

Customer awareness and adoption of Islamic Banking in Pakistan

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Abstract

The purpose of this research is to investigate the customer awareness and attitude towards the Islamic Banking. The Pakistan is developing into a hub of Islamic banking and has gained importance in Islamic financial sector due to its fast growing Muslim population. A descriptive study was carried out which involved a 32 items questionnaire grouped in 5 main variables was developed, tested and data is collected from twin cities of Pakistan. The research findings show that there are greater opportunities in Pakistan for development and growth of Islamic financial system because Muslim community is eager to take financial products and they are willing to spend their lives according to Shariah. Furthermore, research also proved that there is a need to educate the Muslim community toward Islamic financial products; service providers need to develop the information system within the communities and Islamic banking institutions are required to work even harder for survival with conventional banking system.

Key Words: *Islamic Banking,, Shariah*

1. Introduction

In today's competitive world, banks are starving to endure survival. After the recession of 2008, due to drastic reduction in demand of products and services, all the financial and manufacturing sectors are facing challenges. Investors are not investing and the boom of credit dealings have resulted in big defaulters. The banking sector today not only faces bad debts, but also finding it hard to maintain capital level and promote investors' interest. In this routine, a glimmer of hope for most of the banks was Islamic banking. It all started back in 1963, when with profit and loss sharing investment by Egypt's MitGhamr Saving Banks was started. After its advent, it prospered in the area of finance, banking, insurance, mortgage, and assets management business with annual growth rate of 10-15 %. But actual development in Islamic banking was started after 1970 with new investment techniques, strategies and product development brought up by Dubai Islamic Bank (DIB), also known as world first

Islamic bank it formed specifically in 1975. The root of Islamic banking is to work according to Shariah Law which states that interest is totally prohibited in Islam because interest has lot of bad effects on society such as their earning capacity, purchasing power and increase poverty, unequal distribution of wealth and credit crisis in an economy. In case of Pakistan Islamic banking is not a challenge because the financial system and investors' interest is now more attracting towards Shariah laws. This also provides Islamic banking further opportunity in the Pakistan to make a prominent position in the Pakistan financial market. The purpose of this research is to look into the role of Islamic Banking in organizational context and how it can help in creating investors' interest. This research will also help the managers to evaluate and assess their investment portfolios according to Shariah Laws. Last but not the least this study will result in helping academics for future implications.

1.2. Objectives of the study

The main endeavor of this proposed research is to understand survival and growth of Islamic banking in Pakistan. The main objectives of this study is to measure the customer awareness of the people towards Islamic Banking, its products, services, its objectives, compliance with Shariah, financial services and customer services and customer attitude based on this awareness.

2. Literature Review

Main objective of Islamic law is to promote welfare of mankind, justice, protection of religious life and prosperity. Islamic legal system facilitates the growth of Islamic finance and to meet the needs of financial markets, Habib Ahmed (2006). Muslims are more eager to lead their lives according to Islamic shariah and law. All kinds of interest are totally prohibited in Islam as it not only leads the economy to the path of crisis but also affect the whole society, Ahmad (2008). Islamic banking is not merely about profit maximization but they focus more on promoting Islamic values, Farook, Hassan and Lanis (2011). More over customer's satisfaction level with respect to the banking products of Islamic banking is more than conventional banking Ahmed et al. (2010). Islamic banking based on Shariah law whereas conventional banking is based on profit maximization, lending and borrowing, findings revealed that in term of cost efficiency and Islamic bank performs better than conventional bank where as in terms of technical efficiency conventional bank give tough time to Islamic bank Shahid et al. (2010). The comparison of Islamic banking and conventional banking system in Pakistan showed that conventional banks are on declining stage due to the financial crises at global level. Where as Islamic banking has emerged as a strong financial system then conventional banking on the basis of assets, financing, profitability and efficiency etc and maintain consistent growth, Awan (2009). Keeping in view the growth, development and prospects of Islamic banking of Pakistan in terms of assets, funds and deposits, Islamic banking with the efforts of bank in Pakistan (SBP) is also playing an active role with the banks which deals with corporate social responsibility, Akram, Rafique and Alam (2011). Islamic banking is rapidly getting recognition in financial market and people are adopting it because it is according to Islamic shariah rules and regulations. Manzoor, Aqeel and Abdul Sattar (2010) investigated motivational, economic, socio-psychological and religious factors that there are greater opportunities in Pakistan for development and growth of Islamic banking system. With an impressing growth of Islamic banking in this contemporary world how Islamic banking compete with conventional banks in regard of customer attitudes and products, Awan and Bukhari (2011). Khattak and Kashif-Ur-Rehman (2010) examined the degree of satisfaction and customer's awareness towards the products and services of Islamic

banking of Pakistan and people are not well aware of some specific Islamic financial products i.e. Murabaha, Ijara etc. The root of Shariah corporate governance comes from Islamic banking and finance. Results have proved that entity in any sector especially in Muslim countries have to follow Shariah corporate governance for their long term sustainability, Muneeza and Hassan (2011).

3.1. Research Methodology

Keeping in view the literature review, 32 item questionnaire grouping in 5 variables along with demographics i.e. service knowledge (SK), Shariah Based (SB), Customer service (CS), objectives (OB), Financial services (FS) was developed that focused on the customer awareness and adoption towards Islamic banking its products.

3.1.1 Sample and Data Collection

Currently, six Islamic banks are working in Pakistan these are Dawood Islamic Bank, Dubai Islamic Bank, Meezan Bank, AlBaraka Islamic Bank, Bank Islami and Emirates Global Islamic Bank. For data collection purpose the researcher chose the branches of Meezan, AlBarak and Bank Islami (three banks out of six) in Rawalpindi and Islamabad. Random sampling technique was used in the study and 300 questionnaires were distributed among the customers and Banks Staff of the selected bank branches.

3.1.2 Analysis Tool

SPSS 16 was used for questionnaire reliability and descriptive analysis of the data collected. Reliability test of the questionnaire was carried out and Cronbach's Alpha was found 0.880.

4. Research Findings

Demographic results revealed that the maximum number of participants filling the questionnaire aging from 26 – 35 years out of which 64 % were males and 36% were females and were either customer, potential customers and employees of sample banks.

4.1 IB and Financial Service Knowledge

4.1.1 Teachings of Islam: Results have shown that more than 58 percent participants agreed that Islamic Banking and financial service have proper knowledge of the teachings of Islam and works accordingly. *4.1.2 Shariah based:* Results have shown that more than 60 percent of sample strongly believes that Islamic Banking and financial service have proper knowledge of Shariah and works accordingly.

4.1.3 Good vehicle to promote Islamic values: 60 percent of participants agreed that the system followed by Islamic Banking and financial service are really helping in promoting Islamic values.

4.1.4 Working as per the teachings of Quran and Sunnah: More than half of the sample agreed to the above statement while perceiving that the rules and regulations given by Shariah experts are according to Quran and Sunnah.

4.1.5 Conformity with the norms of Islam and then in accordance with customer's preferences: It was also found to be perceived true since more than 54 percent of sample agreed that the products and services offered are Islamic and they are in accordance with customer needs and preferences.

4.1.6 Gharar(Risk) free investments: 43 percent of people agreed that Islamic Banking and financial services are investing in less risky options. This answer was more confidently answered mainly by the employees of the banks, since they are 44% of total sample size. Moreover most of the customers just trust the banks that they will secure their investment, regardless of wherever the bank invests.

4.1.7 Indulging in Non Islamic Businesses: Since most of the people believe that the banks are working under rules by Islamic Shariah, they are sure that their investments are used

according to Islamic norms. Moreover according to Islamic teachings it is then the duty of key investor (bank) to make sure that investments are used according to Islamic teachings.

4.1.8 Islamic Products Offered: Majority of people believed that the way of doing business is same in Islamic banks in comparison to conventional banks. The main reason behind this perception is that most of the questionnaires were filled by employees, who agreed that there is not a lot of difference. Furthermore if we look closely into Islamic banking structure and working, it is basis of conventional banking and most of the functions overlap.

4.1.9 Promoting Islamic values and way of life towards staff, clients and general public: 57% of participants agreed to above statement. They perceived Islamic banking as a vehicle in promoting Islam not just by paying interest free returns, but also teaches Islamic values among staff, clients and general public by continuously allocating wealth evenly, sharing losses and distributing Zakat to most needy ones.

4.2. Role Of Shariah Board For Scholars

4.2.1 Role of Shariah scholars while issuing products: Most of the participants agreed that Shariah scholars play their role while issuing different products. Employees also guaranteed that the products are offered after close inspection by expert Islamic scholars.

4.2.2 Shariah board acts as a regulator: 61% of the participants (most of them employees of bank) approved that Shariah scholars from time to time act as a watchdog making sure that the products offered are revolutionized according to Islamic teachings and needs of the customers.

4.3. Islamic Banking and Financial Institutions Customer Dealing

4.3.1 Do not exploit its customers in any way: Most of the people agreed that they trust their banks that they are working in accordance with Islam and do not exploit customer in anyway.

4.3.2 Do not indulge in misleading advertisements: There were mix views since some participants were of the point of view that Islamic banks also indulge in misleading advertisements for more deposits, but all participants agreed that their way of doing business is fair and Islamic.

4.3.3 Do not earn income through unfair means: Most of the participants agreed that Islamic banks work according to Shariah and follow a proper business methodology with fair means of trading. In comparison to conventional banking, Islamic banking can also share loss with investors, providing it with a further chance of getting fairer and realistic.

4.3.4 Free from exploitation, discontentment and strife: This question has mix results because the qualities mentioned can change with employees and staff following the banking procedures. Mostly people think that Islamic banking should improve the conventional way of banking, but it will take time which is basically due to weak technical efficiency on Islamic baking side.

4.3.5 Do you think Islamic Banks and financial institutions are in consonance with the principles of fair dealing, justice and benevolence?: Mostly participants were positive because mentioned attributes are basis of Islamic trading. Moreover since most of the questionnaires are filled by employees, instead of filling the questionnaire with reality, they may be promoting their banks.

4.3.6 Reflecting the values in which they are based: More than half of the participants agreed that in most of the cases employees are trained to act according to the values of Islam. Moreover managers agreed that it is not just professional development that is important to them for their employees; they also focus on personal traits of individuals.

4.3.7 Following Islamic ethics: Most of the people believed that Islamic Shariah teaches Islamic ethics, so without any doubt; banks are following Islamic ethics for their successful Islamic trading.

4.4. Objectives of Islamic Banking and Financial Institutions

4.4.1 Maximizing profits (good percentage of return to investors): The objective of Islamic banks is to maximize profits with safe investments. Most of the participants agreed that as far as the profit is interest free, they want the banks to earn them maximum profits but those profit should be riba free.

4.4.2 Helping in alleviating poverty (poverty eradication): 49 % of sample agreed that since Shariah based business will help in betterment of economy in long run, but this will take some time. Since it has not been so long that Islamic banking has been started in Pakistan, poverty reduction and proper wealth distribution will take time to affect the economy.

4.4.3 Promoting sustainable development projects: Since it has not been so long that Islamic banking has been started in Pakistan, investments directly or indirectly in development projects will increase with time, improving the overall economy.

4.4.4 Providing employment opportunities: 55% of the participants agreed that new system has not only offered new products to customers, but also created new jobs in labor market through new branches for Islamic banking.

4.4.5 Minimizing cost of operations: Participants established that Islamic banking has to reduce the cost since they are offering products with profit and loss basis making sure that they look for loopholes in their control systems.

4.4.6 Enhancing product and service quality: Most participants were of the point of view that Islamic bankers have to enhance products base and improve service quality to make sure that this banking system sustains long term.

4.4.7 Offering viable and competitive financial products: Response to above question was mixed since some of the participants were satisfied from diverse products offered by Islamic baking. All in all, employees and policy makers commented that it will take more time to further improve the competitive financial product range.

4.5. Islamic Bank And Financial Services

4.5.1 Providing enough retail products: Responses to above question were positive at 52% since most of the participants were satisfied from diverse retail products offered by Islamic baking.

4.5.2 Contributing to social welfare: Participants (mostly employees) agreed that most of the Islamic banks are following proper corporate social responsibility and made sure that this is part of their good governance for future.

4.5.3 Collection and distribution of Zakat: Participants (mostly employees) were positive that Islamic banks are making sure that collection and distribution of Zakat is fair and provided to most needy.

4.5.4 Contributing in removing society's inequalities and improving general standard of living: Participants agreed that the basic purpose of Islamic system is to reduce inequalities and improve the overall economy. They perceive that if Shariah rules are strictly followed in future, Islamic banking will surely reduce unequal distribution of wealth and poverty from Pakistan.

4.5.5 Performance judged only through good percentage of profit/return: Participants, mainly employees, approved that in Pakistan they make sure that they use variety of non-financial performance measurement tools for measuring performance of the Islamic system of banking. This not only provides them an extra control on the system, but also helps in fulfilling CSR.

4.5.6 Do you think Islamic Banks and financial institutions use modern technology in performing banking transactions: Both conventional and Islamic banking procedures with respect to technology go hand in hand? Managers of banks mentioned that they are making sure that they further improve the technology to satisfy customers. As far as customers are concerned, they were satisfied from the systems used in banking.

4.5.7 Islamic Banking system completely serves as an alternative banking system: Only half of the sample size agreed because all the customers have their own priorities. Some of them were happy to

get interest free profits, still some investors consider it to be insecure due to fluctuation in interest rate.

6. Conclusion

By analyzing the results following conclusion can be derived that it was found that people have positive attitude and enough awareness towards Islamic banking because most of the results have proved that people in Pakistan are shifting from conventional banking to Islamic banking, which will perform an active role in the Pakistan Financial Market in near future. In Pakistan Islamic banking is perceived to be based on shariah and is working in its true spirit. Since most of the investors, in spite of size of their financial investments are making sure that they generate maximum profits from diverse range of Islamic products. Response from my questionnaire did not deeply measure the effects of economic conditions of a country on development of Islamic banking but still it measures the positive impact of Islamic Banking on economic condition of Pakistan because Islamic banking is asset backed banking whereas conventional banking is not asset backed. It was found regardless of recession and fierce competition, there has been constant increase in customer base of Islamic banking. Furthermore, since most of the people consider it to be a positive step towards developing economy, this perception guarantees optimistic future of Islamic banking in Pakistan. Islamic banks are required to aggressively market their products and conduct awareness sessions to improve the knowledge of the people about the products of Islamic banks and the difference from the conventional banking products and their long term benefits.

7. Recommendations

Islamic banking has some challenges due to financial setup of the developing countries where rules and regulations are more compatible to conventional banking system and some of them due to its early age in the financial sector. Following standards are to be changed;

- Islamic financial system has lack of proper and strong institutional system in Pakistan. Islamic banking needs to improve the branch network throughout the country.
- Moreover Islamic banking has also the shortage of qualified Islamic scholars in Pakistan. To improve the financial system they need to hire more scholars who provide in time and valuable information to service providers.
- Currently Islamic banking is facing the hurdle of different Accounting policies in Pakistan. It is a big obstacle in the way of development of Islamic banking because it creates the problem for internal and external investment.
- It is very important for growth and development of Islamic banking system that the increase in the number of its users. In Pakistan to increase its account holders it is necessary to create the awareness in community about merits of Islamic banking.
- According to my recommendations if Islamic banking wants to get popularity and business then they need to introduce the compatible financial policies and financial tools to conventional banking. Many of Muslims are still confused about to take Islamic banking accounts because they are not satisfied that Islamic banking will fulfill their all requirements in Pakistan.

8. Future Studies

It provides a clear understanding of financing modes of Islamic banking, drawback of interest on economy and benefits of investment through Islamic financial system. This research also provides the indicators of growth of Islamic banking in Pakistan and critically evaluation of challenges of Islamic banking face in developing country like Pakistan. Moreover further research could have been made in the sector of Research and development in connection with all necessary arrangements of conceptual understanding of Islamic finance and banking in Islamic financial sector in general and its impact on economy as a whole. Another area which

can directly affect the growth and development of Islamic banking in country like Pakistan is the role of Government participation and intervention in providing necessary arrangements for legislation and legal framework. Last but not the least, Islamic banking institution should research in Training and Development of employees to make sure that they promote Islamic banking properly.

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Appendix

Reliability Statistics

Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.880	.895	5

Inter-Item Correlation Matrix

	SK	SB	CS	OB	FS
SK	1.000	.765	.700	.574	.632
SB	.765	1.000	.711	.511	.565
CS	.700	.711	1.000	.514	.627
OB	.574	.511	.514	1.000	.701
FS	.632	.565	.627	.701	1.000

Inter-Item Covariance Matrix

	SK	SB	CS	OB	FS
SK	.535	.580	.386	.235	.253
SB	.580	1.075	.556	.296	.320
CS	.386	.556	.568	.217	.258
OB	.235	.296	.217	.313	.214
FS	.253	.320	.258	.214	.299

Age of the	
Age	Percentage
Under 25	10%
26-35	40%
36-45	23%
45 and above	27%

Gender of the

Gender	Percentage
Male	64%
Female	36%
Total	100%

Profession of the respondents

Stake Holders	Percentage
Customer	34%
Employee of Islamic Bank	44%
Shariah Advisor	2%
Local Community	9%
Regulatory Office	0%
Manager of Islamic Bank	11%
Total	100%