Mediating the Effects of Customer Satisfaction and Bank Reputation on the Relationship between Services Quality and Loyalty of Islamic Banking Customers

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Abstract

Amidst a fierce competition within the global banking industry, the issue of retaining existing loyal customers and attracting new customers has been a focus for Islamic banks worldwide, including Islamic banks in Indonesia. Considering this pressing issue, the present study empirically measures and analyzes the mediating effects of bank reputation and customer satisfaction on the relationship between service quality and the loyalty of Islamic banking customers. Out of 113,146 customers of Bank Mandiri Syariah (BSM) in the Banda Aceh City, Indonesia, 320 of them were selected as the respondents for the study using a purposive sampling technique. Data were gathered by distributing questionnaires to the respondents and analyzed using Structural Equation Modeling (SEM). The study recorded that while service quality has a significant positive influence on bank reputation and customer satisfaction, it has an insignificant effect on customer loyalty. Bank reputation and customer satisfaction were also documented to have significant mediating effects on the relationship between service quality and customer loyalty. These findings suggest that in order to enhance customer loyalty further, bank management should design a proper strategy focusing on improving bank reputation and customer satisfaction by strengthening service quality.

Keywords: Customer loyalty, digital-based services, shariah compliant-based services.

1.0   Introduction

Amidst the rapid development of the service industry in Indonesia starting from the last decade, Islamic banks have been facing fierce competition not only from other Islamic banks but also their

conventional banking counterparts. As one of the Islamic banks in Indonesia, Bank Mandiri Syariah (BSM), established on October 25th, 1999, is trying to win the competition within the banking industry. Therefore, the bank must have the ability to survive and win the competition by efficiently managing resources to produce superior value and serving customers with a better product quality that can be better appreciated by their customers (Webster, 1994). Banks operate with the principle of trust by providing continuous good services as expected by their customers (Abd-El-Salam et al., 2013).

In Indonesia, the Islamic banking industry has experienced steady growth. For example, in December 2013, the total assets of Islamic banks to the total banks' assets nationwide were 4.91%. This value has increased twice from the market share in early 2009. After the conversions of Bank Aceh and Bank Nusa Tenggara Barat into full-fledged Islamic banks in 2016 and 2018 respectively, the market share of Islamic banking institutions nationwide jumped to 5.40% (Financial Services Authority, 2018). In December 2019, the market share of Islamic banks in Indonesia reached 8.69%. The Islamic banks recorded total assets of IDR247.1 trillion in 2013 had increased to IDR524.6 trillion in 2019 which showed an average annual increase of 24.32% over the last seven years. The development of Islamic banks, comprising of Islamic commercial banks, Islamic business unit, and Islamic rural banks, is also marked by an increase in the number of Islamic banks from 184 units in 2010 to 198 units in 2019, which showed an average increase of 7.61% over the last ten years. In terms of their offices, it has increased from 1.763 units in 2010 to 2.917 units in 2019, representing a 65.46% annual growth over the period (Financial Services Authority, 2020).

Out of 14 full-fledged Islamic banks currently in Indonesia, BSM is the largest Islamic bank in the country with a captured a market share of 20.60% and 21.08% in terms of total assets and total financing respectively within the Islamic banking industry. Comparing to all banks in the country, both Islamic and conventional, it ranked as the top 15 largest banks in the national banking industry. BSM has recorded an increase in total assets by 11.86% from IDR87.92 billion in 2017 to IDR98.34 billion in 2018. The net profit of the BSM has also increased by 65.74% from IDR365.17 billion in 2017 to IDR605.21 trillion in 2018. At present, the BSM has a total of 765 branches, more than 8,000 personnel, and 219,642 units of Automated Teller Machines (ATMs) throughout Indonesia (Financial Services Authority, 2020). These

figures show a promising achievement of the bank in maintaining operational performance. Amid intense competition within the banking industry, BSM also faces competition from all banks in Indonesia, both Islamic and conventional.

BSM in the city of Banda Aceh, Indonesia is one of the BSM branches in the country that always strives to provide the best services to increase customer satisfaction and at the same time increase and attract new customers. Based on the BSM Report (BSM - Bank Syariah Mandiri, 2019), in 2017, the bank recorded a total of 118,400 customers, and this number is lower by 7.78% from 2016. In 2018, the number of customers only increased by 3.63%. Over the past three years, the average number of BSM customers has decreased by -2.08%. These figures show that BSM has not fully been able to maintain existing customers. Customers are not entirely loyal and this could be partially due to their dissatisfaction with the services provided.

Maintaining the loyalty of customers is a strategic policy to improve bank performance and strengthen its business in the long run. Loyalty refers to a commitment to the purchase of goods and services by repeating and re-protecting consistently related products or services (Oliver, 1997). Loyalty is associated with bank growth towards future progress. Thus, providing exemplary service to existing customers could increase loyalty. Customer's loyalty can be formed from the satisfaction felt by customers in choosing services provided by the banks, in which customers will feel happy if the service is good and vice versa (Belás & Gabcová, 2016). The satisfaction that customers obtained can have a positive or negative impact on their behavior towards the services on an ongoing basis. In other words, satisfaction is the core of customer loyalty, and it is one of the crucial loyalty components (Munari et al., 2013). Most of the previous studies provided evidence that service quality has a positive influence on customer loyalty in the banking industry (Minh & Huu, 2016; Hassan et al., 2012; and Hassan et al., 2013).

Moreover, customer satisfaction is also determined by the quality of services and reputation of the bank in following what is expected by the customer. Thus, guaranteeing the quality of service is a top priority for banks (Oliver, 1997). Customer satisfaction is also related to customer perceptions of perceived services where customers would value the services provided more than their hopes or desires. Thus, customer satisfaction will affect their loyalty in using the services offered by the banks (Fornell, 1992) and customer satisfaction

is becoming the key to the success of the banks (Belás & Gabcová, 2016). The majority of previous studies in the banking industry found supportive evidence of a significant positive effect of service quality on customer satisfaction (Minh & Huu, 2016; and Hunjra et al., 2011).

In addition to service quality, customer loyalty is also influenced by bank reputation which shows how much public trust is placed on the bank. The customer's impression and confidence in the bank will have an important influence as the customer will choose a bank with good reputation. A bank that is able to build a good reputation will increase customer confidence and trust in the bank (Gjerde & Slotnick, 2004). Thus, the bank must be able to maintain its reputation to keep its customers. With a good reputation, customers will continue to subscribe to the services offered by the bank (Wang et al., 2003). By understanding consumer behavior, it is expected that the bank can formulate the proper strategy to attract consumers as much as possible and improve the bank's overall reputation as from a marketing perspective, a good bank reputation influences customer loyalty (Tang, 2007). Loyalty is positively influenced by favorably perceived reputation (Abd-El-Salam et al., 2013; Rindova & Fombrun, 1999; and Helm & Tolsdorf, 2013).

The above discussion shows that in order to retain existing customers and attract new customers, the bank should implement a strategy to get closer to customers and maintain their loyalty by always improving their reputation and customer satisfaction through high-quality services provided. However, in reality, the efforts made by the banks often fail to yield optimal results. The number of customers in the last three years has decreased by an average of 2.08% (BSM - Bank Syariah Mandiri, 2019). These phenomenon drives the present study to empirically explore the extent to which the improvement in the quality of services has been able to create customer satisfaction and at the same time enhance the bank's reputation so that customers have high loyalty towards the bank.

Besides, previous studies related to the influence of service quality on customer satisfaction and bank reputation and the effect of mediating service quality on customer loyalty towards Islamic banks have been focusing more on conventional banks (Abd-El-Salam et al., 2013; Minh & Huu, 2016; Chu et al., 2012; and Leaniz & Rodríguez, 2016) and the Islamic banking industry in other countries, such as Estiri et al. (2011) in Iran, Hassan et al. (2012; 2013), Hunjra et al. (2011),

Ali & Raza (2017), and Khokhar et al. (2019) in Pakistan, and Dawami (2020), and Rahman et al. in Malaysia.

In Indonesia, the issues of banking customer loyalty have not been comprehensively studied. For example, in his research, Saputra (2013) only used one customer satisfaction variable as a mediator, did not include the bank's reputation variable, and focused his analysis on conventional banks. Previous studies focusing on Islamic banks have been carried out by Ningtyas & Rachmad (2011), Junaedi et al. (2012), Putra & Herianingrum (2014), Kurniawan & Shihab (2015), Wijayanto (2015), Atmaja (2018), and Marlius (2018). Ningtyas & Rachmad (2011), in their research, examined service quality by excluding service quality as a determining factor of customer satisfaction and customer loyalty of Islamic banks. They only investigated the direct influence of service quality on customer loyalty while ignoring the mediating effect of customer satisfaction on the relationship between services quality and customer loyalty. Likewise, Junaedi et al. (2012), Putra & Herianingrum (2014), Kurniawan & Shihab (2015), Wijayanto (2015), Atmaja (2018), and Marlius (2018) excluded the bank's reputation variable as a mediating variable that affected service quality towards the loyalty of Islamic bank customers. Whereas from a marketing perspective, bank reputation plays a vital role in enhancing customer loyalty (Helm & Tolsdorf, 2013).

Considering the ongoing phenomena of declining customers experienced by the Islamic banks and the desire to provide more comprehensive and up-to-date empirical evidence by filling up the existing research gaps, this study includes bank's reputation in addition to the customer satisfaction as mediating variables affecting the service quality on the loyalty of the Islamic bank customers. More specifically, this study aims to empirically measure and analyze the mediating effects of bank reputation and customer satisfaction on the relationship between service quality and customer loyalty of Islamic banking in Indonesia with the Structural Equation Modeling (SEM) method by taking the Bank Syariah Mandiri (BSM) of the city of Banda Aceh branch as a case study.

The results of this study are expected to be an essential reference for Islamic banks in designing strategies to retain existing customers and attract new customers through increasing customer satisfaction and bank reputation by improving the quality of bank services. The results of this study are also expected to strengthen the position of Islamic banks and not be abandoned by their customers,

and ultimately be able to win an increasingly intense competition within banking industry in Indonesia.

The rest of this study is organized into the following sequences. Section 2 reviews relevant literature on the determinants of customer loyalty. Section 3 discusses the research method employed in the study. Section 4 provides the discussion of the findings, and finally, Section 5 provides the conclusions and suggestions for further research.

2.0   Literature review

In this section, the related theories and previous studies on determinants of customer loyalty, their measurements, and hypotheses developed are discussed.

2.1   Customer loyalty

Customer loyalty is the loyal behavior of customers in buying products and services from a bank which results in the customer's long-term bond with the bank (Chu et al., 2012). Loyalty is a behavioral response that is biased and is revealed continuously by decision-makers by paying attention to one or more alternative brands from many similar brands and is a function of psychological processes (Agrawal et al., 2012). However, it should be emphasized that it is different from the repurchase behavior as customer loyalty includes the feeling aspect in it (Khokhar et al., 2019).

Previous studies on customer loyalty have been explored in various types of industries. For example, Kandampully & Suhartanto (2000) investigate the effects of image, price, quality service, and loyalty of the chain hotels in New Zealand. They found that all these factors determined customer satisfaction. Kim et al. (2004) explore the value-added services, customer support and satisfaction, and switching barrier on customer loyalty in Korean mobile telecommunication services and found that customer loyalty is positively influenced by quality service and customer satisfaction. Similar findings are documented by Santouridis & Trivellas (2010), where service quality is found to have a positive influence on customer satisfaction and, in turn, it affects loyalty positively in mobile telephony in Greece. For the case of the restaurant industry, Han & Ryu (2009) found a significant effect of the physical environment on customer satisfaction which directly/indirectly impacted customer loyalty. Finally,

Jiang & Zhang (2016) explored the impact of service quality on customer satisfaction and loyalty in China's airline market and found that service quality has enhanced customer satisfaction and loyalty.

According to Griffin (1996), indicators of loyal customers include: (i) making regular purchases, (ii) buying outside the product or service line, (iii) refusing products or services from other banks, (iv) immune to attractiveness, (v) attracting new customers, and (vi) customer notifies weaknesses or deficiencies to the bank.

2.2   Customer satisfaction

Customer satisfaction is the ability to provide satisfying services and products for customers. The customers compare the value that they believe they received against the level of value that they expected to obtain before they purchase or consume the product or services. In this context, consumers essentially confirm (or disconfirm) the extent to which the actual delivery of products and services has met their prior expectations. The level of the customers' expectation have been met (that is, confirmed) or exceeded (positively disconfirmed) or not met (negatively disconfirmed) will determine the customer's satisfaction level (Minh & Huu, 2016; and Zameer et al. (2018). In banking, the customers question themselves about the level of the services provided and decide about repurchase behavior after using the services. The level of satisfaction is always high when the customer pays a minimum price but enjoy maximum benefits (Munari et al., 2013).

Studies on customer satisfaction have focused not only on the banking industry, but they have also explored many sectors. For example, Deng et al. (2010) conducted empirical examination of the determinants of customer satisfaction on mobile instant messages in China and found that trust, perceived service quality, and perceived customer value contributed to generating customer satisfaction. Kim & Lee (2011) examined the importance of perceived service quality and the relationship between perceived service quality, customer satisfaction, and behavioral intention using low-cost carriers in South Korea. They found tangible and responsiveness as the significant dimensions of customer satisfaction. Hussain et al. (2015) also found the significant effects of service quality, perceived value, and brand image on customer satisfaction in a Dubai-based airline. Kursunluoglu (2014) examined the relationships and the impact of customer service

of shopping centre services in Turkey and documented that customer services had effects on customer satisfaction and loyalty. Ojo (2010) investigated the relationship between service quality and customer satisfaction within the telecommunication industry in Nigeria and recorded that service quality had a positive effect on customer satisfaction. Finally, Cao et al. (2018) found both post-purchase shipping and tracking have an impact on customer satisfaction in online shopping in both China and Taiwan.

To measure customer satisfaction, Goodman et al. (1995) introduced three indicators, namely: (i) feeling happy, (ii) satisfaction with services, and (iii) satisfaction with the system.

2.3   Bank reputation

According to Harun et al. (2020), a company's reputation includes the company's good name, image, or expertise. It is a factor that often influences the decisions of buyers in the service sector compared to the product sector. Reputation can be ranked as good, moderate, or bad. A bad reputation will hurt bank business operations and can also weaken the ability for banks to compete (Wang et al., 2003). Reputation becomes an issue of customer attitudes and beliefs with relation to awareness and recognition, behavior, and satisfaction of customers.

Previous studies on the determinants of reputation have also focused on various industries. For instance, Loureiro & Kastenholz (2011) explore the lodging unit's reputation in Portugal and found that it had a more significant effect on customer loyalty than satisfaction. Reputation is also documented to create loyalty through trust and value of the restaurants in Taiwan (Chang, 2013). Parents' satisfaction is found to significantly affect reputation dimensions of the school in Norway (Skallerud, 2011). Fares and Kachkar (2013) also found the critical role of university reputation on the loyalty of international students in International Islamic University, Malaysia. Finally, Lee et al. (2017) found that corporate social responsibility activities determine the corporate reputation, and it in turns, affects the loyalty of non-life insurance customers. Corporate reputation also influenced customer satisfaction and loyalty of the cellular industry of Pakistan (Ali, Rehman, Yilmaz, & Ali, 2010).

Leaniz & Rodríguez (2016) believe that corporate reputation can create a halo effect on the judgment of customer satisfaction and

influence perceived value, customer satisfaction, and loyalty. On this basis, Selnes (1993) advocates that reputation should be considered in the delineating of loyalty and satisfaction of bank customers. To measure bank reputation, Selnes (1993) uses four indicators, namely: (i) good name, (ii) reputation compared to competitors, (iii) widely known, and (iv) easy to remember.

2.4   Service quality

Quality of service is an expected level of excellence and control must be exerted over it to meet customers' desires (Hassan et al., 2013). However, according to Kheng et al. (2010), there is no definition of service quality that can be accepted by everyone. In a service organization like the banks, quality is a measure of the extent to which the service delivered meets the expectations of their customers. As is the nature of most services, the customer is present in the delivery process (Minh & Huu, 2016; and Abby et al., 1994). This indicates that the perceived quality is affected not only by the service outcome but also by the service process.

Previous studies on service quality have not only focused on the banking industry, but also other various sectors. For example, Abd-El-Salam et al. (2013) documented that corporate image and reputation affected service quality and, in turn, impacted customer satisfaction and loyalty of the international service company in Egypt. Store and chain images are recorded to positively affect the quality of services of the Norwegian petrol stations (Helgesen et al., 2010). The service quality of online selling books services in South Africa and online share trading facilities in Australia are documented to influence customer satisfaction (Caruana & Ewing, 2010). Service quality, innovation capability, and corporate image enhance the satisfaction of customers of the air cargo terminals at Taiyuan International Airport, Taiwan (Hu & Huang, 2011). Hussain et al. (2015) found similar empirical evidence where service quality, innovation, and corporate image positively influenced customer's satisfaction and loyalty of a UAE-based airline in an empirical investigation. Finally, Saleem & Raja (2014) found that customer satisfaction, loyalty, and brand image affected by the service quality of the hotel in Pakistan.

According to Parasuraman et al. (1993), service quality or SERVQUAL is measured using five dimensions. First, tangibility includes physical facilities, equipment, personnel appearance,

buildings and front office rooms, parking lots, cleanliness, neatness and comfort of the room, as well as the completeness of communication equipment. Second, reliability comprises of the ability to provide services that are expected to be convincing, accurate, and consistent. Third, responsiveness consists of the willingness to provide fast service and assistance in handling transactions and consumer complaints. Fourth, assurance includes knowledge, manners, and the ability of employees to convey certainty and trust. Finally, empathy is related to the bank's attention given to consumers such as the ease of contacting the company, the ability of employees to communicate with consumers, and the company's efforts to understand the wants and needs of consumers.

2.5 Hypotheses development: determinants of customer loyalty

The determinants of bank's customer loyalty are discussed here based on the relevant theories and past related studies. These determinants include quality service, customer satisfaction, and bank reputation. At the end of discussing each determinant, the hypothesis to be tested in this study is proposed.

2.5.1 Service quality and bank reputation

To ensure sustainability, banks should always strive to provide a better quality of their services. This is one of the ways the banks could enhance their reputation (Gjerde & Slotnick, 2004). Previous studies have recorded that high service quality provided with the minimum costs enhances competitiveness through establishing a good reputation that could retain existing customers and even attract new customers (Wang et al., 2003). Engizek & Yasin (2017) also showed that service quality contributed significantly to the enhancement of bank reputation in Turkey. Additionally, service quality is found to have an impact on corporate reputation as low quality of services invariably leads to negative reputation and bad publicity concerning the corporation (Engizek & Yasin, 2017). Based on the above previous studies, the following Hypothesis 1 is proposed.

H_1:   Service quality influences bank reputation.

2.5.2 Service quality and customer satisfaction

A company always strives to provide greater satisfaction for customers by providing a good quality of products and services. Without the presence of customers, the company could not maintain its sustainability. In the banking industry, interacting and providing services to customers are the core business processes of the bank in order to retain existing customers and attract new customers by providing customers with satisfying services that is the key to the bank's success (Chavan & Ahmad, 2013). Thus, the company always seeks to have a good long-term relationship with their customer and consider them as their top priority.

In the banking context, where contacts with customers are one of the core business processes, customer satisfaction is becoming the key to success (Belás & Gabcová, 2016). This shows that service quality is one of the main determinants in influencing customer satisfaction. The majority of previous studies, particularly in the service industry, such as banks, found supportive evidence on the relationship between service quality and customer satisfaction. Service quality is found to positively affect customer satisfaction (Minh & Huu, 2016; and Hunjra et al., 2011).

Based on these reviewed studies, therefore, the following Hypothesis 2 is proposed:

H_2:   Service quality influences customer satisfaction.

2.5.3 Service quality and customer loyalty

In buying products and services, customers always expect to enjoy the highest benefits based on the cost paid. If they found less than what is expected, customers feel dissatisfied and disappointed. On the other hand, if the benefits they gained are as expected or even more, they will be satisfied. Having these experiences of consuming the products and services would influence the loyalty of customers (Abd-El-Salam et al., 2013).

In their study, Onditi et al. (2012) found that service quality has affected the loyalty of banking customers in Kenya. Similarly, Noor (2020) documented a positive effect of service quality on customer loyalty. Abd-El-Salam et al. (2013) also found that service quality significantly and positively affected customer loyalty. These studies suggest that to enhance customer loyalty, the banks should improve

their quality of services. Based on these reviewed studies, the third hypothesis proposed to be tested in this study, is as follows:

H_3:   Service quality influences customer loyalty.

2.5.4   Bank reputation and customer loyalty

Corporate reputation is viewed as a result of an overall process that incorporates various information received by the consumer to shape the perception of the company (Abd-El-Salam et al., 2013). A consumer who has a better experience with the company will have a good perception of the company's reputation. From a marketing perspective, a good corporate reputation influences customer loyalty (Tang, 2007). Loyalty is theoretically believed to be positively influenced by favorably perceived reputation (Rindova & Fombrun, 1999). Many studies asserted that a good corporate reputation helps to ascertain and maintain customer loyalty (Wang et al., 2003; Tang, 2007; and Helm & Tolsdorf, 2013).

Furthermore, Zinkhan et al. (2001) argued that once customer interacts with a company they frequently lack the capability and proclivity to collect accurate information, corporate reputation could be used as a proxy of the quality of the services. Thus, corporate reputation plays a strategic role in the service industry such as banks because the customer purchase decision is very much depending on the evaluation of service quality which is not an easy task to be done (Wang et al., 2003). Because of their intangibility, the quality of the services become more difficult to be measured by consumers. Thus, the service company such as a bank tends to prefer to create a good reputation than other companies producing similar products (Rindova & Fombrun, 1999).

Abd-El-Salam et al. (2013) provided evidence of the positive role of corporate reputation on customer loyalty. Differently put, the bank with good reputations are prone to get more customer and enhance their loyalty. Hence, and based on the previous literature review, we propose the following Hypothesis 4:

H_4:   Bank reputation influences customer loyalty.

2.5.5 Customer satisfaction and customer loyalty

Customer loyalty represents the final results of the entire experience of customers with a company (Brunner et al. 2008). If the customers have a good experience and feel satisfied with the company, it leads them to be loyal to the service providers. This indicates that customer satisfaction is one of the determinants of customer loyalty in the service industry (Belás & Gabcová, 2016) such as banks.

In their study, Munari et al. (2013) identified that satisfaction is the core of customer loyalty, and it is one of the crucial loyalty components. According to Minh & Huu (2016), the majority of previous studies on the banking industry found that satisfaction is one of the main factors in determining customer loyalty. Most of the studies provided conclusive evidence that service quality has a positive influence on customer loyalty in the banking industry (Hassan et al., 2012; and Hassan et al., 2013). By referring to these reviewed previous studies, the study proposes Hypothesis 5, as follows:

H_5:   Customer satisfaction influences customer loyalty.

2.5.6 Mediating effects of customer satisfaction and bank reputation on service quality – customer loyalty relationship

Wang et al. (2003) stated that a good service quality served efficiently has enhanced competitiveness by creating a good reputation, thereby enabling the company to retain existing customers and attract new ones. Engizek & Yasin (2017) provided evidence that service quality has an impact on corporate reputation. From a marketing perspective, a good corporate reputation would in turn, influences customer loyalty (Abd-El-Salam et al., 2013). Theoretically, corporate reputation affects customers' loyalty (Rindova & Fombrun, 1999) and helps the corporation to ascertain and maintain their loyalty (Helm & Tolsdorf, 2013; and Rahman et al., 2020).

Furthermore, to retain existing customers and attract new ones, banks should provide customers with services which are satisfying (Chavan & Ahmad, 2013). In the banking perspective, where contacts with customers are one of the most core business processes, customer satisfaction is becoming the key to the success of banks (Belás & Gabcová, 2016). This shows that service quality is one of the main determinants influencing customer satisfaction. Service quality is found

to positively affect banks' customer satisfaction (Minh & Huu, 2016; and Hunjra et al., 2011).

Consequently, customers that have a good experience and feel satisfied with the banks would be loyal to their service providers. This indicates that customer satisfaction determines customer loyalty in the banking industry (Belás & Gabcová, 2016; Minh & Huu, 2016, and Hassan et al., 2013). Based on these reviewed studies, the study proposes Hypothesis 6 and Hypothesis 7, as follows:

H_6:   Bank reputation mediates the relationship between service quality and customer loyalty.

H_7:   Customer satisfaction mediates the relationship between service quality and customer loyalty.

Based on the above reviewed studies and hypotheses developed, the proposed research model of the study is illustrated in Figure 1.
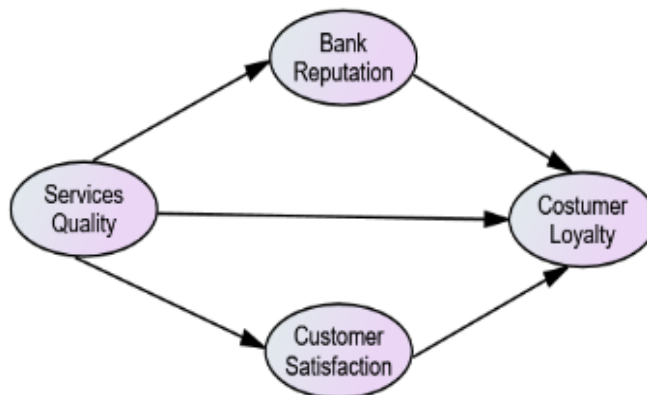

Figure 1 : The proposed research model

3.0   Research methods

This study focuses its analysis on investigating the mediating effects of bank reputation and customer satisfaction on the service quality–customer loyalty relationship at the Bank Syariah Mandiri (BSM) branch of Banda Aceh City, Indonesia.

Out of 113,146 customers of the BSM in the Banda Aceh City, Indonesia in 2018, 320 of them were selected as the respondents of the study using a purposive sampling technique. Only customers who have transacted more than twice in the bank and have been the customers of the bank for more than a year was selected, considering

that they have experienced service quality provided by the bank. Otherwise, it will be less accurate to measure customer satisfaction and loyalty if they lack the experience of transacting with the bank.

The size of the sample is determined using the Slovin formula and considering the minimum number of respondents for the study using the Structural Equation Modeling (SEM) technique for data analysis. According to Hair et al. (2012), the minimum sample size should be at least 5 to 10 times the number of indicators used to measure the variables being investigated. In our study, as 32 indicators were used to measure four variables (i.e., service quality, bank reputation, customer satisfaction, and customer loyalty), at least 160 respondents (i.e., 5 x 31) were required. However, to ensure the robustness of the findings, the study selects 320 respondents (i.e., 10 x 32). Thus, the number of respondents analyzed in the study is believed to be able to provide robust findings.

Data were gathered by distributing questionnaires to the respondents and measured using the five-point Likert scale. The variables investigated comprise of service quality (exogenous variable), bank reputation and customer satisfaction (mediating variables), and customer loyalty (endogenous variable). In this study, service quality is measured using five dimensions (i.e., tangibility, reliability, responsibility, assurance, and empathy) as proposed by Parasuraman et al. (1993). To measure each dimension, 19 indicators were used, and they were adjusted to the needs of the study focusing on Islamic banking. Precisely, the dimensions of tangibility were measured using five indicatora, reliability was measured using three indicators, and responsibility was measured using three indicators while assurance and empathy were measured using four indicators each.

Furthermore, bank reputation was measured using four indicators as proposed by Selnes (1993), customer satisfaction was measured using three indicators proposed by Goodman et al. (1995), and finally, six indicators presented by Griffin (1996) were used to measure customer loyalty. Altogether, the study uses 32 indicators that are discussed in the earlier section of the literature review.

As mentioned earlier, to measure the mediating effects of bank reputation and customer satisfaction on the service quality–customer loyalty relationship, Structural Equation Modeling (SEM) was used. The advantages of the use of the SEM technique in this study were high accuracy and speed of the results obtained from the indicators and

data analysis and its ability to confirm values theoretically (Hair et al., 2012). The study conducts a series of tests of the instrument, classical assumption, and goodness of fit indices to ensure the robustness of the estimated proposed research model. Thus, the study proposes the following SEM equations to be estimated,

$$BR = \gamma_{11}SQ + \zeta_1 \qquad\qquad (1)$$

$$CS = \gamma_{21}SQ + \zeta_2 \qquad\qquad (2)$$

$$CL = \gamma_{31}SQ + \gamma_{32}BR + \gamma_{33}CS + \zeta_3 \qquad\qquad (3)$$

where BR is the bank reputation, SQ is the service quality, CS is the customer satisfaction, CL is the customer loyalty, γ_{ii} are the estimated loading factors for each variable, and ζ_i are the structured error terms.

4.0   Findings and discussion

4.1   Characteristics of respondents

Table 1 illustrates the characteristics of customers of the BSM branch in the city of Banda Aceh, Indonesia. As observed from the table, out of the 320 customers of the bank selected as respondents in the study, the majority of them were female at 71.25%, while the remaining 28.75% were male. In terms of age, the majority of them (53.13%) were aged 21-30 years, followed by 30-40 years old with 30.63% while respondents aged less than 20 years old and above 40 years old were less than 10%, respectively.

In terms of education level, the customers were mostly senior high school graduates (49.38%) who are studying undergraduate programs, followed by the undergraduate degree holders (27.59%), and postgraduate degree holders (10.00%). Meanwhile, respondents with the level of education that is equivalent to a diploma or lower were less than 7%. Finally, in terms of monthly income, the majority of them have monthly income of IDR6-8 millions (26.25%), followed by the monthly income of IDR2-4 million (23.75%), IDR8-10 million (16.25%), IDR4-6 million (14.38%), more than IDR10 million (10.00%), and less than IDR2 million (9.38%).

Table 1 : Characteristics of respondents

Characteristics		Frequency	(%)
Gender	Female	228	71.25
	Gender	92	28.75
Age	< 20	24	7.50
	20-30	170	53.13
	30-40	98	30.63
	40-50	18	5.63
	≥50	10	3.13
Education level	Elementary school	12	3.75
	Junior high school	8	2.50
	Senior high school	158	49.38
	Diploma	22	6.88
	Undergraduate	88	27.50
	Postgraduate	32	10.00
Monthly income	<IDR2,000,000	30	9.38
	IDR2,000,000 – IDR4,000,000	76	23.75
	IDR4,000,000 – IDR6,000,000	46	14.38
	IDR6,000,000 – IDR8,000,000	84	26.25
	IDR8,000,000 – IDR10,000,000	52	16.25
	≥ IDR10,000,000	32	10.00
Total		320	100

4.2   Tests of model measurement

Before the study estimates the Equations (1), (2), and (3), the tests of validity, reliability, normality, outlier, and goodness of fit indices were conducted. The test of validity using the convergent validity test showed that all indicators used to measure the investigated variables were found to be valid. This is indicated as the estimated loading factor value of each indicator was greater than 0.5 (Hair et al., 2012). Likewise, using the construct reliability test, all estimated values of standardized regression weights were found to be greater than 0.6 thus indicating all indicators were reliable. These findings show that the 32 indicators used to measure all variables in the study were valid and reliable.

Next, the study also carried out multivariate variable normality tests and found that all variables were normally distributed, as shown by the loading factor probability value that is greater than 0.05. As for the outlier test done using Mahalanobis distance, the study also found that the estimated value of the Mahalanobis distance is smaller than the chi-square distribution value of 53,491 for the degree of freedom of

32. This shows that all variables were normally distributed, and all the data were free from outliers.

The final step before the results of the estimated SEM equations were reported and discussed, a test of goodness of fit indices was performed. After the SEM models were modified, the estimated values of the goodness of fit indices were reported in Table 2. As reported in Table 2, the study found that all the goodness of fit indices was found to be of good fit, as indicated by estimated values that passed the cut-off values. These indices include probability value, Root Mean Square Error of Approximation (RMSEA), Goodness of Fit Index (GFI), Relative Chi-Square (CMIN/DF), Tucker-Lewis Index (TLI), and Comparative Fit Index (CFI). However, only the estimated goodness of fit indices of X^2-Chi-Square statistics and Augmented Goodness of Fit Index (AGFI) were found to be marginally fit. Out off eight indices, only two indices of the goodness of fit showed to be marginally fit, but the overall estimated SEM model could be said to be a good fit.

Table 2 : Goodness of fit of the model measurement

No.	Indices	Cut-off Value	Finding	Remark
1.	X^2-Chi-Square	≤ 118.599 (X^2; df; $p = 0.01$)	120.903	Marginal fit
2.	Probability	< 0.05	0.001	Good fit
3.	RMSEA	< 0.08	0.062	Good fit
4.	GFI	> 0.90	0.915	Good fit
5.	AGFI	> 0.90	0.846	Marginal fit
6.	CMIN/DF	< 2.00	1.612	Good fit
7.	TLI	> 0.90	0.955	Good fit
8.	CFI	> 0.90	0.972	Good fit

According to Verbeek (2012), it is rare for the previous empirical studies using SEM approach to have their findings meet all the criteria of the model suitability. If the sample size of the study is greater than 100, as in our research, it is tough to find parsimonious SEM estimates and meet the entire goodness of fit indices (Williams & Hazer, 1986). Finally, our findings of the goodness of fit indices were not much different from the results of Martin & Cullen (2006) who recorded the estimated values of Chi-Square ranging from 6.18 to 7.78, RMSEA from 0.96 to 0.109; TLI from 0.50 to 0.53, and CFI from 0.76 to 0.86. Thus, we firmly conclude that our estimated SEM could measure and predict the interrelationships between investigated variables.

4.3 The direct effect of service quality on bank reputation, customer satisfaction, and customer loyalty

Figure 2 illustrates the findings of the estimated SEM equation showing the estimated values of the direct effect of service quality on bank reputation, customer satisfaction, and customer loyalty of the BSM branch of Banda Aceh City, Indonesia. It also shows the estimated values of mediating effects of bank reputation and customer satisfaction on customer loyalty. Since the p-values of each estimated or loading factor of relationships were not presented in the figure to identify their significance effects, the findings from Figure 2 are summarized and shown in Table 3.
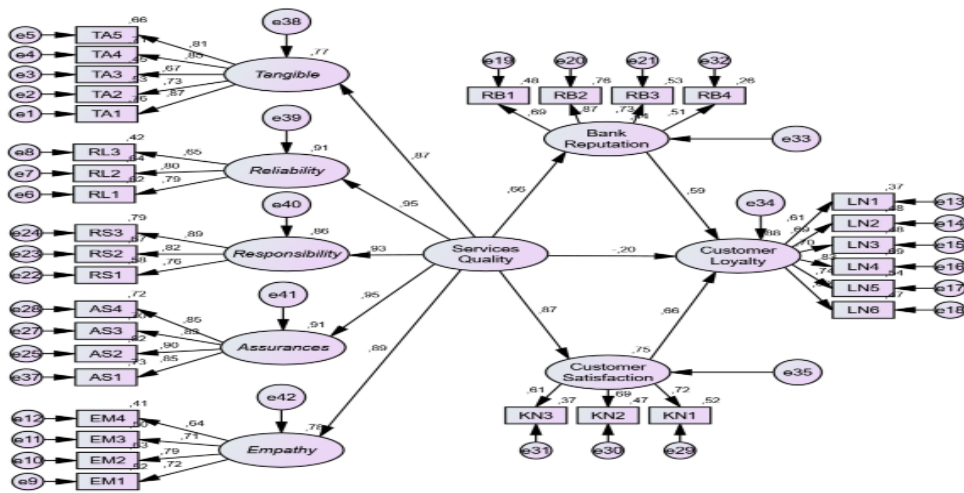

Figure 2 : The findings of estimated SEM

As reported in Table 3, service quality is found to have a significant positive effect on bank reputation and customer satisfaction at 1% level of significance. Specifically, the findings showed that as the service quality increase by 100 units, the bank reputation and customer satisfaction improved by 43.20 units on the Likert scale respectively. These showed that the service quality provided by the bank has significantly enhanced bank reputation and improved customer satisfaction. These findings are not surprising since the bank has a long business experience in the *shariah* banking industry in Indonesia since 1999, capturing the highest market share within the industry by 20.60% in 2018. Presently, the bank has 765 branches with more than 8,000 employees throughout Indonesia (Financial Services Authority, 2020).

The bank has been able to have a good brand reputation especially in the *shariah* banking industry nationwide.

Table 3 : The direct effect of service quality on bank reputation, customer satisfaction, and loyalty

Interaction between variable		Estimate	Critical ratio	Remark
Bank reputation	← Service quality	0.432***	3.349	H_1: Not rejected
Customer satisfaction	← Service quality	0.796***	8.944	H_2: Not rejected
Customer loyalty	← Service quality	0.078	0.604	H_3: Rejected
Customer loyalty	← Bank reputation	0.629***	3.812	H_4: Not rejected
Customer loyalty	← Customer satisfaction	0.480***	3.528	H_5: Not rejected

Note: *** indicates significance at the 1% level.

These findings further indicate that the bank's vision to make it as the choice that provides benefits, peace, and prosperity and become the trusted bank by offering products with the best services to the customers has materialized. This could be partially due to the bank efforts to serve customers beyond their expectations through technology-based services (BSM - Bank Syariah Mandiri, 2019). Additionally, the bank always prioritizes customer satisfaction by providing the best service. The bank does not only offer products that are safe and beneficial to society but also offers maximum protection for consumers by introducing a customer deposit protection policy. To protect customers, the bank has registered them as a participant of the Indonesian Deposit Insurance Corporation and established a reserve for losses on earning assets.

Besides, in order to improve customer satisfaction, the bank has effectively handled customer complaints through the Complaint Handling Management System (CHMS) as indicated by a declining number of complaints by 13.42% from 44,033 in 2017 to 43,974 in 2018. This is simply due to the introduction of artificial intelligence-based Chabot engine which serves to improve service quality and bank efficiency. Specifically, the bank has developed the Chabot service called *Aisyah* (Assistant Interactive *Shariah*) on November 26th 2018, as a 24-hour digital assistant for responding to customers' questions and complaints via Telegram, Facebook Messenger, and live chat on their website (BSM - Bank Syariah Mandiri, 2019).

A *Shariah* clinic forum that was introduced in 2018 to respond to complaints about the issue of *shariah* compliance has also contributed

to customer satisfaction. This is supported by the customer satisfaction survey report conducted by Marketing Research Indonesia - MRI (2019) that 84.14% of the respondents were highly satisfied with the bank. Within the year 2019, the bank has been awarded the Best Digital Brand 2014-2018, the Banking Service Excellence Award, and the 1st Rank Satisfaction Bank (Marketing Research Indonesia - MRI, 2019).

Many previous studies support our findings of a significant positive effect of service quality on customer satisfaction and bank reputation. For example, Gjerde & Slotnick (2004) found that providing better service quality is one of the ways that banks could enhance their reputation. The service quality provided efficiently could enhance banks' competitiveness by establishing a good reputation (Wang et al., 2003). Engizek & Yasin (2017) documented a significant positive contribution of service quality on bank reputation. In addition, in the banking context, ensuring customers' satisfaction by providing them service quality as expected is one of the keys to banks' success (Belás & Gabcová, 2016). Many previous studies in the banking industry found supportive evidence of the significant positive influence of service quality on customer satisfaction (Minh & Huu, 2016; Hassan et al., 2013; and Hunjra et al., 2011).

Unlike service quality that has affected bank reputation and customer satisfaction as illustrated in Table 3, the study found an insignificant effect of service quality on customer loyalty. This finding showed that although the bank has made the continuous improvement of service quality, it has no significant impact on the loyalty of customers. This is as indicated by a declining number of customers by 2.08% over the period of 2016 to 2019. Additionally, in terms of assets, the bank market share had decreased by 0.13% from 20.73% in 2017 to 20.60% in 2018. The inability of the bank to retain customers' loyalty could be partially due to the fierce competition the bank is facing from other Islamic banks that offer better services. As reported by the Marketing Research Indonesia - MRI (2019), the loyalty level of BSM is far behind the loyalty level of customers of Bank Muamalah Indonesia (BMI) that won the Highest Customer Loyalty Award for banks in 2018.

This finding further indicates that to maintain existing customers, attract new customers, and retain their loyalty, the service quality provided should not only be improved but it should be better than services provided by other Islamic and conventional banks. A continuous improvement of service quality should be focused not only

on the dimensions of tangibility, reliability, responsiveness, assurance, and empathy but it should also be on the *shariah* compliance of the banking products and their operation. If the customers perceived that the bank that is labeled with *shariah*, but its operation is still similar to that of a conventional bank, they would shift to other Islamic banks that are more purely *shariah*-based.

Our finding of the insignificant effect of service quality on customer loyalty is supported by previous study conducted by Hermawan (2017). A good service quality provided by banks does not guarantee that the customers will be loyal and do not shift to their competitors. With the advancement of e-marketing nowadays, the customers could easily compare the quality of services offered by other banking competitors and would simply shift to another bank with a better quality of services. Nowadays, it has become too convenient to open an account in any other banks as the switching cost is minimal. If a customer is dissatisfied, their loyalty diminishes automatically and they would shift to another bank (Afsar et al., 2010). This in line with the study conducted by Hermawan (2017) who documented that service quality could not directly affect customer loyalty. Still, its effect is indirectly channeled through the improvement of customer satisfaction.

Furthermore, as reported in Table 3, customer loyalty is found to be positively and significantly affected by the bank reputation and customer satisfaction at 1% level of significance. Notably, an increase of 100% in the bank reputation and customer satisfaction will cause the customer loyalty to increase by 62.9% and 48.0% respectively. This shows that it is important for the bank to improve customer loyalty by designing a proper strategy to enhance bank reputation and customer satisfaction. However, the bank reputation is found to play a more crucial role in improving customer loyalty as compared to the enhancement of customer satisfaction.

The significant contribution of both customer satisfaction and bank reputation on the loyalty of customers towards BMS is very much related to the programs introduced by the bank to retain their customers. BSM has developed the *shariah* digital data management to help the bank to make business decisions for the betterment of the customers. To maintain a close relationship with their customers, the bank has initiated a variety of event activities for marketing communications internally and externally to increase customer loyalty. In these activities, customers are invited to participate actively during

the programs while banking products are closely introduced and discussed. These activities include: BSM friends (the customer gets customer); BSM fantasy (direct prize); BSM brand awareness (direct sales event which is done indoor or outdoor with various themes); *Gebyar* (gather with customers with activities such as cycling, fun walk, and gymnastics); *iBvaganza* (Islamic banking education program); direct gifts for regular customers' fresh funds; priority customer gathering; and customer site visits to the bank offices (BSM - Bank Syariah Mandiri, 2019).

Our findings of the significant influence of customer satisfaction and bank reputation on customer loyalty are in line with the marketing theory and are supported by previous studies (Helm & Tolsdorf, 2013; Wang et al., 2003; Abd-El-Salam et al., 2013; and Tang, 2007). Bank reputation positively influenced customer loyalty (Tang, 2007) as a good bank reputation helps to ascertain customer loyalty (Helm & Tolsdorf, 2013; and Rahman et al., 2020) and attract more new customers (Abd-El-Salam et al., 2013). Other studies have also found that customer satisfaction is the core of customer loyalty (Belás & Gabcová, 2016), and it is one of the crucial customer loyalty components (Munari et al., 2013). Most of the marketing studies found strong evidence that customer satisfaction is one of the most important determinants of customer loyalty in the banking industry (Minh & Huu, 2016; Hassan et al., 2012; and Hassan et al., 2013).

4.4 The Mediating effects of bank reputation and customer satisfaction on the service quality-customer loyalty relationships

Referring to Figure 2, the findings of mediating effects of bank reputation (BR) and customer satisfaction (CS) on the service quality (SQ)-customer loyalty (CL) relationships are respectively reported in Figure 3(a) and Figure 3(b). As illustrated in Figure 3(a), the study documented strong evidence of a significant mediating effect of bank reputation on the service quality-customer loyalty relationship at the 1% level as indicated by the Sobel-test's p-value of 0.012. This indicates a crucial role of having a good bank reputation for retaining customer loyalty through improving the service quality.

Figure 3 (a) : SQ →BR→CL   Figure 3 (b) : SQ →CS→CL
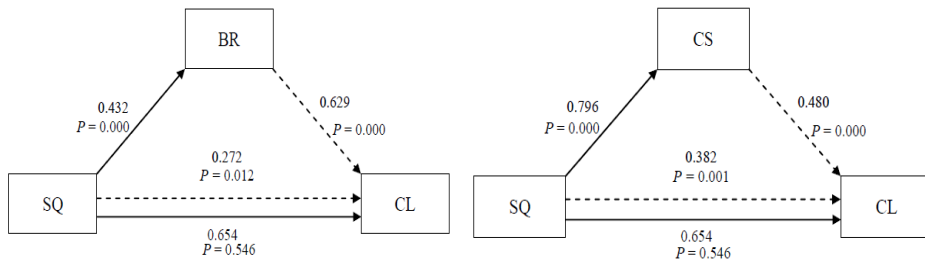
The significant mediating effect of bank reputation (BR) on the service quality (SQ)-customer loyalty (CL) relationships showed that bank reputation acted as a full mediated variable since the effect of service quality on customer loyalty is only found indirectly and significantly through the bank reputation channel, while directly, the service quality is found to have an insignificant effect on customer loyalty. This finding further confirmed the importance of enhancing bank reputation through the improvement of service quality to maintain customer loyalty.

Furthermore, as illustrated in Figure 3(b), the study found a significant mediating effect of customer satisfaction on the service quality-customer loyalty relationship at the 1% level as indicated by the Sobel-test's p-value of 0.001. This represents a critical role in satisfying customers by serving them with better quality as one of the strategic efforts to retain customer loyalty. Since our study found an insignificant direct effect of service quality on customer loyalty, its significant impact is only found between service quality and customer loyalty indirectly through the customer satisfaction channel. Thus, the customer satisfaction variable is recorded to function as the full mediating variable. This finding further validated the importance of satisfying customers through the improvement of service quality to retain the loyalty of existing customers and attract new potential customers.

Our finding of the significant mediating effect of bank reputation on service quality-customer loyalty relationship is supported by previous studies (Tang, 2007; Abd-El-Salam et al., 2013; and Bontis et al., 2007). These studies documented bank reputation as significant in mediating the effect of service quality and loyalty of bank customers. Meanwhile, our empirical evidence of the significant mediating effect of customer satisfaction on service quality-customer loyalty relationship is supported by Saputra (2013), Putra & Herianingrum (2014), Abd-El-

Salam et al. (2013), and Kurniawan & Shihab (2015). These studies documented that customer satisfaction acted as the mediator in the effects of service quality on customer loyalty. The banking consumers who are highly satisfied by their banking experience and enjoy better service quality would have good perceptions of the bank (Abd-El-Salam et al., 2013). Consequently, this would turn them into loyal banking customers (Minh & Huu, 2016; Saputra, 2013; and Leaniz & Rodríguez, 2016).

Overall, our empirical evidence suggested that to retain existing customers and attract new customers, the bank should focus on improving bank reputation and customer satisfaction by providing better service quality. The bank should improve all dimensions of its service quality, both tangibility and intangibility. For the tangible aspect, the bank could for example provide buildings and furniture with a modern design, convenient and large parking lots, information technology-based banking facilities, Islamic and charming personnel appearance, and etc. Meanwhile, the intangible dimensions of service quality are related to reliability, responsibility, empathy, and assurance. These dimensions are closely linked to the improvement of soft skills, face-to-face services, fast and accurate digital-based services, secure online transaction, and bank personnel attitude in which they must be polite, emphatic, and caring. The bank should also ensure the *shariah* compliance of their products and operation so that customers would perceive the bank to not only just be *shariah* compliant in label, but is instead actually practising Islamic values which sets it apart from conventional banks. Customers who enjoy better services and *shariah*-compliant products would have a higher expectation and enjoy more satisfaction. Consequently, this would lead them to view the bank with a good reputation and finally prevent them from switching to other bank competitors, either Islamic and conventional.

However, providing a good service to the customers would not guarantee their loyalty to the bank due to better services provided by other competitors (Afsar et al., 2010). Thus, the bank should always continuously improve its services by benchmarking to the services offered by its competitors in addition to carrying out an evaluation mechanism for measuring customer satisfaction and loyalty periodically. For example, BSM might critically review the report by the Marketing Research Indonesia - MRI (2019) stating that its customer loyalty level was far behind the loyalty level of customers of BMI and use this as reference in designing strategic bank policy considering that

BSM is the largest Islamic bank in Indonesia. The bank should always prioritize customer satisfaction by providing the best service. The bank should not only offer products that are safe and beneficial to society, but it should also provide maximum protection to consumers by enhancing a customer deposit guarantee policy. The bank should ensure all customers are insured at the national deposit insurance corporation to provide a reserve for losses on customers' earning assets.

5.0   Conclusion

This study empirically measured and analyzed the mediating effects of service quality on the loyalty of Islamic banking customers through the channels of bank reputation and customer satisfaction. 320 respondents from 113,146 customers of Bank Mandiri Syariah in the Banda Aceh City, Indonesia were selected as the sample of the study using a purposive sampling technique. Based on the Structural Equation Modeling (SEM) analysis, the study found evidence that while service quality has a significant positive influence on bank reputation and customer satisfaction, but it has an insignificant effect on customer loyalty. Bank reputation and customer satisfaction were also documented to have a significant mediating effect on services quality-customer loyalty relationship.

Our findings suggest that to enhance customer loyalty further, bank management should design a proper strategy focusing on improving bank reputation and customer satisfaction through improving the quality of their services. Both tangible and intangible service quality dimensions should be enhanced continuously by the banks. For the former dimension, the bank should always provide upgraded buildings and furniture with a modern design, comfortable and large parking lots, information technology-based banking facilities, financial technology (fintech) facilities, personnel with pleasant Islamic appearance, and etc. For the latter dimension, the focus should be given on aspects of reliability, responsibility, empathy, and assurance. These dimensions are closely related to the improvement of soft skills, face-to-face services, speedy and accurate digital-based services, secure e-transaction, and bank personnel attitude in which they must be polite, emphatic, and caring. Finally, the bank should also ensure the *shariah* compliance of its products and its operation. The bank customers who have enjoyed better services and *shariah* compliant-based products

would be highly satisfied and perceived the bank to have a good reputation, thus finally becoming loyal to the bank.

To further provide more robust empirical findings of the mediating effects of customer satisfaction and bank reputation on the quality service-customer loyalty relationship of Islamic banking institutions in Indonesia, it is recommended for upcoming studies on this issue to cover more Islamic banks nationwide. Exploring determinants of the customers of Islamic banks versus conventional banks with a comparative treatment would also offer additional insights into the analysis. Finally, considering other determinants of customer loyalty such as switching cost, financial inclusion, literacy, and innovation could enhance the existing empirical findings for the case of Islamic banks in Indonesia in particular, and global Islamic banks at large.

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