

Corporate Customer Perceptions of Islamic Banking Products and Services*

Norafifah Ahmad¹ and Sudin Haron²

ABSTRACT

The Islamic banking system has been established in Malaysia since 1983. To date, Islamic banking products are available at two full-fledged Islamic banks, and at all commercial and merchant banks. However, these products are still not fully accepted by customers. At the end of 2000, for instance, the total deposits at conventional banks amounted to RM 381 billion and only RM 31 billion in Islamic institutions. Since corporate customers are key players in the economy, it is imperative that the reasons for them to choose or not to choose Islamic system be studied. This seminal study explores the perceptions of persons responsible in financial affairs of public listed companies in Malaysia. Among the issues covered in this study are usage of conventional and Islamic banking facilities, respondents' understanding of the Islamic banking system, and their personal opinion on various aspects of Islamic banking products.

I. INTRODUCTION

Malaysia is among those Muslim countries that are committed to developing not only an Islamic banking system, but a complete Islamic *financial* system. Islamic banking started in Malaysia in 1983, when the first Islamic bank, Bank Islam Malaysia Berhad (BIMB), commenced operations. It was the objective of the Malaysian government to develop Islamic banking parallel to the conventional system. Instead of establishing many new Islamic banks, the government introduced the concept of Islamic windows, which allows existing conventional banks to introduce Islamic banking products to customers. This concept was initiated in March 1993, when the central bank, Bank Negara Malaysia (BNM), introduced its Interest-Free Banking Scheme. Twenty-one Islamic financial products were developed, with only three major banks participating initially. By July of the same year, this scheme was extended to all financial institutions in Malaysia. By the end of 2000, the Islamic banking system was represented by two Islamic banks, seventeen domestic commercial banks, five merchant banks and seven discount houses. There were also four foreign-owned banks providing Islamic banking products and services.

The step toward developing a complete Islamic financial system began with the fostering of both Islamic capital and money markets. The former started when the Malaysian government issued Islamic bonds in 1983. To further enhance the development in the capital market, Islamic private debt securities were introduced. At the end of 2000, a total of RM 22,935 private debt securities were issued, out of which RM 6,278 were Islamic bonds (Hassan 2001). The establishment of BIMB Securities in 1994, as Malaysia's first Islamic stockbroker, was the first step toward promoting an Islamic equity market. Apart from providing Islamic broker houses and Islamically managed funds, a separate Islamic Index was established. This index comprises 179 permissible stocks on the Kuala Lumpur Stock Exchange (New Horizon, 1996). Muslim investors have been able to invest directly in *halal* (permitted) counters. Conventional securities firms also set up their own Islamic stockbroking windows to advise investors on *halal* stocks. As of July 1996, 364 stocks of the total 633 listed on the Kuala Lumpur Stock Exchange (KLSE) were considered *halal*. On 17 April 1999 the KLSE *Shari'ah* Index was launched to facilitate public investment in instruments in line with the *shari'ah* law.

The BNM further boosted the growth of a Malaysian Islamic financial system by pioneering an Islamic interbank money market in January 1994. This market was the first Islamic money market in the world. In the year 2000, the volume of funds traded in this market was RM 301.9 billion (BNM Annual Report, 2000).

Malaysia also plays a major role in developing an international Islamic financial system. The first step taken was realigning Labuan from an offshore financial center to an international Islamic financial center. The first international Islamic financial market was to be established in Labuan at the end of 2001.

As a result of the financial turmoil in 1997 and the liberalization of the world banking system, Malaysia has developed a ten-year plan known as "Financial Sector Stability." The aim of this plan is to create a more efficient

¹ Senior Lecturer, School of Banking and Finance, Northern University of Malaysia, Sintok, Malaysia.

² Dean, School of Banking and Finance, Northern University of Malaysia, Sintok, Malaysia.

and competitive, innovative, technology-driven, and strategically more focused financial system. The plan includes the Islamic financial system as a component that can be further developed to become the key player in the Malaysian and international banking sector.

Even with the support of the government in introducing various measures to develop Islamic finance, its success is heavily influenced by the market players. The market share of Islamic banking assets, deposits and financing reflects public acceptance of this system. For example, the total assets in the Islamic banking system were 6.9% of the total in 2000, while Islamic banking deposits and financing constituted 7.4% and 5.3%, respectively. Malaysia is a country in which Muslims represent half of its population and which is governed by a coalition government led by a Muslim-based party. That despite this, the total funds deposited in the Islamic system remain insignificant compared to the total deposits in commercial banks, is a notable indicator of public unwillingness to use the system.

Haron et al. (1994), who pioneered the research on bank patronage in Malaysia, find that almost 100% of Muslims and 75% of non-Muslims were aware of the existence of Islamic banks. Most of them wished to develop a relationship with these banks, but only if they had a complete understanding of the system. The study used retail customers as its samples, and the findings showed that bankers considered retail customers less important than corporate customers. The latter were considered crucial in generating profits for the banks, and thus it is important that a study on their perceptions of Islamic banks be carried out.

This study examines the existing usage of Islamic banking facilities, the level of understanding of Islamic banking features among corporate financial controllers, their roles in switching and using banking products, and their personal opinions toward Islamic banking products. While the government can use these findings in formulating additional strategies and policies, where appropriate, the Islamic bankers will be able to understand the needs of corporate customers, by providing services to fulfill these needs.

This paper is divided into five sections. Section two highlights findings of previous research that deal with corporate customers' perceptions on banking products and services, section three discusses the methodology of our research, section four presents the findings, and the concluding remarks and suggestions for future research are provided in section five.

II. LITERATURE REVIEW

With the exception of a few studies that used individual and small business customers as samples, no attempt has been made in the area of corporate customers' understanding of Islamic banking in mainstream publications. Similarly, there are only a few published works that relate to corporate customers' perceptions on the quality of conventional banking services.

Turnbull (1983) was among the first researchers to study the perceptions of corporate customers toward their banks. He examined the relationship between forty-four corporate customers in the United Kingdom and their bankers, and found that size played an important role in maintaining split banking practices. Another important finding was that large corporations tend to prefer foreign banks to local banks.

Rosenblatt et al. (1988) sampled 423 Canadian corporate treasury personnel in their study to determine the responsible person(s) in selecting bank(s) for the organization, the factors attributed to the selection of the bank(s), and perceptions of these personnel on the bank's service quality. They found that almost half of the corporate treasurers were solely responsible for the selection of the bank(s). The two factors that influenced their decision-making were better branch networks and the quality of services. Half of the respondents also preferred the bank to assign special officers familiar with customers' business operations. The corporate treasurers were also more concerned about quality products and services than innovative products. They were not keen on the concept of the "one-stop banking center."

Turnbull and Gibbs (1989) conducted a study using "large" and "very large" companies in South Africa. The objectives of their study were to find factors that were considered important among corporate customers in selecting their banks, and whether companies have single or split banking relationships. The findings generally showed that the corporate customers felt the quality of service to be the most important factor in establishing a relationship. Other influential factors were quality of staff, the bank manager's attitude, and price of service. Although very large companies considered quality of service the most important factor, both price and quality of staff were equally important. Split banking relationships were common among corporate customers. Almost all of the treasurers agreed that the physical appearance of banks had no impact on their selection process.

Chan and Ma's (1990) study in Hong Kong was aimed at understanding corporate customers behavior on split-banking, bank-switching, factors that attribute to patronage, level of awareness, and usage of banking product and services. They found that corporate customers preferred to use big and reputable banks, and split banking.

Corporate customers would only switch their banks if the new bank could show that the quality of its products and services was superior.

Tyler and Stanley (1999) used orthodoxy-grounded theory in their study, with the objective of identifying key elements of perceived service quality by large corporations. They found that elements considered important were reliability, assurance, empathy, responsiveness and pro-activity.

The studies of Erol and El Bdour (1989) and Erol et al. (1990) are considered the earliest patronage studies on Islamic banking. Using both conventional and Islamic bank customers, they found that customers who patronized Islamic banks perceived that the three most important criteria in bank selection were the provision of fast and efficient service, the bank's reputation, and confidentiality.

Haron et al. (1994) sought to establish the selection criteria used by Muslim customers in Malaysia when selecting their banks. The three most important criteria perceived by Muslims in Malaysia were fast and efficient service, speed of transaction, and friendly bank personnel. Another important contribution from this study was the potentiality of individual customers in patronizing an Islamic bank when they had knowledge of this new system. 80% of Muslim and 53% of non-Muslim respondents indicated that they would consider establishing a relationship with an Islamic bank if they had substantial understanding of its operations.

While applying Haron et al.'s study, Gerrard and Cunningham (1997) found that as with their Malaysian counterparts, Singaporean Muslims were more aware of the existence of Islamic banking than non-Muslims. Similarly, this study found no evidence of Muslims and non-Muslims differing in their bank's selection criteria. Gerrard and Cunningham's study did not include any question that could measure the intention of their respondents to patronize Islamic banking.

Metawa and Almossawi (1998) focused on customers of Bahrain Islamic Bank and Faisal Islamic Bank of Bahrain. They found that customers of these two Islamic banks considered Islamic principles the most important factor when selecting Islamic banks. The second most important factor was the reward extended by the banks, followed by influence of family and friends, and convenient locations. This study also indicated that socio-demographic factors such as age, income and education were important criteria in bank selection. The finding that religion, in the form of Islamic principles, was the most important reason for customers' patronizing Islamic banks countered the findings of Haron et al. (1994), and Gerrard and Cunningham (1997).

III. METHODOLOGY

The respondents participating in this exploratory study were the persons responsible for the financial affairs of companies listed in the Kuala Lumpur Stock Exchange. Research assistants made initial telephone calls to selected companies for the purpose of identifying these persons. Once the person was identified, a call was made to explain the intention of this research and the types of assistance required from him/her. A total of 100 respondents were identified and willing to participate in this study. These respondents were financial directors, financial managers, general managers of finance, and accountants.

Out of the 100 questionnaires sent to all agreed participants, 45 were returned. No further attempt was made to increase the samples. The questionnaire contained five sections; the first section was designed to gather information about the respondent's personal background. The profiles of the respondents are shown in Table 1, below. About 80% of the respondents were non-Muslims. This study therefore reported mostly the opinions of non-Muslims toward Islamic banking. About 55% of the respondents were less than forty years old, with most having professional qualifications such as CPA, CA and ACCA. About 60% of the respondents had been working for their companies for less than five years.

TABLE 1: PROFILE OF RESPONDENTS

	N	%
1. Religion		
Muslim	9	20.0
Non-Muslim	35	77.7
Missing Value	1	2.3
	45	100.0
2. Age		
<30 years	4	8.8
30-39 years	21	46.7
40-49 years	14	31.1
50 and above	5	11.1
Missing Value	1	2.3
	45	100.0
3. Qualifications		
University/College	12	26.7
Professional	20	44.4
Both University/Professional	13	28.9
	45	100.0
4. Years in the present position		
< 1years	7	15.6
1-5 years	14	31.1
6-10 years	11	24.4
more than 10 years	13	28.9
	45	100.0
5. Years with the present organization		
< 1 years	7	15.5
1-5 years	21	46.7
6-10 years	7	15.6
more than 10 years	10	22.2
	45	100.0

In the second section of the questionnaire, the respondents were asked to indicate the usage of common conventional and Islamic banking facilities and derivatives by their companies. The banking facilities and derivatives included overdraft, term and fixed loans, letters of credit, trusts receipts, bankers acceptances, export credit refinancing facilities, bank guarantees, notes issuance facilities, bonds, current accounts, fixed deposits and other facilities. With regard to Islamic banking, the respondents were asked when their company started using these facilities.

The third section of the questionnaire was designed to measure the respondents' overall knowledge of the Islamic banking system. The questions asked in this section included those that measured the respondents' level of understanding of the concepts and principles of Islamic banking. The questionnaire in the fourth section was designed to determine the role of respondents in the decision-making process of the bank selection. The final section of the questionnaire sought respondents' perceptions on some general matters of which answers could be used by Islamic banking product and service providers in their effort to win these customers.

Since this study is exploratory in nature, no rigorous statistical technique was used in analyzing the data.

IV. FINDINGS

A. Usage of Banking Facilities:

The banking facilities used by respondents are shown in Table 2. All the respondents used current accounts for their daily transactions, while 75% had conventional fixed deposit facilities. Overdraft, followed by bank guarantee, was the most popular facility for financing and trade facilities, while bond and note issuance facilities were unpopular among the respondents.

TABLE 2: USAGE OF CONVENTIONAL/ISLAMIC BANKING FACILITIES/DERIVATIVES

Types of Facilities	Conventional		Islamic	
	N	%	N	%
Overdraft	42	93.3	3	6.7
Term/Fixed loan	33	73.3	5	11.1
Letters of Credit	21	46.7	3	6.7
Trusts receipts	15	33.3	2	4.4
Bankers acceptance	25	55.6	5	11.1
ECR	3	6.7	1	2.2
Bank guarantee	38	84.4	3	6.7
Note Issuance Facility	5	11.1	1	2.2
Bond	8	17.8	1	2.2
Current Account	45	100.0	11	24.2
Fixed deposit	34	75.6	4	8.9
Others	6	13.3	2	4.4

Based on the findings in Table 2, it seems that Islamic banking products were not popular among Malaysian corporate customers. Only eleven respondents maintained banking relationships under the Islamic banking system. Despite Islamic banking having been established more than 15 years ago, most of the respondents started patronizing Islamic banks less than five years ago.

B. Knowledge of Islamic Banking

As indicated in Table 3, the respondents indicated that they had knowledge of the Islamic banking system, but more than 65% indicated that their knowledge was limited. Although the majority of the respondents were non-Muslims, they knew that Muslims were forbidden to engage in conventional banking, due to the Islamic prohibition on interest. This table also indicates that there was a misconception among the respondents about the objective and philosophy of the establishment of Islamic banks. About 65% of the respondents believed that Islamic banks must adopt profit-maximization principles in order to survive in the competitive business environment: a perception contradictory to the objective of Islamic banks, i.e., a combination of moral and profit motives. The lack of knowledge among the respondents of the Islamic banking system was further confirmed when they were questioned about the principles used in Islamic banking. While 38.1% of the respondents were unsure of the nature of the profit-sharing principle, about 50% believed that this was the only principle used by Islamic banks to replace interest. They were unfamiliar with other principles such as *mudaraba*, *bay' mu'ajjal*, *ijara*, *istisna'*, *bay' salam*. This unfamiliarity is to be expected since 80% of the respondents were non-Muslims.

TABLE 3: SALIENT FEATURES OF THE ISLAMIC BANKING SYSTEM

	N	%
1. Islamic banking was introduced because Muslims are prohibited from associating themselves with interest as practiced by conventional banking system.	2	4.8
Absolutely untrue	5	11.9
Untrue	4	9.5
Not sure	-	-
True	10	23.8
Absolutely true		
	21	50.0
2. Both Islamic and conventional banks must adopt a profit-maximization principle in order to survive in this competitive business environment.		
Absolutely untrue	2	4.7
Untrue	10	23.3
Not sure	3	7.0
True	19	44.2
Absolutely true	9	20.9
	43	100.1
3. The profit-sharing principle is the only principle that can replace the element of interest in the operations of an Islamic banking system.		
Absolutely untrue	-	-
Untrue	5	11.9
Not sure	16	38.1
True	15	35.7
Absolutely true	6	14.3
	42	100.0
4. How do you rate your level of overall knowledge of Islamic banking?		
Very knowledgeable	-	-
Knowledgeable	4	9.1
Understand partially	11	25.0
Limited knowledge	29	65.9
No knowledge at all	-	-
	44	100.0

C. Roles of Respondents

The findings in Table 4 indicate that only one respondent had no authority at all, while 16% had no influential power. The rest of the respondents were those who made influential recommendations, took part in decision-making processes, or were authorized to make decisions. In most cases the respondents were those who had the power to determine relationships with banks.

TABLE 4: ADMINISTRATIVE MATTERS: RESPONDENTS' ROLE IN BANK ACTIVITIES

	N	%
1. Opening an account with a new bank.		
Recommendation with influential power	19	42.2
Recommendation with no influential power	7	15.6
Authorized to make decision	5	11.1
Take part in decision-making	13	28.9
No authority at all	1	2.2
	45	100.0
2. Applying new financing facilities.		
Recommendation with influential power	14	31.1
Recommendation with no influential power	11	24.4
Authorized to make decision	2	4.4
Take part in decision-making	16	35.6
No authority at all	2	4.4
	45	99.9
3. Applying additional financing facilities.		
Recommendation with influential power	14	31.1
Recommendation with no influential power	13	28.9
Authorized to make decision	2	4.4
Take part in decision-making	14	31.1
No authority at all	2	4.4
	45	99.9
4. Terminating a relationship with the existing bank.		
Recommendation with influential power	17	37.8
Recommendation with no influential power	10	22.2
Authorized to make decision	3	6.7
Take part in decision-making	13	28.9
No authority at all	2	4.4
	45	100.0

Similar trends were apparent in the case of applying new financing or additional facilities, and ceasing relationships with bank. In both cases about 70% of the respondents had either made influential recommendations, taken part in decision-making, or were authorized to make decisions.

D. Potentiality of Islamic Banking

As indicated in Table 5, few respondents believed that religion was the only reason for customers to select Islamic banks. More than 55% felt that both religion and economics were factors. About 50% believed that Islamic banking products and services had the potential to be accepted by customers. About 75% of the respondents felt that Islamic banks in Malaysia have not done enough marketing to promote their products and services to corporate customers.

TABLE 5: PERSONAL OPINIONS

	N	%
1. The main reason why people select Islamic banking products.		
Strictly religion	5	11.1
Economics (profit & cost elements)	8	17.8
Both religion and economics	25	55.6
Other reasons	-	-
No idea	7	15.6
	45	100.1
2. The potential of Islamic banking products in the Malaysian corporate sector.		
A very good potential	3	6.8
A good potential	19	43.2
Some potential	5	11.4
No potential	11	25.0
No potential at all	1	2.3
No idea	5	11.4
	44	100.1
3. Is it true the Islamic banking products available in Malaysia are similar to the products of conventional banks except that the banks use different names in highlighting those products?		
Absolutely true	2	4.5
True	12	27.3
Partly true	22	50.0
Untrue	6	13.6
Absolutely untrue	2	4.5
	44	99.9
4. Do you think that Islamic banks have done enough in marketing their products to corporate sector?		
More than enough	-	-
Enough	1	2.3
Just enough	4	9.3
Not enough	32	74.4
Not enough at all	6	14.0
	43	100.0

Table 6 shows the factors perceived as important in selecting banks. The most important one was cost and benefit to the company, followed by service delivery (fast and efficient), size and reputation of the bank, convenience (location and ample parking), and friendliness of bank personnel. This finding was inconsistent with previous research whereby the size of banks was considered the most important criterion.

TABLE 6: SELECTION CRITERIA OF BANK (%)

Factors	Very Important	Important	Moderately Important	Of Little Important	Least Important
Cost/Benefit	73.3	11.1	11.1	-	4.4
Service	13.6	29.5	31.8	13.6	11.4
Size and Reputation	13.6	52.3	18.2	13.6	2.3
Convenience (location & parking)	2.3	9.1	22.7	29.5	36.4
Friendliness of Bank Personnel	2.3	9.1	13.6	36.4	38.6
Total	105.1	111.1	97.4	93.1	93.1

V. CONCLUSION

This study, though exploratory in nature, provides useful information to both policymakers in the government and also those who manage Islamic banks in Malaysia.

Firstly, it is a strong possibility that a dream has come true for the late Tan Sri Jaafar Mohammed, the former Governor of Bank Negara Malaysia. He wished to see an Islamic banking system operating parallel to the conventional system. Almost half of the individuals surveyed who had financial decision-making authority in the Malaysian corporate sector believed that the Islamic banking system had a good potential as an alternative to the conventional system.

Secondly, this study shows that providers of Islamic banking products and services have not done enough to educate customers and market their products. For example, more than 65% of the respondents indicated that they had limited knowledge of Islamic banking. Similarly, despite the fact that the Bank Islam Malaysia Bhd has gained footing since 1984, and that the Interest-Free Banking Scheme was launched in 1993, most respondents started relationships with this system only four years ago. This lack of a marketing effort among the providers could be a contributory factor toward the smaller market share of Islamic deposits and loans against the total loans and deposits of the Malaysian banking system.

Finally, this study also shows that the most important factor perceived by corporate customers in selecting their banks is the cost of the services and products. This means that Islamic bank products will not be attractive to this market unless and until its costs are lower than those of the products of the conventional banks.

REFERENCES

- Bank Negara Malaysia. *Monthly Bulletin*. Kuala Lumpur: Various issues.
- Bank Negara Malaysia. *The Central Bank and the Financial System in Malaysia*. Kuala Lumpur: 1999.
- Chan, AKK and Ma, SM. "Corporate Banking Behaviour: A Survey in Hong Kong." *International Journal of Bank Marketing* 8.2 (1990): 25-31.
- Erol, C and El-Bdour, R. "Attitudes, Behaviour and Patronage Factors of Bank Customers towards Islamic Banks." *International Journal of Bank Marketing* 7.6 (1989): 31-39.
- Erol, C, Kaynak, E and El-Bdour, R. "Conventional and Islamic Bank: Patronage Behaviour of Jordanian Customers." *International Journal of Bank Marketing* 8.5 (1990): 25-35.
- Gerrard, P and Cunningham, JB. "Islamic Banking: A Study in Singapore." *International Journal of Bank Marketing* 15.6 (1997): 204-216.
- Haron, S, Ahmad, N and Planisek, S. "Bank Patronage Factors of Muslim and Non-Muslim Customers." *International Journal of Bank Marketing*. 12.1 (1994): 32-40.
- Hassan, MZ. "Challenges Towards Deepening of the Islamic Bond Market and Islamic Multi-Investment Funds." Paper presented at *Kuala Lumpur International Summit of Islamic Banking & Finance*, 19-21 February. Kuala Lumpur: 2001.
- Khan, M Fahim. "Islamic Banking as Practised Now in the World." In *Money and Banking in Islam*. Ziauddin Ahmed et al. (eds.). Islamabad: Institute of Policy Studies, 1983. 259-276.
- Metawa, SA and Almosawi, M. "Banking Behaviour of Islamic Bank Customers: Perspectives and Implications." *International Journal of Bank Marketing* 16.7 (1998): 299-313.
- "News Monitor: Malaysia to Establish Islamic Index." *New Horizon* 52 (1996): 19.
- Rosenblatt, J, Laroche, M, Hochstein, A, Mctavish, R and Sheahan, M. "Commercial Banking in Canada: A Study of the Selection Criteria and Service Expectations of Treasury Officers." *International Journal of Bank Marketing* 6.4 (1988) 20-30.
- Turnbull, PW. "Corporate Attitudes Towards Bank Services." *International Journal of Bank Marketing* 1.1 (1983): 53-68.
- Turnbull, PW and Gibbs, MJ. "The Selections of Banks and Banking Services among Corporate Customers in South Africa." *International Journal of Bank Marketing* 7.5 (1989): 36-39.
- Tyler, K and Stanley, E. "UK Bank-Corporate Relationships: Large Corporates' Expectations of Service." *International Journal of Bank Marketing* 17.4 (1999): 158-172.

* The authors wish to thank Badariah Mohd Zahir and Khairul Anuar Adnan for their administrative assistance, and to acknowledge the grant from Universiti Utara Malaysia.