International Journal of Economic Perspectives, 2017, Volume 11, Issue 4, 702-716.

Customer Satisfaction, Loyalty, and Financial Performance in the Tourism and Hospitality Industry: Evidence from North Cyprus

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ABSTRACT

This study investigates the relationship among customer satisfaction, loyalty and financial performance in the tourism and hospitality industry for the case of North Cyprus. The results indicate that SERVQUAL items have a positive effect on both customer satisfaction and customer loyalty. The study also demonstrates the positive effect of service quality factors on customer satisfaction and loyalty towards a hotel. Moreover, there are direct effects of customer satisfaction and loyalty on the financial performance of hotels while service quality factors affect the financial performance of the hotels indirectly.

JEL Classification: L80; L83; M10; M30.

Keywords: Customer Satisfaction; Loyalty; Financial Performance; Tourism; Cyprus.

1. INTRODUCTION

The competitiveness in the world market increases from day to day as technology brings new opportunities and facilities to the manufacturing and services industries. This also caused an increase in competition in education institutions to supply qualified labors to the job market which also causes another competition in the job market among labors. Services sector increasingly became a major element for the economies in the last few decades more importantly in industrialized countries. The increased competition also brought a requirement for service quality in the services sector. Therefore, service quality is increasingly recognized as being one of key strategic value by organizations in both the manufacturing and service sectors (Lewis, 1991). It is also considered a critical determinant of competitiveness (Lewis, 1991). Increasing competition, technology, social and cultural factors were the chief drivers of service quality initiatives during the 1990s (Newman, 2001). "Quality" in a service organization is a measure of the extent to which the service delivered meets the customer's expectations (Ghobadian et. al, 1994). There are major differences between services and manufacturing sectors as far as "quality" is concerned (Ghobadian et. al, 1994).

The determinants of service quality focus on interactions between a service organization and its customers and typically related to technical dimension, where it is the outcome of the service process to include systems and technology, to functional dimension, where it is the way in which the service is delivered to include inter-personal interactions, and to the corporate image dimension which is the result of how customers perceive a company (Lewis, 1991). The service marketing literature of the 1990s has advocated customer service excellence and prescriptions for improving service quality as a way to enhance customer satisfaction and loyalty leading to increased competitiveness and profitability (Newman, 2001). It is widely accepted that quality products and services produce benefits not only by lowering costs through reduced waste and decreased deficiencies in product and service, but also by increasing competitiveness through the establishment of a good reputation and the attraction and retention of customers (Wang et al., 2003).

Customer satisfaction is another important aspect for a service organization. It is highly related with service quality. As service quality improves, the probability of customer satisfaction increases. Customer satisfaction is increasingly and mainly recognized as a main ingredient for success in the market places (Weiser, 1995). Increased customer satisfaction and customer retention causes profits to improve, a positive word-of-mouth, and lower marketing expenditures (Reichheld, 1996; Heskett et al., 1997).

Superior service quality and high levels of customer satisfaction are seen as two major goals by service providers in order to enhance their business performance (Sureshchandar et al., 2002). The nature of the exact relationship between service quality and customer satisfaction is still shrouded with uncertainty although the relationship between the two has received considerable academic attention in the past few years (Sureshchandar et al., 2002). As a result of higher service quality and higher customer satisfaction, it is proved in the literature that customer loyalty towards companies will also increase (Arasli et al., 2005). Therefore, it is very important for companies to retain their customers; this can only be achieved by increasing service quality level, customer satisfaction, and customer loyalty towards their companies. In the literature, it has been also proved that higher customer satisfaction and higher customer loyalty do also result in higher financial performance and higher profitability in the companies (Keisidou et al., 2013). Therefore, there is important question if customer satisfaction and customer loyalty will really result in higher financial performance of the companies.

The tourism industry has been developed rapidly in North Cyprus during the last two decades. According to the TRNC state planning organization, number of tourists reached more than 1.1 million in 2012 with tourism contributing to the gross domestic products of North Cyprus of more than 8.5%. Therefore, tourism industry of North Cyprus is a hot sector for researchers. Searching the determinants of financial performance in tourism and hospitality nowadays is a trending issue for scholars.

The aim of this research is to examine the impact of customer satisfaction and customer loyalty on financial performance in the tourism industry of North Cyprus. Therefore, investigating the determinants of financial performance of hotels and travel agencies in North Cyprus would be an interesting research area. There are very rare studies in this field that Keisidou et al. (2013) is one of them. Thus, the issue is still hot in such an interesting country. To the best of our knowledge, this study is the first of its kind in the literature of tourism. Therefore, results from this research study will be an original contribution to the literature.

2. LITERATURE REVIEW

Researchers sought to understand the relationship between customer satisfaction, loyalty, and financial performance. Most companies in the market are trying to gain a wide base of customers, to keep those customers by satisfying their needs and to develop their products and services to enhance the chances of the customers' coming back to the same company. In other words, Customer satisfaction is crucial for companies to grow and compete in the market. Naumann, (1995) drew the attention to the fact that it costs 80% less in money, time and resources to keep a customer rather than to attain a new customer. Therefore, customer satisfaction increasing and customer relations to retain the customer can be a good strategy for the company to grow and to survive the competition. In addition, customer satisfaction is a major criterion in the characteristics of the quality aspect of goods and services offered to the customer (Vavra, 1997), and according to Anderson and Sullivan (1993), there is an increasing interest in customer satisfaction as a way of measuring quality. Moreover, customer satisfaction is seen as the measurement that is generally accepted around the world (Morgan et al., 2005) as well as an indicator of the competition profile of the company and the strength of its marketing strategy (Kaplan and Norton, 1996). Customer satisfaction concept has been studied by a vast number of researchers due to its importance to the companies and the marketing sector. According to Oliver (1980), when a customer buys a good or a service from any company, he will have pre-purchase expectations about the good or the service quality and performance, so after the good or service has been bought and used, outcomes of it are compared to the expectation, if the outcome is in line with the expectations, the customer will have confirmation. Disconfirmation is created in the case of different outcome than the expectation. Disconfirmation has two possibilities, positive disconfirmation which arises when the outcome is better than the expectations and negative disconfirmation which occurs when the outcome is worse than the expectations. Customer satisfaction is created by either confirmation or positive disconfirmation. This is called expectancy disconfirmation theory which was studied and confirmed by many researchers (Oliver and DeSarbo, 1988; Pizam and Ellis, 1999; Tse and Wilton, 1988).

Another definition was proposed by Vavra (1997) where he suggested that customer satisfaction is the end-state of the consumption process. This end-state can differ in shape as it can be a state of reward, an emotional outcome of the process, or a comparison between the expected rewards and costs with the real ones. Customer satisfaction topic was researched widely in the last three decades (Luo and Homburg, 2007). Keiningham, Munn, and Evans (2003) found that most academicians and professionals accept that customer satisfaction affect the consumer behavior to a positive attitude towards the business. Researchers surveyed the theoretical concepts of consumer satisfaction and the consequences of it (Anderson and Sullivan, 1993; Bolton and Lemon, 1999; Fornell et al., 1996; Luo and Bhattacharya, 2006; Oliver, 1980; Oliver, 1997; Rust et al., 2004; Szymanski and Henard, 2001).

The literature on customer satisfaction outcomes has four divisions as the researchers found. The outcomes are: customer related outcomes, efficiency related outcomes, employee related outcomes, and overall performance related outcomes. The positive relationship between customer satisfaction outcomes and financial performance is explained by the first three categories. The largest section of the literature is examining the customer related outcomes, in this regards, researchers found that customer satisfaction increase customer loyalty and better the chances of customer retention which in turn influence the probability of future purchases (Fornell et al., 1996; Mittal and Kamakura, 2001; Mittal, Ross, and Baldasare, 1998; Olsen, 2002). Naumann (1995) noted that the cost of keeping customers and strengthening the relationship with existing customers is much less than the cost of gaining new customers. Therefore, customer satisfaction which has a direct relationship with the retention of customers saves costs on the company and gives the company the ability to increase profitability in the future. Moreover, Anderson and Sullivan (1993) found that there is a positive relationship between repurchases and customer satisfaction. The authors found that when a customer is satisfied, the number of repurchases in the future increases. In addition, Homburg, Koschate, and Hoyer (2005) and Stock (2005) noted that customer satisfaction can affect pricing of services and enhance profitability of the firm. The authors noted that satisfied customers tend to accept the payment of premium prices and have less sensitivity towards prices. Luo and Homburg (2007) found that customer satisfaction leads to good word of mouth advertisement for the company which in turn will save marketing costs in the future. They also found a relationship between customer satisfaction and human resource of the company in form on a positive relationship. These findings suggest that customer satisfaction would better the marketing process in the future and lower the costs of advertising investment.

Over the years, researchers identified factors that influence customer satisfaction and loyalty, one of the examples is service quality which researchers believe that it has a strong positive relationship with customer satisfaction (Bojanic and Rosen, 1994; Taylor and Baker, 1994; Levesque and McDougall, 1996; Johnston, 1997; Lassar et al., 2000; Oppewal and Vriens, 2000; Jamal and Naser, 2002; Ndubisi, 2006; Arbore and Busacca, 2009; Culiberg and Rojsek, 2010; Saleh and Ryan, 1991). Parasuraman, Zeithaml and Berry (1985) have developed a model to study service quality. The authors noted that service quality consists of five dimensions (See Figure 1). First dimension is reliability, which is defined as the ability to achieve the promised service with accuracy and dependability. Second dimension is assurance, which is defined as the knowledge of employees and their trustworthy and confident personality. Third dimension is tangibles, which refers to the shape and overall look of the facilities, employees, equipment, and overall prestige of the company. Fourth dimension is empathy, which means the customized service provided to the customer to provide attention and caring to customers. The last dimension is responsiveness, which happens after the service or product is bought, and means the care, attention and help that is provided to customers to assure fast service. The authors called these dimension as the SERVQUAL model.

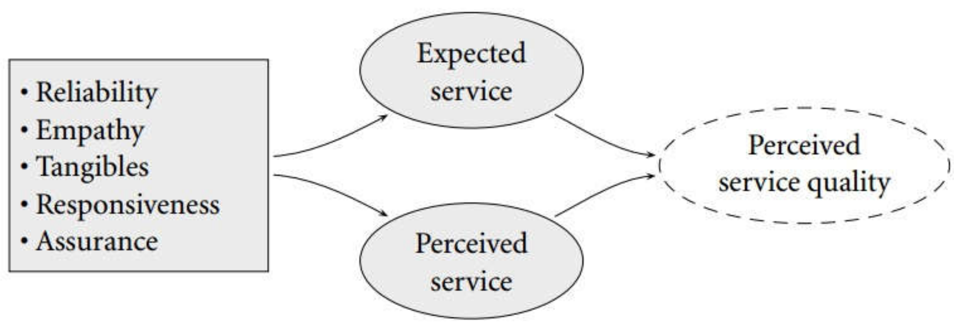

Figure 1.
SERVQUAL MODEL

Researchers used the SERVQUAL model extensively to assess the relationship between these dimensions and customer satisfaction. Most of the researchers found that the relationship is positive (Ananstasiadou, 2009; Arasli et al., 2005; Carman, 1990; Culiberg and Rojsek, 2010; Ehigie, 2006; González, Comesaña and Brea, 2007; Hu, Kandampully, and Juwaheer, 2009; Ladhari et al., 2011; Naik, Gantasala, and Prabhakar, 2010; Saleh and Ryan, 1992; Shemwell, Yavas, Bilgin, 1998) While small number of researchers found that the SERVQUAL elements does not affect customer satisfaction (Kheng et al., 2010). Culiberg and Rojsek (2010) investigated the relationship between service quality and customer satisfaction using the SERVQUAL model. They included the five traditional factors alongside with access and found that all factors have a strong positive relationship with customer satisfaction with assurance and empathy factors being the strongest. Ladhari et al. (2011) also used SERVQUAL model to investigate the service quality dimensions in Tunisia and Canada. Their findings suggest that tangibles have no effect on customer satisfaction and loyalty. In addition, empathy was found to be the strongest factor affecting satisfaction in Canada, while in Tunisia, responsiveness and reliability were the most influential factors on both satisfaction and loyalty. Korda and Snoj (2010) examined the relationship that exists between customer satisfaction, service quality and value. The authors found a positive relationship between satisfaction and service quality and value.

In the literature on the relationship between customer satisfaction and financial performance, the general stream is supporting that an increase in the customer satisfaction will result in a higher financial performance in the future and enhances the profitability of the company (Anderson et al., 1997; Grewal, Chandrashekaran, and Citrin, 2010; Gruca and Rego, 2005; O'Sullivan and McCallig, 2009; Tuli and Bharadwaj, 2009). Kotler (1991) noted that an increasing customer satisfaction is one of the best measurements of the company's future profitability. Anderson, Fornell, and Lehmann (1994) noted that customer satisfaction results from a sample of 77 Swedish companies has a positive relationship with return on investments and enhance the profitability of these firms. The same results were found by Rust, Moorman, and Dickson (2002) with a positive relationship between customer satisfaction and financial performance indices (return on assets and return on investments). Nelson et al. (1992) showed that higher customer satisfaction results in high return on assets, earnings and net value. Moreover, Rust and Zahorik (1993), and Ittner and Larcker (1998) found that there is a positive relationship between customer satisfaction and financial performance proxies (return on investments and operating margin). However, other researchers found that the relationship between customer satisfaction and financial performance is mixed, negative, or indecisive (Anderson, Fornell, and Lehmann, 1994; Foster and Gupta, 1997; Ittner and Larcker, 1998; Tornow and Wiley, 1991; Wiley, 1991). Tornow and Wiley (1991) found that customer satisfaction affects the firm's profitability in a negative way. Foster and Gupta (1997) performed their analysis on wholesale beverage distributor and found that the relationship between customer satisfaction and financial performance is positive, indecisive or negative depending on the questions included in the customer satisfaction measurement. Anderson, Fornell, and Lehmann (1994) found a positive relationship between customer satisfaction and financial performance in the case of manufacturing companies. However, they found that the relationship is weak or negative in the case of service companies.

Hospitality and tourism companies are a big section of the service industry, and like most of service companies, their assets mostly consists of intangible assets which are used to satisfy customers. Customer satisfaction is the number one goal of the tourism and hospitality industry and the outcome of the operations of tourism companies. Fornell et al,. (1996) noted that the increase in customer satisfaction can increase performance of the company. The literature focused on the effects of customer satisfaction on profitability of companies in general, and tourism and hospitality industry had its share from studies. Studies did not reach conclusion on the relationship between profitability of the company and customer satisfaction, some researchers said that the relationship is positive (Banker, Potter, and Srinivasan, 2000; Denizci and Li; 2009) while others found that the relationship is negative or indecisive (Gursoy and Swanger; 2007; Schneider, 1991). Banker, Potter and Srinivasan (2000) studied a sample consisting of 18 hotels and found that the relationship between future accounting performance and customer satisfaction is positive. A more recent study done by Denizci and Li (2009) asserts that the relationship between financial performance and customer satisfaction. The authors found that customer satisfaction is highly related to financial performance such as return on assets and Tobin's q. On the other hand, Gursoy and Swanger (2007) noted that increasing customer service does not mean increasing future financial performance for hospitality and tourism businesses. The authors explained that because customer satisfaction is the core outcome of the tourism industry, customers expect to be satisfied after getting any service from the company and that hospitality and tourism companies cannot survive without customer satisfaction. Moreover, to increase customer satisfaction, companies will have to spend money on training the staff, enhancing facilities and improving the services as a whole which in turn increase costs and might potentially decrease future financial performance of the company.

The literature on brand loyalty is vast and still growing because of its benefit on existing customers and the fact that it is one of the most effective measures in marketing (Knox and Walker, 2001). According to Jacoby and Chestnut (1978), in the long run, the determinant of the success of a brand is the number of customers who become regular buyers and not the number of buyers who only buys once. Loyalty has many benefits which Reichheld (1996) has noted in his paper. First, it stimulates financial performance of the company as more profit is generated from a loyal customer; second, it minimizes the advertising and marketing costs as firms spend high costs on marketing to attain new customers and raise the sales of the company but for loyal customers these costs are minimized. Third, it increases word of mouth (referrals) as loyal satisfied customers will spread good word of mouth about the company and recommend its products to their contact which is an important source of new customers to the company. In addition, customers who come through recommendation tend to become loyal customers themselves. Fourth, it increases the profit margin of the company as loyal customers are willing to pay more for the trusted goods or services that the company offers and will not substitute away from the company with discounts from competitors. Fifth, loyalty increases the growth of revenue per customer as loyal and satisfied customers will tend to try other products or services that the company is offering and their spending grow over time. Sixth, it reduces the operational expenses as loyal customers are familiar with the company's products and services and they will not need extra inquiries or information from employees of the company. Kandampully and Suhartanto (2000) also assured on the importance of loyalty in the tourism industry. The authors studied the relationship between customer satisfaction and loyalty and found that in the competitive nature of the tourism industry, for hotels to gain a competitive advantage they have to adapt one of two strategies; either to discount their prices to gain price advantage over other hotels, or to work on developing brand loyalty through offering unique services to their customers. The first strategy of discounting prices shows negative effects in the medium and long run as it affects the profitability of the hotel. Therefore, the authors found that brand loyalty is the adequate option for hotels. In addition, Tepeci (1999) argues that in a mature market like the hospitality industry, hotels should pursue a strategy that increases the market share profit rather than market growth gains. The profitable approach is to increase customers' loyalty instead of using other marketing strategies like price discount or advertising. The author explained that brand loyalty cuts expenses as it is less costly to deal with loyal customers as they are familiar with the products of the hotel which in turn will cut operational cost.

Numerous numbers of researchers studied the relationship between financial performance and other factors such as quality and convenience, but not many studies have emerged examining the relationship between customer satisfaction, loyalty and financial performance of companies. One of the pioneer studies on financial performance of companies was the profit impact of market share by Buzzell, Gale, and Sultan (1975). The study concluded that market share is one of the most important factors to increase profitability. This result and other similar papers results have pushed companies in the 1980s to try to enlarge their market share by mergers and acquisitions. However, companies who did not have a large market share showed good financial performance. The best example is Southwest Airlines, which did not have a large market share but always had a good financial performance. The management of Southwest Airlines focused on customer loyalty instead of market share. Their analysts estimated that an increase of five points in their customers' loyalty will lead to an increase in profits by 55% with a standard deviation of 30%. Reichheld (1996) also argue that market share is not the prime cause of high profitability. The author identified a series of financial effects of loyalty on the company. First, sales and the market share of the company will increase as loyal customers repurchase products and services. Second, the growth in the company's profitability allows the company to attract and keep the most qualified employees. Third, loyal employees reduce operational costs as the quality of the service provided is higher with time. Fourth, loyal investors act like business partners as they decrease costs of the company, increase efficiency, and stabilize the company. Prus and Brandt (1995) stated that a loyal customer is the customer that acquires the highest level of satisfaction, recommends the brand and product, and has the intention to continue purchasing the service or product in the future. The authors called this customer the "secure customer".

In general, researchers divided the literature on customer satisfaction, loyalty and financial performance into two broad categories. The first is the service management which states that the relationship between loyalty and financial performance is a positive direct relationship and the relationship between customer satisfaction and financial performance is indirect positive relationship through loyalty (Reichheld and Sasser, 1990). This division is supported by many researchers, for instance, (Anderson and Fornell, 1994; Storbacka et al., 1994; Rust et al., 1995; Schneider and Bowen, 1995; Hallowell, 1996; Zeithaml et al., 1990). A satisfied customer will lead to recommendations and to the increase of loyalty to this brand, when loyalty increases, revenues will grow as repurchases increase and therefore the profitability of the company will increase (Chi and Gursoy, 2009).

3. DATA AND METHODOLOGY

The data collection process employs the convenience sampling technique due to the restricted access to the actual number of consumers. The survey was of two parts. The first part focused on the demographic information of the respondents, and the second part focused on latent factors. The sample size of this study was 465. The individuals who answered this survey were tourists in the North Cyprus. Survey collectors approached people asking them if they wanted to participate in a survey about tourism, and they waited for the participants to finish the survey and then collected it back from them. 465 surveys were collected, while only 414 surveys qualified after removing surveys completed by people who did not qualify, not completed surveys, and useless surveys (same answer for all questions). This paper followed a rule suggested by Hair et al. (2008) that a sample size should be at least five times the number of items in the questionnaire. The variables were measured by a 5-point Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree). The respondents' demographics can be summarized that 188 respondents were males, while the rest of the respondents were females (45.4% males, 54.4% females). In terms of nationality, 36.5% of the respondents were from Turkey, 48.1% were Turkish Cypriot and 15.5% from other countries.

The data collected went through several stages of analysis as per the process of Structural Equation Modelling (SEM). In SEM, the factor analysis technique and the path analysis technique are combined to explain the type of interrelation between the latent variables, which will be determined by more than two items (Hair et al., 2010; Whittaker, 2011). Also SEM has the ability to measure the reliability and the validity of the data and the model created and the model fit (Hair et al., 2010).

The process started with factor analysis so the underlying relationship between variables can be identified. EFA is a statistical mechanism used to understand the link between the variables and their loading into a single factor (Hair et al., 2010). Hence, the study will run factor analyses and provide the results and the reliability and validity of each tool. In EFA, the Maximum likelihood method and Varimax rotation method was used and the reliability and validity of the model was registered. For validity testing, the approach of Hu and Bentler (1999) was used and the maximum likelihood estimation was adopted. The Average variance extraction (AVE) was used to define convergent validity, and for the discriminant validity, the construct reliability (CR) test was used. CR => 0.7, and AVE > 0.50 were accepted in this study (Hu and Bentler, 1999). In the Structural equation modelling stage, the inter-relations between the exogenous factors and the endogenous factors were tested using a one-way effect relationship. Using Amos 23, the relationship and the parameters were tested again.

Data screening was conducted and 51 surveys were eliminated due to achieving less than 95% completion (Hair et al., 2010) , or they are repetitive answers.

As per Kline (2015), an absolute value greater than 3 is considered skewed. In this study there was no skewness value of more than absolute 1. Regarding kurtosis, the benchmark value is 10, as per Kline (2015), in this study; the highest registered kurtosis was less, which makes the data adequate for testing. The data analysis was done in two stages. The first stage considered the relationship between the underlying latent factors and the observed variables, the correlation between these factors and the error correlation (if required) using Factor analysis. The second stage included the causal model between the endogenous and the exogenous factors using SEM. The assessment of the model fit was taken for the entire model instead of each construct. The assessment of reliability and validity was conducted in the model. Post this stage, a test can be conducted to understand whether the data concurred with the theoretical model. (Hair et al., 2010).

4. EMPIRICAL RESULTS

SPSS Amos 24 was used to analyse the data. A factor analysis was conducted on the data and 5 factors were generated, all factors had a loading average of 0.7 and the Cronbach's alpha was calculated to measure validity at this point. Cronbach's alpha for each factor exceeded 0.7 (Hair et al., 1998). This included most of the variables and few variables was excluded. Table **1** shows the details of factor loading and alphas.

The factor loading showed 5 main factors with good loading. The factor loading generated the following factors:

1- SERVQUAL 1
2- SERVQUAL 2
3- Customer Satisfaction
4- Customer Loyalty
5- Firm Performance

Table 1. Factor analysis, Cronbach alpha and KMO

FACTOR	LOADING	ALPHA
SERVQUAL 1		*0.947*
B1	*0.689*	
B2	*0.689*	
B3	*0.677*	
B4	*0.763*	
B5	*0.755*	
B6	*0.663*	
B7	*0.691*	
B8	*0.737*	
B9	*0.56*	
B10	*0.669*	
B11	*0.606*	
SERVQUAL 2		*0.935*
B16	*0.735*	
B17	*0.593*	
B18	*0.685*	
B19	*0.541*	
B20	*0.622*	
B21	*0.67*	
B22	*0.624*	
B24	*0.53*	
B27	*0.653*	
B30	*0.644*	
B31	*0.562*	
B32	*0.549*	
SATISFACTION		*0.929*
C1	*0.58*	
C2	*0.673*	
C3	*0.762*	
LOYALTY		*0.927*
C4	*0.853*	
C5	*0.909*	
C6	*0.796*	
PERFORMANCE		*0.932*
ROE	*0.876*	
ROA	*0.909*	
NPM	*0.887*	

Notes: Maximum Likelihood analysis with Kaiser normalisation, Varimax rotation, KMO = 0.933; Bartlett's test of Sphericity = $\chi 2$ = 12580.722 (p=0.000), To check the adequacy of the sample for factor analysis, the KMO (Kaiser-Mayer-Olkin) test and the Bartlett's Sphericity tests were performed on the data. For KMO, the value has to be higher than 0.5 in order to be accepted for factor analysis and the pairs of variable correlations would be explainable by other variables. As for the Bartlett's Sphericity test, the result should be significant in order to reject the null hypothesis that the variables are uncorrelated. In this research, the KMO was 0.933 which makes it adequate for the factor analysis. Furthermore, the Bartlett's Sphericity test was significant (X2 = 12580.722, df = 496, $p < 0.01$), so the null hypothesis is rejected, and the variables are correlated, Table II shows the details.

As per the rule, RMSEA should be equal to or less than 0.07 and CFI is more than 0.92 (Hair et al., 2010), and SRMR less than 0.09 when TLI is more than 0.95 (Hu & Bentler, 1999); these conditions have to be met to claim the goodness of fit. The model fitted with GFI = 0.909, NFI = 0.919, IFI = 0.977, TLI = 0.970, CFI = 0.977, RMSEA = 0.45.

As per Hair et al. (2010), testing reliability and validity of the constructed model is done by calculating the construct reliability (CR), average variance extracted (AVE) and discriminant validity.

The CR is calculated based on the factor loading (the squared sum) for every construct and the sum of errors of the same construct (Hair et al., 2010).

It should be more than 0.7 to represent a good reliability. While the AVE represents the sum of squared multiple correlation divided by the items (variables) in each construct (Hair et al., 2010), it should be => 0.5 to be considered valid. The discriminant validity was tested by comparing the correlation between the factors and the square root of AVE. The correlation should not exceed 0.85 (Kline, 2015; Yousafzai et al., 2010). The square roots of AVE should exceed the values of the correlations (Hair et al., 2010), and the maximum shared variance MSV is < AVE (Hu & Bentler, 1999).

Table 2 provides the CRs, the AVEs and the MSV and the square roots of AVE on the shaded diagonal. Table II shows that the model passed all reliability and validity tests and as the correlation is < 0.8, the model proved to be free of multicollinearity (Hair et al., 2010).

Table 2. Reliability and Validity measurements

	Model Validity Measures								
	CR	AVE	MSV	MaxR(H)	serv1	serv2	performance	Satisfaction	Loyalty
serv1	0.944	0.805	0.739	0.948	0.778				
serv2	0.935	0.751	0.739	0.944	0.860***	0.742			
performance	0.935	0.827	0.114	0.935	-0.096†	-0.130*	0.909		
Satisfaction	0.93	0.817	0.207	0.937	0.379***	0.367***	0.338***	0.904	
Loyalty	0.934	0.824	0.628	0.936	0.770***	0.793***	-0.201***	0.456***	0.908

After confirming the reliability and validity of the model, the causal relationships between the factors were drawn using SEM. This is the original model representing the underlying theoretical model. The paths cover the hypotheses to understand the relationship and test these hypotheses. In Figure 3, based on the rule, RMSEA should be equal to or less than 0.07 and CFI is more than 0.92 (Hair et al., 2010), and SRMR less than 0.09 when TLI is more than 0.95 (Hu & Bentler, 1999); these conditions have to be met to claim the goodness of fit.

As per the results, the model was found to fit with X2/df = 1.357, GFI = 0.909, NFI = 0.919, IFI = 0.977, TLI = 0.970, CFI = 0.977, RMSEA = 0.45, Standard RMR = 0.0478

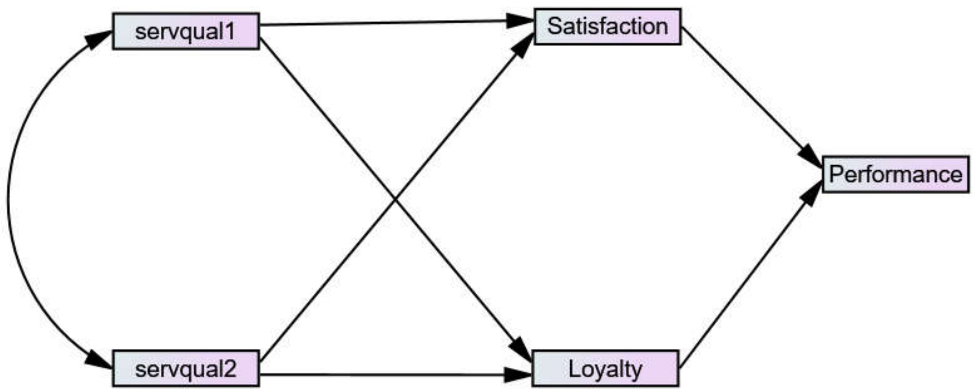

Figure 1.
The proposed structural model with estimated standardized path coefficients

Once the model was finalized and fit, the path coefficients were tested. Table **3** provides information about all the coefficients, the significance and the critical ratio.

Table 3. Path Coefficients

Destination		**Origin**	**Standardized**	**S.E.**	**C.R.**	**Hypothesis support**
Satisfaction	<---	servqual1	0.319***	0.073	5.299	H1 supported
Loyalty	<---	servqual2	0.167*	0.151	1.626	H2 supported
Satisfaction	<---	servqual2	0.547***	0.071	9.066	H1 supported
Loyalty	<---	servqual1	0.26*	0.156	2.53	H2 supported
Performance	<---	Loyalty	0.562***	0.035	3.257	H4 supported
Performance	<---	Satisfaction	0.465***	0.044	0.968	H3 supported

Note: ***and *denote significance at the 0.01 and 0.05 levels, respectively

Two factors (SERVQUAL 1 and 2) were tested to understand their indirect effect on Performance mediated by Satisfaction and Loyalty; this is consistent with the theoretical model of this study. Those factors did not have any direct effect on performance and hence they will be tested for full indirect effect. As per Cohen (1988), the standardized path coefficient of values less than 0.1 show a small indirect effect. While values of .30s show a medium effect and values equal to or above 0.5 shows a major effect. Table 4 provides the indirect effects and the significance of each of them. Tested factors have significant but low effects (0.1). Furthermore, the squared multiple correlation (R^2) was extracted for each endogenous variable. As per Cohen (1988), R^2 indicates the size of the predicted variable for each endogenous variable. Values of .01, .09 and .25 represent small, medium and large prediction respectively (Cohen, 1988). In this study, the R2 is .17 for Loyalty, .22 for Satisfaction and .19 for Performance.

Table 4. Testing Indirect Effects

DESTINATION		ORIGIN	STAND INDIRECT EFFECT (THROUGH ATTITUDE)	RESULT	**HYPOTHESIS SUPPORT**
PERFORM	<---	SERVQUAL 1	0.096***	full indirect effect	H5 & H6 supported
PERFORM	<---	SERVQUAL 2	0.092***	full indirect effect	H5 & H6 supported

Note: ***and *denote significance at the 0.01 and 0.05 levels, respectively

The results showed that all the hypotheses are supported. The results also showed that two factors, namely Satisfaction and loyalty, have significant direct effects on the hotel performance and this is in line with previous studies like (Arshad, Zahra, & Draz, 2016; Sayani, 2015). Servqual presented by two factors has positive significant effect on customer satisfaction and loyalty, this is in line with several previous studies showing that the service quality of the hotel positively correlates with the satisfaction of customers and their loyalty (Jabnoun & Khalifa, 2005; Rashid, Hassan, & Ahmad, 2009). Also, the service quality of the hotel reflected on the financial performance of the hotel indirectly through customer satisfaction and loyalty. This reflects the importance of service quality for the tourism industry to enhance the financial performance of this sector.

The results of this study also confirm that satisfaction and loyalty are reliable mediators. This finding is consistent with (Keisidou, Sarigiannidis, Maditinos, & Thalassinos, 2013)that prove the importance of satisfaction and loyalty as mediating factors in consumer research. This proves that the effect of service quality can be mediated by customer satisfaction and loyalty. With regards to the fitness of the model, R2 reached 0.19 for performance, which can be considered as high and R2 of loyalty is 0.17 and for satisfaction is 0.22, indicating large predictions of these variables.

5. CONCLUSION

This study examined the impact of customer satisfaction and customer loyalty on financial performance in the tourism industry of North Cyprus. The study relied on surveys that are answered by tourists in North Cyprus and amounted to 465 surveys. The study started with factor analysis so the underlying relationship between variables can be identified. Afterwards, the assumptions of structural equation modelling were checked with data screening, checking skewness and kurtosis. Then, structural equation modelling was applied to the data.

The study provides the factors affecting hotel financial performance in Turkish Cypriot. The results show that SERVQUAL has a positive effect on both customer satisfaction and customer loyalty. Moreover, the study shows the positive effect of service quality factors on customer satisfaction and loyalty towards a hotel. And the direct effect of customer satisfaction and loyalty on the hotel financial performance. The study also demonstrated the indirect effect of service quality factors on the hotel financial performance.

The study contributes to the literature in several areas. First, the study contributes to the behavioral study of consumer by adding the factors affecting his satisfaction and loyalty. Second, the study enhances the understanding of customers' satisfaction and loyalty on financial performance. Third, the study provides a proof of the importance of satisfaction and loyalty as a mediator between several factors and the financial performance of hotels.

Overall, the results show the positive direct and indirect effects of service quality factors, customer loyalty, and customer satisfaction on the hotel financial performance. Therefore, hotel management should focus on service quality to enhance both customers' satisfaction and loyalty which leads to the increase in the overall profitability of the hotel. Service quality enhancement can be through the improvement of customer service, customer experience in the hotel, online hotel services, quality control over all the areas of the hotel, and better communication channels in the hotels. Moreover, the policy makers of North Cyprus should maintain the necessary infrastructure and enhance the public transportation system as well as the public utilities in order to attract more tourists to come to North Cyprus.

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