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## Understanding the Role of Bank Relationships, Relationship Marketing, and Organizational Learning in the Performance of People's Credit Bank

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## **Chapter 8**

### **CLIENT INTENTION TO LEAVE MODEL**

This chapter deals with the last research question (section 1.3) which is transformed into the hypothesized models of a client's intention to leave a relationship model in section 2.10 (from now on, the client intention model). Chapter 8 is a continuation of Chapter 6 which has the same unit of analysis, that is the BPR clients, but with a different focus on the analysis. The former analysis focused on an explanatory analysis by involving a sub-set of measurable variables available in Chapter 6. Chapter 6 put more of an emphasis on the exploratory analysis, which covers a large number of measurable variables of bank-client relationships.

From the BPR point of view, relationship marketing provides a basic premise in which keeping existing clients is preferable to attracting new ones. Transaction costs associated with the searching for and screening of new borrowers are higher than the costs of maintaining (retaining) existing borrowers (Reinartz & Kumar, 2003). Various empirical studies suggest that a higher level of client satisfaction leads to greater loyalty, hence, a higher retention rate and higher sales. Client satisfaction can reduce the intention to leave the relationship, hence, reduce the client switching rate of good clients.

However, satisfaction is not enough whenever competing banks move aggressively to lure new clients, including those clients already in a relationship with an incumbent bank. According to Gale (1997), the customer value approach considers both satisfaction and competitors' moves in offering value to bank customers.

The hypothesized model of client intention to leave a relationship put emphasis on two major variables that affect switching behavior i.e., (1) a satisfaction construct – an endogenous factor that internally triggers switches and (2) a lure construct – an exogenous factor that externally triggers switches. The termination of a relationship with good clients is an outcome of opportunistic behavior that exists at any point in time, but through relationship marketing it can be minimized. Most of the studies focus on ex-post relationship termination at the firm level and use the customer satisfaction index (Chapter 2), while this analysis focuses on ex-ante termination – the client intention to leave at the client level.

Given the hypothesized model and 146 cases of data sets, the structural equation model in Chapter 7 is used. The sequence of discussion in this chapter is presented as follows. Section 8.1 is the Confirmatory Factor Analysis of the Measurement Models. Section 8.2 is the Analysis of full latent SEM of the client intention to leave model. Section 8.3 is the Discussion. Finally, section 8.4 is the Conclusion: findings and limitations.

### 8.1 Confirmatory Analysis of the Measurement Model

The hypothesized client intention model consists of six constructs; four of them are measured by multiple indicators as shown in Table 8-1. The other two constructs are the duration of the relationship and the intention to leave the relationship. Each of them is measured by a single indicator. The duration of the relationship between the bank and the client is different between the year of the survey (2003) and the starting year of the relationship with the incumbent BPR. The intention to leave the relationship is measured by a single indicator<sup>1</sup>. Table 8-1 provides a summary of AMOS output five goodness of fit indexes to test the discrepancy between four hypothesized measurement models of four constructs and the data.

Table 8-1: Summary of Some Selected Goodness of Fit Indexes (or statistics) with Regards to the Main Constructs of the Client Intention Model

No.	Construct	Number of Indicators	CMIN (Chi-sq)		CMIN/DF	RMSEA	TLI	CFI
			Abs	Prob.				
1	Satisfaction	5	27.740	0.00%	5.54	0.18	0.98*	0.99*
2	Lure	5	46.291	0.00%	9.26	0.24	0.96*	0.98*
3	Prevention	6	57.559	0.50%	6.39	0.19	0.95*	0.98*
4	Value	8	108.547	0.00%	5.43	0.17	0.95*	0.97*
Total		24						
Rules of thumb of the GFI threshold level				≥0.05	≤2.00	≤0.080	≥ 0.95	≥0.94

Note: \* represents the corresponding hypothesized measurement model, which is a good fit with the sample data. The measurement model is judged to be a good fit as long as it meets one or more of the GFI criteria.

<sup>1</sup> Rust and Zahorik, (1993) inspired this approach instead of making an intention index, which is cheapest and fastest although it may risk bias (error) based on response inaccuracies due to (a) memory limitations and (b) dissonance which may cause subjects to exaggerate certain differences in service levels between current and former providers. A reduction of cost may often justify the somewhat reduced validity. Rust and Zahorik, (1993) measure switching behavior and customer satisfaction constructs.

All measurement models of the four constructs (Table 8-2) are a good fit as they have passed the threshold levels of both TLI and CFI. Fortunately, 23 regression weight indicators are statistically significant at 0.05 significant levels or above 1.96 critical ratios. One regression weight indicator – progressive lending – is statistically insignificant which will be excluded from further analysis of the full latent variable model in section 8.2 below.

## 8.2 Confirmatory Analysis of the Client Intention to Leave Model

At this juncture the full latent variable model (FLV) can be examined, which consists of (a) a path diagram of the hypothesized model in section 2.10 and (b) the result of the confirmatory analysis of measurement models of constructs in section 8.1. First, the FLV is examined by using the AMOS output of five goodness of fit indexes (GFIs) of the client intention model appearing in Table 8-2.

Table 8-2: Goodness of Fit Indexes of the Client Intention Model of both Model 1 and Model 2 Scenarios.

No.	FLV Scenario	Indicators	CMIN (Chi-sq)		CMIN/DF	RMSEA	TLI	CFI
			Abs	Prob.				
1	Model 1	23	691.02	0.00%	2.58	0.010*	0.96*	0.97*
2	Model 2	23	694.63	0.00%	2.59	0.011*	0.95*	0.96*
Rules of thumb for the GFI threshold level				$\geq 0.05$	$\leq 2.00$	$\leq 0.080$	$\geq 0.95$	$\geq 0.94$

Note: \* represents that the full latent variable of the hypothesized model is a good fit with the data.

According to the GFI criteria in Table 8-2, the two hypothesized client intention models are a good fit with the survey data. They have passed three out of five GFI threshold levels i.e., RMSEA, TLI, and CFI. Each of the models has 23 indicators that will be verified from the statistical significance of their regression weights (loading factors). Fortunately, all of the 46 indicators (measuring variables) in both model 1 and model 2 are statistically significant at a 5% level or above 1, 96 critical ratio. This means that no indicators are eliminated from the full latent variable models of both model 1 and model 2. Next, an examination of a statistical significance test of path coefficients for both model 1 and model 2 can be done. Table 8-3 displays the path coefficients output along with corresponding t-ratios.

Table 8-3: Regression Weights (Path Coefficients) of the Client Intention Model of both Model 1 and Model 2

No	Causal link			Model 1	Model 2
1	Duration	-->	Value	0.002* (4.549)	-0.004* (-1.085)
2	Duration	-->	Satisfaction	0.027* (25.479)	
3	Value	-->	Satisfaction	0.131* (2.550)	0.129* (2.311)
4	Prevention	-->	Satisfaction	-0.131 (-1.484)	-0.110 (-0.979)
5	Satisfaction	-->	Intention	-0.153* (-4.374)	-0.175* (-2.767)
6	Lure	-->	Intention	0.138* (4.099)	0.145* (3.862)
7	Prevention	-->	Value		0.243 (1.212)
8	Duration	-->	Intention		0.014 (1.693)
Number of regression weights of measuring variables					
insignificant				0	0
significant				23	23
Total				23	23

Note: The figure within the parentheses is the critical ratio (CR) or t-value of the path coefficient.

\* is statistically significant at a 5% significant level ( $t=1.96$ )

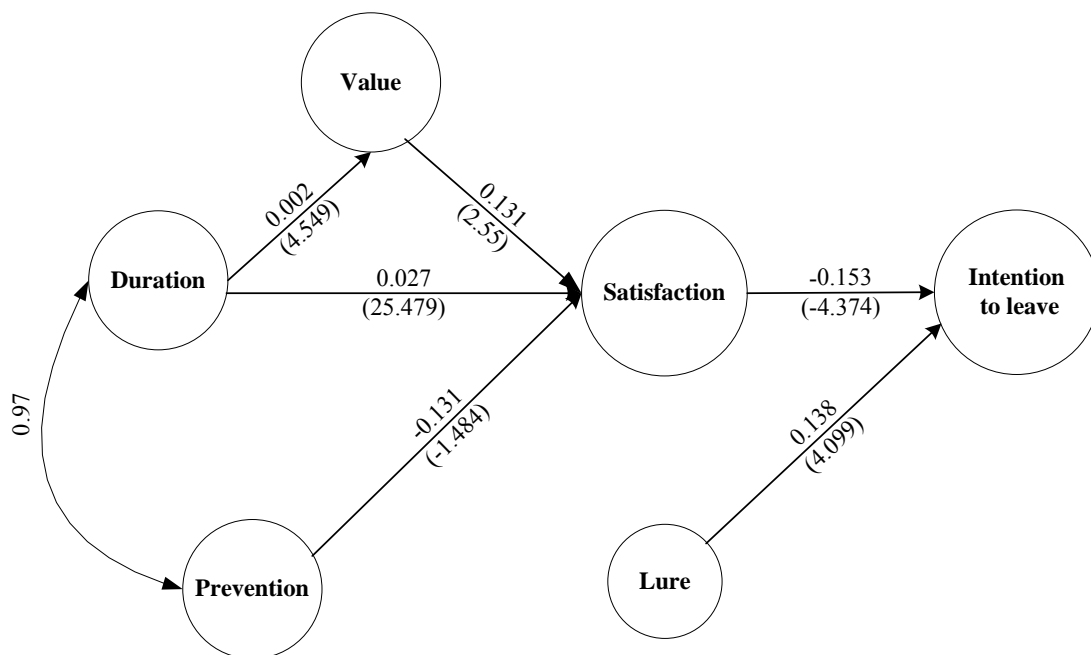
Based on the statistical significance test (Table 8-3), one of the models can be eliminated after comparing the differences between the profiles of path coefficients of models 1 and 2 as follows:

First, there are some shortcomings in path coefficient outputs of the models. Model 1 has a negative sign in the path coefficient of prevention on satisfaction. It should have been positive and statistically insignificant at a 5% level. This coefficient has critical value -1.484. Meanwhile, model 2 has two negative signs i.e., the path coefficient of (1) duration on intention to leave; and (2) prevention upon satisfaction are negatives, while it should have been positive. Second, model 1 has five path coefficients that are statistically insignificant, while model 2 has four path coefficients that are statistically insignificant.

This comparison implies that model 1 is superior to model 2, which means that model 2 is eliminated from further analysis. The path diagram in Figure 8-1 represents model 1 with its path coefficients.

The source of negative sign of path coefficient of prevention on satisfaction perhaps comes from a co-linearity between prevention and duration. This path coefficient has a bigger standard error that leads to the coefficient being statistically significant at a 13.8% level. However, in calculating path coefficients, simultaneous equation modeling (SEM) has taken into account the multi-colinearity among independent/exogenous variables (Hair et al., 1993, p. 587-588; Biderman, 2000).

Figure 8-1: Path Diagram of Client Intention to Leave the Model



Given that intention to leave relationship is a precondition to client switching, the impact analysis of the path coefficients suggests that the internally triggered to switch factor (i.e., satisfaction) is (in absolute figure of path coefficient) bigger than that externally-triggered to switch factor (i.e. lure), which are 0.153 and 0.138 respectively. The signs of those two impacts imply that (a) the higher the satisfaction leads to a lower intention to leave the relationship (or the higher potential loyalty or retention rate), and (b) the more aggressively a competitor lures the existing client, the greater the likelihood the client will leave the relationship (propensity to switch to a competing financial provider). All antecedent constructs seem to support the model, except for prevention. Moreover, the puzzle regarding the impact of preventive action on satisfaction will be covered in the next section. The impact of duration on value appears very low in comparison with the rest of the path coefficients. However, it is

necessary to be careful to infer this figure since the duration is measured in years of the relationship, while the rest of the constructs are measured by the five-scale Likert category. This means the impact of duration on value and satisfaction in absolute value can be higher<sup>2</sup>.

### 8.3 Discussion

One threat for BPR is when a good client moves to another bank / financial institution. In the 2003 survey (Chapter 6), there are only 27 (17%) clients who had the intention to transfer to another bank, and the other 109 (83%) never had an intention to leave the relationship with the incumbent BPR. BPR may feel secure based on this information. The problem is that (a) there is no data available for clients who have moved or exited from BPRs; thus the client respondents are those who still have a relationship with BPR. Therefore, client respondents may be those who have a high level of trust and loyalty to BPR; and (b) a higher level of competition in years to come may increase, inducing their intention to leave and eventually the exit rate for good clients who have a higher bargaining power will increase. This is an iceberg problem of the intention to leave phenomenon. The next chapter (Chapter 9) will be a clearer picture about how BPR deals with the opportunistic behavior of clients where the re-joiner clients can be a signal of an un-monitored intention to leave the relationship. As a matter of fact, although the relationship starts multilaterally initiated through a signed loan contract of both parties, BPR and the client, the exit is usually unilaterally initiated by good (creditworthy) clients or by the bank in cases of bad (un-creditworthy) clients. The good clients may pretend to remain in a relationship with BPR, but they can engage in a new relationship with competing financial providers for a while and then return to the former BPR as long as it offers at least equal value with competing financial providers. These explanations emerge from the fact that (a) the path coefficient of lure and intention to leave is positive and statistically significant; and (b) there are some re-joiner clients – revealed in Chapter 6; and (c) more importantly, there is increasing pressure of an offensive marketing strategy of some large commercial banks entering the market segment of BPRs. In 2003, some chiefs of BPR associations of Central Java, Gathyt and Said Hartono started complaining that some commercial banks were expanding their markets to

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<sup>2</sup> In other words, the standardized value of the path coefficients can be compared.

lower segments within the domain of BPR's loan market. This complaint echoes the sentiment of other provinces in the country where a commercial bank actively intrudes into the BPR domain (see Chapter 3). In intense competition, most likely the number of clients intending to move will increase since competitors attract (lure) prospective clients by promising many benefits in comparison with the existing relationship.

The discussion about client exit has been given little attention in the bank-relationship study. Ongena & Smith (2001) cover the topic lightly in which switching from one bank to another is the behavior of a client from one bank to end a bank relationship driven by exogenous or endogenous factors. Meanwhile, the relationship marketing study put heavy emphasis on the client exit under a group of discussion topics such as: customer satisfaction and loyalty (disloyalty), marketing orientation to increase client retention or to prevent client defection, etc. The termination of a relationship is seen as a loss of future company income and possibly company profit. Among others, according Reinartz and Kumar (2003) relationship marketing is concerned with the establishment and maintenance of long-term buyer-seller relationships. They also quote, for example, the case of AT&T, which claims it is much more efficient in (1) keeping customers who are at risk of defection and (2) better at pinpointing the customers who are likely to be long-life customers in its acquisition campaigns. This reasoning becomes a groundwork of the client intention model. As mentioned above, the model considers both internally-triggered factors (satisfaction) and externally-triggered factors (lure) as the core factors driving client intention to leave relationship with incumbent BPR. However, there is a big puzzle with the model i.e., negative sign path coefficient of the prevention on satisfaction. The prevention measures may be perceived by clients as counter productive actions. Anecdotal evidence shows the loan officers who actively keep in contact with clients can not fully accommodate client dissatisfaction (in the form of complaints), or give promises, or negotiate for a possible better solution. Generally, a loan officer as a bank representative has limited authority to make an instant decision to respond to an urgent need from a complaining client. Or, it implies that BPR only takes preventive measures seriously at the last moment when client dissatisfaction endangers a client exiting. BPR is a bureaucratic organization where the governance is guided by restrictive rules and regulations, standard operating procedures, a rigid job description, and a delegation of authority. In this context, preventive actions may



become an empty promise to clients that lead to counter productive actions. This may also signal that BPRs actually do not have true or clear strategies and policies regarding preventive measures to handle customer dissatisfaction. The duration and value of a bank-client relationship positively affect satisfaction that may offset negative effects from preventive measures. However, the existing duration studies on bank-client relationships suggest that the longer the duration of the relationship, the more likely a client exits (e.g., Farinha and Santos, 2002; Ongena and Smith, 2001). It means that the risk of client exits can occur at any point in time.

#### **8.4 Conclusion**

The BPR's client is the unit of analysis in this explanatory study of the client intention to leave model. However, this study reinforces the main study of the bank performance model. By doing so, BPR can learn the voices (complaints, grievances) from clients and client behavior in response to BPR policies or actions and provoking competitors, through their frequent interactions with clients, loan officers can seek for a clue and take prompt necessary actions.

From BPR's view, this study is concerned with what is called a defensive marketing strategy (Fornel and Wernerfel 1987, 1988), in the sense that the underlying intent of BPR's competition emphasizes that marketing resources may be better spent in keeping existing customers than by attracting new ones.

This study also gives some lessons to learn. Client satisfaction is necessary to increase the retention rate, but according to Gale (1997) satisfaction is not enough. BPR's board of directors has to respond proactively to clients and listen to client concerns to overcome the gap between their expectations and the real action taken by loan officers. The loan officers who stay in the front line may not be able to take corrective action. Within a dynamic environment, the BPR strategy may become obsolete, which can reduce client satisfaction. Moreover, Gale (1997) shares his experience that retail banks with higher retention rates perform better than branches with lower retention rates. Customer retention rates and attraction rates are driven by the customers' perception of what a particular bank offers relative to its competitors.

This experience may alert the BPR director to proactively revise the preventive actions in order to focus on client satisfaction positively. Increasing competition is real and offensive strategies from commercial banks, such as Bank Danamon with the

Danamon Simpan Pinjan: DSP (Danamon Savings and Loan<sup>3</sup>), increase tension in the microfinance market. Commercial banks have competitive advantages in terms of: (a) fund mobilization, (b) personnel quality, (c) technological advancements, and (d) geographical network. One thing that BPR can do to remain competitive is through the defensive strategies mentioned above. This could be a promising shield for BPR to remain in the market and grow with the progress of their clients. The need to cater to specific customers rather than all possible customers should be a more important policy for BPR. More specifically, the managerial implications of this analysis are a signal to BPR to look forward so the board of directors can take necessary actions, among others:

First, they can redefine job descriptions, especially related to the scope and/or depth of tasks of loan officers. For example, in Chapter 6 it was revealed that during the monitoring stage, loan officers put emphasis on repayment collections. In this case, the director can assign them additional tasks to pay more attention to information gathering. By doing so, they can start sorting borrowers into two categories – promising (creditworthy) and unpromising (credit unworthy) in such a way that BPR can anticipate potential valuable clients.

Second, they can improve the organizational learning – not only learning by doing but also learning by planning. Beyond their awareness, loan officers accumulate enormous tacit information from the field visit of monitoring. Without a regular and systematic mechanism of information codification and sharing for organizational improvements, this information will disappear. Learning by planning means BPR should take advantage of this information to anticipate future external changes (competitors' moves, mounting client dissatisfaction, etc.). This action is a corrective measure toward the weaknesses of BPR in information codification (Chapter 5) and counter productive in preventive measures toward client satisfaction. In addition to this, BPR can initiate complaint handling promptly to increase service quality. Practically, it reinforces speedy delivery in loan disbursements with an increasing degree of confidence, since the manager receives more up-to-date and accurate information from the field of loan monitoring

Third, they can revise the meaning of a “doorstep” or proactive approach which is not merely an expression of loan officers to onsite visits to clients, but also gives

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<sup>3</sup> See Chapter 3. BPR sees that DSP replicate BPR strategy and move offensively to the doorstep of a client within BPR market segment.

more meaning of the visit. The meaning of this approach are not only loan repayment or onsite collection that reduce the transaction costs of borrowers but also the utilization of frequent face-to-face contact to build trust and understanding between loan officers and clients to facilitate information updating. It facilitates the flow of private information from clients to BPR through loan officers. However, it is not an easy task because it entails a specific skill in “service excellence”, time allocation, and span of control loan officers toward their clients. This is a managerial problem where competitive pressures force BPR to be more creative to survive. In other words, giving additional meaning of “door steps” approach is turning information collection from by outcome of monitoring to main outcome comparable to repayment collection. The main outcome of monitoring is not only repayment collection but also information collection.