

## Requirements and Selection Decision of Customers in Islamic and Conventional Banking Environment

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### ABSTRAK

*Persaingan merupakan cabaran utama yang dihadapi oleh bank perdagangan di seluruh dunia. Mereka bukan sahaja bersaing sesama sendiri, tetapi juga bersaing dengan pelbagai institusi dalam industri kewangan. Di Malaysia, persaingan ini ditambah lagi dengan adanya bank yang operasinya berlandaskan prinsip Islam. Sebelum mengambil strategi tertentu bagi menarik lebih ramai pelanggan, bank perdagangan dan bank Islam ini perlulah mempunyai maklumat mengenai faktor-faktor yang mempengaruhi orang ramai melanggan sesebuah bank. Penyelidikan ini mengkaji bagaimana orang Islam dan bukan Islam yang menjadi pelanggan bank perdagangan memilih banknya dan perkhidmatan yang dikhendakinya. Mereka juga dikehendaki memberi pendapat mengenai bank Islam. Hasil penyelidikan ini menunjukkan lebih banyak kesamaan untuk dua kumpulan ini di dalam memilih bank dan perkhidmatan yang diguna. Perbezaan yang sedikit wujud pada tahap pengetahuan mereka mengenai bank Islam.*

### ABSTRACT

*Competition is the main challenge faced by commercial banks globally. They are not only competing just among themselves but also with other institutions within the financial industry. In Malaysia, the competition is becoming fiercer with the existence of banks which operate based on Islamic principles. To attract more customers both the bankers of conventional and Islamic banks should acquire information about factors which influence people in patronising their bank. This study investigates how Malaysian bank users select conventional banks, what services they want, and also how they perceive Islamic banking. Results show that there are many similarities between Muslims and non-Muslims in their selection of banks and utilization of services. A slight difference however, exists in their knowledge of Islamic banks.*

### INTRODUCTION

Fierce competition is becoming the most influential factor in the structure and the activities of the banking system around the globe. In the United Kingdom, for example, increasing competition has pushed British banks into much greater customer - oriented and competitive behavior. In other countries, the industry has been transformed from its traditional staid image to that of a vibrant and dynamic environment (Turnbull & Gibbs, 1989).

Malaysia, the banking system of which is in the maturity stage, also shares the same

problem with other countries in the world. One of the likely challenges which it would face in the near future is greater competition from within the banking system itself (Bank Negara Malaysia, 1990).

The 1990's forebode even more threats to the commercial banks than they do to other financial institutions. The most prevalent challenge is from Bank Islam Malaysia Berhad (BIMB). The establishment of BIMB in 1983 marked a milestone in the Malaysian banking system in the sense that it provided an alternative to the existing conventional system. Operating on Islamic principles, which prohibit

interest, BIMB is able to fulfil the needs of the Muslim population. At the end of 1991, BIMB had 29 branches and a total deposit of \$1,270 million as compared with the commercial banks which had 1050 branches and a total deposit of \$96,018 million.

Due to the highly competitive environment, it is essential for both bankers of commercial and Islamic banks to obtain information concerning the factors that affect customers' patronage of a particular bank. The bankers must also know the degree to which various product or service characteristics are important to the potential customers and how these factors influence their selection of banks. This information is needed prior to the introduction of any new product or service. Understanding customer characteristics is very important to the bankers since they are involved directly in providing these critical determinant factors.

This study was undertaken to determine what the Muslims and the non-Muslims perceived as important when initially selecting their banks, and what services they subsequently used that would keep them with those banks. A comparison of younger and older respondents was made to evaluate current needs against the needs of the future as the younger depositors begin to dominate the market. Besides the age group, the level of education was also taken into consideration when analysing the selection. With this information both Islamic and conventional banks can develop their marketing strategies to assure their future viability in a more competitive manner.

For the benefit of BIMB, this study also focused on the perception of Muslims and non-Muslims towards BIMB's existence and operational matters. With the knowledge of the needs of potential customers, an Islamic bank, particularly BIMB, can develop a strategy for future growth which will appeal to all potential customers and not just to the strictly-devout Muslims.

### LITERATURE REVIEW

The literature contains many bank patronage studies which suggest an array of bank features which attract new customers. Most of these studies have been conducted in the Western countries, a few in Asia but only one in an

Islamic country, Jordan. A review of these studies shows that the important factors in bank selection are convenience, staff quality, availability of products and services, and recommendation by family and friends. But these factors vary in importance with the age, education and culture of the potential bank customer.

Grimm (1974) and Reed (1972) summarized the early literature and reported that American customers rated a convenient location as the most important consideration in their selection of their main financial institutions. More recent studies have found convenience to be decreasing in importance while recommendation by friends and family has risen in importance (Anderson et al., 1976; Tan, 1986). With bank branches and ATM machines now available even in smaller towns, it is not surprising that a conventional location is no longer the deciding factor. Product differentiation could no longer be used as a strategy to attract potential customers due to the homogeneity in products and services offered by most banks. These customers now feel more confident relying on their friends' recommendation as a mode of choosing their bank. The quality of bank staff and the range of bank's products are also increasingly considered important in deciding which bank they wish to select (Evans, 1979; Grimm, 1974; Kaynak, 1986).

A study by Jawalgi et al. (1989) using 'Analytical Hierarchy Process' to determine the bank selection criteria reported that safety of one's funds to be the main criterion followed by paying the highest interest rate on savings, location, reputation, availability of loans, low interest on loans, ease of qualifying for checking account by maintaining a minimum balance, and lastly, Saturday banking.

Grimm (1974) and Reed (1972) reported that different demographic-type of customers used different criteria in selecting their banks. Anderson et al. (1976) strengthen this argument by hypothesizing that bank customers could be classified into the dichotomy of service-oriented customers and convenience-oriented customers. Laroche (1986), confirmed that different demographic groups had different motivations and Tan (1986), who studied Chinese customers in Singapore, suggested that culture made a difference in bank selection.

Erol and El-Bdour (1989), the only study

TABLE 1 : Respondent's Characteristics.

	MUSLIMS		NON-MUSLIMS	
	N=150	%	N=151	%
<i>Age :</i>				
< 20 years	3	2.0	12	7.9
20 - 29 years	45	30.0	82	54.3
30 - 39 years	72	48.0	36	23.8
40 - 49 years	20	13.3	16	10.6
> 50 years	10	6.7	5	3.3
<i>Level of education:</i>				
Nil	1	0.7	5	3.3
Primary	7	4.7	16	10.6
Secondary	105	70.0	89	58.9
University/College	31	20.7	31	20.5
Professional	3	2.0	10	6.6
Missing Value	3	2.0	-	-
<i>Type of employers:</i>				
Private	26	17.3	78	51.7
Government/public agency	98	65.3	27	17.9
Self-employed	26	17.3	46	30.5
<i>Type of job:</i>				
Professional	12	8.0	16	10.6
Management	7	4.7	3	2.0
White collar	60	40.0	61	40.4
Blue collar	35	23.4	19	12.6
Own business	26	17.3	46	30.5
Missing value	10	6.6	6	3.9
<i>Years on job/business:</i>				
< 5 years	38	25.3	84	55.6
5 - 9 years	33	22.0	38	25.2
10 - 14 years	36	24.0	14	9.3
15 - 20 years	27	18.0	5	3.3
> 20 years	15	10.0	10	6.6
Missing value	1	0.7	-	-
<i>Monthly income (Ringgit) :</i>				
< \$1000	74	59.7	77	73.4
1000 - 1999	45	36.3	24	22.9
2000 - 2999	5	4.0	2	1.9
3000 - 3999	-	-	-	-
> \$4000	-	-	1	0.9
Missing value	-	-	1	0.9
<i>Monthly sales (own business):</i>				
< \$15,000	18	69.2	30	65.2
15,000 - 29,999	4	15.5	5	10.9
30,000 - 44,999	2	7.7	5	10.9
45,000 - 59,999	-	-	2	4.3
> 60,000	1	3.8	4	8.7
Missing value	1	3.8	-	-

available of an Islamic culture, compared Islamic bank customers with conventional bank customers in Jordan. Surprisingly religion was not the main reason for the customers in choosing an Islamic bank; the religious "edge" of Islamic banks with Muslims was not a major advantage. Islamic bank customers valued efficient and friendly staff coupled with a wide range of bank products.

While Erol and El-Bdour (1989) compared Islamic and conventional bank customers, no one has compared the Muslim and non-Muslim bank customers' perception towards their bankers in a banking environment where both Islamic and conventional banks operate. The information obtained from such a comparative study could be used to help both banks enlarge their customers base.

## METHODOLOGY

A sample of 301 commercial bank customers in Alor Setar, Sungai Petani and Kangar towns were surveyed. The selection of the samples were based on convenience. The towns were chosen as they represented a highly competitive banking environment compared with other towns in the two states surveyed. Furthermore, these customers had a wide range of banks and other non-bank financial institutions including BIMB branches to choose from.

The data for this study were collected through a self-administered questionnaire distributed by research assistants. The questionnaire contained four sections. The first section of the questionnaire was designed to gather information about the respondent's personal, demographic and economic characteristics. The profile of the respondent's characteristics is shown in TABLE 1.

In the second section of the questionnaire, the respondents were asked to indicate on a five point Likert scale, ranging from 'very important' to 'not important at all', their view of a series of factors in selecting a commercial bank. Many of the factors were adapted from Anderson et.al. (1976), Kaynak (1986), Laroche et.al. (1986) and Erol & El Bdour (1989).

The third section of the questionnaire was designed to generate data concerning the usefulness of products or services offered by the commercial banks for their customers. The

perceived level of usefulness of these products or services was also measured on a five-point Likert scale. The scale ranged from 'used all the time' to 'never being used'. The bank product or service choices were derived from Laroche et.al. (1986), and Erol and El-Bdour (1989). The final section contained questions which could generate information about customers' perception towards BIMB.

Data analysis included both univariate and multivariate statistics. Univariate techniques were used to identify the overall attitudes of bank customers towards commercial banks and the usefulness of bank services. The primary tool of multivariate statistic was a principal component analysis with Varimax rotation which was used to cluster bank selection criteria.

## FINDINGS

### *Bank Selection Criteria*

The first hurdle in attracting potential bank customers is to get their attention at the time when they are selecting their banks. Of the 26 bank-selection criteria rated by importance on the Likert scales, the following ten differed significantly in importance to Muslim relative to non-Muslim respondents.

TABLE 2 : Bank-selection criteria showing a significant t-test for the difference in means between Muslims and non-Muslims. ( $\alpha=.05$ )

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### *Criteria Muslims valued more highly:*

- Fast and efficient service
- Internal appearance of bank
- Interior comfort
- Wide range of services offered
- Overdraft privileges
- Speed of transactions
- Hours of operation
- Impression of manager
- Ability to meet individual banking needs

### *Criteria non-Muslims valued more highly:*

- Reception received at the bank

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In an effort to more clearly delineate patterns, a Varimax-rotated factor analysis was run on the 26 selection criteria for both Muslims and non-Muslims. Calculated item weights of 0.6 and above were considered

TABLE 3 : Criteria in Bank Selection. (Varimax-rotated factor analysis results).

MUSLIMS	NON-MUSLIMS
<i>Factor 1 - Bank products</i> Overdraft privileges Inter-branch facilities Financial counselling available Wide range of services offered	<i>Factor 1 - Image</i> External appearance of bank Internal appearance of bank Mass media advertising
<i>Factor 2 - Image</i> External appearance of bank Mass media advertising Recommendation of business associates or friends	<i>Factor 2 - Service</i> Fast and efficient service Inter-branch facilities Confidentiality of bank
<i>Factor 3 - Pricing</i> High interest payments on savings accounts Low interest charges on loans	<i>Factor 3 - Bank Products</i> Overdraft privileges Financial counselling available Hours of operation
<i>Factor 4 - Service</i> Fast and efficient service Friendliness of bank personnel	<i>Factor 4 - Pricing</i> High interest payments on savings accounts Low interest charges on loans

significant. Four factors emerged for both groups of respondents and these were named bank products, image, pricing and service. TABLE 3 shows the constituency of each factor and its importance for the group.

Muslims and non-Muslims basically value the same bank-traits when they select their bank. Banks need to offer a wide range of products at favorable terms through a friendly staff in a comfortable environment. These findings only differ from earlier research in not emphasizing a convenient location. This can probably be explained by the clustered locations and hence equivalent convenience of all banks in the towns sampled.

The only difference between Muslim and non-Muslim bank-selection criteria appears to be the added weight Muslims gave to the range of products the banks offers (see TABLE 4). Both groups valued pricing in their banking relation, defined as achieving a high return on savings and a low cost on loans; however, Muslims valued a profitable relationship slightly more than non-Muslims.

TABLE 4 : Percentage of total variance explained by factor.

	MUSLIM %	NON-MUSLIM %
Products	24	14
Image	16	17
Pricing	15	12
Service	14	17

Since the education level of Malaysians differs, a factor analysis was run to compare respondents having an education above the high school(H.S.) level with those below the high school level, regardless of their religions. The same basic factor patterns emerged except that the service factor splintered into several smaller factors and the more educated respondents weighted the factor 'Bank's products' more than the less educated did (see TABLE 5).

TABLE 5: Percentage of total variance explained by factor.

	H.S. OR LESS %	ABOVE H.S. EDUCATION %
Products	13	24
Image	18	18
Pricing	11	16
Service	Split into several factors for both groups	

Young and old bank customers did not differ substantially in their weighting of the factors. Although not significant there was a slight tendency for the younger customers to rely on friends and family for bank recommendation while the older respondents felt that location and parking were slightly more important.

#### *Bank Product Usage*

Since a full range of products seemed to be the key to attracting new bank customers, particularly the Muslims and the well educated, respondents were given a choice of 15 bank products and were asked to rate the frequency with which they used each. A t-test for the difference in usage by the two groups showed that 14 to 15 products were used significantly more by non-Muslims than Muslims. The sole exception was remittance services. The top three products in order of utilisation were:

- \* Savings accounts
- \* ATMs
- \* Checking accounts

The ranking was the same for both Muslims and non-Muslims. The fourth most important product was remittance services for Muslims and time deposits for non-Muslims.

#### *Perception of Islamic Banking*

Since knowing what the customer wants is only half of the marketing problem solved, attention should be directed to the image reflected by a bank. The word "Islamic" presumes that an Islamic bank would easily attract Muslim cus-

tomers. The word could also lead to a refusal or acceptance in doing business by non-Muslims. Therefore, the last section of the questionnaire was designed to determine non-users' attitudes toward Islamic banks.

When asked whether they were aware of BIMB'S existence and how it differed from conventional banks, the Muslims indicated substantially more awareness than non-Muslims (see TABLE 6). There was some misconception by the non-Muslims about BIMB since a substantial number of this group indicated that the bank was intended for Muslims only, contrary to the bank's official position of being accessible to all Malaysians regardless of religion.

TABLE 6: Percentage of awareness of BIMB and its differences compared with conventional banks.

	Muslim %	Non-Muslim %
Aware of bank's existence	98.0	74.8
Aware of differences from conventional banks	63.3	19.2
BIMB for Muslims only	12.0	31.8

Respondents knowledge about the bank was acquired from numerous sources (TABLE 7). Newspapers or magazines were the biggest sources of information for both Muslims and non-Muslims. Television or radio was cited as the second most important source of information, followed closely by friends and family. However, the latter two sources were used nearly twice as often by Muslims compared with the non-Muslims. Muslims were more active in pursuing information and visiting the bank; non-Muslims obtained some information from public meetings but visited the bank far less.

To find out whether there was a consistency in the opinion of respondents in two Islamic nations, a similar question, pertaining to the reason for customers selecting Islamic banks, as forwarded in the Jordanian study, was asked. Almost thirty-nine per cent of the

TABLE 7 : Percentage of Muslims and Non-Muslims getting information about BIMB from these sources

	MUSLIMS %	NON-MUSLIMS %
Newspapers/magazines	78.0	53.6
TV/radio	58.7	27.8
Friends and family	50.0	23.2
Visits to bank and discussion with staff	43.3	10.6
Public meetings	10.7	19.2
Outside meetings with bank staff	8.7	2.0

TABLE 8 : Percentage of respondent's opinion on reasons for customers' patronage of BIMB

	MUSLIMS %	NON-MUSLIMS %
<i>Reasons:</i>		
Religion	38.7	30.1
Profit	2.0	14.7
Both religion and profit	52.0	29.5
Others	6.7	21.2

T-test of difference of proportions showed all pairs to differ significantly at  $\alpha=.05$

Muslim respondents thought that religion was their reason for selecting BIMB, while 52 per cent of the Muslim respondents thought a combination of religion and profits motivated them to choose BIMB (see TABLE 8). The non-Muslims were more evenly divided in their response and gave substantially more weight to factors other than profits.

Lastly, questions were asked to determine what were, and were not, attractive about BIMB to these non-users. The significant differences between Muslims and non-Muslims were:

Muslims perceived that:

1. more branches would encourage more use
2. financing without interest was the best way to solve business problems

Non-Muslims felt that:

1. BIMB staff were less efficient than conventional bank staff
2. BIMB had not succeeded in attracting the Muslim population

3. BIMB had the most advantageous banking practices from the customer's perspective

#### IMPLICATIONS AND CONCLUSION

This paper investigated the demographics, criteria for bank selection, bank products used by conventional bank customers in the northern part of Malaysia and their perception of BIMB.

Survey respondents rated a list of variables which were important to them in selecting their bank. A factor analysis of the results produced four factors labelled: Bank products, Image, Pricing and Service. Both Muslims and non-Muslims were concerned about pricing and this confirmed the Jordanian results. However, pricing was not the most important selection criterion, since both groups valued products more than price. Muslims valued products most highly in the list of four factors, whereas

non-Muslims valued image and service most highly. The more educated respondents valued products more highly than the less educated.

As for product usage, Muslims and non-Muslims basically used the same set of services: savings accounts, ATMs and checking accounts. Currently BIMB does not offer ATM facilities and this could be limiting its appeal.

The results of the survey of the respondents' perception of Islamic banking supported the stereotypes. The non-Muslims felt that Islamic banking was not for them but for Muslims only. They felt that religion was the main reason why customers dealt with BIMB. Sixty-eight per cent of the Muslims on the other hand thought that the bank was for everyone, and their reasons for patronizing this bank were religion and profit.

On a positive note, both groups thought that the bank's products were advantageous to customers but, on a negative note, criticisms were laid on the small number of branches and inefficient staff. The complaint about staff was an echo of the Jordanian study.

Assuming that all Islamic banks want to attract the Muslim population then BIMB is doing certain things correctly and some, incorrectly. Even though the Muslim non-users are aware of the Islamic bank and have acquired information from numerous sources, they have not switched their accounts to BIMB. A more fully developed line of bank products, including more branches and ATM machines, seemed to be a prerequisite to switching. The bank is perceived as having certain advantages including treatment advantageous to customers. BIMB could promote this strength in its advertising while working to build its infrastructure.

Non-Muslims, on the other hand, need more information if they are to be induced to patronize BIMB. They perceived the bank as not wanting their business and not offering suitable returns for their money. Advertising and better infrastructure will be able to help this group switch their accounts. The advertising should emphasize the bank's unique offerings, its high quality service, good returns, and the desire to deal with all groups irrespective of their religious persuasions.

The Jordanian study concludes that Islamic bank managers should:

1. lengthen the commitments in their investment portfolio to generate higher profits for depositors
2. place extra emphasis on staff training
3. direct the advertising effort through peer groups, and
4. offer unique products without trying to duplicate conventional banks.

Several of these recommendations are not generalizable to Malaysia. A comparable list derived from this research recommends the following:

1. build infrastructure comparable to the competition
2. offer a full range of bank products
3. place extra emphasis on staff training
4. dispel the image that the bank operates exclusively for the benefit of Muslims, and
5. build on the image that the bank offers more favorable treatment to customers than conventional banks do.

Neither the Jordanian, nor this study collected information on the opportunities of offering unique products. It is reasonable to speculate that unique products may attract new customers. In societies where the current account is the major bank product, enticing customers to switch their bank is difficult since it involves a major adjustment for the customers. However, Malaysia is not a checking-based economy so bank switching probably would occur more readily. Even so, instead of convincing them to switch account, there may be greater potential in encouraging customers to open a second supplemental banking arrangement, a practice not unknown in South-east Asia (Denton & Chan, 1991).

Today's customers are more educated and selective of the banks they wish to patronize. If the aim is to attract new users, BIMB and conventional banks in general cannot offer a minimal range of products. They must grow to sufficient size to provide a complete branching network and a full line of products to meet customers' requirements.



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