

**FACTORS THAT INFLUENCE MUSLIM CONSUMERS PREFERENCE
TOWARDS ISLAMIC BANKING PRODUCTS OR FACILITIES:
THEORY OF REASONED ACTION**

By

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DEDICATION

**To my understanding, patient, and loving husband, Abdul Hanif Mohamad and to
my beautiful children, Hilmi and Aqeel**

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ABSTRAK

Kajian yang telah dijalankan ini adalah bertujuan bagi mengenalpasti penentu-penentu bagi niat pengguna-pengguna yang beragama Islam untuk mengguna produk Skim Perbankan Islam (SPI) atau sebaliknya. Teori Tindakan Beralasan oleh Fishbein and Ajzen telah digunakan sebagai asas kepada kajian ini. Teori ini mencadangkan bahawa penentu paling hampir kepada perlakuan ialah niat. Niat ditentukan oleh sikap terhadap perlakuan dan norma subjektif yang dipertimbangkan. Faktor-faktor yang dikaji ialah perlakuan, niat, sikap, norma subjektif, dan faktor luaran iaitu pengetahuan tentang produk SPI dan tahap keimanan seseorang itu. Sikap terhadap perlakuan dan norma subjektif ditentukan oleh gabungan kepercayaan, penilaian, dan motivasi untuk menyetujui. Seramai 123 pengguna beragama Islam di kawasan Pulau Pinang telah mengambil bahagian dalam satu soal-selidik yang dijalankan bagi bertujuan mengumpul data yang berkaitan. Pearson's correlation, regresi berganda, dan analisis diskriminan telah digunakan bagi menguji hipotesis. Keputusan kajian menunjukkan niat mempunyai pengaruh yang lebih ketara untuk membezakan antara mereka yang memilih SPI atau sebaliknya. Juga keputusan menunjukkan bahawa niat untuk menggunakan SPI produk dipengaruhi oleh komponen sikap (lebih ketara) dan komponen norma. Bagi faktor luaran seperti pengetahuan tentang produk SPI dan tahap keimanan seseorang itu pula, menunjukkan bahawa ianya tiada pengaruh langsung dengan komponen sikap dan komponen norma. Walau bagaimanapun, tahap keimanan seseorang itu menunjukkan ada sedikit mempengaruhi komponen norma. Implikasi dan arah tuju kajian menggunakan Teori Tindakan Beralasan ini juga turut dibincangkan di dalam kajian ini.

ABSTRACT

The purpose of this study is to identify the determinants of Muslim consumers' intention whether to engage in Islamic banking facilities or not to engage. Ajzen and Fishbein's (1980) Theory of Reasoned Action was used as a basis for this study. The theory posits that the immediate determinant of behavior is intention. Intention is determined by the weighted attitude toward the behavior and the weighted subjective norm. The variables under studied in this research were actual behavior, intention, attitude toward the behavior, subjective norm, and the external variables i.e. knowledge and religiosity. Combination of beliefs, evaluations, and motivation to comply determined attitude and subjective norm towards behavior. The sample consisted of 123 Muslim consumers located in Penang area. The Pearson's correlation, Multiple Regression, and the Discriminant analysis were used in the hypothesis testing. The findings indicated that the intention predictive power can be used to discriminate whether a person would choose to engage in Islamic banking or otherwise. Empirically, it was shown that the intention to engage in Islamic banking facilities was influenced by both the attitudinal and normative components with attitudinal components being more influential. As for the external variables (religiosity and knowledge), it was surprisingly noted that there were no significant influences towards the attitudinal and normative components with an exception of religiosity. Religiosity was indicated to have a significant influence towards the normative components. The implications and directions for future research using the Theory of Reasoned Action are discussed in this study.

Chapter 1

INTRODUCTION

1.1 Background study

Today, Islamic banking in Malaysia has firmed its position as a viable and vibrant component of the banking system. Bank Negara Malaysia has been in the forefront in providing the necessary and required infrastructure for the sector to grow further. There are currently two Islamic banks and 33 conventional banks with Islamic windows offering the full range of Islamic financial services. The Islamic banking system is expected to face strong competition not only from the Islamic banks but also from well-established conventional banks offering Islamic products and services.

According to Dr. Zeti Akhtar Aziz, the Governor of the Central Bank of Malaysia, in her speech at the Malaysian Banking and Financial Services Summit 2002, Islamic banking in Malaysia is now at the threshold of entering its next stage of development, to expand on a global basis, to gain greater acceptance as an effective and efficient means of intermediation and to contribute to the overall wealth creation. In order to expand globally, to gain greater acceptance, and to contribute to overall wealth creation, the factors that contribute to consumer's preference and behavior need to be studied in depth. In other words, it is imperative to understand why people choose which type of banking system, either conventional banking system or interest-free banking system, to satisfy their financial needs.

Under the Capital Market Masterplan, the Government had envisioned Islamic banking to constitute 20 per cent of the banking market share in 2010 (Bank Negara Malaysia). In order for the Islamic banking products or facilities to compete in the

competitive banking industries, customer preferences need to be satisfied. Given the fact that Banking industries either Islamic way or conventional way being very competitive, customers' satisfactions and preferences are very important in supporting the Islamic banking industries.

Several studies (Anderson, Cox, & Fulcher, 1976; Tan & Chua, 1986; Erol & El-Bdour, 1989; Erol, Kaynak, & El-Bdour, 1990; Haron, Ahmad, & Planisek, 1994; Hegazy, 1995; Gerrard & Cunningham 1997; Mettawa & Almosawi, 1998) have been done on determining customer preferences on selecting banking facilities in the United States of America, Jordan, Bahrain, Singapore, and even in Malaysia itself. Some of the studies even compared customer preferences on Islamic banks and conventional banks as well as among Muslims and non-Muslims. The most popular banking selection criteria among the customers are fast and efficient service, bank's reputation and image, and bank's confidentiality, the speed of transaction, and friendly bank personnel, reward extended by the banks, convenient location. Therefore, knowing what are the factors lead to customer preferences will give a competitive advantage to the banks in promoting their Islamic banking products or facilities.

1.2 Problem statement

With most of the banks in Malaysia now are offering Islamic banking products or facilities in order to be competitive nowadays, determining the marketing strategies for the products is crucial. The study purposely focuses on Muslim customers in order to see how attractive the facilities are among the Muslims. It is imperative to know whether Muslims consumers engage in the Islamic banking facilities or not and if they do, what

are the factors influencing them in choosing the facilities? Also, this study will examine to what extent do the external variables for examples, religiosity and knowledge of the Islamic banking facilities, influence their behavior?

1.3 Research Questions

The research questions concern, in one way or another, the consumer behavior in the context of Islamic banking. The fact that consumer behavior in Islamic banking lacks thoroughgoing research is one of the reason as to why this study is conducted.

The research questions to be addressed are as follows:

1. What are the characteristics of Muslim consumers who utilize the Islamic banking facilities?
2. What is the level of usage of the Islamic banking facilities?
3. How are the attitude and subjective norm of the Muslim consumers dependent on the external variables such as religiosity and knowledge of the products?

The next questions to be answered relates to the causal type of research because it deals with the relationship between attitudes towards Islamic banking and intention to engage in Islamic banking products or facilities.

4. How are attitudes towards Islamic banking facilities formed and how are they related to the intention to engage in the behavior?

The Theory of Reasoned Action (Fishbein, 1980) will be used in explaining the importance of subjective norms in banking behavior. Additionally, the Theory of Reasoned Action forms the basis for the development of the theoretical framework in this study. Thus, one major purpose of this thesis is to test whether the theory is valid in

predicting and explicating consumer behavior. Once the attitudes are known, this study will answer the following questions:

5. How are the subjective norms toward Islamic banking facilities formed and how are they related to the intention to engage in the behavior?
6. How is this relationship of the intention to engage in Islamic banking facilities and the actual behavior of engaging in Islamic banking facilities?

1.4 Research Objectives

The ultimate goal of this study is to determine why Muslim consumers choose Islamic banking facilities instead of conventional facilities. Once the reasons have been identified through this study, it is hope that effective measures or strategies can be established in making the Islamic banking facilities more attractive compared to the conventional facilities. Therefore, the marketing strategies that can attract consumers in choosing Islamic banking facilities can be implemented. In order to reach this goal, the following objectives of the study had been clearly identified:

1. To identify the characteristic of consumer who utilize the banking facilities.
2. To investigate the relationship of one's attitude (behavioral beliefs and outcome evaluations) on his or her intention to engage in Islamic banking facilities.
3. To investigate the relationship of one's subjective norms (normative beliefs and motivation to comply) on his or her intention to engage in Islamic banking facilities.

4. To examine the relationship between religiosity and knowledge of the products on one's attitude and subjective norms towards his or her intention to engage in Islamic banking facilities.
5. To identify the relationship between the intention to engage in Islamic banking facilities and the actual behavior of engaging in Islamic banking facilities.

1.5 Significance of Study

Research on Islamic banking has not previously focused much on attitude research for example on consumers' behavioral intention towards the products. Thus, this present study attempts to develop a model that is based on previous models such as the Theory of Reasoned Action (Fishbein, 1980). The external variables such as religiosity and knowledge in this study that are expected to influence the customers' intentional behavior. It is believed that those who are religious are most likely to accept or prefer Islamic banking facilities in order for them to conform to Sharia'h laws. Since majority of Malaysia population is Muslim, no doubt that Islamic banking facilities will be popular among them. In terms of knowledge of the products, the more knowledgeable the person is about the product, the more likely he or she will utilize the facilities. Therefore, in order to capture greater market share, consumers must be well informed of the products as well as the Islamic banking system itself. Not only does this study will contribute to the theory, it is also intended to have pragmatic value as well.

One of the objectives outlined in the Capital Market Masterplan was to establish Malaysia as an international Islamic capital market center. Under the plan, the Government had envisioned Islamic banking to constitute 20 per cent of the banking

market share in 2010. The Islamic banking and financial services grew by 30 percent with the industry registers about 45 percent growth per annum in 2001 (Bank Negara Malaysia).

As at end of June 2003, total deposits in the Islamic banking sector increased to RM45.4 billion, accounting for 9.4 percent share of the banking system, while Islamic financing in the same period increased to RM47.8 billion, accounting for a market share of 10.85 percent (Bank Negara Malaysia).

From a practical point of view, if all Muslims are to conform to Sharia'h, by engaging into the Islamic banking facilities, the objective of achieving 20 percent market share by 2010 can easily be accomplished sooner than planned. However, that will not be the case where not all Muslims will conform to Sharia'h because this is a very subjective and personal matter. In order to achieve the objective, strategic marketing plans must be established to aggressively promote the Islamic banking products and therefore, factors influencing the Muslims consumers' preference to engage into Islamic banking facilities should be determined.

1.6 Definition of the variables

Several key terms are used throughout this study and it is very important to define the meaning of each to enable better conceptualization.

- a. Religiosity – is defined as the intrinsic religious orientation in which religion provides the individual with a meaning-endowing framework in terms of which life is understood. In other words, it is more on a spirituality of an individual.

- b. Knowledge – is defined as the consumer’s knowledge of the Islamic banking products offered by the Islamic banks and the conventional banks that operate through the Islamic window. Example of these products are al-Wadiah, al-Bai-Bithaman Ajil, al-Murabahah, al-Mudharabah, Al-Gardh Ul-Hassan, al-Ijarah, al-Kafalah, ar-Rahnu, Takaful, and others such as Tabung Haji.
- c. Behavioral belief – is the Muslim consumers’ beliefs that engaging in Islamic banking facilities will lead to certain outcomes
- d. Outcome evaluation – is the Muslim consumers’ evaluations of the outcomes if he or she engages in Islamic banking facilities.
- e. Normative belief – are beliefs that specific referents think he or she should or should not engage in Islamic banking facilities.
- f. Motivation to comply – means that the motivation to comply with the specific referents who think he or she should or should not engage in Islamic banking facilities.
- g. Attitude – is defined as Muslim consumers attitude towards engaging in Islamic banking facilities. It is influenced by the behavioral beliefs and outcome evaluations.
- h. Subjective norm – is defined as Muslim consumers’ perception of engaging in Islamic Banking facilities. It is influenced by the normative beliefs and motivation.
- i. Intention – is viewed as a function of two factors which are the person’s attitude toward the behavior and the person’s subjective norm with respect to the behavior. In this study, it is defined as whether the Muslim consumers have the

intention of engaging into the Islamic banking facilities or not, are depending on their attitude and their subjective norms towards the Islamic banking facilities. The respondent might have the intention to utilize Islamic banking facilities but it does not necessarily mean that he or she will actually utilize it.

- j. Actual behavior – Muslim consumers who actually utilized the Islamic banking facilities.

Islamic banking products or Islamic banking facilities mentioned throughout this study will be used interchangeably and they are not only restricted to facilities or products offered by the two Islamic banks in Malaysia. It also consists of a full range of Islamic financial services offered by other conventional banks through the Islamic windows.

1.7 Organization of the thesis

This thesis is divided into five chapters. Following this chapter is Chapter two which review the literature related to Islamic banking research and the theory used as a framework of this study, Theory of Reasoned Action (Fishbein, 1980). In chapter three the research methodology adopted for the current study will be discussed. It consists of research design, research hypotheses, population and sample, data collection methods, variables and measurement, questionnaire design, as well as the statistical tools used in analyzing the data. Result of the findings is reported in chapter four and finally, chapter five will conclude the results of the study, the limitations, and suggestions for the future research.

Chapter 2

LITERATURE REVIEW

2.1 Background

In making financial decisions, consumers require information on a wide range of matters and details about the processes and documentation involved, the relevant fees and charges to be incurred, and the risks and benefits of each type of product or service. Increased access by the public to information will also increase the level of awareness not only of the rights of consumers but also on the responsibilities of both the consumers and financial institutions with regard to the financial products and services being offered. It is important for the consumers to be well informed of the Interest Free Banking system (Islamic Banking system) so that they can make the right financial decisions especially for the Muslim consumers. As consumers become aware of the Islamic banking financial product characteristics and the choice of financial providers, they will be in a better position to demand for a broader range of products and services customized to their requirements, at more competitive prices and through more convenient channels. For example, according to Ahmad Fuad Mohd Ali, the head of Islamic Banking at Standard Chartered Bank Malaysia Bhd, one of the success stories of demand has been in the unit trust sales. The bank distributes 16 Islamic unit trust funds and of these unit trust sales, 4.5 percent are from Islamic funds and 60 percent of the customers are non-Muslims. This indicates that Islamic banking instruments are also appealing to non-Muslim consumers. Therefore, well-informed and discerning consumers are a powerful force in shaping and driving the market. Banking institutions will thus have to continually

innovate in order to meet consumers' preferences and expectations. Consumers' demand will thus be able to drive business competitiveness, spur greater innovation and challenge banking institutions to strengthen their competitive advantage.

The Malaysian government has been doing a tremendous job in promoting the Islamic banking system to Malaysian consumers. All banks play their important role into getting people to accept the Islamic banking facilities. The promotions have been through advertisements in all communication media as well as having a program on television to educate people of Islamic financial system. With all the effort the government and financial institutions have put in promoting the Islamic banking facilities, many banking customers still prefer to bank with conventional system rather than the interest-free system. It is the consumers' choice to select their own banks in satisfying their financial needs. What determines this choice is believed to be determinants from the individual's belief, attitude, as well as the subjective norm towards the engagement into this interest-free banking system.

Many writers (e.g. Kotler, 1988; McIver & Naylor, 1986; Engel, Blackwell, & Miniard, 1995) claim that understanding and adapting to customer motivation and behavior is not an option but an absolute necessity for competitive survival. Early investigations by academics (Engel et al., 1995; Martineu, 1958) have indicated that a variety of characteristics are vital to understanding the consumer. Consumer behavior is often examined through two major psychological disciplines: (1) cognitive psychology, and (2) social psychology (Karjaluoto, 2002). The former refers to knowledge related to mental behaviors, i.e. attention, perception, comprehension and the decision making

process. The latter refers to the manner in which personality traits, attitudes, intentions and behaviors of the consumer influence and is influenced by social groups.

Studies of the intention-behavior relation have primarily been concerned with the intention to perform single behavior. However, in real life people commonly face a choice between alternative behaviors. In such cases people may be more deliberate about how to implement the behaviors, in particular if they need to be coordinated. In an extensive meta-analysis by Sheppard, Hartwick, and Warshaw (1988), it was in fact found that the correlation between intention and behavior increased in studies that involved a choice between different behaviors as compared to studies where no such choice was involved. In this present study, the intention of engaging in Islamic banking products or facilities is expected to be highly correlated with the actual behavior since the respondents are given the choice either to engage in the Islamic banking products/facilities or not to engage in the products/facilities.

The literature review will begin with the history of Islamic banking, and followed by researches in Islamic banking as well as the theory of consumer behavior research known as the Theory of Reasoned Action (Fishbein, 1980).

2.2 History of Islamic banking

The Islamic resurgence brought about the emergence of Islamic financial system for Muslims to fulfill their financial needs in a system that is in line with their religious belief. The development of an Islamic financial system led to the establishment of Islamic Development Bank in 1974 and the first Islamic commercial bank, the Islamic Bank of Dubai in 1975. Subsequent to that, a number of Islamic banks were established

in the Middle East, such as the Islamic Bank of Faisal in Egypt (1977), the Islamic Bank of Faisal in Jordan (1978), Bank of Islam Finance and Investment in Jordan (1978), and Islamic Investment Co Ltd. in UAE (1979).

Even prior to the mushrooming of Islamic bank, the Malaysian government has established the Pilgrims Fund Board or Lembaga Tabung Haji. This body was set-up to mobilize the savings of Malaysian Muslims to cover the cost of the annual Pilgrimage and invest them in productive sectors to yield returns free from interest or riba. The first Islamic bank in Malaysia, Bank Islam Malaysia Bhd (BIMB) was incorporated in March 1983, with an initial paid-up capital of RM80 million. BIMB business grew at an average annual growth of about 48 percent over a ten-year period. Total assets rose from RM325.5 million in 1984 to RM12.13 billion in 2002. This success led to the listing of BIMB on the Kuala Lumpur Stock Exchange main board on Jan 17, 1992. A single Islamic bank, however, does not fulfill the government's aspiration for a comprehensive Islamic banking and finance system. From only three banks in March 1993, the number of Islamic financial institutions has increased to 36, comprising two Islamic banks, 13 commercial banks (of which four are foreign banks), nine finance companies, five merchant banks, and seven discount houses. As at June 2003, total Islamic banking assets accounted for 9.4 percent or RM75.5 billion of total assets in the banking system. Deposits and financing respectively accounts for 10 percent and 9 percent of the banking system. Takaful assets accounted for 5.3 percent of RM4 billion of the industry as at 30 June 2003.

Today, Malaysia has succeeded in implementing a dual banking system and has emerged as the first nation to have a full-fledged Islamic system operating side-by-side with conventional banking system.

2.3 Research in Islamic banking

To date, Islamic banking products in Malaysia are available at two full-fledged Islamic banks and at all commercial and merchants banks. However, these products are still not fully accepted by customers (Ahmad & Haron, 2002). According to Bank Negara Statistical Bulletin Report, as at the end of 2002, total deposits at conventional banks were RM388 billion while total deposits in Islamic system was RM53 billion. In the case of loans, RM563 billion was extended by conventional system, and RM37 billion was given by Islamic system. Even with the support of the Government in introducing various measures to develop the Islamic financial system, its success is very much influenced by the market players. The market share of Islamic banking assets, deposits, and financing reflects public acceptance of this system (Ahmad & Haron, 2002). With the majority of the population in Malaysia is Muslims, the total funds deposited in the Islamic system remained insignificant compared to the total deposits in commercial banks and this is an indicator of public unwillingness to use the system (Ahmad & Haron, 2002). Due to this situation, there is a need to explore factors influencing consumers' preference towards the facilities, and therefore can further increase the Islamic banking market share in the banking industry.

Erol and El-Bdour (1989), Erol et al. (1990), Haron et al. (1994) and Gerrard and Cunningham (1997) in their studies found that the fast and efficient service is considered

as the most important factor for the bank customers, either Muslims or non-Muslims, in patronizing the Islamic banks. However, all these authors differ in their second and third factor in patronizing the Islamic banks.

The studies of Erol and El-Bdour (1989) and Erol et al. (1990) are considered as 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 second and third most important criteria in bank selection were the bank's reputation and image, and confidentiality respectively. This is because the customers are more confident in having their financial matters privacy protected apart from receiving excellent quality services from the banks.

Haron et al. (1994), however, in their study found that following the provision of a fast and efficient service as the most important criteria in selecting Islamic banking, the speed of transaction, and friendly bank personnel were considered as the second and third most important criteria perceived by Muslims customers in Malaysia.

Unlike, study done by Gerrard and Cunningham (1997) in Singapore, the second most important factor in patronizing the Islamic banks perceived by Singaporean Muslims differs from Muslims in Malaysia which was confidentiality of the bank, followed by the confidence in the bank's management respectively.

Mettawa and Almosawi (1998) focused their study to customers of Bahrain Islamic Bank and Faisal Islamic Bank of Bahrain. It was a different case from the previous study done in Jordan, Malaysia, and Singapore where they found that customers of these two Islamic banks perceived Islamic principle as the most important factor while

selecting Islamic banks. The second important factor was reward extended by the banks, followed by influence of family and friends, and convenient location.

Erol and El-Bdour (1989), Erol et al. (1990), Haron et al. (1994), Gerrard and Cunningham (1997), and Mettawa and Almosawi (1998) in their studies regarding the bank selection criteria shows that in order for the Islamic banks to be competitive in the market, quality of services need to be addressed importantly. Therefore, the success and survival of the Islamic banks depends on the bankers' ability to understand customer's needs and to find effective way to satisfy these needs.

Anderson et al. (1976) used "determinant attribute analysis" in a survey in the USA and stratified their samples according to convenience and services. Based on 15 selection criteria, convenience customers selected "recommendation by friends" as the most important factor in selecting a bank. Similarly, Tan and Chua (1986) in their research in Singapore, shows that the advice of friends, neighbors, and family members has a stronger influence on customers' decisions compared with other variables in selecting financial institutions. Even though these studies conducted on the conventional banks in USA and Singapore, this present study is attempt to see if these recommendations from friends and family has significant impact on the intention to engage in Islamic banking facilities.

Hegazy (1995) has investigated bank selection criteria for both Islamic banks and commercial banks in Egypt. He concluded that the selection attributes for Islamic banks are different from those for commercial banks. For the selection of Islamic banks, it was found that the most important factor was the advice and recommendations made by relatives and friends.

However, studies by Haron et al. (1994) proved the result otherwise. The recommendations by friends and relatives ranked number twenty-third from twenty-six selection criteria for Muslims respondents in Malaysia. The authors found that the findings is rather strange since in oriental culture, people still maintain strong traditional values, friends' and relatives' advice still has a strong influence on someone's decision-making processes.

The same result also found in Bahrain in which the reference-oriented factor was not the most important factor in selecting Islamic banks. It was found that a reference-oriented factor, reflecting the relative importance of friends' and peers' advice, and recommendations was the third important factor in the selection of Islamic banks besides, religiosity, the most important factor followed by the rate of return (Metawa & Almassawi, 1998). It indicates a relatively strong role for family and friends in passing on recommendations to their members and peers regarding the bank selection decision with a mean score of 3.51 for this factor.

Abd. Razak (1999) in his study of the relationship between attitude (independent variable) and usage (dependant variable) in Islamic banking found that significant positive relationship exists between attitude to and extend of usage of Islamic banking facilities, implying that persons with favorable attitude tend to engage in the facilities. In his study, the author did not use any theory to conceptualize the theoretical framework. Abd. Razak (1999) conceptualized usage and extent of usage as dependent variables, attitude towards Islamic banking as independent variable, with age, gender, education, marital status, income, and work experience as moderating variables. However, in this present study the model of TRA will be used as a tool to determine the relationship of

attitude and subjective norm towards Muslim consumers' intention to engage in Islamic banking facilities.

Lim (2001) used TRA model in predicting choice decision of numbers buyers in gambling, and the results showed that the model could be used in predicting choice decision of numbers buyers by explaining almost 59 percent of the variance in the intervening variable, intention to select the operator type. It was found that the subjective norm component has a higher predictive power than the attitudinal component. This finding was consistent with study done by Quah (2000) who also found that the normative component has a higher predictive power than attitudinal component in predicting the behavioral intention of consumer's preferences in infant formula selection.

Another study done by Hassan (2000) who also used the TRA model, revealed that attitude toward behavior and subjective norm explained significantly amounts of variance in behavioral intention for both private and public higher learning institutions. Contradicted with study done by Quah (2000) and Lim (2001), this author found that attitudinal component has a higher predictive power than the subjective norm component.

Therefore, it would be interesting to do a research in finding which components has a more predictive power over the intention to engage in Islamic banking, and see if the greater the intention is among the Muslim consumers, the more likely that they will utilize the facilities.

2.3.1 Knowledge as an External Factor

Even though it has been two decades since the Islamic bank was first established in Malaysia, not all Muslims have understood the differences between the Islamic banks

and conventional banks. A study by Haron, Ahmad, and Planisek (1994) in Malaysia where respondents are divided into Muslim (n=150) and non-Muslim (n=151) found that only about 63 percent of the Muslims have understood either partly or completely, of the differences. It is believed that the lack of Islamic banking knowledge is due to the customers not well informed. However, the important contribution from this study found that individual customers in patronizing an Islamic bank when they had knowledge of this new system. Approximately 80 percent of Muslim and 53 percent of non-Muslim respondents indicated that they would consider establishing a relationship with an Islamic bank if they had substantial understanding of its operation. Haron and friends conceptualized knowledge by assessing the consumers' awareness of the existence of the Islamic banks and by determining the sources of knowledge (i.e. newspaper, magazines, television and radio, and family members). In addition, one of the sections in the questionnaire asked the consumers' knowledge on the Islamic banking system itself.

Unlike Haron et al (1994), this present study will focus more on the consumer's behavioral model in assessing the consumer's intention to engage in Islamic banking system and how knowledge of the Islamic banking products influence the attitude and later lead to the intention towards utilizing the products. Therefore, the Theory of Reasoned Action model will further understands the consumers' behavior.

A similar situation occurred in Singapore, where only 22.6 percent of Muslims deposit money in Islamic banks solely because of religious reasons and over two-third of Muslim respondents said that deposits would be made for a combination of religious and profitability reasons (Gerrard & Cunningham, 1997). A study in Singapore showed that only 20.7 percent know the meaning of Riba' and 31 percent know the meaning of

Sharia'h. The study also showed that only 3 percent could explain accurately the meaning of Ijarah, Mudarabah, and Musharakah. Surprisingly, no one could explain accurately the meaning of Murabaha (Gerrad & Cunningham, 1997). Here, the authors measured the understanding of Islamic banking by asking whether the respondents know the meaning of the fundamental terms used in Islam and Islamic banking and finance, for example, Riba, Sharia'h, Ijara, Modaraba, Musharaka and Murabha. One of the contributing factors to this absence of awareness among Muslims is the lack of understanding of Islamic banking.

In a study done by Hamid and Nordin (2001), who sampled 967 commercial bank customers in Kuala Lumpur, Malaysia found that almost all respondents knew the existence of Islamic banking in Malaysia and the products and facilities offered by this Interest-free banking system. However, only about 50 percent of the respondents have been using Islamic banking facilities. Even though about 48 percent of the respondent says that they know Islamic banking financial product, but when asked about the meaning of the products, an average of less than 15 percent able to answer correctly. This is because the products are termed in Arabic words, which is very difficult for an average person to understand. The term in Arabic would not be a problem if the person were literate in Arabic language. The findings also highlighted that even though 54 percent of the respondent knew about the Interest-free Banking (IFB) Scheme, but more than 60 percent could not differentiate between IFB scheme and conventional banking financial products. This shows that there is a lack in knowledge of the Islamic banking products and the system itself. Similarly, knowledge as an external factor in this study will be conceptualized as a knowledge of the products or facilities, which are termed in Arabic

language. In this case the knowledge is expected to influence the attitude towards engaging in Islamic banking facilities as well as the subjective norm. As the more knowledgeable the person is about the products/facilities, the more likely the person will utilize the products/facilities.

2.3.2 Religiosity as an External Factor

Since the 1970s, Islamic banking has emerged as a new reality in the international financial scene. Its philosophies and principles are however, not new, having been outlined in the Holy Qur'an and the Sunnah of Prophet Muhammad (s.a.w.) more than 1400 years ago. The emergence of Islamic banking is often related to the revival of Islam and the desire of Muslims to live all aspects of their life in accordance with the teachings of Islam. As a Muslims it is required by Islam to live the live in accordance with Sharia'h. Religiosity is a very subjective issue and to measure this variable is not easy as it is determined by the person's spirituality. Being a religious person does not mean that the person has to engage in the Islamic banking facilities and in this study, the person's religiosity will be evaluated and see if there is an influence on the person's attitude towards engaging in Islamic banking facilities.

As institutions and facilities whose foundations are based on religious doctrine, it is paramount for the banks management to believe there are other factors that dominate the economic behavior of Muslims. These principles comprise the belief in the Day of Judgment and the life in the hereafter, the Islamic concept of riches, and the Islamic concept of success (Haron & Ahmad, 2000). All of these principles are expected not

only to have a significant impact on the decision-making process of Muslims, but also to have an influence on their perceptions of Islamic banks and Islamic banking facilities.

First of all, the definition of the religiosity itself needs to be established. As stated in Khairam (2000), the early famous classical “minimum definition” of religion was given by Taylor (1891), as the “belief in Spiritual Beings”, and Johnstones (1975) defines religion as “a system of beliefs and practices by which group of people interprets and responds to what they feel is supernatural and sacred.” Based on extensive definitions, Khairam (2000) in the end defines Islamic religiosity as “the degree level of individual commitment, involvement and practice internally and externally to the fundamental principals of Islam.”

Erol and El-Bdour (1989), Metawa and Almosawi (1998), Haron et al. (1994), and Gerrard and Cunningham (1997) used religion as one of the factors in the bank selection criteria. They conceptualize the religion as a factor in patronizing Islamic banks. Unlike in this present study, the religion will not be one of the factors in choosing to engage in Islamic banking facilities or products but it will be based on individual’s religiosity (spirituality) that is adopted from Khairam (2000) definition. Religiosity is taken as an external factor to the TRA model and it is expected to have influence towards the attitude and the subjective norms that leads to positive intentional behavior. Religiosity is seen as an important factor in this model because it is believed that there will be strong relationship with attitudinal and subjective norm components, which will then will increase the intention level of engaging in Islamic banking facilities.

Metawa and Almosawi (1998) in their study of Islamic bank customers in the state of Bahrain found that factor which received the highest degree of importance in the

bank selection process is a religious factor; the adherence to the Islamic principles, with a score of 4.7. This high score indicates that the selection of Islamic banks appears to be predominantly a religious-based decision. However, the findings are contradicted to those findings by Haron et al. (1994), and Gerrard and Cunningham (1997). The inconsistency might be because of the degree of Islamic culture of the origin country. Bahrain can be considered a very Islamic country and therefore, the intensity of the people religiosity might influence their decision in engaging in Islamic banking facilities. Whereas, Malaysia and Singapore are more on interracial types of countries even though Malaysia is considered as a Muslim country. The Muslim people in these countries lead a modern way of life that still abides by the Islamic principles. Therefore, their religiosity might or might not influence their decision to engage in Islamic banking.

Contrary to study done by Erol and El-Bdour (1989), Muslims in Jordan patronized Islamic banks not so much because of religious factor, but more because of the returns they would receive from their investments.

A study by Haron et al. (1994) in Malaysia where respondents are divided into Muslim (n=150) and non-Muslim (n=151) found that in terms of why people patronized the Islamic bank, about 39 percent of the Muslim respondents believe that religion is the only reason why people patronize the Islamic bank, and surprisingly, the percentage is much lower for non-Muslim respondent, which was about 31 percent.

2.4 Theory of Reasoned Action (TRA)

The Theory of Reasoned Action (Fishbein & Ajzen 1975; Ajzen & Fishbein 1980) states that the individual performance of a given behavior is primarily determined by a

person's intention to perform that behavior. This intention is determined by two major factors: the person's attitude toward the behavior (beliefs about the outcomes of the behavior and value of these outcomes) and the influence of the person's societal environment or subjective norm (beliefs about what other think the person should do).

In other words, a person's behavior can be predicted by knowing two things: (1) the person's attitude toward the behavior (A_B) and (2) the person's subjective norm (SN). The first component refers to the person's positive or negative feelings about engaging in the behavior. The second component refers to the person's perceptions of the social pressures to perform or not perform the behavior in question. Generally, people will perform behaviors that they value highly and that are popular with others and will refrain from behaviors that they do not regard favorably and that are unpopular with others (Petty & Cacioppo, 1981).

This theory provides a framework to study attitudes toward engaging in Islamic banking facilities. According to the theory, the most important determinant of a person's behavior is behavior intent. The greater the intention to engage in Islamic banking facilities, the greater the chances the person will eventually perform that behavior. The individual's intention to perform a behavior is a combination of attitude of performing the behavior and subjective norm. The attitudinal component consists of behavioral belief and evaluations of behavioral outcome, whereas the subjective norm component includes normative beliefs and the motivation to comply.

The TRA model can be expressed as

$$B \sim I = (A_B) w_1 + (SN) w_2 \text{ ----- Equation 1}$$

Where:

B = Behavior

I = Intention to perform behavior B

A_B = Attitude toward performing behavior B

SN = Subjective norm

w₁ and w₂ = weights

Normally the weights would be available for each individual with respect to each behavior in a given situation. However, if the estimates are not available, multiple regression techniques, and standardized regression coefficients will have to serve as estimates of the weights for the theory's components.

2.4.1. Attitude

Attitude is determined by his or her salient beliefs about the result of performing the behavior multiplied by the evaluation of those results. It is the first determinant of behavioral intention. It is the degree to which the person has a favorable or unfavorable evaluation of the behavior in question. If a person perceives that the outcome from engaging in Islamic banking facilities is positive, he or she will have a positive attitude toward performing that behavior. The opposite can also be stated if the behavior is thought to be negative.