

# **Service Quality and Customer Loyalty in Malaysian Islamic Insurance Sector**

## **Exploring the mediating effects of Customer Satisfaction**

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DOI: 10.6007/IJARBSS/v6-i3/2030 URL: <http://dx.doi.org/10.6007/IJARBSS/v6-i3/2030>

**Abstracts:** The purpose of this study is to explore the mediating role of customer satisfaction between service quality dimensions and customer loyalty in Malaysian Islamic insurance sector. Based on the literature, six service quality dimensions were used to develop theoretical understanding about customer satisfaction and loyalty. This study proposes and tests a framework via structural equation modeling (Amos-16). The results of the analysis indicated that four of six service quality dimensions (tangible, responsiveness, fairness, and reliability) positively influence customer satisfaction which further influences customer loyalty. In other words, customer satisfaction mediates the relationship between four of six service quality dimensions (tangible, responsiveness, fairness, and reliability) and customer loyalty. Only two service quality dimensions (assurance and empathy) were not significantly related with customer satisfaction and loyalty. The findings further suggest that fairness have strongest effect on customer satisfaction and loyalty. The result of the study will help the managers and professionals to better understand how customer perceive service quality dimension and how these service quality dimensions are important for customers as well as for the organization. The study tested the impact of service quality dimensions on customer satisfaction and customer loyalty and found that tangibility, responsiveness, reliability, and fairness positively influence customer satisfaction. Therefore, the result of the study will help managers and professionals about how to deal with the customers to maximize the organizational profit. The result of the study suggested that fairness have strong influence on customer satisfactions and

managers should pay attention on the fairness to improve service quality and maximize the customer satisfaction. As per our best knowledge, the suggested model and Islamic insurance sector have never been investigated before.

**Keywords:** Service quality, SEVAQUAL model, fairness, customer satisfaction, customer loyalty.

Over the last two decades, researchers and professionals interest has been increasing in the customer services. The main reason behind increasing interest is major contribution of service sector (50 to 70 per cent in developed countries) in economic development. Assessing the quality of services is difficult because of their intangible nature as compare to product which can be inspected and evaluate before sales. Therefore, researchers are eager to develop a suitable measure to evaluate service quality but unfortunately, to date there is not universally accepted measure exists (Pollack, 2009). Kanovska (2009) argued that organizations have been trying their level best to identify customer needs and provide better services in order to satisfy customers and get competitive advantage in the market.

Customer loyalty, with its final effect on customer's repeat purchasing of the same item or using same distributing channel, is perhaps most important factor in services marketing. Indeed, loyal customers who are engage in repeat purchases are main supporters of any business. Service quality has been gain special attention from both researchers and practitioners in the recent years with the supported of original work by Paresuraman et al (1985). Practitioners believe that service quality leads to significant and beneficial effects on the roots of the performance for the firm. Sandhu and NeetuBala (2011) suggested that explaining customer satisfaction, customer loyalty and service quality concept can help researchers to develop service marketing models. In competitive environment there is scarcity of resources, so good understanding and knowledge about the influence of customer satisfaction and customer loyalty on customer loyalty provided indication to the practitioners that where is the best to devote marketing attention.

Among few studies focus on service quality and customer satisfaction mostly researchers did not use few dimensions and some researchers didn't use all dimensions suggested by SERVQUAL model (Kuo, 2003). The statistics of past literature shows that from 2003 to 2010 only 6 studies used all dimensions of SERVQUAL model to examine the effect of service quality on customer satisfaction. Therefore, as per the statistics little attention has been paid to understand the relationship between service quality using all service dimensions and customer satisfaction. Therefore, this study will further examine the effects of service quality using SERVQUAL dimension on customer satisfaction and loyalty in Malaysian Takaful.

Issues related to customers' satisfaction and loyalty in term of service quality in insurance industry have several prior researches worldwide, for examples in India (K. Mridula, 2011), (Sandhu & NeetuBala; 2011), (Deepika & Manish; 2011); Malaysia (Ahmad & Sungip; 2008); Bangladesh (Rahman, Afza & Chowdhury; 2007), but mostly the researches limited to conventional insurance. The similar researches but more focus on Islamic insurance industry still limited published and little effort to investigate it (Sharif & NorHafiiyah; 2011), (Hamid; 2011).

### **Islamic Insurance (Takaful) in Malaysia:**

Nowadays, Islamic Insurance (Takaful) industry in Malaysia is expected to flourish well made up of the overall Malaysian Takaful Sectoring and insurance market and this drawn an attention of researcher toward this industry. Based on primary information published by Malaysian Takaful Sector Negara Malaysia, the central Malaysian Takaful Sector, confirm that conventional and Islamic insurance sector are making remarkable progress.

The healthy growth will be continued in future due to strong economic fundamentals in Malaysian economy. But, why this sector becomes popular? There is some critical factors lead to the successful development of this industry such as development of human capital in order to ensure that *Sharia* governance and compliance become important part of business operation and governance. The highly skilled and knowledgeable employees are involved in Takaful operation and providing good services to Muslim and non-Muslim consumers.

In order to support the growth, Malaysian Takaful Sector Negara Malaysia continuously endeavor's to provide a sufficient financial environment and to promote the development of a progressive and flexible Takaful industry in this challenging global environment. In recent times competition has become increasingly fierce among Takaful companies in terms of satisfying customer's needs. Therefore many Takaful companies have started devising various methods and means of attracting more customers through these methods. Therefore, this study focuses on service quality and customers' satisfaction and loyalty in the Takaful industry in Malaysia.

### **Service Quality:**

Parasuraman et al., (1991) proposed service quality model which is known as SERVQUAL instrument. In the beginning this instrument was based on ten dimensions of service quality; reliability, tangible, responsiveness, competence, courtesy, credibility, security, communication, understanding and access. But then in the subsequent study, Parasuraman et al., (1988) realized that dimension not all useful on measuring the service quality, so summarized these ten dimension into only five, whereby here, the authors developed SERVQUAL, a five-dimension scale represent Reliability, Tangible, Responsiveness, Assurance and Empathy. Then new researchers such as (Juga et al., 2010; Yuan et al., 2010) also use this five dimension in their studies.

**Tangible** defined as "Equipment's, physical facilities and appearance of personnel" (Jayaraman,et. al, 2010) defined that tangible factor can give appearance to the company representative facilities, equipment and communication materials. The authors highlight that there is positive correlation and more significant in customer satisfaction. These statement also support by (Salman,et al, 2011) which is indicated the same finding. The data shows that customer satisfy by the infrastructure facilities, staff appearance and the décor. **Reliability** defined as "able to perform the promised services accurately and dependably. According to the Parasuraman, et al., (1988) indicated that reliability is the ability of organization to get their services on time and based on the promised that already made with customer. (Salman, et al, 2011) argued that reliability extent as delivered services based on the standards expected and a promise by services provider. The meaning here is the customer supposed to get the same

value services as much as they already paid. The author found that there is positive relationship between reliability and customer satisfaction. **Empathy** defined as “individual attention provided by firm to its customer”. (Salman, et al, 2011) stated that the core meaning for empathy is known the customer need and give the individual attention. **Assurance** describes assurance as “courtesy and knowledge of employee and their abilities to inspire trust and level of confidence” (Parasuraman et al., 1988, p.23). **Responsiveness** defined as “willing to help and providing prompt services to the customers” (Jayaraman, et. al, 2010) defined that responsiveness factor as a need of the customer in providing the quality of services but not obligation. Based on (Salman, et al 2011) customer prefers to have a friendly relationship with service providers and found that responsiveness and customer satisfaction are positive correlated.

### **Fairness:**

Berry et al. (1994) explained that due to intangibility of services, customer sensitivity to fairness is important in service industry. Furthermore, Carr (2007) also argued that based on equality theory, customer evaluate services by comparing services they received from different service providers. Adams (1963) also introduced the concept of “comparison others” which explain that “individual are motivated by a comparison of the ratio of their input to their outcome relatively to the same ratio of other that are comparable to them”. Further suggested that “comparison also be made against a pertinent norm or standard (Jacoby, 1976, p.1053)”. Equity services are reported to be the main drivers of satisfactions of customer and customer’s loyalty in the services encounters (Olsen and Johanson, 2003).

Researchers have always been connected the concept of fairness with service industries because intangibility of services makes the customer to rely on fairness issue for satisfaction and loyalty (Berry et al., 1994). Zhu and Chen (2012) argued that customer perception about unfair treatment by the company leads to un-satisfactory feelings. Researchers have been considered fairness or justice as an important factor for customer satisfaction in different setting e.g. airline, banking, IT services, hospitals, phone services (Carry, 2007; Han et al., 2008; Zhu and Chen, 2012) but limited literature about effect of fairness on customer satisfaction in Islamic insurance sector motivated researchers to investigate this area.

### **Customer satisfaction:**

Customer satisfaction is one of the key themes in management and marketing research in last two decades and researchers found significant relationship between customer satisfaction and customer loyalty. Luo and Bhattacharya, (2006) have examined the theoretical and conceptual foundation of customer satisfaction and found that customer satisfaction is a key driver for customer loyalty. Furthermore, many other empirical researches provide strong evidence that customer satisfaction play key role in business success and organizations with high number of satisfied customers enjoy high revenue (Abu-Elsamen et al., 2011). Chadha and Kapoor (2009) conducted research in the area of marketing theory and found that customer satisfaction strongly influence customer loyalty.

Andreassen (2000) suggested two conceptualization of customer satisfaction; first conceptualization is transaction specific and second conceptualization is cumulative. In the view of transaction specific, customer satisfaction is considered as post-choice evaluation judgment of certain buying decision. Researchers have been contributed to the body of literature related to advantages and disadvantages of this specific customer satisfaction at individual level. In contrast, cumulative customer satisfaction is considered as overall evaluation of customer satisfaction which is based on overall purchase and consumption experience with organization service or product over specific time. Fornell (1992) argued that cumulative customer satisfaction is more effective than transaction to predict customer past, present and future satisfaction. Therefore, cumulative customer satisfaction encourages organization to invest more in customer satisfaction.

Cronin & Taylor (1992) argued that customer satisfaction is based on customer experience about services provided by the organization. In other words, service quality is considered as determinant of customer satisfaction because service quality is considered as output of service providers. Researchers have been trying to clearly explain the meaning and measurement of customer satisfaction and service quality. There are few things in common between service quality and customer satisfaction. In comparison between them, customer satisfaction is considered as broader term whereas service quality more specifically focuses on service dimensions (Wilson et al., 2008). There are some other factors like product quality and price might effect on customer satisfaction but perceived service qualities are major components of customer satisfaction.

### **Customer Loyalty:**

Abu-Elsamen et al., (2011) argued that many professional beliefs on retaining customers by increasing customer satisfaction and customer loyalty as core marketing strategy. Furthermore, researchers argued that service quality and customer satisfaction are most core marketing priorities since they are essential for customer loyalty, such as positive feedback from customer, repeat sales (Han and Ryu, 2009; Liu and Jang, 2009b). In addition, Ryu et al., (2012) found that service quality enhance the level of customer satisfaction.

Dick and Basu (1994) explain three different of attitudes in the form of three different types of loyalty. Relative attitude explain that product characteristics are the main reason which influence repeat purchase. Relative attitudes consist on two dimensions: attitude strength which evaluate the characteristics of the product and attitudinal differences which explain that if customer find great difference between alternative products the customer attitudes is more relative.

Pritchard and Howard (1997) conducted research in tourism context and found relationship between customer satisfaction and true loyalty. Furthermore, Selnes (1993) argued that in some segments customer loyalty can be derived from brand reputation whereas in other segments customer loyalty may be derived from customer satisfaction. Albert and Msida (2000) studied customer loyalty, service quality and customer satisfaction.

**Hypothesis:**

**H1:** Customer satisfaction mediates the relationship between tangible and customer loyalty.

**H2:** Customer satisfaction mediates the relationship between reliability and customer loyalty.

**H3:** Customer satisfaction mediates the relationship between responsiveness and customer loyalty.

**H4:** Customer satisfaction mediates the relationship between assurance and customer loyalty.

**H5:** Customer satisfaction mediates the relationship between Empathy and customer loyalty.

**H6:** Customer satisfaction mediates the relationship between fairness and customer loyalty.

**CONCEPTUAL FRAMEWORK**

*(Independent Variable)*      *(Mediating Variable)*      *(Dependent Variable)*

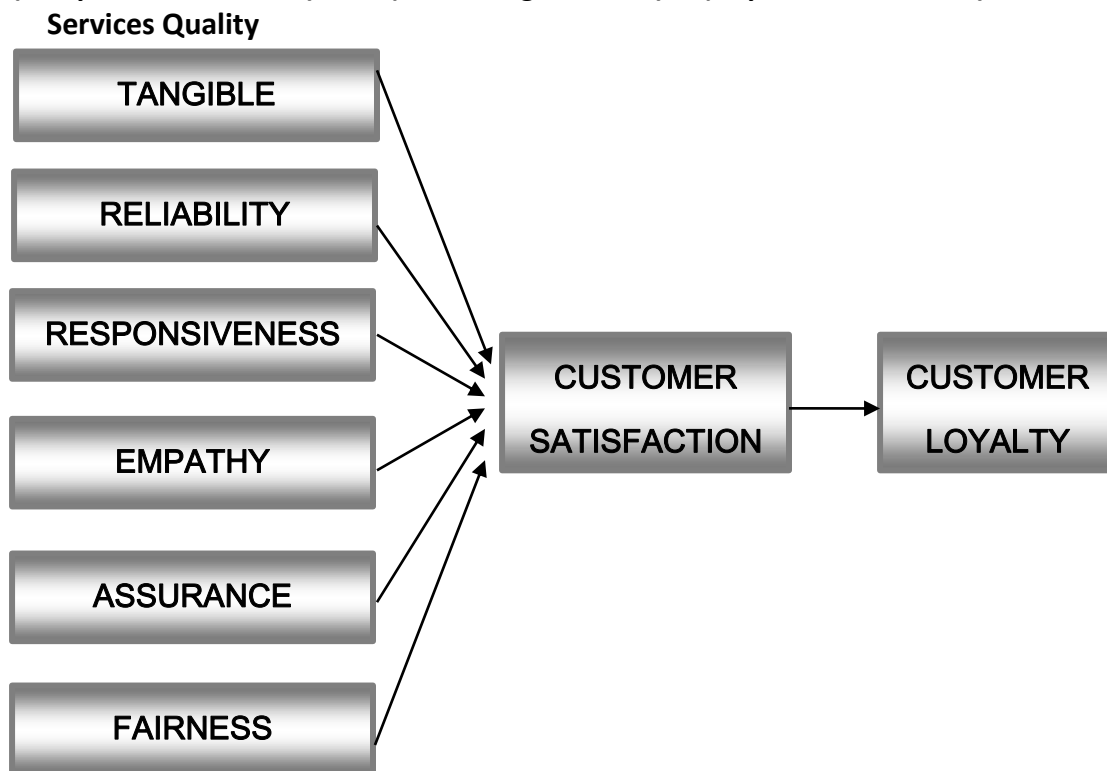


Figure 1: Conceptual Framework

**Methodology:**

The purpose of this study is to investigate the mediating role of customer satisfaction between service quality dimensions and customer loyalty. Takaful policyholders from list of Takaful providers in Malaysia become as the sample. (Latest information retrieved from Malaysian Takaful Sector Negara Malaysia; the total numbers of listed Licensed Takaful Operators in Malaysia is 12 companies). The data was collected from 193 policy holders of 12 Malaysian Islamic insurance providers.

**Measurement**

The measurement used in this study was adopted from past research. In order to measure the customer satisfaction the 3-items scale developed by Bitner and Hubbert (1994) was used. Furthermore, to measure the customer loyalty, 8-items instrument developed by Abu-ELSamen et al., (2011) was used. In order to measure the service quality dimensions, 21-items was used commonly known as SERVQUAL scale. In this, the researcher added one additional service quality dimension which in not included in SERVQUAL model with the name of “Fairness”. In order to measure fairness, the 11-items instrument developed by Zhu and Chen (2012) was used to measure fairness.

Table 1: Reliability of the Scale

Constructs	Reliability
Tangible	0.654
Reliability	0.711
Responsiveness	0.723
Assurance	0.810
Empathy	0.845
Fairness	0.869
Customer Satisfaction	0.799
Customer Loyalty	0.818

Table II

Measure of Model fit

Measures	Base Line	Suggested By
RMSEA	<0.05	Byrne, 2001
CFI	>0.90	Byrne, 2001; Cleveland et al., 2009, Chen, 2008
AGFI	>0.80	Chau, 1997
CMIN/DF	<3	Byrne, 2001
TLI	>0.89	Loible et al., 2009
IFI	>0.90	Lai, 2009

Table III

Measurement Model fit

Overall Model Measure	Model Score	Acceptable Model fit	Acceptable Baseline
CFI	0.951	Passed	>0.90
AGFI	0.891	Passed	>0.80
RMSEA	0.022	Passed	<0.10
CMIN/DF	0.964	Passed	<3
TLI	0.943	Passed	>0.89

Table IV

Structural Model fit

Overall Model Measure	Model Score	Acceptable Model fit	Acceptable Baseline
CFI	0.963	Passed	>0.90
AGFI	0.905	Passed	>0.80
RMSEA	0.012	Passed	<0.10
CMIN/DF	0.971	Passed	<3
TLI	0.956	Passed	>0.89

Table V

Summary of Effects

Variables	Direct Effects	Indirect Effects	Total Effects
Tangible --> Customer Satisfaction	0.511	-----	0.511
Reliability --> Customer Satisfaction	0.459	-----	0.459
Assurance-> Customer Satisfaction	0.122	-----	0.122
Responsiveness--> Customer Satisfaction	0.687	-----	0.687
Empathy -----> Customer Satisfaction	0.101	-----	0.101
Fairness --> Customer Satisfaction	0.399	-----	0.399
Tangible--> Customer Loyalty	.114	.614	0.728
Reliability---> Customer Loyalty	.201	.624	0.825
Assurance --> Customer Loyalty	.225	.112	0.337
Responsiveness--> Customer Loyalty	.213	.711	0.924
Empathy --> Customer Loyalty	.024	.069	0.093
Fairness --> Customer Loyalty	.149	.859	0.908
Customer Satisfaction --> Customer Loyalty	.844	-----	0.844

Based on table V, Responsiveness have strongest direct effect on customer satisfaction (effect=.687) whereas assurance and empathy have weakest direct effect on customer satisfaction (effect=0.122, 0.101) respectively. Furthermore, other service quality dimensions such as



tangible, reliability and fairness have considerable direct effect on customer satisfaction (effect=0.511, 0.459, 0.399). In contrast, six service quality dimensions have direct and indirect effect on customer loyalty. Such as tangible have stronger indirect effect on customer loyalty (indirect effect=.614) but weak direct effect (effect = .114). Similarly, reliability have stronger indirect effect on customer loyalty (effect=.624) but weak direct effect (effect=.201). Surprisingly, assurance have slightly stronger direct effect (effect=.225) on customer loyalty but weak indirect effect (effect=.112). Furthermore, responsiveness indirectly influence customer loyalty (effect=.711) but weak direct effect (effect=.213) on customer loyalty. With reference to empathy, direct (effect=.024) and indirect effect (effect=.069) on customer loyalty is weak. Among all service quality dimensions, fairness have strongest indirect effect on customer loyalty (effect=.859) but direct effect on customer loyalty is weak (effect=.149). Finally, customer satisfaction strongly and directly influence customer loyalty (effect=.844).

Table VI display the summary of hypothesis, which shows that all structural paths are statistical significant except assurance and empathy. According to hypothesis results, H1 postulates that if service providers have better equipment's, physical facility and attractive appearance of the staff, the customer will feel satisfied and that satisfaction will leads to loyalty (H1=0.315). Furthermore, if service provider provide services on time as promised (reliability), it creates sense of satisfaction and enhance customer loyalty (H2=0.441). Subsequently, prompt help and friendly behavior of service provider enhance customer loyalty through customer satisfaction (H3=0.201). Surprisingly, individual attention provided by the company to its customer and employees ability to inspire customer trust and confidence does not create customer satisfaction (H4=0.051, H5=0.034). Finally, customer perception about fair treatment of the service providers leads to satisfactory feelings which create sense of loyalty (H6=0.518).

Table VI

Hypothesis and Results

	Hypotheses	P-value	t-value	Accept or Reject
H1	Customer satisfaction mediates the relationship between tangible and customer loyalty.	0.001	4.61	Accept
H2	Customer satisfaction mediates the relationship between reliability and customer loyalty.	0.020	2.32	Accept
H3	Customer satisfaction mediates the relationship between responsiveness and customer loyalty.	0.049	4.08	Accept
H4	Customer satisfaction mediates the relationship between assurance and customer loyalty.	0.910	1.15	Reject

H5	Customer satisfaction mediates the relationship between Empathy and customer loyalty.	1.120	0.49	Reject
H6	Customer satisfaction mediates the relationship between fairness and customer loyalty.	0.031	3.15	Accept

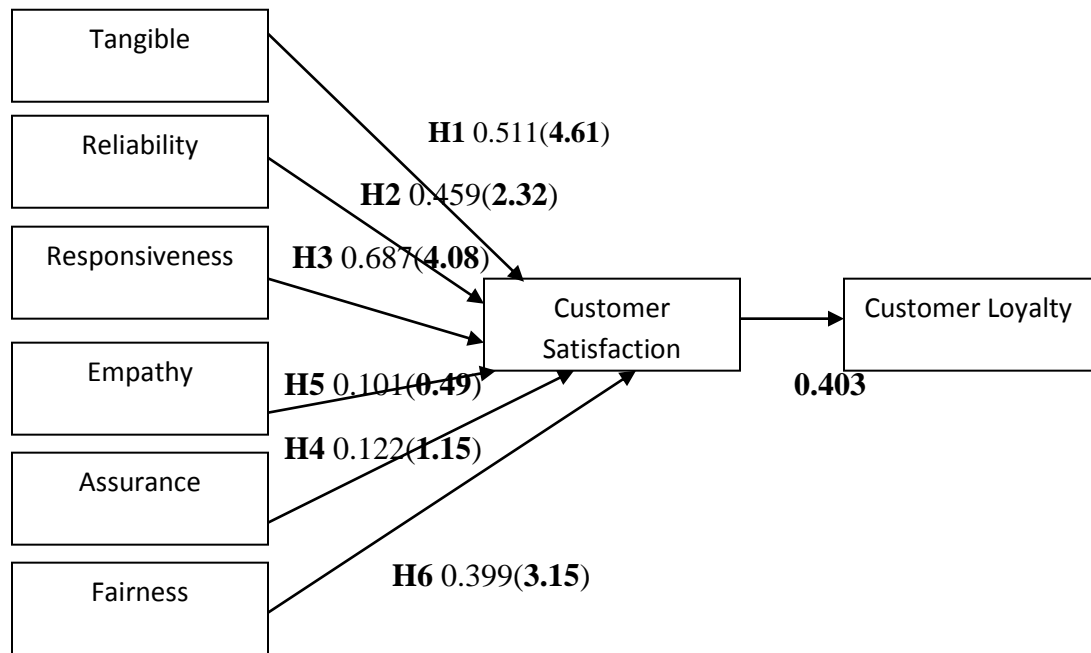


Figure 2: Complete model (Standardized)

**Discussion and Future Research Directions:**

The result of the analysis indicate that reliability positively influence customer satisfaction in Malaysian takaful. The policy holders in Malaysian takaful perceived that their company provides services as promised. In addition, policy holders also believe that their company provides timely services to them and their operating hours are reasonable. Furthermore, policy holders also satisfied with organization services in terms of problem solving. Policy holders in Malaysian takaful consider reliability in terms of quality of services as promised, timely services within reasonable operating hours and solving the problem on urgent basis. In short, policy holders in Malaysian takaful consider reliability as important factor to satisfy their needs and create loyalty.

Responsiveness is another factor for service quality dimension and the result of this study indicate that responsiveness positively influence customer satisfaction. Policy holders perceived

that staff in Malaysian takaful are trustable and their claim system is reliable which grouped and named as responsiveness. Referring to the definition of assurance “willing to help and providing prompt services to the customers” (Parasuraman et al., 1988). If the staffs is trustable and claim system is reliable, the policy holders will be more satisfied with the company with will further enhance their loyalty towards the company. In other words, when policy holder find takaful staff trustable and reliable claim system, it increase policy holder satisfaction and improve loyalty.

Tangibility is another dimension of service quality and the result of this study indicated that tangibility positively influence customer satisfaction. Referring to the definition of tangibility “tangible facilities, pamphlets, and staff appearance” (Parasuraman et al., 1988). Policy holders in Malaysian takaful perceived tangibility in terms of insurance system well designed pamphlets and cooperative staff. In other words, if insurance system is friendly, pamphlets are well designed, and staffs helps the policy holders to understand the policy and claim system, it will increase the policy holders satisfaction and create loyalty with the organization.

The result of the study indicated that fairness positively influence customer satisfaction in Malaysian takaful. Policy holders in Malaysian takaful perceived that the organization treat all customer equally and facilitate them without being biased. The reasonable explanation to the policy holders, consistent procedure across users and consistency in meeting with all users make policy holders satisfy with the company and create loyalty. With reference to past studies, the result of this study is consistent with Laroche et al., (2004) result. According to the Negi (2009) tangibility, assurance, reliability is important predictor for customer satisfaction and play important role in customer loyalty should not be ignored in analyzing service quality.

The result of this study regarding customer satisfaction, customer loyalty and service dimensions further support the theoretical view point of Kotler & Keller (2009) in which they claimed that “high level of quality leads to high level of customer satisfaction”. Therefore, the result of this study confirms that service quality dimensions are important predictors for customer satisfaction and customer loyalty. Reichheld (2003) argued that commonly used customer loyalty metrics cannot really measure the actual customer loyalty (purchase and recommendations). Bitner and Hubert (1994) stated that, over all customers’ satisfaction with the services of an organization base on all types of experiences of the customer with particular organization. On general customer loyalty seems to be the part of strategic management; there are many ways of measuring and defining this issue. In literature generally we found three appropriate concepts to trace the customer loyalty. According to Wicks & Roethlein, (2009) those organizations continuously satisfy their customers, enjoy high profits and customer retention due to great customer loyalty. Therefore, every company trying their best to win customer hearts by satisfying them to make them loyal with the company brand which ultimately increase company sales and profits. In this regards, Larreche (1998) argue that the better customer perception about company brand always encourage the customers to go for that brand because customer perception and attitude about that brand is better as compare to competing brands. Therefore, to retain these kinds of customers, organizations should develop good relationship with them. To know, customer perception and buying decision, organizations conduct research and try to find the answers of different questions like what is the criteria to

buy certain product or services and are you satisfy with that product of services? Thus customer always prefers to buy that product or services that give them maximum satisfaction. The point of consideration is that what if customer expectation is changes, customer habits change? How companies can get to know about the competitors brands (might be competitors improved their brand) and customer change their brands. With the fast moving economies and rapidly changing market situations, every company make their customers as first choice. Therefore, organizations killing two birds with one stone by improving the product and service quality companies not only satisfy the customers but also develop brand loyalty and maximize their profits.

As discussed earlier, fairness has strongest positive effect on customer satisfaction but the point of consideration for researchers is that fairness is not service quality dimension in SERVAQUL model. SERVAQUL model consist on five service quality dimension which includes tangible, reliability, assurance, empathy, responsiveness and six dimensions "Fairness" was additional in the research framework. If the fairness has strongest effect on customer satisfaction it means that there might be some other service dimension which is not included in SERVAQUL model which might have some effect on customer satisfaction and customer loyalty. Therefore, researchers should investigate some other service quality dimension then SERVAQUL model in order to further strengthen the literature in the field of service quality, customer satisfaction, and customer loyalty.

### **Implications**

This study has theoretical and practical contribution. The purpose of the study was to examine the relationship between service quality dimensions which includes (tangibility, assurance, responsiveness, empathy, reliability, and fairness) on customer satisfaction and customer loyalty. The result of the study will help the managers and professionals to better understand how customer perceive service quality dimension and how these service quality dimensions are important for customers as well as for the organization. The study tested the impact of service quality dimensions on customer satisfaction and customer loyalty and found that tangibility, responsiveness, reliability, and fairness positively influence customer satisfaction. Therefore, the result of the study will help managers and professionals about how to deal with the customers to maximize the organizational profit. The result of the study suggested that fairness have strong influence on customer satisfactions and managers should pay attention on the fairness to improve service quality and maximize the customer satisfaction.

In terms of theoretical implications, this study contributes to the body of knowledge of service quality, customer satisfaction, and customer loyalty. The result of this study strengthen and support the view points of past researcher who claim that service quality work as predictor for customer satisfaction and customer loyalty. The researcher should further test these service quality dimensions in other sectors to examine the role of service quality in customer satisfaction. Furthermore, the findings of this study will help the researchers to understand the nature of effect and better understanding about service quality dimensions.

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