

Research Article

# The Effect of Perceived Fairness on Trust and Loyalty in family Takaful

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**Abstract:** The Takaful industry has experienced significant development in Malaysia. It is a substantial component in the Islamic finance system and has continued to play an important role in supporting the economic and social development of this country. Bank Negara Malaysia reports revealed the performance of the Takaful industry in Malaysia is strongly contributed by family Takaful business compared to the general Takaful business. However, this industry is facing a problem of retaining its existing participants, particularly in family Takaful. It is observed within five years, between 2013 and 2017, there was always the number of participants who surrender their family Takaful certificates. The increasing number of family Takaful participants' surrender has affected the slower rate of Takaful penetration in Malaysia. It is vital for the Takaful industry in Malaysia to focus on participants' retention by understanding loyalty tendencies. Hence, the objective of this study is to examine the effect of perceived fairness and trust on loyalty in family Takaful. This study also aims to examine the mediating role of trust which can help extend the current understanding of loyalty. The findings of the study expected that perceived fairness will have a significant effect on trust and loyalty. Similarly, trust also expected to have a significant effect on loyalty. Additionally, trust is expected to mediate the relationship between perceived fairness and loyalty. This study will contribute to the existing literature as a reference to better understand the loyalty tendencies, especially in Takaful industry settings.

**Keywords:** Perceived fairness; Trust; Loyalty; Family Takaful; Malaysia.

## About the Authors

Juliana Arifin is a PhD student in the field of Business Management (Insurance). Her current research interests include insurance, Takaful, risk management, consumer behaviour, and marketing. During her study as a PhD student, she managed to publish articles in journals and presented papers in conferences. She intends to complete other related articles for publication from her PhD research.

## Public Interest Statement

Every experience of fairness has important attitudinal, affective, and behavioural consequences for any customers. As a results, the perception of fairness can serve as a customer relationship-building tool that will foster loyalty intentions and other favorable behavioral consequences.

The research, at best, can contribute to customers to understand how important the concept of fairness, which can help enhance positive attitudes and behaviours in an exchange relationship.

## 1. Introduction

The Takaful industry in Malaysia has been gaining momentum and increasingly recognised as a significant contributor to Malaysia's overall Islamic financial system. It continues to play an important role in supporting the economic and social development of this country. According to the Monthly Highlights and Statistics Report (2018) from Bank Negara Malaysia (BNM), the total of Takaful business performance in terms of gross contribution increased from RM6, 197 million in 2013 to RM8, 217 million in 2017. It can be seen that for family Takaful business, the gross contribution increased from RM4, 807 million in 2013 to RM6, 353 million in 2017. Similarly, for general Takaful business, the gross contribution also increased, albeit only at a slower pace which was from RM1, 390 million in 2013 to RM1, 864 million in 2017. The performance of the Takaful industry in Malaysia is proven to have strongly contributed by family Takaful business as compared with the general Takaful business which remained the primary income generator for the Takaful industry in Malaysia. The domination of family Takaful business emphasized its importance as a tool for long-term savings and investment, whilst protecting against financial vulnerabilities arising from critical illness, death, disability or unemployment, or providing for children's education. This is also in line with Rahman et al. (2008) that family Takaful become a form of savings instrument that is popular especially among Malaysian Muslims in general and has its appeal due to its shari'ah compliant attributes.

Even though Malaysia has been dominated by the family Takaful business in terms of their contribution, but an untapped market still exists and does not meet the potential market. It showed that the market penetration rate in family Takaful is still relatively low and presents a huge business opportunity (Kadir, 2011; Hashim, 2012; OSK research report, 2012; Azman, 2013). Market penetration rate is equal to the total number of family Takaful certificates divided by the total Malaysian population. Evidence from the report in Ernst and Young (2015) depicted that the market penetration rate of Malaysia's family Takaful sector is only at 14.5% in 2014 compared with the life insurance's market penetration which is at 41.2 %. Hence, there is a large gap between family Takaful and the conventional life insurance by which the family Takaful market has a tremendous opportunity to boost untapped areas in their business to compete with its conventional peers. Furthermore, it was also discovered that the slower rate of market penetration in Malaysia is due to the increasing number of family Takaful participants who surrendered their certificates (Salleh et al., 2013; Salleh, 2016). Additionally, the penetration rate is highly related to the loyalty from customers (Oliver, 1997; Rambocas & Arjoon, 2012; Salleh, 2014) and is supported by the fact that the surrenders of life insurance policies and family Takaful certificates have increased in recent years (Financial Stability and Payment Systems Report, 2016). It also evidenced that there were always the number of family Takaful participants surrendered their certificates by each year (Monthly Statistical Bulletin, 2018). This can be observed within five (5) years, between 2013 and 2017 whereby there are inconsistencies as the highest number was recorded in 2013 in which approximately 314,036 participants surrendered their family Takaful certificates excluding death and maturity. This can be argued that the Takaful industry are facing a problem in retaining their existing participants.

Based on the bucket theory, it is imperative to pay more focus on customer retention than on acquiring new customers (Ziethmal et al., 2013). This is supported by Wills (2009) and Singh and Imran (2012) that the expense of gaining new customers may cost companies to spend five times more than to keep existing ones. This aspect highlights the concern that only 'customer loyalty' can ensure competitiveness and continuous survival (Haque et al., 2009). A study conducted by Lam and Burton (2006) suggests that the loyal customers tend to have higher likelihood of repurchasing from a supplier than non-loyal customers. They further suggested that loyal customers significantly contribute to market share growth. It is believed that customer loyalty can create competitive advantage, and profit in the long term as well as can reduce the cost of marketing among other promotional costs (Utami, 2015). This is corresponds with the past researchers that stated the relationship between the increase in the number of loyal customers and sales can be used as an indicator of corporate performance as well as improves its level of profitability (Reichheld & Teal, 1996; Eakuru & Mat, 2008; Rasheed & Abadi, 2014; Abtin & Pouramiri, 2016). Additionally, customer

loyalty can also be used as a surrogate for market penetration since it creates a stable pool of customers for a firm's product and service (Oliver, 1997; Torres & Tribo, 2011). Since the market penetration rate of Malaysia's family Takaful sector is still relatively low, it is crucial to maintain present participants which can help to increase the market penetration rate in the Takaful industry.

It is highlighted that in the new global economy, service providers including Takaful industry are competing to develop and retain customers (participants) through increased loyalty. Based on this situation, it is vital for the Takaful industry in Malaysia to assume strategies in maintaining their participant's loyalty. Moreover, to the best of researcher's knowledge, there is limited studies that focused on loyalty especially in the context of family Takaful in Malaysia. Since family Takaful is believed as an intangible products and services, in this way, the affectability of the participants to fairness is vital in the service industry (Berry et al., 1994). According to Loch et al. (2012) fairness can be a source of competitive advantage and as a key performance indicator into firms' market research plans. In addition, fairness perceptions is highlighted to play an important role in consumer behavior (Sebjan et al., 2015). Service fairness is an antecedent of consumption emotions (positive and negative) that in turn influence customers' satisfaction and behavioural intentions (Su & Hsu, 2013; Dwidienawati et al., 2018). It is extremely important for Takaful industry pay attention on the fairness in order to maintain the loyalty of their participants in family Takaful. Service fairness is a means of retaining customers, which service providers can achieve by keeping promises in the provision of services, reflecting the quality of the relationship between the Takaful industry and the participants. Roy and Eshgi (2013) stated that fairness considered as an integral part of relationship quality strategy for service providers. Thus, perceived fairness influences loyalty indirectly by strengthening the supplier-customer relationship quality, which has been proven to be a better predictor of customer attitude and behaviour (Chen et al., 2012; Vrontis et al., 2013).

Besides, perceived fairness offers a useful means through which to explain and understand individuals' feelings of trust or mistrust (Saunders & Thornhill 2003). Based on Morgan and Hunt (1994) fairness subsequently acts as an antecedent of trust and this is supported by Nguyen et al. (2013) that the successful of consumers fairness perceptions is built on trust in order to create mutually satisfying relationships by delivering equally beneficial outcomes for consumer. This is supported by Devlin et al. (2013) who pointed out that perceptions of fairness can also be related to levels of trust and consumers' behavioural intention. It provides a strong effect on development of trust and commitment, and contributes to the development of an effective long-term relationship (Peppers & Rogers, 2004; Poppo & Zhou, 2014). Fu (2013) discovered it is essential for a company to build and sustain a long term relationship with customers by treating them fairly. As customers stay with the same provider for longer periods due to fair treatment and high-quality services, trust and commitment increase whereby, a relationship is developed and therefore, these customers exhibit an intention to stay with the same provider, and have a tendency to refer the provider to others (Giovanis et al., 2015). However, the conjecture about the effect of these constructs had not been empirically tested in the context of family Takaful. There is still available gap to be explored whether perceived fairness have an effect on trust and loyalty in family Takaful. Therefore, the motivation of this study is to provide insight as to what extent perceived fairness plays a role on trust and loyalty in the context of family Takaful. This represents a gap in the literature that is worth investigating. Hence the needs to retain and attract participants present a key tactics and objective for Takaful industry as the primary financial turnover. Thus, this study emphasis on the subject of fairness for the industry, as perceived fairness is contributes to the participant trust, where in turn leads to the participant loyalty in family Takaful. In order to make the study easier to understand the research objective are stated as below:

1. To examine the effect of perceived fairness on trust and loyalty in family Takaful.
2. To examine the effect of trust on loyalty in family Takaful.
3. To determine whether trust mediates the relationship between perceived fairness and loyalty in family Takaful.

## 2. Literature Review

### 2.1 Theories Underpinning

#### 2.1.1 Equity Theory

The perception of fairness can be explained by equity theory suggested by Adams (1965) in which, an individual tend to compare their input-outcome ratio with the referent other. Adams' equity theory is based on a ratio consisting of inputs to outcomes. Inputs consist of contributions by an individual such as abilities, effort, performance, age, seniority, education, and other attributes. Meanwhile, outcomes are the rewards an individual receives for their inputs such as pay, benefits, status symbols, and even intrinsic rewards. The value of an outcome is determined by the recipient (Adams, 1965), hence, no outcome has a specific objective measure.

Additionally, this theory is based on a principle that peoples' actions and motivations are guided by fairness and that discrepancies in this fairness in an organization will spur them to try and redress it. This theory also recognized that motivation can be affected through an individual's perception of fair treatment in social exchanges. Besides, individuals who are fairly rewarded experience satisfaction and will be motivated to engage in a certain behaviour (Adams 1965). This is supported by Redmond (2010) that a person's motivation is based on what he or she considers to be fair when compared to others.

On the other hand, fairness is a multifaceted construct rooted in equity theory (Adam, 1965). As a concept fairness is characterised by a number of features and there are posited to be three main dimensions of fairness, namely, distributive fairness, procedural fairness and interactional fairness (Homans, 1961; Adam, 1965; Thibaut & Walker, 1975; Niehoff & Moorman 1993; Blodgett et al., 1997; Ramaswami & Singh 2003; Worthington & Devlin, 2013; Sekhon et al., 2016). This theory has been used to test several types of dyadic relationships like marriages, teacher-student, employee-employer and buyer-seller relationships. As a part of process to develop the participant of family Takaful and Takaful operator relations in this study, fairness can be positioned as a source of competitive advantage (Loch et al., 2012).

#### 2.1.2 Social Exchange Theory

Social exchange theory was introduced by Thibaut and Kelley (1959) and Homans (1961). This theory proposes that an exchange relationship develops between two parties when one party provides a benefits to the other party resulting in the other party being obligated to respond also with something beneficial. The exchange of benefits could involves various resources, such as money, services, information, as well as socio-emotional benefits such as respect and loyalty (Blau, 1964). Social exchange also involves a series of interactions commonly taken as interdependent depends on the actions of another person, which then generate obligations and high quality relationship such as trust, commitment and loyalty (Blau, 1964; Emerson, 1976).

Homans (1961) also stated that social exchange theory as the premise that human behavior or social interaction is an exchange of activity, tangible, and intangible. It thus suitable to the context of this research as there is social interaction between Takaful operator and their family Takaful participants and involving tangible (contribution in terms of money) and intangible (services provided by the Takaful operator) aspects. Accordingly, social exchange also presents the existence of interpersonal relationships between the parties (Hutchinson et al., 1997) and this is in line with the context of this research (service provider-customer relationship).

### 2.2 Perceived Fairness and Trust

According to Duffy (1998) creating long-term relationships with customers is the key to the survival and growth of service operations. This is in line with Anderson and Weitz (1989) that suppliers or any service providers with a reputation of fairness are trusted more by customers and are rewarded with more and longer term relationships. Most of previous researchers believed that

fairness is important for developing trust between service providers and their customers (Chiu et al., 2010; Kim & Kandampully, 2011; Chen et al., 2012; Zhu & Chen, 2012). This is supported by Shaikh et al. (2017) that perceived fairness can help enhance positive attitudes and behaviours in an exchange relationship (Shaikh et al., 2017). Since there is limited studies on Takaful regarding the relationship between perceived fairness and trust, the researcher make an effort to rely on the related field of studies. For instance, Chen et al. (2012) conducted a survey on customer from the financial industry in Taiwan. They found fairness plays a critical role in determining customer trust and perceived value, which in turn lead to other customer behaviors and satisfaction. Nguyen and Nham (2014) conducted a study in an online shopping and found that fairness is significantly influenced trust. Meanwhile, Giovanis et al. (2015) carried out a study to investigate the impact of service fairness on relationship quality which consists of trust, commitment and satisfaction dimension. The result from their study showed that service fairness is positively effect the relationship quality in their study. Another research conducted in the mobile sector by Al-Amri and Al-Shmmary (2017) also found that fairness have a positive relationship with the customer trust.

### *2.3 Perceived Fairness and Loyalty*

Nguyen and Nham (2014) suggested that service providers should offer fair services to their customers as it is the most crucial factor for creating customer loyalty. This is in line with Giovanis et al. (2015) that if customers feel good about the treatment they get from their service provider, they are likely to perceive a higher service quality for services rendered and they will be more willing to enter a long-term relationship with the provider. Many of the past empirical studies discovered that fairness considered as an important factor that influence the customer loyalty (Hwang & Wen, 2009; Hassan et al., 2013; Nguyen & Nham, 2014; Bassey, 2014; Giovanis et al., 2015; Juhari et al., 2016). The study by Hwang & Wen (2009) deals with customers' perceptions of fairness towards hotel overbooking and compensation policy practices on customer loyalty. The findings from their study showed the perceived fairness toward hotel overbooking and compensation policy has a positive significant relationship with customers loyalty. Hassan et al. (2013) found that service fairness is also positively and significantly associated with the customer loyalty in mobile telecommunication sector. Another study by Bassey (2014) also found that fairness in terms of price is positively related with the customer loyalty which classified into behavioral loyalty and affective loyalty. The relationship between fairness and customer loyalty is further supported by Giovanis et al. (2015). They found that service fairness has the highest overall effect on customer loyalty. On the other hand, Juhari et al. (2016) carried out a study which focuses on service quality and customers' satisfaction and loyalty in the Takaful industry in Malaysia. This findings revealed that fairness is one of the elements in service quality which considered as an important factor for customer satisfaction as well as customer loyalty.

### *2.4 Trust and Loyalty*

Many past researchers agreed that trust has significant influence on customer loyalty. For instance, in the context of financial service industry, it is found that customer trust as well as commitment has direct and positive relationships to customer loyalty (Madjid et al., 2013; Nguyen et al., 2013; Damtew & Pagidimarri, 2013; Rai & Medha, 2013; Chakiso, 2015; Van Tonder, 2016; Simbolon, 2016; Hasandoust & Saravi, 2017). Sarwar et al. (2012) carried out a study to explore the effect of customer trust on customer loyalty and customer retention by moderating effect of cause related marketing in Pakistan among cellular service companies. The findings from their research found that customer loyalty is greatly affected by customer trust. This also in line with the study by Rauyruen et al. (2007), whereby trust is related to the attitudinal loyalty in business to business context. On the other hand, Ghasemi and Beiranvand (2016) conducted their study in the air travel agencies. They found that customer trust has positively influences the customer loyalty.

### *2.5 The Mediating Effect of Trust between Perceived Fairness and Loyalty*

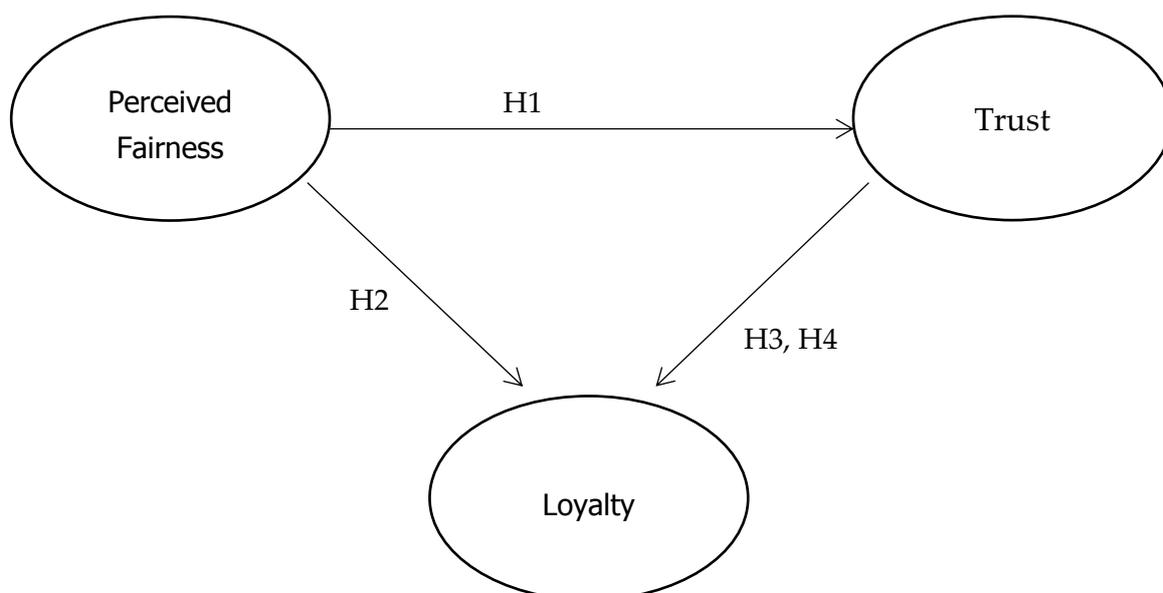
Fairness considered as an important factor that influences the customer trust in the context of financial and banking service industry (Chen et al., 2012; Roy et al., 2015). Besides, fairness is found to have significant influences on customer loyalty (Hwang & Wen, 2009; Hassan et al., 2013; Bassey, 2014; Nguyen & Nham, 2014; Giovanis et al., 2015; Juhari et al., 2016). Trust also has significant influence on customer loyalty. It is found that customer trust has direct and positive relationships to customer loyalty in the context of financial service industry including banking and insurance (Nguyen et al., 2013; Damtew & Pagidimarri, 2013; Rai & Medha, 2013; Chakiso, 2015; Hasandoust & Saravi, 2017).

Based on Baron and Kenny's (1986) procedure to investigate mediated relationships, the above studies and research output provide evidence on the existence of direct relationships between fairness and trust. There are also evidence from the discussion above on the direct effects of fairness on loyalty. Additionally the discussion also show that there is direct effect of trust on loyalty. Research on trust as a mediating variable was conducted by Nguyen et al. (2013). They found that customer trust play a role as a mediating variable that enhances the impact of corporate identity, corporate image and the reputation of the firm on customer loyalty. This is supported by Madjid (2013) that found the customer trust is a mediator between the relationship between customer satisfaction and customer loyalty in the Bank Rakyat Indonesia. In addition, Van Tonder (2016) also confirmed trust as mediator of the relationship between quality advice and customer loyalty in the context of insurance agents environment. Meanwhile, the findings of study conducted by Pringviriya (2015) indicated that customer trust mediated the relationship between service quality and customer loyalty in audit firm. Another research on trust as a mediator to the relationship between attitude and behavioural were studied by Noor and Saad (2016) and Chiu et al., (2017).

### 3. Conceptual Model and Hypothesis

The conceptual model for the present study was developed based on research material; and Figure 1 shows that model as a simple diagram.

Figure 1. Conceptual model



On the basis of the discussion related on the theoretical and empirical research above, this current research proposed the following hypothesis:

- Hypothesis 1: Perceived fairness positively and significantly influences participant trust in family Takaful.
- Hypothesis 2: Perceived fairness positively and significantly influences participant loyalty.
- Hypothesis 3: Participant trust positively and significantly influences participant loyalty.
- Hypothesis 4: Participant trust mediates the relationship between perceived fairness and participant loyalty.

#### 4. Methodology

The research is design quantitatively where the data is collected through a survey using the structured questionnaire. The question items were adapted from previous studies with appropriate changes to make the items more relevant to the present study. Each item was evaluated on a ten-point Likert scale ranging from (1) Strongly Disagree to (10) Strongly Agree.

The target populations in this research are the Malaysian Takaful participants. Meanwhile, this research specifies the participants who are participating in the family Takaful for more than two year would be the target sample. A total 500 questionnaires were distributed to the respondents via four (4) Takaful operators in Malaysia, namely, Etiqa Takaful Berhad, Syarikat Takaful Malaysia Berhad, Takaful Ikhlas Sdn Bhd, and Prudential BSN Takaful Berhad. The stratified random sampling and simple random sampling were used in this study in order to select the respondents.

As for data analysis, there were two stages of analysis involved. First, the descriptive analysis and second, the multivariate statistical analysis. The first stage describes the profiling of the respondents using SPSS. Meanwhile, second stage is to answers the objectives of this research whereby Structural Equation Modelling (SEM) was carried out using AMOS.

#### 5. Conclusion

The findings of this research will be useful to the understanding of participant loyalty in a family Takaful setting. This research expects a positive and significantly influences between perceived fairness, trust, and loyalty in family Takaful. It also expects trust mediates the relationship between perceived fairness and loyalty in family Takaful. The findings from the research will assist Takaful operators, policymakers, regulators, marketing practitioners, and government to pay more attention in enhancing fairness to create solid anchors. It is because from solid anchors, trust will be established, with the domino effects spilling over to participant loyalty.

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