail banking sector and would try to identify and describe those factors which makes a customer loyal towards a bank. In addition, paper would also try to examine the impact of these factors on behaviour of bank customers.

Keywords : Customer Loyalty, Retail Banking, Customer Satisfaction, Affective Commitment, Dedication and Constraints

Introduction

Banking system accelerates the growth and development process of a country because it mobilizes the resources from the saver to the investors. Banking system of India has show gigantic expansion after the economic liberalization in 1991. Expansion of banking sector in India has created a new and fast growing segment of banking business i.e. Retail banking which works on the principles of service industry and delivers various kind of services to its customer and tries to attain a satisfied pool of customers who make positive word of mouth for retail banking services.

Banking sector in India have seen major changes in past few years, technological advancement, entry of private sector and foreign banks, liberalized policies of central government have changed the overall scenario of banking sector and converted it into a competitive sector. In a competitive market it is important for players to make it customer pleased and satisfied to build a strong base of loyal customers so that business can grow and develop faster. For doing this it is necessary to make such strategies which focuses upon the need and wants of the customers and make them easy to use banking services. This kind of strategies helps in building strong customer relationship and provides high level of satisfaction to bank customers.

In general it is believed that Customer loyalty can only be attained by providing high level of satisfaction to customers but there are several other factors which have an impact over the loyalty status. A highly satisfied customer generally stays longer, buys more as the company introduces new products and services and upgrades existing products and services, talks favourably to others about the company, pays less attention to competing brands, offers product or service ideas to the company, and costs less to serve than new customers because transactions can become routine (Homburg, Koschate, & Hoyer, 2005). Customer satisfaction is also helpful in achieving o higher returns and faster growth of a company.

Concept of Customer Loyalty

Recent years have shown a growing interest in customer loyalty. The globalisation of competition, saturation of markets, and development of information technology have enhanced customer awareness and created a situation where long-term success is no longer achieved through optimised product price and qualities. Instead, companies build their success on a long-term customer relationship.

Customer loyalty can be defined as the totality of feelings, attitude that would incline a customer to consider the re-purchase of a particular product or services, re-visit a particular bank, company or shop. Customer loyalty has always critical to business success and profitability.

Customer loyalty has long been a topic of higher interest to both academia & practice and a loyal customer has been found to beneficial for the organisation. During the last decade, customer loyalty has gained a lot of attention of both academician and professionals.

Reichheld & Sasser (1990) claims that only 5% improvement in the customer retention can lead to an increase in profitability between 25%

to 85%, depending upon industry sector, Therefore increased in customer loyalty has a direct relationship with increased profitability and customer base.

Jones and Sasser (1995) define loyalty as 'the feeling of attachment to or affection for a company's people, products or services these feelings manifest themselves in many forms of customer behaviour. The ultimate measure of loyalty, of course, is share of purchases in the category'.

A loyal customer demonstrates the following behaviour and attitude:-

1. Repeatedly purchase from organisation.
2. Have a high level of satisfaction with the organisation.
3. Will recommend organisation's product & services to others.
4. Will highly trust the organisation.
5. Spend proportionally more than with that organisation than other i.e. share of wallet.

Concept of Retail Banking

The evolving macro-economic environment owing to financial market reforms and myriad of micro-level demand and supply side factors and fast changing personal, familial and social values of the people, commercial banks from traditional banking activities to broad based retail banking business. Retail banking has emerged as a core segment of the banking business all over the world and gained prominence in the recent years to meet the competitive challenges to improve the quality of services and profit margin.

Retail banking refers to the dealing of commercial bank with individual customers both on liabilities and asset sides of balance sheet. It encompasses fixed, current and saving deposits linked products on liability side and mortgages, loans (e.g. personal, auto, housing, educational) and other financial products on asset side.

Currently, the pure retail banking is conceived to be provision of mass banking product and services to individual for personal consumption as opposed to wholesale banking having thrust on corporate and institutional clients. The essence of retail banking lies in individual customers; it is akin to mass banking which lays focus on masses rather than classes.

In retail banking all the banking need of individual customers are taken care of in integrated manner. Retail banking business today has multi products and services range for its multi customers. It offers multiple product like deposits, loans, credit cards, insurance, investment and securities to multiple customers group comprising consumers, small business and corporate.

Retail banking in India is not a new phenomenon. It has always been in existence in different form. In recent few years, it has emerged as an important segment of banks 'portfolio'. The year 1995 marked the starting point of Retail banking revolution with Foreign and new generation Private banks and there is a paradigm shift in banking business of Indian commercial banks from wholesale banking to retail banking.

Objectives and Methodology

The general purpose of this paper is to identify and describe the factors that have a direct or indirect impact on customer loyalty in retail banking sector. The paper will focus on the customer loyalty in retail banking sector and will try to know the causes that makes a customer loyal. The present paper is descriptive in nature as it is an attempt to redefine the factors affecting customer behavior while opting banking services. The paper is primarily based on secondary sources of information which includes various books, national & international journals & research reports, and reputed websites.

Review of Literature

Jain, Pinson& Malhotra (1987), studied the customer loyalty in retail banking and found that customer loyalty is a useful construct. Economic rationale swayed bank non-loyal segment whereas the bank loyal segment placed greater emphasis on human aspects of banking.

Meidan and Bloutinho (1988), conducted an attitudinal research on bank customer perceptions and loyalty. The key findings were that banks should develop ATM usage; financial institutions should review basic banking services and that customer loyalty is a function of more than one variable.

Boyd, Leonard and White (1994), studied differences in selection criteria for retail banks with respect to basic demographic factors and found that white collar households indicated a greater importance of reputation, modern facilities and location, high income household attached greater importance to interest rates, opening hours, friendliness of staff and low income households relied on favorable publicity and word of mouth

Prus and Brandt (1995), have described a 'Secure customer Satisfaction Index' where they have taken three major components to measure loyalty: overall customer satisfaction, likelihood of repeat business, and likelihood to recommend the company to others. They describe these three components as the core of a meaningful customer loyalty index.

Singh and Kaur (2011), determined the factors that have an impact on customer satisfaction as regards the working of select Indian universal banks. The key findings of the study show that customer satisfaction is influenced by seven factors – employee responsiveness, appearance of tangibles, social responsibility, services innovation, positive word-of-mouth, competence, and reliability. The results of multiple regression showed that three variables: social responsibility, positive word-of-mouth, and reliability have major influences on the overall satisfaction of the customer.

Factors Affecting Customer Loyalty Status

There are a variety of factors which influences customer behaviour & attitude and maintains or strengthening loyalty status. A loyalty-supporting factor may be defined in the following way, "A loyalty-supporting factor is a factor that works to maintain or increase customer loyalty status by increasing customer behavioural loyalty and or attitudinal loyalty."

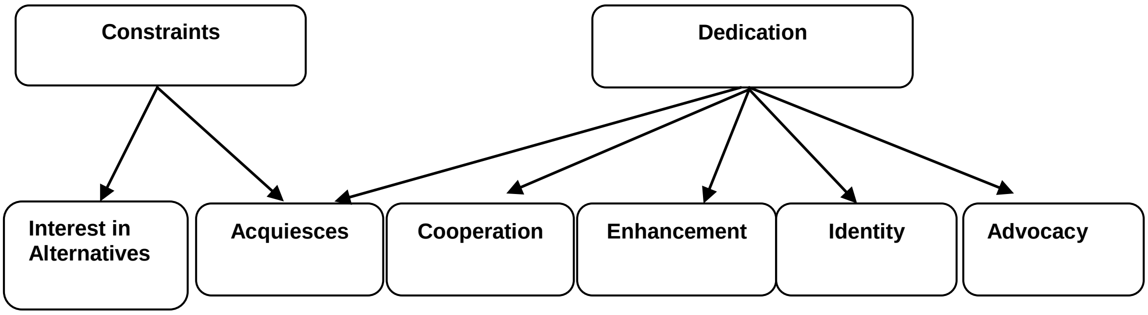
Loyalty-supporting factors

As customer retention and relationship maintenance are central concepts of the relationship marketing paradigm (Harker 1999), considerable research has been conducted about factors that maintain relationships. In the begining, the focus was on situational and personality factors which to result in a sale, but the focus is shifted in the direction of studying factors that assist relationship development.

Reasons for relationship maintenance in customer behavioural loyalty, have two perspective viz. economic and psychological perspective. The economic point of view considers economic factors such as the costs and benefits of staying loyal, while the psychological point of view considers affective factors such as satisfaction and commitment (Bendapudi and Berry 1997).

According to Bendapudi and Berry, customers stay loyal to a service provider either because they want to, or because they do not perceive any other options. They used romance theories to describe relationships as dedication- or constraint-based. Constraint-based loyalty occurs when customers believe they cannot exit a relationship due to economic, social, or psychological costs.

Continuation is the essential element of dedication-based relationship of customer. Constraints can make a relationship continue, while dedication can make it grow. Both factors that grounds dedication and constraining factors are hence loyalty-supporting factors, but with diverse effects on the customer loyalty status.



Loyalty-Supporting Factors That Cause Dedication

Dedication-based relationships are based on the customer's eagerness to be involved in a relationship. A key feature of dedication-causing factors is that customers recognize them positively, thereby causing dedication rather than constraint. Factors that source dedication are: affective commitment, positive bonds, trust, relational benefits, satisfaction and service quality, and company image.

Affective commitment is an antecedent of dedication. It is a psychological state which results from customers liking or even loving, and therefore becoming emotionally attached to their service provider. Affective commitment is the most effective kind of commitment for developing and maintaining relationships (Wetzels et al. 1998). It has a positive effect on

- Intentions to stay in the relationship,
- Desire to stay in a relationship,
- Performance and
- Willingness to invest in a relationship.

On the other hand it has a negative impact on

- Interest in alternatives, and
- Opportunistic behaviour.

Bonds can be positive, negative or neutral and several bond types exist as both positive and negative but only positive bonds generate dedication. Bonds may be of following kinds

1. Economic or financial bonds (Berry 1995) can be perceived as positive by the customer if the current service provider is perceived to provide greater economic conditions, e.g. special pricing.
2. Legal bonds can promote dedication if the fact that both parties are bound by an agreement, e.g. concerning a loan, makes the customer feel more secure and therefore dedicated to the relationship.
3. Knowledge bonds can be perceived as positive if familiarity reduces risks and increases customers' comfort levels.
4. Structural bonds exist if the service level and structure appeal to the customer .
5. Geographical bonds can promote dedication if the customer chooses to remain loyal to a bank due to its origin, i.e. prefers a local bank.

Trust is defined as the willingness to rely on an exchange partner in whom one has assurance or assurance in an exchange partner's reliability and truthfulness. In social psychology trust is considered to consist of two essentials: trust in the partner's honesty, and trust in the partner's benevolence. Honesty is the faith that a partner stands by his word, while benevolence is the faith that the partner is interested in the customer's welfare, and will not take actions with negative impact on the customer. (Morgan and Hunt 1994)

Relational benefits consist of the customer's awareness of benefits that are available to the customer as a result of being involved in a relationship. These are the benefits customers obtain from enduring relationships above and further than the core service performance. Benefits may be classified into monetary rewards, soft rewards, and recognition Arantola (2003).

1. Monetary rewards consist of both free items/services, discounts or bonuses
2. Soft rewards are unique handling benefits that divides into convenience benefits, e.g. fast service, avoided search and learning costs, customisation benefits, e.g. special service or preferential treatment, and specials, e.g. happenings and seminars or gifts.
3. Recognition consists of confidence benefits, e.g. feelings of comfort, security, trust, relevance benefits, i.e. important role in the customer's life, creating meaning for the customer, and social benefits, which can be either tangible signs of the

relationship or benefits realised by personnel, e.g. personal recognition or friendship.

Satisfaction has generally been thought of as a key factor influencing customer loyalty and to understand the relationship between satisfaction and loyalty focus is given on intensity of satisfaction.

Company image has also been found to have a significant influence on customer loyalty and it has an even stronger impact on prospect customer loyalty than satisfaction (Zins 2001). The importance of company image is particularly high in complex services where customers tend to use extrinsic cues (such as company image) rather than intrinsic cues (e.g. service characteristics).

Loyalty-supporting factors that act as constraints

Constraints have an affirmative effect on behavioural loyalty but not on attitudes, and may even have unpleasant effects on customer attitudes. Hence, constraints have a weaker positive effect on customer loyalty position and will only decide whether a relationship will continue.

The major trait of constraint-based loyalty is that it exists for other reasons than the customer's wish to stay loyal. When a relationship is maintained due to calculative obligation, it will just persist as long as the benefit of enduring in the relationship is more that the benefits of switching service providers. The benefits and costs are influenced by bonds, switching barriers or switching costs. Following are the factors that can be considered as constraints:

Economic costs or bonds

There are diverse forms of economic costs such as either termination costs of leaving the provider or joining costs of starting a new relationship. This can be considered an investment in the relationship, which is gone if the relationship is discontinued. Once a consumer has made this investment, it may become a constraining cause to reside with a service provider.

Search and evaluation costs

Pre-switching search and evaluation costs represent consumer perceptions of the time and effort invested in finding an alternative service provider and evaluating option. Some of the features of services like intangibility, heterogeneity and inseparability, makes these costs important.

Learning costs, knowledge bonds or post-switching behavioural and cognitive cost work as constraining factors if the customer perceives that it is too demanding to learn to know a new service provider and the services provided there.

Perceived risk or uncertainty costs

Consumer behaviour is enthused by a wish to reduce risk, and therefore consumers expand various strategies for this. One mode of dropping risk is to become loyal to brands, products, stores or marketers, thereby sinking the set of choices. Perceived risk is considered to have six elements: financial, performance, social, psychological, safety, and time/convenience loss (Colgate and Lang 2001).

Lack of perceived available or attractive alternatives

Customers are encouraged to continue relationships by short of choice and perceived alternatives which may result into a low degree of differentiation. Even if the customer is conscious of other possible service providers, a low degree of differentiation may cause the customer to perceive little differences between the providers, and therefore not perceive benefits large enough for switching (Colgate and Lang 2001).

Legal bonds ties customers through an agreement preventing way out. In banking, mortgage deeds can be tied so that excess amounts of the mortgage deed cannot be used as security for a loan at another bank. This might make it impossible for the customer to seek new loans at another bank and can therefore act as a powerful barrier to switching. Time-bound financial services, e.g. deposits or loans, can create barriers to switching if they cannot be altered before the point of maturity (Liljander and Strandvik 1995).

Structural bonds exist if the customer has achieved preferential treatment that would demand time to reach elsewhere (Berry and Parasuraman 1991). In banking, structural bonds can exist if a customer has reached high in the customer loyalty program and does not want to lose that position.

Geographical bonds exist if the service location ties the customer to the provider include geographic bonds among the relationship extrinsic factors driving relationship endurance. In banking, this could happen for customers who experience a need to live close to a branch office and therefore believe they cannot switch banks.

Social costs consist of the customer's perception of loss related to a switch of service providers in a social sense, i.e. related to the loss of contact to appreciated contact persons (Johnson 1982).

Customer apathy, passivity, inertia, habit, convenience, lack of motivating event: The permanent nature of banking services makes it simple to continue using the service without a real aspiration to do so (Becket 2000), and as long as the customer does not perceive strong enough reasons to switch banks, the simplest solution is to stay loyal. Inertia keeps customers engaged in relationships due to either low motivation for change or a low degree of involvement.

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