

Role of Religiosity, Rationality and Similarity Perception in Adoption of Islamic Banking: A Case of Pakistan

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Abstract

Some clients focus on the service quality, associated risk and the financial impact of the bank whereas other clients prefer to select the bank on the basis of their religiosity. The main objective of this study is to explore the reasons of the bank selection by the clients. This study also tries to explore the impact of the rationality and religiosity on the adoption of Islamic banks in the presence of the perception that both banks are similar. We applied mixed method approach. At first stage, in-depth interviews were conducted for the qualitative judgment of the problem and then quantitative approach was used by collecting data through questionnaires. Structural equation modeling was applied by using AMOS and SPSS. Results indicate that both religiosity and rationality have positive impact on selection of Islamic banks but, in the presence of rationality, religiosity is having insignificant influence. Perception about the similarity of both types of banks reduces the impact of religiosity on adoption of Islamic banks. However, this perception does not have any impact on the relationship of rationality with adoption of Islamic banks because the rational clients don't bother about the similarity of bank types.

Keywords: Rationality, Religiosity, Islamic Banking, Similarity Perception

Introduction

Islamic banking has achieved a remarkable growth over the last twenty years. It is even becoming a preferred choice of clients who have options of selecting conventional or Islamic banks when both the options are available. Islamic banks are providing their services in almost 75 countries of the world. Islamic banking has evolved from minimal level to a considerable market player. It has even become a strong competitor to the conventional banks in some countries¹. Islamic banks are not only providing Shariah compliant products for the fulfillment of the religious belief of the Muslim clients but they are also providing wide range of products and quality services to attract customers on competitive grounds². However, it is a critical issue to recognize the reason of acceptance of Islamic banks because bank selection is a financial decision which may be grounded on the rational reasons or the religious obligations.

Religiosity is spiritual need of individual and comes through education and experiences. Religiosity consists of beliefs and practices, prescribed by a certain religion, which show a person's responsibility and understanding towards other individuals and to the society as a whole. Religiosity is defined as "the extent to which an individual is

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¹ Saad, N. M. (2012), Comparative analysis of customer satisfaction on Islamic and conventional banks in Malaysia Asian Social Science, 8(1), pp.73-80

² Dusuki, A.W. and Abdullah, N.I. (2007), "Why do Malaysian customers patronize Islamic banks?" *International Journal of Bank Marketing*, Vol. 25 No. 3, pp.142-160

committed to the religion.” Religious obligations play critical role in the lives of people through shaping their beliefs and knowledge. Every religious group such as Muslims, Christians, Buddhist and others have different religious beliefs and orientations³.

Rationality of decision makers is one of the basic assumptions of economic theories. Rationality plays an important role in shaping the consumer behavior. Decision making is quite easy for a person, who is either fully committed to religious obligations or prefers rationality only. But economic decisions become difficult for the persons who want to achieve economic objectives in concurrence of religious obligations. So, it becomes imperative to investigate the real motive behind the economic decisions. This study focuses on exploring the impact of rationality or religiosity on the adoption of Islamic banks in Pakistan.

Literature Review:

Several studies conducted in different countries on bank selection criteria found religiosity as the primary factor that influences clients to adopt Islamic banking for the fulfillment of their religious obligations⁴. Rising adoption level of Islamic banking by the Muslim clients in Middle East, South East Asia and other parts of the world points out that religiosity is a driving factor that influences the selection decision of clients to choose Islamic bank instead of conventional bank⁵. Religious obligations are main reason for adoption of Islamic banks but the quality and attractiveness of offerings and potential of Islamic banking also influences on customer decision⁶. It is argued that religious thought process of clients is an influencing variable for Islamic bank customers but selection of traditional banks is independent of it⁷. Modern literature point out that quality of services, location of branches, accessibility of ATM's, efficient transaction procedure are specifically significant for adoption of conventional banks. It is also argued that religiosity factor plays a significant role in selection of Islamic banking by young generation. Islamic banks are adopted due to religious discernments, cost adequacy and efficiency quality services⁸.

A large number of studies found that people adopt Islamic banking because of the rationality factor instead of religious obligations. It is also pointed out by current researchers that service quality is the main factor in adoption of banks; clients give less

³ Rehman, Ateeq and Muhammad Shahbaz Shabbir. (2010). “The Relationship between Religiosity and new Product Adoption.” *Journal of Islamic Marketing* 1(1): pp.63–69

⁴ Osman, Ismah, Husniyati Ali, Anizah Zainuddin, Wan Edura Wan Rashid, and Kamaruzaman Jusoff. 2009. “Customers Satisfaction in Malaysian Islamic Banking.” *International Journal of Economics and Finance* 1(1): pp.197–202

⁵ Weill, L. & Godlewski, C. (2012). Why Do Large Firms Go For Islamic Loans? BOFIT Discussion Paper 2/1012. ISBN 978-952-462-738-2.10 April.

⁶ Nawi, Farah Amalina Md, Ahmad ShukriYazid, and Mustafa Omar Mohammed. 2013. “A Critical Literature Review for Islamic Banks Selection Criteria in Malaysia.” *International Business Research* 6(6): pp.143–51

⁷ Srouji, AnanFathi, MohdSuberi, AbHalim, ZulkarnainLubis, and MadherEbrahimHamdallah. 2015. “Determinants of Bank Selection Criteria’ S in Relation To Jordanian Islamic and Conventional Banks.” *International Journal of Economics, Commerce and Management United Kingdom* III (10): pp.294–306

⁸ Asdullah, M. A., & Yazdifar, H. (2016).Evaluation of factors influencing youth towards Islamic banking in Pakistan. *ICTAT Journal on Management Studies*, 2(1), pp.217-223

Role of Religiosity, Rationality and Similarity Perception in Adoption of Islamic Banking: A Case of Pakistan importance to religious commitments while choosing banks⁹. Current studies reveal that people are less aware about the Islamic banking as the Islamic banks are unable to provide information which gives them credibility under the Shariah compliant rules. It is also declared by some researchers that attraction in the banks are quality of services and facilities either it is Islamic or conventional banking. Currently, clients have more choices because of the expansion of banking sector. Therefore, they can easily switch their choice if not satisfied from the previous selection¹⁰. Customers choose the bank which gives them better quality services and facilities as compared to the competitors. Customers are more aware about their benefits and they adopt those banks which give them more profit. Customers do not choose bank on the basis of their religious believes¹¹. They give more preference to profitability rather than religious motivation. Contemporary literature argues that both Muslim and non-Muslim prefer factors including cost-benefit, convenience, service facility and influence of the companions instead of ethnic foundation and religion for the decision of adopting Islamic banks¹².

Recent research has uncovered substantial evidence that Islamic banks and their customers mimic their conventional counterparts. The coexistence of economic rationality and religious constraints makes Islamic bank customer an interesting case to explore the dominance of one of these two opposite forces: economic rationality and religious commitments. There are many studies which note that Islamic banking relies primarily on non-PLS models in practice. Islamic banks also, to the larger extent, don't use the profit and loss sharing models and operate like conventional banks. This aspect raises questions on the purity and Shariah compliance of Islamic banking¹³. The similarity between Islamic and conventional banking is also induced by the behavior of depositors. Especially, when banks are at risk of failure, Islamic bank depositors also behave like the conventional bank clients¹⁴. Based on the codification of Islamic principles, the reasonable expectation is that Islamic bank depositors are ready to share the losses of their banks during a downturn. However, concerns remain that Islamic depositors will be as responsive as their conventional counterparts to increased bank risk, and this in turn would lead to deposit withdrawals. It is expected that clients use to select the Islamic banks due to the religious or rational reasons but the selection of Islamic banks is affected by the perception of the clients when they think that Islamic banks are just like conventional banks and hence they don't think that it will be religiously useful to

⁹ Awan, H. M., Bukhari, K. S. (2011) Customer's criteria for selecting an Islamic bank: evidence from Pakistan. *Journal of Islamic Marketing*, 2(1), pp.14–27

¹⁰ Quresh, A. H., Hussain, Z., & Rehman, K. U., (2012). A comparison between Islamic banking and conventional banking sector in Pakistan. *Information Management and Business Review*, 4(4), pp.195-204

¹¹ Mansour, W., Abdelhamid, M. B., Masood, O., & Niazi, G. S. K. (2010). Islamic banking and customers' preferences: the case of the UK. *Qualitative Research in Financial Markets*, 2(3), pp.185-199

¹² Marimuthu, Maran, Chan Wai Jing, Lim PheiGie, Low PeyMun, and Tan Yew Ping. 2010. "Islamic Banking : Selection Criteria and Implications." *Global Journal of Human Social Science* 10(4): pp.52–62

¹³ Cokgezen, M. and Kuran, T. (2015). Between Consumer Demand and Islamic Law: The Evolution of Islamic Credit Cards in Turkey. *Journal of Comparative Economics*, 43(4): pp.862–882.

¹⁴ Ahmet F. Aysan, Mustafa Disli, Meryem Duygun, Huseyin Ozturk, and Religiosity versus Rationality: Depositor Behavior in Islamic and Conventional Banks, *Journal of Comparative Economics* (2017), doi: 10.1016/j.jce.2017.03.001

go for Islamic bank. The current study is an attempt to examine what matters most in adoption of Islamic banks religiosity or rationality and how perception about the similarity perception of Islamic and conventional banks plays role in adoption of Islamic bank.

Figure A1 shows that religiosity and rationality determine the selection of banks. Rationality is specified in terms of variables like financial benefits, risk associated, services and facilities. Previous studies pointed out the impact of rationality or religiosity on the adoption of Islamic banks. Main contribution of this study is to introduce a new construct similarity perception as moderator to strengthen or weaken the relationship of rationality and religiosity on adoption of Islamic banks. It is expected that the impact of religiosity on the selection of Islamic banks will be reduced if the clients consider the similarity in Islamic and conventional banks. Similarly, the impact of rationality on the bank selection will be influenced by the similarity perception. The construct similarity perception is proposed as a result of the preliminary investigation by interviews with the current and potential clients of Islamic banks.

Methodology:

Mixed method of qualitative and quantitative approach is used in this study. It consists of exploratory study using interviews of the stake holders and then the questionnaire based quantitative survey. During the preliminary stage of discussion with few stake holders, we found that most of them consider Islamic and conventional banks as identical. Therefore, we conducted 20 in depth interviews to explore the perception of people about Islamic and conventional banks.

For the quantitative approach of questionnaire based survey, convenient sampling technique is used due to large population size. Our targeted respondents were clients of banks (Islamic, conventional) and general public (students, teachers) from Multan and other cities of South Punjab. Our total sample size is 350 questionnaires. The questionnaires were distributed to the target respondents. From 350 questionnaires, 330 responses were received and after initial screening, the valid responses left to 320.

Data Collection Tool:

Questionnaire is adapted from multiple previously used tools. For the rationality construct we borrowed items from the Servqual instrument of Parasuraman, Zeithaml and Berry (1988). Religiosity and adoption of Islamic bank constructs are used from the study of Ahmad *et al.* (2008). All the constructs are based on five point Likert Scale. SPSS and AMOS 20 are used for simultaneous equation estimations.

Results:

In the in depth interviews of current and potential clients of Islamic banks, about 70% of them were of the view that Islamic and conventional banks are doing the same business and both are almost similar in the financial operations. Respondents pointed out that the cost of financing is almost same for both types. Even, in some cases Islamic banks use to charge higher cost on the financing. Similarly, both types pay almost similar returns on the deposits. However, some of the clients who were familiar to the Islamic modes of financing have the vision that there was a clear difference in the both types and they believed that Islamic banks were providing Riba free and Shariah compliant modes of solutions to the financial problems.

In the second stage, during the quantitative approach, from a total of 350 questionnaires 320 questionnaires were found to be valid for analysis. Table A2 summarizes the descriptive statistics which shows that rationality financial variable has the highest mean value of 3.97 which indicates that people have tendency towards rationality. Second highest mean value is religiosity which is 3.60 that shows people adopt Islamic banks for fulfillment of their religious obligations. Table A3 shows the reliability result of skewness and kurtosis. Skewness value is within the range of -1 and +1 and kurtosis value of all variables is within the range of -4 to +4 showing the normality and reliability of data. Table A4 shows the cronbach's alpha values between 0.8 and 0.95 confirming that the variables are highly reliable. Table A5 shows the Pearson correlation. There is no indication of multicollinearity.

Relationship between Religiosity and Adoption:

Through path analysis, relationship of religiosity and adoption is determined. Results of Table A6 show that religiosity has significant impact on adoption. Due to the religiosity factor, people are adopting Islamic banking.

Relationship between Religiosity and Adoption in presence of Rationality:

Table A7 shows that all variables of rationality (service, risk, and financial) have significant impact on adoption which indicate that people select bank on the basis of rationality and it is the important selection criteria for adoption of banks. Religiosity has negative relationship with adoption in the presence of rationality having coefficient value of -.062.

Relationship between Similarity Perception and Adoption:

Table A8 shows that similarity perception has negative or reverse relationship with adoption having -.089 beta value which means that people do not adopt Islamic bank due to similarity perception. When they perceive that the Islamic and conventional banks are same, the chances of adopting the Islamic banks decrease.

Relationship between Religiosity and Adoption with moderating effect of Similarity perception:

Table A9 shows that religiosity has significant impact on adoption when interact with less similarity perception and religiosity has negative impact on adoption when interact with more similarity perception. Figure A2 shows that religiosity has significant relationship with adoption. When religiosity level is high and there is more similarity perception then adoption of Islamic banking will be low. When religiosity level is high and there is less similarity perception then adoption of Islamic banking will be high.

Relationship between Rationality and Adoption with moderating effect of Similarity Perception:

Table A10 shows that when rationality factor interact with similarity perception, it has insignificant impact on adoption having beta value of -.196 and probability value of .301 which means there is no relationship.

Discussion:

What matters most in adoption of Islamic banking: Religiosity or financial rationality?

The purpose of this study is to identify the role of religiosity and rationality in adoption of Islamic banking in Pakistan in presence of moderating effect of similarity perception. Previous studies conducted on religiosity and rationality in adoption of Islamic banks reveal that customers of banks choose Islamic banks because of their

religious believes However, many studies concluded that rationality is more significant in adoption of Islamic banks and who argue that both Muslims and non-Muslims prefer rationality factors in adopting Islamic banks and religiosity don't generally affect their choices¹⁵. Our study results indicate that religiosity has significant impact on adoption of Islamic banking because of the religious belief of people. For the fulfillment of their religious obligation, people will adopt Islamic banking. Religiosity factor is the main factor in selection of Islamic banks. This factor was also confirmed during exploratory study. Rationality variables like service and facility, risk associated, and financial impact have significant value which shows that rationality is an important criterion for bank selection and this was also confirmed during in-depth interviews. Rationality is stronger determinant of bank selection therefore religiosity becomes insignificant in the presence of rationality.

How Perception about the Similarity of Islamic and Conventional Banks plays role in adoption of Islamic banks?

Islamic bank depositors withdraw their money during the crisis time of Islamic banks which indicate their behavior similar to conventional bank clients¹⁶. During the preliminary stage of discussion with few stake holders, we found that most of them consider Islamic and conventional banks as identical. Therefore, we conducted 20 in-depth interviews to explore the perception of people about Islamic and conventional banks. Results of our study identified that common people do not have clear understanding about Islamic banking. Many people considered that Islamic and conventional banking are same. They were not able to clearly differentiate between both banking modes. Adoption of Islamic banks is reduced when people have the perception that it is similar to conventional bank. Similarity perception has beta value of -.089 with .042 probability value which indicates similarity perception has reverse relationship with adoption of Islamic bank. If people consider Islamic banking is just like conventional banking, then they will not adopt Islamic banks.

Influence of Religiosity and Rationality in Adoption of Islamic Banking: Moderating Role of Similarity Perception:

Our study results reveal that there is a moderating impact of similarity perception on the religiosity-adoption relationship. There exists high adoption of Islamic banks in more religious people when they perceive lesser similarity in Islamic and conventional banks whereas there is low adoption of Islamic banks by more religious people when the similarity perception is high. There is no moderating role of similarity perception on adoption with reference to rationality which implies that if clients consider the rationality as selection criteria then similarity perception does not play any role. Such result was also confirmed during qualitative study that rational client do not bother about the Shariah compliance. When rationality interacts with similarity perception, it has beta value of -.196 and probability value is .301 which indicates no relationship between rationality and similarity perception. Rational clients do not bother to think about the similarity perception. They will adopt banks on the basis of benefits.

¹⁵ Khayruzzaman. 2016. "Impact of Religiosity on Buying Behavior of Financial Products: A Literature Review." *International Journal of Finance and Banking Research* 2(1): pp.18–23

¹⁶ Ahmet F. Aysan, Mustafa Disli, Meryem Duygun, Huseyin Ozturk, and Religiosity versus Rationality: Depositor Behavior in Islamic and Conventional Banks, *Journal of Comparative Economics* (2017), doi: 10.1016/j.jce.2017.03.001.

Implications of the study:

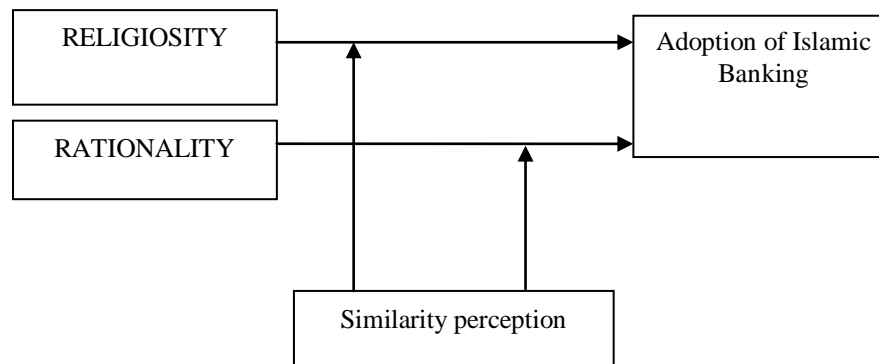
Policy makers of Islamic bank may find this study useful while making policies to attract their clients. This study will help the client of Islamic banking and conventional banking for bank selection criteria. Moreover it discloses the perception of people regarding Islamic banking which may give guideline to Shariah committee of Islamic banks for making rules and principles of Islamic banking.

Conclusion:

This study investigates the role of religiosity and rationality in adoption of Islamic banking in Pakistan in presence of moderating effect of similarity perception. Results of the study show that religiosity plays a significant role in adoption of Islamic banking which support the previous studies on adoption criteria of Islamic banking¹⁷ This study also reveal that rationality is the important determinant of bank selection. Therefore, religiosity has insignificant relationship with adoption of Islamic banking in presence of rationality. Customers are more attracted towards the financial benefits. They are more rational in selecting the banks. Islamic banks should provide the competitive benefits to attract more clients as the rationality is more important element of bank selection. Our study concluded that there is inverse relationship of similarity perception and adoption of Islamic bank. People will not adopt Islamic banking when they consider it similar to conventional banking. Moreover, there is moderating role of similarity perception on adoption when interacted with religiosity and there is no moderating role of similarity perception on adoption when interacted with rationality which indicates there exists no relationship of rationality with adoption of Islamic banking in presence of moderating role of similarity perception. Study results reveal that common people do not have much understanding regarding the Islamic banking. They consider it similar to conventional banking. Awareness should be provided to clients regarding the Islamic banking rules and procedure. Seminars should be conducted to clear the perspective of people. Moreover, Islamic banks should focus on advertising their products and services to make the clear differentiation between Islamic and conventional products and services.

Tables and Figures

Figure A1



¹⁷ Khan, F. (2010) How “Islamic” is Islamic Banking? Journal of Economic Behavior and Organization, 76, pp.805–820

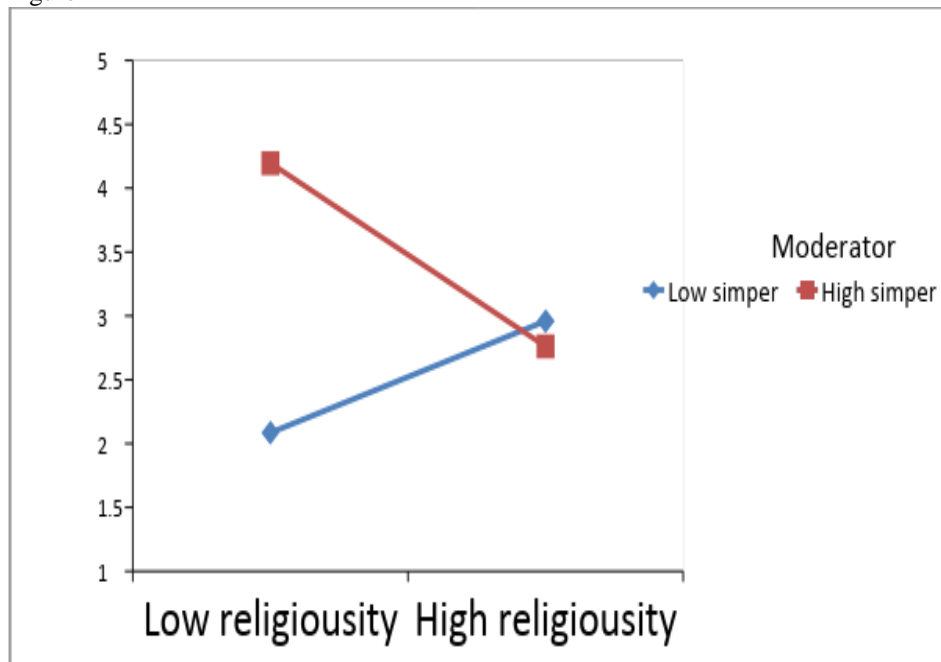


Table A2

variables	Number	Minimum	Maximum	Mean	Std (standard Deviation)	Variance
Religiosity	320	1.19	4.46	3.6072	.56720	.322
Rationality	320	.93	3.14	2.3049	.34764	.121
Similarity per	320	.91	3.12	2.3291	.38483	.148
Service	320	1.07	3.70	2.7094	.42989	.185
Risk	320	1.26	4.25	3.0503	.49577	.246
Financial	320	1.55	5.64	3.9744	.68020	.463

Table A3

Variables	Skewness	Kurtosis
Rationality	-.221	.243
Adoption	-.653	-.082
Similarity Perception	-.275	.199
Religiosity	-.912	.964
Service	-.246	.217
Risk	-.301	.605
Financial	-.238	.058

Table A4

variable	No of item	Cronbach's Alpha
Religiosity	5	.781
financial	5	.723
Risk	6	.652
Service facility	6	.754
Similarity perception	13	.840

Table A6

Model summary			Estimate	P
Adoption	<--	Religiosity	.377	**

Table A7

Model summary			Estimate	P
Adoption	<---	Service	.395	.004
Adoption	<---	Risk	.369	.011
Adoption	<---	Financial	.395	***
Adoption	<---	Religiosity	-.062	.324

Table A8

Variables			Estimate	P
Adoption	<--	Religiosity	-.176	.02
Adoption	<---	Rationality	1.723	***
Adoption	<---	Zsimp	-.089	.042

Table A9

Variables			Estimate	S.E.	C.R.	P
Adoption	<---	Religiosity	-1.422	.266	5.339	**
Adoption	<---	Zsimp	.386	.092	4.210	**
Adoption	<---	Relx_simp	.577	.121	4.761	**

Table A10

Variables			Estimate	S.E.	C.R.	P
Adoption	<---	Rationality	1.602	.500	3.205	.001
Adoption	<---	Zsimp	.386	.092	4.210	***
Adoption	<---	Rati_x_Sim	-.196	.190	-1.035	.301