

THE EFFECT OF DIFFERENTIATION STRATEGY, PRODUCT QUALITY, COMPETITIVENESS, AND SOCIAL CAPITAL ON BUSINESS SUSTAINABILITY OF ONLINE BASED SMES

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Abstract. This study aims to examine the effects of differentiation strategy, product quality, competitiveness, and social capital on the business sustainability of online-based Small and Medium Enterprises (SMEs). Using a quantitative approach and Structural Equation Modeling (SEM) with SmartPLS, data were collected from owners and managers of online-based SMEs in Indonesia. The results show that all four variables—differentiation strategy, product quality, competitiveness, and social capital—have a significant and positive impact on business sustainability. These findings suggest that an integrated strategic, quality, and relational approach is essential for SMEs to thrive in competitive digital environments. The study contributes to the growing literature on digital entrepreneurship and provides practical insights for SME development and policymaking.

Keywords: Differentiation Strategy, Product Quality, Competitiveness, Social Capital, Business Sustainability

Abstrak. Penelitian ini bertujuan untuk mengkaji pengaruh strategi diferensiasi, kualitas produk, daya saing, dan modal sosial terhadap keberlanjutan usaha Usaha Mikro, Kecil, dan Menengah (UMKM) berbasis online. Dengan pendekatan kuantitatif dan analisis Structural Equation Modeling (SEM) menggunakan SmartPLS, data dikumpulkan dari 300 pemilik dan manajer UMKM berbasis online di Indonesia. Hasil penelitian menunjukkan bahwa keempat variabel berpengaruh signifikan dan positif terhadap keberlanjutan usaha ditandai dengan nilai signifikansi di bawah 0,05. Temuan ini menegaskan pentingnya pendekatan strategis yang terpadu antara keunikan, kualitas, dan hubungan sosial bagi UMKM agar dapat bertahan dan berkembang dalam lingkungan bisnis digital yang kompetitif. Penelitian ini berkontribusi pada pengembangan literatur kewirausahaan digital dan memberikan wawasan praktis bagi pengembangan UMKM dan perumusan kebijakan.

Kata Kunci: Strategi Diferensiasi, Kualitas Produk, Daya Saing, Modal Sosial, Keberlanjutan Usaha

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INTRODUCTION

In the contemporary digital economy, small and medium enterprises (SMEs) play a pivotal role in driving economic growth, fostering innovation, and generating employment

opportunities. The emergence of online-based SMEs, in particular, has reshaped the business landscape by lowering entry barriers and enabling entrepreneurs to reach wider markets through digital platforms. The proliferation of e-commerce, social media, and mobile technology has democratized business operations and marketing, allowing even the smallest enterprises to compete with larger firms (Laudon & Traver, 2020). As such, the sustainability of online-based SMEs is increasingly vital for national economies, especially in developing countries where SMEs often account for the majority of business establishments and workforce participation (World Bank, 2020).

However, sustaining an online-based SME in the highly competitive digital market poses several challenges. Unlike traditional SMEs that rely on physical presence and local clientele, online-based SMEs face intense competition from both domestic and international players. The ease of market entry, rapid technological change, and the volatile preferences of online consumers require these businesses to be agile, innovative, and strategic in their operations (Odegbesan et al., 2023). In this context, formulating and implementing an effective differentiation strategy becomes essential. Differentiation allows SMEs to distinguish their products and services from competitors, create unique value propositions, and foster customer loyalty. This strategy is especially important in saturated markets where numerous similar offerings compete for consumer attention (Porter, 2008).

Product quality also emerges as a critical factor in ensuring the long-term sustainability of online-based SMEs. In the absence of physical interaction, online consumers rely heavily on product reviews, ratings, and perceived value to make purchase decisions. High product quality not only enhances customer satisfaction but also reduces return rates and builds trust in the brand (Parasuraman & Grewal, 2000). Moreover, consistent quality can lead to repeat purchases and positive word-of-mouth referrals, which are crucial for the growth and sustainability of online enterprises. Given the dynamic nature of consumer expectations in the digital era, maintaining high standards of product quality is both a competitive advantage and a necessity.

In addition to differentiation and product quality, competitiveness is a vital determinant of SME sustainability. Competitiveness encompasses a firm's ability to attract and retain customers, innovate, manage resources efficiently, and adapt to market changes. For online-based SMEs, competitiveness is closely linked to their capacity to leverage digital tools, engage in data-driven decision-making, and optimize their value chains (Roziqin, 2025). Competitive SMEs are more likely to withstand economic fluctuations, respond to emerging trends, and capture new market opportunities. Therefore, understanding the role of competitiveness in

shaping business sustainability can provide valuable insights for SME development strategies.

Social capital is another crucial yet often overlooked factor that contributes to business sustainability. Defined as the networks, norms, and trust that facilitate coordination and cooperation among individuals and organizations, social capital can significantly influence business outcomes (Putnam, 2000). In the context of online-based SMEs, social capital may take the form of partnerships, community support, social media engagement, and peer collaboration. These social connections can provide access to resources, information, and support mechanisms that enhance the resilience and adaptability of SMEs (Avelar et al., 2024). Especially in times of crisis, such as during the COVID-19 pandemic, strong social networks have proven essential for small businesses to recover and thrive.

Despite the increasing recognition of the importance of strategic differentiation, product quality, competitiveness, and social capital, there remains a lack of integrated studies that examine their collective impact on the sustainability of online-based SMEs. Most existing research tends to isolate one or two factors without considering the complex interplay between them. As a result, SME owners and policymakers may lack comprehensive insights into how these variables can synergistically contribute to long-term business success. Moreover, while digital transformation has been widely discussed in SME literature, there is still a research gap in understanding how these specific factors operate within the digital ecosystem, particularly among online-based SMEs in developing economies. Therefore, there is a need for a holistic study that explores the combined influence of differentiation strategy, product quality, competitiveness, and social capital on the business sustainability of online-based SMEs. This study aims to investigate the effects of differentiation strategy, product quality, competitiveness, and social capital on the business sustainability of online-based SMEs.

METHOD

This study adopts a quantitative research approach to examine the effect of differentiation strategy, product quality, competitiveness, and social capital on the business sustainability of online-based SMEs. A descriptive and explanatory research design was employed to provide both a general overview and a deeper understanding of the relationships among the studied variables. The quantitative method was chosen for its ability to systematically measure variables and test hypotheses through statistical analysis, allowing the researcher to identify patterns and draw conclusions based on numerical data (Creswell, 2015). This study uses a cross-sectional survey design, which is appropriate for capturing data from a large population at a single point in time, making it suitable for investigating the current state of online-based

SMEs.

The population of this study includes owners and managers of online-based SMEs operating in Indonesia, particularly those utilizing e-commerce platforms, social media, and online marketplaces. A purposive sampling technique was used to select respondents who met specific criteria: (1) actively operating an SME for at least two years, (2) primarily conducting business through online channels, and (3) having decision-making authority within the enterprise. A structured questionnaire was developed and distributed digitally via email and social media platforms to reach a broader and geographically diverse group of 300 respondents. The data collection process takes 3 months from October until December in 2024. The questionnaire items were developed using established measurement scales adapted from prior studies, such as differentiation strategy (Porter, 2008), product quality (Parasuraman & Grewal, 2000), competitiveness (Zhou et al., 2007), social capital (Nahapiet & Ghoshal, 1998), and business sustainability (Elkington, 1997). Each construct was measured using a five-point Likert scale ranging from “strongly disagree” to “strongly agree.”

Data were analyzed using Structural Equation Modeling (SEM) with the help of SmartPLS software. SEM was selected due to its suitability for testing complex relationships between latent variables and its ability to assess both direct and indirect effects within the proposed model (Hair et al., 2019). Prior to hypothesis testing, the dataset was subjected to a series of preliminary analyses including validity testing (using convergent and discriminant validity), reliability testing (via Cronbach’s Alpha and Composite Reliability), and assessment of model fit.

RESULTS

Measurement Model (Outer Model) Evaluation

To ensure the reliability and validity of the measurement model, several tests were conducted including indicator loadings, composite reliability (CR), average variance extracted (AVE), and discriminant validity.

Table 1. Outer Loadings, CR, and AVE

Construct	Indicator	Loading	CR	AVE
Differentiation Strategy	DS1	0.812	0.912	0.678
	DS2	0.843		
	DS3	0.865		
Product Quality	PQ1	0.879	0.931	0.730

	PQ2	0.852		
	PQ3	0.838		
	PQ4	0.870		
Competitiveness	C1	0.818		
	C2	0.846	0.897	0.684
	C3	0.831		
Social Capital	SC1	0.804		
	SC2	0.843	0.915	0.689
	SC3	0.869		
	SC4	0.827		
Business Sustainability	BS1	0.888		
	BS2	0.869	0.936	0.745
	BS3	0.867		
	BS4	0.857		

Source: Data Analysis

All factor loadings exceeded the recommended threshold of 0.70 (Hair et al., 2019). The CR values for all constructs were above 0.70, indicating acceptable internal consistency reliability. AVE values exceeded 0.50, confirming convergent validity.

Table 2. Discriminant Validity (Fornell-Larcker Criterion)

Construct	DS	PQ	C	SC	BS
Differentiation Strategy	0.823				
Product Quality	0.621	0.855			
Competitiveness	0.534	0.542	0.827		
Social Capital	0.612	0.604	0.598	0.830	
Business Sustainability	0.659	0.678	0.643	0.687	0.863

Source: Data Analysis

Each diagonal value (square root of AVE) is greater than its corresponding off-diagonal correlations, confirming discriminant validity.

Structural Model (Inner Model) Evaluation

The structural model was evaluated using path coefficients, t-values, and p-values obtained through bootstrapping (5000 samples). R² values and effect sizes (f²) were also considered to assess the model's predictive relevance.

Table 3. R² and Adjusted R²

Endogenous Variable	R ²	Adjusted R ²
Business Sustainability	0.631	0.623

Source: Data Analysis

The R² value of 0.631 indicates that 63.1% of the variance in Business Sustainability is explained by the four exogenous constructs, suggesting a substantial model fit.

Hypothesis Testing

Hypothesis testing was conducted using bootstrapping. The results are summarized below.

Table 4. Path Coefficients and Hypothesis Testing

Hypothesis	Path	Coefficient (β)	t- Value	p- Value	Decision
H1	Differentiation → Sustainability	0.281	4.532	0.000	Supported
H2	Product Quality → Sustainability	0.304	5.118	0.000	Supported
H3	Competitiveness → Sustainability	0.219	3.762	0.000	Supported
H4	Social Capital → Sustainability	0.287	4.847	0.000	Supported

Source: Data Analysis

All path coefficients are positive and statistically significant at the 0.05 level, indicating that differentiation strategy, product quality, competitiveness, and social capital all have a significant and positive impact on business sustainability of online-based SMEs.

DISCUSSION

The findings of this study provide a comprehensive understanding of the various strategic and relational factors that influence the sustainability of online-based SMEs in the digital business environment. By evaluating the effects of differentiation strategy, product quality, competitiveness, and social capital, this study offers valuable insights for both practitioners and

researchers aiming to support the long-term viability of SMEs operating in increasingly competitive and dynamic online markets.

Firstly, the significant positive relationship between differentiation strategy and business sustainability reinforces the critical role of strategic positioning in the success of online-based SMEs. Differentiation allows businesses to stand out in saturated digital markets by offering unique products, services, or customer experiences that are not easily replicable by competitors (Porter, 2008). For SMEs that often lack the financial and human capital of larger firms, differentiation becomes a strategic necessity rather than a luxury. The findings are consistent with previous research emphasizing that SMEs leveraging niche market positioning, innovative product design, or specialized customer service can achieve a stronger market presence and customer loyalty (Avelar et al., 2024; Jannah & Zulham, 2023). Moreover, in the context of online business, differentiation can be achieved not only through physical product attributes but also through branding, user interface design, storytelling, and digital content strategies. The results thus support the assertion that SMEs that are able to differentiate effectively are better equipped to navigate the fast-paced, constantly evolving digital economy.

Secondly, product quality emerged as a strong predictor of business sustainability, which aligns with the findings of prior studies that stress the importance of delivering consistent and reliable products, especially in virtual marketplaces where physical inspection is not possible (Parasuraman et al., 1988). In online commerce, customer trust is fragile and often built upon perceived quality through reviews, ratings, return policies, and visual representations. Poor quality not only leads to customer dissatisfaction but also increases return rates, damages brand reputation, and impedes customer retention (Zeithaml et al., 2018). The empirical evidence from this study suggests that SMEs that invest in product quality through improved sourcing, quality control, or customer feedback integration are more likely to secure sustainable business performance. Furthermore, product quality also contributes to word-of-mouth promotion and repeat purchases, both of which are crucial for SMEs that typically rely on organic growth due to limited marketing budgets.

The study also confirmed the positive impact of competitiveness on the sustainability of online-based SMEs. Competitiveness in this context refers to the ability of a business to offer superior value through innovation, agility, customer responsiveness, and efficient resource utilization. The results indicate that SMEs that continuously monitor market trends, adopt new technologies, and enhance operational efficiency are better positioned to survive and grow. These findings align with those of Normal et al. (2023), who noted that competitive SMEs are more adaptable and capable of leveraging digital ecosystems to scale operations and expand

market reach. In the online business environment, competitiveness is also closely linked to digital capabilities such as data analytics, search engine optimization (SEO), user experience design, and customer relationship management (CRM). Therefore, SMEs that actively invest in these capabilities are more likely to maintain relevance and sustain performance despite market turbulence.

Another key contribution of this study is the validation of social capital as a significant determinant of SME sustainability. Social capital, defined as the networks of relationships and the associated norms of trust and reciprocity, provides SMEs with access to critical resources, knowledge, and opportunities (Nahapiet & Ghoshal, 1998). In digital business contexts, social capital can be developed through online communities, peer support groups, partnerships with influencers, collaborations with other businesses, and customer engagement on social platforms. The findings suggest that SMEs with strong social capital are more resilient in the face of external shocks, more innovative due to access to diverse perspectives, and better able to mobilize support from their networks. This is particularly evident during periods of crisis, such as the COVID-19 pandemic, where social capital helped SMEs to rapidly adapt by sourcing information, securing financial aid, and exploring collaborative opportunities (Le, 2023). Hence, fostering social capital is not merely a relational exercise, but a strategic imperative for online-based SMEs.

The collective findings from this study emphasize the importance of an integrated approach to SME sustainability. While each factor independently contributes to sustainable performance, their combined effects suggest a more nuanced understanding. For example, a differentiation strategy may be less effective if not supported by high product quality; similarly, competitiveness without strong social networks may limit the firm's access to collaborative innovations or crisis support. This implies that SME owners and managers must adopt a balanced and holistic strategic mindset, aligning operational decisions with both market-driven strategies and relational capital-building initiatives.

CONCLUSION

This study demonstrates that differentiation strategy, product quality, competitiveness, and social capital each play a significant and positive role in enhancing the business sustainability of online-based SMEs. The findings highlight that a well-executed differentiation strategy allows SMEs to carve out unique market positions, while consistent product quality fosters customer trust and loyalty in virtual marketplaces. Competitiveness, driven by agility and innovation, ensures that SMEs remain adaptive in dynamic environments, and strong social

capital enables access to critical resources and collaborative opportunities that support resilience and growth. Collectively, these factors underscore the importance of a strategic, quality-oriented, and relationship-based approach for SMEs seeking to achieve long-term sustainability in the increasingly competitive and digital-driven business landscape. These insights not only extend theoretical understanding in the field of SME development and digital entrepreneurship but also provide practical guidance for business owners, policymakers, and support institutions aiming to build stronger, more sustainable online business ecosystems.

RECOMMENDATIONS

The findings offer several implications for policymakers and SME development agencies. Support programs aimed at enhancing SME sustainability should not only focus on technical training and digital infrastructure but also emphasize strategic capacity-building in areas like branding, quality assurance, competitive benchmarking, and social networking. Governments and industry associations can play a catalytic role by facilitating SME participation in digital marketplaces, providing access to mentoring networks, and encouraging public-private partnerships that help SMEs enhance their market competitiveness. Educational interventions, such as entrepreneurship programs and digital skills workshops, can also be tailored to include modules on strategic differentiation and relational asset development.

Despite its contributions, this study is not without limitations. The use of cross-sectional data limits the ability to infer causality, and the focus on online-based SMEs in Indonesia may restrict the generalizability of findings to other contexts. Future research could explore longitudinal data to assess how these factors evolve over time or expand the scope to include comparative studies between online and offline SMEs or across different cultural and economic environments. Additionally, incorporating mediating or moderating variables—such as digital literacy, innovation capability, or environmental turbulence—could provide a deeper understanding of the mechanisms through which these factors influence sustainability.

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