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The Influence of Relationship Quality on Customer Loyalty in the Dual-Banking System in the Northern States of Peninsular Malaysia

Maria Abdul Rahman ^{a*}, Mona Fairuz Ramli^b

^{a,b} School of Business Management, Universiti Utara Malaysia, 06010 Sintok, Kedah, Malaysia

Abstract

While relationship quality has been known as one of the most influential predictors of customer loyalty, relational norms are also likely to have an impact on relationship quality and customer loyalty. However, limited research had been conducted on the relationships between relational norms, relationship quality, and customer loyalty in a single framework and in business-to-consumer context. Therefore, this study intends to investigate the relationships between relational norms and relationship quality, and between relationship quality and customer loyalty. Results indicate that a mediation effect of relationship quality exists on the link between relational norms and customer loyalty.

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Keywords: Customer loyalty; Dual-banking system; Islamic banks; Partial Least Squares; Relational norms; Relationship quality

1. Introduction

It is undeniable that the Malaysian Islamic banking industry which started almost four decades ago plays an important socioeconomic role within the nation's economy. The Malaysian Islamic banking industry is unique. Besides the full fledged Islamic banks, the industry also consists of the dual-window Islamic banks. Under this system, conventional banks are given the permission by Bank Negara Malaysia to offer and sell Islamic banking products through their subsidiaries by utilizing their existing infrastructure, staff, and branch network. As a result, the Malaysian Islamic banking is facing fierce competitions where the conventional and Islamic banks are competing to gain market share (Muhammad et al., 2015). As competition intensifies in this near-saturated banking industry, it is crucial for

* Corresponding author. Tel.: 604-9287483; fax: 604-9287422.
E-mail address: maria@uum.edu.my

Islamic banks to retain current customer since the costs of retaining existing customers are lower than the costs of acquiring new customers (Reichheld and Sasser, 1990). In the competitive financial services landscape, it is appropriate to use relationship marketing strategy as a strategic tool (Liang and Wang, 2005). Review on past literature has noted the importance of relationship quality in predicting customer loyalty (Liu et al., 2011; Athavale et al., 2015). Numerous factors including price fairness, customer value, and communication had been found to have significant influence on relationship quality (Kim et al., 2006). Nevertheless, along with these “hard” factors, “soft” factors also play an important role. Morgan and Hunt (1994) examined the “soft” factors that matters in relationships and relational norms were identified to have strong impact on the customer’s quality of relationship. While relational norms are quite apparent in inter-firm relationships, in marketing they have received little attention among scholars (Berthon et al., 2003).

Although several research has examine the impact of relationship quality on customer loyalty and that of relational norms on relationship quality, however, less often they are studied in a single framework. Therefore, it is crucial to determine the contributions of relational norms and relationship quality to customer loyalty in the B2C settings. In addition, relationship quality has also been found to be a mediator variable in several studies (e.g., Crosby et al., 1990; Lin and Ding, 2006; Zhang et al., 2011). Thus, this study aims to examine the impact of relational norms on relationship quality among the dual-window Islamic banks and their customers and the effect of these two variables on customer loyalty. This study will also investigate the likely mediation effect of relationship quality on the link between relational norms and customer loyalty. It is important to examine these relationships as service providers can maximize the magnitude of relational norms and relationship quality in predicting customer loyalty.

2. Literature Review

2.1 Customer Loyalty

The most commonly used definition of loyalty in the context of consumption is given by Oliver (1997) as “a deeply-held commitment to rebuy or patronize a preferred product or service consistently in the future, thereby causing repetitive purchasing, despite situational factors that may cause switching behavior.” According to George and Stavros (2013) customer loyalty has consistently been recognized as a key determinant of customer retention. In the relationship marketing research, customer loyalty plays a central role due to its positive effect on long-term profitability (Floh and Treiblmaier; 2006). Customers who are loyal toward the firms’ products or services tend to repurchase more often and spend more money. As suggested by Reichheld and Sasser (1990), firms that aim to achieve superior performance and gain long-term profitability should focus on customer loyalty. This study conceptualized loyalty as an attitudinal loyalty due to the criticism on behavioral loyalty which lacks of conceptual basis of the causes of loyalty (Samaan, 2015). Customer loyalty in the Islamic banking system has been a major concern to practitioners due to the stiff competitions and the current focus on the relationships between consumers and organizations (Samaan, 2015).

2.2 Relational Norms and Relationship Quality

Relational norms exist in any relationship but their strength varies according to the position of the relationship on the relationship continuum (Chen and Lin, 2011). Norms can be used to govern a relationship when they become internal to a relationship and may apply to industry sectors, firm, to an individual business, or to each separate transaction (Ivens, 2006). Unlike norms that governed behavior in discrete transactions, relational norms are an endogenous form of behavior control that do not rely on market forces, but rely on cooperation, trust, common goals, and communication to coordinate the relationship (Morgan and Hunt, 1994). This study treated relational norms as a higher order construct consisting of flexibility, solidarity, and information exchange as suggested by Heide and John (1992). Flexibility refers to the service providers’ readiness to adapt to changes in circumstances that occur in their relationship and it can reduce the possibility of a broken relationship (Heide and John, 1992). Solidarity is a belief that parties in a relationship will support each other to maintain the relationship (Cannon and Perreault, 1999). Information exchange norm reduces the likelihood of being cheated because parties receive information to better cope with uncertainties (Heide and John, 1992). Ivens and Pardo (2007) found relational norms directly influenced relationship quality among German purchasing managers. In the pharmacy settings, Doucette (1996) found relational norms influenced relationship quality. Thus, the following hypothesis was developed:

H1: There is a positive relationship between relational norms and relationship quality in the context of Islamic banks in the dual-window system.

2.3 Relationship Quality and Customer Loyalty

Relationship quality is an emerging mega-construct in marketing literature and has become a strategic imperative since good relationship is associated with loyalty creation, close collaboration, improved operational planning, security, and business flow continuity (Moliner et al., 2007). Many studies regard relationship quality as a meta-construct composed of several distinct and related dimensions, while several empirical studies examine relationship quality as a pure single construct (Crosby et al., 1990; Dorsch et al., 1998). Even though there is no agreement among researchers as to what dimensions make up relationship quality, discussions of relationship quality often centers and assessed through some combinations of the three primary dimensions: trust with exchange partners, satisfaction with the exchange partners, and commitment on the ongoing relationship (Dorsch et al., 1998). This study defines relationship quality as higher-order constructs composed of trust, commitment and satisfaction. Huntley (2006) found relationship quality had a direct effect on willingness to recommend in business-to-business (B2B) relationships. Lin and Ding (2006) also found relationship quality has an impact on customer loyalty of the Taiwanese Internet service providers. In addition, relationship quality has also been used as a mediating variable in many studies (Crosby et al., 1990; Lin and Ding, 2006; Zhang et al., 2011). Thus, the following hypotheses were developed:

H2: There is a positive relationship between relationship quality and customer loyalty in the context of Islamic banks in the dual-window system.

H3: Relationship quality mediates the relationship between relational norms and customer loyalty in context of Islamic banks in the dual-window system.

3. Research Methodology

The research focused on determinants of customer loyalty among dual-window Islamic banks' customers. Therefore, the population of this study is customers who patronize the dual-window Islamic banks. Following previous studies on customer loyalty, a survey was adopted as a method for data collection. Questionnaire with Likert scale ranging from 1 as "strongly disagree" and 7 as "strongly agree" was developed and distributed to individual customers of the five dual-window Islamic in the Northern States of Peninsular Malaysia. The items were adapted from previous studies and appropriate changes were made to make the items relevant to the present study. The questionnaires were distributed to 15 different branches of five dual-window Islamic banks in three towns (i.e. AlorSetar, Jitra, and Kangar) in the Northern States of Peninsular Malaysia. To avoid bias, respondents were randomly selected among the banks' customers who visited the selected branches during the chosen time intervals. The researcher approached every fifth bank customers to fill the questionnaire. In total, 300 questionnaires were distributed to the respondents in the selected branches. Out of the 300 questionnaires distributed, 139 were returned and this produces a response rate of 46.3 per cent. According to Crimp and Wright (1995) the response rate above 30 per cent is good and acceptable when the research uses survey questionnaire. To test the research hypotheses Partial Least Squares (PLS) approach was adapted. PLS can overcome limitations in the first generation multivariate statistical data and is also robust against skewed distributions. PLS can also be applied to complex structural equation model with a large number of constructs and it can handle both reflective and formative constructs. PLS is more suitable for prediction and theory development.

4. Research Findings

4.1 Response rate and demographic profile

Majority of the respondents of this study were male with the frequency level at 62.6 per cent while the female respondents' frequency level was 37.4 per cent. In terms of respondents' age, most of the respondents were in the age bracket of 20-29 years of age (69.8 per cent) while only 2.2 per cent were 60 years and above. Majority of the

respondents) holds Bachelor degrees (50.3 per cent), completed secondary level education (18.0 percent), and hold Diploma (15.8 per cent). Seventyone point two percent of the respondents earned between RM2,001 to RM4,000 per month followed with 10.8 per cent of the respondents earning between RM4,001 to RM6,000 per month.

4.2 *Confirmatory Factor Analysis*

4.2.1 *Measurement Model*

A measurement model was estimated with the purpose to refine all structural model measures. All items developed for this study were subjected to a confirmatory factor analysis (CFA). PLS approach was utilized to run the CFA and to test the research hypotheses. PLS analyses all path coefficients simultaneously and predominantly focuses on estimating and analyzing the relationship between latent variables in the inner model. The assessments of construct validity (convergent and discriminant validity) and reliability of the measurement model was done by conducting CFA using Smart PLS 2.0 software (Ringle et al., 2005). The items were analyzed for convergent validity, discriminant validity, and reliability based on the guidelines by Fornell and Larcker (1981). The measurement items are considered to have convergent validity when they are in agreement of measuring the same concept (Ramayah et al., 2011). In assessing convergent validity, factor loadings, average variance extracted (AVE), and composite reliability (CR) are commonly used. As suggested by Hair et al. (2011) loadings of all items should exceed the recommended value of 0.5, as shown in Table 1. AVE should also be greater than 0.5 to justify using a construct (Barclay et al., 1995). The AVE measures the variance captured by the indicators relative to measurement error. Results show that the AVE is between 0.675 and 0.826. The CR values are between the range of 0.907 and 0.947, which are above 0.7 as suggested by Fornell and Larcker (1981). These values are used to assess the inter-item consistency of the measurement model. Results show all items have adequate level of convergent validity.

The degree to which items measure different concepts known as discriminant validity (Garver and Mentzer, 1999) can be assessed using the following methods; (i) by examining whether items were loaded strongly on their own constructs, or (ii) by comparing the square root of all AVE for each construct so that they exceeded all the inter-factor correlations between that and each other construct, or (iii) by comparing the AVE with the squared correlation estimates. The bold values in Table 2 show the square root of the AVE of each construct, while the other values are the correlation coefficients between constructs. Results show that the square root of all AVE values for each construct exceeds all the inter-factor correlations between that and each other construct for each construct, indicating adequate level of discriminant validity. Results show that the measurement model is valid and reliable.

4.2.2 *Structural Model*

Structural model evaluation was conducted to test the predictive or causal relationship between constructs in the model. The assessment of structural model was conducted after checking for validity and reliability of the constructs in the measurement model. Once the validity and the reliability of the measurement model were confirmed, the model was evaluated by running the PLS Algorithm to examine the β -values of the path coefficients values. Next, a bootstrap re-sampling procedure (500 sub-samples) was used to generate the standard errors and t-values, which permits the β values (path coefficients) to be made statistically significant. This step involved testing the statistical significance of each path coefficient and to provide confidence intervals for all parameter estimates.

Table 1: Results of Measurement Model

Construct	Dimension	Item	Loadings	AVE ^b	CR ^a		
Relational Norms	Flexibility	FX1	0.914	0.814	0.929		
		FX2	0.910				
		FX3	0.879				
	Info Exchange	IE1	0.866			0.750	0.923
		IE2	0.874				

		IE3	0.846		
		IE4	0.878		
Relationship Quality	Solidarity	SO1	0.866	0.803	0.924
		SO2	0.914		
		SO3	0.905		
		TS1	0.857	0.709	0.907
	Trust	TS2	0.828		
		TS3	0.869		
		TS4	0.813		
		CO1	0.908	0.826	0.934
	Commitment	CO2	0.935		
		CO3	0.882		
		ST1	0.879	0.818	0.947
		ST2	0.921		
	Satisfaction	ST3	0.894		
		ST4	0.923		
		LO1	0.836	0.675	0.912
LO2		0.895			
Loyalty	LO3	0.826			
	LO4	0.743			
	LO5	0.800			

^aComposite reliability (CR) = (square of the summation of the factor loadings) / {(square of the summation of the factor loadings) + (square of the summation of the error variances)}

^bAverage variance extracted (AVE) = (summation of the square of the factor loadings) / {(summation of the square of the factor loadings) + (summation of the error variances)}

Results in Table 3 show that relational norms positively influence ($\beta = 0.869, p < 0.05$) relationship quality. Relationship quality also exhibited a strong positive influence ($\beta = 0.837, p < 0.05$) on customer loyalty. The results gave a t-value of 31.828 from relational norms to relationship quality, thus, supporting H1. H2 is also supported in which relationship quality was shown to have a significant impact on customer loyalty with the t-value of 32.349.

Table 2: Results of Discriminant Validity

	Commitment	Loyalty	Flexibility	Information Exchange	Satisfaction	Solidarity	Trust
Commitment	0.909						
Loyalty	0.768	0.821					
Flexibility	0.704	0.764	0.902				
Information Exchange	0.665	0.781	0.810	0.866			
Satisfaction	0.832	0.797	0.780	0.713	0.904		
Solidarity	0.698	0.777	0.846	0.802	0.754	0.896	
Trust	0.762	0.759	0.813	0.847	0.774	0.802	0.842

Diagonals (in bold) represent the square root of average variance extracted while the other entries represent the correlations.

4.2.3 Testing for Mediating Effect of Relationship Quality

The mediating effect of relationship quality (MV) on the link between relational norms (IV) and customer loyalty (DV) was tested using the steps suggested by Preacher and Hayes (2004). The indirect effect ab , an estimated standard error, and both the indirect effects interval at 95% confidence level were estimated using the bootstrapping procedure. Path a and b represent the values of the relationships between relational norms (IV) and relationship quality (MV), and relationship quality (MV) and customer loyalty (DV), respectively.

Table 3: Results of the Structural Model

Hypothesis	Relationships	Beta	Std Error	t-value	Decision
H1	Relational Norms -> Relationship Quality	0.869	0.027	31.828	Supported*
H2	Relationship Quality -> Customer Loyalty	0.837	0.026	32.349	Supported*

* $p < 0.05$

Results in Table 4 shows the indirect effect is estimated to be 0.727. In addition, the bootstrapped estimation of lower and upper limit lie between 0.649 and 0.805 at 95% confidence level. Since zero does not lie in the 95% confidence interval, it can be concluded that the indirect effect is significantly different from zero at $p < 0.05$ (two tailed) (Preacher and Hayes, 2004). Therefore, hypothesis H3 is supported, confirming relationship quality has a mediating effect on the link between relational norms and customer loyalty.

4. Discussions and Implications

This study found that relational norms and relationship quality have been found influence customer loyalty. Relationship quality was also found to be a mediator between relational norms and customer loyalty. This result added to the literature by providing additional support to the findings in previous empirical studies. Studies conducted by Lin and Wang (2006) in the B2C market and by Eggert and Ulaga (2006) in the B2B market found that loyalty is mediated by relationship quality. Result of the latter also confirms that relational norms are contributing factors to high quality and long-term relationships. Findings from this study suggest that if the Islamic bank

Table 4: Results of Mediator Testing

Hypothesis	Path a	Path b	Indirect Effect	Std Error	t-value	Bootstrapped Confidence Interval	
			a*b			95% Lower Limit	95% Upper Limit
H3	0.869	0.837	0.727	0.040	18.14*	0.649	0.805

* $p < 0.05$

bank wants to benefit from customer loyalty (e.g. increase in profitability and positive word of mouth) there is a need to emphasis on relational norms and the quality of relationship with its customers. Moreover, this study shows if the bank practices flexibility, solidarity, and exchange of information in their services, it will be able to develop high quality relationships with their customer, which will lead to customer loyalty. It is important for the Islamic banks in the dual banking system to provide continuous training to the front liners. This practice ensures the bank employees to have the knowledge that can create good relationships with the customer. Since most banks are offering almost identical products, they banks should emphasis on relationship marketing in developing relationships with their customers. It should also be noted that the development of customer loyalty depends on a well-managed formation of relational norms and relationship quality. Customer loyalty will only develop after relational norms create customer satisfaction, trust, and commitment towards the Islamic bank in the dual-banking system.

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