

CONSUMERS' PREFERENCE TOWARDS ISLAMIC BANKING

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Abstract

Objective - This research aims to provide empirical evidence on the factors motivating consumers to save in Islamic banking.

Methods - The one sample t-test is employed to test hypothesis. The validity and the reliability of research variables have been examined.

Results - The result proved that consumers' decision to save in Islamic banking are influenced by economic and religious factors, such as receiving economic benefits, quick services, online facilities, easily reachable locations, and having a better understanding of Islamic principles.

Conclusions - The existence of a relationship between economic and religious preference proves that, in making decisions, consumers wish to attain two satisfaction levels: satisfaction in the world and in the hereafter.

Keywords: Economic Preferences, Religious Preference, Islamic Banking.

Abstrak

Tujuan - Penelitian ini bertujuan untuk memberikan bukti secara empiris faktor-faktor yang mendorong nasabah menabung di bank syariah.

Metode - Alat analisis yang digunakan untuk menguji hipotesis adalah one sample t test. Sedangkan test validitas dan reliabilitas digunakan untuk menguji variabel penelitian.

Hasil - Hasil penelitian menunjukkan bahwa dalam menabung di bank syariah, nasabah dipengaruhi oleh faktor ekonomis dan faktor agamis, seperti mendapatkan manfaat ekonomi, pelayanan yang cepat, fasilitas online, lokasi yang mudah dijangkau, dan memiliki pemahaman terhadap prinsip-prinsip agama islam dengan baik.

Kesimpulan - Adanya hubungan antara preferensi ekonomis dan preferensi agamis menunjukkan bahwa nasabah dalam menabung di bank syariah ingin mencapai tingkat kepuasan, yaitu kepuasan duniawi dan ukhrawi akhirat)

Kata Kunci : Preferensi Ekonomis, Preferensi Agamis, Perbankan Syariah

1. Introduction

One of the concepts often discussed by economist these days is Islamic banking. This concept applies Islamic teachings in the banking system, particularly related to interest-free financial transactions (Caragata, 2000). Islamic banking function as a financial intermediary institution conducts financial transactions that are similar to the conventional banking. Funds collected by Islamic banking from those having excess capital are further transmitted to those having shortage capitals, so that economic development process can be realized.

One main actor in the development of Islamic banking is Islamic Development Bank (IDB), which supervises the organization of Daar-al-Maal al-Islami (Islamic House of Founds) or DMI. Likewise, International Association of Islamic Banks (IAIB) was established as a technical advisory institution for Islamic banking in August 1997 (Erol and of El Bdour, 1989). The first attempt to establish local Islamic bank was managed at the end of 1950 in a rural area in Pakistan, where the essence of interest is missed. Later, followed by the Moslems in Malaysia, who tried to establish an interest-free bank in the middle of 1940-s.

In India, Jamaat-E-Islami Hind started the practice of free interest loan in 1968. While in Egypt, the first Islamic bank named Nasser Social Bank was founded in September 1971 (Erol and El-Bdour, 1989), in Iran, the Islamic banking system was started in 1979, by the nationalization of commercial banks (Yousefi et al, 1995).

On the first November 1991, the first Islamic bank was established in Indonesia, namely PT. Bank Muamalat Indonesia (BMI). At the beginning, the operation of BMI had not been strengthened with the banking act covering Islamic principles for banking practice. The existing Banking Act at the time, i.e. Act No. 7/1992, explains only “bank with profit sharing system” with no greater detail. Since the prevailing of Banking Act No.10/1998, the existence of Islamic banking has been expressly regulated. Banking Act No.10/1998 also regulates the opportunity for conventional banks to open Islamic branches or convert them to Islamic banks. While some conventional bank open Islamic branches, such as Bank IFI, Bank BNI, and Bank Jabar, a conventional bank, i.e. Bank Susila Bhakti, was transformed itself into Islamic bank and named as Bank Syariah Mandiri.

Fundamentally, objections from Muslims on conventional banking system comes from the understanding that interest is equal to forbidden *riba*, besides the operational activities of the banking system, within which un-Islamic business activities exist. These activities include the channeling of the fund to businesses concerning unlawful goods and services, the speculative

activities (*maysir*), the unjust profit sharing for lenders and borrowers (*jahala*), and the uncertain contracts (*gharar*) (Iqbal, 1997).

In making decision to save, consumers usually consider the interest rate. Savings is, according to neoclassical economists, a function of interest rate. The higher interest rate level, the more are money to be saved and current consumptions to be sacrificed. The sacrifice of current consumptions will benefit future consumptions. Keynes admits that interest rate influences consumptions, though he contends that in the short run, with constant income, the influence of interest on expending is not significant (Mankiw, 1997).

Interest rate agreed in advance by a conventional bank and consumers indicate certainty, i.e. a number of interest consumers will earn. This amount of interest can be counted as a certain percentage of savings. Concept offered by Islamic banking does not use interest rate. An agreement between an Islamic bank and consumers concerns the proportion of profit sharing and contains uncertainty. Earned profit sharing determined by the success of Islamic bank to make a profit (Karsten, 1982).

The uncertainty of profit earned by Islamic banking raises a question on whether consumer behavior in Islamic banking refers also to the general economic behavior, i.e. considering the profit as most important. If their behavior refers to profit, and the profit rate in Islamic and conventional banking is the same, consumers will have to decide whether to choose Islamic banking or choose the conventional ones.

In a situation where the economy is still predominated by the conventional banking system, the interest rate becomes a reference (bench-mark) for the consumers, though it does not prevail for those avoiding conventional banks because of *riba*. In recent economic crisis showed the low read sector growth, profit sharing earned by Islamic banking is also small, far smaller than the interest rate. Consequently, those choosing a bank with economic profit motives will consider saving money in Islamic as uninteresting (Karim, 2001).

An opinion stating that to save in Islamic banking is uninteresting can be argued as the third party fund in Islamic banking increases from year to year (except in 1998 when all banks experience serious crisis). In 1999, third party fund collected by Islamic banking (i.e. Bank Muamalat Indonesia) reached IDR 528.08 billion, meaning that there was an increase of IDR 136.16 billion or 34.78% from IDR 391.92 billion in 1998. This amount exceeds the attainment in 1997 when the economic crisis was starting, i.e. IDR 463.27 billion. The increase happened from demand deposit, savings, and time deposit. *Wadiah* increased 17.77% from IDR 68.01 billion to IDR 80.09 billion. *Mudharabah* savings, increased 44.48% from IDR 102.85 billion to

IDR 148.58 billion, whereas *mudharabah* time deposit increased 3.77% from IDR 221.08 billion to IDR 229.42 billion. This increase of third party fund indicated the restoration of society's and business partners' trust to Bank Muamalat Indonesia after the decrease in 1998 when interest rates in conventional banking were rapidly increasing (Bank Muamalat Indonesia, 1999).

Table 1: Third Party Fund Collected by Islamic Bank

Year	Third Party Fund (in billions of IDR)
1999	528.08
1998	391.92
1997	463.27

Source: Bank Muamalat Indonesia

From the above explanation, it can be concluded that if Islamic banking management believes consumers' attitude is different, Islamic banking will have to attain the same profit level as the conventional bank. However, if every consumer is also considered to have economic motive and expect more profit, Islamic banking will have to be able to compete with the conventional bank. Differences between the concept of Islamic banking and conventional banking can influence consumers' attitude in taking their choice. Here, special qualities must be offered by Islamic banking to compete with the conventional one.

Ratnawati (2000) studies to analyze potency, preference, and behavior of society to Islamic banking in West Java region. Using a logit model to all respondents, factors influencing society to use Islamic banking service are location/access, service, credibility, facility, status, and as well as knowledge of Islamic banking. Using a logit model to Islamic banking consumers, factors influencing society to continue to adopt Islamic banking is accessibility (having a negative effect on Islamic banks), as well as knowledge of Islamic banking, Islamic banking is more beneficial, and service easiness. Using logit model to all non-Islamic banking consumers, factors influencing the potency of society to adopt Islamic banking are: First, accessibility (having a negative effect on Islamic banks). Second, banking location/access. Third, service (tend to make consumer do not want to adopt Islamic banking). Fourth, knowledge of Islamic banking. Fifth, profit (Islamic banking is more beneficial). Sixth, Islamic banking follow the Islamic law. Seventh, easy service. Conclusion taken from this research is that society chooses Islamic banking because of economic factors.

The same study by Wiratno (2000) to analyze potency, preference and behavior of society to Islamic banking in Central Java and D.I Yogyakarta regions. The result is aimed at knowing

society's preference to place their deposits in Islamic banking. Using a logit model to all responders, factors influencing society's preference are their acceptance of new technology, mobility (preference to save enthused more by society with low mobility), tolerance to the religious deviation, and comprehensive (respondents' knowledge on Islamic banking comprehensiveness).

Preference to Islamic banking system indicates that society chooses an Islamic Bank because of its relative profit, its compatibility, its comprehensiveness or how far Islamic banking has a universal dimension concerning economic, culture and social aspects, and its observability. General conclusion taken from the logit model analysis is that society chooses Islamic banking because of economic and religious factors. Information on consumers' characteristics and behavior are very important for developing Islamic banking. In order to understand the consumers' characteristics and behaviors, this research is aimed at providing empirical evidence on their preferences toward Islamic banking and factors motivate them to save in Islamic banking.

In modern economics, the problem of choice is much depended on individual behavior and possibly taking no account of the norms prevails in society. In Islamic economics, we do not reside in a position to distribute resources in the way we are willing to do. There is a serious ethical boundary based on principles derived from the Quran and Sunnah (Mannan, 1993). The moral filter is, according to Chapra (2000), needed to less unlimited desires in exploiting resources. Islamic economics considered by economists as based on ethical values (El-Askher, 1987) because it has the philosophy of Tawhid as a background. Tawhid has ethical contexts referring to the integration of spiritual and temporal aspects of human being's existence (Muhammad, 2000). Ethics, a Moslem's Tawhid attitude is reflected.

The plan of this paper is as follows: section 1 is the introduction, section 2 provides the theory of consumer behavior, section 3 discusses the methodology, section 4 presents result and discussion, and finally section 5 is the conclusion.

2. Methodology

The spreading of questioners was conducted in January-February 2015 with total 43 respondents. The method used in taking the sample is purposive sampling. To identify factors motivating consumers to choose an Islamic banking, variables used by the researcher are grouped into two categories, i.e. Economic variables (consumers save because of economic factors) and religious factors (consumers save because of religious factors).

Test on research variables is important, to ensure whether used variables (which are formulated in detailed questions) are valid and reliable or not. The validity of research questioner indicates its ability to represent something that will be measured in the research, whereas reliability of question indicates the consistency of answer given by responders from time to time.

Test of validity and reliability was conducted using SPSS program. Validity can be seen from the correlation value while reliability is seen from the value of Cronbach alpha. A scale used to determine respondents answer is the scale of Likert, i.e. extremely agree (SS) or (1), agree (s) or (2), neutral or (3) disagree (TS) or (4), and extremely disagree (STS) or (5).

The test of the hypothesis is conducted to answer research questions so that objectives proposed in this research can be attained. The hypothesis proposed in this research is: It is expected that there are economic, and religious factors motivating consumers to save in Islamic banking. A tool used to analyze the first hypothesis is one sample test.

3. Result and Discussion

Test of Validity and Reliability

Test of validity and reliability was conducted using SPSS program. Validity is seen from the correlation value, while reliability is seen from the value of Cronbach alpha. The correlation value 0,7320 is more than r table ($\alpha=5\%$ $df=40$ equal to 1,684). Thus, it can conclude that is valid. While. The value of Cronbach alpha 0,8442 is more than r table ($\alpha=5\%$ $df=40$ equal to 1,684) or more than 0,5 and positive. Thus, it can conclude that it is reliable.

Table 2. Validity

Variable	Correlation Value	Valid or Not
Economic	0,7320	Valid
Religious	0,7320	Valid

Table 3. Reliability

Variable	Alpha Cronbach Value	Reliable or Not
Preference	0,8442	Reliable

Result of One Sample Test

One sample test is used to test the hypothesis concerning consumers' preference to Islamic banking, i.e. to identify factors motivating consumers to save in Islamic banking. The expected factor are economic and religious factors; all of them later to be tested. The result shows that the first null hypothesis is rejected. Obtained statistic (49.014) is more than t table ($\alpha=5\%$ $df=40$ equal to 1.684), and the probability is 0.00 (smaller than 0.05). Thus, it can be concluded that economic and religious factors have motivated consumers to save in Islamic banking.

Test on each variable (economic and religious variables) is also conducted, to see whether these variables motivate consumers to save in Islamic banking. The test is also conducted with one sample test, and the result indicates that null hypothesis is rejected. Such rejection can be seen from t statistics that is more than t table, or probability, that is less than 0.05. For the economic variable, t statistic (48,024) is again more than t table. At the same time, the probability is 0.00 smaller than 0.05. For religious factors t statistic (43,464) is again more than t table. At the same time, the probability is 0.00 smaller than 0.05). Here, there are factors significantly motivating consumers to save in Islamic banking, i.e. economic, and religious factors.

Table 4. One-Sample t-Test

Variable	T statistic Value	Probability (significant)
Economic	48,024	0.000
Religious	43,364	0.000

Metawa and Almossawi (1998) found evidence that the consumers' decision in choosing an Islamic bank is motivated by religious factors, where consumers emphasize their adherence to Islamic principles. Further, this decision is also motivated by the factors of profit, families and friends, and bank's location. These factors here in after contribute to responders' characteristics, such as age, income and education.

Erol and el-bdour (1989) through their empirical study found that motive in choosing an Islamic bank as a depository institution is not a religion, but profit. The existence of Islamic bank's new branch is not such an important consideration for the improvement of service. Besides, peer groups have an influence on consumers' decision to choose an Islamic bank and consumers' awareness to obtain profit from profit and loss sharing investment and income redistribution role of Islamic banking system. Later in 1990, Erol *et al.* Conduct and study or conventional banking. This study reports that consumer chooses an Islamic bank because of its quick and

efficient services, its reputation, and its banking services. The conclusion is that the profit motive (economic factor) exists in choosing Islamic banking.

Research conducted by Haron and Norafifah (2000) proves the relationship between the interest rate in conventional banking and the amount of deposits placed in Islamic banking and return given to these deposits. The result shows that the relationship between return and a number of deposits placed in Islamic banking positive, where the increase of return increases a number of deposits. At the same time, the relationship between the interest rate in conventional banking and a number of deposits placed in Islamic banking is negative, where the increase of interest rate in conventional banking decreases a number of deposits in Islamic banking. The conclusion can be taken from this study is that profit (economic factor) motivates a consumer to place their money in a bank.

The result of research conducted by Naser, Jamal, and Al-Khatib (1999) indicates that factors motivating consumers to choose Islamic banking are bank reputation, reason of religion, perception that Islamic banking do not only offering facilities which is equal to conventional banking but also apply Islamic principles, and its ability to take care of secrecy, as well as profit. At the same time, factors motivating consumers to choose both Islamic and the conventional bank is to diversify investment and the limitation of Islamic banking branches and service time. A conclusion can be taken from this research is that the consumer chooses Islamic banking because of both religious factors and profit (economic factors).

Gerrad and Cunningham (1997), Moslems' and non Moslems' attitude in choosing Islamic banking is not significantly different, where they choose an Islamic bank because of its expeditious service, its secrecy, and its reputation and image, its light costs of checking as well as the availability of parking. Pursuant to these results, consumers choose Islamic banking because of economic factors.

According to this research, the result proved that consumers' decision to save in Islamic banking is influenced by economic and religious factors. The result of research conducted by Naser, Jamal, and Al-Khatib is that the consumer chooses Islamic banking because of both religious factors and profit (economic factors).

One's motivation in doing an activity is related to his psychological condition. If one in doing an economic activity, such as saving in Islamic banking, motivated by religious and economics motive, this will be appropriate to those arranged by Islam. According to Qardhawi (1996), the human being is Allah's creation that having the character of *mukallaf* (shouldering religious obligation). Pursuant to this nature, the human being in conduction an activity is according to

religious demand. Besides, the freedom to do the economic activity (in the boundaries of Islamic law) is also a motivator for the human being to pursue profit, in order to reach happiness and welfare. The freedom given by Allah must be executed in a way agreeing with the principle of permissiveness-forbidden, committing to the obligations determined by Islamic law, and generating no disadvantage for the people, as well as supporting the existence of togetherness in realizing prosperity (Fikri, 1997).

4. Conclusion

The results of this research concerning consumers' preference to Islamic banking proved that economic and religious factors have prompted consumers to save in Islamic banking, such as taking in economic benefits, quick service, online facilities, easily reachable locations, and having a better understanding of Islamic principles. There is a relationship between economic and religious preferences in saving in Islamic banking.

The purpose of human life in Islam is to take for the rewards and favors of Allah. Every activity, including economic activity, will be addressed to attain such a purpose. According to Chapra (2000), the elementary principles formulating Muslim's worldview, i.e. Tawhid (the oneness of God), Khilafah (vicegerent), and justice. Thereby, the human being is Allah's vicegerent on the earth. In executing the function, the human being has to respect justice. This will be reached, when the human being has universal fraternal feelings, understanding that resources are trusteeship must be worked efficiently for human prosperity, and confession on the freedom of the human being.

The Islamic consumer behavior is that referring to the boundaries of Islamic law, which is enabled/allowed for and which is prohibited /forbidden. Islamic consumers are enabled to fulfill their needs by utilizing resources on the earth and without being luxurious because Islam frowns upon luxurious/extravagant life.

These conclusions indicate that consumers consider two satisfaction levels through saving in Islamic Banking, i.e., satisfaction in the world and the hereafter. Every Muslim is claimed to achieve happiness in the world and the hereafter (*falah*), i.e, by fulfilling needs in both life.

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