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Service Profit Chain Relation in Commercial Banks: A Study in Kathmandu Valley

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Abstract

Purpose: *The service profit chain (SPC) is an important framework in the banking sector that explains the relationship between internal service quality, employee satisfaction, customer satisfaction, and profitability. This study examines SPC relationships in commercial banks of Kathmandu Valley.*

Methods: *An explanatory research design was adopted using purposive sampling. Data were collected from 384 employees of commercial banks in Kathmandu Valley. The study was grounded in Emotional Contagion Theory and analyzed using descriptive statistics, inferential statistics, and Structural Equation Modeling (SEM).*

Results: *Findings revealed that job design, training and development, rewards and recognition, and tools for serving customers significantly influenced employee satisfaction, while workplace design was insignificant. Employee satisfaction strongly affected customer satisfaction, which in turn significantly enhanced profitability. The model confirmed sequential mediation and supported the applicability of SPC in Nepal's banking sector.*

Conclusions: *The study concludes that strong internal service quality increases employee satisfaction and productivity, leading to greater customer satisfaction and improved profitability in commercial banks.*

Keywords: Emotional contagion theory, Kathmandu valley, commercial banks, employees, Structural equation modeling.

JEL Classification: A23, G21, J54

I. Introduction

The Service-Profit Chain (SPC) is a widely recognized framework in service management literature that emphasizes the critical role of both internal and external service quality in determining organizational performance and financial success (Benjarongrat & Neal, 2017). Initially proposed by Heskett et al. (1994), the SPC framework has gained substantial scholarly attention for explaining the interrelationship among key service-related variables, including employee satisfaction, customer satisfaction, customer loyalty, and organizational profitability (Ansari, 2021). The model primarily incorporates three interconnected dimensions:

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internal marketing, which focuses on internal service quality and employee attitudes; external marketing, which concerns service delivery and customer perceptions; and organizational performance, represented through revenue growth, profitability, and market performance indicators (Hogreve et al., 2022).

In developing economies, the service sector has become increasingly competitive due to globalization, technological advancement, and rising customer expectations. Under such conditions, service quality serves as a crucial strategic differentiator that enhances customer retention, organizational sustainability, and profitability (Adeinat & Kassim, 2019). This is particularly relevant in the banking industry, where service quality has evolved into a fundamental source of competitive advantage and long-term organizational success (Auka, 2012). The SPC framework enables organizations to establish a customer-oriented culture by aligning employee performance, service delivery, and organizational objectives toward achieving superior customer experiences and financial outcomes.

Employee behavior constitutes a central component of the SPC framework because motivated, empowered, and satisfied employees are more likely to deliver high-quality services consistently (Schiavone et al., 2022). Furthermore, organizational knowledge, human resource competencies, and operational capabilities significantly influence service excellence and market performance (Roth & Jackson, 1995). Customer satisfaction, which is strongly associated with service value created by employees, plays a vital role in promoting customer retention and loyalty. Similarly, employee loyalty contributes to stable productivity and organizational effectiveness, thereby improving overall business performance (Pratyush & Ranjan, 2016). The SPC framework illustrates a sequential relationship in which satisfied employees generate satisfied customers, ultimately leading to enhanced organizational growth and profitability. Consequently, organizations can strategically strengthen their competitive position by investing in employee welfare, specialized training, supportive work environments, and customer-focused service delivery systems. Improved service quality enhances customer satisfaction and loyalty, which subsequently contributes to increased revenue generation and long-term profitability (Abusomwan et al., 2023).

Accordingly, employee satisfaction has emerged as a critical organizational resource that directly influences employee engagement, productivity, and service performance. Organizations are therefore encouraged to foster positive work environments, regularly assess employee satisfaction, and implement continuous improvement strategies to strengthen organizational commitment and service excellence. Although the SPC framework has been extensively examined in developed economies, empirical research within the Nepalese context remains limited due to inadequate research infrastructure, insufficient organizational data, and the lack of systematic record-keeping practices concerning employee and customer attitudes in organizations (Shrestha et al., 2013).

Despite the growing importance of service quality and employee-driven performance in the banking sector, limited empirical studies in Nepal have systematically examined the complete Service-Profit Chain relationship within commercial banks. Most existing studies in Nepal have primarily focused on isolated dimensions such as customer satisfaction, service quality, or employee performance, without integrating the sequential linkage among internal service quality, employee satisfaction, customer satisfaction, and profitability. Furthermore, the increasing competition among commercial banks in Kathmandu Valley, rapid technological transformation, and changing customer expectations have created significant managerial challenges in maintaining service excellence and organizational profitability. However, there is still inadequate empirical evidence regarding how internal organizational practices influence employee attitudes and subsequently affect customer satisfaction and financial outcomes in the Nepalese banking context. This creates a significant research gap in understanding whether the SPC model, widely validated in developed economies, is equally applicable in Nepal's commercial banking industry. Therefore, this study aims to analyze the Service-Profit Chain relation in commercial banks of Kathmandu Valley by examining the effect of internal service quality factors on employee satisfaction and their subsequent impact on customer

satisfaction and profitability.

II. Reviews

This study is primarily grounded in the Service-Profit Chain (SPC) Theory and supported by Emotional Contagion Theory, which together provide a comprehensive explanation of how internal organizational practices translate into employee attitudes, customer experiences, and financial performance in commercial banks. The integration of these theories is particularly relevant for understanding service-driven organizations such as banks, where human interaction plays a central role in value creation.

The Service-Profit Chain Theory (Heskett et al., 1994) serves as the core theoretical foundation of this study. The theory posits a sequential relationship beginning with internal service quality, which influences employee satisfaction, productivity, and retention. In the context of this study, internal service quality is operationalized through workplace design, job design, training and development, rewards and recognition, and tools for serving customers. These factors represent the organizational inputs that shape employees' work environment and experiences. According to SPC logic, improvements in these internal dimensions enhance employee satisfaction, which subsequently leads to higher levels of service quality delivered to customers. Satisfied employees are more motivated, efficient, and consistent in service delivery, which strengthens customer perceptions and experiences. The next stage of the SPC framework emphasizes the link between employee satisfaction and customer satisfaction. In banking services, employees directly interact with customers, and their attitudes and behaviors significantly influence service encounters. When employees are satisfied, they demonstrate greater commitment, responsiveness, and professionalism, which enhances customer perceptions of service quality. This improved service experience results in higher customer satisfaction, which is a critical determinant of customer loyalty and retention. Ultimately, customer satisfaction drives financial outcomes such as revenue growth and profitability, completing the service-profit chain process.

To further explain the psychological mechanism underlying the employee-customer relationship, this study incorporates Emotional Contagion Theory (Hatfield et al., 1994). This theory suggests that emotions are transferred between individuals through verbal and non-verbal cues during interpersonal interactions. In the banking sector, employees' emotional states such as enthusiasm, stress, or satisfaction are transmitted to customers during service encounters. Thus, when employees experience high job satisfaction due to supportive internal organizational practices, they are more likely to express positive emotions, which are unconsciously absorbed by customers. This emotional transmission enhances customers' perceived service experience and strengthens their satisfaction. Therefore, Emotional Contagion Theory provides a micro-level explanation for the pathway between employee satisfaction and customer satisfaction in the conceptual model. By integrating these two theories, the study establishes a strong multi-level framework. The SPC Theory explains the structural and organizational pathway from internal service quality to profitability, while Emotional Contagion Theory explains the behavioral and psychological mechanism that connects employees' attitudes to customer outcomes. Together, they provide a holistic understanding of how internal service practices in commercial banks of Kathmandu Valley translate into improved customer satisfaction and enhanced financial performance.

Figure 1

Conceptual Framework

Note. Walters (2018)

Workplace Design

Workplace Design (WD) refers to the physical and structural arrangement of the work environment, including layout, ergonomics, lighting, and workspace configuration, which collectively influence employee experiences. Grounded in Herzberg's Two-Factor Theory, workplace conditions act as hygiene factors that prevent dissatisfaction, while Person Environment Fit Theory emphasizes alignment between employees and their physical environment to enhance satisfaction (Alshmemri et al., 2017). Kamarulzaman et al. (2011), and Knight and Haslam (2010) confirm that well-designed workplaces significantly improve employee satisfaction, well-being, and engagement.

H_1: Workplace design has a significant positive relationship with employee satisfaction.

Job Design

Job design encompasses the structured arrangement of tasks, responsibilities, and duties assigned to employees. Key dimensions include autonomy, task variety, task significance, feedback mechanisms, and task identity. Jobs designed with appropriate flexibility and clear performance expectations enhance employee satisfaction and performance (Ali & Zia-ur-Rehman, 2014).

H_2: Job design has a significant positive relationship with employee satisfaction.

Training and Development

Training and Development (TD) refers to the systematic and continuous organizational efforts aimed at enhancing employees' knowledge, skills, and competencies to improve both current job performance and future career readiness. Empirically, Khan et al. (2016) found that structured training programs significantly improve employee satisfaction by increasing confidence and performance. Similarly, Aguinis and Kraiger (2009) highlighted that training enhances both individual and organizational outcomes, including job satisfaction and engagement.

H_3: Training and development has a significant positive relationship with employee satisfaction.

Reward and Recognition

Reward and Recognition (RR) comprises financial compensation and non-financial acknowledgment of employee contributions, including performance-based incentives and formal recognition programs. These practices motivate employees, reinforce desired behaviors, and create a sense of organizational value and fulfilment. When employees perceive that their efforts are fairly rewarded and appreciated, their motivation and engagement increase, which in turn enhances job satisfaction. Empirical evidence by Martono et al. (2018) indicates that effective reward and recognition systems significantly improve employee satisfaction by strengthening motivation, perceived fairness, and commitment within the organization.

H_4: Reward and recognition have a significant positive relationship with employee satisfaction.

Tools for Serving Customer

Tools for Serving Customers (TS) refers to the technological resources, information systems, service equipment, and workplace tools that enable employees to deliver efficient and high-quality services. When adequate and reliable tools are available, employees are better equipped to perform their tasks effectively with reduced effort and frustration. This not only improves service delivery but also enhances employees' sense of ease and competence in their work. Empirical evidence by Hogreve et al. (2022) indicates that the availability of appropriate service tools positively influences employee satisfaction by improving work efficiency and service quality.

H_5: Tools for serving customers has a significant positive relationship with employee satisfaction.

Employee Satisfaction

Employee Satisfaction (ES) refers to employees' overall affective evaluation of their work experience, including the extent to which their personal, professional, and financial needs are fulfilled within the organization. It reflects how positively employees perceive their job roles, working conditions, and organizational environment. Higher levels of satisfaction are associated with greater commitment, improved productivity, and a stronger willingness to deliver high-quality customer service. Empirical evidence by Chi and Gursoy (2009) indicates that satisfied employees are more likely to exhibit positive work behaviors, enhanced performance, and stronger service orientation.

H_6: Employee satisfaction has a significant positive relationship with customer satisfaction.

Customer Satisfaction

Customer Satisfaction (CS) reflects customers' evaluative judgment of service experiences, indicating whether service delivery meets or exceeds expectations. Satisfied customers exhibit greater loyalty, positive word-of-mouth, and continued patronage (Yee et al., 2007).

H_7: Customer satisfaction has a significant positive relationship with profitability.

Profitability

Bank profitability significantly influences financial development and economic growth Profitability (P) denotes the financial performance outcomes of commercial banks, measured through indicators such as return on investment, revenue growth, and market performance. Profitability represents the ultimate organizational outcome in the service-profit chain, influenced by both internal quality and customer satisfaction (Rew et al., 2020).

Variables and Definition

Table 1

Variable Construct

Construct	Observed Variables	Indicator	Explanation
Internal Quality	Layout and design	WD1	The layout and design of our workplace promote a comfortable and productive working environment
(Hogreve et al., 2016)	Collaboration and teamwork	WD2	The workplace is organized to encourage collaboration and teamwork among employees.
Workplace Design	Autonomy and responsibility	WD3	The work design within bank encourages autonomy and responsibility among employees.
	Departmental goals	WD4	Workgroups or teams within bank are organized effectively to achieve departmental goals.
Job Design	Autonomy	JD1	The autonomy to make decisions related to work tasks.
(Suhaimi et al., 2023)	Encouragement	JD2	Employees in the bank are actively encouraged to participate in decision-making processes.
	Workload and job	JD3	The workload and job tasks are distributed fairly among employees.
	Values and promote	JD4	The bank values and promotes a culture of self-management and self-leadership.
Training and Development	Employees skills	TD1	The bank provides comprehensive training programs to enhance employees' skills.
(Suhaimi et al., 2023)	Career prospects	TD2	Training and development offerings at the bank significantly enhance future career prospects.
	Opportunities	TD3	Access to continuous learning and development opportunities.
	Career growth	TD4	The bank offers mentorship or coaching programs to support employees in their career growth.
Employee rewards and recognition	Behavior based evaluation	ERR1	Employees are provided with clear and specific criteria for behavior-based evaluations.
(Suhaimi et al., 2023)	Contributions	ERR2	The contributions are appropriately recognized and rewarded.
	Compensation	ERR3	Additional compensation for the overtime hours work.
	Bonuses	ERR4	Performance incentives, such as bonuses or recognition, motivate employees to excel in their roles.
Tools for Serving Customers	Operations	TS1	IT systems in the bank are efficient and support day-to-day operations effectively.
(Suhaimi et al., 2023)	Software	TS2	Access to the necessary technology tools and software to perform roles effectively.
	Adequate resources	TS3	The bank provides adequate resources, including computers, software, and equipment, for employees to perform their tasks.
	Advanced service system	TS4	The bank utilizes advanced service systems to provide a seamless customer experience.

Employee Satisfaction (Suhaimi et al., 2023)	Salary	ES1	Satisfied with the salary of job (Chen et al., 2022)
	Security	ES2	Satisfied with the job security.
	Promotion	ES3	Satisfied with the promotion opportunity within the bank.
	Employment	ES4	Intend to continue employment in this company.
	Effort	ES5	Intend to contribute extra effort for the benefit of this bank
	Keep working	ES6	Intend to take any job to keep working for this bank
Customer Satisfaction (Adeinat et al., 2019)	Inquiry	CS1	Satisfied with the inquiry service provided by this bank.
	Promise	CS2	Employee provide service at the time they promise to do.
	Needs	CS3	Understand customer needs.
	Concerns	CS4	Actively listening to customer concerns and taking necessary actions to resolve issues.
	Coming Years	CS5	Customers of this bank will intend to conduct more financial transactions with in the coming years.
	Feedback	CS6	Customers are likely to share positive feedback about the bank with others
	Transaction	CS7	Customers are generally satisfied with their transactions with the bank.
Profitability (Silwal, 2022)	Higher salaries	P1	Bank pays higher salaries along with bonuses than competitors on average
	Profit growth	P2	This bank has demonstrated consistent profit growth in recent years.
	ROI	P3	A gradual increase in the bank's return on investment (ROI) over the years (Briggs et al., 2020).
	Market	P4	Organization's market development has increased significantly over the years
	Sales	P5	Gradual increase in sales volume within the bank over the years.

III. Methodology

This study adopts a post-positivist research philosophy, assuming that reality exists but can only be imperfectly measured through observable indicators. A deductive research approach is employed, where hypotheses are developed from existing theories and tested empirically. The study uses a quantitative survey method to collect data from respondents using structured questionnaires. Furthermore, a cross-sectional research design is applied, where data are gathered at a single point in time to examine relationships among variables. This methodological framework ensures objective analysis and hypothesis testing.

Study Area and Population

As the research study region, the Kathmandu Valley in Nepal's Province 3 has been selected. Within Nepal, the Kathmandu Valley is the most widespread and advanced area. Kathmandu, Lalitpur, and Bhaktapur are the three districts that comprise the Kathmandu Valley (Haack & Rafter, 2006). As a major economic and financial center in Nepal and the location of numerous banking institutions, the Kathmandu Valley was chosen as the study area. The individuals or entities that are the subject of the research within the banks of the Kathmandu Valley are considered to be the population in this study area. Whether examining satisfaction among employees, internal quality, customer behavior, or financial performance linked to banking operations, the banks in this region are appropriate for their research goals. Target population

is the group of people for which data is collected. The employees in the banking industry are the population in this case. This covers individuals who work in a variety of banking roles, including tellers, loan officers, branch managers, financial analysts, risk managers, IT specialists, and executives at various levels.

Sampling Technique and Sample Size

The sampling technique used in this study was non-probability purposive sampling, where the respondents used are the individuals who were directly involved in the banking operations and who had the ability to assess the service profit chain relationships (Devkota & Mahapatra, 2025). The population of interest was the employees that worked in commercial banks in the Kathmandu valley. Purposive sampling was deemed suitable because it provided an opportunity to select respondents who had the relevant knowledge and experience about the internal quality of services and employee satisfaction (Aalam et al., 2025). The sample size was determined using the standard formula (Amatya et al., 2023; Singh et al., 2024) at a 95% confidence level and 5% margin of error, with a population proportion of 0.5 (Alvi, 2016). This meant that the required sample size was 403 respondents. The final analysis involved usable responses of 384 employees due to the time constraints. The structured questionnaire was used to collect primary data that was aimed at measuring the internal service quality, employee satisfaction, customer satisfaction and profitability. The questionnaire questions were derived out of existing literature hence valid content and measured on a five-point Likert scale. Initial pilot test was done with 15 respondents to determine the clarity and reliability, and slight changes were also made. The information was gathered online and face to face via the Kobo toolbox. This two-sided method promoted accessibility and accuracy of response. The data collected was then coded and ready to be analyzed by the use of MS Excel and SmartPLS

IV. Results and Discussion

Socio Demographic Analysis

The socio-demographic analysis total of 384 respondent is surveyed to identify the analysis of service profit chain relation where majority of respondents are males i.e.,53.47% and remaining 48.53% are female. Additionally, majority of the respondents (52.86%) are married an 47.14% of the respondents are unmarried. The age range of most of respondents was 18-27 years at (49.43%) followed by 27-35 years at (40.36%), 35-43 years at (14.2%) whereas only 4.43% of the respondent belong to the age group of 43 and above. This reveals that mostly the bank of employee of 18-27 years given response. Considering the education level, the study revealed that majority of respondents were dominated by bachelor degree graduates by (57.03%), followed by Master's and above i.e. (35.94%), intermediate (6.25%), very few respondents were found to be level SLC (0.78%). This displays that most of the employees have completed bachelors' level. Furthermore, the majority of respondents occupations were in Private sector by (69.79%) and followed by governmental sector (20.31%). 5.47% of respondents involved in industrial sector whereas 7.29% are self-employed and 5.47% are others. Mostly the respondents are officer level by (30.47%) followed by assistant level by (29.17%), 19.79% are Managers, 15.1 % are others and remaining 5.47% are level of senior manager. Most of respondents had monthly income in the range of 25000-50000 by (48.18%) followed by 50000-75000 by (29.43%), 6.77% had income of 75000-100000 and only 4.95% employee's income of 1000000 and above. Most of the employee's bank tenure period is 1-5 year i.e. (53.39%) followed by Less than 1 year by (22.4%), 6-10 year i.e. (16.41%) and 7.81% are working from more than years.

Table 2

Socio-Demographic Characteristics of the Respondents

Variable	Category	Frequency (n)	Percentage (%)
Location	Kathmandu	228	59.38
	Lalitpur	97	25.26
	Bhaktapur	59	15.36
Gender	Male	200	53.47
	Female	181	48.53
Age	18–27	157	40.89
	27–35	155	40.36
	35–43	55	14.32
	43 and above	17	4.43
Marital Status	Married	180	52.86
	Unmarried	202	47.14
Education Level	SLC/SEE	3	0.78
	Intermediate	24	6.25
	Bachelor's	219	57.03
	Master's and above	138	35.94
Occupation	Private sector	268	69.79
	Government sector	78	20.31
	Industrial sector	21	5.47
	Self-employed	28	7.29
	Others	21	5.47
Employee Level	Assistant	112	29.17
	Officer	117	30.47
	Manager	76	19.79
	Senior manager	21	5.47
	Others	58	15.10
Income Level	< 25,000	41	10.68
	25,000–50,000	185	48.18
	50,000–75,000	113	29.43
	75,000–100,000	26	6.77
	100,000 and above	19	4.95
Bank Tenure	< 1 year	86	22.40
	1–5 years	205	53.39
	6–10 years	63	16.41
	> 10 years	30	7.81

Inferential Analysis

A. Common Method Bias (CMB) and Measurement Model Assessment

Since all the constructs data was gathered through the same source utilizing a structured questionnaire, it was needed to evaluate the possibility of common method bias (CMB) which artificially increases the relationship between constructs. To deal with this issue the research used the full collinearity assessment method whereby the researcher looked at the values of variance inflation factors (VIF) of all the latent constructs. Such an approach is highly suggested in PLS-SEM studies because it is known to measure both vertical and horizontal collinearity effects (Kock, 2017). The findings are that all VIF value was between 1.048 and 1.935, which is not even close to the conservative of 3.3 (Table 3). These results offer good reasons to believe that the issue of common method bias is not very severe in the current research and the derived path relationships can be treated as substantive and not methodological effects. After the evaluation of CMB, the measurement model was tested on reliability and validity to be sure about the robustness of the latent constructs.

Cronbach alpha and composite reliability were used to measure internal consistency reliability. The findings indicate that the Cronbach alpha values fell between 0.773 and 0.874, and the composite reliability values fell between 0.774 and 0.876. All values were above the recommended minimum point of 0.70 (Table 4), as recommended by Kock (2017), which shows high levels of internal consistency between the indicators of every construct. This proves that the scales that were employed to measure the constructs in the study are effective in capturing the theoretical constructs.

Convergent validity was measured by using indicator loadings and Average variance extracted (AVE). The outer loadings of all the observed indicators were high, above the recommended level of 0.70 (Hair et. al., 2017), which shows that the indicators were highly related to the constructs. In addition, the AVE values were 0.557 to 0.665, which is higher than the required minimum of 0.50 (Table 5). The above findings support the fact that each construct accounts over fifty percent of the variance in their indicators, which thus provides acceptable convergent validity.

Several complementary methods were used to assess discriminant validity to make sure that the constructs are empirically different. First, the analysis of cross-loading showed that every indicator loaded higher on the construct that it was designed to measure than any other measure. Second, Fornell-Larcker criterion was met since the square root of AVE of each construct was higher than the correlations of constructs with the rest of the constructs. Lastly, heterotrait-monotrait (HTMT) ratio of correlations was also tested as a stricter test of discriminant validity. The values of all HTMT were lower than the conservative value of 0.85, which implies distinct discriminant validity between the constructs (Hair et. al., 2017). The internal consistency of these three methods is a good enough validation that the constructs represent different theoretical phenomena. Combined, the findings of the common method bias analysis, internal consistency reliability analysis, convergent validity analysis, and the discriminant validity analysis prove the suitability of the measurement model. The case of the lack of a common method bias, the high level of reliability, and validity in the research, indicates that the quality of data is high and the measurement tools are working as expected. Therefore, the model has a good empirical basis to test the proposed hypothesized relationships of the Service-Profit Chain.

Table 3

Common Method Bias

	cs	err	es	jd	p	td	tsc	wd
VIF	1.492	1.782	1.609	1.728	1.468	1.202	1.935	1.048

Table 4

Internal Consistent Reliability

	Cronbach's alpha	Composite reliability
Cs	0.868	0.871
err	0.773	0.774
es	0.874	0.876
jd	0.782	0.786
p	0.873	0.873
td	0.801	0.803
tsc	0.81	0.811
wd	0.805	0.806

Table 5

Convergent Validity

Construct	Indicators	Outer Loading	Average variance extracted (AVE)
Workplace design	Wd1	0.79	0.631
	Wd2	0.825	
	Wd3	0.76	
	Wd4	0.801	
Job Design	jd1	0.746	0.603
	jd2	0.793	
	jd3	0.784	
	jd4	0.783	
Training and Development	td1	0.788	0.627
	td2	0.781	
	td3	0.833	
	Td4	0.764	
Employee Rewards and Recognition	err1	0.784	0.595
	err2	0.811	
	err3	0.779	
	err4	0.708	
Tools for Serving Customers	tsc1	0.778	0.637
	tsc2	0.806	
	tsc3	0.801	
	tsc4	0.808	

Employee Satisfaction	es1	0.749	0.614
	es2	0.751	
	es3	0.791	
	es4	0.811	
	es5	0.8	
	es6	0.797	
Customer Satisfaction	cs1	0.687	0.557
	cs2	0.736	
	cs3	0.726	
	cs4	0.753	
	cs5	0.786	
	cs6	0.775	
	cs7	0.759	
Profitability	p1	0.738	0.665
	p2	0.84	
	p3	0.851	
	p4	0.831	
	p5	0.812	

Table 6

Factors Cross-loading

	cs	err	es	jd	p	td	tsc	wd
cs1	**0.687**	0.502	0.532	0.488	0.501	0.502	0.534	0.438
cs2	**0.736**	0.382	0.296	0.315	0.401	0.374	0.479	0.488
cs3	**0.726**	0.362	0.267	0.259	0.318	0.378	0.464	0.409
cs4	**0.753**	0.324	0.214	0.243	0.286	0.409	0.484	0.426
cs5	**0.786**	0.449	0.47	0.394	0.459	0.538	0.527	0.43
cs6	**0.775**	0.462	0.479	0.377	0.495	0.52	0.51	0.414
cs7	**0.759**	0.411	0.485	0.365	0.521	0.466	0.528	0.42
err1	0.425	**0.784**	0.541	0.524	0.433	0.511	0.428	0.399
err2	0.398	**0.811**	0.495	0.529	0.401	0.474	0.45	0.444
err3	0.389	**0.779**	0.366	0.443	0.415	0.408	0.438	0.343
err4	0.519	**0.708**	0.344	0.369	0.417	0.469	0.567	0.428
es1	0.362	0.475	**0.749**	0.533	0.369	0.425	0.329	0.286
es2	0.42	0.427	**0.751**	0.472	0.392	0.435	0.401	0.287
es3	0.356	0.447	**0.791**	0.432	0.379	0.409	0.345	0.238
es4	0.43	0.429	**0.811**	0.423	0.429	0.425	0.393	0.299

es5	0.529	0.45	**0.800**	0.446	0.471	0.487	0.437	0.384
es6	0.448	0.461	**0.797**	0.471	0.445	0.45	0.44	0.376
jd1	0.319	0.452	0.387	**0.746**	0.329	0.411	0.298	0.374
jd2	0.334	0.462	0.499	**0.793**	0.338	0.436	0.316	0.447
jd3	0.353	0.475	0.467	**0.784**	0.403	0.464	0.322	0.359
jd4	0.467	0.496	0.471	**0.783**	0.415	0.505	0.394	0.452
p1	0.399	0.508	0.554	0.464	**0.738**	0.358	0.326	0.33
p2	0.455	0.456	0.42	0.41	**0.84**	0.404	0.382	0.371
p3	0.481	0.431	0.419	0.397	**0.851**	0.401	0.43	0.327
p4	0.509	0.417	0.386	0.324	**0.831**	0.397	0.435	0.311
p5	0.542	0.387	0.377	0.361	**0.812**	0.424	0.458	0.328
td1	0.494	0.424	0.468	0.471	0.4	**0.788**	0.516	0.441
td2	0.527	0.463	0.357	0.373	0.345	**0.781**	0.532	0.533
td3	0.497	0.487	0.468	0.474	0.42	**0.833**	0.505	0.422
td4	0.445	0.55	0.48	0.541	0.373	**0.764**	0.477	0.391
tsc1	0.489	0.548	0.427	0.341	0.373	0.547	**0.778**	0.452
tsc2	0.539	0.494	0.381	0.366	0.341	0.524	**0.806**	0.472
tsc3	0.564	0.426	0.409	0.366	0.43	0.455	**0.801**	0.41
tsc4	0.572	0.487	0.386	0.306	0.44	0.524	**0.808**	0.382
wd1	0.484	0.417	0.344	0.354	0.284	0.408	0.443	**0.79**
wd2	0.433	0.407	0.34	0.424	0.301	0.443	0.406	**0.825**
wd3	0.421	0.4	0.275	0.412	0.341	0.463	0.42	**0.76**
wd4	0.494	0.442	0.315	0.482	0.373	0.472	0.432	**0.801**

Table 7

HTMT Ratio

	cs	err	es	jd	p	td	tsc	wd
cs								
err	0.674							
es	0.597	0.689						
jd	0.559	0.776	0.711					
p	0.655	0.656	0.603	0.577				
td	0.731	0.769	0.667	0.737	0.581			
tsc	0.802	0.775	0.593	0.538	0.59	0.798		
wd	0.689	0.663	0.474	0.661	0.488	0.703	0.665	

Table 8

Fornell-Larcker Criterion

	cs	Err	es	jd	p	td	Tsc	Wd
Cs	**0.747**							
Err	0.563	**0.772**						
Es	0.546	0.572	**0.784**					
Jd	0.48	0.607	0.59	**0.777**				
P	0.586	0.541	0.531	0.481	0.816			
Td	0.619	0.607	0.561	0.588	0.487	0.792		
Tsc	0.679	0.61	0.502	0.431	0.498	0.641	0.798	
Wd	0.579	0.525	0.402	0.528	0.41	0.562	0.536	0.794

B. Structural Model Assessment

The structural model was assessed after the reliability and validity of the measurement model had been confirmed to test the hypothesized relationships between the constructs. The evaluation of the structural model was carried out using a set of guidelines of Partial Least Squares Structural Equation Modeling (PLS-SEM) as suggested by Hair et al. (2019). The assessment was based on several factors such as path coefficients (B), their statistical significance (t-values and p-values), the coefficient of determination (R^2), the effect sizes (b^2 or f^2) and predictive relevance (Q^2). To obtain standard errors and t-statistics, a bootstrapping process that used 5,000 resamples was used to obtain robust estimates of the path coefficients and the level of significance (Henseler, Ringle, and Sarstedt, 2015). The outcome of the structural model such as the path coefficients and R^2 values are shown in Figure 2. The model shows a significant explanatory ability, as the five internal quality dimensions explain the variation in Employee Satisfaction (R^2= 0.624). Based on the criteria laid out by Hair et al. (2019), this R^2 value is that of a moderate-substantial predictive level, meaning that the internal quality variables are strong predictors of employee satisfaction when applied to the Nepalese commercial banks. Moreover, Customer Satisfaction is explained by Employee Satisfaction (R^2 = 0.316) and all the models combined explain 36.0% of the variance in Profitability (R^2 = 0.360). These values illustrate the upward explanatory force of the service-profit chain model where a successive outcome variable is significantly predicted by prior variables.

Hypothesis Testing

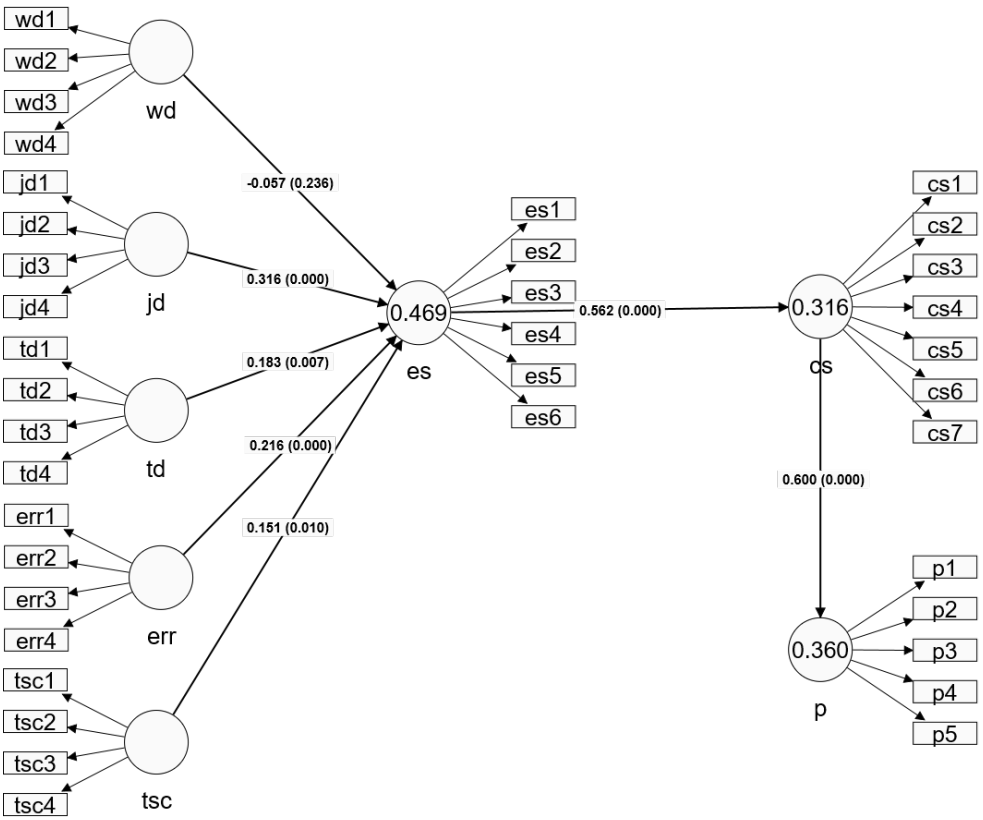
Table 9

Hypothesis Testing

Hypothesis		B	SD	T values	P values	CI		Decision
						LL (2.5%)	UL (97.5%)	
H1	wd -> es	-0.057	0.048	1.185	0.236	-0.154	0.037	Not Supported
H2	jd -> es	0.316	0.061	5.207	0	0.198	0.436	Supported
H3	td -> es	0.183	0.068	2.701	0.007	0.051	0.315	Supported
H4	err -> es	0.216	0.056	3.87	0	0.108	0.328	Supported
H5	tsc -> es	0.151	0.059	2.57	0.01	0.038	0.266	Supported
H6	es -> cs	0.562	0.047	11.857	0	0.463	0.648	Supported
H7	cs -> p	0.6	0.041	14.53	0	0.511	0.673	Supported

Figure 2

Structural Model



The outcome of hypothesis testing gives high empirical evidence on service-profit chain model when applied in the case of commercial banks in Kathmandu Valley, Nepal. Out of the five internal quality dimensions proposed to affect employee satisfaction, four of them were found to be statistically significant (Table 9), and they were job design (which proved to have the strongest positive correlation to employee satisfaction (= 0.316, p = 0.001), rewards and recognition (= 0.216, p = 0.001), training and development (= 0.183, p = 0.010), and customer serving tools (= 0.151, p = 0.010). The four dimensions were able to explain 62.4% of the variance in the employee satisfaction hence a great degree of explanatory power. Nevertheless, the workplace design did not have a significant correlation with employee satisfaction (= -0.057, p = 0.236), which indicates that the physical workspace features can be not so crucial in the Nepalese banking scenario as work-related and organizational variables. Moreover, customer satisfaction had a strong positive correlation with employee satisfaction (β = 0.562, p < 0.001), which subsequently establishes a solid foundation of emotional contagion mechanism according to which the affective state of employees is transferred to a customer when they interact during service provisions. Lastly, customer satisfaction was found to have a positive relationship with profitability (= 0.600, p = 0.001) which is the ultimate service-profit relationship where satisfied customers contribute to financial performance by being loyal, creating positive word-of-mouth and increasing business relationships. These results confirm the central sequential correlations suggested in the service-profit chain model and make it applicable to the banking industry of South Asia.

Table 10

Results of Mediation Analysis

Hypothesis		β	SD	T value	P values	LL (2.5%)	UL (97.5%)	Decision
H8	wd -> es -> cs -> p	-0.019	0.017	1.161	0.246	-0.055	0.012	Not Supported
H9	jd -> es -> cs -> p	0.106	0.025	4.324	0	0.064	0.16	Supported
H10	td -> es -> cs -> p	0.062	0.026	2.421	0.015	0.017	0.119	Supported
H11	tsc -> es -> cs -> p	0.051	0.023	2.255	0.024	0.013	0.101	Supported
H12	err -> es -> cs -> p	0.073	0.022	3.356	0.001	0.035	0.122	Supported
H13	es -> cs -> p	0.337	0.045	7.419	0	0.249	0.427	Supported

The mediation analysis showed the sequential chain of effects that exists in the service-profit chain theory, where internal investments on quality measures on quality translate to profitability via employee and customer satisfaction channels (Table 10). All the internal quality dimensions were found to have significant indirect effects on profitability via the sequential mediation of employee satisfaction and customer satisfaction except the workplace design where job design (= 0.106, p = 0.001), rewards and recognition (= 0.073, p = 0.001), training and development (= 0.062, p = 0.015), and customer serving tool satisfaction (= 0.051, p = 0.024) expressions were found. These notable indirect impacts are an indication that designed jobs, proper rewards, extensive training, and proper service tools would promote employee satisfaction, which further promotes customer satisfaction and eventually leads to profitability. Moreover, the indirect impact of employee satisfaction on profitability mediated by customer satisfaction was considerable and considerable (= 0.337, p < 0.001), which proved that customer satisfaction is the key process by which employee attitudes are converted into financial performance. All of these mediation findings are strong arguments in support of the cascading-like nature of the service-profit chain relationships and support the theoretical hypothesis that the investments in internal service quality produce financial returns, not directly, but through the cascading influence they have on employee outcomes and customer perceptions. The results highlight the strategic significance of combined management practices viewing the experiences of employees, customer performance, and financial performance as related factors of organizational success.

Discussion

The Service Profit Chain (SPC) model explains how internal service quality leads to employee satisfaction, which enhances customer satisfaction and ultimately improves organizational profitability. In banking institutions, this sequential relationship is particularly relevant due to high customer interaction and service dependency. This study applies the SPC framework in commercial banks in Kathmandu Valley, a developing economy context where service efficiency and human resource practices are increasingly critical. It examines how internal organizational factors shape employee attitudes and drive performance outcomes through customer experiences. The study provides empirical evidence supporting the SPC model in

Nepalese commercial banks, confirming that internal service quality influences organizational profitability indirectly through employee satisfaction and customer satisfaction. This finding reinforces the sequential logic proposed in SPC theory and indicates that financial performance in service organizations is the outcome of interconnected human, operational, and customer-related processes (Adeinat & Kassim, 2019). The main objective of this study was to examine the relationship between internal service quality dimensions workplace design, job design, training and development, employee rewards and recognition, and tools for serving customers and employee satisfaction, as well as the subsequent impact of employee satisfaction on customer satisfaction and profitability. The findings from hypothesis testing provide strong empirical support for the SPC framework in the Nepalese banking context.

The results indicate that four internal service quality dimensions significantly influence employee satisfaction. Job design shows the strongest positive effect ($\beta = 0.316$, $p < 0.001$), highlighting that autonomy, role clarity, task variety, and feedback systems are critical in enhancing employee satisfaction in banking environments where tasks are complex and compliance-driven. This finding align Martono et al. (2018) who finds that well-structured jobs reduce role ambiguity and job stress, thereby increasing employee enthusiasm and satisfaction, consistent with motivation theories emphasizing the importance of intrinsic job characteristics Training and development also significantly affect employee satisfaction ($\beta = 0.183$, $p = 0.007$), suggesting that continuous skill enhancement is essential in a rapidly evolving digital banking context. This supports the view that regular training improves employee competence, confidence, and psychological attachment to the organization, particularly in environments characterized by technological change and increasing customer expectations (Chi & Gursoy, 2009). Employee rewards and recognition demonstrate a significant positive relationship ($\beta = 0.216$, $p < 0.001$), indicating that perceived fairness and appreciation play an important role in motivating employees and strengthening their satisfaction, aligning with social exchange theory which emphasizes reciprocal relationships between organizational support and employee commitment (Suhaimi et al., 2023; Walter, 2018). Similarly, tools for serving customers significantly influence employee satisfaction ($\beta = 0.151$, $p = 0.010$), confirming that adequate technological systems and operational resources improve efficiency and reduce workplace frustration, thereby enabling better service delivery. In contrast, workplace design does not have a statistically significant effect on employee satisfaction ($\beta = -0.057$, $p = 0.236$), suggesting that physical work environment factors are less influential in structured banking institutions where standardized layouts and formal procedures dominate, making functional job factors more important than physical aesthetics. Furthermore, employee satisfaction has a strong positive effect on customer satisfaction ($\beta = 0.562$, $p < 0.001$), indicating that satisfied employees exhibit positive emotions, attentiveness, and responsiveness that enhance customer experience, consistent with the emotional contagion mechanism in service literature (Silwal, 2022). Finally, customer satisfaction significantly influences profitability ($\beta = 0.600$, $p < 0.001$), demonstrating that customer loyalty, repeat transactions, and positive word-of-mouth drive financial performance. Overall, the findings provide strong empirical support for SPC logic in Nepalese banks, confirming that internal service quality enhances employee satisfaction, which ultimately improves customer satisfaction and profitability.

V. Conclusion and Implications

The paper concludes by finding that the Service-Profit Chain model can be very useful and applied to the commercial banking industry of Nepal. The results confirm that internal quality of service delivery especially, job design, training and development, reward and recognition, service support tools are crucial in improving employee satisfaction. Employee satisfaction, in turn, is a significant controller of customer satisfaction, which eventually results in the enhanced profitability. These findings support the fact that the financial performance of service organizations does not exist in a vacuum but emerges as an epitome of a transactional and interdependent process between the employees and the customers. The lack of a substantial result between place of work design and satisfaction of workers is an indication of a contextual change in the character of banking labor where digital technology and service

procedures takes precedence over corporeal work settings. This presents the necessity of having bank management to concentrate on the functional and the psychological facet of work and not just the symbolic or the aesthetic enhancement. The close relationship between the employee satisfaction and the customer satisfaction highlights the strategic importance of front-line employees as the first stage of contact between banks and customers. In general, the research adds to the existing literature by confirming the links between SPC in the context of a developing economy as well as introducing Emotional Contagion Theory to illustrate the process of transmission between employees and customers. In real life sense, the research highlights that bank profitability can only be sustainable when there are long-term investments in human capital, staff welfare, and service-support infrastructure. Thus, banks, which give importance to internal quality and employee satisfaction, have a higher chance of attaining high customer results and financial prosperity in the long-run.

This research can be further developed by future researchers using longitudinal designs to observe changes in Service-Profit Chain with time. The findings might be improved in terms of the generalizability through comparative research involving public and private banks, or various service industries. Other variables like the employee engagement, leadership style, organizational culture, or digital service quality could be incorporated to enhance the model. The study may also be extended toS investigate the perceptions of the customers to establish the satisfaction mirror assumption. Lastly, the cross-country research of the related developing economies would bring better insight into the situational strength of the Service-Profit Chain framework.

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