

Research Article

A Case from a Developing Country: Why MSME Must Be Islamic Bank Clients

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Abstract

This research is intended to create reasons that why Micro Small Medium Enterprises (MSME) have to make decision for becoming a customer of Islamic Banking. We used semi-structured interviews to collect data from top management staff of MSME. (1) Which main variables influence top MSME management to become Islamic banking clients and why? Qualitative research method is restricted by the study research question. The data was coded and grouped for analysis later as per procedure. There were six possible themes that influenced the decisions made. Studies show that deciding for MSME's management for using Islamic banks as a source of financing found to be better and lucrative.

Keywords: Micro Small Medium Enterprises, Islamic Banking, Semi-structured Interviews, Qualitative.

Introduction

Islamic banks may be found in more than 75 countries, mainly in the Middle East and Southeast Asia, with Bahrain and Malaysia serving as the primary financial centres for Islamic banking. Islamic banking has emerged as a viable alternative to traditional interest-based banking in Muslim and non-Muslim nations alike during the past two decades. In many countries, the Islamic banking business is becoming a competitor to the conventional sector as it grows from its specialized niche. It was said by Dusuki and Abdullah (2006) that Islamic banking is no longer only focused on fulfilling Muslim community religious duties, but is also working to meet the needs and expectations of new clients (as cited in Wilson, 1995).

A growing number of financial institutions across the globe are taking note of Islamic banking's expansion. Islamic financial institutions currently exist in nations where Muslims constitute a minority population, while interest-based banks have created Islamic windows to appeal to the increasing Muslim population in Europe and North America (Pollard & Samers, 2007). The Islamic Finance House was founded in Luxembourg in 1997 as the first Islamic bank in the West. The Islamic Investment Company of Melbourne, Australia, and the Islamic Bank International of Denmark, both located in Copenhagen, round out the list. An enormous amount of Islamic banking has been established in Western countries, particularly in the United Kingdom, Australia, and the United States, as reported by Shanmugam, Perumal and Ridzwa (2004), proliferation of Islamic financial institutions such as interest-free savings and loans started to in countries where Muslims are a minority such as India in the 1970s (Siddiqi, 1988).

1-1. Categorization of Perception towards Islamic Banking

There are four types of previous researches on Islamic banking consumers' views. For the first category, researchers looked at how people perceived Islamic banking in mainly Muslim countries like Pakistan versus non-Muslim countries like Singapore. Other studies have looked at Islamic banking customers as a whole, rather than just Muslims and non-Muslims separately. Customers of Islamic and conventional banks are compared in the third area of research. As a last group, non-Muslim clients of Islamic banks have been the subject of recent research. These studies demonstrate that nation specifics have an impact on the results since people's worldview is formed by the legal, social, religious, and economic settings of a given country. When it comes to Islamic banking, respondents from mainly Muslim countries like Pakistan are more knowledgeable than those from primarily non-Muslim countries like Singapore and the United Kingdom (Hassan, 2007; Bley & Kuehn, 2004; Khan et al., 2007; Metawa & Al-Mossawi, 1998; Gerrard & Cunningham, 1997).

Consumers of Islamic and conventional banks were studied side by side to get an idea of the preferences of non-Muslim customers (Ahmad & Harun, 2002; Khan, Hassan, & Shahid, 2008; Zainol & Shaari, 2008; Haque et al., 2009). The reason for this is because earlier research has shown that although consumers share certain patronage criteria, there was no agreement on which one was more significant than the others.

1-2. The Role of Sharia Banks in Support of Social Welfare

Banking is a development agent in state economics because of its main role as an intermediary financial institution. The bank's job is to receive deposits from the public and then lend or finance the money back to the community. In addition to managing zakat, infaq, and shodaqoh (ZIS), Islamic banking also serves as an intermediary financial institution (Aggarwal & Yousef, 2000).

Because banks collect funds from surplus units and transmit credit to units with deficits, they play an important role in propelling the national economy. As a location where people may save and make payments making banks as the vital part of any healthy economy. Incorporating Islamic banking within a country's national financial system is anticipated to have a significant positive impact on economic

growth. To achieve economic development, Islamic banks in the economy strive for full employment, equal distribution of wealth, and a stable currency value (Herliansyah et al., 2020).

This is due to the application of the anti-Maysir (Speculation/Gambling) anti-sunset principle, Gharar (uncertainty) and usury so that Islamic banks have the following principles according to the Herliansyah et al. (2020).

- Brotherhood (ukhuwah);
- Justice;
- Benefit;
- Balance (tawazun);
- Universalism (syumuliyah).

1-3. Religious Factors Against the Decision to Become Customers of Conventional Banks

Religion is a set of ideas and practises that binds together moral communities such as Mosques, Churches, Temples, and other places of worship. These moral communities are referred to as "religious institutions." For example, it shows that the term "religion" can refer to a belief system that establishes rules for worship rituals to be performed, or it can refer to religion as a system that encompasses all aspects of life, including problems associated with economic development and the banking industry as a key economic driver (Ltifi et al., 2016).

It is called Islamic banking because it is based on the Islamic law system known as Sharia (Islamic law). Creating this method is motivated by Islamic law, which forbids charging interest on loans or borrowing money with the intent of repaying the loan with interest. An further support for this viewpoint comes from the MUI fatwa of 2004 on interest, which effectively prohibited banks from charging interest with usury components. Interestingly, Islamic banks' restriction on usury collecting, which is a key characteristic, has origins in non-Islamic religious beliefs as well (Sarwer, Ramzan, & Ahmad,2013).

The Qur'an Surah Al-Baqarah 2: 275-276 prohibits usury collecting, however it turns out that we may also discover similar prohibitions in the English-language Gospel updated version of Exodus 22:25 and Eutronomy 23: 19-20. Laws of Manu in Hinduism and Buddhism define usury, whereas Exodus 22: 25 and Leviticus 25: 35-37 in Judaism define usury (Herliansyah et al., 2020).

1-4. Location Factors against Decision to Become Customers of Sharia Banks

Purchasing a product or service is heavily influenced by where it may be located. Customers are unlikely to do product searches for items that are situated too far away from them. Customers will undoubtedly believe they have the time, energy, and money to do so (Erol & El-Bdour,1989).

As a result, the placement of the product or service in the business is largely reliant on the customer's buying choice. The bank branch serves as both a trading point for the bank's goods and a central control point. When it comes to actual bank office locations, there are a number of different kinds to choose from. These include the head office site, the primary branch, auxiliary branches, cash offices, and ATM locations (Herliansyah et al., 2020).

1. Literature Review

Previous research served as a foundation for understanding how consumers felt about Islamic banking. For example, in Pakistan, Hassan (2007) looked at how consumers perceived Islamic banking. Many factors were considered in his research, including: knowledge, socio-religious background, Sharia compliance, desire to work with Islamic banks, and the quality and attractiveness of products. According to the findings of this research, consumers have a more favorable opinion of Islamic banks' goods and services when compared to those of conventional banks on all aspects.

A research by Rashid, Hassan, and Ahmad (2010) looked at how consumers in Bangladesh felt about their local Islamic banks. They looked at six critical elements, including corporate efficiency, Islamic rule compliance, convenience, core banking, trust and cost-benefit analysis. According to the findings of this study, consumers place a high value on corporate efficiency and adherence to Islamic law as important deciding criteria when selecting a service. As an example, Dusuki and Abdullah (2006) looked at why Malaysians use Islamic banks and found that consumers were more satisfied with the quality of service and lower prices offered by Islamic banks. Patronage is influenced mostly by Islamic and financial repute, as well as service quality, according to the findings of the research.

Ahmad and Harun (2002) conducted a study on the impression of Islamic banking in Malaysia among business clients. They looked at things including how people use financial services, how well they understand Islamic banking concepts and procedures, and how they feel about it personally. When it comes to choosing a bank, business clients cite price as the most significant consideration. As an example, Rustam et al. (2011) looked at three key criteria to determine how Pakistani corporate clients perceive Islamic banking. According to their findings, variables including the use of conventional and Islamic banking facilities, respondent knowledge of the Islamic banking system, and individual opinions on different Islamic banking products like economic and religious views were all taken into account. They discovered that the Pakistani business sector has great potential for the Islamic banking industry.

Research has focused on how Islamic bankers and students see themselves as opposed to those who use the banks' services. Zainol and Shaari (2008) performed a study on the perception of Islamic banking among bankers in Islamic and conventional institutions. Islamic goods and services, training and experience, and Malaysia's potential for Islamic banking are all covered in their analysis. Compared to traditional banks, Islamic bankers have a more favourable view of Islamic banking, according to the study's findings.

In the United Arab Emirates (UAE), Bley and Kuehn (2004) studied students' knowledge and perceptions of conventional and Islamic finance. It was discovered that students' understanding of conventional banking terminology was superior than Islamic banking terminology when looking at attitudes and preferences for financial services as self-reported by them. Islamic banking ideas and procedures were better understood by students who scored higher on the academic performance scale.

Muslim and non-Muslim consumers in Malaysia were surveyed by Razak and Mohammed (2008) about their attitudes about the features and functionality of a particular Islamic banking product called Bai Bithaman Ajil (BBA). Because consumers were dissatisfied, the researchers recommended replacing BBA with Musyarakah Mutanakisah Partnership as a result of their findings (MMP).

Thambiah et al. (2011) examined consumers' perceptions and preferences about Islamic Retail Banking in the retail banking sector (IRB). They looked at the disparity between urban and rural Malaysian bank clients in terms of IRB awareness, perception, and preferences. In terms of awareness and perceptions of complexity, ambiguity, and observability, the research revealed a substantial difference. Returns, loan payback term, service costs, and overdraft facilities all seem to vary.

To see how Muslims and non-Muslims see Islamic banking, Loo (2010) looked examined attitudes and perceptions in Malaysia. He looked at knowledge, understanding of Islamic banking concepts, conflicts with religious beliefs, and other aspects of Islamic banking's attractiveness, disadvantages, promotional influence, Islamic banking's prospects, and willingness to do business with Islamic banking. He concluded that knowledge and understanding were the most important factors. According to the findings of this research, Muslims favour Islamic banking, while non-Muslims believe that Islamic banking is only important to Muslim communities.

Researchers Mahamad and Tahir (2010) in Kuala Terengganu looked at how non-Muslims perceive Islamic banking from two perspectives: comprehending Islamic banking concept and practices, and bank selection criteria. The results showed that non-Muslims had a positive view of Islamic banking. According to their findings, non-Muslims have less faith in Islamic banks' capacity to successfully compete with conventional ones, and non-users are less inclined to do business with them. In addition, non-Muslims prioritize good return on investment while choosing a bank, according to the results of this study. Abdullah, Sidek and Adnan (2012) conducted a study in Kuala Lumpur on perception of non-Muslim customers towards Malaysian Islamic banks and found that Islamic banking services are gaining ground among non-Muslims in Kuala Lumpur, by observing respondents' knowledge and understanding of Islamic banking, bank selection criteria and general customer perception among others.

According to research, saving money in an Islamic bank is not against the religion's teachings. However, knowledge factors were shown to be significant in the study's findings, while religion variables had a substantial impact on the decision to establish an Islamic bank savings account (Murniati, Deni, & Nani, 2020).

Using Islamic Banks as a Case Study, Aditya Putra Pratama (2017) looked at "Analysis of the Effect of Knowledge, Religiosity, and Rational Motives on the Decision Processes of Lecturers in Jakarta." It seems that knowledge factors, religiosity variables, and rational motivation variables all have a substantial impact on professor decision making while utilising Islamic Bank goods and services, according to the findings (Usman et al., 2017).

According to Utama (2017), "The Effect of Product Quality, Religion, Promotion Mix and Location on the Decision Process of Becoming BNI Syariah Branch IB Hasanah Savings Customers" was another comparable study. According to the findings of this research, product quality had a role in consumer decision-making to some extent, religiosity also played a role, and the promotion mix partially (location) also played a role (Herliansyah et al., 2020).

2-1. Rationale of the Study

However, it appears as though no studies have specifically examined top management's perceptions of MSME on Islamic banks in the context of Pakistani Banking Industry, which explore the factors influencing choice from traditional conventional banking rather than Islamic banking have been carried out.

2-2. Research Question

What are the major factors influencing top management of MSME to become the customers of Islamic banking and why?

2. Data Collection

Semi-Structured interviews have been utilised in the study to investigate the phenomena in depth. For the top management of MSME, interviews will be utilized to get insight into the reasons driving their decision to adopt Islamic banking instead of traditional conventional banking. Interviewing in an office environment is a difficulty since participants may be preoccupied with their job and unable to communicate their worries in a relaxed way because of their executive position. To get over this obstacle, we arranged the interview ahead of time at a time that was convenient for the participants, and then we conducted it somewhere else from where the employee usually sits. Participants were able to voice their opinions in a more comfortable environment because of the pre-scheduling and remote office settings. All interviews were semi-structured before being transcribed, coded, and then thematically or categorically classified. Finally, the relationship between the various sub-categories was examined.

3-1. Sample Size & Selection

With Quota Sampling, we chose instances to reach a certain number of individuals in each group. Quota Sampling is a non-random sample in which the researcher beforehand determines broad categories into which the participants would be selected (Radley & Chamberlain, 2012).

We made sure the interviewee was a reasonably senior management employee (15 to 20 years of experience) so that he or she could contribute recorded as well as tacit knowledge throughout the interview. A requirement of working in a Micro or Small or Medium Business restricted our samples, and we performed 29 interviews in all. The sample size indicates the number of interviews needed based on the information obtained from the interviews. Samples were taken from two major Pakistani cities (Karachi and Hyderabad).

3-2. Criteria for Exclusion

Employees with fewer than 15 years of experience are not taken into account in the selection process, even if they hold a position of leadership that is the top management position in MSME.

3-3. Analysis and Findings

The data was coded and grouped for analysis. Figure No. 1 shows this information so that similarities and variances in reactions to a comparable topic may be recognised. Respondents' answers to semi-structured interviews were transcribed and coded, and the eight following themes emerged from the transcripts and coding as a result.

Figure 1: Building Themes & Categories



- (1) **Religiosity:** Religiosity is the quality or state of being religious. Some participants were found to be religious while some were not completely religious minded; however, they were interested in Islamic banking due to increase in number of Islamic banks in Pakistan.
- (2) **Location:** Due to busy work schedule, mostly management is reluctant to visit those banks which are far from their territories. However, some participants have convinced that online banking has reduced the distances and location is not important nowadays.
- (3) **Interest Free:** Interest-free banking is an interest-free system that relies on a profit-and-loss sharing scheme. Participants claim that interest-free banking encourages individuals to spend their money and become partners in order to share profits and risks in the company instead of becoming debtors, thus management feels happy with this profitable Islamic banking feature.
- (4) **Reputation:** In the transmission of monetary policy, banks play a critical role, as one of the government's most effective instruments for promoting economic development while avoiding inflation. According to participants, opening an account at a poorly managed bank with astronomical fees or bad customer service can be annoying, very expensive and incredibly time consuming. Good reputed banks successfully attract depositors and investors and to maintain share price, banks need to maintain a reputation for good corporate governance and regulatory compliance. According to participants, reputation is very important but Islamic banks and conventional banks do not have extra edge on each other on behalf of that point only.
- (5) **Cultural Fit:** Islamic bank fits to the culture of Pakistan where influence of Sharia is increasing in the common people nowadays as per our participants. However mostly participants are convinced that there is not any understanding that conventional banking is not fit in our culture so either Islamic or Conventional, both are still seeming to fit to the culture.
- (6) **Religion:** For this reason, Islamic banking is often known as interest-free banking since it uses Sharia principles and does not incorporate riba (interest) in any of its products. According to participants, if MSME would follow the religious followings then it will entice their stakeholders too.

3. Discussion, Conclusion and Implications

With the completion of the data analysis, this section of study seeks to discuss. Prior to this study, researchers such as Kaawaase and Nalukwago (2017) discovered that commercial banks should take their clients' religious views into account when designing new products and marketing plans. Since both holy scriptures (the Quran and the Bible) forbid exploitation of a borrower, commercial banks and other similar organisations must recognize that Islamic banking principles are not limited to Muslim consumers alone. Religiosity, it turns out, has an effect on the decision to use Islamic banking.

Kaufman (1967) looked into the determining variables that consumers and businesses in the United States utilized to make bank selection decisions. There were three key criteria identified by him: the suitability of location for either a home or a company, as well as the duration of bank-customer relationships and the quality of banking services provided. 140 homes in Montreal, Canada were studied in order to learn how individuals choose their banks by Laroche, Rosenblatt, and Manaing (1986). Ranking the selection criteria reveals that the friendliness of the bank's employees is the most significant element in the choosing process. This is followed by hours of operation, length of waiting lines, and the bank's convenience. A study performed in Hong Kong by Kaynak and Kucukemiroglu (1992) examined the importance of the selection factors utilised by customers when selecting banks. Convenient location, financial advice, close parking, vault location, and loans and mortgages were cited as the most important aspects. According to our findings, internet banking has altered people's thinking and reduced the importance of physical location. In our study, we found that online banking somehow changed the thinking and have minimize the factor of location.

Okumus and Genc (2013) claim that for certain consumers, religious belief is the most important determining factor in bank selection criteria. However, among the other banks' selection criteria, factors like rate of return are in last place. According to Metawa and Almosawi, Naser et.al. (1999), Gaith and Worthington (2008) and Lee & Ullah (2011), religious motive is the main motivator in selecting an Islamic bank since interest is absolutely forbidden in Islam. Their research showed support for these claims.

There are several features that make banking and financial services distinct from other types of service. Banks' buying activity is unique, and access to capital costs play a critical role in how well they operate. Inter-bank ties were jarred as well by the financial crisis. The significance of financial reputation and its effect on interbank transaction price have been studied in many research related to this (Camba-Mendez, 2014; Buckley-Nixon, 2009). According to Saary and Medye (2017), the current account-keeping bank's reputation is very important when making a decision. However, in our study, reputation is worthy but there is no extra edge of Islamic banking on conventional banking due to this point.

Culture has become a key component in the social construction of the merger phenomena, and is therefore an essential aspect of the broader debate (Gertsen et al., 2004). The bank's culture may add value to a transaction and help it achieve its goals, but cultural incompatibilities might jeopardise its long-term performance (Warter & Warter, 2015). However, our research has shown that such an idea that conventional banking is the same as our culture does not contradict.

Islamic banking is the conduct of banking based on Syariah principles. Islamic bank is prohibited from taking and offering interest (riba). Profit sharing is encouraged by an Islamic bank. Two or more parties combine their investment resources and share the investment's profit and loss in a profit sharing arrangement (Marimuthu et al., 2010).

Expanding the network of Islamic bank branch offices and ATMs, as well as having a digital branch available to the community, would help Islamic banks gain clients. In order for clients like MSME to use Islamic banking, they don't have to be creative, but comprehending Islamic finance principles and

looking for the benefits are more essential factors to consider; while Islamic banks need to increase awareness among people about the benefits of adopting Islamic banking over the existing conventional banking. Looking aspects throughout this study, it is preferable for MSME management for taking decision to become Islamic bank customers. According to our study, if MSME would follow the religious followings then it will entice their stakeholders too. It is anticipated that the results of this study would shed light on the future growth of Pakistan's interest-free banking industry.

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