

Bai Bithaman Ajil (BBA) and Musharakah Mutanaqisah (MM): Comparative Analysis

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Abstract

Malaysia has always be at the forefront of Shariah-compliant financial products and is seeing a growth in Shariah or Islamic home financing. This paper investigates the most important factors need to be considered by home buyers in choosing Islamic Home Financing. Specifically, this paper examines home buyers preference in choosing Islamic home financing between Bai Bithaman Ajil (BBA) and Musharakah Mutanaqisah (MM). Ignorance on Maqasid al Shariah in Islamic home financing led to misinterpretation, disruption, chaos, and trivial conflicts among the contracting parties. busines stransactions, particularly for Islamic There are three main variables that are being used to identify most influenced factor which are *Shariah* compliant, pricing, and equality. Data was collected via questionnaires from 100 homebuyers who are taking either BBA or MM's home financing in Kota Bharu, Kelantan. Data was analysed using SPSS to analyse on Cronbach's alpha, frequency analysis, mean analysis, independent samples T-test and ANOVA. All variables have a significant value towards preference on Islamic home financing, it meet the purpose of the *Shariah (Maqasid al Shariah)*. MM home financing mode is more preferable based on Mean value as *Shariah* compliant and Equality shows a higher value compared to BBA. Findings are useful as it may help Islamic bank managers to enhance their planning for Isamic home financing products and develop effective strategies accordingly that benefit their customers.

Keywords: Islamic Home Financing, Bai Bithaman Ajil, Musharakah Mutanaqisah, Syariah Compliant, Pricing, Equality

1. Introduction

In early 1970s, the Islamic banking and finance institutions emerged in the Middle Eastern financial market while some Western bank also launched Islamic banking and finance product to serve their Muslim customers. In order to strengthening the regional business and finance, Middle East and Asian regions have become proactive in promoting Islamic banking and finance activities which it lead to give a big impact toward global financial markets. While number of Western financial institutions which offer Islamic's products and services is keep on increasing. The growing of Islamic banking and finance industry reached especially in Middle East and Southern Asia shows that Bahrain and Malaysia are the biggest hubs (Mansoor, &. Ishaq, 2008).

At some point of life, majority of the people will engage in house acquisition in order to fulfil their basic need in order to sustain their life (Maslow,1943). Accommodation is a fundamental

need which was one of Shariah objectives (Yusof and Usman, 2015). This is largely attributed to the population expansion and the change in lifestyle of individuals as living with family onto one house is the predominant tradition (Muneeza et.al, 2018). Muneeza et. al (2018) further mentioned that Islamic finance, house financing is one of the most requested forms of financing facility.

Islamic home financing shows tremendous growth throughout the years. From the existing 16 Islamic banks under Bank Negara Malaysia (BNM), the amount of Islamic home financing transactions amplified from RM29.8 billion in 2010 to RM131.1 billion as at the end of 2017, representing 27.1 per cent to Islamic banking's total financing. Hashim and Halim (2014), state that the increase in the demand for house in Malaysia is parallel to the growth of the population and their way of life, and bring forth the idea of purchasing a house is one of the strategies for long-term investment. Islamic Financial Institutions (IFIs) in Malaysia provide broad selection for house financing which facilitating the acquisition of houses by an individual irrespective of their motives.

Islamic banking and finance offers more ethical and efficient alternative especially to the Muslim that eliminate the element of *riba* (interest). Islamic home financing offers financial assistance to Muslims especially for those who intend to purchase their dream house. Islamic home financing is based on *Shariah* principles where the contract based on sales and purchase transaction between two parties. Islam prohibits the elements of *riba* (usury) and *gharar* (uncertainty). Among the Islamic home financing offered by the institutions such as Bai Bithaman Ajil (BBA), Musharakah Mutanaqisah (MM) and Ijarah Muntahiyah Bittamalik (IMB), this study will focus on BBA and MM only.

Generally, BBA is a deferred payment sale where the bank (financier) will buy the house at equal price but sell it back to customer (homebuyer) at a price plus profit margin over a tenor of financing. While MM is a concept of diminishing partnership where there is joint ownership agreement between customer and the bank where both parties will enter into partnership.

Various efforts have been Islamic banks captivated to promote Islamic home financing products, however, comparison on the acceptance of the products between Bai Bithaman Ajil and Musharakah Mutanaqisah is still lagging. When Islamic banks designed the products, customers' significant perspective not a pority. The aim of this study was to make a comparative analysis between BBA and MM for the homebuyers' preference in choosing Islamic home financing. By learning these factors, it might be possible to categorize homebuyers of home financing based on the level of information that they should be given. This present study may provide guidelines to the bank managers in understanding the homebuyer acceptance on Islamic home financing products.

2. Review of The Literature

Attitude, subjective norms, perceived control and Islamicity of product are instrumental in determining the consumer acceptance of Islamic home financing products by using the ordered

probit model (Amin et al., 2014). Based on *Theory of Planned Behavior (TPB)*, it shows that religiosity, attitude and perceived behavior had significant influences and positive effects on the intention of Islamic home financing among Muslims in Klang Valley (Janor, Che Wel, & Ahsan, 2012). A number of authors have considered the effects of religious belief is positive and significantly associated with the customer intentions to use Islamic home financing except pricing factor which is negative but significant (Ali, Raza, & Chin-Hong, 2015).

Bai Bithaman Ajil

By definition, BBA is a contract for financing sales by deferred instalments where the determination of the mark-up or selling price will depend on the stipulated annual rate of profit the bank desires from the transaction (Rosly, 1999). The BBA principle has been familiarized in almost all Malaysian financial institutions since 1983 (Abdul Razak, Mohamed, and Md Taib, 2008). Bank Islam Malaysia Berhad (BIMB) was the first financial institution that introduced BBA in Malaysia when it was established in 1984 (Aris et al, 2012). BBA often mistakenly took as a loan though in truth it is a sale with deferred payment (Smolo, 2010). However, the practice of BBA in Malaysia brings forth Shariah issue where the mechanism used allow a back-to-back buying and selling mode which similar to Bay al-inah. BBA is the most popular type of financing by almost every Islamic bank in Malaysia.

Figure 1 and 2 shows a clear understanding to compare the concept of Bai Bithaman Ajil and Musharakah Mutanaqisah being practiced in Malaysia (Azli et al, 2011).

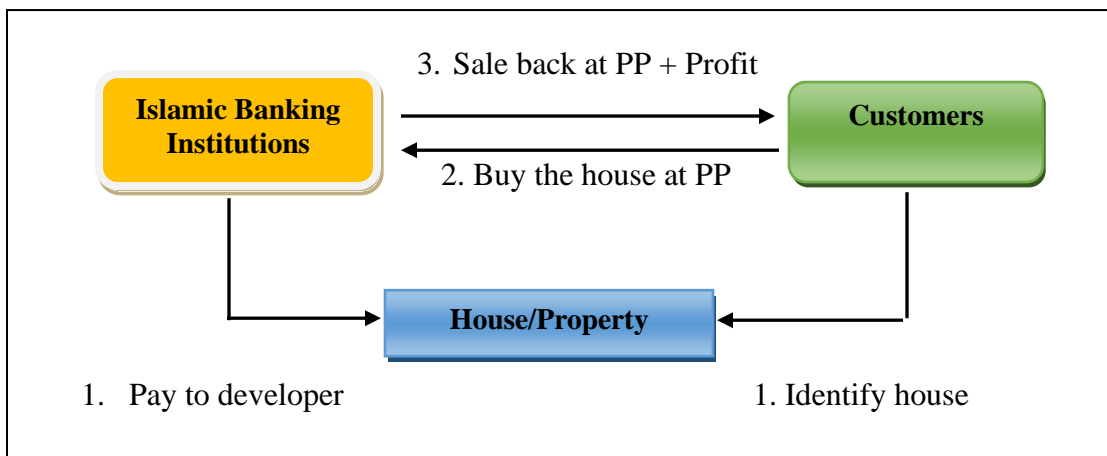


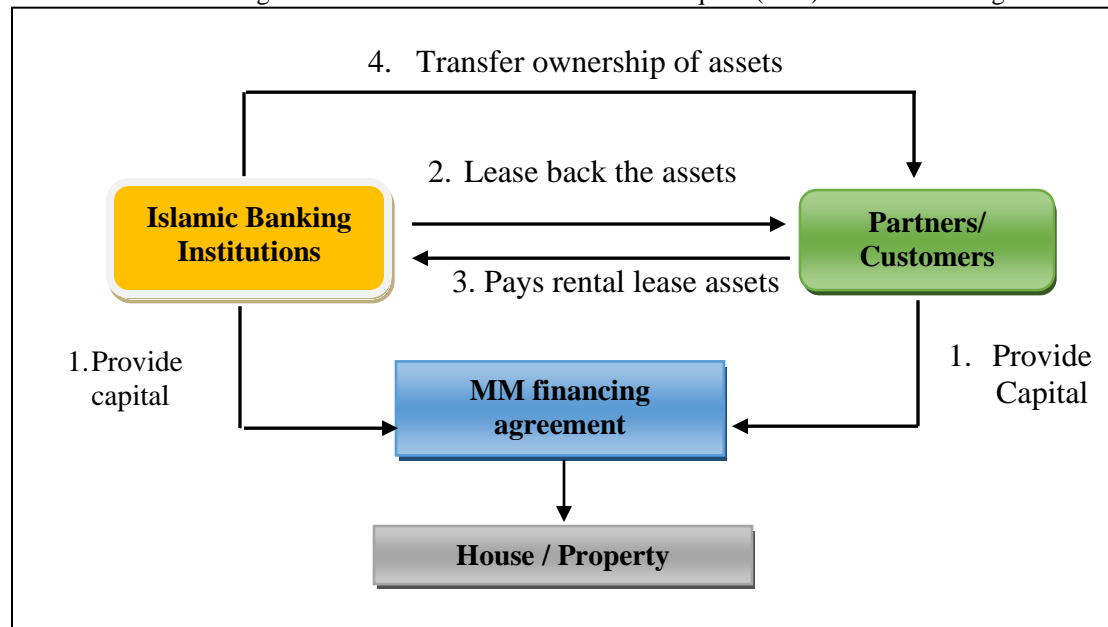
Figure 1: Structure of Bai Bithaman Ajil (BBA) Home Financing

1. The customer identifies the property and normally pays 20% of the selling price and asks the bank to finance 80%.
2. The customer then signs an agreement with the bank. The bank will buy the property from the customer at a price equal to the financing amount required. The bank will pay the remaining 80% to the developer.

3. The customer then agrees to buy back the asst at a price equal to the financing amount plus profit charged by the bank. The amount will be paid on deferred terms based on tenor agreed.

Musharakah Mutanaqisah

Figure 2: Structure of Musharakah Mutanaqisah (MM) Home Financing



1. The customer identifies the property and normally pays 20% of the selling price with 80% being financed by the bank. The customer and the bank will therefore own 20% and 80% of the property, respectively.
2. The customer then leases/uses the property.
3. To compensate the bank, the customer pays rent for the use of the bank's share of the property.
4. The bank's share of the property is divided into 20 units of 4% each (assuming the tenor is for 20 years). The customer promises to buy one unit each year for the next 20 years in the form of rental payment. Once the units have been fully owned by the customer, the property will be the customer's and the bank will have the profits.

Particularly, MM has been used by Islamic bank to govern their Islamic home financing products. Musharakah is a term that is commonly associated with Islamic finance (Usmani, 2008). Musharakah Mutanaqisah (MM) is a concept of decreasing partnership that consists of three contracts, which are Musharakah (partnership), Ijarah (renting) and Bai (sales) (Smolo and Hassan, 2011). As a hybrid contract, MM was described by Bank Negara Malaysia (BNM) as a partnership contract that permits one (or more) partner(s) to grant the right to progressively own

its share of the asset to the remaining partners on the basis of negotiated terms and conditions (Bank Negara Malaysia, 2010).

MM has a few procedures which are at first place, bank and the customer will participate in joint ownership of a house (Shahwan et al., 2013). Bank then buy the house and leases the house to the customer using *ijarah* (leasing) principle. The customer pays the monthly installment in a form of rental payment to the bank. The monthly payment will gradually increase the share of the customer while at the same time it reduces the share of the bank. At the end of the contract period, all ownership of the house is belongs to the customer, making him solely owner of the house.

Islam encourage to strive for social justice, thus requires fair and equitable distribution of wealth (Ajaz, A.K. & Helen, M., 2008). Since bank and the customer is joint owners of the house, both of them have same commitments in ensuring the transactions is based on the *Shariah* principle and effectively successful in term of the transfer of ownership of the house and monthly payment (Hanudin, 2014). Thus, profit loss sharing in MM is been the best solution in order to ensure justice among Muslims.

Issue on Bai Bithaman Ajil and Musharakah Mutanaqisah

Studied done by Razak, D. A. & Abduh, M. (2012), conventional home financing does not followed *Shariah* where the bank does not own the house from developer and does not have the possession on the property. In other words, bank does not have the ownership of the house before selling the house to the customer with price plus profit margin. According to Dzuljastri, A.R. & Fauziah, M.T. (2011), the practice of Bai Inah has drawn criticism on the practice of BBA home financing when bank does not have the ownership on the house. In contrast, MM home financing is followed *Shariah* where it does not involve in Bai Inah because bank and the customer is a joint owner of the house.

According to Aris et al. (2012), theoretically it has been claimed that the financing facility based on Musharakah Mutanaqisah (MM) is more superior to BBA as due to the claim that MM offers an equity contract which promotes the welfare of the people as the unsettled balance of the financing at any point in stipulated period would never exceeds the original price of the asset agreed upon signing the contract.

MM is trusted as fully-Shariah product and perceived by the customer to substitute BBA application for home financing. They agreed that MM is not similar to the conventional pricing. Nowadays, the importance of Shariah rules and regulation and also Maqasid Shariah among customers are gaining more awareness (Hasnat, Alom, & Talukderc, 2017). Current practice of MM in Islamic bank still contains the element of interest particularly in determining rental rate. It might be because of the elements of uncertainties and speculation but it can be resolved with the consistency of the real value of MM and upholding the spirit of partnership and mutual consent. They also suggest to replace interest and Base-Lending Rate (BLR) with the new structure which comprise of Islamic rental rate, risk premium, over-head expenses and profit margin (Mahfudz et al, 2016).

According to Razak et al. (2008), the term of “interest rate” was replaced by “profit rate” in the pricing computation of BBA. The profit rate in BBA financing is based on market interest rate or base lending rate (BLR). While in MM financing, the pricing is not a predetermined matter. The MM financing is relies on performance and not guaranteeing specific return as the nature of MM financing is based on partnership (Syahidawati et al., 2013). According to Roslin et al. (2012), propose rental rate pricing is a replacement of interest rate as benchmark of profit rate. The rental rate is based on the actual market value where the rate is different depending on the type of house. The rental rate also depends on

MM is significantly influenced by promotion and religious compliance. By doing large scale advertisenets by Islamic banking insitutions would increse consumer awareness of the advantages of MM products and the disparities between these products and other home financing products (Zakaria Baharia, 2019). Research done by Hanudin Amina (2019), bank’s branch manager should concentrate on building the beliefs of subjective standard, pricing policy, insitutional enforcement on maqasid and blog influence, customer attitude and preference as part of their home financing strategy in a highly competitive marketplace. By retaining and improving the position of these variables, both Muslim and non-Muslim customers have increased demand on Islamic home financing. With better packages and service delivery, banks will facilitate better pricing practices for all potential borrowers.

3. Research Methodology

This study is conducted in Kota Bharu, Kelantan due to the time amd financial resources constraints. Kota Bharu is situated in the north-eastern cornr of the peninsular of Malaysia where the population of Muslim is 96.2% (Department of Statistics, 2010). The sampling unit of this study is the homebuyers who are users of BBA or MM’s Islamic home financing that using Islamic banks’ home financing products to participate in the study. The techniques of sampling used in this study was non-probability sampling method to select the samples since the sampling frame for the study is unavailable. This study uses convenience sampling for data collection because of the limited access of the actual number of bank customers of Islamic banking. Besides, convenience sampling is the most common sampling method in Islamic banking research (Amin, 2012). Data was collected via online questionnaires from 100 respondents assisted by numerators who have been trained to handle the survey. The division of the respondents for BBA and MM is equal. Thus, according to this sample size for this research, it shows minimum sample size is 100 based on the population given as referred to sampling method suggested by Yamane (1967). Questionnaires was sent to the respondents in Google Form. Since this study employs homebuyers of Islamic home financing, therefore it has an effect on the generalization of findings for the homebuyers of Islamic home financing population in Kota Bharu, Kelantan, Malaysia.

The instruments used in the study is a online questionnaire. The questionnaires contained two parts: the first part, collecting data on demographic characteristics which are academic qualification, employment sector and monthly income The second part of the questionnaire

collected on the *Shariah* Compliant factors, followed by Pricing, and Equality. An instruction section was also prepared to help the researcher estimate the respondents' awareness first and then proceed to other sections. Items of *Shariah* Compliant, pricing, equality and home financing are adapted from previous studies (Al-Ajmi et.al, 2009; Erol and El-Bdour, 1989; Haron et. al, 1994). The respondents were asked to indicate, on a five-point Likert-scale ranging from "strongly disagree" (1) to "strongly agree" (5). This approach similar to study done by Devlin, J.F. (2002). The data for this study were collected through self-administered questionnaires distributed by the researchers.

Statistical analysis was employed with SPSS (version 21.0, IBM) to analyses the raw data in this study. In this study, Cronbach's alpha used to test reliability of the research instruments. The results shows that Cronbach's alpha coefficient for all variables are between 0.80 and 0.90 which considered "very good" and the instrument used is consistent and stable. Furthermore, a number of statistical analyses were performed, frequency analysis which uses to extract the characteristics of respondents, mean analysis, independent samples *t*-test and ANOVA. The former is used to analyses preference criteria in general whilst the latter is used to analyses preference criteria with respect to BBA and MM. For the investigation to examine differences between preference criteria, two analyses were used, notably independent samples *t*-test and ANOVA. The 95% confidence interval was used to present the precision of the estimates.

4. Results and Findings

Descriptive Statistics

Frequency analysis is employed to observe the number of responses that the researcher obtained from the respondents. Number of survey responses were 100 homebuyers. As depicted in **Table 1**, majority of respondents are well educated, with more than 34 percent holding Diploma/Certificate and about 45 percent holding a bachelor degree or above.. In terms of employment sector, most of the respondents worked in public sector (66 percent), while 24 percent worked in private sector and balance of 10 percent are self-employed.. The result showed that about 47 percent of the respondents earned RM2,501-RM5,000 per month, and 19 percent earned below RM2,500. This result indicates that most of the respondents can be classified as middle-class income earners since majority have monthly incomes range between RM2,500 to RM5,000 as definition given in the Eight Malaysian Plan (2001-2005). Lower-income households were defined as those earnings less than RM1,500 per month. The middle-income households, defined as those earnings between RM1,500 and 5,000. While higher-income households, defined as those earnings between RM5,000 and above.

Table 1 Respondents' Characteristics

Items	Frequency	Percentile
<i>Academic Qualification</i>		
▪ PhD/Master	44	14%
▪ Bachelor Degree	45	45%
▪ Diploma/Certificate	34	34%
▪ Others	7	7%
Total	100	100%
<i>Employment Sector</i>		
▪ Public Sector	66	66%
▪ Private Sector	24	24%
▪ Self-Employed	10	10%
Total	100	100%
<i>Monthly Income</i>		
▪ Below RM2,500	19	19%
▪ RM2,501 – RM5,000	47	47%
▪ RM5,001 – RM10,000	29	29%
▪ Above RM10,000	5	5%
Total	100	100%

Table 2: Descriptive Statistics

Variables	Type of product use in Islamic home financing	Mean
Shariah compliant	BBA	2.7880
	MM	4.3240
Pricing	BBA	3.5000
	MM	3.3240
Equality	BBA	4.1200
	MM	4.2360

As presented in **Table 2** for MM, the home buyer has higher preferences on *Shariah* Compliant and Equality as compared to BBA. While for BBA, Pricing has a higher preference from the homebuyer as compared to MM. This result supported by previous study conducted in the United Kingdom, in which the demand and supply of Islamic home financing is influenced by the features of the product that based on *Shariah* Compliant (Tameme, Mohammad El Khatim, 2009). Besides that, Islamic society is influenced by a district Islamic worldwide based on *Shariah* where practice justice and equality. Islamic banks must sensitive to the need of the society as the goal is not profit making but to endorse socio-economic development according to Kamal (2009).

Independent Sample T-Test

Table 3: Independent Sample T-Test

Variables	t	Sig. (2-tailed)
Shariah Compliant	-14.996	.000
Pricing	1.996	.049
Equality	-2.120	.037

Table 3 shows that independent sample *t*-test being carried out in order to compare the two groups which are group that used BBA and MM. Since the *p*-value for all variables have a significant value, it shows that there are differences between BBA and MM for *Shariah* Compliant, Pricing, and Equality.

5. Conclusion and Recommendation

The main motivation for this study is to examine home buyers' preference on two modes of Islamic home financing namely BBA and MM. The results show that the home buyers are sophisticated in their assessment whether or not the product is *Shariah* Compliant. Since all variables have a significant value towards preference on Islamic home financing, it meet the purpose of the *Shariah (Maqasid al Shariah)*. *MM* home financing mode is more preferable based on Mean value as *Shariah* compliant and Equality shows a higher value compared to BBA. The challenges remain for the bankers to offer a product that fully embraces the concept including using rental rate as a benchmark to satisfy the equality. *MM* can be extended or applied to the purchase of equipment or vehicles, partnership and private equity arrangements.

Midset, subjective standard, perceived behavioral influenced price fairness have a major impact on the intention of Muslim bank customers to choose Islamic home financing products (Sayuti, and Amin, 2019). The challenges remain for the bankers to offer a product that fully embraces the concept including using rental rate as a benchmark to satisfy the equality. *MM* can be extended or applied to the purchase of equipment or vehicles, partnership and private equity arrangements.

The limitations of the study are discussed to clearly establish the boundaries and to identify future avenues for research. First, due to time and situational constraints, the respondents were only limited to the Kota Bharu, Kelantan area only. Nonetheless, the study received encouraging responses from the respondents and future researchers could be conducted on this basis. It is important to note that there might be regionalization of the respondents. Hence, generalizing the results of the study of the overall population need to be done cautiously.

The number of respondents for this research may not be substantive enough for such behavioral research, especially in measuring intention of non-Muslims. This exploratory research could be improved in the future research through empirical cross-culture and cross-country studies. In

addition, future research could investigate similarities and distinguishing characteristics of home buyers from various nationalities.

In order to raise the confidence level among the Muslims, Islamic bank should robust research in developing more products which are fully *Shariah* Compliant. They have to produce more Syariah compliance product to capture Muslim market and must go through the Islamic laws and norms. They also must comply with the framework regulate by *Shariah* Board in order to ensure their conduct of business in line with Islamic principles. There is a conflict in BBA home financing where the bank gains profit plus margin. Thus, Islamic banking institutions should resolve the problem by producing more products based on profit-loss-sharing (PLS). PLS is not only representing a true spirit of Islamic banking but also departs significantly from interest-based system (Dusuki and Abdullah, 2006). Islamic banking should make paradigm shift by implementation of PLS's products hence increase the productivity and output can eliminate the problems of poverty and society become more stable.

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