

Customers' Acceptability of Islamic Banking: Employees' Perspective in Peshawar

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Abstract

This paper aims to incorporate the banks employees' perspective on acceptability of Islamic banking by the customers of Peshawar. A qualitative approach is adopted for which six in-depth interviews with employees of Islamic banks are conducted. The employees were asked to share their experience regarding customers' acceptance attitude towards acceptability of Islamic banking. Collected data was analyzed through thematic analysis technique and its synthesis with the current literature. Through data analysis a theoretical framework is developed, which highlights the factors which drive customers towards Islamic banking, as witnessed by the employees. The practical implication of analyzed data evident that a new model could be developed on the basis of four determinants of human preference namely: inner satisfaction, time, faith and market forces.

Keywords: Customers' attraction, Employees' perspective, Islamic banking, *Riba*

Introduction

Islamic banking is exponentially growing in assets base, outreach, and product lines (Ullah, 2015). To support this growth, both researchers and practitioners are interested to know the factors that cause the acceptance of Islamic banking by the customers. However, there seem many external and internal factors needs to be explored and described. The State Bank of Pakistan also introduced regulations to accelerate the growth through products that are acceptable to customers and market (Volk, 2010). The external factors such as regulations affect customers' acceptance at large scale but are well predictable whereas the internal factors are more unpredictable and contextual to the customers and involved employees. For instance, the customers'

preferences for the bank and deposits are largely impacted by the customer own contextual factors.

The current literature is more focused on the abstract factors such as the service quality, revocation of *Riba*, information about the Islamic banks, and religion sentiments. Other studies show some indications towards the difference between conventional and Islamic finance (Abdel Karim & Ali, 1989), which might cause acceptance of one over the other. This paper further explores the phenomenon to find out factors which might affect the Islamic banking acceptability. The research takes the banks employees' perspectives because employees usually encounter multiple customers over prolong period and their deep experiential insights can bring in novel findings. The rest of the paper is organized as follows; next section discusses the currently known factors through a review of literature. Then a brief research design is explained followed by an analytical account and conclusion.

Literature Review

Current debates in literature identify mainly four factors of customers' acceptability of Islamic banking namely revocation of *Riba*, service quality, religion, and knowledge of banks with the customers.

Revocation of *Riba*

The most commonly understood reason of accepting Islamic banking is the prohibition of *Riba* which exist in the conventional banking system. *Riba* means usury and that causes economic exploitations within society. *Riba* is prohibited which could be authenticated from the verses of Quran:

That which you give as Riba to increase the peoples' wealth increases not with God; but that which you give in charity, seeking the goodwill of God, multiples manifold" (30:39) (Surah al –Rum, verse 39)

Riba is completely prohibited in Islamic banking system and Muslims have firm belief on it that is why the conventional banking systems are diverting towards Islamic model. There are two types of *riba* i.e. *Riba Al Fadl* and *Riba Al Nassia*. *Riba Al Fadl* deals in buying and selling while *Riba Al Nassia* deals in lending and borrowing (Lewis, 1983). In Pakistan *Riba* free economy was first introduced in February 1980 when the panel of

economists and bankers put forward report about *Riba* free economy which was reviewed by council in June 1980 and action plan was sketch out in December 1981. After that *Zakat* was introduced in place of *Riba* to gain some commission (Mehmood, 2002). Though Islam prohibits the payment and receipt of *Riba*, but encourages sharing of profit (Abdel Karim & Ali, 1989). In Islamic banking, deposits are treated as profit-sharing mechanisms so, banks have to develop financial transactions to carry out their proposed ideas and in these transactions the *Riba* factor is attempted to be abolished. The transactions were based on *Mudarabah* (silent partnership), *Musharakah* (partnership), *Muqaradah* (debt and equity financing), *Murabaha* (mark-up), *Salam* (forward sale). (Muhammad , 1993).

Many authors advocating Islamic economic and financial system which is free of *riba* (like (Ahmad & Hassan, 2007); Usmani, 2002, Jan, Ullah, and Asutay, 2015). Haque (1986) proposed a model of the *Riba* free banking system on the basis of certainty and uncertainty. This implies the effect of risk on rate of return, i.e. the rate of return should not exceed when there is no risk in the transaction. They also proposed two contracts ‘individual firm- specific’ and ‘project-specific’ in order to maintain healthy investment between borrower and lender as they have diverse information regarding their investments. Although their model was credible, but still there were some of the practical issues observed in Iran and Pakistan which implies that banks are not amenable to share the loss.

Service Quality

Service quality of the banks also impacts the customer acceptability. Service quality is a fleeting and abstruse construct that is difficult to measure and define (Cronin & Taylor, 1992). Bolton *et al*, 1991 define service quality is an attitude of the customers’ satisfaction after performance. According to Dick (2007) there are some customers who pay higher prices in order to get more quality services. Sutton (1991) suggests that customers prefer higher quality good and if not provided by the company then such firms are galvanized out of the market. For keeping the firms in market Parasuarmann and Zeithmal in 1988 suggested two scales for measuring the service quality of the firm, namely ‘SERVQUAL’ and ‘SERVPERF’. SERVQUAL is a 22 item scale having five dimensions (tangible, responsiveness, reliability,

assurance and empathy). SERVPERF model is the measure of service quality from customers' perception on the basis of service provider performance (Setijono *et al*, 2008).

Mukherjee *et al*, (2003) also proposed that service quality is the key driver for the performance of the banks and causes tangible profit. Bolton *et al*, (1992) evidence that satisfaction is the antecedent of service quality which concludes that if the bank has a quality service attitude towards the customer then retention and repurchase is a green signal for profit maximization of banks. Islamic banks in Islamic countries face stiff competition not only from other Islamic banks also from rival conventional banks for that they have to provide better customer services to maintain the pace in the market and it is the preeminent duty of Islamic banks to achieve higher levels of customer satisfaction (Ahsanul *et al*, 2009).

Religion

Islamic banking is based on *Shariah* Law. The principle sources of Islamic law are *Quran*, the revelations given by God, and *Sunnah*, which are the customs and actions recorded by the follower of the Prophet ﷺ (Noughton, 2000). Alongside rituals and ethics, *Shariah* covers man to man dealings including economic and financial dealings (Darrat, 1988; Ullah, 2014). On the basis of Islamic principles e.g, *Tauhid*, *Adala*, *Baya*, *Shura* and *Khalifa* new economic such as *Khilafah*, *Tazkiyah* and *Hisab* are formulated (Gambling *et al* 1991). These principles also inform the Islamic development goals such as knowledge, work and social welfare (Jan, Ullah, and Asutay, 2015).

In Pakistan, a *Shariah* Ordinance was established in 1988 to commensurate *Shariah* principles in financial institutions. A law was promulgated entitled 'the enforcement of *Shariah* Act 1991'. To ensure that economic system of Pakistan becomes Islamic, the objective of elimination of *Riba* from all the business transactions in shortest possible time was putted as the primary objective (Mehmood, 2002).

Shariah also prohibits speculative trading, hence, in this regards Malaysia is structuring a platform to do *Shariah* complaint stock trading by establishing Islamic brokerage house and Islamic funds in Islamic index (Noughton, 2000). As in Pakistan there is Meezan bank index for carrying out Islamic stock trading. Islam sets down the code of conduct for every aspect of life, including social and spiritual as all the economic injunctions are defined

explicitly in the *Quran* (Pickthall, 1953). Customers take into account these factors while accepting any financial services.

Knowledge about Islamic Banks

The customer knowledge of banking also play a role in the acceptability of Islamic financial services. Ramaiyah, Zain & Ahmed (2007) conducted a survey about the customers' perception on Islamic banks. The two factors which influence their decision are quality, service and better branching network. He also concluded that the physical outlook of the bank doesn't matter instead the employees' attitude and price for the service play important role in selection of bank for corporate customers. There is also the consideration of quick and dynamic service of reputable banks and confidentiality while selection of Islamic banks in the light of Erol *et al*, 1989 study. The Malaysian customers prefer speedy transactions, friendly bank personnel and efficient services (Ahmad, 2002). Haroon *et al*, (1994) in their concluding remarks evidenced that Islamic bank's corporate customers prefer the cost of service as vital in selection criteria instead of the nature and procedure of the product. Customers' approach towards service quality influences the employees' perception of the service-related practices (Schneider *et al*, 1980). If the organization engages in practices and is aware of the environmental pressure like the changes customers demand, according to the demand of time, then such firms flourish and out shine in delivering services.

Most of the studies are from customers' eye and very rare from employees point of view which gave rise to new perspective under discussion as employees are the drivers of banks, there should be study form their aspect because they might give responses on the basis of their experience which would definitely be different from all the studies conducted so far. The service quality scales i.e. SERVQUAL and SERVPERF should be incorporated in banks for measuring service quality.

Research Methodology

The researchers find the inductive approach suitable for the study because new variables are identified from bank's employees' perspective. The research is qualitative in nature as the literature review is only for the sake of evidence for the purpose of study and to identify the underlying factors of customer acceptability of Islamic banking. The literature review is limited and guides the research questions and provides a room for the researcher to

explore the phenomenon to find new factors (Clark, 2007). After collecting six interviews the data was saturated and due to similarity in answers, researchers conducted two more interviews in order to authenticate the information. The main source of data gathering was in depth interview. Interviews are backed by observation because sometimes researcher presence may influence the respondent's attitude, so for authentication of data this method was used. A thematic analysis method is used. According to Stirling (2001), thematic analyses derive themes which are important in a text at different levels, and thematic network help in facilitating the representation of these themes. This analysis in the research includes the formation of codes followed by sub themes to drive the main theme. The themes generated are *Riba* free banking, satisfaction, awareness, and acceptability.

Analytical Evidence

***Riba* Free Banking**

As referring to literature “*Riba* is the charge for the privilege of borrowing money”. According to this definition ‘privilege’ is used as a sugar coated word, though it is mere exploitation within society. The literature states *Riba* rise in exchange of homogeneous commodities. *Riba* free transactions were omitted with profit and loss sharing accounts and government imposed the fixed percentage for collection of *zakat* on income kept for the year of the individuals and named it as Islamic taxation. Literature quoted that *Riba* free transactions were introduced by Islamic ordinance in February 1980 and executed in December 1981 in Pakistan. Elimination of *Riba* accepted warmly by the public in the early stages, but as time passes; the non-followers mold the system according to their own ease and introduced *Riba* transactions which gave rise to many unwanted occasions like exploitation of society, unjust earning etc.

Customers accept Islamic banking due to religious sentiments as evident by the respondents. There are certain factors which influence their selection such as exploitation of society, effect on inflation and protection of five rights of humanity namely right of life, religion, wealth, intellect and wisdom. These three factors are identified by the employees of banks which affect the attitude of acceptability towards Islamic banks. *Riba* exploit the society as it is fixed amount which has to be paid even if the customer is unable to pay. This affect the principle of Islam namely welfare for the society. Hence, the customers having

knowledge of this principle are more likely to select Islamic banks than those having less knowledge. Stiff inflation is considered as evil for the society because this factor is inversely related to the *riba* rate which states that if rate increase inflation decreases because people will prefer saving in the bank and the borrowing will be less which ultimately affect the economy as purchasing power of customers decrease. *Riba* affected the rights of humanity. In order to protect these rights customers select Islamic banking. Again dropping down the curtain on this statement that knowledge about Islamic banking is mere stone for selecting Islamic banking.

Satisfaction

Satisfaction actually means the attitude of the customers to purchase or consume a product (Yi, 1990). This slightly affirms with the thought process of researcher that satisfaction is the factor which directs customers' wants, if the customer is satisfied with a product then he will want it more and will spread positive word of mouth. It can be concluded from the above statement that customers' satisfaction and service quality are interrelated ultimately affecting the profit of the organization. Some of the scholars stated that it's difficult to measure the service quality from customers' perspective because every individual have their own set of priorities on the basis of which they prefer their services. This implies that the delivery of services must match with the expectations of customers.

Satisfying each and every customer is near to impossible as the demands and nature vary with individual. Employees of Islamic banks consider customer satisfaction prior factor while considering attitude of acceptability and they are well aware about the major issues associated with customers. The bankers are also working hard to satisfy their demands in order to establish positive impact among customers. Interviews with the employees evident that employees of Islamic banking should be satisfied because they are the representation of the organization. Employees' responses suggested that customers need to have access to shariah advisor in order to get complete knowledge about shariah principles.

Employees of the Islamic banks have highlighted impressive finding which gave birth to future research model. The findings state that the customers wants are driven by four forces of human preference namely market forces, inner satisfaction, and faith and time management. Either the customer would be driven by external factors namely market forces/time management or

inner factors namely inner satisfaction/faith. Employees' responses states that if the customers are driven by inner factors are more satisfied than the customers' who change their preference on the basis of external factors.

Awareness

Customers preferences differ according to the area and the culture of that region as the people of Indonesia are most aware of the Islamic banking practices and products because there is a complete amalgamation of Islamic banking in the system of trading. Whereas some of the countries the customers are not aware of the products, in some regions they are aware but not practicing it. Muslims are more anxious to lead their lives according to Islamic law as *Riba* is prohibited from banking practices. This shows a positive signal for the Islamic banks to flourish in this saturated market of conventional banking as Islamic banking promotes Islamic values rather than only profit maximization. Islamic banking provides cost efficient services and conventional banking provides technical efficiency. The customers having such knowledge are more likely to select the bank then with less knowledgeable customers.

Findings evidenced that employees are well aware of the significance of Shariah knowledge and are of the opinion that front desk officers are the representations of the organization. Employees somewhere makes the customers responsible for the selection of Islamic banking as some responses evidenced that customer prefer their own perception while making any choice.

Acceptability

There is an issue in accepting Islamic banking among customers as there is lack of clarity of Shariah compliance and awareness of Islamic banking practices among individuals. However, this is important to create a clear background of the Shariah and its laws among the general public in order to create positive word of mouth. Analyses of the data also evident that Islamic banking demand is dependent on the study of potential customers' need for Shariah compliant products and their religiosity level to interpret Shariah principles in banking practices. Here the analysis is diverted towards the marketing strategy of bank to attract potential customers and make it acceptable among them. Islamic banking promotion could be done through educating customers not only Muslim but also non-Muslim customers to change the perception holistically. This means that Islamic banks

have to work on creating the brand name in the world by targeting the basic need for Shariah among customers.

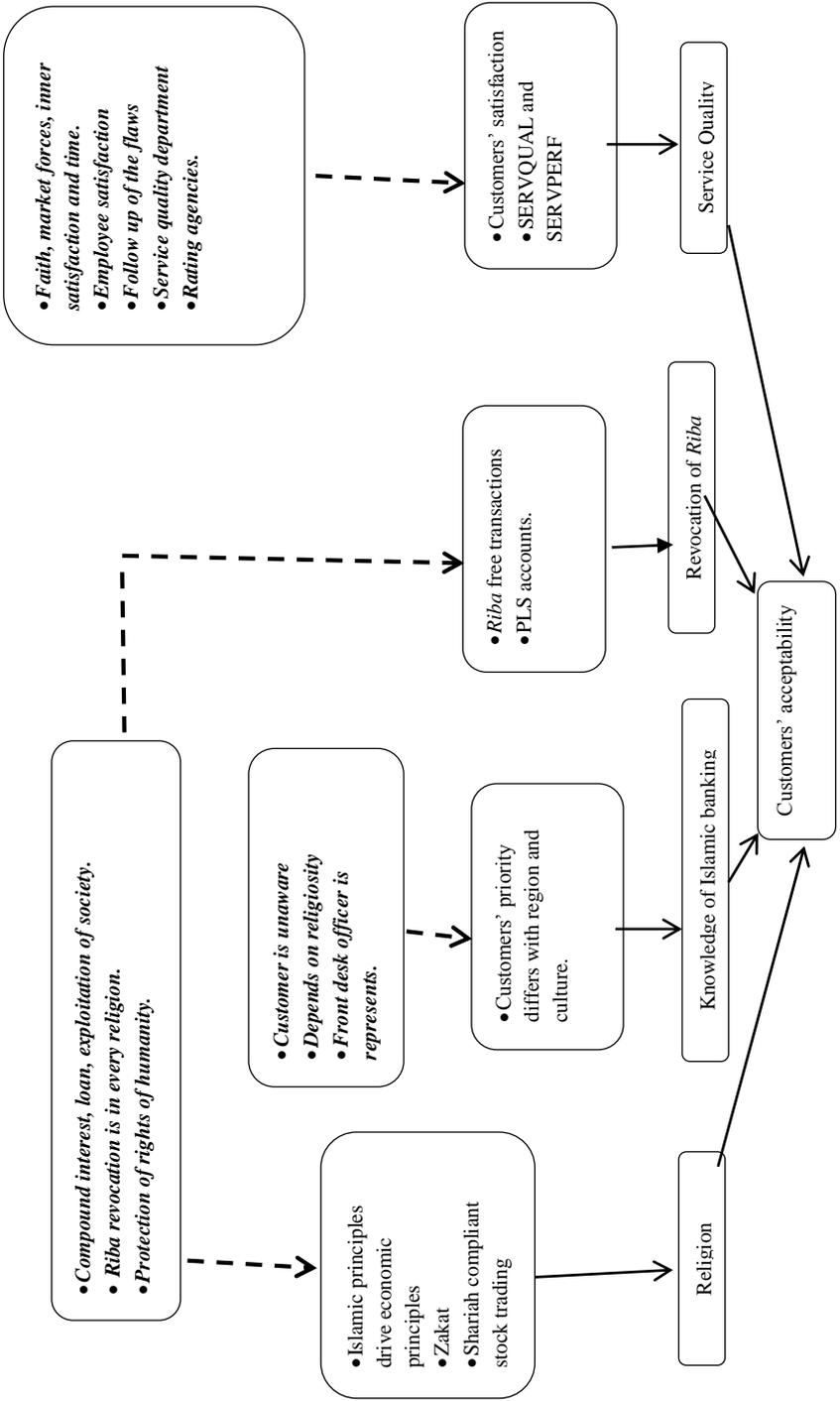
Employees states that there are different areas bank have to work on like service quality, arrangement of separate promotional teams working continuously to create awareness about Islamic banking practices through seminars, workshops etc. Associating with educational institutes should be prime concern for the banks because the employees are not aware of the theoretical updated knowledge although they are practicing but that practice should align with current researches in the field. This approach would give an edge to bank in markets and customers would get appealed in selecting Islamic banks.

Theoretical Framework

Through the synthesis of literature and findings, a new theoretical framework is developed. In this framework the independent variables are service quality, revocation of *Riba*, knowledge and religion whereas customers' acceptability is dependent variable. Therefore, it can be concluded from literature that customers accept Islamic bank by keeping in view revocation of *Riba* as one factor and the level of knowledge they have regarding Islamic banks as another factor. Whereas from employees' perspective customers are not aware of the service quality of the bank as there is no set benchmark. Accepting Islamic bank on the basis of religion is going to be a positive aspect of the employees of Islamic bank as they might attract them emotionally. From employees' angle revocation of *Riba* is one of the factors which is co related to religion that's the reason there is little literature regarding religion as independent factor for selecting Islamic banking. Most of the research has concluded *Riba* in religion as Islam revoke the exploitation of society and *Riba* is profiteering of the society. According to state bank's regulations PLS accounts will be open on the basis of *Mudaraba* which means that the bank is the *Mudarib* (manager) and the customer will be *Rabulmaal* (owner) as the money is in its hand

This theoretical framework shows the summary of literature and link between the variables with the factor under research. The new findings from the analysis are presented in the theoretical framework with highlighted in italics. The explored areas are already discussed in analysis chapter. The point to ponder is interconnection between religion and revocation of *Riba* because respondents were of the view that the prohibition of *Riba* is

semantic order which is part of religion, it should be interrelated. Another factor identified is asset backed securities, according to employees customers feel secure in Islamic bank that's why opt for it. But the question arises that conventional government banks are also giving asset backed securities, then why customers are selecting. To justify researcher went through the literature and talked to different employees, then came to conclusion that customers select it because some of them are prioritizing their preference and second factor as asset backed securities while selecting Islamic banking.



Conclusion

This paper provides an insight of the employee's perception about the customers' acceptability of Islamic banking. The identified factors suggest that religion including the revocation of *Riba* is the major factor which compels the customers to motivate and select Islamic banking for transactions. Therefore, this can be inferred that Islamic banking employees have an edge since being Muslims customers will approach if they are faith driven regardless of return. This statement means that according to employees, majority of the Islamic banking customers are faith driven along and if it gives good returns then it is an edge for the customer. Another factor highlighted is the asset backed securities in Islamic banks, although the government conventional banks also have this edge, but if the customer is religious than he would prefer Islamic banking and would not concern for security or any fear of bankruptcy as the mechanism of Islamic banking is asset backed.

Hence, the study concludes that *Shariah* understanding is important for every employee working in Islamic banks for that there should be acknowledgement courses along with awareness program for customers to ensure authentication of knowledge. Government should be involved in amalgamation of theory in practice as it is the regulatory body. On the basis of four determinants of human preference namely market forces, time, faith and inner satisfaction, customer drive their wants for Islamic banking, according to employees. Further research could be conducted in driving model for identifying customers' preferences in accepting Islamic banking. By identifying customers' preference level the banks would better be able to attract huge lot of customers and would soon be market leader in Islamic banking industry.

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