UCP Journal of Business Perspectives
Vol. 1, Issue 1(January-June 2023)
Journal website: http://ojs.ucp.edu.pk/index.php/jbp/index

Evaluating the Role of Reputational Risk on the Performance of Banks

Naqeeb Ullah [1*], Umair Asghar [2]

ABSTRACTS

The purpose of the study was to evaluate the role of reputational risk on the performance of banks in Pakistan. For this research, the data was collected through the primary quantitative technique where the survey was conducted from the 100 bank managers of Pakistan. The data was analysed through correlation and regression analysis using SPSS software. The findings of the study state that reliability and integrity have a negative and insignificant influence over bank performance. While on the other hand, quality of financial product and services are found to have positive and significant influence on bank performance which suggests that an increase in the quality of financial product leads to an increase in Pakistani banks' performance. Further, Customer care has also been found to have positive and significant influence on bank performance. The study has certain limitations such as the sample size which is small and data generalizability can be an issue. Furthermore, the secondary data was not used as there is no such reputation index of Pakistan. Therefore, the future studies can consider various risk factors in evaluating their effect on bank performance. Further, future research can be considered developing reputation index for Banks using secondary quantitative data.

Keywords: *Reputation Risk, Bank Performance, reliability and integrity, Quality of financial products*

1. INTRODUCTION

The following research paper evaluate the role of the reputational risk on the performance of banks. The post-crisis period has carried out increased consideration towards the reputational risk among customers and specifically in the banking industry. As scandals from the pre-crisis period surface and money spent to save the bank increases public resistance, restructuring during and after crises leads to a greater focus on corporate culture and trust difficulties. (Trostianska & Semencha, 2020). The crisis of 2007-2009 caused losses of multibillions and shows the weakness of growth foundation and risk management system failure in the large banks. Even a decade after the financial crisis, the banks are experiencing a decline

[1] Asia e University, Malaysia
[2]Hajvery University, Lahore, Pakistan.
[*]Corresponding author's E-mail: chasefor16@yahoo.com
Article History:
Received: 25-08-2023; Accepted: 06-09-2023
Available online: 21-09-2023
This is an open-access article.

in client support, signifying that client will not place their confidence in banks (Tăchiciu et al., 2020). The study of Gatzer et al. (2016), states that protecting the reputation of a financial institution is the major challenge that financial firms are experiencing and trust in the financial sector integrity is the foundation of its development and stability.

The framework of reputational risk management in the banking industry is still volatile and underdeveloped, and the banks are developing the reputational risk framework to minimize the losses and not considering that for the long-term, strategic goals. Measures to deal with customer complaints and the quality of products and services can also create a reputation risk for the banks, and there are limited studies that evaluate these factors and measure the performance of banks. Moreover, the efforts to regulate the operational risk are quantified effectively and successfully in the last decade however the concept of reputational risk still requires further research as the reputational risk significance is still limited specifically in the context of Pakistan. Therefore, the following study aims to evaluate the role of reputational risk by mainly considering the performance of Pakistani banks. The following study aims to fill the research gap by considering variables including customer complaints and product services quality and how impact the reputation and performances of banks in Pakistan. The findings of the following study will contribute to the existing literature on the reputational risk concept in financial institutions. This study has important ramifications for bank risk administrators, policymakers, and scholars who are trying to understand how reputational risk relates to financial risk in terms of enhancing bank performance.

2. LITERATURE REVIEW

Reputation risk refers to the damage which arises when the institutions loose the capability to meet the stakeholder's expectations and therefore it is negatively perceived. Reputational risk creates an impact on business despite the industry and size. Reputational risk in financial and banking services is related to firms losing the trust of stakeholders and consumers (Heidinger & Gatzert, 2018). da Silva Vinhado & Banco do Brasil (2017) state that developing a robust reputation gives a competitive advantage and a better reputation which reinforce the market position of companies and enhance the shareholder value. Concerning the banks, communication between the stakeholders and banks can be the cornerstone for a better reputation. Moreover, the bank's capability to regulate the risk also creates an impact on the decision of investors, even if the financial institution is gaining profits, the dearth of risk management can decline the revenues because of the loan losses.

Miklaszewska et al. (2020) evaluate the reputational risk and importance for the banks and also evaluate its consequences and sources, particularly taking the evidence from the CEE-11 banks. The research provides a new approach to examining reputation risk, which is referred to as the stakeholder reputation score (SRS). The findings of the study state that efforts improve the reputation of banks have a positive influence on the bank's performance. The study further indicates that banks focus on the reputational risk particularity to deal with the loss the banks face after the scandal, despite evaluating the reputation risk for the long-term and strategic goals.

Butt et al. (2022) conducts a study on the financial performance and risk of Islamic and financial banks, considering the concept of reputational risk while taking evidence from Pakistan. Using SEM (structural equation model), the research implemented a panel data set approach considering the sample size of 24 Islamic and conventional banks, particularly considering the time period of 2007–2017. According to the study's findings, the relationship between the effectiveness of financial risks and conventional banks is mediated in part by reputational risk. The reputational risk for Islamic banks in their role as a middleman is still quite low. Since, the Shariah compliance and an Islamic bank's reputation risk are closely related, Islamic banks are given a higher reputation risk rating than regular banks. However, Shariah compliance was not taken into account in the credit rating techniques used by foreign rating organisations. Additionally, it is difficult to measure and monitor reputational risk in dual financial institutions like Pakistan, where Islamic banks had significant growth in 2016 of approximately 14% compared to the average financial industry increase of 6%. Adeabah et al. (2022) evaluated the trends of research on the reputational risk in banks by incorporating the network and systematic literature review, including the 35 articles published between the periods of 2010 to 2020. The findings of the study state that only developed nations mainly Europe and the United States have a proactive contribution to reputational risks in banks and further states that it does not acquire global consideration.

Reputation is built on a combination of prior experiences, but it also considers the future and embodies goals for the business. Customers who are happy with the way the bank conducts business are more dependable, which improves the bank's reputation and competitiveness. But problems with the bank's reputation can lead to a loss of current and potential customers, employees and managers, as well as present and future business partners. Additionally, they can increase the cost of financing by using loans or financial markets (Devlin et al., 2015).

Sharma & Joshi (2022), examine the bank reputation role through the proposed dimensions in impelling the trust of banks and its following effects on customer loyalty. The findings of the study demonstrate that all of the suggested characteristics of corporate reputation and bank reputation namely, stability, service quality, corporate performance and customer centricity, have a substantial impact on bank trust. Additionally, a considerable impact of bank confidence on loyalty was discovered. A key mediator between the characteristics of bank image and bank trust was found to be bank type. It demonstrates that there are considerable differences between private and public banks in the impact of stability, service quality, corporate performance and customer centricity on bank trust. According to the study's findings, customer centricity is seen as being high in private banks, but the three other aspects are regarded as being greater in public sector banks.

El-Chaarani & El-Abiad (2020) state that quality offer, customer care, financial strength and reliability and integrity has a positive and significant influence on the Lebanese banking sector's reputation in a time of crisis, moreover the study also states that satisfaction and customer trust have more significant influence. Based on the above discussion, most of the studies shows that the quality of financial product and services, customer care and reliability and integrity has a positive influence on bank performance, therefore the conceptual framework and hypothesis for the following study has been presented below:

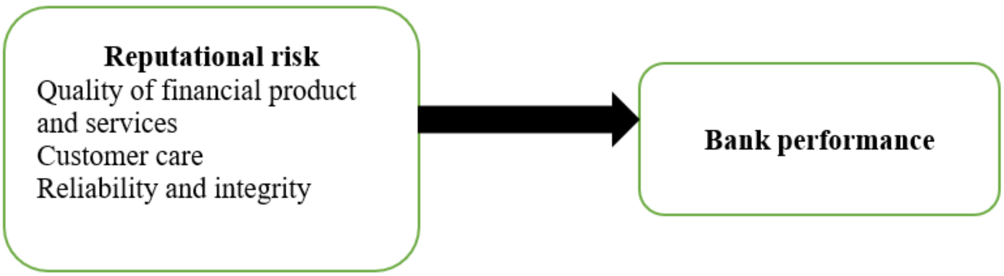

Figure 1: *Conceptual Framework*

H1: Quality of financial product and services has a positive influence on the performance of banks.

H1: Customer care has a positive influence on the performance of banks.

H1: Reliability and Integrity has a positive influence on the performance of banks.

3. METHODOLOGY

The main emphasis of the current study is to evaluate the role of reputational risk on the performance of banks. Based on the nature of the study, the quantitative research design was selected. The primary reason behind the selection of this particular research design is that it enables to incorporate the numerical data and information and the other reason is that it evaluates the relationship between the variables of the study and assists to test the hypothesis. Moving forwards, there are two methods that are used to collect the data, one is the primary data collection method and the other is the secondary data collection method. The following study opted for the primary data collection method the reason behind selecting the primary data collection method is that it provides first-hand data and it comes from direct sources which ensure reliability and accuracy. The data and information were gathered through the survey questionnaire that was based on the 5-point Likert scale. In addition to that the sample size was selected based on the non-probability sampling technique as this sampling technique assists to escape an unconscious bias.

The data was collected from 100 respondents that were bank managers. The data were analyzed through statistical measures including SPSS software. The test and analyses included were descriptive analysis, correlation analysis and regression analysis.

4. RESULTS

4.1. Demographic analysis

Table 1: *Demographic Analysis*

	Frequency	Percent	Valid Percent	Cumulative Percent
Gender				
Male	74	74.0	74.0	74.0
Female	26	26.0	26.0	100.0
Total	100	100.0	100.0	
Age				
25-30	1	1.0	1.0	1.0
31-35	37	37.0	37.0	38.0
36-40	47	47.0	47.0	85.0
41-45	5	5.0	5.0	90.0
45+	10	10.0	10.0	100.0
Total	100	100.0	100.0	
Experience in Banking Sector				
1- 2 years	62	62.0	62.0	62.0
2-3 years	29	29.0	29.0	91.0
More than 3 years	9	9.0	9.0	100.0
Total	100	100.0	100.0	

Table 1 shows the demographic of the respondent which includes the gender, age and experience of the managers in the banking sector. Table 1 states that the majority of managers were male with a proportion of 74%, while there were 26% of managers were female.

The above table also shows the manager’s age, it can be seen that there were 1.0% of the respondent were in the age group of 25 to 31. 37.0% of the bank managers were aged between 31 and 35. Furthermore, there are about 47.0% of the respondents have an age group of 36 to 40. 5.0% of the bank manager aged 41-45. Lastly, there were 10% of respondents were aged above 45.

In addition, the table presented above also presented the experience of the managers in the banking industry, where it can be seen that there were 62% of the respondents have experience of 1 to 2 years. Moreover, there were 29.0% of the respondents have experience of 2 to 3 years. Lastly, only 9% of the managers state that they have experience of the banking sector more than three years.

4.2. Descriptive analysis

Table 2: *Descriptive Statistics Analysis*

Descriptive Statistics					
	N	Minimum	Maximum	Mean	Std. Deviation
Reliability and integrity	100	1.0000	5.0000	3.3133	0.9414
Quality of financial products & services	100	1.0000	5.0000	3.1967	1.0107
Customer care	100	1.0000	5.0000	3.4900	0.9622
Bank performance	100	1.0000	5.0000	3.7067	0.9408
Valid N (listwise)	100				

Table 2 above shows the descriptive analysis which defines the mean value of variables and standard deviation. It has been found that reliability has a mean value of 3.3133 and the standard deviation of 0.9414. It implies that the reliability and integrity of the Pakistan Banks is neutral on average. The quality of financial products and services has a mean value of 3.196, and this value can be increased or decreased by the 1.010 value. It shows the response for quality to be neutral on average. Moreover, the average value of customer care is computed as 3.490 and this value can be deviated by the value of 0.9622. It shows that the value of customers has the average response of agree to neutral. Lastly, the bank performance has a mean value of 3.706 and its standard deviation is computed as 0.940. It shows that bank performance has sufficiently improved as average response is agree to neutral.

4.3. Reliability analysis

Table 3: *Reliability Analysis*

Reliability Statistics	
Cronbach's Alpha	N of Items
.934	12

Reliability analysis is used to analyse the validity of each of the constructs involved in the current research. As per the research of Kline (2015), Cronbach's alpha value must be greater than threshold of 0.7 to ensure the validity of each items. Table 3, shows that all items are found to be valid, as Cronbach's alpha value is found to be greater than threshold (i.e. 0.934 > 0.7). Thus, it implies that all variables involved in this specified research are reliable and valid for analysis.

4.4. Correlation analysis

Table 4: *Correlation Analysis*

Correlations	[1]	[2]	[3]	[4]
[1] Reliability and integrity	1	.931**	.792**	.432**
[2] Quality of financial product and services	.931**	1	.621**	.433**
[3] Customer care	.792**	.621**	1	.395**
[4] Bank performance	.432**	.433**	.395**	1

**. Correlation is significant at the 0.01 level (2-tailed).

Correlation analysis is used to evaluate the association between each of the latent construct. Referring to the bank performance with respect to reliability, it has been found to positive and moderate association between variables, as coefficient value is found to be .432**. Similarly, bank performance has also a positive moderate and significant association with quality of financial product and services, as coefficient value is found to be 0.433**. Lastly, bank performance is also positively and moderately associated with customer care, as coefficient value is identified as 0.395**. Thus, it implies that all variables in the research are positively association with bank performance. Despite these, reliability and integrity, quality of financial product, and customer care are also found to be positively associated with each other.

4.5. Regression analysis

Table 5 - Linear Regression Analysis

	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
(Constant)	2.097***	0.334		6.272	0.000
Reliability and integrity	-0.258	0.372	-0.258	-0.692	0.490
Quality of financial product & services	0.457*	0.270	0.491	1.689	0.094
Customer care	0.288*	0.169	0.294	1.699	0.093

R Square: 0.217
Adjusted R Square: 0.193
Sig : 0.000

*Sig *** 1% ** 5% * 10%*

Table 5, shows influence of explanatory variable (i.e. reliability and integrity, quality, and customer care) on explained variable (i.e. bank performance). Notably, reliability and integrity has a negative influence over bank performance, but it has been found to be insignificant, as B= -0.258, and P= 0.490 > 0.1. On contrary, quality of financial product and services are found to be positive and significant influence over bank performance, as B= 0.457* and P= 0.94. Thus, it implies that increase in quality of financial product leads to increase in the performance of the banks. Further, Customer care has also found to be positive and significant influence over bank performance, as B= 0.288* and P = 0.093. It demonstrated that improvement in customer care leads to higher performance of banks. Further, from above table value of R square is also found to be 0.217 which suggested that 21.7% variance in the model is predicted due to variance in independent variable. Lastly, sig value is also found to be less than threshold (i.e. 0.000 < 0.05) which implies that overall model is fit for analysis.

5. DISCUSSION

The following research was conducted to evaluate the role of reputation risk on the performance of banks. The correlation analysis revealed that reputation risk (i.e. quality of financial products and services, customer care and reliability) has a significant relationship with the performance of banks. Moreover, the regression analysis implies that the reputation risk (i.e. quality of financial products and customer care) has significance and positive influence on the performance of Pakistani banks. The findings of the current study are similar to the research study conducted by El-Chaarani & El-Abiad (2020) which states that the quality of offers and customers has a positive and significant influence on the bank's performance during the period of crisis. In addition, the above-mentioned study also shows the positive and significant influence of reliability on banks' performance. However, these results are in contradiction with the findings of the current study. The findings of the current study states show that reliability and integrity have insignificant and negative influence on banks' performance.

Furthermore, Mutunga & Wamitu (2020) also provide similar results relating to product and service quality. The study demonstrates that the quality of financial product and services significantly and positively influence commercial banks' performance. The study further states that sustainability and success in the banking sector depend on several aspects including quality of services, accountability and technological modifications. With respect to that banks should not only consider the shareholder's expectations. However, they are also required to consider the products and services quality and customers. Satisfaction with a customer that can be led through the quality of products impacts the bank's performance in the long run. Moreover, the current is also suggesting maintaining the existing clients and attracting the nee client to succeed in the marketplace. In addition, the study of Ruiz et al. (2014) elucidates that banks are required to give consideration to the reputation to strengthen the manager's leadership and to also convey reliability. They should give consideration to customer trust and satisfaction to attain the optimization of banks' status and reputation in times of crisis.

6. CONCLUSION

The purpose of the study was to evaluate the role of reputational risk on the performance of banks particularly taking the evidence from Pakistani banks. For this purpose, the data was collected through the primary quantitative measures where the survey was conducted from the 100 bank managers of Pakistan and SPSS was used as a statistical software to undertake the empirical investigation. The findings of the study state that reliability and integrity have a negative as well as insignificant influence over bank performance. While on the other hand quality of financial product and services are found to be a positive and significant influence on bank performance which suggests that an increase in the quality of financial product leads to an increase in Pakistani banks' performance. Further, Customer care has also been found to be a positive and significant influence on bank performance, which further suggests that improvement in customer care leads to higher performance of banks.

Based on the current analysis of the reputation risk on banks' performance, it is recommended that bank distractors and executive are required to invest in the approaches that progress the financial product and service quality leading to customer satisfaction and further improving bank performance. It is also recommended that the banks need to consider the need of clients and redesign their products and services to acclimatize with their exceptions. Moreover, through effective communication channels, managers can ensure the expectation of customers in an understandable manner which will decrease the reputation risk and positively influences the performance of Pakistani banks.

The study has certain limitations such as the sample size which is small and data generalizability can be an issue. Furthermore, the secondary data was not used as there is no such reputation index of Pakistan. Therefore, the future studies can consider various risk factors in evaluating their effect on bank performance. Further, future research can be considered developing reputation index for Banks using secondary quantitative data.

Reference

Adeabah, D., Andoh, C., Asongu, S. and Gemegah, A., 2022. Reputational risks in banks: A review of research themes, frameworks, methods, and future research directions. *Journal of Economic Surveys*.

Butt, M.A., Ayub, H., Latif, B., Asif, F., Shabbir, M.S. and Raja, A.A., 2022. Financial risks and performance of conventional and Islamic banks: do reputational risk matters?. *Journal of Islamic Accounting and Business Research*, *13*(4), pp.581-595.

da Silva Vinhado, F. and Banco do Brasil, S.A., 2017. REPUTATIONAL RISK MEASUREMENT: BRAZILIAN BANKS. *ISSN 2168-0612 FLASH DRIVE ISSN 1941-9589 ONLINE*, p.2.

Devlin, J.F., Ennew, C.T., Sekhon, H.S. and Roy, S.K., 2015. Trust in financial services: Retrospect and prospect. *Journal of Financial Services Marketing*, *20*, pp.234-245.

El-Chaarani, H. and El-Abiad, Z., 2020. Determinants of banks reputation during crises. *El-CHAARANI H. and El-Abiad*, (2020).

Gatzert, N., Schmit, J.T. and Kolb, A., 2016. Assessing the risks of insuring reputation risk. *Journal of Risk and Insurance*, *83*(3), pp.641-679.

Heidinger, D. and Gatzert, N., 2018. Awareness, determinants and value of reputation risk management: Empirical evidence from the banking and insurance industry. *Journal of Banking & Finance*, *91*, pp.106-118.

Kline, R. B. 2015. *Principles and practice of structural equation modeling*. Guilford publications.

Miklaszewska, E., Kil, K. and Pawłowska, M., 2020. Is reputational risk important for bank performance? Evidence from CEE-11 countries. *Argumenta Oeconomica*, *2*, pp.31-51.

Mutunga, M.N. and Wamitu, S.N., 2020. Effects of quality of bank products and services on the performance of commercial banks in Makueni County. *International Journal of Finance and Accounting*, *5*(1), pp.32-46.

Ruiz, B., Esteban, Á. and Gutiérrez, S., 2014. Determinants of reputation of leading Spanish financial institutions among their customers in a context of economic crisis. *BRQ Business Research Quarterly*, *17*(4), pp.259-278.

Sharma, R. and Joshi, R., 2022. The effect of bank reputation on loyalty–the moderating role of bank type. *South Asian Journal of Business Studies*, (ahead-of-print).

Tăchiciu, L., Fülöp, M.T., Marin-Pantelescu, A., Oncioiu, I. and Topor, D.I., 2020. Non-financial reporting and reputational risk in the Romanian financial sector. *Amfiteatru Economic*, *22*(55), pp.668-691.

Trostianska, K. and Semencha, I., 2020. Reputational risk management in conditions of credibility gap in the banking system. *Journal of Financial Economic Policy*, *12*(3), pp.327-343.