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A REVIEW ON MEDIATING EFFECT OF SERVICE QUALITY ON NON BANKING FINANCIAL INSTITUTION

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ABSTRACT

The non-banking financial companies (NBFCs) flourished in India in the decade of the1980s against the back drop of a highly regulated banking sector. While the simplified sanction procedures and low entry barriers encouraged the entry of a host of NBFCs, factors like flexibility, timeliness in meeting credit needs and low operating cost provided the NBFCs with an edge over the banking sector.NBFCs proliferated by the early 1990s. This rapid expansion was driven by the scope created by the process of financial liberalization in fresh avenues of operations in areas, such as, hire purchase, housing, equipment leasing and investment. The business of asset reconstruction has recently emerged as a green field within this sector following the passage of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002.NBFCs are financial intermediaries engaged primarily in the business of accepting deposits delivering credit. They play an important role in channelising the scarce financial resources to capital formation. NBFCs supplement the role of banking sector in meeting the increasing financial needs of the corporate sector, delivering credit to the unorganized sector & to small local borrowers. All NBFCs are under direct control of RBI in India. Paper highlights on review of impact of service quality of NBFC.

Key words: ***Non banking financial institution, Classification, and its service quality & its impact on the success of NBFC.***

I. INTRODUCTION

Non Banking Financial Companies (NBFCs)

According to the Reserve Bank of India Amendment Act 1997 the Non Banking Finance company was defined as under:-

⇒A financial institution which is a company,

⇒A non banking institution which is a company and whose principal business is to receiving of deposits under any scheme/arrangement/in any other manner or lending in any manner and

⇒Other non banking institutions/class of institutions as the RBI may specify.

The directions apply to a NBFC which is defined to include only non-banking institution,which is any hire-purchase finance, loan or mutual benefit financial company and an equipment leasing company but excludes an insurance company/stock exchange/stock broking company /merchant banking company.

The RBI (Amendment) Act, 1997defines NBFC'S as an Institution or company whose principal business is to accept deposits under any scheme or arrangement or in any other manner, and to lend in any manner. As a result of this new definition, a number of loan and investment Companies registered under the Companies Act by Business houses for the purpose of making

investments in group of companies are now included as NBFC. The Financial intermediaries in Indian Financial System are broadly characterized by Public owned, Monopoly or Oligopoly or Monopolistic market structure and are centralized. The Indian financial system has another part which comprises a large number of private owned, decentralized, and relatively small sized financial intermediaries and which makes a more or less competitive market. Some of them are fund based, and are called (NBFCs) and some are provide financial services (NBFSCs) Both NBFIs, NBFCs are (1) Loan companies (LCs) (2) Investment companies or ICs (3) Hire-Purchase finance companies or HPFCs (4) Lease finance companies or LFCs (5) Housing finance companies (or) HFCs (6) Mutual Benefit financial companies or MBFCs (7) Residuary

non-banking companies or RNBCs (8) Merchant Banks (9) Venture capital funds (10)

Factors (11) Credit Rating Agencies (12) Depositories and custodial services.

Classification of NBFCs

Classification of NBFCs as given in the Reserve Bank Amendment Act 1997, 1) Equipment leasing company (ELC): Carrying on as its Principal Business, the activity of leasing of equipment. 2) Hire Purchase finance company (HPFC): Carrying hire purchase transactions (or) financing of such transactions. 3) Housing finance company (HFC). 4) Investment Company (IC): Carrying the business of acquisition of securities. 5) Loan Company (LC): Financing by making loans and advances. (Does not include ELC, HPFC, HFC).6) Mutual Benefit companies (MBFC). 7) Residual non-banking company (RNBC): Company which receives any deposit under any scheme or arrangement, in one lump sum or in installments by way of contributions or subscriptions or by sale of units or certificates or other instruments or in any other form according to definition of NBFC. 8) Miscellaneous non-banking companies (MNBC): Managing,

Conducting or supervising as a promoter foreman or agent of any transaction or arrangement.

Ex: conducting any other form of Chit and Kuri which is different from

type of business mentioned above. After the above classification the Non Banking Financial companies were re-classified twice, during 1998 it was classified as four types they were 1) Equipment leasing, 2) Hire Purchase, 3) Investment Company and 4) Loan Companies.

During 2006 the NBFCswere reclassified as three types they are 1) Asset Finance companies (in this bothEquipment Leasing and Hire Purchase companies were merged), 2) Investment Companies and 3) Loan Companies

Apart from those classifications, in order to operate these NBFCs smoothly certain regulations/directions were issued they are a) Regulations for deposits for NBFCs accepting deposits, b) Regulations for NBFCs not accepting deposits and c) Regulations for core investment companies to smooth functioning of their businesses as well as to give confidence to the participants as well as operators.

In a very broad sense, NBFIs would include even financial institutions like insurance companies, Life insurance Corporation of India, Unit Trust of India, Industrial Credit and Investment Corporation of India Ltd., Industrial Finance Corporation of India and Industrial Reconstruction Corporation of India Ltd., as also State Financial Corporations. But for the purpose of our present study, the scope of the term is confined to the types of financial companies enumerated in clause (p) of paragraph 2(1) of the Non-Banking Financial Companies (Reserve Bank) Directions, 1966, which mobilize savings of the community by way of deposits or otherwise and utilize them for the purpose of lending or investment. Thus the NBFCs that we shall discuss here are hire-purchase finance, housing finance, investment, loan, miscellaneous financial or mutual benefit financial companies but excluding insurance, stock exchange or stock broking companies. Non-banking financial companies (NBFCs) encompass an extremely heterogeneous

group of intermediaries. They differ in various attributes, such as, size, nature of

incorporation and regulation, as well as the basic functionality of financial intermediation. Notwithstanding their diversity, NBFCs are characterised by their ability to provide *niche* financial services in the Indian economy. Because of their relative organisational flexibility leading to a better response mechanism, they are often able to provide tailor-made services relatively faster than banks and financial institutions.

II. REVIEW LITERATURE

In this chapter an attempt has been made to analyse the various studieson different views of banking industry related to the present study. Anumber of studies have been carried out on different aspects of customerservices by the researchers, economists and academicians of Indians andabroad. Some of the important studies conducted on customers services ofbanking sector are reviewed here. The reviews keep the researcher toidentify the research gap and formulate a better analysis.

Zeithmal et al., (1990)1 analysed profitability positions of banks andgrowth of client base are interlinked. With intensifying competition in themarket, it is very important for the banks to understand “How customerschoose their banks?”. Then only banks can take proper marketing efforts toincrease client base. Improper identification of true determinants ofconsumers‟ bank selection decision may result in poor results for marketingefforts. Management‟ s failure to identify customers‟ desire is one kind ofquality gap.

Gerrard and Cunningham (2001)2 in their study, conducted inSingapore, investigates three important aspects of service quality. Thesample customers of two specific banks, one of which is publicly quoted andone of which is fully government owned. For comparative purposes, five
service quality dimensions, which the authors created, were used. The resultsshowed that customer expectations about an excellent bank's service qualitywere not significantly different as between the public sector bank and thegovernment bank. The perceptions that consumers had about the servicequality of the bank they patronized, though, showed some significantdifferences. The public sector bank was perceived as having a significantlybetter 'services portfolio', specifically in regard to making customers awareof its services and offering a variety of services through its AsynchronousTransfer Mode (ATM). The government bank was perceived as havingbetter 'staff who deliver the service', specifically in the way the staff dressed
and the efficiency with which they served customers. The five servicequality dimensions were found to have better predictive capabilities for themeasurement of the overall satisfaction of customers who patronised thegovernment bank.

Hays and Hill (2001)3 in their article explained that most expertsagree that a learning organization whose employees have a clear vision ofthe importance of service quality and are motivated to provide that qualitywill achieve superior service quality. It develop a theoretical framework andconduct a cross-sectional empirical study to investigate the interrelationshipsamong these constructs. The results indicate that higher levelsof both employees‟ motivation/vision and organizational learning positivelyaffect perceived service quality. Additionally, employees‟ motivation/visionwas found to mediate the relationship between organizational learning andperceived service quality. These results highlight the importance of
employees‟ motivation/vision in both the service and the learning process.

Li et al., (2001)4 in their study found that as an international financialcenter, the banking industry in Hong Kong (HK) plays a significant role.Because of increasingly competitive pressure from domestic and overseasbanks, HK banks must tightly control cost and improve quality andefficiency of operations in order to maintain profitability. For this purpose,quality management has emerged as an effective tool in recent years. In fact,it has been regarded as a vital strategic element for meeting the challenge ofthe new and intensified competition in the financial services industry. Thispaper reports the result of a survey on quality management initiatives inHK‟ s banking industry between 1997 and 2000. The trend of changes inthese years is analyzed and the results from HK are compared with thosefrom British financial institutions. The results show that HK banks havegradually adopted quality initiatives and gained significant success in qualitymanagement over the past 3 years. They focused more on meeting servicestandard and providing prompt services while banking institutions in the UKfocused more on understanding and meeting customers‟ needs.

Newman (2001)5in his paper presents a case study of a pioneeringnationwide implementation of SERVQUAL by a major United Kingdom(UK) high street bank between 1993 and 1997 at an annual cost of onemillion pounds. In addition to highlighting serious weaknesses in the value

of SERVQUAL as a measure of service quality and as a diagnostic tool, thisstudy raises some of the practical difficulties entailed in its implementation.Moreover, in this particular instance, it becomes apparent that difficulties areintroduced by the separation of service quality management from themanagement of marketing and human resources. In addition, there was a
discernible lack of top management commitment, as well as obstacles in theform of functional and informational silos, which served to constrain anintegrated company response to SERVQUAL criteria.

Hussein A Hassan Al-Tamimi and Abdullah Al-Amiri (2003)6discussed in their article that it is generally agreed that service quality inbanking is a significant issue facing this industry. The objective of this studyis to analyse service quality in the UAE Islamic banks and to compareservice quality between the Dubai Islamic Bank and the Abu Dhabi IslamicBank. Linear regression results indicate that there was a positive andstatistically significant relationship between overall service quality and theSERVQUAL dimensions in the UAE Islamic banks. It was also found thatempathy and tangibles were the most important dimensions. Analysis of
covariance(ANOVA) results showed that there was no significant differencebetween the level of overall service quality in the Dubai Islamic Bank andthe Abu Dhabi Islamic Bank. ANOVA results also indicate that there was nosignificant difference in the level of service quality in the UAE Islamicbanks based on the customer's gender and nationality. The results indicate,however, that there was a significant difference in the level of service qualityin the UAE Islamic banks based on the customer's age, education andnumber of years with the bank.

Yonggui Wang et al., (2003)7 in their paper deals with although anincreasing number of studies is being performed in the field of servicemanagement, less work is being done on an integrated framework of servicequality and product quality, especially that supported with evidence fromdeveloping countries. As a result, little is known about the distinctionbetween service quality and product quality, their respective antecedents,and their distinctive contributions to performance in service industries in thedeveloping world. Generalization of related findings from developedcountries is not necessarily appropriate. Unlike most related studies that arebased on evidence from developed countries, focuses attention on thedistinction between, and respective antecedents of, service quality andproduct quality in the Chinese context.

Chaisomphol Chaoprasert and Elsey (2004)8 in their paperdiscussed that at the retail level, service quality is a key factor in consumersatisfaction with his or her bank. This article examines commitment to andemphasis within service quality. Despite the rapid growth in electronicbanking it was found that in Thailand the emphasis has been on improvingpersonal counter services. A model for investigating service in a retailbanking environment is set out in the article.

Charalambos Spathis et al., (2004)9 in their paper discussed theservice quality of Greek banks on the basis of their customers‟ perceptions,and analyses how gender differences affect customers‟ perceptions ofservice quality dimensions such as effectiveness and assurance, access,price, tangibles, service portfolio, and reliability. The results of an empiricalstudy of 1,260 customers of Greek banks generally support the hypothesisthat gender affects service quality perceptions and the relative importanceattached to various banking service quality

dimensions. This paper providesimportant information for bank managers to use in developing operational,human resource, and marketing strategies, and in targeting those strategies interms of the gender differences in quality perceptions among theircustomers.

Ugur Yavas et al., (2004)10 in their article examines the nature ofrelationships between service quality, background characteristics, andsatisfaction and selected behavioral outcomes by using retail banking inGermany as its setting. Study results show that service quality is at the rootof customer satisfaction and is linked to such behavioral outcomes as wordof mouth, complaint, recommending and switching. However, differentaspects of service quality and different customer characteristics seem to beassociated with different outcomes. For instance, the results suggest thattangible elements of service quality and being a female are more closelyassociated with positive word of mouth and commitment. On the other hand,"timeliness" aspects of service delivery are more closely related to customersatisfaction, and complaint and switching behaviors. Implications of theseresults to induce greater customer satisfaction, to attain higher levels offavorable outcomes and to alleviate negative outcomes are discussed.

Mohammed Al-Hawari et al., (2005)11 explained in their paper thatautomated service quality has been recognised as the factor whichdetermines the success or failure of electronic commerce. Those modelscurrently available to measure automated service quality are limited in theirfocus, encompassing only one electronic channel the internet therebyignoring attributes of the other automated service channels. In relation to thebanking sector, research has identified that bank customers tend to use acombination of automated service channels. As such, this research strives todevelop a comprehensive model of banking automated service quality taking into consideration the unique attributes of each delivery channel and otherdimensions that have a potential influence on quality issues. The proposedmodel has been empirically tested for unidimensionality, reliability, andvalidity using factor analysis.

III. FINDINGS

The above review literature shows that the most important service quality practice on customer satisfaction isresponsiveness as it is perceived as a dominant service quality. The results reveal that the service qualitydimensions of tangibles, responsiveness, reliability and assurance are positively and significantly influencing thecustomers overall satisfaction, while the empathy is negatively and significantly influencing the customers overall satisfaction. Thus, this present research concluded that service quality is the basic and also most important factor that influences the overall customer satisfaction. This finding reinforces the need for banks managers to place an emphasis on the underlying dimensions of service quality especially on responsiveness and should start with improving service quality in order to raise overall customer satisfaction. Further, this study is consistent with those of prior research in concluding that: service quality is a significant influence of overall customer satisfaction, and service quality dimensions are the basic factors that affect overall customer satisfaction. It is apparent that focusing on delivering high quality services and improve service quality effectively is critical for customer satisfaction. In addition, the satisfaction of customers was significantly

influenced by the (Tangibles, Responsiveness, Reliability and assurance). It is thus apparent that managers of new private sector banks could make assessing and monitoring service quality in banks periodically, to enable the banks to identify where improvements are needed from the customers' viewpoint and to place an emphasis on the underlying dimensions of service quality, especially on responsiveness and should start with improving service quality in order to raise overall customer satisfaction.

IV CONCLUSION

Review highlights that mediating effect of service quality of non banking financial institution plays effective role in identifying customer needs based on their socio-demographic profile, launching of various financial product according to their needs and desire with valid consent of services benefitting customers as well the financial institutions. Besides that service quality of non banking financial institution depends on digital services in order attain accuracy and reducing the time consumptions of customers. A Service provider has to be motivated and trained to achieve the target group in turn with attractive increments and incentives. On the whole service quality ultimately relies on the risk and return analysis of financial products they reap and enjoy long term satisfaction and pleasure.

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