# Customers' Perception about the Determinants of Service Quality of Foreign and Domestic Banks: An Empirical Study on Bangladesh

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**ABSTRACT**

*This paper investigates the determinants of perceived service quality among the customers of domestic and foreign banks in Dhaka, Bangladesh using a modified version of SERVQUAL model. It finds that in general the foreign banks provided marginally better measures in most of the dimensions than did the domestic banks. For domestic private banks reliability, communication, credibility, security, and tangibility are found to be significantly affecting the service quality. On the other hand, for foreign banks, reliability, credibility, and tangibility are the only significant factors affecting their service quality.*

**Keywords:** Determinants of Service quality, Banking industry, Bangladesh, SERVQUAL Model.

## 1. INTRODUCTION

**Background of the Research**

In the modern competitive environment, the pursuit of service quality (SQ) is considered to be an essential strategy. Many service organizations have responded to the promise of the strategic and financial impact of quality, treating it as a valuable tool (Paradise-Tornow, 1991). Companies that have goods and services perceived as being of high quality typically enhances customer retention rate, helps attract new customers through word of mouth advertising, increases productivity, leads to higher market shares, lowers staff turnover and operating cost and improves employee morale, financial performance and profitability

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(Julian and Ramaseshan, 1994; Lewis, 1989; 1993) But the companies that have goods and services that are perceived as being of low quality cannot achieve the above. It is apparent that, in the long term, the most important factor affecting business performance is the quality of goods and services offered by the organization, relative to its competitors. Attention to SQ can help an organization to differentiate itself from others and to gain a lasting competitive advantage. Many companies therefore, try to deliver a service with superior and differentiated SQ.

Perceived service quality determinants tend to play an important role in high skill and technology-involving industry like banking service. Banks have traditionally placed a high value on customer relationships with both commercial and retailing customers. However, the nature of the customer relationship is changing particularly in the retail side of banking. In other words, as their (i.e., banks) services become more or more "high tech", their technical services become standardized, reducing the importance of such services as differentiating factors; thus customers will evaluate banks based more on their "high touch" factors than their "high tech" factors (Urban and Hauser, 1993). In view of this, delivering quality service to customers is a must for success and survival in today's competitive banking environment (Samit and Frohlich, 1992).These service-quality issues have long been neglected in developing economies unlike the developed economies like the USA and Europe (Kassem, 1989; Firoz and Maghrabi, 1994; Yavas et al., 1997) and this also applies to the banking industry (Angur et al., 1999). Bangladesh being a developing economy, its banking sector with a wide geographical reach catering to the needs of a huge clientele offers an excellent scope for research on the issue of customer service quality in banking (as perceived by the customers), and can provide the beacon for the evaluation of effectiveness of banking in developing economies. So, the identification of the determinants of service quality of different foreign and domestic banks could be managerial tactical tools for improving the banking service.

## Research Problem and Research Questions

Banking is no longer regarded as a business dealing with money transactions alone, but is also seen as a business related to information on financial transactions (Padwal, 1995). In other words, it is believed that information technology (IT) plays a significant role in providing better customer service, presumably at a lower cost. Several innovative IT-based services such as automated teller machines (ATM), electronic fund transfer, anywhere-anytime banking, smart cards; net banking, etc. are no longer alien concepts to banking customers (Rawani and Gupta, 2000). But the diffusion of technology is somewhat slow in domestic banks (public and private sector banks) (Banker, 1998). In the case of private sector banks, bank automation has been far easier as

their size is small and they also started their operations afresh. As regards the foreign banks, they already have the advantage of good automation experience in several banking applications (Kaujalgi, 1999). Although the presence of private sector banks and foreign banks have kindled a competitive spirit among them, with respect to the quality of services delivered by them in terms of the intensity, depth, diversity and range of services offered differ from one another. In this backdrop, the present study makes a spirited attempt to investigate the service-quality issues from the perspective of the customers in the foreign and domestic banking industry of the developing economy of Bangladesh.

This study intends to answer the following two questions:

Question one: What are the dimensions of customer service quality and how valid and reliable are these dimensions?

Question two: Are there differences in service quality between foreign and domestic banks?

Question one: is necessary because of the recognized instability of the dimensions of SERVQUAL (VanDykeetal., 1997; Carman, 1990).The convergent validity is addressed by conducting factor analysis.

Question two: will shed light on the level of satisfaction of customer with service quality they receive at foreign and domestic banks, and provide improvement directions to bank managers. It will also test the assumption that foreign banks provide higher service quality than domestic ones.

## Domestic and Foreign Banks in Bangladesh

Banking institutions in Bangladesh can be classified under different groups. Most banks practice branch banking, i.e., the banks operate through branches at home and abroad under the control of their head offices. Foreign branches of Bangladeshi banks have to abide by home country regulations. Under the ownership-based classification, banks in Bangladesh are classified as government/nationalized, private, foreign, and joint ownership banks.

## 2. LITERATURE REVIEW

### Perceived Service Quality

Quality has been defined as the consumer's overall impression of the relative inferiority or superiority of the organization and its services (Zeithaml *et al*., 1990; Taylor and Baker, 1994). Perceived service quality is an attitude of a consumer judgment on the overall service. Perceived service quality results from a comparison of consumers' expectations with their perceptions of the service actually delivered by supplier (Kangis and Voukelatos, 1997) e.g. providing services which are not provided by others; positive word of mouth to others

about the service overall the customers are found to be satisfied with services of the bank.

**Perceived Service Quality Models**

Various models have been developed for measuring perceptions of service quality (Grönroos, 1983, 1990; Parasuraman *et al*., 1985, 1988; Stafford, 1996; Bahia and Nantel, 2000). Most writers agree that customers' expectations are rarely concerned with a single aspect of the service package but rather with many aspects (see, for example, Berry et al., 1985; Johnston and Lyth, 1991; Sasser et al., 1978). Parasuraman et al. (1985) provided a list of ten determinants of service quality as a result of their focus group studies with service providers and customers: *access, communication, competence, courtesy, credibility, reliability, responsiveness, security, understanding and tangibles*. In a later article that year (Berry et al., 1985) added that: although the relative importance of the categories would vary from one service industry to the next, we believe the determinants of service quality in most (if not all) consumer service industries are included in this list.

In the next phase of their research, Berry et al. (1985) found a high degree of correlation between, on the one hand, communication, competence, courtesy, credibility and security, and, on the other, between access and understanding; and so they created two broad dimensions of assurance and empathy, that made it a total of five consolidated dimensions. They then used the five dimensions – tangibility, reliability, responsiveness, assurance and empathy – as the basis for their service quality measurement instrument, SERVQUAL (Parasuraman et al., 1988; Zeithaml et al., 1990). Finn and Lamb (1991), for example, in a study of retailing, concluded that their results did not support Berry et al.'s (1985) belief that the instrument could be used to assess quality in a wide range of service-firms. They found that the model's five dimensions were insufficient to cover quality in a retailing setting. They questioned particularly whether the five dimensions are generic and suggested that much development and refinement was needed. Cronin and Taylor (1992), in their research into service quality in banks, pest control, dry cleaning and fast food, also found little support for the five dimensions. They stated: our results suggest that the 5-component structure proposed by Parasuraman et al. (1988) for their SERVQUAL scale is not confirmed in any of the research samples. On the other extreme, research by Johnston et al. (1990) involved some testing of the comprehensiveness of Parasuraman et al.'s (1988) service quality determinants in the light of empirical data gathered in ten UK service organizations. The questionnaire used in this study is based on the ten-dimensions instrument developed by Parasuraman et al. (1985). This earlier version of SERVQUAL was preferred over the five-dimension alone, as a starting point for developing a customer service quality

instrument (ReidenbachandSandifer-Smallwood, 1990). This is because it explicitly includes ten dimensions, which allows better coverage of all aspects of bank service quality.

## 3. METHODOLOGY

**Model**

In principle, to estimate the service quality of foreign banks and domestic banks, the key approach is to treat service quality as our dependent variables, which in turn is determined by the various independent variables that measure different hypotheses. This study need to identify the different indicators/constructs, which can be used to measure these qualitative variables. The Basic, Model for the study is the following:

*Overall Service quality = f (reliability, responsiveness, Competence, Accessibility, Courtesy, Communication, Credibility, Security, Understanding/knowing, Tangibility)*

Measured perceived service quality toward foreign banks and domestic banking as a dummy variable and run the following regression model of the perceived service quality toward foreign banks and domestic bank.

Specifically,

$$SERVQUAL = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + \beta_8 X_8 + \beta_9 X_9 + \beta_{10} + e$$

Where,

SERVQUAL = Overall service quality of bank

$X_1$ = Reliability

$X_2$ = Responsiveness

$X_3$ = Competence

$X_4$ = Accessibility

$X_5$ = Courtesy

$X_6$ = Communication

$X_7$ = Credibility

$X_8$ = Security

$X_9$ = Understanding/Knowing

$X_{10}$ = Tangibility

Where, $\alpha$ is constant and $\beta_1$, $\beta_2$, $\beta_3$, $\beta_4$, $\beta_5$, $\beta_6$, $\beta_7$, $\beta_8$, $\beta_9$, $\beta_{10}$ are coefficients to estimate, and e is the error term, which the authors assumed as NID for this research.

**Secondary Data Collection**

Some secondary data like the background of the banks and the services they are providing in this country. These secondary data have been collected from different web sites and from the brochures of these banks. Unfortunately the data insufficiency and provided little guidance, numbers of private banks are increasing rapidly.

**Primary Data Collection**

3.3.1 Sampling plan: The first step of the sampling design is to define the study population. This study restricted its sample within the banks of Dhaka city. The population has been defined as the customers of domestic or foreign banks services. The customers have been selected from different demographic variables e.g. age, gender, income, occupation, education. Because of the limited number of foreign banks in the area under consideration, the criteria for selecting foreign banks were non-probabilistic. First the foreign banks have been selected on the basis of their size and nature. Then the customers have been selected using a simple random sampling method. In case of selecting domestic banks, the study used cluster sampling where the customers were categorized based on their income. The domestic banks in Dhaka city have been divided into three clusters, namely higher net income, medium net income and low net income. After clustering the domestic banks, the study selected five domestic banks from each cluster randomly. In the final stage of selecting the samples, the customers from these fifteen domestic banks were chosen using stratified random sampling criteria. The stratification had been done in terms of number of customer in the clusters. Because of resource and time constraints and preliminary nature of investigation, 300 interviews were planned from Dhaka city.

*Questionnaire Design and Pretest*

The developed instrument includes 34 items: four items each were considered to measure tangibility and communication dimensions, six items for measuring accessibility, two items for courtesy and three items each for measuring understanding, reliability, security, credibility, responsiveness and competence dimensions. Respondents were asked to indicate to what extent they agree that each item met their expectations on a five-point Likert scale with *"strongly agree"* reflecting the highest level of service quality and *"strongly disagree"* indicating the lowest level of service quality . The questionnaire was developed in English on the basis of insights from interviews with the customers

of the banks. Very few questions were open ended because analysis and interpretation of such question can be complex and subjective. Close-ended questionnaire was used to collect data from the respondents. The hypotheses, the constructs and their operational definitions are given as annex – 1 of this study. Some demographic questions were in the questionnaire for a more in-depth interpretation of responses. The original a questionnaire was pre-tested with a few dummy respondents to ensure quality of the questions in terms of preciseness, conciseness, objectivity and understandability of the questions. On the basis of feedback from the pre-testing, the original questionnaire has been modified for the final and ultimate survey.

### Survey Method

Those who agreed to complete the survey were informed of the purpose of the study and assumed anonymity. After a quick screening the questions on whether respondents used this bank in past twelve months, interviewers' proceeded with the survey questions and face-to-face interview with the respondents were conducted. In the event that the respondents were educated, they were asked to fill the questionnaire; otherwise the interviewer fills the questionnaire based on the respondent's verbal response to the questions. A total of 290 surveys were completed, of these, 18 were considered problematic due to excessive missing data; refused to answer many questions and response biases. The data from these questionnaires were not included in the data set. Thus a total of 272 responses were documented and analyzed.

### 4. ANALYSIS OF DATA

Table 1 presents the mean values of all the variables for both the types of banks. It shows that the mean values for almost all the variables are higher for the foreign banks than that of the domestic banks. Among all the attributes accuracy in the billing scores the highest for both types of banks. It can be inferred that people's trust in the banking system from the viewpoint of accuracy is quite high.

The differences between the mean values of both types of banks further indicate that on the technology related services such as availability of debit/credit cards and internet banking, people are better satisfied with the private banks. Besides this the public banks mostly lagging with the services related to evening banking.

Table 2 shows the regression results run on both the foreign banks and domestic banks. The F statistic shows the significance of regression equation, though the independent variables selected only explain 33% and 48% of change in the dependent variable for the foreign banks and domestic banks respectively. It is interesting to note that the same independent variables explain quite

substantial changes in dependent variable for foreign banks compared to the domestic banks. Some different attributes need to be incorporated to measure the service quality. Overall for a cross-sectional $R^2$ values can be considered as satisfactory in explaining the goodness of fit of the regression equation.

TABLE 1

**MEAN VALUES OF 34 ATTRIBUTES/VARIABLES MEASURED N 5 POINTS LIKERT SCALES OF FOREIGN AND DOMESTIC BANKS**

| SL. NO. | Attributes/ Variables | Mean Value for Foreign Banks | Mean Value for Domestic Banks |
|---|---|---|---|
| 1. | Accuracy in billing is very essential for banking transaction | 4.92 | 4.72 |
| 2. | Bank keeps record correctly | 4.62 | 4.49 |
| 3. | Bank performs the service at a designated banking time | 4.31 | 4.17 |
| 4. | Bank mails me the transaction slip as soon as any transaction occurs | 3.9 | 3.48 |
| 5. | Bank calls me back quickly if I face any porblem | 3.71 | 3.71 |
| 6. | If customer face any problem bank sets appointment quickly with the right person | 3.83 | 3.7 |
| 7. | Employees are highly knowledgeable and skilled in bank | 4.23 | 3.68 |
| 8. | Overall knowledge and skill of operational support personnel in bank is very high | 4.18 | 3.65 |
| 9. | Bank often conduct research(survey on consumers perception about their service) | 3.59 | 2.85 |
| 10. | never find the line busy whenever I access by telephone | 3.23 | 3.22 |
| 11. | Bank do not put me on hold during accessing the service by phone | 3.3 | 3.29 |
| 12. | Do not have to wait for long to receive the service at the bank | 3.7 | 3.65 |
| 13. | Bank provides ATM service and they are located in convenient place | 4 | 2.89 |
| 14. | Bank provides internet transaction service | 3.3 | 2.81 |
| 15. | Bank provides evening banking service | 4.15 | 2.86 |
| 16. | Employees of the bank are very much friendly and polite | 4.03 | 3.83 |
| 17. | Public contact personnel of this bank are very clean and neat in appearance | 4.33 | 3.96 |
| 18. | Bank clearly explains their service whenever I want to receive it | 4.18 | 3.96 |
| 19. | Employee clearly explain the cost for receiving the service | 3.83 | 3.82 |
| 20. | Bank always inform about the alternative whenever receive a service | 3.8 | 3.83 |
| 21. | Whenever customer face any problem bank assure the problem will be handled | 4.07 | 3.88 |
| 22. | Overall service reputation of bank is appreciable | 4.34 | 3.93 |
| 23. | This bank has a well reputation in this industry | 4.61 | 4.01 |
| 24. | Contract personnel of this bank are very trustworthy and honest | 4.09 | 3.9 |
| 25. | This bank provides high physical safety | 3.63 | 3.62 |
| 26. | No outsider knows about the deals between customer and banks | 4.44 | 4.25 |
| 27. | All branches of this bank are located in secured places | 3.83 | 3.81 |
| 28. | Employees of the bank can understand customer need perfectly | 3.6 | 3.61 |
| 29. | This bank always pays greater attention to individuals(customers) | 3.77 | 3.62 |
| 30. | Employees could recognize customer when came to bank for the second time | 3.76 | 3.55 |
| 31. | Interior decoration of the bank is very impressive | 4.23 | 3.69 |
| 32. | All the machines it is using are in good condition | 3.94 | 3.57 |
| 33. | Personnel of the banks are very formal in appearance | 4.24 | 3.79 |
| 34. | ATM/debit/credit card of this bank does not easily tear down | 4 | 3.11 |

TABLE 2

**REGRESSION MODEL OF FOREIGN AND DOMESTIC BANKS**

| Types of banks | R | R Square | Adjusted R Square | Std. Error of the Estimate | F | Sig. |
|---|---|---|---|---|---|---|
| Foreign bank | 0.642 | 0.412 | 0.335 | 0.48120 | 5.336 | 0.000 |
| Domestic Bank | 0.714 | 0.510 | 0.482 | 0.53840 | 18.130 | 0.000 |

A. Predictors: (constant), tangible, communication, reliability, responsiveness, understanding, security, competence, credibility, courtesy, accessibility.

B. Predictors: (constant), tangible, communication, reliability, responsiveness, understanding, security, competence, credibility, courtesy, accessibility

TABLE 3

**COEFFICIENTS OF FOREIGN AND DOMESTIC BANKS**

| Types of banks | | Model | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|---|---|
| | | | B | Std. Error | Beta | | |
| **Foreign bank** | 1 | (Constant) | 1.378 | .699 | | 1.970 | .052 |
| | | Reliability | .343 | .146 | .247 | 2.359 | .021 |
| | | Responsiveness | .114 | .096 | .155 | 1.190 | .238 |
| | | Competence | .094 | .104 | .125 | .909 | .366 |
| | | Accessibility | .165 | .123 | .206 | 1.348 | .182 |
| | | Courtesy | .051 | .115 | .068 | .446 | .657 |
| | | Communication | .151 | .126 | .156 | 1.195 | .236 |
| | | Credibility | -.289 | .160 | -.244 | -1.801 | .076 |
| | | Security | -.160 | .131 | -.169 | -1.220 | .226 |
| | | Understanding | -.045 | .096 | -.066 | -.467 | .642 |
| | | Tangible | .299 | .107 | .341 | 2.779 | .007 |

*Cont. Table 3*

| | | Coefficients[a] | | | | |
|---|---|---|---|---|---|---|
| **Types of banks** | **Model** | **Unstandardized Coefficients** | | **Standardized Coefficients** | **t** | **Sig.** |
| | | B | Std. Error | Beta | | |
| **Domestic Bank** | 1  (Constant) | -.127 | .481 | | -.263 | .793 |
| | Reliability | .219 | .104 | .124 | 2.119 | .036 |
| | Responsiveness | .060 | .065 | .061 | .934 | .352 |
| | Competence | -.078 | .067 | -.081 | -1.157 | .249 |
| | Accessibility | .110 | .076 | .101 | 1.439 | .152 |
| | Courtesy | .061 | .068 | .070 | .896 | .371 |
| | Communication | -.218 | .081 | -.194 | -2.691 | .008 |
| | Credibility | .476 | .084 | .423 | 5.663 | .000 |
| | Security | .115 | .070 | .103 | 1.649 | .101 |
| | Understanding | .077 | .077 | .076 | .992 | .322 |
| | Tangible | .244 | .071 | .240 | 3.420 | .001 |

a. **Dependent Variable: Service quality**

As far as Table 3 is concerned, the significant coefficients (at 10%) affecting the service quality for foreign and domestic banks differ from each other. For foreign banks significant variables affecting the customer satisfaction are reliability, credibility and tangibility of their services. On the other hand, for domestic banks, the significant variables are reliability, communication, credibility, security and tangibility. It is interesting to note that the customers' feel more secure with the domestic banks rather than the foreign banks. Furthermore they can better communicate with the domestic banks than the foreign banks.

## 5. CONCLUSIONS AND IMPLICATIONS

In banking today, the different actors offer a wide variety of products/services. Every bank has to consider how to build and protect its competitive position. They are forced to find a new basis for competition. A bank must examine its opportunities and take a position in the marketplace. Positioning is an attempt to distinguish the bank from its competitors along real dimensions in order to be the most preferred bank for a certain market segment.

Consequently, strategic positioning has become increasingly relevant and important for the banking industry. The ten determinants of service quality highlight the importance of effective market positioning and have examined the concept of bank positioning and different approaches that a bank can use to occupy a competitive position in the competitive marketplace. Attention has been focused on the strategies and approaches that a bank can use in positioning itself in the competitive marketplace (e.g. institutional, product/service, delivery system, and segment positioning). The study also reviews different variables and bases for bank positioning in the retail banking market and sheds light on the variables determining the customer satisfaction.

This study indicates that reliability, credibility and tangibility are common attributes determining the customer satisfaction for both foreign and domestic banks. However the customer feel more secured and are able to communicate better for the domestic banks rather than those of the foreign banks. The results of this analysis can be used as a message from the customers to the banks. The message is short and clear. This survey of customers' perceptions of the competing banks and their attributes is essential in providing the bank manager with a visual representation of the customers' view on the bank's attributes and position in the marketplace.

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Annex – 1

Hypotheses, Independent and Dependent Variables, Constructs and

Operational Definitions

| Hypothesis 1: | Construct: | Operational definitions: |
|---|---|---|
| Service quality toward a bank is influenced by customers' reliability for the banks | Reliability | • accuracy in billing;<br>• keeping records correctly;<br>• performing the service at the designated time. |
| *Hypothesis 2:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by bank's employee responsiveness towards customer | Responsiveness | • mailing a transaction slip immediately;<br>• calling the customer-back quickly;<br>• face any problem, set appointment quickly with the right person |
| *Hypothesis 3:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by competence of the employee | Competence | • knowledge and skill of the contact personnel;<br>• overall knowledge and skill of operational support personnel;<br>• research capability of the organization (often conduct the research) |
| *Hypothesis 4:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by accessibility with bank by the customer | Accessibility | • the service is easily accessible by telephone (lines are not busy and<br>• they don't put you on hold during accessing the service<br>• waiting time to receive service (e.g., at a bank) is not extensive;<br>• ATM services and convenient location of service facility<br>• evening banking service<br>• internet transaction service |
| *Hypothesis 5:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by courtesy of the employee towards the customer | *Courtesy* | • Friendliness and politeness of public contact personnel.<br>• clean and neat in appearance of public contact personnel. |

*Cont. Annex 1*

| Hypothesis 1: | Construct: | Operational definitions: |
|---|---|---|
| *Hypothesis 6:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by : communication between the customer and bank | Communication | • clearly explain the service whenever customer receive<br>• clearly explain the cost of receiving the service<br>• always inform about the alternative services<br>• assuring the consumer that a problem will be handled, |
| *Hypothesis 7:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by: credibility of the bank | Credibility | • Bank reputation in the industry;<br>• overall service reputation;<br>• personal characteristics (trustworthiness) of the contact personnel, |
| *Hypothesis 8:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by security of the bank | Security | • physical safety (Will I get mugged at the automatic teller machine?);<br>• financial security (no outsider knows about the deal );<br>• located in secured place |
| *Hypothesis 9:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by understanding/knowing the customer by the bank | Understanding/ knowing | • understand need perfectly<br>• learning the customer's specific requirements;<br>• providing greater individualized attention;<br>• recognizing the regular customer |
| *Hypothesis 10:* | Construct: | Operational definitions: |
| Service quality toward a bank is influenced by tangibility of the bank | Tangibility | • physical facilities (exterior/interior decoration of the bank);<br>• formal appearance of personnel ;<br>• Machines/equipment condition to provide the service;<br>• physical representations of the service, such as ATM/debit/credit card |
| Service quality toward a bank is influenced by Satisfaction | perceived service quality | • overall satisfied with service of the bank |