Evaluation of Customer Satisfaction on Islamic Microfinance: Empirical Evidence from Central Java, Indonesia

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ABSTRACT

The impact of customer loyalty was examined through the influence of service quality on customer satisfaction for a sample of 220 respondents, which were customers of Islamic microfinance institutions at Central Java, Indonesia. The Structural Equation Modeling (SEM) was used for analysis and it indicated that service quality has a significantly positive impact on customer satisfaction in this specific industry and region. The findings also supported that customer satisfaction has a significantly positive influence on customer loyalty.

Keywords: Customer satisfaction, Islamic microfinance.

Introduction

The Islamic microfinance institutions (IMFIs) are the non-bank financial institutions that have the highest expansion rate among all the MFIs in Central Java, Indonesia. There are approximately more than 515 institutions spread over some regencies.

The development of Baitul maal wattamwil (BMT), which are profit-loss sharing islamic microfinance institutions, today is no longer unique due to the fact that some other microfinance institutions are also offering similar services. The Islamic microfinance is offering similar services and operates side by side with the conventional ones. In addition, commercial banks also have begun to target Islamic microfinance's traditional customers. They have built small branches in the traditional market out of which most of them are IMFI customers. The competition will be strong not only in products but also services offered. The quality of service will be the final judgment factor for customers to make a decision about whether or not they should remain with the current provider or move to banks or others microfinance institutions, which provide better service quality. The factor of customer-loss might negatively affect IMFI. . Thus, IMFIs should be concerned with customer satisfaction and retention in order to survive in this competitive environment. Customer satisfaction has a great impact on securing the market position and for the survival for the institution.

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Most research studies stated that service quality has a strong association with customer satisfaction, manufacturing costs, customer retention, financial performance, customer loyalty and the success of marketing strategy (Cronin, Brady & Hult, 2000; Wong, Rexha & Phau, 2008). These studies generally looked at the interrelationship between customer service and satisfaction, and also product availability and customer satisfaction. Clearly, customers preferred better customer service in order to enhance their satisfaction levels.

Over the years, research on microfinance has mostly been concentrated on three key areas - sustainability of the institution, outreach to the poor and effect among the clients. In the context of Indonesia, there are a few studies, which focus on customer satisfaction in the Islamic-microfinance institutions. This paper investigated the effect of service quality on customer satisfaction and loyalty while focusing on the customers of Islamic Microfinance Institutions at the Central Java Province of Indonesia. The objective was to investigate the five dimensions of service quality of Islamic-microfinance in Indonesia and to assess the effect of service quality on customer satisfaction.

Figure 1: Theoretical Model of the Research
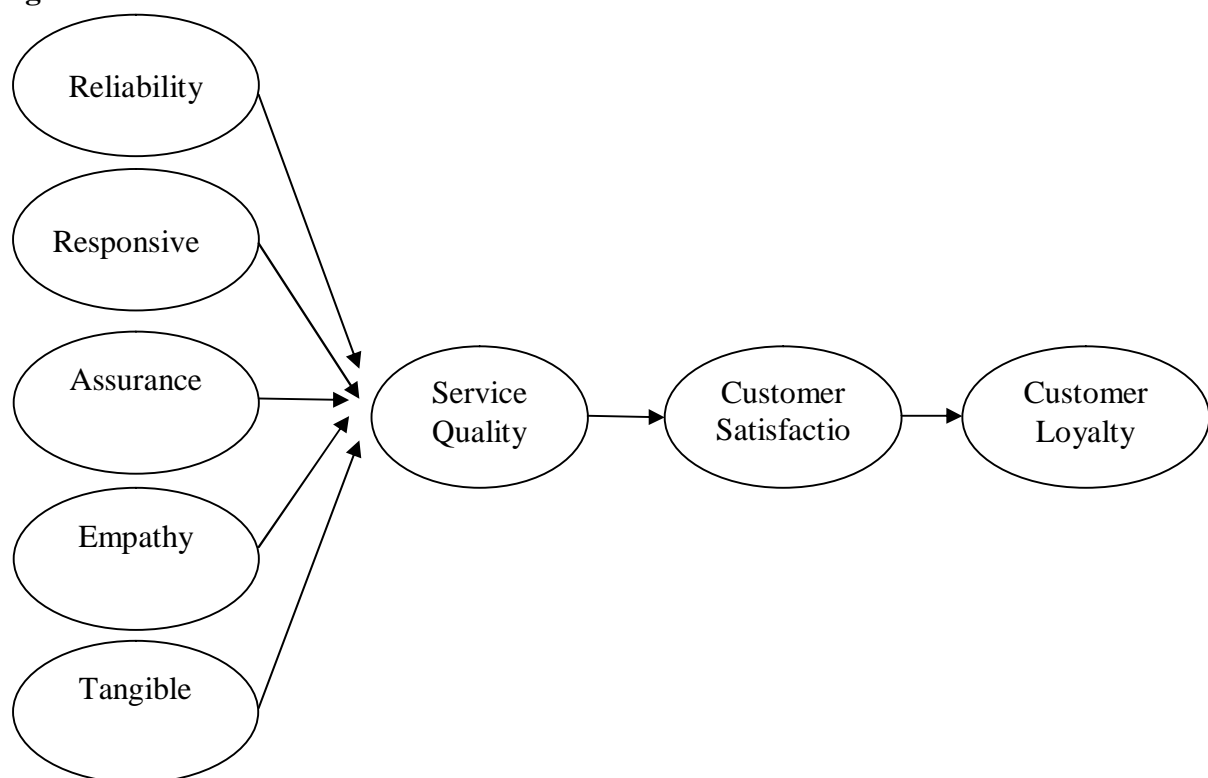
Correlations, means, and standard deviations for all variables are presented in Table 3.

Literature Review

Service Quality and Customer Satisfaction

Service quality has been identified as a critical element for success for organizations, which plan to establish their competitive advantage (Brahmbhatt & Panelia, 2008). According to Parasuraman, Zeithaml, and Berry (1988), excellence in service quality entails that a firm will have to excel along the five dimensions of service performance. These dimensions consist of: reliability, tangible, responsiveness, assurance and empathy.

The tangible dimension relates to the equipment, physical facilities, personnel, and communication materials. The reliability dimension refers to the aptitude to carry out the assured services consistently and correctly. The responsiveness dimension reflects the readiness of service providers to facilitate customers and provide timely service. The assurance dimension links to the knowledge and consideration of the employees and their capacity to express reliance and self-confidence. The empathy dimension denotes to the provision of consideration and special attention to the customers (Brahmbhatt and Panelia, 2008).

Brahmbhatt and Panelia (2008), explained service quality as perceived judgments resultant from an assessment method where customers equate their former expectations with the new perception was about the service received. The other dimensions are:

1. Functional quality: entails attributes related to process like: appearance, behavior, attitude, accessibility, internal relationship and service-mindedness and customer contact.
2. Technical quality: entails five attributes related to output: computerized systems, technical solutions, employees' technical ability, employees' knowledge and machine quality.
3. Image of the service provider: overall perception about the supplier.

A study on customer satisfaction has demonstrated that there is a significant and reasonable role of customer satisfaction with regard to organizational strategies of microfinance. Customers are determinant of business growth; therefore customer satisfaction is very important for retaining existing customers and attracting new ones (Khattak & Rehman, 2010).

In another study conducted by Dusuki and Abdullah (2007), it was found that employees' attributes like their competence, level of courtesy toward the customers and efficiency in banking operations are important determinants of bank selection for the customers. A study conducted by Haron, Ahmad, and Planisek (1994) supported that customers of banks consider employees behavior, friendliness, and efficient customer handling as the most important factors in the bank selection decision-making.

Amin and Isa (2008) studied that service quality is positively related with customer satisfaction in Malaysian Islamic banking. The service quality dimension also holds importance and the banking sector of UAE and Kumait (Otheman & Owen, 2001).

When satisfaction is evaluated via service quality, one can find the effect is strong; the service quality acts a mediator between purchase intention and service quality. Similarly, the banking industry of Turkey also indicated the similar results on relationship between service quality and customer satisfaction (Karatape, Yavas, & Babakus, 2005).
The following hypotheses can be devised:

Hypothesis 1: Perceived service quality has a positive effect on customer satisfaction

Customer satisfaction and loyalty

Customers remain loyal if quality services are provided to them, which adds worth to the firm. The loyalty is gauged through service quality and satisfaction, which has been studied by Boulding, Kalra, Staelin, and Zeithaml (1993); Cronin, Brady and Hult (2000); Zeithaml, Berry and Parasuraman, 1993).

In a study by Kurtz and Clow (1998), customers switched to a different service due to its quality and another study by Bell, Auh and Smalley (2005) found that technical service quality has a stronger impact on customer satisfaction than the functional service quality.

Customer can be defined as anyone to whom a good or a service is supplied to (Crocker & West, 2003). In order to enhance the customer's experience, firms provide

customer service (Harris, 2007). In order to provide customer service, a service provider should understand their consumers better in order to satisfy their needs regarding the service. Poor customer service has been witnessed in public banks due to lack of empathy and responsiveness (Sudesh, 2007). Private and foreign banks are relatively better in providing customer service to their clients. It was also found that demographic variables brought a change in the results of service quality.

Harris (2007) noted there are five needs of customers that have to be met in order to satisfy them. These include: service, price, quality, actions, and appreciation. The quality of services proffered determines the customer fulfillment and attitudinal loyalty (Ravichandran, Prabhakaran, & Kumar, 2010). For banking sector, customer satisfaction is the key driver to ascertain if the customer stays with the same bank or switches to the other one. It all relies on the quality of the service, which leads to better and satisfied customers.

(Ravichandran, Prabhakaran, & Kumar, 2010) stated that if the customer gets satisfied to a little extent by the service then it may lead to dramatic customer loyalty. This was found for Bangladesh banking sector as well and similarly found that happy and satisfied customers of the bank will also recommend the service to other people. It was also evident that loyal customers regardless to the product /service in use are not much sensitive to price variations (Cohen, Gan, Yong, & Choong 2006).

On the basis of the review of literature above, the following hypothesis can be deduced:

Hypothesis 2: Customer satisfaction has a positive effect on customer loyalty.

Research Method

Samples

The data of this study were collected from customers of the Islamic microfinance institutions from central Java, Indonesia. Respondents were chosen through convenience sample. 300 questionnaires were distributed, out of which 220 responses were received, yielding a response rate of 73%.

Measurement

There were three parts to the questionnaire. The first part focused on gathering general information of the respondents and it also included demographic variables of: gender, age, education level, current job, monthly income, and the duration of their experience as customers with the micro-financing institutions. The second part of the questionnaire measured: service quality, customer satisfaction, and customer loyalty. Service quality attributes were derived, with some modifications, from the attributes developed by Parasuraman, Zeithaml, and Berry., 1994 ; Zeithaml & Bitner, 1996). Five dimensions of service quality were outlined as reliability, tangible, responsiveness, empathy and assurance. Likert-point scale ranged from 1= strongly disagree, 2= disagree, 3= neither disagree nor agree, 4= agree, to 5= strongly agree.

Customer Satisfaction

The dimension of overall satisfaction was taken from the Angelova and Zekiri (2011) customer satisfaction measurement scale.

Customer Loyalty

Narayandas (1996), customer loyalty scale has been used for this study, which has the reliability above 0.88.

All the scales taken for this study has 5-point Likert scales, where 1= strongly disagree, 2= disagree, 3= neither disagree nor agree, 4= agree, and 5= strongly agree.

Table 1: The Characteristics of Respondents

Demographic Variable	Category	Frequency	Percentage
Gender	Male	101	46
	Female	119	54
Age	Less than 20	50	23
	21 - 25	76	34
	26 - 30	50	23
	31 - 35	18	8
	36 -above	26	12
Education Level	Junior high school	16	7
	Senior high school	122	55
	Diploma	21	10
	Undergraduate	50	22
	Postgraduate	11	5
Occupation	Student	75	34
	Employees	37	17
	Business	58	26
	Government	12	6
	others	38	17
Monthly Income (Million IDR)	Less than 2	186	85
	2- 5	27	12
	More than 5	7	3
Microfinance's Membership (Year)	1-2	108	49
	2-5	79	36
	More than 5	33	15

Present analysis showed that 54% are female and 46% of the respondents are male. The Table 1 showed that 34 % of the respondents are in the age bracket of 21-25 years. The next largest group of respondents, are of the age bracket 26-30 years (23%); the same percentage of respondents (23%) also lie in the age bracket of "less than 20 years". 12 % of the respondents are from the age bracket of above 36 years. Only 8% of the respondents are in the age bracket of 31-35 years. In the terms of qualification however, there is a wide variation: Junior school (16%), Senior school (55%), Diploma (10 %), Undergraduate (22 %), and postgraduate (5 %).

      The estimated correlation matrix for the constructs showed that the estimated correlation among the constructs did not indicate any multicollinearity problem of the lack-of-discriminant-validity, where all correlation values are lower than 0.70. The correlations among some of this study's variables also provided initial support for the hypotheses. In support of H_1, service quality was positively associated with customer satisfaction, the result showed that customer satisfaction was significantly correlated with the dimensions of service

quality: reliability (r = 0.544, p < 0.01), responsiveness(r = 0.432, p <0.01), assurance(r = 0.622, p <0.01), empathy(r = 0.458, p < 0.01), tangibles (r =0.381, p <0.01). In addition, customer satisfaction positively correlated with customer loyalty (r = 0.346, p <0.01), these results are consistent with the existing literature.

Table 2: Means, Standard Deviations, and Correlations between Variables

Variable	Mean	SD	1	2	3	4	5	6
1. Reliability (1)	4.1	.55	1.00					
2. Responsiveness (2)	3.7	.70	.488**	1.00				
3. Assurance (3)	4.0	.53	.535**	.423**	1.00			
4. Empathy (4)	3.9	.62	.455**	.462**	.439**	1.00		
5. Tangible (5)	4.0	.61	.433**	.347**	.361**	.451**	1.00	
6. Customer Satisfaction (6)	4.0	.54	.544**	.432**	.622**	.458**	.381**	1.00
7.Customer Loyalty (7)	3.6	.57	.227**	.351**	.420**	.308**	.177**	.426**

Notes: ** is significant at p < 0.01, * is significant at p < 0.05

The current study utilized the structural equation modeling (SEM) to examine the theoretical model.

Test of the Measurement Model

The prime reason of a measurement model described how well the observed indicators serve as measurement instrument (either -> as a measurement instrument –or- as measurement instruments) for the latent variables (Kline 2005). It means that the measurement model outlines the link between the latent variables and the observed measures. The test of measurement model was carried using the confirmatory factor analysis (CFA). Assessments of goodness of fit of each measurement model were determined by several criteria: Chi-square, Root Mean Square Error of Approximation (RMSEA), Tucker-Lewis Index (TLI), Goodness-of-fit Index (GFI), and Comparative Fit Index (CFI). The CFA was conducted together with all the variables. The summary of measurement analyses is shown in Table 3.

**Table 3: Results of Confirmatory Factor Analysis**

Model	χ^2/DF	GFI	TLI	CFI	RMSEA
Cut-off point	< 3	>.90	<.90	>.90	<.08
CFA of all variables	1.162	093	.956	.968	.037

The table above reported the goodness-of-fit indicators. 125 degrees of freedom yields a value of 1.62, which is much better than the demanded maximum of 3.0 for a good model. The other fit indices (GFI=0.930; TLI=0.956; CFI=0.968) and the low standardized root mean square residual (RMSEA=0.037) are in an acceptable range and highlighted that a considerable quantity of variation is accounted for by the model. Therefore, the model well represented the data.

Test of the Structural Model

The subsequent analysis for testing the overall model and the developed hypotheses, utilized structural equation modeling using AMOS 7.0 program. An objective of the testing is to assess the goodness of fit between the model and the sample data (Byrne, 2001). Hair et al (2006) recommended three type of goodness-of-fit measures, namely *absolute fit measures*, *incremental fit measures*, and *parsimonious fit measures*. Test statistic for parameter estimates is assessed by critical ratio (c.r.); it represents the parameter estimate divided by its standard error. Critical ratio values are larger than 1.96 and prove the path coefficient to be statistically significant at level p< .05. The chi-square of the theoretical model was 18.601 with 5 degrees of freedom (df). This is statistically significant at level p<.001. A non-significant chi-square shows support for believing that the differences of the predicted and the actual matrices are non-significant, indicating an acceptable fit (Hair et al. 2006), therefore a non-significant chi-square is desired. Statistical significance level of chi-square indicates the probability that the differences are solely due to sampling variation. However, "statistical non-significance does not assure the researcher that another model would not fit as well or better" (Hair et al. 2006, p.654). In addition, the chi-square values are sensitive to the sample size. If the sample size becomes large enough, significant differences will be found for the specified model. Using the χ^2 index renders little guidance in determining the extent to which the model does not fit (Byrne 2001). For this reason, others fit indices (χ^2/df ; GFI ; RMSEA ;AGFI ; TLI ; NFI ; CFI ; RMR), which may minimize the effect of sample size, are utilized to assess the fit model. The result of the structural-equations-test of the composite variables indicated that the theoretical model achieved an acceptable fit to the data (χ^2/df = 1.171; GFI = .929; RMSEA = .082; AGFI = .903; TLI = .975; CFI = .98; RMR = .025), which is above the cutoffs for the goodness of fit indices.

Figure 2: The Results of the Testing Model
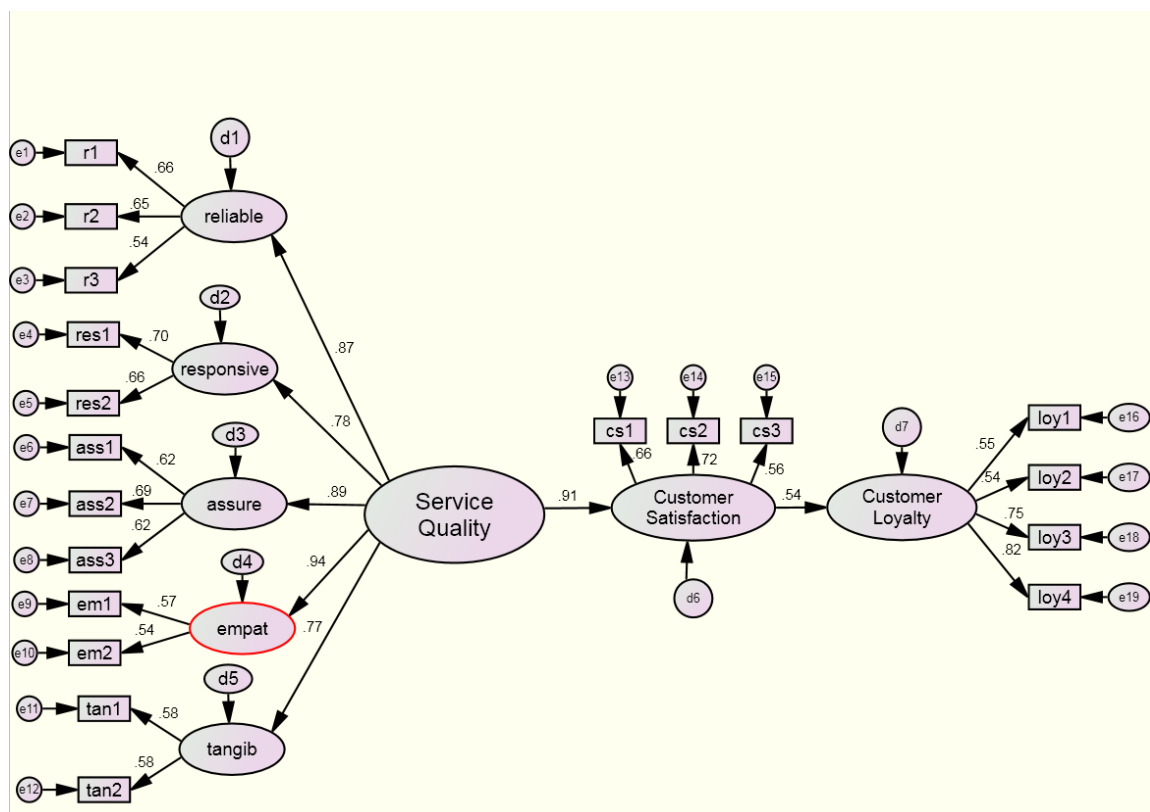
Hypothesis 1 investigated the relation between service quality and customer satisfaction. The result of AMOS 7 analysis showed the relation between service quality and customer satisfaction. The results of the assessment of the structural model showed that the standard path coefficients of 0.91 were significant at p <0 .01. Hence, the hypothesis 1 is supported. Furthermore, the data showed that customer satisfaction has a significantly positive direct effect on customer loyalty, with the standard path coefficient of 0.54. These relationships were significant at p < 0.01. Therefore, the hypothesis 2 is supported.

Table 4: Results of the Structural Model

Hypotheses	Causal Path	Estimate	Standard Error	t- Value	P	Results
H1	SQ → CS	.426	.045	9.566	***	Supported
H2	CS → CL	.791	.116	6.800	***	Supported

Notes: *** is significant at p < 0.01. SQ: Service Quality, CS: Customer Satisfaction, CL: Costumer Loyalty.

Discussion and Conclusion

The results of the structural equation modeling indicated that service quality explained more than 40 per cent of the variance in customer satisfaction. The findings of this study suggested that service quality has a significant impact on customer loyalty, amongst the customer-base of the Islamic microfinance institutions in the study area. Thus, the result indicates that the greater the customer satisfaction along with the service quality, the more positive is the influence on customer loyalty. This finding is in line with the studies conducted by Hu, Kandampully, and Juwaheer (2009), Pollack (2009) and Kuo and Ye (2009). They had found that service quality generally has a positive effect on customer satisfaction, and in turn also has a positive influence on customer-loyalty.

The significance of this study can be seen from two perspectives, which has theoretical and practical implications. The current study showed interrelationships among customer satisfaction, service quality and customer loyalty in the Islamic microfinance industry of Central Java, Indonesia. The study also suggested that the conceptual framework of Gronroos's (2007) model employed for this study was suitable for measuring the service quality of microfinance institutions. Moreover, the modeling of structural equations with the use AMOS program to test out the conceptual framework or the hypotheses was appropriate. Implying that, in order to enhance the customer satisfaction and customer loyalty, service quality needs to be improved.

Finally, there are some limitations to this study which need to be considered. Firstly, both the sample-size and the number of organizations considered are small; any further studies should utilize a larger sample size and involve various industries in order to get a better result. Secondly, the generalizability of the findings of the present study might be questionable due to the nature of the sample.

Thirdly, in regards of service quality as a predictor of consumer loyalty, it can be stated that other exogenous variables can be taken into account for elaborating this study's preciseness, which are places, types of customers, product /service features, physical aspects, security and technological aspects. These exogenous variables will be tested versus endogenous variables, which are customer satisfaction and customer loyalty. In this direction, the microfinance institutions and businesses can make use of the beneficial findings.

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