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SELECTION CRITERIA FOR ISLAMIC HOME FINANCING CASE STUDY: CUSTOMERS OF BANK ISLAM MALAYSIA BERHAD

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Abstract

Of Man's most basic needs, shelter is the most expensive, especially if he chooses to live in an urban environment. To obtain long term loans, borrowers must possess some measures of credit worthiness thus limits the number who can afford to pay for a house. Nowadays, there are many financial institution that offer housing loans. However, each financial institutions are varies in terms of the types of loan as well as the lending rate. In lieu of the rapid and massive development especially the residential houses have resulted to the tremendous increment of the number of housing loans being offered by financial institutions. Besides Middle East countries, Malaysia has been one of the famous financial centres for Islamic finance. Amongst the financial institutions in Malaysia, Bank Islam Malaysia Berhad (BIMB) has been of the earlier pioneer for Islamic financing as an alternative from existing conventional banking. The main objective of this research was to find out the top five choice criterions for Islamic home financing among Bank Islam Malaysia Berhad customers in Kuala Lumpur.

Keywords: Choice criterions, Home financing, Islamic Bank, Islamic Financing

1. Introduction

Of Man's most basic needs, shelter is the most expensive, especially if he chooses to live in an urban environment. The daily needs of food and clothing are purchased with long term loan usually using property, if any, as collateral. To obtain long term loans, borrowers must possess some measures of credit worthiness. This immediately limits the number who can afford to pay for a house. (S. Jagatheesan, 1976).

Nowadays, there are many financial institution that offer housing loans. However, different financial institutions offer different type of loan. Since the production of the residential is on the rise, the number of housing loans being offered by the financial institutions is also rising. There are varieties of housing loans being offered in the market. Different financial institutions offer different lending rates in completion to get hold of the house buyers.

For the house buyers, they should spend more time on choosing the best housing loans offered in the market. Since there are varieties of housing loans being offered in the markets, prospective buyers and of houses are provided with a lot of choices in choosing housing loans to finance their houses. Therefore, the features of housing loans offered by the financial institutions are very important for the prospective buyers to consider in choosing housing loans. Besides, there are also other factors that will influence decision making in choosing housing loan.

1.1. Definition of Islamic Banking

An Islamic bank is defined as an institution offers interest-free products and services where Shariah will curb the operation of the bank through Shariah Advisory Council or SAC. In general, Islamic banks still perform similar functions to that of conventional bank, although some differences do remain (Dusuki and Abdullah, 2007; Iqbal and Mirakhor, 2007). According to Dar and Presley (2000), an Islamic bank is an intermediary and trustee of other people's money with a key difference, in that it shares profit and loss with its depositors. Additionally, the Islamic banking operation must abide by Islamic law commonly known as Shariah. Most of the definitions of Islamic Banking revolve around two main points – Prohibition of interest and Profit Sharing. According to Investor Dictionary (2006), Islamic banking refers to a system of banking which is consistent with Islamic law and guided by Islamic economies. In particular, Islamic law prohibits the collection of interest, also commonly called the *riba* in Islam discourse.

1.2. Concepts of Islamic Banking in Malaysia

Malaysia is the second biggest hub of Islamic banking and finance. The first Islamic bank, Bank Malaysia Berhad (BIMB) was established in Malaysia in 1983 in order to provide Shariah compliant financial products and services to Malaysians, regardless of their religion. At the same time, BIMB was the player with a monopoly in the country to offer Shariah compliant products and services. The conventional banks were not allowed to offer Shariah compliant products and services due to two main reasons. First, the governments decide to give BIMB a lead period of 10 years before allowing another Islamic bank to be established. This was enabling the bank to fully focus on the development of Islamic banking. Secondly, it allows BIMB create as many products as possible to provide Malaysian, particularly Muslims, with adequate Islamic banking products and services.

1.3. Islamic Banking Housing Finance: Home Financing-i

This part of the literature review on Islamic banking housing finance is obtained from Banking Info (2005). The Islamic banking product of housing loan offered by banking institutions in Malaysia commonly known as home financing-i or house-financing-i. Home financing-i is a Shariah based financing facility to finance the purchase of all types of residential properties including houses, flats, apartments or condominiums. It can also be used to refinance existing facilities taken either from conventional housing loans or other house financing-i schemes.

The amount of financing provided by Islamic banking institutions depends on the market value (for completed properties only) or the price of the property. The margin of financing could be up to 95% of the value of the property, depending on the policy of the Islamic banking institution. Meanwhile, the tenure of financing can be as long as 30 years or until the purchaser reaches age 65. The plus points of home financing-i as opposed to the conventional housing loan is that the selling price of the property is fixed at the time of contract and there is no additional or hidden costs that will change the selling price of the property later on. Also, the repayment amount is not subjected to fluctuations in interest rates. There is no compounding of arrears and it allows for better personal financial planning.

1.4. Concepts of Home Financing-i

The three main concepts applicable in Islamic banking and recognized by the central bank of Malaysia are Bai' Bithaman Ajil, AL-Istisna' and Variable Rate Ijarah. Therefore, it is of utmost important to understand how the dominating BBA facility works on Islamic bank, before going into detail choice criteria for Islamic home financing.

1.5. Choice Criteria for Banking

The investigation of choice criteria for Islamic banking by Erol and El Bdour (1989) discovered that the most important criteria considered by customers in patronizing Islamic banks are the provision of fast and efficient services, the banks reputation and image confidentiality. This finding by Erol and El-Bdour (1989) was supported by Naser et al., (1999) who studied Jordanians customer's satisfaction which mainly focused on the bank's name, image, confidentiality and reputation. Indeed, provision of fast and efficient services are always regarded as high quality services by bank customers who value time and expect the transaction to be completed as quickly as possible. Therefore, it is argued here that in order to survive, Islamic bank should not rely on religious factor alone since other factors stated earlier are also important.

This is consistent with findings from Haron et al (1994) who based in their study in Alor Setar, Sungai Petani and Kangar and found fast and efficient services, speed of transactions, friendliness of bank personnel and confidentiality of bank are important factors affecting banking selection. A study by Metawa and Almoosawi (1998) pointed out that provision of Shariah compliant products and services were highly regarded by majority customers while selecting banks. Other factors were the reward given by banks, family influence, convenience location and customers' education and knowledge. This study does not seem to uphold the findings by Haron et al. (1994) and Gerrard and Cunningham (2001) where the important lessons are twofold. Haron et al. (1994) did a study in Malaysia on the dual banking framework where multicultural societies are found and about 60 per cent of the population are Muslims. Gerrard and Cunningham (1997) undertook a study in Singapore where non-Muslims are 70 percent and over. Conversely, most of the respondents employed by Metawa and Almoosawi (1998) study were Muslim equating to 90 percent and over. These factors have contributed to different results.

Boyd et al, (1994) found the five most important factors affecting bank customers' selection for bank are:

- (1) Bank reputation
- (2) Interest on savings account
- (3) Interest charged on loans
- (4) Quick service
- (5) Location in the city

2. Research Question

A research question is a statement that identifies the phenomenon to be studied. In this study key research question is:

1. What are the five main decision criteria that influence bank customers in choosing Islamic home financing?

3. Research Objective

Research objectives are in short, the goals that a researcher wants to achieve. As a process, they help us to stay focuses on the issues at hand. The research endeavours to achieve the following objective:

1. To determine the top five choice criteria that influence bank customers when choosing Islamic home financing.

3. Research Methods

Methods of data collection in this research are questionnaire based survey. The questionnaire for this study was constructed into two sections. The first section consisted of demographic elements namely gender, religion, marital status, age range, educational level and monthly income. The second section consisted of the selection criteria. The measures employed in this study are extracted from previous studies but some selection criteria are self-created in order to better reflect Islamic home financing.

5. Findings

5.1 Respondents Profile

Section A of the questionnaires deals with the profile of the respondents, which constitutes the personal information of respondents. Only 50 questionnaires were distributed and out of these, only 47 questionnaires were filled completely without errors with a response rate equivalent to 80 per cent. The demographic profile of the respondents is outlined below.

5.2 Section B: Choice Criteria for Islamic Home Financing

Part B were more on finding the factors that influenced the bank customers in choosing the Islamic home financing

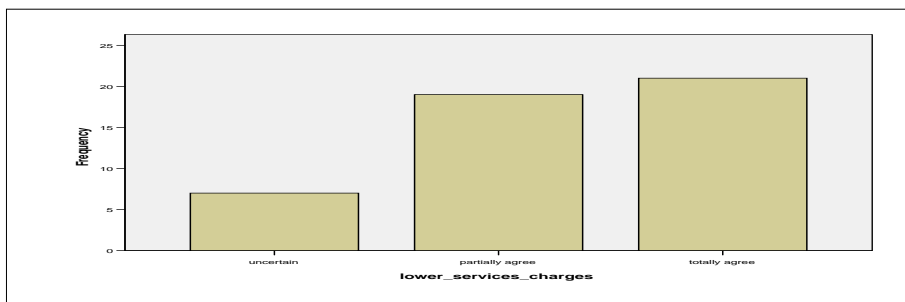


Figure 1: Lower services charges
(Source: Own Research, 2012)

The study showed that majority of the respondents were totally agreed that lower service charges have major influence on bank's customers decision in choosing the Islamic home financing product. Nevertheless, 19 of the respondents involved in the survey were partially agreed on this particular choice criterion and followed by the remainder of 7 respondents were uncertain on the above mentioned criteria.

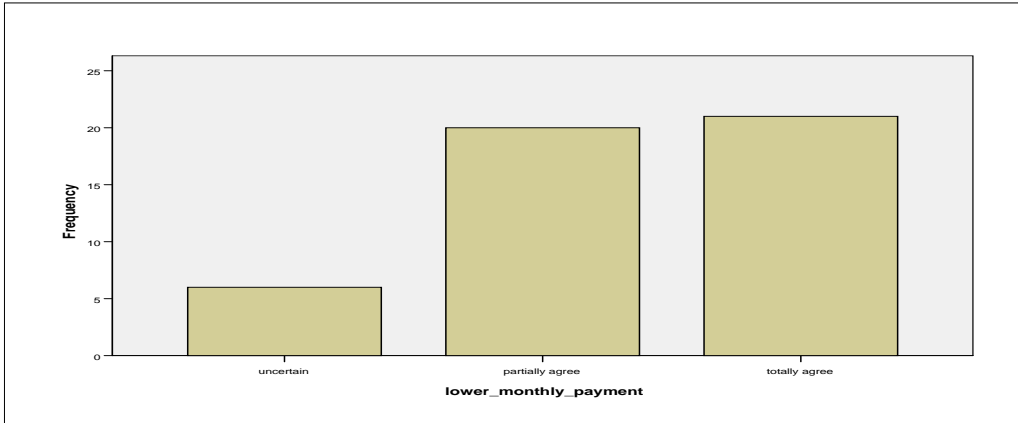


Figure 2: Lower monthly payments
 (Source: Own Research, 2012)

In terms of lower monthly payment, as can be seen in the above table, majority numbers of 21 respondents were totally agreed that lower monthly payment was one of the choices criteria that important in choosing Islamic home financing. Meanwhile, 20 of the respondents indicated that they were partially agreed and 6 respondents were uncertain on this choice criterion.

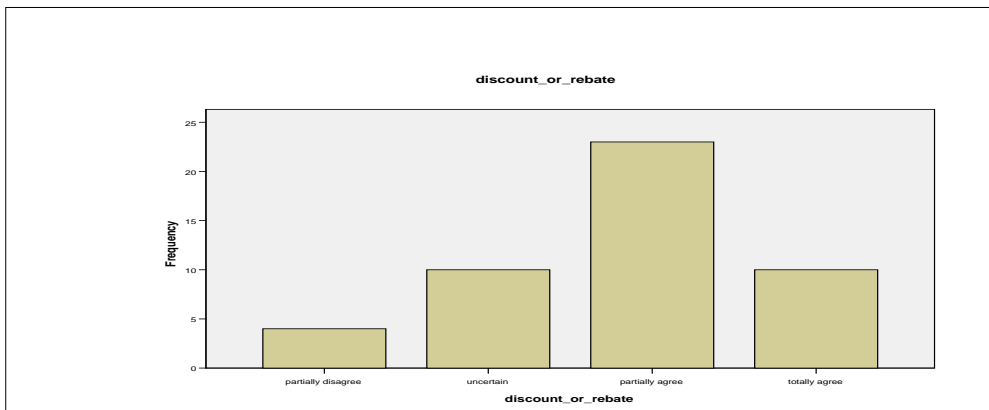


Figure 3: Discount or rebate
 (Source: Own Research, 2012)

As shown on the above figure, as many as 4 of the respondents partially disagreed that this factor affecting their choices of Islamic home financing. Meanwhile, 23 out of 47 respondents or 48.9% were partially agreed while the remainder of the respondents were both uncertain and totally agreed that this choice criterion was their main considerations before selecting any banks for Islamic home financing purposes.

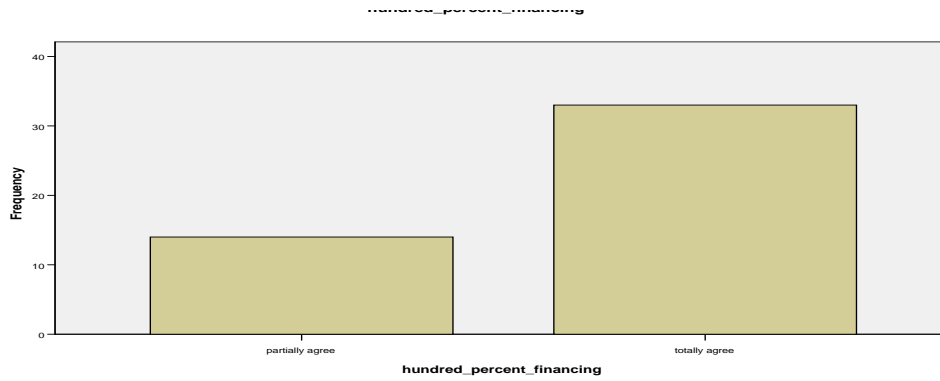


Figure 4: Hundred percent financing
 (Source: Own Research, 2012)

Figure 4 illustrates one of the important factors affecting the choice criteria for Islamic mortgage provider which was a hundred percent financing the lending bank. From the figure, it can be clearly seen that 33 of the respondents considered that a hundred percent financing from the lending bank is important in choosing the Islamic home mortgages while 14 of the respondents, however, were partially agreed on that factor.

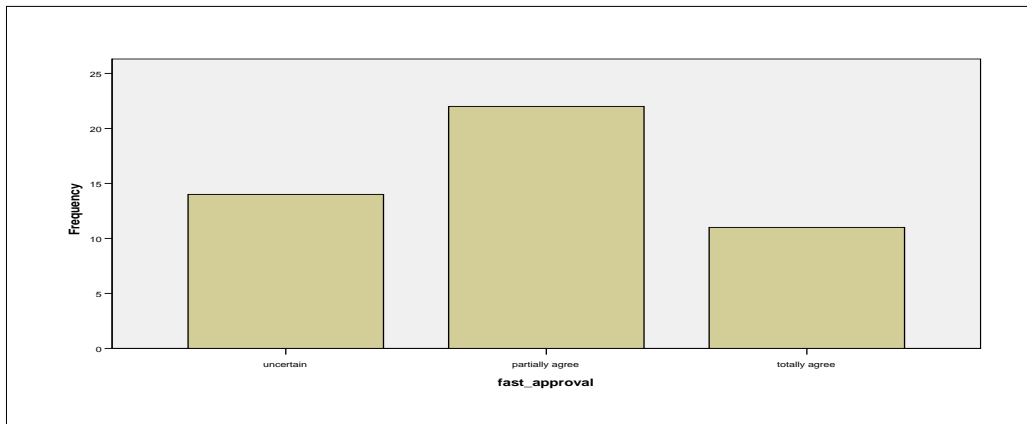


Figure 5: Fast approval
 (Source: Own Research, 2012)

Figure 5 shows that 22 of the respondents were partially agreed that fast approval is the main consideration criteria in choosing Islamic home financing product while 11 out of the 47 respondents were totally agreed on that factor and the remaining respondents were uncertain about this choice of criteria.

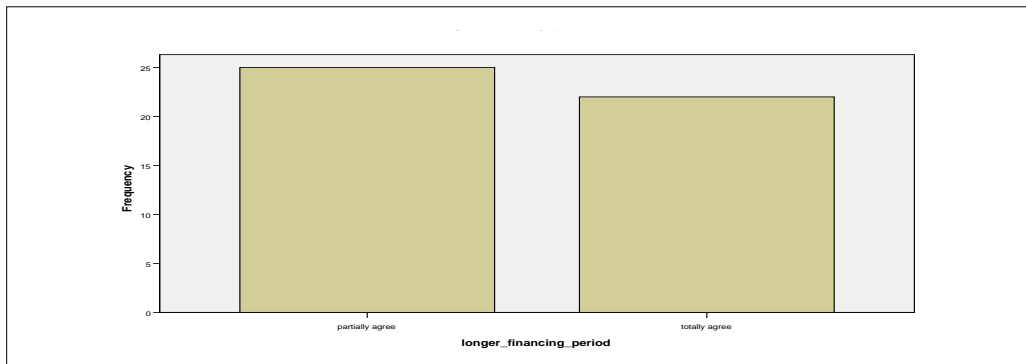


Figure 6: Longer Financing Period
 (Source: Own Research, 2012)

The study showed that majority of the respondents were partially agreed that longer financing period have major influence on their decision in choosing the Islamic home financing product. Nevertheless, 22 of the respondents involved in the survey were totally agreed on this particular choice criterion. No respondents were fall into strongly disagree, partially disagree and uncertain situations.

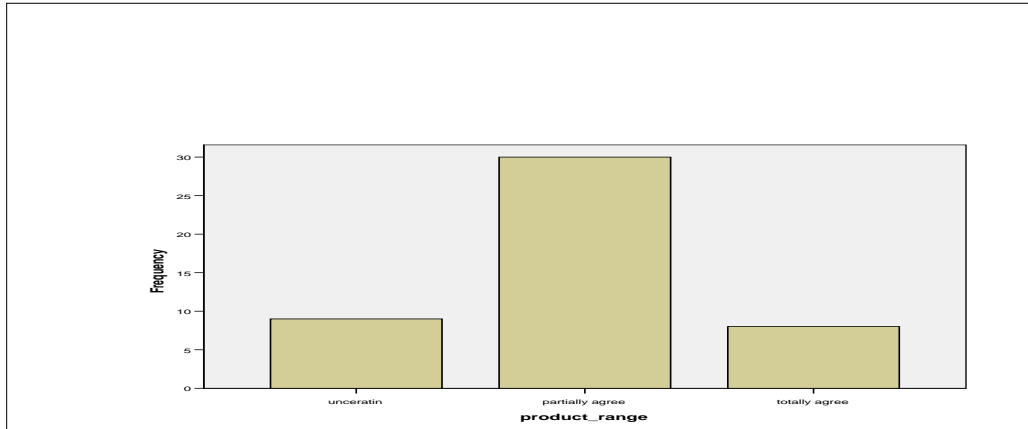


Figure 7: Product range
 (Source: Own Research, 2012)

Figure 7 show that product range in terms of the packages of the Islamic home financing had attracted the respondents' attentions. From the figure, 30 out of the 47 respondents were partially agreed that product range is one of the criteria that would influence them to choose an Islamic home financing. However, 8 of the respondents were totally agreed that this choice criteria are the main consideration in their decision to choose an Islamic home loans while the other 9 respondents were uncertain whether this choice criteria would have any effect or not in their decision making process.

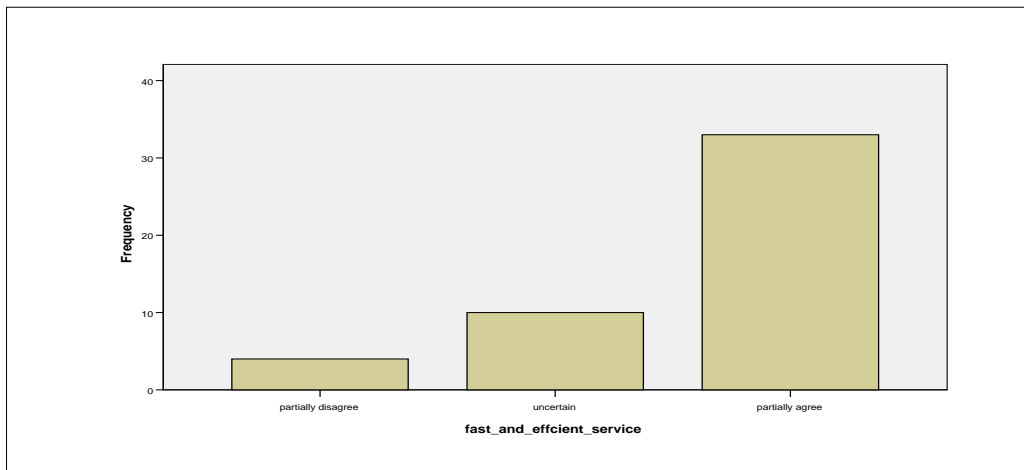


Figure 8: Fast and efficient service
 (Source: Own Research, 2012)

Figure 8 illustrates that one of the factors affecting the choice criteria for Islamic mortgage provider was fast and efficient service provided by the lending bank. Out of the total respondents, 4 of them were partially disagreed with the statement followed by 10 of the respondents were uncertain about it. Nevertheless, majority of the respondents were partially agreed that fast and efficient service is a crucial factor in selecting an Islamic home financing product

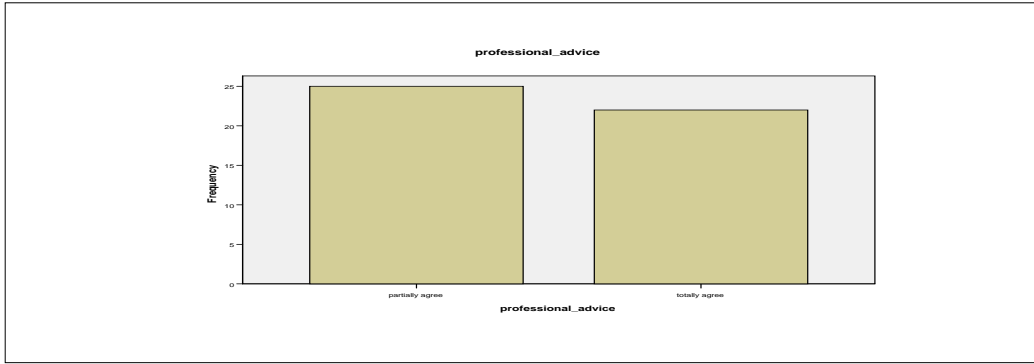


Figure 9: Professional advice
 (Source: Own Research, 2012)

From the figure shown above, as many as 25 respondents involved in the survey were partially agreed and were of the opinion that professional advice was considered as an important factor of choice criteria in choosing an Islamic home financing while 22 of the remaining respondents were totally agreed with the statement. Professional advice refers to suggestion or recommendation from the bank officers itself

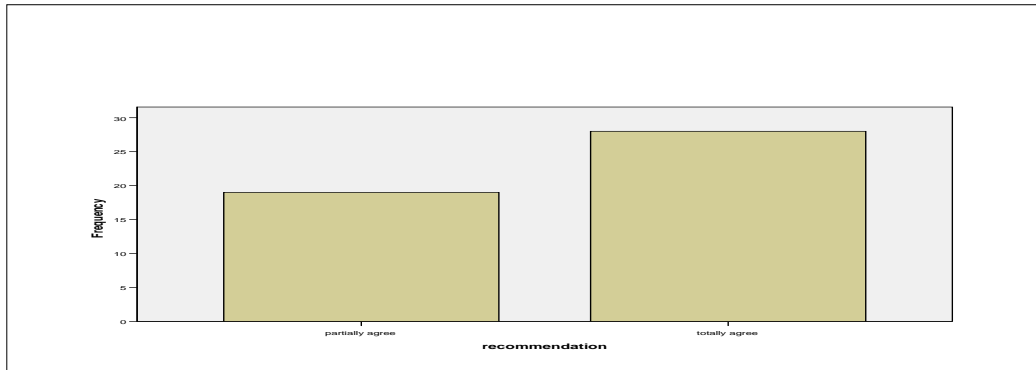


Figure 10: Recommendation
 (Source: Own Research, 2012)

The study showed that majority of the respondents were totally agreed that recommendation from the developers, friends, family members and housing exhibition have major influence on their decision in choosing the Islamic home financing product. Nevertheless, 19 of the respondents involved in the survey were partially agreed on this particular choice criterion. No respondents were fall into strongly disagree, partially disagree and uncertain situations for this above mentioned criteria.

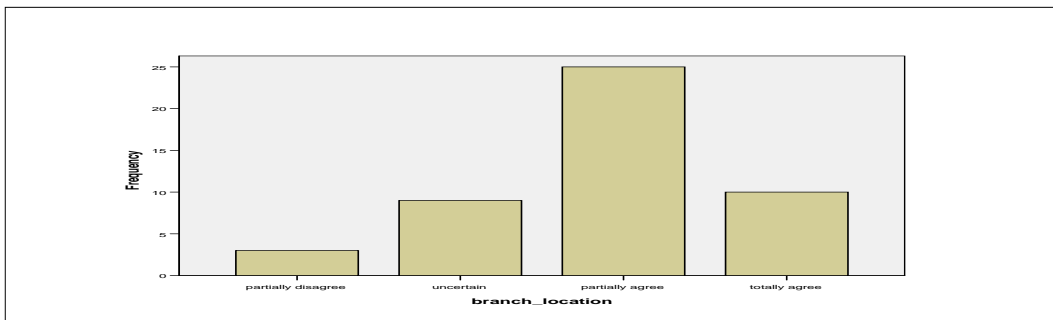


Figure 11: Branch Location
 (Source: Own Research, 2012)

As shown on the above figure, as many as 3 of the respondents partially disagreed that this factor affecting their choices of Islamic home financing. Meanwhile, 25 out of 47 respondents or 48.9% were partially agreed while the remaining respondents were both uncertain and totally agreed that this choice criterion was their main considerations before selecting any banks for Islamic home financing purposes.

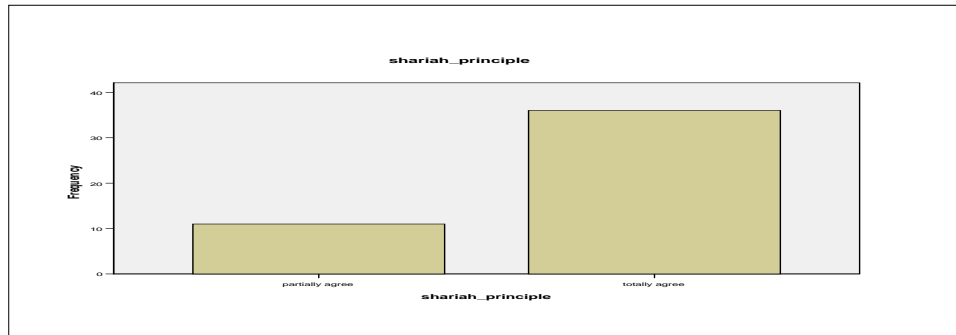


Figure 12: Shariah principle
 (Source: Own Research, 2012)

The above figure shows another important factor for bank customers in selecting the Islamic home financing product which is the Shariah principle practice by the lending bank. From the figure, it was noted that majority of the respondents with a number of 36 were totally agreed that Shariah principle practice by the lending bank would influence them in choosing an Islamic home financing product. Whilst, only 11 of the respondents were partially agreed on the statement and no respondents were fall on strongly disagree, partially disagree and uncertain condition for the mentioned criteria.

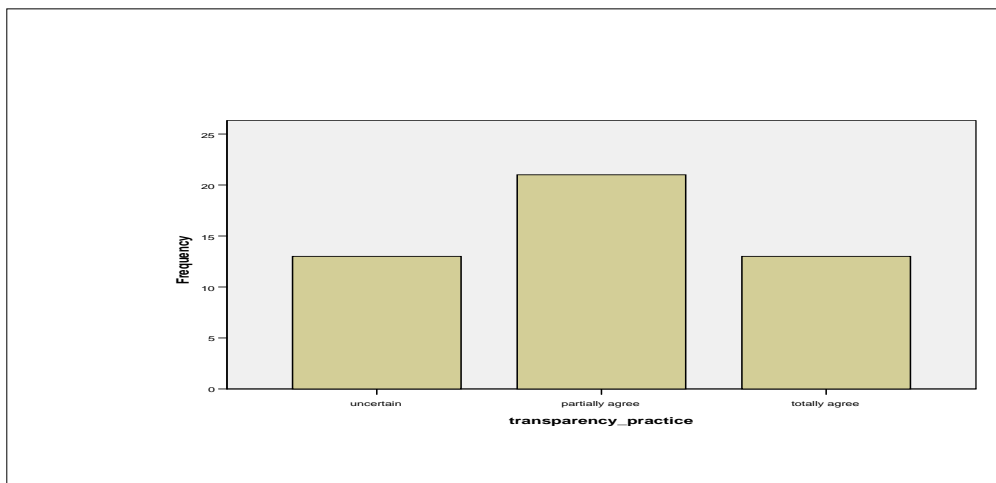


Figure 13: Transparency practice
 (Source: Own Research, 2012)

The studies showed that majority of the respondents were partially agreed that transparency practice have major influence on their decision in choosing the Islamic home financing product. Nevertheless, 13 of the respondents involved in the survey were totally agreed on this particular choice criterion and the other 13 respondents were uncertain for the above mentioned criteria.

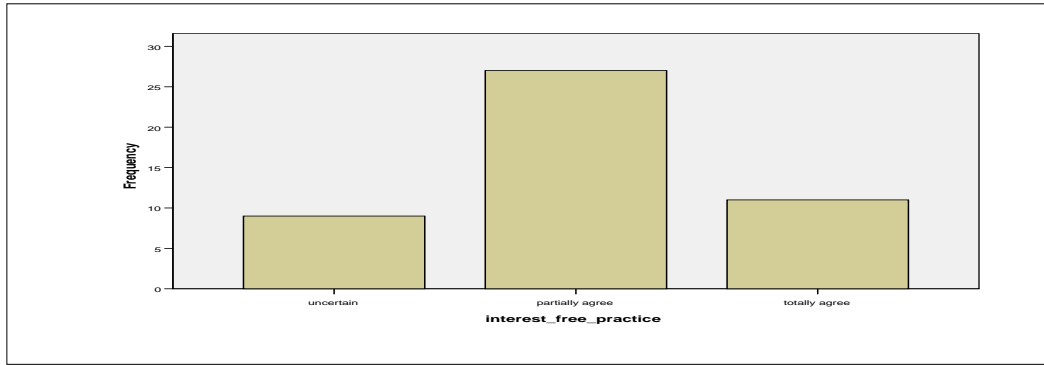


Figure 14 Interest free practices
 (Source: Own Research, 2012)

The above figure shows another important factor for bank customers in selecting the Islamic home financing product which is the interest free practice factor by the lending bank. From the figure, it was noted that majority of the respondents with a number of 27 were partially agreed that interest free practice by the lending bank would influence them in choosing an Islamic home financing product. Whilst, only 11 of the respondents were totally agreed on the statement and the remaining of 9 respondents were seemed to be uncertain about the subject.

Table 1: Ranking of Choice Criteria for Islamic home financing

Choice Criteria	N	Minimum	Maximum	Mean	Ranking
Shariah principle	47	4	5	4.77	1
100% financing	47	4	5	4.70	2
Lower monthly payment	47	4	5	4.60	3
Interest free practice	47	3	5	4.47	4
Longer financing period	47	3	5	4.32	5
Lower services charges	47	3	5	4.30	6
Professional advice	47	3	5	4.04	7
Product range	47	3	5	3.98	8
Fast approval	47	3	5	3.94	9
Branch Location	47	2	5	3.93	10
Discount or rebate	47	2	5	3.89	11
Fast and efficient service	47	2	5	3.83	12
Transparency practice	47	3	5	3.74	13
Recommendations	47	3	5	3.62	14

This part considers mean analysis of the choice criteria for the Islamic home financing. The mean score represents to what level do the choice criteria influenced the bank customers to choose Islamic home financing. Choice criteria with high mean score indicates the most important criteria in choosing Islamic home financing while the choice criteria with low mean score reflects to the least important factors affecting the bank customer's decision in selecting Islamic home financing.

As presented in the Table 1 above, the respondents believed that "Shariah Principle" is the main criteria with mean score 4.77 that influenced them to choose Islamic home financing and this is consistent to what Metawa and Almossawi (1998) had pointed out. According to them, the provisions of Shariah compliant products were highly regarded by majority customers while selecting banks for home financing. Criteria number 2 is "100% financing" seems Islamic home financing (BBA) run on the basis of deferred payment where the Malaysian customers will first receive a house and in terms of payment, they need to pay the installment from the beginning of the contract until the settlement. Criteria number 3 is "lower monthly payment". The concept of "lower monthly payment" is the price paid by customers to settle Islamic home financing facilities. In the real world, customers practically choose an Islamic mortgage provider on the basis of "lower monthly payment". "Interest free practice" was on ranking number

4 and criteria number 5 is “longer financing period” where the financing period offered by the Islamic bank up to 30 years.

As noted above, “Shariah principle” considers the important factors affecting a bank customer’s decision in selecting Islamic home financing, which is due to the fact that about 85 per cent of this study are Muslim. This result is consistent to what Dusuki and Abdullah (2007) found, who claimed that Islamic banks must show Islamic activities in their operations and at the same time the banks are able to provide quality services.

On the other hand, the least important choice criteria are “recommendations” with mean score 3.62, “transparency practice”, “fast and efficient service”, “discount or rebate” and “branch location”. The present study also supports the results of the study conducted by Devlin and Gerrard (2004), where the recommendations was be unrealistic choice criteria.

CONCLUSION

This research is an attempt to examined the issue of choice or selection criteria in the field of Islamic home financing offered by Bank Islam Malaysia Berhad (BIMB), case study at Kuala Lumpur. This research is based on collected data from 50 respondents among Islamic home financing customers offered by Bank Islam Malaysia Berhad which cover public workers, private worker and business person. Fourteen independent variables have been used that is lower service charges, lower monthly payment, discount or rebate, 100 per cent financing, fast approval, longer financing period, product range, fast and efficient service, professional advice, recommendation, branch location, Shariah principle, transparency practice and interest free practice. It was not little papers have been done in demined choice criteria for banking but not much in the matter of home financing selection criteria.

Overall the findings revealed that customers of Islamic home financing offered by Bank Islam Malaysia Berhad at Kuala Lumpur have generally positive views of selection factor. From an Islamic point of view, “Shariah principle”, “100% financing”, “lower monthly payment”, “interest free practice”, “longer financing period” are considered to be the first five choice criteria affecting a bank customer’s decision to choose a mortgage provider, notably an Islamic bank.

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