The Effect of Product Quality and Price Fairness through Customer Loyalty on Local Skincare in Indonesia

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ABSTRACT

Objective - This study discusses the emergence of various local skincare companies that manufacture high-quality products at a fair price and have successfully attracted customer loyalty through their customer engagement. This paper aims to identify the effect of Product Quality and Price Fairness on Customer Loyalty and Customer Engagement as intervening variables in local skincare products.

Methodology/Technique - This study used quantitative methods. The data collection technique is questionnaires distributed to 171 skincare users. All the data is processed with Path Analysis using double-multiple linear regression SPSS.

Findings – The results are that Product Quality and Price Fairness have a significant effect on Customer Engagement and Customer Loyalty, Product Quality does not have a significant effect on Customer Loyalty, and Product Quality has a significant effect on Customer Loyalty through Customer Engagement. In contrast, Price Fairness does not significantly affect Customer Loyalty through Customer Engagement.

Novelty - This research novelty is filling the gap of previous research by combining the direct effects of Product Quality and Price Fairness from several studies focusing on Customer Engagement as mediation to Customer Loyalty.

Type of Paper: Empirical

JEL Classification: F44; M20; M30.

Keywords: Customer Engagement; Customer Loyalty; Price Fairness; Product Quality; Skincare.

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1. Introduction

The cosmetics industry is rapidly evolving in the present times. Statista says skincare products are the most popular and account for 37% of the cosmetics industry. The global market for skincare products is projected to grow at a CAGR of 4.7% from 2016 to 2022 and is estimated to reach USD 179 billion by 2022 (Lee et al., 2019). Indonesia’s National Agency of Drug and Food Control (BPOM) has recently introduced a Gradual Fulfilment Certificate for cosmetic companies to improve the quality of locally produced cosmetics. Nowadays, customers who use skincare products are knowledgeable and seek high-quality products at a reasonable price. Companies are facing tough competition and, as a result, are increasingly implementing various customer retention strategies to maintain their customer base.

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During the 1990s and early 2000s, companies achieved customer loyalty to a large extent by building customer relationships. Nonetheless, following the trends, companies are now transitioning from a traditional approach to customer relations to an evolving philosophy of customer retention (Bei & Chiao, 2001). Research supporting this claim shows that customer engagement can improve user retention, which is, to a certain extent, a reflection of customer loyalty (Hu et al., 2021). The concept of customer engagement refers to the extent of a customer's interactions and associations with a brand or a company's offerings and initiatives, often encompassing social network interactions beyond purchases (Vivek et al., 2014). According to Apoorv Sood, Vice President of Web Engage, nowadays, a coordinated, multi-channel approach supported by data-driven strategies, AI analytics, and automation can enhance customer loyalty through various interaction and connection methods, potentially increasing conversions by as much as 25%.

Product Quality and Price Fairness are also believed to affect Customer Loyalty. Good Product Quality is the beginning of a positive customer response to the product and the customer's interest in staying loyal to the product (Keller, 2008), and price can be said to be fair if the transaction process performed by the client is reasonable and acceptable based on the results obtained (Bolton et al., 2002). To make customers feel that the prices offered are fair, companies can transparently allow customers to rate and review prices compared to competitors. Fair and transparent pricing (Dhasan & Aryupong, 2019) can earn engaged and loyal customers. In line with a previous study, Product Quality (Xhema et al., 2018) and Price Fairness (Bei & Chiao, 2001) have a considerable impact on Customer Loyalty, as does Customer Engagement (Panjaitan, 2017).

This study has provided insights into the attribution theory about factors such as Product Quality, Price Fairness, Customer Engagement, and Customer Loyalty in the scope of International Business Management with a specific focus on the local skincare industry in Indonesia. Furthermore, the practical implications of this study can assist local skincare companies in addressing challenges related to the mentioned variables by offering possible solutions. Thus, this study aims to address the existing research gap by examining the difficulties companies face in retaining Customer Loyalty through buying various factors as Product Quality, Price Fairness, and Customer Engagement, which are believed to impact Customer Loyalty. Additionally, the research aims to evaluate how Product Quality and Price Fairness indirectly influence Customer Loyalty via Customer Engagement.

Similar research (Noerindah & Bernarto, 2022) only discussed the direct effects of variables and did not incorporate any intervening variables to assess the indirect specific local skincare brands. Moreover, a study by (Dhasan & Aryupong, 2019) produced conflicting results compared to previous research conducted by (Nguyen et al., 2016; Parihar et al., 2019).

The subsequent sections of the study are structured as follows: Section 2 contains a literature review, followed by the methodology and hypothesis development sections in Section 3. The results and discussion are presented in the subsequent section, while the last section considers the implications, and limitations, and provides suggestions for future research.

2. Literature Review

2.1 Product Quality and Customer Engagement

Product quality is a product or service's general characteristics and properties that affect its ability to satisfy explicit or implicit needs (Panjaitan, 2017). Keller's 2008 study showed that brand judgments often start with positive perceptions of quality (product), but almost always require attitudinal engagement to achieve customer loyalty. The customer engagement process begins with the customer's need for product/service/company information, which requires an interactive relationship and a sense of belonging (Brodie et al., 2013). A study by (Dhasan & Aryupong, 2019; van Doorn et al., 2010) showed a direct effect of higher perceived Product Quality and Customer Engagement. In order to simplify the shopping process for consumers and ensure that they prioritize Product Quality when choosing to use local skincare products, it is
imperative to have a dedicated and involved customer base. Therefore, the hypothesis which will be analyzed is:

**H1:** *Product Quality in skincare has a positive effect on Customer Engagement.*

### 2.2 Price Fairness and Customer Engagement

Price Fairness refers to how consumers perceive whether the difference between a given price and either a socially accepted price or the price offered by a comparable seller is reasonable, acceptable, or justifiable (Matzler et al., 2007). Thus, sales prices may be compared with the usage experience before purchase. Price Fairness comparisons can motivate customers to participate in verifying Price Fairness (Andrés Martínez et al., 2013; as cited in Dhasan & Aryupong, 2019). Price is a crucial indicator of customer negotiability; the prices offered by online service providers can affect online community involvement (Nguyen et al., 2016). Based on the conclusion, Price Fairness is positively related to Customer Engagement (Nguyen et al., 2016).

This study aims to determine whether the prices of local skincare products are considered acceptable by the Indonesian market and whether they are effective in engaging customers. Therefore, the following assumptions are made:

**H2:** *Price Fairness in skincare has a positive effect on Customer Engagement.*

### 2.3 Product Quality and Customer Loyalty

Product quality is a product or service characteristic determined by its ability to meet an explicit or implicit customer need or desire (Kotler & Armstrong, 2017). The higher the involvement of the customer, the alignment of the customer’s Product Quality expectations that the customer wants with the reality that is obtained or felt by the customer will make them loyal to the brand of the product. When the level of consistency exceeds customer expectations and leads to customer loyalty, the perception of product quality improves (Dhasan & Aryupong, 2019). Customer Loyalty can be improved by better understanding customer perceived quality (Kenyon & Sen, 2012). Thus, we have put forth the subsequent suppositions:

**H3:** *Product Quality has a positive effect on Customer Loyalty.*

**H6:** *Product Quality positively affects Customer Loyalty through Customer Engagement.*

### 2.4 Price Fairness and Customer Loyalty

A study stated that if the price the customer receives is fair enough, the company can provide transparency to the customer when comparing prices, and the customer will feel the fairness between the price and the product received, thereby increasing Customer Loyalty (Nainggolan & Hidayat, 2020). Another also said that a transparent form of Price Fairness helps retain customers and build loyalty (Dhasan & Aryupong, 2019). Customer loyalty is crucial for a company's survival and competitiveness. Building Customer Loyalty necessitates a company's commitment to maintaining the highest possible quality for each product or related service, thereby embracing a solid reputation for quality in customers’ minds. As local skincare grows and becomes more competitive, we also want to know whether fair prices foster loyalty. Therefore, based on the previous study, the hypothesis which will be analyzing is:

**H4:** *Price Fairness has a positive effect on Customer Loyalty.*

**H7:** *Price Fairness positively affects Customer Loyalty through Customer Engagement.*
2.5 Customer Engagement and Customer Loyalty

Study reveals that Customer Engagement may enhance the user retention rate (Hu et al., 2021), and user retention mirrors Customer Loyalty to an acceptable level as reported by (Brodie et al., 2013). Customer Engagement is possible as an independent variable for Customer Loyalty (Hu et al., 2021). Higher fit will result in more connected customers with the company and emotional commitment between them, which leads to higher Customer Loyalty. A study shows that Customer Engagement builds Customer Loyalty and has a significant positive impact on customer retention. Customer Loyalty can be used to create value and improve customer retention. From the customer's point of view, “the level of commitment depends on the customer's evaluation of the user experience.” Hereafter, a study by (So et al., 2016a) showed that Customer Engagement positively impacts Customer Retention. Local skincare brands have come up with various methods to connect with their customers, and we aim to verify if this is reflected in the loyalty of consumers. Therefore, the following assumption is proposed:

**H5: Customer Engagement has a positive effect on Customer Loyalty**

![Figure 1. Research Model](image)

3. Research Methodology

3.1 Data Collection and Sample Design

The research approach for this study is an associative case study and measured with a Likert scale ranging from 1 (strongly disagree) to 5 (strongly agree). The population of this sample comes from 158 Indonesian who have used local skincare and follow local skincare information by using a purposive sampling method with a cross-sectional research design. Data was collected through questionnaires, received by 171 respondents, and based on the respondent's criteria 18 data were trimmed so that the data became a total of 153 respondents.

3.2 Measurement and Scales

The measurement items used in this study were taken from instruments that had been validated before. Five items for measuring PQ were adopted from (Rofianah, Patricia Dhiana Paramita, 2016), whereas five items of PF were retrieved from (Sofiana & Prihandono, 2019) (Kartini et al., 2016) and (Hamenda, 2018).
Five items for measuring CE were adopted from (Panjaitan, 2017) and (So et al., 2016b). Lastly, four items for measuring CL were adopted from (Sambo et al., 2022) and (Rais et al., 2022).

Table 1. Demographic Information for Respondents (N=153)

<table>
<thead>
<tr>
<th>Gender</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Female</td>
<td>110 72%</td>
</tr>
<tr>
<td>Male</td>
<td>43 28%</td>
</tr>
<tr>
<td>Total</td>
<td>153 100%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Age Range</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>15 - 18 years old</td>
<td>2 1%</td>
</tr>
<tr>
<td>19 - 23 years old</td>
<td>119 78%</td>
</tr>
<tr>
<td>24 - 30 years old</td>
<td>30 20%</td>
</tr>
<tr>
<td>31 - 40 years old</td>
<td>2 1%</td>
</tr>
<tr>
<td>Total</td>
<td>153 100%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Income Range</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; Rp 2.500.000</td>
<td>42 27%</td>
</tr>
<tr>
<td>Rp 2.500.000 - Rp 5.000.000</td>
<td>61 40%</td>
</tr>
<tr>
<td>Rp 5.000.000 - Rp 10.000.000</td>
<td>33 22%</td>
</tr>
<tr>
<td>Rp 10.000.000 - Rp 15.000.000</td>
<td>9 6%</td>
</tr>
<tr>
<td>&gt; Rp 15.000.000</td>
<td>8 5%</td>
</tr>
<tr>
<td>Total</td>
<td>153 100%</td>
</tr>
</tbody>
</table>

4. Results & Discussion

According to the item-total correlation test, there was a 5% significance level for 153 sample size, the value of $r$ table is 0.13 and $t$ table is 1.66 which indicates all variables are proven to be valid. In accordance, the dependability of all scales with the Pearson technique was acceptable with Cronbach Alpha = 0.915 ≥ 0.60 (Ghozali, 2011) and considered normal with the sig value (0.283) > alpha value (0.05).

For hypothesis testing, data were divided into two substructures. For the first substructure model, Product Quality and Price Fairness are assumed to be independent variables, and Customer Engagement is the dependent variable. There is a positive and significant effect between Product Quality to Customer Engagement ($\beta=0.553; p<0.05$) with the Durability indicator as the highest value for the PQ variable, and this result is contrary with (Dhasan & Aryupong, 2019) that stated Product Quality does not have a significant effect on Customer Engagement. It is possible that with the help of Customer Engagement, the product quality of a brand can be more widely known by skin care users. For example, customers will better understand the ingredients or quality of the products they use through engagement in the form of customer education about skincare ingredients.

The study also reveals a significant and favourable impact of Price Fairness on Customer Engagement ($\beta=0.304; p<0.05$) with Reasonable Price and Comparing Price with Competitors indicators as the highest value for PF, and this research is in line with a previous study from (Nguyen et al., 2016). Consequently, skincare companies must also be wiser in determining fair and ethical prices to maintain good customer relationships. Indonesian skincare companies frequently implement a pricing policy that sets a floor price for their distributors. This approach aims to create a consistent and stable pricing environment for consumers and prevent consumers from perceiving significant fluctuations in the product’s price over time. By avoiding sudden changes in pricing, consumers can maintain trust in the product, and it can contribute to fostering their engagement.

In the second model, Product Quality, Price Fairness, and Customer Engagement are assumed to be predictors of Customer Loyalty. In this model, there is a positive and significant effect between Price Fairness to Customer Loyalty ($\beta=0.294; p<0.05$); hence it is apparent that the skincare industry in Indonesia upholds its reputation and cultivates a loyal customer base by implementing fairness and transparency in their
pricing. There is also a positive and significant effect from Customer Engagement to Customer Loyalty ($\beta=0.433; p<0.05$), with Integrity as the most significant factor in promoting Customer Engagement while Buy inter-line products and services are crucial for fostering Customer Loyalty. This also demonstrates that when consumers form an emotional connection with a product and have a positive experience, they tend to develop a strong commitment and loyalty toward the product. The two outcomes are consistent with previous research (Dhasan & Aryupong, 2019).

However, on the contrary side from (Dhasan & Aryupong 2019), directly there is no significant effect of Product Quality on Customer Loyalty ($\beta=0.126; p>0.05$). This result challenge the notion that meeting consumer expectations through good Product Quality alone is sufficient to ensure Customer Loyalty. Product Quality in skincare is intricately linked to the ingredients utilized. As everyone has unique skin types, the perception of what constitutes a good product will vary significantly based on individual preferences. Consequently, even if a product is perceived as high quality, if the ingredients are not suitable for a particular consumer’s skin type, that consumer may not develop loyalty toward the product.

Subsequently, the indirect effect of Product Quality on Customer Loyalty mediated by Customer Engagement and the indirect effect of Price Fairness on Customer Loyalty mediated by Customer Engagement is posited to test the mediating variable. Product Quality had a significant indirect effect on Customer Loyalty ($\beta=0.231; p<0.05$) through Customer Engagement, which is in accordance with a previous study from (Parihar et al., 2019) with a value of 61.7% on Customer Engagement from Product Quality to Customer Loyalty having more considerable value compared to Price Fairness. Based on these discoveries, it is also necessary to establish a connection with the brand to achieve loyal customers.

Price Fairness through Customer Engagement indirectly does not significantly affect Customer Loyalty ($\beta=0.132; p<0.05$) with a value of 58.9% mediation effect on Customer Engagement from Price Fairness to Customer Loyalty. This result failed to align with previous research (Dhasan & Aryupong, 2019). Another interesting finding is that from PF to CL through CE, the mediating effect (13%) is considered more minor than the direct one (29%). Our research suggests that this could occur because, when customers are engaged with the concept of price fairness, they are more likely to compare prices with those of competitors. This makes it easier for them to switch to other products if they perceive that competitors offer similar value at lower prices.

Table 2. Result analysis

<table>
<thead>
<tr>
<th>Independent Variable</th>
<th>Dependent Variable</th>
<th>Customer Engagement</th>
<th>Customer Loyalty</th>
<th>Mediating</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>($\beta$)</td>
<td>Sig</td>
<td>($\beta$)</td>
<td>Sig</td>
</tr>
<tr>
<td>Product Quality</td>
<td>0.553</td>
<td>0.000</td>
<td>0.126</td>
<td>0.134</td>
</tr>
<tr>
<td>Price Fairness</td>
<td>0.304</td>
<td>0.000</td>
<td>0.294</td>
<td>0.000</td>
</tr>
<tr>
<td>Customer Engagement</td>
<td></td>
<td>0.433</td>
<td>0.000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>$R^2=0.617$</td>
<td></td>
<td>$R^2=0.589$</td>
<td></td>
</tr>
</tbody>
</table>
5. Conclusion

This study yields important managerial implications. Based on our findings, when PQ and PF are compared on their effect on CE, PQ has a more significant value of 25% than PF on CE. Our suggestion to skincare companies is to enhance their research and development efforts to attract more committed customers. This could involve experimenting with various cutting-edge technologies and ingredients on a range of skin types to find formulations that work well for everyone. However, regarding the role of CE in the relationship between PQ and CL, we observed a mediating effect of 23%. This differs from previous research that claimed PQ had no substantial impact on CL via CE (Dhasan & Aryupong, 2019).

Our recommendation for companies is to enhance customer engagement, such as hosting launch events, offering personalized products, and implementing customer loyalty programs. A greater direct effect was observed regarding the impact from PF to CL via CE. Therefore, the company must maintain transparency in pricing and provide comprehensive product information to promote customer loyalty toward using the product. Lastly, in line with previous studies (Hu et al., 2021), it was found that there was a significant effect from CE to CL (43%). It would benefit the company to acknowledge its engaged customers by offering exclusive discounts, providing customer rewards, soliciting and responding to feedback, and establishing customer communities.

This research fills in the gap of previous research by combining the direct effects of Product Quality and Price Fairness from several studies focusing on Customer Engagement as mediation to Customer Loyalty. In terms of theoretical gains, this study contributes significantly to using specific indicators on Product Quality and Price Fairness for local skincare in Indonesia by increasing Customer Loyalty with Customer Engagement to mediate using path analysis. In terms of international business strategy, the study provides insight for increasing customer loyalty through product quality and price fairness through customer engagement in the macroeconomic scope for future research.

The limitation of this research is the number of samples and variables, and we only confirm through path analysis. For further research, it is recommended to use larger samples, add other suggested variables such as Brand Image, Brand Awareness, and others, use other analysis, and extend the data analysis technique to SEM because there is the value from each model and also the value of the structural equation or using qualitative techniques to add elaboration from experts regarding the influence of these variables.

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