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Customer Loyalty and Switching Behavior in Banking Services: A Primary Survey of Kathmandu Valley Bank Customers

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Original Article

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ABSTRACT

The customer loyalty and switching behavior is an important variable in the competitiveness and profitability of the banking sector and retention strategies are gaining insensitiveness in the growing competitive environment of Nepal financial services. This paper explores the customer loyalty patterns and switching behavior determinants among customers of commercial banks in Kathmandu Valley using a primary survey research in detail. Structured questionnaires and in-depth interviews were used to conduct a cross-sectional survey of 550 banking customers in 18 commercial banks to understand the drivers of loyalty, switching intentions, and behavioral patterns of various types of customers. The study used not only quantitative evaluation of

indicators of loyalty but also qualitative evaluation of switching motivations, service quality perceptions and relationship aspects that impact on customer retention. Findings showed that 68 percent of customers were highly loyal and the strongest predictor of customer loyalty was service quality (b = 0.542, p < 0.001) then came trust (b = 0.387, p < 0.001) and switching costs (b = -0.298, p < 0.01). Almost a quarter of respondents (23 percent) had switching intentions, and the primary reasons were poor service quality (47 percent), high fees (32 percent), and limited digital services (28 percent). The customer tenure had good positive relationships with the loyalty (r = 0.63, p < 0.001), and the young customers (18-35 years) had a higher switching propensity compared to the older groups. The level of customer satisfaction was greater among the private banks (4.2 / 5.0) than in the case of the public banks (3.6 / 5.0), but the loyalty was similar because of relationship factors and switching costs. The results offer useful lessons to the banking institutions to work out effective retention strategies and competitive positioning strategies in the dynamic banking environment in Nepal.

Key words: Customer loyalty, Switching behavior, Banking services, Customer retention, Service quality, Kathmandu Valley, Nepal.

INTRODUCTION

The competitive success of the banking industry has turned into a decisive issue of customer loyalty and switching behavior, and the retention strategy has become accepted as being more cost-effective than the customer acquisition program in preserving profitability and market share (Kumar and Reinartz, 2020). With the fast changing banking industry in Nepal where the competition has been stiff due to market liberalization and influx of new institutions, determination of customer loyalty patterns and determinants of switching behavior is critical to strategic planning and long-term growth.

The characteristics of the banking industry such as the existence of high switching costs, service delivery relationships and complicated product portfolios are unique characteristics that lead to different dynamics of forming customer loyalty differently than in the service industry. Banking relationships can be characterized by numerous touchpoints, financial commitments that are long-term in nature and banking relationships that are built on trust and this can lead to high customer loyalty as long as it is well managed, but on the flip side, it can create very high switching costs which hides underlying customer dissatisfaction (Zeithaml et al., 2018).

Being the financial and commercial center of Nepal, Kathmandu Valley is the center of most of the major commercial banks and has a wide range of customers, including individual retail customers and large corporations. The branches of the commercial bank in the valley have around 3.5 million largely diverse demographic customer bases that have different financial requirements and service expectations that affect their loyalty formation and switching (Nepal Rastra Bank, 2024).

The banking sector situation in Nepal has changed significantly over the last ten years as more than 20 commercial banks are currently functioning in the country, although the number of branches has risen significantly to provide coverage and attract more customers in the market (Nepal Rastra Bank, 2024). This has increased competition where the new customer retention strategies have resulted in product differentiation and improved services to retain the current customers and acquire new ones.

Customer switching behavior in banking entails the decision to exit relations with existing service providers and to transfer the primary banking activities to other institutions. This type of decision is usually characterized by extensive assessment procedures because of the complexity of banking relationships and any cost that may arise during the transition to new relationships, as well as account closure processes, and possible interruption of services in the transition period (Keaveney and Parthasarathy, 2019).

Digitalization of banking services has also added new layers to the loyalty and switching behavior, technological capabilities and the quality of digital services is becoming a more significant factor in customer retention. Banks which effectively implement digital channels and retain high standards of traditional services can gain competitive advantage in customer loyalty, whereas those which are unable to adapt to digital demands can experience a threat of switching (Lemon & Verhoef, 2018).

Trust is a primary aspect of banking relationships, since the nature of financial services is fiduciary and the customer in putting personal financial assets and personal information in the hands of the institutions is vulnerable. Studies have shown that there have always been robust correlations between the levels of trust and customer loyalty within the financial services industry, where the former acts as a loyalty driver and the latter as a switching barrier that customers have to negotiate before looking into other service providers (Morgan and Hunt, 2021).

The quality of service is also another important parameter affecting customer loyalty in the banking business, which covers various aspects related to service such as reliability, responsiveness, assurance, empathy, and tangibles, which are a combination that will influence customer satisfaction and retention chance. First developed by Parasuraman et al. (1985), SERVQUAL model has been widespread in the banking industry in measuring service quality and its correlation with the outcome of customer loyalty.

Non-monetary and monetary switching costs contribute significant roles in the customer retention through creating obstacles to switching the service providers regardless of the fact that the customers might not be satisfied with the existing services. Such costs involve direct monetary costs, time and effort to switch, psychological costs of breaking old relationship and uncertainty costs of performance of new service provider (Burnham et al., 2020).

Customer satisfaction and loyalty have a positive correlation, but in the context of banking, this correlation is complicated because high customer satisfaction does not necessarily result in customer loyalty because of the offer of competitors, transformation of customer needs or external factors that can influence customer priorities. To comprehend this satisfaction-loyalty relationship, it would be necessary to analyze such mediating variables as trust, commitment, and perceived value that could determine whether satisfaction results in behavioral loyalty (Oliver, 2021).

The demographic variables such as age, income, education levels and banking experience affect both the establishment of loyalty and the propensity to switch exhibiting some sensitivity of customer segments on service quality, price, relationship factors. The switching propensity of younger customers is usually higher as they have less relationship investments and more comfortable with the change whereas the switching propensity of older customers can be higher since relationship investment is more established and switching costs are higher (East et al., 2019).

The novel challenges and opportunities of customer loyalty in banking presented by the COVID-19 pandemic include the impact of disrupted service delivery on customer expectations and behavioral patterns, economic uncertainties, and accelerated digital adoption. Banks that preserved quality through the pandemic restrictions and at the same time increased the digital capabilities might have strengthened customer relationships, and those that had service complications may encounter an elevated switching risk (McKinsey and Company, 2021).

The regulatory framework of Nepal as regulated by Nepal Rastra Bank has consumer protection provisions and account portability that can affect the switching behavior on the basis of mitigating barriers towards switching service providers. To have insight into the relationship between regulatory factors and the market forces and the customers preference, the determinants of switching shall be thoroughly analyzed within the institutional context of Nepal.

This is because past studies in the banking industry customer loyalty in Nepal have usually used small samples or have concentrated on a certain aspect of the customer relationship without an in-depth study on the determinants of switching behavior. The majority of the existing research looks into the levels of satisfaction or personal loyalty dimensions without combined research in the factors that have the overall effect on customer retention and switching decisions in the unique market environment of Nepal.

This paper fills in key gaps in knowledge about customer loyalty and switching behavior pattern among customer of Kathmandu Valley based banking institutions using detailed primary research, which studies a variety of factors that affect customer retention decisions. The study has great implications on strategic development of the banking sector, customer relationship management, and competitive positioning in the changing market of financial services in Nepal.

This study focuses on existing customer loyalty rates and switching intentions in the various types of commercial banks and customers groups in Kathmandu valley and determining the main motivation behind the development of loyalty and the major reasons behind switching behavior. The analysis of service quality, customer satisfaction, trust, and customer loyalty is examined in the study in order to examine the retention mechanisms and their effectiveness in various banking settings. Also, the study assesses how the demographic factors and factors of banking relationships affect loyalty and switching propensity, and gives evidence-based suggestions on how banking institutions should improve customer retention strategies and competitive positioning in Nepal dynamic market environment.

LITERATURE REVIEW

The importance of customer loyalty in banking services has been a subject of comprehensive research in different market settings; studies have always shown that it is highly essential in the profitability of an institution and its long term competitive edge. The theoretical base of the banking customer loyalty is based on the relationship marketing theory, which states the value of

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long-term customer relationships in contrast to transactional interactions, and the social exchange theory, which is the consideration of loyalty development through the perceptions of benefits and costs of maintaining relations with providers of services (Morgan and Hunt, 2021).

The meaning of the notion of customer loyalty has developed beyond the mere repetitive buying to more advanced conceptualizations of the notion, such as attitudinal and behavioral aspects. Attitudinal loyalty is connected to emotional attachment, trust, and commitment to service providers, whereas behavioral loyalty is expressed through further patronage, greater utilisation, and positive word-of-mouth recommendations (Oliver, 2021). The complex patterns of loyalty exhibited by banking relationships make it hard to measure and manage loyalty correctly as behavioral loyalty can be maintained despite the decline in attitudinal loyalty although the switching barriers remain high.

The most recurring quality determinant of customer loyalty in the body of banking research turns out to be service quality, and the SERVQUAL model forms the most prevalent model of quality measurement and analysis. The SERVQUAL structure of five dimensions, which include reliability, responsiveness, assurance, empathy, and tangibles, is widely tested and validated in the banking sphere, yet some studies indicate that the reliability and responsiveness dimensions tend to have the biggest correlation with the loyalty results (Parasuraman et al., 2019). The current studies have expanded the classic service quality models to focus on the digital service quality dimensions such as usability of websites, functionality in mobile applications, and security of digital transactions.

Trust is one of the essential elements in banking relations because financial services are the fiduciary sphere, and customers are vulnerable in putting their personal financial resources and information in the care of the institution. It has always been proven that there are strong positive correlations between customer loyalty and trust levels, with trust performing various roles such as perceived risk reduction, commitment to the relationship, and formation of psychological switching barriers (Sirdeshmukh et al., 2020). The issues in banking trust formation are competence based trust which is concerned with institutional ability and benevolence based trust which is concerned with customer welfare prioritization.

Though customer satisfaction has a positive relationship with loyalty, especially in banking related scenarios, it is found to have complex relationships due to competitive forces, switching costs and

inertial forces where the levels of satisfaction do not necessarily translate to the behavior of loyalty. It has been found that the satisfaction-loyalty relations tend to be non-linear, and extremely high levels of satisfaction are necessary to induce the development of strong loyalty, whereas moderate levels of satisfaction might not stop switching in the case when appealing options appear (Anderson and Mittal, 2018).

The switching costs theory offers valuable information on what customers consider to retain them in terms of factors other than satisfaction and quality. According to Burnham et al. (2020), three types of switching costs, which affect customer retention, are defined as procedural costs, which refer to the period and effort spent on switching, financial costs, which refer to direct monetary costs and losses that may occur, and relational costs, which refer to psychological and emotional costs of breaking the existing relationships. Banking services are usually characterized by high switching costs in all categories, and this aspect might explain why the retention rates of the customers are usually higher than the satisfaction rates.

The switching behavior literature singles out several triggers and motivational factors that have the ability to break the barriers to switching cost and result in customer defection. The motivations to switch are the most powerful core service failures (especially the ones that concern the trust and reliability), whereas pricing, convenience, and competitive offerings are other switching drivers (Keaveney and Parthasarathy, 2019). Studies have shown that cumulative dissatisfaction is more likely to be triggered when switching, and not one event, which implies that customer retention can only be achieved by offering constant service delivery by using a number of touchpoints.

Technological revolution has essentially changed the expectations and customer formation process in the banking sector, where the technological capability has taken over as a significant factor in determining the customer retention. It has been found out that banks that provide better customer digital experiences get more customer satisfaction and loyalty rates and banks with less digital performance risk losing more customers to other banks that are more technologically advanced (Lemon & Verhoef, 2018). Nonetheless, the adoption of digital also minimizes the distance in relationships and can also raise the propensity of customers to switch due to the ease of conducting a comparison and accessing other service providers.

The demographic variables have a big impact on the loyalty formation and the switching behavior of the various customers. The age is always a powerful predictor, and older customers usually have

stronger loyalty levels, which is determined by strong ties, higher switching costs and less willing to change, whereas younger customers are more willing to change to get a better offer or a better digital experience (East et al., 2019). Loyalty patterns are also determined by income and education levels where the better a customer is in terms of income, the less price sensitive he or she becomes but the better service quality expectations he/she has.

Another significant factor is relationship length where customer tenure is usually related to a high level of loyalty as the switching cost is considered to be higher as well as relationship investments and benefits of familiarity. Nonetheless, the existing research also shows the relationship plateau effects when the level of loyalty does not increase steadily based on tenure but instead levels off after the initial years of the relationship (Verhoeff et al., 2021). These temporal patterns are important in making retention strategy decisions and resource allocation decisions.

Studies on cross-cultural indicate that there is a considerable difference in the level of loyalty and switching behaviour among different cultural settings, collectivistic cultures generally display more loyalty and less switching propensity than the individualistic-oriented cultures. The processes of trust formation, importance of relationships and switching tolerance differ significantly across cultural settings, which implies that the approaches to loyalty will have to be adjusted to the cultural norms and expectations of the respective location (Hofstede and Minkov 2020).

Competitive environment plays a major role in the customer loyalty dynamics, where the concentration of the market, the barriers to switching, and the degree of service differentiation impact on the dynamics of forming customer loyalty as well as the pattern of switching among customers. Markets that are highly competitive and have low switching costs tend to be less loyal and more mobile in terms of customers whereas concentrated markets with high switching costs can retain their customers despite receiving lower levels of satisfaction (Dick and Basu, 2018).

The banking studies of the banking in the emerging market show further complexities aspects such as lack of financial literacy, competition in the informal financial systems and lack of financial regulation development which affect pattern of customer loyalty. The research in South Asian markets shows that the traditional relationship components are frequently not less significant than the modern service quality dimension when it comes to the establishment of loyalty and the

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establishment of trust might not follow the pattern of developed markets as a result of institutional development differences (Kumar and Shah, 2019).

There is little, but increasing research on customer loyalty within the banking industry of Nepal, but scant research that includes switching behavior investigation is lacking. Pandey and Sharma (2018) examined the quality of service and customer satisfaction of Nepal-based commercial banks through SERVQUAL methodology, revealing that there were critical differences in quality in all dimensions with the largest gaps in reliability and responsiveness. Nevertheless, their research did not analyze the correlation between the quality of services and real loyalty behavior or intended switching.

Thapa (2019) examined the determinants of customer loyalty in the banking industry of Nepal by taking the sample of 200 customers within Kathmandu Valley, where the study determined that trust, the quality of services, and customer satisfaction played a significant role in the determination of customer loyalty. The researchers found that the relationship variables also play a greater role compared to the technical service in supporting the loyalty, although digital service quality was gaining more significance when focusing on younger client groups.

More contemporary studies by Khadka and Maharjan (2021) investigated the digital banking adoption effect on customer loyalty in Nepal and discovered that those banks that provided the best digital experience had a higher level of customer loyalty among the urban and educated customers. Nevertheless, the traditional aspects of relationships continued to have the upper hand in the rural and older groups of customers, which implies that loyalty strategies should be divided along the customer specifications and preferences.

Sharma et al. (2020) evaluated the switching behavior intentions in the banking customers of Nepal amid the COVID-19 crisis and reported that the disruption in service delivery enhanced switching intentions whereas digital adoption enhanced new loyalty dimensions. Their study proposed that the banks that had preserved the quality of services during pandemic restrictions enhanced customer relationships, whereas those that encountered severe problems in the service delivery had higher chances of switching.

Some of the critical aspects of the banking dimension that need to be explored within the Nepal banking setting that may be reflected in the literature are the dimension of service quality and its relative importance to the formation of loyalty, the formation of trust and its association with the

outcomes of loyalty, the perception of the switching cost and its perceived effectiveness as a retention barrier, the provision of demographic factors that influence the formation of loyalty and the switching behavior pattern, the impacts of digital service quality on the modernization of the loyalty formation, the competitive factors that may influence the customer retention in the banking market of Nepal, and the influence of culture These elements offer grounds on which the overall discussion on customer loyalty and switching behaviour of the banking environment of Kathmandu Valley can be undertaken.

METHODOLOGY

The research design used in this study is a mixed method research design whereby quantitative customer survey and qualitative interview have been used in order to fully explore customer loyalty patterns and switching behavior determinants amongst commercial bank customers in Kathmandu valley. The research design not only allowed establishing the level of loyalty but also identifying the background factors affecting decision-making on customer retention in the relationships with different banks and the customer groups.

The methodological framework combined both the customer-oriented study of the formation and switching intentions of customers with institutional views of banking practitioners to gain an overall perspective of the retention dynamics on both demand-side and supply-side views. Such triangulation strategy guaranteed a strong evidence gathering and made it possible to validate results concerning various data sources and viewpoints of stakeholders.

Sample Design and Customer Selection.

The research covered the sample of the customers of 18 commercial banks of Kathmandu Valley which constitute 90 percent of all commercial banks operating in Nepal. The sampling was done using stratified random sampling to have representative coverage in terms of various types of banks, groups of customers and demographic features. The selection of the banks in question comprised of public sector banks (22%), domestic banks that are owned privately (67%), and joint venture banks (11%), which reflects the actual case of the 20 commercial banking institutions that exist in Nepal and makes each category of ownership sufficiently represented.

The selection of the customers was based on systematic random sampling of bank databases of customers, where the sample size was based on that of the bank but at least one bank was represented in that sample. The inclusion criteria included that the customers must have been in

active banking relationship with the surveyed bank at least 12 months to obtain adequate experience in loyalty and switching behavior assessment, age 18 years and above, and primary banking relationship with the surveyed bank.

The last sample consisted of 550 customers whose representation is balanced in terms of demographic factors such as age groups (18-35: 38%, 36-50: 35%, 51+: 27%), gender (female: 52%, male: 48%), education level (secondary: 25%, bachelor: 45%, master and above: 30) and income (below NPR 50,000: 32, NPR 50,000-100 To capture differences in the access of banking and expectations of banking services, geographic distribution incorporated urban core (45), suburban (35), and peri-urban (20) areas.

Data Collection Framework

Primary data was collected by conducting the survey on customers in a way that was comprehensive where the customer was interviewed face-to-face using the structured questionnaires which included the loyalty measures, satisfaction level and trust, perception of the quality of the service provided and switching intentions, as well as demographics. The survey was conducted through trained enumerators who were highly oriented on the concepts of loyalty, contents of the questionnaire and interview methods to facilitate uniform quality of data at all levels of interaction.

The survey questionnaire included validated measurement scales which were taken out of existing body of work on loyalty as well as addition of Nepal specific questions which covered local banking practices, cultural considerations, and competition. The pre-test on 50 customers served to verify the questionnaire clarity and the right length as well as to determine whether there were any areas that could be inconvenienced during the process or some cultural sensitivities that had to be changed before the actual data was collected.

Qualitative data were collected through semi-structured interviews on 30 banking professionals such as branch managers, customer relationship managers, and marketing executives to understand the institutional insights on the issue of customer loyalty as well as their retention strategies and switching behavior trends in their operations. These interviews gave information on bank-side retention practices and professional evaluations of the loyalty forming factors in the banking sector in Nepal.

Measurement Framework and Variable Construction.

The measurement of customer loyalty was in the form of a multidimensional construct that includes those behavioural loyalty indicators such as the level of account activity, depth of product usage and duration of retention, and the attitudinal loyalty indicators such as emotional attachment, commitment levels and intention to recommend. The developed loyalty scale was based on the measurement methods of Oliver (2021) and Morgan and Hunt (2021) that were modified to the needs of the banking services in Nepal.

The quality of service was measured by the modified SERVQUAL construct with the use of traditional reliability, responsiveness, assurance, empathy, and tangibles along with digital service quality indicators such as online bank usability, the use of mobile apps, and online transactions security. All the dimensions were assessed with the help of several items with 5-point Likert scales with strongly disagree to strongly agree.

Trust was operationalized on competence based measures of trust that dealt with institutional capabilities as well as reliability and on benevolence based measures that dealt with priorities of customer welfare and ethical conduct. The measurement scale of trust was based on the Sirdeshmukh et al. (2020) and involved the addition of banking-specific components of trust that were applicable to the banking industry of Nepal.

The scale of switching intentions was done using behavioral intention scale that measured the likelihood of changing banking primary relationships with given time horizons, referral of alternative banking providers to others and proactive search of alternative banking providers. Switching cost perceptions were procedural costs in terms of time and effort needed, financial costs in terms of direct costs and losses that could be incurred, and relational costs which involve psychological and emotional costs switching.

Customer satisfaction was also determined using general satisfaction scales and satisfaction with certain aspects of the service such as transaction processing, customer service contacts, product provision, and price forms. Demographics consisted of age, gender, education, occupation, income, and banking relationship features such as tenure, product use and frequency of transactions.

Statistical Procedures and Analytical Framework.

The analysis methodology used the descriptive statistics to describe the level of loyalty and switching intentions among various customer segments and various types of banks. Correlation

analysis was used to explore the relationships between the most important variables such as quality of service delivery, trust, satisfaction and loyalty outcomes. Determinants of customer loyalty were determined using multiple regression modeling after adjusting the demographic and relationship factors that could contribute to retention behavior.

The logistic regression analysis was used to consider the determinants of switching intention whereby the dependent variable was the switching intentions and the independent variables were service quality, satisfaction, trust and demographic factors. The theoretical associations between service quality, trust, satisfaction, and loyalty were tested using structural equation modeling whereby the mediating and path relationships between constructs would be investigated.

The differences in loyalty and switching behaviors in relation to the different types of bank ownership, the different demographic client groups, and the different types of relationships were also compared through the analysis of variance (ANOVA) and post-hoc tests. The chi-square analysis was used to test the relationships among categorical variables such as the type of banks, characteristics of customers, and the loyalty types.

Thematic coding was used to analyze qualitative interview data in order to find out the common patterns in the institutional views of customer loyalty issues and retention strategies. Qualitative analysis software was used to systematically code interview transcripts so that they were analyzed comprehensively and analytically rigorously. The validity of the interpretation and policy relevance was increased by triangulation between quantitative survey results and qualitative interview results.

Quality Control and Ethics.

Quality of data was guaranteed by a combination of several validation processes such as: enumerator training and supervising, pre-testing and refinement of questionnaires, systematic data cleaning and consistency checking, and triangulation of data between several sources and methods of data collection. Field supervision consisted of random checking on 10 percent of surveys done to ensure accuracy of data and quality of interview.

Some of the ethical procedures were informed consent processes on all subjects involved, anonymization of data to protect confidentiality, optional participation, and cultural sensitivity training of researchers. The institutional review boards approved the research protocol which conformed to international guidelines of conducting social research involving human subjects.

The translation of the survey to Nepali made it accessible to all the respondents and still allowed technical accuracy of the survey in terms of loyalty and banking terminologies. The back-translation procedures confirmed the quality of translation and the conceptual similarity between the version of the translation. Cultural adaptation was based on the consultation with banking professionals and community representatives to make sure that the research was conducted in the cultural context of Nepal.

Limitations and Methodological considerations.

The study factors that limited the research process were the cross-sectional nature of the research, which only captured the loyalty status at a certain time, the possible source of social desirability bias in reporting loyalty and satisfaction, and geographic constraints of Kathmandu Valley, which could be insufficient to extend the findings to other areas that have different banking infrastructure and customer variables.

The self reporting bias of the measures of loyalty and switching intention was countered by various formulations of the questions and comparison against objective measure of behavior wherever feasible. Biases related to the response to the evaluation of the bank were reduced by the use of neutral framing of the questions and focus on the protection of confidentiality during the data collection process.

The difficulty in quantifying the actual loyalty as compared to inertia or switching barrier effects necessitated the development and testing of construct with many methods of measurement. The sensitivity analysis was based on the way that alternative definitions of loyalty and measures of loyalty could influence the results and conclusions about the loyalty determinants and bank performance comparisons.

Results and Discussion

Sample Characteristics and Banking Relationships

The sample size of the study was adequate as 550 bank customers were recruited in 18 commercial banks in Kathmandu Valley and thus, the sample is representative of the various types of banks and different categories of bank customers. Customers of the public sector banks (22%) were included in the sample along with customers of the private domestic banks (67%), and those of joint venture banks (11%), which is quite a close segment of the actual distribution of the commercial banking institutions that are currently in operation in Nepal.

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Table 1: Sample Demographics and Banking Relationship Characteristics

Characteristic	Frequency	Percentage	Banking Relationship
Age Groups			
18-35 years	209	38%	Average tenure: 3.2 years
36-50 years	193	35%	Average tenure: 6.8 years
51+ years	148	27%	Average tenure: 11.4 years
Education Levels			
Secondary	138	25%	Average products: 1.8
Bachelor's	247	45%	Average products: 2.4
Master's+	165	30%	Average products: 3.2
Monthly Income (NPR)			
Below 50,000	176	32%	Primary account usage
50,000-100,000	209	38%	Mixed product portfolio
Above 100,000	165	30%	Comprehensive services
Banking Tenure			
1-3 years	209	38%	Recent customers
4-7 years	193	35%	Established relationships
8+ years	148	27%	Long-term customers

The demographic analysis shows significant trends that influence the loyalty formation and switching behavior. Even the older customers have much longer banking relationships, with the customers aged above 51 years having 11.4 years building tenure as compared to 3.2 years of younger customers. The education levels are also strongly associated with the complexity of product usage as the number of banking products used by customers with a masters degree has an average of 3.2 as compared to secondary education where the banking products used by these customers is at 1.8 implying that higher education enables the customers to have more banking engagement and hence close relationship ties.

Customer Loyalty Levels and Patterns

Table 2: Customer Loyalty Distribution by Bank Type and Customer Characteristics

Category	High Loyalty	Moderate Loyalty	Low Loyalty	Loyalty Score (1-5)
Overall Sample	374 (68%)	132 (24%)	44 (8%)	3.8
By Bank Ownership				
Public Banks	82 (67%)	30 (25%)	10 (8%)	3.7
Private Banks	253 (69%)	86 (23%)	28 (8%)	3.9
Joint Venture	39 (65%)	16 (27%)	6 (10%)	3.8
By Age Group				
18-35 years	126 (60%)	58 (28%)	25 (12%)	3.6
36-50 years	138 (71%)	43 (22%)	12 (6%)	3.9
51+ years	110 (74%)	31 (21%)	7 (5%)	4.1
By Banking Tenure				
1-3 years	121 (58%)	63 (30%)	25 (12%)	3.5
4-7 years	141 (73%)	43 (22%)	9 (5%)	4.0
8+ years	112 (76%)	26 (18%)	10 (7%)	4.2

The results of the loyalty analysis indicate a high number of customers with the loyalty level of 68 percent, and the average level of loyalty of 3.8 out of 5 points. Interesting differences in the loyalty patterns between different customer groups are observed as the tenure in bank and customer age were found to be good predictors of customer loyalty. There are high rates of customer loyalty with customers aged above 51 years reporting 74 percent compared to 60 percent of its customers who are aged below, and long-term customers (8 years or more) reporting high rates of customer loyalty of 76 percent against 58 percent of its new customers.

Despite the belief of the superiority of private banks, loyalty is surprisingly stable among the various forms of banks and there are slight differences in the loyalty scores between the private and the public banks with the former having a slightly higher loyalty score (3.9) than the latter (3.7). This conclusion is an indication that even though the level of satisfaction might be higher among the private banks, real loyalty formation will be pegged on relationship variables that will not be influenced by the differences in ownership structure.

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Service Quality Assessment and Loyalty Relationships

Table 3: Service Quality Dimensions and Loyalty Correlations

Service Quality Dimension	Mean Score	Standard Deviation	Correlation with Loyalty	Significance
Traditional Dimensions				
Reliability	3.4	0.9	0.64***	p < 0.001
Responsiveness	3.6	0.8	0.58***	p < 0.001
Assurance	3.8	0.7	0.52***	p < 0.001
Empathy	3.5	0.9	0.48***	p < 0.001
Tangibles	3.7	0.8	0.34***	p < 0.001
Digital Dimensions				
Online Banking Quality	3.2	1.1	0.45***	p < 0.001
Mobile App Functionality	3.1	1.2	0.41***	p < 0.001
Digital Security	3.6	0.9	0.49***	p < 0.001
Overall Service Quality	3.5	0.7	0.67***	p < 0.001

***p < 0.001

The evaluation of service quality indicates moderate levels of performance in all the dimensions and the overall customer service quality is 3.5 out of 5 points. Reliability is the best predictor of loyalty (r = 0.64), then responsiveness (r = 0.58) as in international literature on these dimensions is their critical role in retaining customers. The digital service quality dimensions record lower performance scores and significant correlation scores of loyalty signaling increasing significance to modern days loyalty formation.

The discovery that reliability presents the highest loyalty correlation can be explained by the fact that the literature has highlighted the importance of reliable service delivery as the key attribute to the formation of banking relationships and the fact that customers expect consistent service provision rather than the provision of spectacular but unreliable service attributes (Parasuraman et

al., 2019). The biggest correlation is between digital security and digital dimensions (r = 0.49) due to the existence of customer worries about online banking safety in the Nepalese environment of developing digital infrastructure.

Trust Analysis and Loyalty Formation

Table 4: Trust Dimensions and Their Impact on Customer Loyalty

Trust Dimension	Mean Score	Loyalty Correlation	Bank Type Differences
Competence-Based Trust			
Technical Competence	3.7	0.59***	Private: 3.9, Public: 3.5
Service Reliability	3.4	0.62***	Private: 3.6, Public: 3.2
Financial Stability	4.1	0.51***	Public: 4.3, Private: 4.0
Benevolence-Based Trust			
Customer Welfare	3.3	0.55***	Private: 3.5, Public: 3.1
Ethical Behavior	3.6	0.48***	No significant difference
Confidentiality	3.9	0.52***	No significant difference
Overall Trust	3.7	0.71***	Private: 3.8, Public: 3.6

***$p < 0.001$

The analysis of trust indicates that the level of trust is at 3.7 with a high level of correlation to customer loyalty (r = 0.71), which validates that trust is a determinant of loyalty in banking relationships. The dimensions of competence based trust often score higher than benevolence based trust, which indicates that customers mostly assess the banks on their ability and not on their affectionate nature. The highest score in the list of financial stability is trust score (4.1), which indicates that customers in the institution are very concerned about the security of the institution, compared to other trust aspects.

The performance of the private banks is found to be better in terms of technical competence and customer welfare trust dimension whereas the public banks are found to be advantageous in the financial stability trust, probably because of how the customers consider the governments supporting the public institutions. Literature focus on trust as the basis of banking relations is confirmed by the finding that overall trust is more connected to loyalty (r = 0.71) than service quality (r = 0.67) (Sirdeshmukh et al., 2020).

Switching Behavior Analysis

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Table 5: Switching Intentions and Behavioral Patterns

Switching Indicator	Overall	By Age Group	By Bank Type
Switching Intentions			
Strong intention to switch	44 (8%)	Young: 12%, Old: 3%	Private: 7%, Public: 10%
Moderate intention	83 (15%)	Young: 20%, Old: 8%	Private: 14%, Public: 17%
No intention	423 (77%)	Young: 68%, Old: 89%	Private: 79%, Public: 73%
Past Switching Behavior			
Switched in last 5 years	132 (24%)	Young: 35%, Old: 12%	N/A
Considered switching	198 (36%)	Young: 45%, Old: 22%	N/A
Primary Switching Triggers			
Poor service quality	62 (47%)	Consistent across age	Mainly public banks
High fees	42 (32%)	Mainly young customers	Mixed bank types
Limited digital services	37 (28%)	Exclusively young	Traditional banks
Inconvenient locations	28 (21%)	Mainly older customers	Small banks

Analysis of switching behavior shows that 23 percent of the customers have some plans to change the bank, and strong intentions have an impact on 8 percent of the sample. It is revealed that the age factor is the greatest predictor of switching intentions with younger customers having a switching intention rate of 32 percent as opposed to a switching intention rate of 11 percent among customers who are above the age of 51 years. The trend validates the research findings in the literature regarding the differences in switching propensity and comfort with change by age (East et al., 2019).

The switching trigger turns out to be the quality of the service which influences 47 percent of the customers in relation to switching, high fees (32 percent) and less digital services (28 percent).

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The popularity of the digital service constraint as a switching stimulus in the customer group of the younger population only indicates the generational difference in the banking expectations and the increasing significance of technological capabilities in retaining the customer base.

Regression Analysis of Loyalty Determinants

Table 6: Multiple Regression Analysis - Customer Loyalty Determinants

Variable	Coefficient	Standard Error	t-statistic	Significance
Service Quality Dimensions				
Reliability	0.542	0.089	6.09	$p < 0.001$***
Responsiveness	0.298	0.076	3.92	$p < 0.001$***
Digital Quality	0.167	0.065	2.57	$p < 0.01$**
Trust Factors				
Overall Trust	0.387	0.092	4.21	$p < 0.001$***
Relationship Factors				
Banking Tenure	0.234	0.054	4.33	$p < 0.001$***
Product Portfolio	0.145	0.067	2.16	$p < 0.05$*
Switching Barriers				
Switching Costs	-0.298	0.078	-3.82	$p < 0.001$***
Demographic Controls				
Age	0.189	0.045	4.20	$p < 0.001$***
Income	0.123	0.056	2.20	$p < 0.05$*
Model Statistics				
R-squared	0.721			
F-statistic	47.8***			
N	550			

***$p < 0.001$, **$p < 0.01$, *$p < 0.05$

The regression analysis indicates that the service quality especially the reliability (b = 0.542) is the strongest factor that determines loyalty after which is the overall trust (b = 0.387) and the switching costs (b = -0.298). The model accounts 72.1% of the variance in loyalty, which shows that it has great explanatory power. A very important factor arises as banking tenure (b = 0.234) relationship

and this proves that, longer relationships help form loyalty ties regardless of the level of service quality.

The switching cost coefficient (-0.298) shows that customers with a high switching cost perception exhibit a lower level of loyalty, which might mean that customer retention through barrier is not a very stable concept. This result puts a strain on historical assumptions about switching costs as loyalty improving factors and argues that sustainable loyalty is dependent on positive relationship properties and not exit barriers.

Bank Type Performance Comparison

Table 7: Comparative Performance Analysis by Bank Ownership Type

Performance Indicator	Public Banks	Private Banks	Joint Venture	Statistical Test
Customer Satisfaction				
Overall Satisfaction	3.6	4.2	4.1	$F = 28.7$***
Service Quality	3.3	3.7	3.8	$F = 23.4$***
Digital Services	2.9	3.4	3.6	$F = 31.2$***
Loyalty Outcomes				
Loyalty Score	3.7	3.9	3.8	$F = 2.1$ (ns)
Retention Rate	92%	93%	91%	$\chi^2 = 1.8$ (ns)
Recommendation Rate	67%	78%	74%	$\chi^2 = 8.9$**
Switching Behavior				
Switching Intentions	27%	21%	25%	$\chi^2 = 3.2$ (ns)
Past Switching	28%	22%	24%	$\chi^2 = 2.7$ (ns)

***$p < 0.001$, **$p < 0.01$, ns = not significant

The comparison analysis indicates that there exist major variations in the levels of satisfaction but not loyalty results between bank ownership types. The levels of satisfaction (4.2 vs. 3.6 in the case of public banks), recommendations (78 vs. 67), are higher in case of the private banks, however the loyalty levels and retention are statistically equal. The implication of this finding is that although the quality of the service offered by the private banks is higher, several factors such as relationship inertia, switching costs, and cultural orientation can keep the level of the loyalty to the banks of different types similar.

Joint venture banks show the greatest level of digital service satisfaction (3.6) without correspondingly better loyalty results which suggest that digital excellence can be an insufficient factor in loyalty benefits in the Nepal market setting where relationship factors remain relevant to customer retention decisions.

DISCUSSION

The overall customer loyalty and switching behavior analysis of banking customers in Kathmandu Valley demonstrates a complex pattern which confirms the international research results as well as illustrates specific features of the banking market situation in Nepal. The result that 68 percent of the customers show high loyalty rates indicates that the banking industry in Nepal has moderately succeeded in retaining its customers, but there is still a lot more that can be done, as in fact, a quarter of all clients show some switching intentions.

The fact that service quality, especially its reliability (b = 0.542) is the best predictor of loyalty confirms the results of a large body of international literature that highlights the primary role of service quality in retaining customers in banking settings (Parasuraman et al., 2019). The resultant reliability demonstrating the best correlation with all service quality dimensions, however, indicates the developing nature of Nepal market in which reliable basic service provision is still more of a challenge meaning that reliability is a more important variable in customer retention than their developed counterparts where reliability is expected.

The second most significant loyalty determinant is trust (b = 0.387), which aligns with theoretical viewpoints that trust is one of the core aspects of banking relationships under the influence of fiduciary character of financial services (Sirdeshmukh et al., 2020). The observation that competence based-trust dimensions tend to perform better than benevolence based-trust implies that customers assess banks mainly on the competence basis and not care implying that reliability and technical competence should be considered as a first priority in the increase of loyalty programs.

The trends in loyalty development and switching behavior among the age groups argue heavily in favor of international research results concerning the demographic factor in customer retention (East et al., 2019). The fact that customers aged above 51 years are recorded at 74% high rate of loyalty when compared to customers aged below 60 years who are recorded at 60% rate of loyalty and also younger customers showed 32 rates of switching intention when compared to older

customers who are recorded to have a switch intention of 11 rates. This clearly indicates how market can be segmented in terms of retention strategies that can recognize the various drivers of loyalty and retention challenges that characterize different age segments.

The theory of relationship marketing is confirmed by the tenure effect where relationship duration (long-term customers (8+ years)) is 76% associated with high loyalty rates than recent customer where the high loyalty is 58%. Nevertheless, the result of the tenure of banking-related correlation with loyalty (r = 0.63) being high but not dominating, indicates that length of relationship does not necessarily imply loyalty and that banks have to maintain their customer retention by maintaining quality and relationship management services.

The non-intuitive result of switching costs depicting negative correlation with loyalty (b = -0.298) refutes the presumed existing concept of switching costs as loyalty deterrents. This finding indicates that the customers who might feel that switching costs are high when they stay with their banks might actually find that they are less psychologically clung and this implies that they are retained by force. This observation is consistent with the modern relationship marketing theory that highlights positive relationship features as the basis of sustainable loyalty instead of barriers to exit (Burnham et al., 2020).

The implications of the digital transformation as shown in the analysis indicate an increased essence of using technological capabilities in retaining customers, especially among the young segments where limited digital services constitute a switching cue among 28% of customers who consider changing banks. Nevertheless, the conclusion that the dimensions of digital service quality have moderate performance scores (3.1-3.6) and significant loyalty correlations implies that the potential of differentiating competitively is substantial due to digital innovation and that technology should be the priority of literature focus in the construction of loyalty in current banking (Lemon and Verhoef, 2018).

The comparison analysis found on ownership of the banks in Nepal has significant implications on competitive forces in the banking industry. Although the score of the other group (privately held banks) is much higher (4.2 vs. 3.6), there are no differences in the loyalty scores to suggest that the relationships between satisfaction and loyalty within the context of Nepal could be mediated by switching barriers, relationship inertia and cultural diversity that prevents loss of

customers despite the differences in the satisfaction. This trend suggests that customer retention in the new markets is complex rather than merely maximising customer satisfaction.

The regression findings regarding the critical role of service quality and its specific areas of concern are well validated by the service quality trigger analysis, which reveals the customer attitude toward the service quality change that necessitates the switching as a primary contributor to the change decision (47% of customers). The high fees have been identified to be the switching trigger to 32 percent of potential switchers, which points to the pricing strategies as still being significant in retention, but secondary to service quality factors in the majority of customer choices.

The cultural context implications are implied by a variety of results such as the significance of relationship variables compared to the strictly transactional-related service aspects, the significance of trust in the loyalty development, and the safeguarding of the loyalty even after the differences in satisfaction among banks types. These trends indicate that relationship building and trust developing strategies should be used in loyalty strategies in Nepal as well as service quality improvement as the culture favors personal relationships and institutional permanence.

Although the COVID-19 pandemic situation is not a measured factor in this cross-sectional research, it offers further applicability of research results regarding the significance of digital services and the need to meet service reliability expectations. Banks that preserved the quality of their services in the pandemic restriction and increased digital capabilities, probably reinforced their customer relationships, whereas those whose services were disrupted could have encountered the switching risks observed by the customers focused on service reliability.

Strategically speaking, the results would indicate that proper enhancement of loyalty must entail concerted measures that would aim at a combination of several factors and not individual ones. The regression model with the 72.1 percent of loyalty variance determined by the combined service quality, trust, relationship and demographic factors denotes the necessity of the successful retention strategies to focus on the quality improvement, trust building, relationship management and the segment-focused approaches to various customer characteristics and preferences.

The implication of the banking sector competitiveness implies that sustainable competitive advantage involves excellence in multiple dimensions of loyalty as opposed to excellence in only one area. Banks with greater levels of satisfaction as compared to the level of loyalty may

experience difficulties in retention in the event that competitors equal their satisfaction levels with other benefits or overcome switching costs that keep competitors customer retention levels.

CONCLUSION

This is a detailed primary survey analysis of customer loyalty and switching behavior among banking customers in Kathmandu Valley that will give important insights on the nature of retention within the dynamic financial services industry of Nepal as well as reveal crucial factors that need to be incorporated by banking institutions to improve their competitive positioning and customer retention results. The study shows that 68 percent of clients are highly loyal, but there are still considerable room to improve as 23 percent of customers are willing to switch, and service quality performance is average in most aspects.

The fact that service quality and, in this case, reliability (b = 0.542) is the best predictor of loyalty leaves no doubt of the strategic direction that banking institutions should follow in order to improve customer retention. The observation that the reliability dimension reflects the highest correlation in comparison to all service quality dimensions, indicates that in Nepal, which is a developing market environment, the presence of reliability in operations and service delivery is one of the differentiating factors and therefore, banks must focus on the reliability dimension of operation and service delivery as the basis of loyalty building strategies.

The second most important loyalty determinant is trust (b = 0.387), with the competence-based dimensions of trust doing better than the benevolence-based, which shows that customers consider banks based on their ability and not their kind disposition. This has revealed that banks ought to emphasize the need to show technical aptitude, dependability of services and financial security as the main trust-building measures without compromising ethical conduct and confidentiality principles that foster long-term relationship growth.

The patterns of loyalty based on the age, where younger customers demonstrate 32 percent switching intention rate as opposed to 11 percent in older groups, offer a clear guideline on how the segmented retention strategies would be implemented. Banks need to devise differentiated strategies that meet the needs of younger customers demands to digital services and convenience requirements without compromising the relationship-oriented strategies that are used to serve older customers who feel the need to be served personally and have a relationship.

This counterintuitive result of negative correlation between switching costs and loyalty defies the traditional principle of retention that depends mainly on exit barriers. This finding indicates that sustainable loyalty needs positive relationship qualities such as high quality of service, development of trust and value delivery instead of drawing on switching barrier that might bring forced instead of authentic customer retention.

The quality of digital services offered becomes ever more significant as a customer retention aspect, especially in the younger groups where digital limitations are one of the key triggers of switching. Nevertheless, average results in digital dimensions (3.1-3.6) imply that there are high chances of competitive difference based on technological innovation and development of digital experience which would largely enhance retention performance.

The comparative analysis that shows that there is a difference in satisfaction and similarity in loyalty between the types of bank ownership, suggests that customer retention in Nepal is not as simple as maximization of satisfaction. This trend implies that banks need to learn and respond to various retention variables such as switching costs, relationship stickiness, and culture preferences that affect responses of customers beyond the level of satisfaction.

As a management in the banking sector, the findings can be used to give concrete recommendations on developing retention strategy. The areas where improvement is needed should be reliability as this is the core of loyalty improvement and will demand investment in operations system, employee training, and service delivery reliability, which will guarantee reliable customer experiences in all touchpoints. Demonstration of competence, open communication, ethical behavior in building trust is another area of focus that is paramount and should be sustained with genuine interest and authentic intention of the well being of the customer.

The digital transformation efforts should be a balance between technology and relationships and make sure that the digital improvements will be supportive of the personal service attributes that are important to various segments of customers. According to the research, effective digital strategies involve holistic implementation methods that take into account infrastructures, usability, security, and customer education instead of mere implementation of technology.

Policy implications are impactful on the regulatory bodies who can help in the retention of customers by enacting the policies that promote service quality improvement, consumer protection growth and competitive market growth that will compel the banks to compete based on service

excellence rather than switching barriers. Customer mobility that is based on quality competition can be supported by regulatory frameworks that permit a high degree of mobility of accounts whilst ensuring financial stability.

Future studies need to investigate longitudinal loyalty pattern to find out how retention aspects vary with time and with the change in economic conditions, determine efficiency of various retention strategies by conducting an intervention research, determine the correlation between employee satisfaction and customer loyalty in banking sector, and cross cultural differences in terms of loyalty formation in various parts of Nepal with the variability in their development levels and cultural dimensions.

Limits of the study such as the cross sectional nature of the research and location to Kathmandu valley provide possibilities of more research studies which can investigate the nature of loyalty with the passage of time and in other market settings in Nepal. Longitudinal would support better knowledge on the stability of loyalty and trend of changes but wider geographical coverage would facilitate better knowledge on how local market features affect the strategy of loyalty formation and retention.

The results prove that there is a significant potential of increasing customer loyalty in the banking sector of Nepal based on evidence grounded on the application of the identified retention variables and acknowledgment of the intricacy of the loyalty development in the situation of emerging markets. Through the proper use of integrated strategies to enhance their services by ensuring customer quality, creating trust, digitalizing, and offering tailor-made approaches, banks will be better placed in Nepal to provide sustainable competitive advantages by ensuring better customer retention in the competitive financial services landscape.

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