

**FACTORS AFFECTING THE CHOICE OF ISLAMIC BANKING AMONG
MUSLIMS IN KENYA: A SURVEY OF SELECTED MUSLIMS IN NAIROBI**

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**A RESEARCH PROJECT REPORT SUBMITTED TO THE SCHOOL OF
HUMAN RESOURCE DEVELOPMENT IN PARTIAL FULFILLMENT OF
THE REQUIREMENTS FOR THE AWARD OF THE DEGREE OF
EXECUTIVE MASTERS IN BUSINESS ADMINISTRATION OF JOMO
KENYATTA UNIVERSITY OF AGRICULTURE AND TECHNOLOGY**

MAY 2012

DECLARATION

This Research Project Report is my original work and has not been submitted for any award in any other university.

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ACKNOWLEDGEMENT

I thank Allah (A.M) for the grace and blessings He has bestowed on me and made it possible to accomplish this work.

Secondly, I wish to acknowledge the constructive criticism of all at each step along the way, and I am grateful to my dedicated supervisors Dr. Ombuki and Mr. John M. Kabiru for their time and expertise. Also, I would like to thank the following individuals for their tremendous support and encouragement: Ali Mohamed of Q-Invest, Qatar and Sheikh Badru Jaffar of Majlis Al Ulamaa, Kenya.

I also wish to acknowledge all the writers and scholars whose literature was my reference and guide, and the lecturers whose ideas have changed my view of the business world.

DEDICATIONS

This work is dedicated to my mother, Juliana, my wife, Amina Abdulqadir and my lovely daughter Rawhiya Al Najar, their love is wonderful. Also, to the twenty-six letters of the alphabet, especially the letters A, B, and C, this taught me a great deal!

ABSTRACT

The emergence of strong Islamic movements in last three decades has generated a renewed interest in Islamic economics, especially in Islamic interest free banking. Currently, Islamic banks are strategically offering high quality products and services to satisfy their customers due to the strong competition, customer expectation for high quality services and rapid changes in technology. The purpose of this study was to investigate the factors affecting the choice of an Islamic banking among Muslims in Nairobi. The study hoped to establish whether the cost of services, conformity of the bank products to Islamic ethics, the customer delivery process and service availability are these influencing factors. Primary data for the study were collected using self administered questionnaires from Islamic bank customers in Nairobi with purposive sampling technique since respondents had to be Muslims and Islamic banking customers. Analysis done based on 82.5% response rate realised comprised of 75.6% males and 24.4% females. Respondents were grouped to fully-fledged Islamic bank customers who were 54.6% of the sample and conventional bank customers, 45.4% of the sample. Descriptive analysis using SPSS Version 14.0 gave the following results. 56% of fully-fledged Islamic bank customers agreed that cost of the bank influenced their choice with 47% of conventional bank patrons agreeing cost was a factor. Religiosity of Muslim bank patrons was clear with 72% agreeing conformity was paramount in choosing banking with fully-fledged Islamic banks while 47% of conventional bank patrons admitted conformity was important. Customers of both Islamic banks and conventional banks value customer service delivery, 61% and 60% respectively agreed to this. Conventional bank customers agreed availability of services was important in their choice of a bank, with 73% agreeing, while a meagre 33% of fully-fledged Islamic bank customers saw availability of services as important in their choice of bank. Conformity of bank services to Islamic finance ethics and service delivery process appears to have passed through a peak in terms of its influence on choice in the fully-fledged Islamic banks, a wakeup call to the stakeholders of Islamic finance industry. Synchronization of services with other institutions widening availability of services is a must for fully-fledged Islamic banks if they are to continue growing. The area of factors influencing customers on Islamic bank selection needs further research work to validate the findings with larger sample size and findings will help banks to make proper decisions on bank service design to attract more customers of Muslim faith.

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DEFINITION OF TERMS

Fiqh

Islamic jurisprudence, the source of a range of laws in different topics that govern the lives of the Muslims in all facets of everyday life.

Hajj

The annual pilgrimage to Mecca, Saudi Arabia

Ijarah

A contract under which an Islamic bank provides equipment, building, or other assets to the client against an agreed rental together with a unilateral undertaking by the bank or the client that at the end of the lease period, the ownership in the asset would be transferred to the lessee.

Gharar

Islamic finance term describing a risky or hazardous sale, where details concerning the sale of an item are unknown or uncertain. Gharar is forbidden by the Quran, which explicitly forbids trades that are considered to have excessive risk due to uncertainty.

Mudarabah

Special kind of partnership where one partner gives money to another for investing it in a commercial enterprise. The investment comes from the first partner while the management and work is an exclusive responsibility of the other.

Murabaha

A particular kind of sale, compliant with Sharia, where the seller expressly mentions the cost incurred on the commodities to be sold and sells it to another party by adding some profit or mark-up thereon which is known to the buyer.

Musharakah

Joint venture with capital, an arrangement between two or more partners, whereby each partner provides funds to be used in a venture, resulting profits and losses are shared between according to the invested capital

Riba

An addition to, or an increase of, a thing over and above its original size or amount. In Islam, the term riba signifies an unlawful and forced addition to the payback value of money or goods lent from one party to another.

Salam

A contract in which an advance payment, the seller undertakes to supply some specific goods to the buyer at a future date in exchange of an advance price fully paid at the time of contract.

Sharia

It is used to refer both to the Islamic system of law and the totality of the Islamic way of life. Sharia deals with many things, including politics, economics, banking, business, contracts, family, sexuality, hygiene and social issues among others.

Takaful

An alternative form of cover that a Muslim can avail himself against the risk of loss due to misfortunes. It is based on the idea that what is uncertain with respect to an individual may cease to be uncertain with respect to a very large number of similar individuals.

Sukuk

A financial certificate but can be seen as an Islamic equivalent of bond i.e. are securities that comply with the Islamic law and its investment principles.

Wadiah

Bank is deemed as a keeper and trustee of funds. A party deposits funds in the bank and the bank guarantees refund of the entire amount of the deposit, or any part of the outstanding amount, when the depositor demands it.

ABBREVIATIONS

A.M	All Mighty
AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
PBUH	Peace Be Upon Him
SSB	Sharia Supervisory Board

CHAPTER ONE

1.0 INTRODUCTION

Chapter one contains the background information of the research where Islamic banking is defined and its main differences from the conventional banking outlined. In the chapter too, a brief history of Islamic banking is given, highlighting its existence first as an idea and later how the Islamic institutions currently known globally and nationally came into being.

1.1. Background Information

Islamic banking refers to a system of banking which is consistent with Islamic law and guided by Islamic economics. In particular, Islamic law prohibits the collection of interest, also commonly called *riba* in Islamic discourse. One form of the argument against interest is that money is not a good and profit should be earned on goods and services only; not on control of money itself. Therefore, Islamic banking differs from conventional banking in several ways, such as the prohibition of transactions based on interest rate and the requirement that bank's operations be carried out according to certain procedures through the use of certain financial instruments (AbdulQawi and Lynn, 2001). However, the Islamic bank can also offer products and services which are similar to those offered by a conventional bank. AbdulQawi and Lynn go on to generally define the Islamic bank as a non-interest based financial institution which complies fully with Islamic laws and has creative and progressive financial engineering to offer efficient and competitive banking, investment, trade finance, commercial and real estate financing service.

1.1.1. A brief history of Islamic Banking

The history of interest-free banking can be divided into two parts according to the literature available. First, when it still remained an idea; second, when it became a reality by private initiative in some countries and by law in others. Abdulghafoor (1995), observed that the earliest references to the reorganization of banking on the basis of profit sharing rather than interest are found in literatures of early 1940s through 1950s to late 1960s and that these writings have all recognized the need for commercial

banks and the evil of interest in that enterprise, and emphasized on profit and loss sharing.

The first attempt at modern Islamic banking, which occurred in Pakistan during the 1950s, was unsuccessful. In the 1960s, however, a small number of banks formed to offer limited Islamic banking products. These banks succeeded and became the model for subsequent efforts. Prominent among these first banks were the Perbadanan Wang Simpanan Bakal-Bakal Haji (PWSBH) in Malaysia and the Mit Ghamr Savings Bank in Egypt. PWSBH still exists as Lembaga Tajung Haji and provides financing for religious pilgrimage to Mecca; the savings bank established in 1963 at Mit-Ghamr in Egypt was very popular and prospered initially and then closed down for various reasons. However this experiment led to the creation of the Nasser Social Bank in 1972 whose objectives were more social than commercial. (Rad, 1991)

In 1970s and the decades after, interest-free banking attracted more attention, partly because of the political interest it created in Pakistan and partly because of the emergence of young Muslim economists. Early 70s saw the institutional involvement in the Conference of the Finance Ministers of the Islamic Countries held in Karachi in 1970, the Egyptian study in 1972, First International Conference on Islamic Economics in Mecca in 1976, International Economic Conference in London in 1977 were the result of such involvement. The involvement of institutions and governments led to the application of theory to practice and resulted in the establishment of the first interest-free banks. The Islamic Development Bank, an inter-governmental bank established in 1975, was born of this process.

In the latter half of the 1970s, a number of Islamic banks were formed that became highly successful, among them Dubai Islamic Bank, Kuwait Finance House, and First Gulf Bank (UAE). In contrast to the earlier Islamic banking efforts, these banks offered a robust product set of *Sharia* compliant products. Abdulghafoor noted that the success of these early Islamic banks and increasing wealth among Muslims led Egypt's Bank Misr to create an Islamic subsidiary in 1979. This practice was followed by an

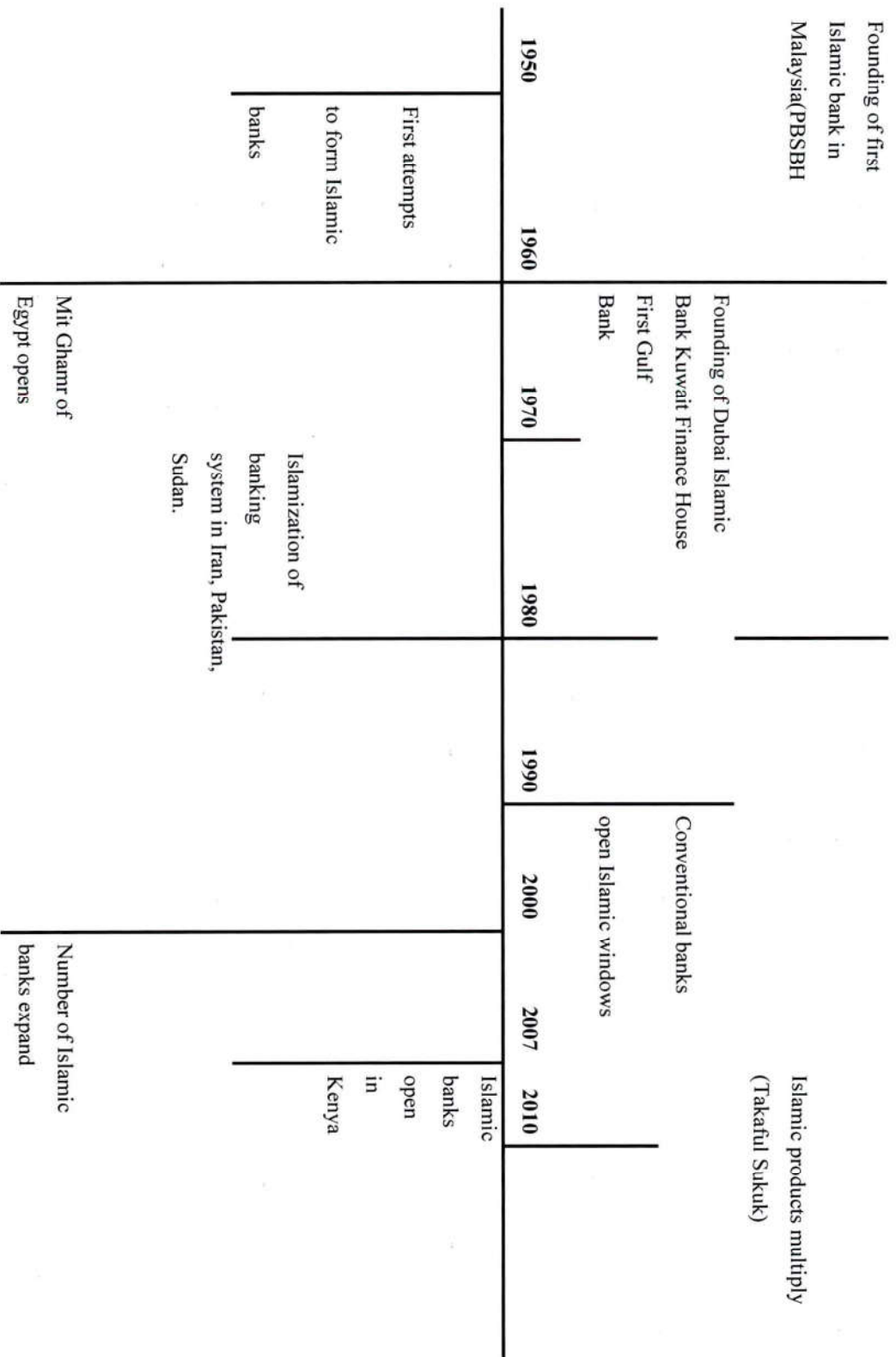
estimated 50 banks in the next five years. At the end of the 1970s, Islamic banking gained momentum as the Pakistani government began conversion of the nation's banking system to Islamic banking. Sudan and Iran followed suit in the early 1980s. Later in the decade, prominent conventional banks such as Al Rahji Bank and National Commercial Bank, both in Saudi Arabia, began offering *Sharia* compliant products. Global banks, including HSBC, Citibank, and JP Morgan Chase, began offering Islamic products during the last two decades of the 20th century.

The growth in Islamic banking has been facilitated by the development of Islamic accounting standards and policies. The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), founded in 1991, provides guidelines for accounting policies and processes. Similarly, the Islamic Financial Services Board, formed in 2002, addresses risk and compliance issues for Islamic banking. These organizations have helped ensure the soundness of Islamic banking and provide guidelines for core vendors in developing the accounting software for Islamic banking products.

As of 2000, an estimated 200 financial services institutions worldwide offered Islamic banking products and collectively held nearly \$160 billion (USD) in assets and the number of institutions offering Islamic products has grown to more than 250, and their holdings now represent an estimated \$750 billion in Islamic assets (Hunt 2007). Hunt estimates that \$350 billion of this amount is held by fully Islamic institutions and the remaining \$400 billion by conventional banks that offer Islamic banking services.

According to an IMF study reported in the MENAFN - Arab News, the institutions that were least affected by the global financial crisis were Islamic banks because they engage mainly in asset-based financing, and that the Islamic banking and finance, had a total asset of \$1.4 Trillion and more than 1,000 institutions operating in many countries worldwide.

Fig. 1.1: A timeline for Islamic Banking, (1950 – 2010)



Source: Author

1.1.2. A brief description of Islamic Banking Products

The idea of participatory financing introduced by the Islamic banking movement is a unique and positive contribution to modern banking. Islamic finance operates by profit and loss sharing (PLS) mode. These principles focus on the necessity of sharing risk in a fair and stable society, and therefore Islamic banking products are coined on this fundamental principle.

Table 1.1: Features of commonly offered Islamic Banking Products

Deposit products	Concept	Features
Wadiah	Safekeeping	No specific return on funds; banks may periodically distribute returns.
Mudaraba	Pooled or directed investment with profit sharing	Funds are comingled for banks general use. Profits are shared between the bank and the customers and losses are borne by the customers
Financing products	Ownership	Features
Murabaha	Customer	Customer and bank agree to bank's profit amount prior to closing. Typically fixed payment amount that includes bank's profits
Ijara	Financier	Rent-to-own financing. Payments are based on the amount financed plus viable rent amount.
Musharaka	Shared	Joint ownership with profit and loss sharing based on percentage of ownership. Payments change periodically based on the share of ownership.
Hajj	Not applicable	Financing of and individual pilgrimage to Makkah. Repayment may use multiple payments or a single payment.
Istina	Financier	Financing for future delivery of manufactured goods at a fixed price that includes a profit for the bank.
Salam	Financier	Financing for future delivery with amount fully paid at contract signing, typically used for agriculture.

Source: Author

1.1.3. Developments of Islamic banking in Kenya

Muslims in Kenya are estimated to be as much as 9 million inhabitants, which is nearly 25% of the country's total population (Makau, 2008). The significance of this Muslim population as the target market of Islamic banks in Kenya cannot be underestimated and especially for the growth and development of the banking sector and the realization of Vision 2030. Their continuous support is prelude to ensure the success of the Islamic banking system.

The licensing of the banks by the Kenyan Treasury and the Central bank of Kenya (CBK) is the result of the 2006 amendments to the Banking Act, allowing banks to widen their products and services. It should be noted that the leading conventional banks had already taken advantage of the amendments to introduce Islamic banking products. In 2006, Barclays Bank of Kenya introduced 'La *Riba* account', a current account to specifically address the needs of the Muslim community (Omar, 2009). Some of the specifications that come with the service include interest-free loans. In 2007 the two fully *Sharia* compliant banks namely Gulf African Bank and First Community Bank started operations, with the former being the first to roll out its services. National Bank of Kenya-*Al-Muumin* account in 2008 was the last to be instituted.

During the year 2007, the Kenya's banking sector had 143 institutions comprising of 43 commercial banks (Economic Survey, 2008). Over the same period, 2 commercial banks that were to operate on Islamic banking principle were approved. The Economic Survey also noted that the number of bank branches had risen by 44.5% from 512 in 2003 to 740 by the end of 2007 and that that financial sector had registered a real growth of 6.5% in 2007 compared to 5.5% in 2006. Omar 2009 observed that Islamic banking appears to have caught root and were growing in terms of the increase of number of branch offices, sub-branch offices, ATMs, assets, and of course customers.

Omondi (2008) found that according to the financial access study launched in January 2006, 38% of Kenyans did not have access to any form of financial services or products, an anomaly that the government seeks to address in its 2030 economic blue

print. Even among those with ready access to banking services, some still opt to keep money away from the mainstream banking. The most common business amongst the Muslims is the Hawalla business i.e. transfers of funds both locally and internationally (Omar, 2009).

1.2 The Statement of the Problem

Islamic Banking is currently one of the fastest growing sectors in international finance and Kenya has emerged as a proponent of Islamic finance with the rapid establishment and acceptance of Islamic Banking in the country. The popularity of the Islamic banking system is not limited to the Islamic banks only. Central Bank of Kenya had anticipated that the licensing of the two Islamic banks and four other conventional banks to offer Islamic products was to propel Kenya into a premier financial services hub in the region, with a wide range of competitive products.

The consequence of this is that Islamic banks operating in Kenya are faced with strong competition not only from Islamic banks but also from conventional banks with Islamic banking windows. When competition intensifies and when banks start to offer more or less similar products and services, it is the customer's satisfaction that can influence the performance of an Islamic bank and determines its competitiveness and success.

In buyers' markets, customers can choose from a wide array of goods and services. In these markets, if sellers fail to deliver acceptable product and service quality, they will quickly lose customers to competitors because consumers buy from the firm that they believe offers the highest customer delivered value. In a competitive marketplace where businesses compete for customers, customer satisfaction is seen as a key differentiator. In Islamic finance value and quality is expressed in terms of the presence of the key features. These are avoidance of interest and risk, asset backed finance, money as a medium of exchange and not tool of trade, the *Sharia* board, transparency in transactions, profit and loss sharing among others.

The practices of the banks offering Islamic banking products have evoked questions of morality and quality among Muslims in Kenya because some banks offered these

banking products do not even have Sharia advisory boards, a vital requirement in an Islamic bank, it is of paramount importance to assess the factors that influence the selection of an Islamic bank among Muslims. In this context, the prime question can be, in a country where both Islamic and conventional banks offer Islamic banking services, what are the main factors that motivate customers to deal with an Islamic bank?

1.3 Research Objective

The general objective of the study was to analyze the factors that affecting the choice of Islamic banking among a selected Muslims in Nairobi.

Specific Objectives

- i. To find out how the cost of services offered by the banks affect the choice of Islamic banks by Muslims.
- ii. To determine how conformity of products to Islamic finance ethics influence the choice of an Islamic bank.
- iii. To establish how customer service delivery process affects the choice of Islamic banks.
- iv. To find out how the availability of Islamic banking services to the customers affects the choice of an Islamic bank.

1.4 Research Questions

The study was guided by the following research questions,

- i. How does the cost of services offered affect the choice of an Islamic bank?
- ii. Is conformity of products to Muslim faith important in the choice of an institution for Islamic banking services?
- iii. What role does the service delivery process play in the choice of an Islamic bank among customers?
- iv. How does availability of Islamic banking services to the customers affect the choice of the bank?

1.5 Significance of the Study

This survey research can play an important role in providing the necessary information for guiding a firm's development of new marketing strategies. The study has shed light on Islamic bank customer preferences. Since Islamic banking and finance is a new concept in the Kenya's banking sector, the study is an eye opener to potential investors wanting to venture in the banking industry.

The findings in this study can also be important to the policy makers who are still designing this new industry to ensure its success. To the existing institutions, the study will give them the information on their customers five years after the inception of this industry, such information is important for service and product improvement.

1.6 Scope of the Study

Islamic banks in the world generally operate within three different types of environment; First, those that function in countries where some degree of Islamic *Sharia* principles are observed (e.g., Iran, Pakistan, and Sudan); Second, those that function in predominantly Muslim countries along with conventional banks (Arab and Muslim countries such as Saudi Arabia, Indonesia and Malaysia); and thirdly, those that function in predominantly non-Muslim countries along with conventional banks (Western countries and others, Kenya included). This study focused on the customer choices of Islamic banks in the third environment.

The research project was carried out in the Islamic bank branches and premises of Islamic bank customers, targeted *sharia* banking patrons.

1.7 Assumptions of the Study

The main assumption of the study was that the views offered by the customers were factual and representative of all others Islamic banking patrons in Nairobi; and that the respondents volunteer all the necessary information to the researcher without suspicion. It was also assumed that banks offering Islamic finance products have specific feature that are similar and therefore what attracts a customer in one Islamic bank will do so in another. The last and also important assumption was that of homogeneity of population

and therefore all individuals had the same information, therefore gender does not affect bank preferences.

1.8 Limitations of the Study

The study was restricted to only city in the country with sizeable Islamic banks, i.e. Nairobi only. Important customer information in conventional banks might have been left out since the study focused on Islamic aspects of the banks only.

The investigation targeted a small sample of 40, selected subjectively and therefore, it might be hard to generalize the findings of this study. The data used in the study were collected in such a manner that necessitated individuals recalling the reasons why they chose a bank with which to hold their account, even though some respondents made this decision more than three years ago. Such an approach is dependent upon individuals accurately recollecting the reasons for their choice. Perhaps the ideal methodology would have been to collect data continuously over a long time period (say in excess of 10 years); polling every individual shortly after they opened their account. However, the implementation of such an intricate and long-term research plan is neither a practical nor realistic option. The chosen approach, therefore, represents a practical and operationalizable alternative which yields valid insights. In addition, as discussed above, evidence suggests that individuals regard the opening of their main bank account as a significant act and can accurately report the reasons for their choice, even after a lengthy lapse of time.

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This chapter contains an exploration of the literature of some of the studies done on the subject or related to it in other parts of the Muslim world by other authors. Further, the author brings out the some simple analysis of the independent variables for a better comprehension.

Islamic finance flows from the principle that religion cannot be divorced from any aspect of life, including business. *Sharia* law governing Islamic finance is derived from the guidance from Allah (A.M) found in the Quran and the *Sunnah* (teachings) of the Prophet Muhammad. (PBUH).This necessitates tailoring conventional financial practices to fit within religious rules stemming from as far back as the time of Muhammad (PBUH) in 7th Century AD. Therefore, the industry of Islamic banking is quite distinct from the modern and secular investing practices of the West. The following are the key features of Islamic Finance;

2.1.1 Interest (*Riba*) is Forbidden

Even though there are different schools of thought regarding *riba*, most scholars and academics regard *riba* as interest and/or usury, in other words, the additional amount that is payable to the supplier of funds in return for the utilization of the funds and its prohibition is to discourage society from conducting business undertakings in such a manner that will encourage debt and passive participation in the economy (Karim and Archer 2002).

2.1.2 Prohibition of *Gharar* (Risk and Uncertainty)

The second significant prohibition in Islamic finance is *Gharar*, generally translated as risk, hazard or uncertainty. Al-Dareer (1997, p.10) defines *Gharar* as “cases of doubtfulness or uncertainty, as in the case of not knowing whether something will take place or not.” El-Gamal (2000, p.7) defines *Gharar* as ‘the sale of probable items whose existence or characteristics are not certain, due to the risky nature which makes the trade similar to gambling’.

2.1.3 Profit and Risk Sharing

Contrary to capitalist economic theory, which defines entrepreneurship and capital as separate factors of production, Islam teaches that an entrepreneur cannot participate in the free market without the capital needed to fund such participation (Usmani, 2002). A party other than the entrepreneur, such as a bank, can contribute capital, and the contribution of capital implies that the contributor and entrepreneur are both parties to the free market enterprise, with rights and obligations (Usmani, 2002).

2.1.4 Money is a Medium of Exchange

The crucial difference within the Islamic economic approach is to deny to money the role of a commodity which can be traded for profit. Conventional economics always defined money as a key factor of production whose worth was determined by the rate of interest. Islam only permits money to be used as a medium of exchange. As such the bank issuing money cannot rely on collateral alone as the principal criteria in determining whether to extend a loan.

2.1.5 Transparency in Transactions

Islam stresses transparency in all financial transactions. A sale is rendered void if the purchaser is not made fully aware of what he is buying or if in fact a defect in the product is concealed by the seller. A prerequisite to sale is clearly identifying the existence and quantity of the subject matter. Often, even the conditions of delivery are left unambiguous.

2.1.6 Asset-Based Financial Instruments

Islam encourages property ownership and free trade (Usmani 2002). Islamic finance encourages the use of assets, fixed and otherwise, in all business transactions, and assets can be used as collateral for loans or as commodities to be financed (Usmani 2002). This could suggest that most Islamic finance products should be geared towards asset finance or investment instruments. Examples of assets are land and buildings, vehicles, investments, equipment, furniture and stock for resale, to name a few. Some of the most frequently used financial transactions include:

2.1.7 The Sharia Board

Islamic financial institutions are guided by a legitimate control body known as the *Shariah* Supervisory Board (SSB). The purpose of the SSB is to ensure that the financial institutions operate in conformity with *Shariah* and are “usually made up of a number of jurists who provide clarification in regards to any questions that the financial institutions may have,” (Rammal, 2006 p. 205). These SSBs consist of *Shariah* advisers who are hired by the financial institutions and act as an internal control body in the organization, therefore, enhancing the credibility of the institutions in the eyes of its customers, and bolstering their Islamic credentials.

2.2 Specific Literature Review

In terms of marketing, the product or offering will be successful if it delivers value and satisfaction to the target buyer. The buyer chooses between different offerings on the basis of which is perceived to deliver the most value (Kotler et.al., 1999). Value can be defined as a ratio between what the customer gets and what the customer gives. These benefits that customers seek to get are functional benefits and emotional benefits. In Islamic banking, the emotional benefits are the ethical benefits derived from the products offered by the banks.

Consumers usually face a broad array of products and services that might satisfy a given need. Consumers make buying choices based on their perceptions of the value that various products and services deliver. Customers often do not judge product values and costs accurately or objectively but instead they act on perceived value. Customer satisfaction is closely linked to quality, which begins with customer needs and ends with customer satisfaction. The cultural environment is made up of institutions and other forces that affect society's basic values, perceptions, preferences and behaviors. So when it comes to Muslims, religion plays a major role in choices and therefore cannot be divorced from customer satisfaction.

Customer satisfaction begins with clear, operational definitions from both the customer and the organization. Understanding the motivations, expectations and desires of both gives a foundation in how to provide best service to the customer. It may even provide

information on making improvements in the nature of business. This is the heart of research into customer satisfaction (Naylor and Greco, 2002). Customer satisfaction is the extent to which a product's perceived performance matches a buyer's expectations. If the product's performance falls short of expectations, the buyer is dissatisfied. If performance matches or exceeds expectations the buyer is satisfied, or delighted (Kotler et.al 1999). Clearly defining the key concepts and elements of satisfaction provides a template by which information can be gathered about what does and what does not work. Hayes, (1998) observed that this includes both the hard measures those that are more tangible and observable (i.e., number of complaints, average wait time, product returns, etc.) and the soft measures-those less tangible aspects (i.e., friendliness, helpfulness, politeness, etc.). These definitions often start with the most vague and general one and end up with the highly specified and precise examples. The bottom line is that in order to know about customer satisfaction, one need to know what to look for, and (Mitchell, J., 1999). The organization needs to seek this information from both within and without.

2.2.1 The Cost of the Products

Studies have focused on surveying qualitative aspects of banking selection criteria which directly relate customer preferences towards the Islamic banks. On the other hand, at the macro-level, quantitative models have been developed to investigate the factors that influence the level of deposit mobilized by the Islamic banks, hence provide insights into the determinants of Islamic bank's growth. In this context, Jalaluddin (1992) argues that in contrast to the Keynes' absolute income hypothesis, saving is not merely a 'residual' concept, in the sense that what a Muslim saves to perform his duties to himself, family, society, and Allah (AM), which definitely require economic backing. Thus, there is a social welfare dimension to the savings behavior of a Muslim. In fact, as savings are invested, economically rewarding opportunities will increase which is expected to increase the welfare of Muslim *ummah*.

Jalaluddin further argued that the life-cycle hypothesis proposed by Modigliani and Brumberg (1954) is more applicable for the framework of Muslim's saving behavior. The four motives of saving proposed in the life-cycle model are consistent with Islamic

norm behaviors. These motives are evident not only contemporarily, but also during the Prophet's (PBUH) time. A Quranic verse, for example, states that a Muslim should "...not spend everything so that you became blameworthy and destitute" (Al-Qur'an 17:29), hence emphasizes the importance of savings.

The normative aspects are later developed into empirical models. At the micro-level, extensive studies have been conducted to survey the banking selection criteria among customers of the Islamic banks. Researchers find various factors that influence the customer's choice of Islamic banks such as cost and benefit of product offered (products prices and rate of return of the investment), service quality (fast/efficient banking service and friendliness of the bank's staff), size and reputation of the bank, convenience (location and ample parking space) and friends/families influences (Erol and El-Bdour, 1989; Erol et al., 1990; Haron et al., 1994; Gerrard and Cunningham, 1997; Nasser et al., 1999; Ahmad and Haron, 2002; and Bank Indonesia, 2005b). Religious and corporate social responsibility issues are also regarded as important consideration in selecting Islamic banking (Haron et al., 1994; Metawa and Almosawi, 1998; Almosawi, 2001; Bank Indonesia, 2005b; and Dusuki and Abdullah, 2007).

In one of the earliest studies on Islamic banking selection criteria, Erol and El-Bdour (1989) discover that the most important consideration in dealing with Islamic banks in Jordan are the provision of fast and efficient services, bank's reputation and image, and bank confidentiality. Interestingly, they observe that that religious motive is not a primary consideration among the customers to patronize the Islamic banks. The importance of these banks' attributes is confirmed by the finding of Edris and Almahmeed (1997) for the case of Kuwait. However, recent findings suggest the opposite. Nasser, et.al (1999) report that religiosity and adherence to *Sharia* is indeed major reasons in selecting Islamic banks services in Jordan. They also find that other factors such as bank's reputation, provision of various banking products, confidentiality, location, provision of quality services and profitability motives are equally important for customers in choosing the bank. Similar results are also found in Bahrain, in which bank's specific factors including image, availability of parking space near the bank, friendliness of bank's personnel and availability of Automatic Teller

Machine (ATM) are found to be significant in determining the preference toward Islamic banks (Metawa and Almosawi, 1998; and Almosawi, 2001).

Several banking selection studies are also conducted for the case of the Asian countries. The selection of Islamic banks in Malaysia appears to be based on a combination of religious motive, financial reputation and quality services offered by the banks (Haron et al., 1994; Ahmad and Haron, 2002). In addition, recent study by Dusuki and Abdullah (2007) point out that good social responsibility practices, location and/ or convenience, and product prices are also important in patronizing the Islamic banks. In Singapore, the behavior is relatively different due to customers' segregation into Muslim and non-Muslim group. While the Muslim customers consider religious and quality services as major reasons for choosing Islamic banks, the non-Muslim place high importance for getting more interest payment from the banks in making their decision and choosing an Islamic bank's services (Gerrard and Cunningham, 1997). Furthermore, in Indonesia, study on potency, preference and people's behavior towards Islamic banks conducted by Bank Indonesia (2005) finds that the main reason to choose Islamic banks service in the country are religious motive and bank's location (people's accessibility to the bank). The study also reveals that return of Islamic banks is not a significant reason in choosing the Islamic bank's services. However, the perception on interest rate is rather ambiguous. Although most of the respondents agree that interest rate is prohibited in Islam, they are not against the interest rate application in the banking system. Despite their strengths in explaining preference towards Islamic banks, the survey on banking selection criteria explained above have some limitations.⁵ The limitation of the banking selection studies is filled by empirical studies on determinants of Islamic banking growth from the macro perspective.

2.2.2 Conformity of the Islamic Banking Products

Chase et. al. (2004) defines conformance quality as the degree to which the product or service design specifications are met. In Islamic banking products, design specifications are those directed by the *Sharia* board, which must be in conformity with the Islamic religious teachings. The activities involved in achieving conformance are tactical, and

day to day in nature. It should be evident that a product or service can have a high design quality but a low conformance quality and vice versa, (Chase et. al., 2004)

Religiosity is expected to have a significant influence on a customer ethical beliefs and this itself is usually reflected in daily conducts and commitments (Conroy & Emerson, 2004). Studies on religiosity being a determinant of consumer attitudes and practices like conclude that due to the fact that religiosity is a significant determinant of both idealism and relativism then it is indirectly a significant determinant of consumer ethical beliefs and practices.

Islamic banks are a true reflection of *Sharia*-compatible formulation, which the clients themselves respect and believe in, but previous empirical studies have found that religious motivation is not the only criterion for the selection of Islamic banking institutions or services. Some studies found that Muslim clients would approve Islamic banking products and/or services for religious reasons (Metawa & Al Mossawi 1998). Other studies found that Muslims would buy or approve Islamic banking products and services not only for religious reasons, but also for religious and business reasons.

2.2.3 Service Delivery Process

A process is any part of the organization that takes inputs and transforms them into outputs that are of greater value (Chase et. al. 2004). Organizations must determine the best way to deliver quality products and services and to provide effective follow up support. Lucas, (2005) noted that everything done in customer service is crucial, this includes the way information is made available to customers initial contacts and handling of customer issues, sales techniques, order collection and processing, price quotations product and service delivery. There is a delicate balance in selecting customer delivery systems. This is because each customer is unique and has personal preferences. For Islamic bank customers, much reviewed literature pointed out that the process need to be that is in line with the Islamic culture, starting with Islamic salutation and even many a times, the tellers of men and that of women separated.

Customer satisfaction can thus be based not only on the judgment of customers towards the reliability of the delivered service but also on customers' experiences with the service delivery process. This is the reason why in the services literature, there is a strong emphasis on the importance of service quality perceptions and the relationship between customer satisfaction and service quality (Cronin and Taylor, 1992). Research conducted by Bitner, 1990 argues that satisfaction with a service encounter affects assessments of service quality and subsequent loyalty and switching behavior. The recognition that there are positive (although not perfect) links between satisfactions in general, relationship satisfaction in particular and subsequent retention and repurchase highlight the importance of identifying and explaining the conditions under which satisfaction develops.

The Islamic banking client service model requires good integration of client needs with the bank's obligation to promote profit- and risk-sharing and to identify a win-win banking solutions (Silva , 2006). Banks generally have sufficient information to accurately enforce strong risk management processes and to monitor a client's account so that they can alert the client to mitigate any potential business risks (Ghannadian & Goswami 2004). Silva, (2006) suggested that providing the necessary security, promoting transparent and full disclosure, and implementing measures to prevent money-laundering activities are just some of the vital banking services that Islamic banks can offer their clientele.. A good client service model would provide these, thereby obtaining support from the community in which the bank operates, which could positively impact on the bank's market share.

2.2.4 The Availability of the Services

How accessible services are to customers is a feature to be designed into service production decisions. Accessibility to a service can be an important point of differentiation between service providers, Lucas, (2005). Many of the banking patronage studies have identified a number of factors among them convenience (*location and ample parking*), long business hours being very important criteria for the customers in selecting a particular Islamic bank.

Widespread accessibility to services is of paramount importance given the business nature of Muslims. The advancement of technology could assist Islamic banks to spread their reach more (Taylor 2003). Studies in Jordan and Malaysia have found that clients were not happy with the bank infrastructure and requested more branches and automatic teller machines (ATMs). Metawa & Al Mossawi also acknowledged a well-crafted advertising strategy could lead to good product take-up. Islamic banks need to continuously communicate their products and services to their clients and make best use of brochures.

2.3 Empirical Literature Review

In Jordan, a study by Erol, and Radi, 1989 found that religion did not play significant role to select an Islamic bank but profit motivated criteria was an important factor to choose a bank. The opening new branches by Islamic banks were also not a significant factor in Jordan according to the same authors. However, other major findings are that peer group influence plays an important role in selecting Islamic banks as depository institution. The study explored that the demographic factors such as religion and knowledge played a significant role to select a bank. Researchers found that customers do not have so much knowledge about the Islamic banking products such as *Mudaraba*, *Mushaaraka*, *Murabaha* etc., but they buy these products for the reason of religion. This study also revealed that bank's name and reputation also strongly effect on selecting a bank. Yet in another study in Malaysia, the researchers explored that reputation and image factor are evidenced as one of the important criteria in the banking selection decision (Yousuff and Azurah, 2006).

On banking selection and religiosity, studies like that of Gerard and Cunningham, 1997 has attempted to look at the influence of Islam on the choice of banking, depth of knowledge, perception and awareness among the public regarding Islamic banking. When comparing the Islamic and conventional bank customers, it was found that profitability motivation supersedes religious motivation in selection of banks. This was attributed to the fact that the customers may have been used to the profit-oriented conventional banking environment and the possibility that the respondents may have underestimated their religious motivations when answering the questions surveyed. In

contrary, (Bley & Kuehn: 2004) found that the preference for Islamic banking is primarily driven by religious beliefs, not financial knowledge, i.e. the stronger the religious commitment the more preference for Islamic banking services.

Research conducted on Islamic banking to examine customer satisfaction and perception among Jordanian people by Kamal and Khalid, 1999 revealed that there is a certain degree of satisfaction of many of the Islamic banks' facilities and products. The respondents expressed their dissatisfaction with some of the Islamic banks' services. Although the respondents indicated that they are aware of a number of specific Islamic financial products like *Murabaha*, *Musharaka* and *Mudaraba*, they showed that they do not deal with them.

In a study done in Malaysia, a country where majority of the population is Muslims, on "Factor Influences on Selection of Islamic banking, by Haque et. al 2005, to investigate the major factors that reflected customers perception and satisfaction, in Islamic banking reported that there was no too much difference between males and females in Malaysia terms of perception about Islamic banking and that 89.4% of the respondents knew about Islamic banking since the banks provided information about their services. To make useful comparison while evaluating quality of services of the Islamic banks, 75% had not opened accounts with Islamic banks yet and 24.54% had accounts in both Islamic banks and conventional banks. The authors also reported with 95% confidence, that age does not have significant relationship with overall perception towards Islamic banks and that there was no significant relationship between level of education and overall perception towards Islamic banks. Race also showed significant relationships with overall perception towards Islamic bank.

Based on the results by Logit model, Haque et. al found that with 95% confidence, customer perception about Islamic banking were influenced significantly by quality of services, confidence in bank, social and religious perspective and availability of services. Haque et. al concluded that the provision of high standard of service quality may manage to increase customer satisfaction and that there was positive perception on Islamic banking. Moreover, availability of services and social, as well as religious

perspective at higher level could make Islamic Banking easier and comfortable. On the other hand, negative values of confidence in Bank indicated comparatively less impact on customer perception for selecting bank products.

This study targeted all potential bank customers but did not zero in to establish exact preferences of customers who had accounts with the Islamic banks. Furthermore, Islamic banking in Malaysia is in advanced stages unlike in Kenya where the sector is just starting and mired with teething problems, therefore, awareness is expected to be high in the former environment than the latter.

Another research on the effects of automated service quality on Australian banks' financial performance and the mediating role of customer satisfaction found that customer satisfaction mediates the effects of automated bank service quality on financial performance (Al-Hawari and Tony 2006). Customer satisfaction can thus be considered as the key construct to bank financial performance. However, this research found that internet service quality had no significant relationship with customer satisfaction; improvement in the quality aspects of this dimension could enhance overall satisfaction and thus financial performance. Results showed that service problems and the bank's service recovery ability have a major impact on customer satisfaction and intention to switch. It is interesting to note that the bank's features and competitive interest rates were significant contributors to customer satisfaction in conventional banking.

In a study by Karim and Affif, (2007) on "Islamic Banking Consumer Behaviour in Indonesia", they found that in terms of perception, beside the perception that an Islamic bank is a bank that operates under Islamic principles (including avoiding interest), other important perceptions that surface are banks that were especially for Islamic consumers only, had limited facilities compared to conventional banks and do not have a large customer base. These findings show that even though awareness of Islamic banks may be quite high in Indonesia, the understanding of what the Islamic bank is and is not was still lacking.

Religiosity is expected to have a significant influence on a customer ethical beliefs and this itself will be reflected in his daily conducts and commitments (Conroy & Emerson: 2004). The authors observed that studies on religiosity being a determinant of consumer attitudes and practices and concluded that due to the fact that religiosity is a significant determinant of both idealism and relativism then it is indirectly a significant determinant of consumer ethical beliefs and practices.

2.4 Overview of Literature

Past studies on Islamic banking consumer behaviour, such like the ones reviewed in the above literature have been conducted in countries like Jordan, Malaysia and Indonesia. However, surprisingly in these countries, the majority of the population is Muslim. Having been introduced in these counties some decades ago, Islamic banking is not a niche but in advanced stages (personal observation) with strong structures that enhance the quality of services being offered.

This study however will be conducted in Kenya, a country where the majority of the population is non-Muslim and conventional banking is all that the public has known including the Muslims who are the target of Islamic banking. Studies in many Muslim and Arab countries have mainly concentrated on consumer perceptions only. Islamic banking being a niche that has elicited many players in the country, this survey is designed to capture customer choices given that some players in this field do not yet have the required institutions required in this sector.

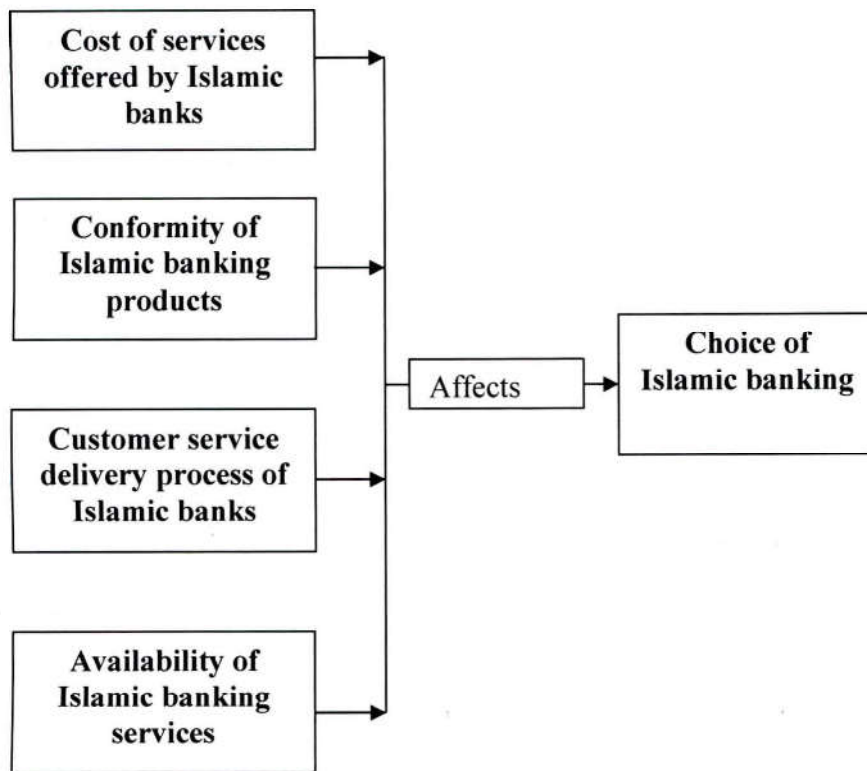
In countries like Jordan and Malaysia where related research has been conducted, Islamic banking is in advanced stages with a variety of products ranging from bank accounts, mortgages, *sukuk* bonds to *takaful* (Islamic insurance). Important to highlight is also that the financial industry in these countries is far much developed compared to that of Kenya and therefore the level of customer knowledge of finance is at variance. In Kenya, the sector is three years old and customers are yet to fully start enjoying highly standardized services. The cost of the services of Islamic banks has not yet manifested itself unlike in the former environment where mortgages, bonds and many other short and medium term services have well known costs.

The industry of Islamic banking having been introduced in the country in 2007 has still not caught root in the country and it is of paramount importance to know how it is fairing on from the consumer side. The practices in use by the Islamic banks have evoked questions of morality with sections of the public wondering whether the practices adopted to avoid interest really do their job or is it simply a change of name. Some banks offering Islamic banking windows in Kenya do not even have *Sharia* boards, putting the conformity of their services into question. In the light of this, knowledge of how social and religious factor influences customers choice will be surveyed.

This study will also be conducted in a country whose awareness and financial information flow is not as advanced as the countries where such studies have been conducted before. For instance, Kuala Lumpur, Malaysia is a significant financial hub of South East Asia, trading in billions of US dollars worth of *sukuk* bonds annually. This study will capture information and availability of services in a less developed financial industry, Kenya.

2.5 Conceptual Framework:

According to Mugenda and Mugenda (2003), conceptual framework helps the reader to quickly see the proposed relationship between the variables in the study and also show the same graphically and diagrammatically. This study identifies the factors contributing to the choice of an Islamic bank. Kenya is a multicultural country but the percentage of Muslims is lower. Based on the discussion in literature review, it was identified that the cost of services, conformity of an institution with Islamic banking principles, the customer delivery process and information and availability of services are factors that elicit confidence in the bank and therefore bring about customer choice. Therefore, based on these factors conceptual framework of this study has been developed as follows.



INDEPENDENT VARIABLES

DEPENDENT VARIABLE

Fig. 2.1 Conceptual Framework

Source: Author

CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the procedure that was followed while conducting this study. It covers the research design, model specification, definition and measurement of variables, the study area and the study population, sampling and the type of data to be collected. Also covered is the research instruments to be used and data analysis among others.

3.2 Research Design

A descriptive research design was used because the study aimed at assessing the factors that influence customers to choose an Islamic bank. Maholtra, (1993) described descriptive research as a fact finding survey whose major purpose is to describe the state of affairs as it exists at present. It is an *ex post facto* research and its main characteristic is that the researcher has no control over the variables and therefore can only report what has happened or what is happening. The descriptive approach will also facilitate an in-depth analysis of the research variables in understanding and interpretations of findings and hence the ability to answer the research questions.

According to Mugenda and Mugenda, (1999) this design is a systematic inquiry into which the researcher does not have direct control of the independent variables because their manifestation has already occurred. It is a method suitable for extensive research and accounts for a substantial proportion of research in the field of social sciences.

3.3 Study Area

Nairobi was the study area; it was assumed to be representative area in terms of Kenyan Muslims. As Kenya's capital and financial center, it is where most banks have Islamic banking services in their branches.

3.4 Target Population

This study investigated factors influencing the choice of Islamic banking services by customers and the Muslims in Kenya were the universe and therefore perceived to be the population of the study.

3.5 Sampling Techniques

A non-probability sampling method, purposive sampling was used in the study, where respondents were selected because of some characteristic i.e. being muslims and having an account with either a fully fledged Islamic banks in Kenya or the conventional banks offering Islamic banking services windows. The power of purposive sampling lies in selecting information rich cases for in-depth analysis related to the central issues being studied. Purposive sampling was particularly relevant to this study since the researcher was concerned in exploring the universe and understanding the factors that make them choose an Islamic bank. This led to the use of commonsense and the best judgment in choosing the right respondents for the purpose of this study. By the use of this method, those who did not suit the purpose were excluded. The respondents were conveniently picked randomly in the city estates of South C, Eastleigh and in Muslim owned businesses in Jamia Mall in the Nairobi's central business district.

3.6 Data Type and Source

The data used in this study were generated from responses to questionnaires completed at face-to-face interviews, with questions posed verbally by the researcher, who noted consumer responses. The data used in this study were taken from responses to questions about their choice of retail bank.

3.7 Research Instrument

To minimize the element of bias that could emerge from the study, a structured questionnaire consisting of close-ended types of questions was constructed for the study for collecting the necessary information which is related to the research objectives, the factors affecting of customers' choices to Islamic banks in Kenya. The survey questions consisted of four specific sections each containing questions pertaining different parts or objectives of the study.

The questionnaire employed Likert scale, where respondents were required to respond according to their degree of disagreement or agreement to a list of statements related to the research variables. Each degree of disagreement or agreement had a numerical score between 1 (one) and 5 (five), and the respondents total score in each variable (section), was computed by summing the scores from all the statements. This way the instrument then yielded a total score for each respondent.

3.8 Validation and Reliability of the Research Instrument

Mugenda and Mugenda highlighted the importance of this process for assessing the degree to which a research's data collection instrument yields consistent results or data after repeated trials. The questionnaire was then reviewed by an Islamic banking specialist and then a test-re-test method was used to test the questionnaires validity with the first sample being done in January 2011 and after minor corrections, a second sample was administered in February 2011.

3.9 Data Collection

Upon verification of the validity of the data collection instrument, data for this study were collected in the first two weeks of March 2011 by the use of purposive sampling method. Random sampling was used to obtain a representative sample of the larger population and then those subjects that are not members of the desired population are screened or filtered out. The screening out condition was that the respondent had to be a Muslim having an account with either of the two fully fledged Islamic banks in Kenya of a conventional bank having the same services and had to know how to read and write.

3.10 Data Analysis

Being a qualitative research, the data was analyzed by use of descriptive statistics. Specifically percentages were employed by the researcher. The data analysis tools are simple tabulations and presentations of the report using statistical packages for social sciences (SPSS).The data was then presented using percentage tables.

3.11 Ethical Issues

Ethics are norms or standards of behaviour that guide moral choices about our behaviour and relationships with others. In this study, ethics were observed in the following ways; in the data collection instrument, the goal of the research was briefly but clearly stated so as to put respondents at ease. The respondents were not required to write their names anywhere in the questionnaire. Questions seeking personal information were avoided.

CHAPTER FOUR

4.0 DATA ANALYSIS RESULTS AND DISCUSSION

4.1 Introduction

This research sought to investigate the factors affecting the choice of Islamic banking by a selected group of Muslims in Nairobi. Questionnaires comprising of closed-ended questions were circulated to a sample of 40 Islamic bank customers out of which 33 responded. The data were then analyzed on the basis of this response rate (82.5%) and sequentially presented in form of tables and pie-charts. From the descriptive analysis 75.6% of the respondents were male, while 24.4% were female and as stated in the assumptions of this study, gender was presumed not to affect the dependent variable.

Islamic banking products in Kenya are offered by eight financial institutions, namely; First Community Bank, Gulf African Bank, Barclays Bank, Kenya Commercial Bank, National Bank of Kenya Co-operative Bank, Dubai Bank and Chase Bank.

However for the purpose of this study, these banks have been grouped in to two categories; the Fully-Fledged Islamic Banks i.e. First Community Bank and Gulf African Bank and the Conventional Banks i.e. Barclays Bank, Kenya Commercial Bank, National Bank of Kenya Co-operative Bank, Dubai Bank and Chase Bank. On the basis of bank patronage, out of the 33 valid responses, 18 were fully-fledged s Islamic Bank customers while 15 were conventional bank customers as depicted in Table 4.1 below;

Table 4.1 The bank composition of the respondents

Type of Bank	No. of Respondents	Percentage
Fully Fledged Islamic Banks	18	54.6
Conventional Banks	15	45.4
TOTAL	33	100.0

The questionnaire listed the important factors identified as the influencing factors on decision making and satisfaction levels of the clients from various studies referred in the literature survey and captured the respondents' perceived importance of the factors viz. a viz. the performance of the bank on each of the factors. The responses were captured in a scale of 1 to 5, 1 representing the "Strongly Disagree" while 5 representing "Strongly Agree". The weighted average scores of all responses were calculated and the scores on importance were ranked and tabulated.

4.2 Descriptive Analysis

Descriptive survey design was adopted with a view to provide explanations with regard to the factors influencing the choice of Islamic banks in Kenya. The data collected were entered and analyzed by simple descriptive analysis using Statistical Package for Social Scientists (SPSS) version 14.0 software. The software was chosen because it is the most used package for analyzing survey data. The software has the following advantages; it is user friendly, can easily be used to already coded questions like the ones contained in the research questionnaire, cross section and time series analysis and cross tabulation; (i.e. relate two sets of variables) and it can also be used alongside Microsoft excel and word.

4.3 Results and Discussion

Data realized from this survey were analyzed based on the type of Islamic banks the respondents patronized and the results presented objective wise.

The cost of services offered and the choice of Islamic Banking.

The first objective of this study sought to find out if the cost of the services offered by the banks had an effect on the choice of an Islamic bank by Muslim patrons. Asked whether the cost of services offered by particular banks influenced their choice of an Islamic bank, 56% of the fully fledged Islamic bank customers agreed that cost was a determinant in their choice with 28% being undecided if cost was a factor as shown in figure 4.1 below.

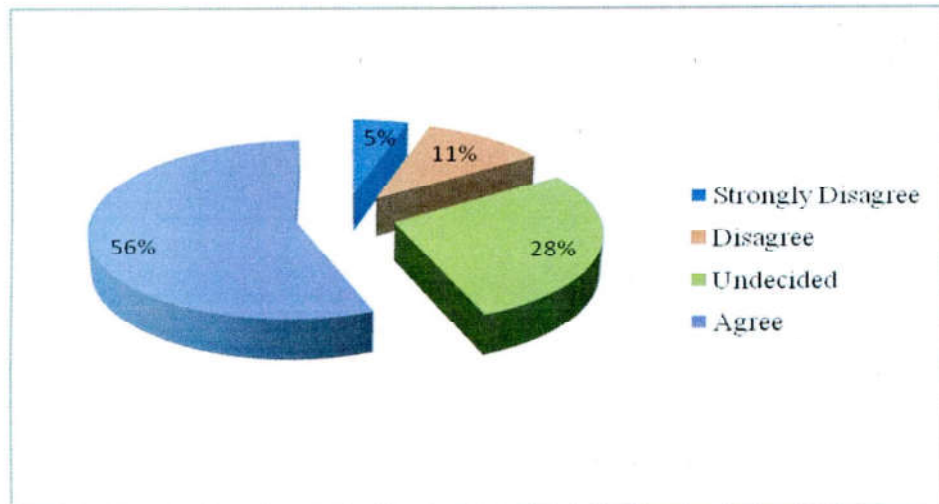


Figure 4.1: Fully fledged Islamic bank customers: Cost as a determinant of Bank choice

Islamic banks in Kenya offer product mix that attracts many customers across the board. They offer personal accounts with no ledger fees, with an ATM card and cheque book services at no extra cost. This might have been an attraction to the mainly unbanked Muslims of lower income cadre.

Only 47% of the patrons in conventional banks accepted cost was a determining factor in their choice of an Islamic bank, but 53% either disagreed or remained undecided if cost was a factor, affirming that it was not very important to them as depicted in figure 4.2 below.

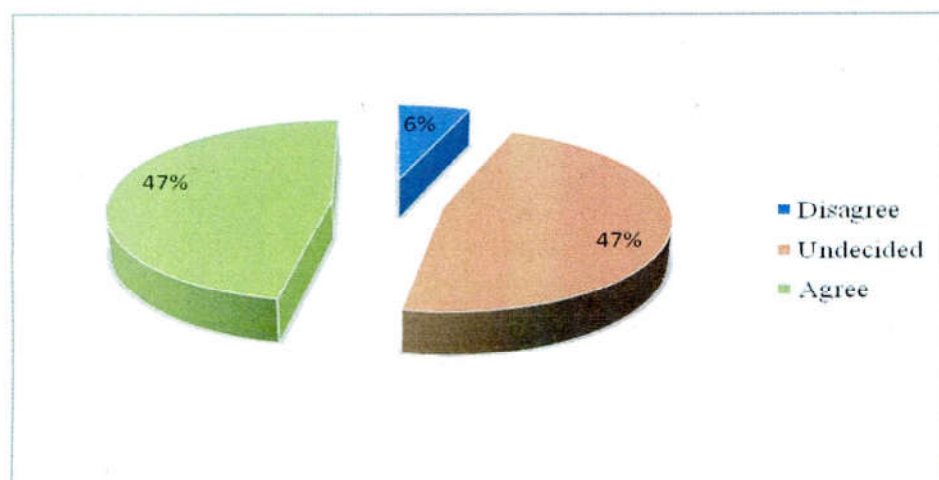


Figure 4.2: Conventional bank customers: Cost as a determinant of Bank choice

Many of the conventional bank customers banked with the same institutions before Islamic banking was licensed in Kenya after which they converted the same accounts to Islamic ones and therefore cost of banking might not have been considered.

In the overall sample, 52% agree that cost was important to them, and 36% remained undecided whether cost was an influencing factor. According to the literature reviewed, studies conducted in various countries where Islamic banking has been existent have found that the cost of the bank products (cost and benefit of product offered i.e. products prices and rate of return of the investment) had an influence in the choice of an Islamic bank. Haque e.t. al in a similar study in Malaysia had found that customer choice and perception towards an Islamic bank was significantly (95% confidence) influenced by the cost of the services the banks offered, in terms of the return on investment from *musharaka* and other Islamic banking products.

The conformity of bank services to Islamic Finance principles and choice of an Islamic bank.

The second objective of this study was to determine the effect of conformity of bank services to the teachings of Islamic faith on the choice of a bank to patronize. This was to highlight whether religiosity was important in Islamic banking industry in the country. Among the surveyed customers of fully fledged Islamic banks, 67% agree that conformity influenced their choice of the Islamic bank and 5% strongly agreed, therefore 72% chose the banks because of conformity as seen in figure 4.3 below.

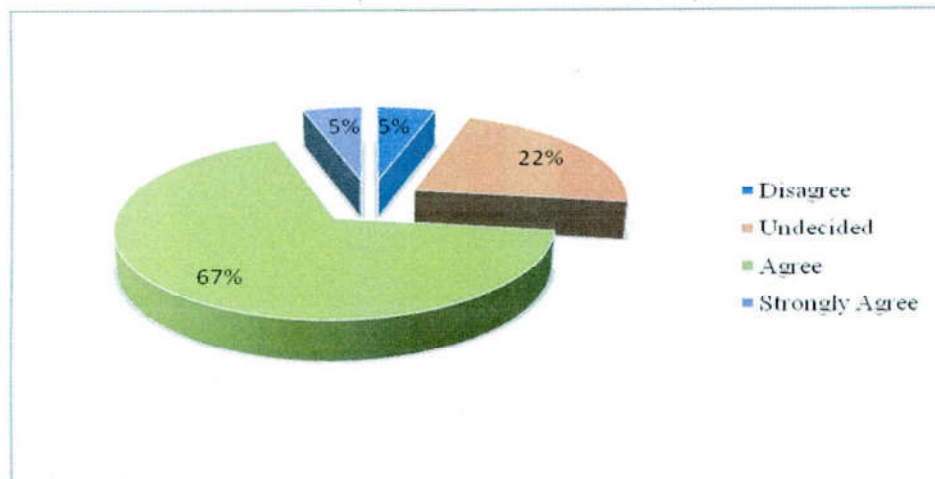


Figure 4.3: Fully-fledged Islamic bank customers: Bank service conformance to Islamic finance ethics and the choice of an Islamic bank.

Of the conventional banks customers surveyed, 47% accepted conformity of products to Islamic teachings was a factor in their bank choice. From literature, it was a common belief that Islamic services offered by conventional banks were not fully compliant to Sharia, prompting those who are sharia sensitive to trust the products of the fully fledged banks only. Lack of compliance of conventional banks to sharia principles can also be evidenced by the lack of sharia vetting boards in these institutions.

In the overall sample, 61% of the respondents agreed that conformity was a determinant in their choice of banking institution. This highlights the importance of this factor of conformity in Islamic banking and Muslims for that matter, with those in fully-fledged Islamic banks attaching more importance to this factor. Recent findings suggest that the role of religiosity where patrons will select a banking institution of the based on latter's conformity to Islamic teachings on finances has been rising. For example, Nasser et.al reported that religiosity and adherence to *Sharia* is indeed a major reason in selecting Islamic banks services in Jordan. Karim and Affif (2007) study on Islamic banking consumer behaviour in Indonesia found that religiosity was a determinant of consumer attitudes and practices towards an Islamic bank. In Islam any action taken by a believer must have a religious basis. It was for this very reason that Islamic banking was licensed in Kenya since before that, most Muslims had been avoiding conventional banks for the fear of interest. This study affirms that the choice of a bank among the

majority of the Muslim believers is based on the fact that the products offered by these institutions are perceived to conform to the Islamic faith.

The customer service delivery process in a bank and the choice of an Islamic Bank.

The third objective of this study was to establish whether customer service delivery process affected the choice of an Islamic bank.

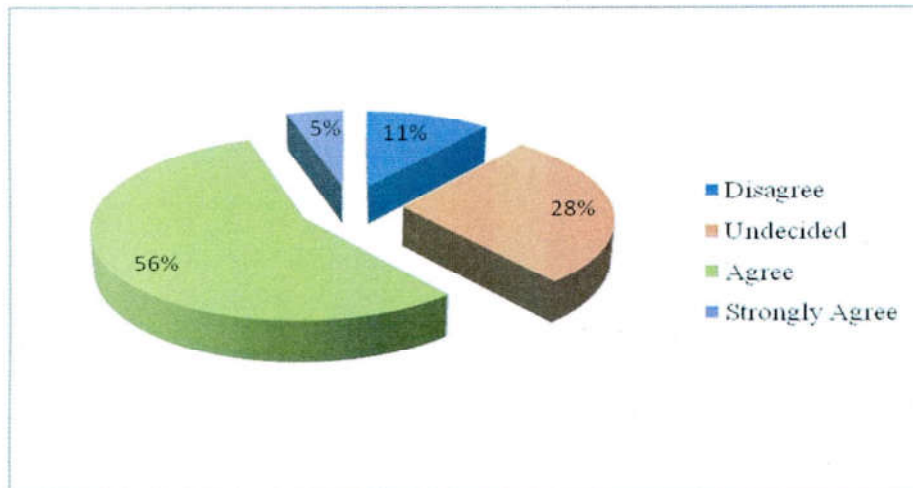


Figure 4.4: Fully-fledged Islamic bank customers: Service delivery and the choice of an Islamic bank

As shown in figure 4.4 above, out of the respondent's sample, 61% (56% agreed and 5% strongly agreed) of the customers of First community and Gulf African banks admit that service delivery process was important.

On the other hand, as seen in figure 4.5 below, 60% (53% in agreement and 7% strongly in agreement) of the surveyed conventional bank customers attested to the fact that service delivery process was an affective factor in their choice of an Islamic bank services.

In the overall sample, also 60% affirmed that service delivery process was a factor in their choice of an Islamic banking institution.



Figure 4.5: Conventional bank customers: Service delivery and the choice of an Islamic bank

Service delivery process is a business virtue that cut across all businesses and highly emphasized by contemporary management. Over time, customer perception of quality has changed and any organization that is in competitive business like banking has to focus on this to avoid losing business hence the similarity of the two groups of customers.

The customer delivery process in an Islamic institution will be expected to go in line with the teachings of Islam, from salutations to the actual transaction that a customer would want to do. This will act as a distinction between the Islamic bank and a conventional bank. Service delivery quality does not apply only to the product or service itself; it also applies to the people, processes, and organizational environment associated with it. For example, the quality of a bank will be judged not only by the quality of staff and product offerings, but also by the efficiency and accuracy of processing paperwork.

Availability of Islamic banking services and its effects on the choice of bank.

Lastly, this study sought to establish whether availability of Islamic banking services influenced Islamic bank patronage. 39% of fully fledged Islamic bank customers were undecided on this factor as a determinant of their choice of an Islamic bank with only 33% agreeing that service availability was important in during their choice.

For the conventional bank patrons, 73% (53% agreeing and 20% strongly agreeing) considered availability of bank services as one of the determining factors in their choice of an Islamic bank as shown in figure 4.6.

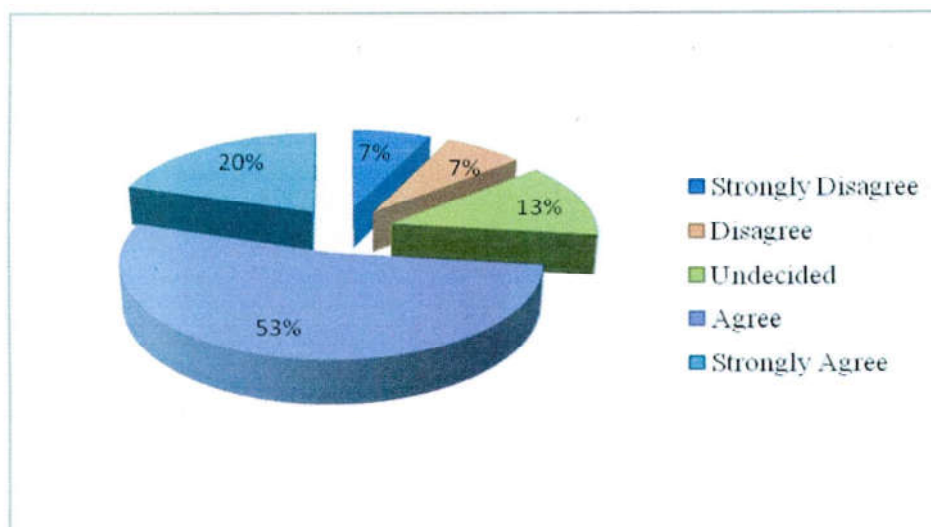


Figure 4.6: Conventional bank customers: Availability of bank services and the choice of an Islamic Bank

Being new in the Kenyan financial market, Islamic banks are found only in the big towns and especially Muslim dominated areas. In light of this, the availability of Islamic bank services is very limited, hence not an important factor for the fully fledged Islamic bank patrons in their choice of an Islamic bank to patronize. However, the conventional banks offering Islamic banking windows such as KCB, Barclays, Co-operative Bank, National Bank and Dubai Bank are better established with services such as wide ATM network, debit and credit cards and branch network. This explains the importance of service availability to conventional bank patrons in their choice of an Islamic bank since the services of these banks are available nationwide and even internationally.

The fully-fledged Islamic banks have a limited availability in the city. First Community Bank currently boasts of five branches whereas Gulf African Bank is the biggest in Nairobi with six branches. For conventional banks offering the Islamic banking windows, the services are available in their numerous branches in the most parts of the city.

CHAPTER FIVE

5.0 SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary of Findings

There were small variations of the factors that affect the choice of an Islamic bank in among Muslims in Nairobi. For the patrons of the fully fledged Islamic Banks, cost of the services, conformity and delivery of the services is important in the choice of Islamic bank. However, other major findings in the literature review were that that peer group influence plays an important role in selecting Islamic banks as depository institution. The studies explored that the demographic factors such as religion and knowledge were playing a significant role in selection of a bank. The researchers found that customers do not have so much knowledge about the Islamic banking products such as *Mudaraba*, *Musharaka*, *Murabaha* etc., but they bought these products for the reason of religion, therefore highlighting the important of religiosity in Islamic banking.

On the other hand the surveyed customers of Islamic banking windows in conventional banks seem to be attracted to the banks because of service delivery process and the availability of the bank services. This is made possible by the wide variety of services found in conventional banks operating Islamic banking windows as compared to the fully-fledged Islamic banks. These conventional banks, i.e. KCB Bank, Barclays Bank, Co-operative Bank, National Bank have their services available not only in Nairobi, but in most other cities and major towns in Kenya and in the East African region.

According to the results of this study, three independent variables have an effect on the choice of an Islamic bank of those customers who patronized fully fledged Islamic banks. These variables were the cost of the bank services, the conformity of those services to Islamic ethics of finance and the service delivery process in these banks. Islamic Finance avoids high costs and risks and this explains the reasons why these customers preferred a fully fledged Islamic bank to a conventional banks, which a usually associated with expensive services and interest in the Islamic *Ummah*. Conformance has been the most sensitive issue among the muslim populations around the world and only fully fledged Islamic banks are taken as the only institutions to be

trusted, but not conventional banks. Service delivery process is important in any industry, Islamic finance included, hence its effect on the choice of a bank. Availability of services was not as important to fully fledged Islamic bank customers as the other three variables.

For conventional bank customers, Service delivery and availability of bank services remained important in determining choice. As patrons of established banks with a big asset base and wide availability of services, customers in these banks disagreed that cost of services and conformity were important in their choice of an Islamic bank.

5.2 Conclusions

In conclusion, this study presented an analysis of how the relative importance of choice criteria can be influenced by religion and culture, highlighting those criteria shown to be important in recent decisions. The study provided important insights for practitioners, as an awareness of trends about the relative influence of choice criteria enables bank marketers to isolate those criteria which have increased or decreased significantly in importance latterly. With such information, marketers can tailor their strategies appropriately, and banks wishing to operate *Sharia* products can now know that mixing such with conventional services will affect their products.

Fully-fledged Islamic bank patrons were found to be cost averse. Islamic Finance itself is based on high cost and risk avoidance (avoiding *gharar*). People professing the Islamic faith find it hard to pay for the services of the bank in the notion that the latter keeps and trades with their money.

Findings show that the influence of religion is significant in the choice of a financial institution, a wakeup call to insurance and investment companies too. A good number of the conventional banks offering Islamic banking windows lack a *Sharia* board for vetting the services that the banks should offer.

Bank service quality was an important element that customers considered in order to select their Islamic banking institution and establish a long-term relationship with them.

Important issue which requires attention is the way bank personnel handle their customers, which definitely involves quality of service. Quality of service here means more than a smile or a passing greeting to customers. The dress code, customer relations, and the technique of answering the telephone are some of the areas to be emphasized.

Location factors, such as choosing a bank close to home or place of a mosque, have increased significantly in importance in motivating choice.

5.3 Recommendations

As customers generally prefer some banks for the reasons highlighted above, banks management should pay attention to factors that have significant effect on the choice of banks. Specifically, fully-fledged Islamic banks should increase the branch network by establishing more branches across the country, adopt appropriate strategic plan aimed at enhancing reputation of the banks and *sharia* conforming, improve personal security of customers, and make bank location more convenient and easily accessible to customers.

Transaction costs might erode the benefits of holding Islamic bank account. Commercial banks should entice customers with accounts that do not incur ledger fees for the services offered. There is also the need for full disclosure of charges and the importance of financial literacy and closer scrutiny of products by clients before they open bank accounts.

Religiosity has been established by the research as a key factor influencing Islamic banking. This result is very important and particularly useful for Islamic banks that have the intention to expand their market share. This can be understood as a religious factor influencing individual's decision to patronize Islamic banks. Muslims patronize Islamic banks due to their conviction that it is a sin to receive and pay bank interest

Because of the strong competition, customer expectation to receive high quality services and quick changes of technology, Islamic banks must therefore think strategically by providing high quality products and services to satisfy their customers.

This research found that availability of services, especially ATMs finds a top priority in customer bank selection. Hence banks have to give due importance in establishing a wide ATM network or entering into alliances with various banks. While studying the switching behavior of bank clients, availability of Technology based services is found to be a major reason for clients to switch banks. Hence banks have to work on that area to understand the needs of the client and have to implement strategies to satisfy the needs in order to retain their existing clients and attract new clients.

5.4 Suggestions for Further Research

The area of factors influencing customers on Islamic bank selection needs further research works to validate the findings with larger sample size and findings will help banks to make proper decisions on bank service design to attract more customers of Muslim faith.

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APPENDICES

APPENDIX I

Cover letter for the Questionnaire

From: Hussein N. Ndonye
To: Respondent
Ref: HD-334-033-0832-2009

March 2011

RE: REQUEST FOR RESEARCH DATA

I am a post graduate student doing my Executive MBA at Jomo Kenyatta University of Agriculture and Technology, Kenya Institute Of management campus. As a requirement in partial fulfillment of the degrees program, I am conducting a research study on ***FACTORS AFFECTING THE CHOICE OF ISLAMIC BANKING AMONG MUSLIMS IN KENYA: A SURVEY OF SELECTED MUSLIMS IN NAIROBI***

The purpose of this letter is to kindly request, for information which will facilitate the completion of my project. In this regard, do please complete the attached questionnaire. The questionnaire will be used to gather academic data only. All the responses will be taken in confidence and your identity kept anonymous. Further, your responses will not be individually analyzed but grouped together to draw a general conclusion of the study.

Thank you in advance and, hoping for your cooperation.

Hussein
EMBA – Student

APPENDIX II

Questionnaire

This questionnaire is designed to get information necessary for research that will be submitted to the School of Human Resource Development of Jomo Kenyatta University of Agriculture and Technology, in partial fulfillment of the Degree of Executive Masters in Business Administration. The information given in this research instrument will be confidential and will be used only for the above stated purpose only and not for any other whatsoever. Please do not write your name or contacts anywhere in this questionnaire.

Thank you.

Please indicate the name of your bank _____ Gender

Male/Female

1. The cost of products offered that attracted you to the bank.

Likert scale:

Strongly	Disagree	Undecided	Agree	Strongly
Disagree (1)	(2	(3)	(4)	Agree (5)

		1	2	3	4	5
1	The Profit and Loss Sharing which is clear to me					
2	The Islamic Bank personal accounts which do not have any charges					
3	Saving money in the bank is more beneficial to me than at home					
4	The returns from investments which are worth the cost incurred					
5	The bank mark up pricing which is fair to me					
	Total score					

2. Conformity the institution to *Sharia* banking principles

Likert scale:

Strongly	Disagree	Undecided	Agree	Strongly
Disagree (1)	(2)	(3)	(4)	Agree (5)

		1	2	3	4	5
1	The presence of <i>Sharia</i> board makes a bank acceptable to me					
2	The bank staff appear to very well know Islamic banking principles					
3	The bank has a friendly environment that is Islamically acceptable					
4	For Islamic products to be acceptable to me, the whole institution must be Islamic.					
5	I prefer to use this bank other than a conventional bank offering Islamic window services					
	Total score					

3. Customer service delivery process

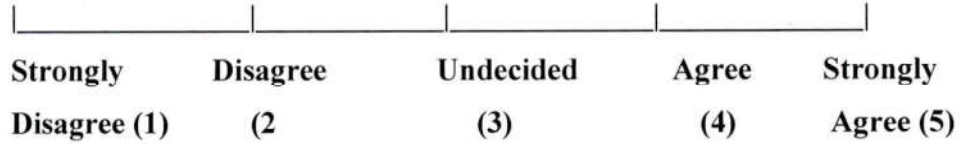
Likert scale:

Strongly	Disagree	Undecided	Agree	Strongly
Disagree (1)	(2)	(3)	(4)	Agree (5)

		1	2	3	4	5
1	My needs as a client are well catered for in the service delivery					
2	Delivery of service follows Islamic finance principles					
3	Staff in the bank is kind, courteous and answer questions to my satisfaction.					
4	The bank staff is knowledgeable in Islamic banking products					
5	The bank atmosphere and décor is satisfying to me					
	Total score					

4. Bank services availability

Likert scale:



		1	2	3	4	5
1	The bank is conveniently located and easy to find					
2	The banking hours of the bank are easy for me as a customer					
3	The bank services are widely available through in Kenya and abroad					
4	My bank advises me on the services offered (Profit and Loss Sharing Products)					
5	Islamic products that I need are available in this bank					
	Total score					

FOR RESEARCHER'S USE ONLY

Respondent total score

	Variable	Score
1	The quality of the services	
2	Conformity of the services	
3	Service delivery process	
4	Service availability	
	TOTAL SCORE	

