MUSLIM CONSUMERS ATTITUDE TOWARDS ISLAMIC FINANCE PRODUCTS IN A NON MUSLIM COUNTRY

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Abstract

The focal point of Islamic banking is adhering to the *shariah* law, which prohibits the utilisation of *Riba* (interest). This banking approach has recently grown in popularity not only in Islamic countries, but has also embryonic in non-Muslim countries. Although these methods is not totally new or revolutionary as it has been written and practiced during the renaissance of the Islamic civilisation, it has yet to establish itself and be tested in the modern world as compared to the conventional banking.

Muslims worldwide are still engaged in the "non-interest-free" system in financing their purchases especially those who are staying in the non-Muslim countries. There are many reasons why Muslims still engage in "non-interest-free" products. One of the reasons is the availability of Islamic financial product or non-interest bearing financial instruments offers by the banks. It is quite difficult to find such instruments, as most of them are not easy to get. To some extent, there are only few financial institutions which offer such products.

This article attempts to examine the attitude of Muslims staying outside the Islamic world, particularly in the U.K., towards Islamic finance products and will explain whether there is demand for such products from them.

It is found out that Muslims living in the U.K. are very much willing to change their practices from indulging in the conventional system into the new system – the Islamic financial system.

INTRODUCTION

Islam is founded upon the notion of Tawhid – a total commitment to the will of God. It requires total submission to the pattern of life revealed by God through the Quran and Sunnah. (Mills and Presley, 1999). Islam is a complete and comprehensive religion providing an exact answer to all questions spiritual and practical. The Quran, the holy book is the primary source of knowledge, while the Sunnah serves as the concept and guidelines, which have been used by Muslims since the glorious years of Prophet Muhammad S.A.W. With reference to these guidelines, Muslim scholars have taken an initiative, in the light of Shariah to develop a modern Islamic banking system.

The question is, what is the difference between the Islamic banking and conventional banking? It is commonly known that Islamic bank has strictly prohibited the use of or dealings with interest. Therefore, elimination of interest is the basic requirements of an Islamic economic order. To show the strictness in the prohibition of interest in Islam, There are quite a number of verses in the Quran telling the Muslims of the heavy punishments if one deals with interest. Allah Almighty says:

> *"O you, who believe, fear Allah and give up what remains due to you of interest if you are indeed Believers. And if you do not, then be warned of war (against you) by Allah and His Messenger, while if you repent you shall have your capital. Do not do wrong and you shall not be wronged". (2:278-279)*
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> *"But Allah hath permitted trade and forbidden usury".*
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> *Al-Baqarah: 275*
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> *"O you, who believe! Eat not up your Property among yourselves in vanities; But let there be amongst you Traffic and Trade by Mutual goodwill nor kill (or destroy)".*
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> *An-Nisaa: 29*

The prophet, peace be upon him, confirms the evil-nature of transactions by saying:

> *Allah has cursed the one who takes Riba, the one who pays it, the one who writes the contract, and the one who witnesses the contract (reported by Ahmed, Abu Daoud, Al-Nisai, Ibn Majah, and Al-Tarmidzi).*

Riba or interest can be defined as 'any increase or profit on a loan which has matured, in return for an extension of the maturity date, in case the borrower is unable to pay, and any increase or profit on the loan at the inception of the loan agreement. Both forms of usury or *Riba* is prohibited under the *sharia*' (The Islamic Fiqh Academy)

There are many justifications for the prohibition of interest in the financial world. Amongst others are that the creditors are not subject to any form of risk. Since Islam teaches their followers to be fair and just, both parties should be exposed to a certain elements of risk. Secondly, interest will encourage the capital owner to remain idle (sleeping partners) and not engage in more productive activities such as trade, agriculture and industry (Al Yousif, 1998). Al Yousif (1998) also mentioned that interest would weaken the cohesion of the society by expecting an easy return on the loan rather than giving it based on charity. In addition, most of the creditors are rich and most of the debtors are poor. Therefore, by imposing interest it will make the debtor poorer as they have to pay back the principal as well as the interest. This will result in a wider gap between the two classes and increase the inequality of income.

In order to eliminate the use of interest, Islamic financial intermediaries or Islamic banks have to play a very important part to create a non-interest mode of financing. Ahmed (2000), stated that Islamic banks are institution that extends all types of modern banking services within an Islamic framework. Thereby the Islamic banks must be directly involved in business on the principles of sharing profit and loss in order to ensure social equity and justice among Muslims as a way of financing. In addition to that, Ahmed (2000) also mentioned that the Islamic bank, just like the other banks, is in the business of management of money. However, the Islamic banks also have responsibilities to perform a socially function in transferring financial resources according to the Islamic framework.

According to the Organisation of Islamic Conference (OIC), the definition of an Islamic bank is: "a financial institution whose status, rules and procedures expressly state its commitment to the principle of Islamic Shariah and to the banning of the receipt and payment of interest in any of its operations".

Given this definition, practising and devout Muslims should not be at all affiliated to the conventional banking system. Therefore the demand of Islamic finance products should be enormous, exceeding the supply especially in a non-Muslim country such as in the U.K. However, whilst there are demands for such products, it is safe to say that it does not reflect the total demand from the Muslim community. Many Muslims still engage in "non-interest-free" financing for their purchases especially those who are staying in the non-Muslim countries, not because of being uncommitted to the teachings of Islam or simply being irreverent, but for the reasons of the availability of Islamic financial product or non-interest bearing financial instruments offers by the banks. It is quite difficult to find such instruments, as most of them are not easy to get. To some extent, there are only few financial institution offers such products.

The next question to be asked is whether the Muslim consumer would switch from conventional banking to Islamic banking if there are such products offered by local banks in the U.K.? Would Muslims in the U.K. embrace the idea of financing their businesses through Islamic financing system although it would not be as attractive financially as the conventional system just to adhere to the *shariah* laws?
Before these questions can be answered, the U.K. Muslims have to be scrutinised.

THE MUSLIM POPULATION IN UNITED KINGDOM

In 1986, from a private survey, it is estimated that the Muslim population in Britain has reach 936 000 people compared to the survey in 1981 which only estimates 690, 000 people. This figure, shows the number of Muslims in the U.K according to their origins (Table 1).

Table 1: Muslim Population in the United Kingdom

Country of Origin	Population
Bangladesh	64 000
India	84 000
Pakistan	357 000
Malaysia	30 000
Arabs	121 000
Iran	50 000
Turkey	21 000
Turkish Cypriots	50 000

East Africa	99 000
Nigeria	25 000
Others	27 000
Total	**928 000**

(Taken from Nielsen 1992 p.41)

is clear that the vast majority of immigrants are from a Muslim background, the ub-continent or specifically from Pakistan, both West and East, and Bangladesh (Nielsen 1992). The reason for such an increase in the population is because of ngs in the labour market in Britain and better education opportunities. However, ainly prior to 1962 when the entry into Britain by citizens of British colonies and nwealth member were unrestricted to enter into United Kingdom.

The increase in the Muslim population can also be measured by the increasing of registered mosque as places of worship. In 1963 there were only 13 mosques ed to Registrar General and the number increased to 338 mosques in 1985 n 1992; 1999). The increase in number of mosque is resulted from the passing of ion of bringing family from the country of origin to Britain (Table 2). The table that before 1975, the number of registration is less compared after 1975. The for this sharp increase in the total of mosques is partly because of the effect of the l wealth of certain Muslim countries. However, there are only a few mosques built il money, whereby the rest are from city centre development. There are quite a r of houses that have been converted into a mosque, where they expected to e such support (oil money) but failed to receive it. Several government departments that the total number of mosque is actually more than 338 since some of them are egistered with the Registrar General (Nielsen 1999, pp. 16)

In Muslim communities, a mosque can be considered as an important place as t of the activities are centred at the mosque. Therefore the number of mosques can be her source of information or an indicator for the number of Muslims in the area. If number of mosques is high, there is a probability that the number of Muslims has also eased.

It can be concluded that the number of ethnic minorities in Britain is increasing d expanding. In years to come, there is a possibility that the number of ethnic norities will be at par with the Caucasians.

Table 2: Annual Registration Of Mosque 1966-85

Year	No. of Mosque	Total
1966	5	18
1967	4	22
1968	9	31
1969	7	38
1970	11	49
1971	8	57
1972	8	65
1973	8	73
1974	8	81

1975	18	99
1976	20	119
1977	17	136
1978	21	157
1979	17	174
1980	29	203
1981	31	234
1982	21	255
1983	22	277
1984	31	308
1985	30	338

(Nielsen 1992 – pg.45)

ISLAMIC FINANCE IN THE UK

Although Islamic banks have made major achievements and developments over the years, the major challenges they face should not be ignored. The challenges may slow down certain developments and innovation given that the Islamic banking and finance have to comply with the principles of *shariah*. Thus the challenges should be critically analysed in order to improve services as well as the product of Islamic finance.

The main challenges faced by Islamic banking are the limitation of financial instruments. The Islamic banking system has very few acceptable investment contracts to choose from. Compared to the conventional system, the Islamic system is confined to short-term, low risk investment instruments, which are normally in the form of trade financing for inventory through the mark-up contract or the *Murabahah* (Vogel, 1998). Although Islamic banking is constantly referred to by many practitioners and academic scholars as profit sharing finance, the major type of financing used by the Islamic bank is the mark-up based financing (*Murabahah*). This shows that the main modes of financing, the *Mudharabah* and *Musharakah* are not as popular as the mark-up based financing. More than 80 percent of the banking practices of Islamic banks are done on the basis of *Murabahah* (Iqbal, 1998).

Asymmetric information and moral hazard are the two main reasons why the use of *Mudharabah* and *Musharakah* were not widely practiced by the Islamic banks. Since the main mode of financing in Islamic banks is highly exposed to the two problem areas above; it is required that Islamic banks provide a way to minimise these problem and act fairly towards both parties when doing the business. Thus it has proved to be very difficult to introduce a system of contracts between the two parties. According to Mohsin Khan (2000), the Islamic banks have to develop a contract to keep the monitoring costs for projects at a reasonable level and eliminate the moral hazards issues arising when the lender and the investor have asymmetric information on the profits from the investment. In conclusion, even though Islamic banking and finance were often referred to as profit sharing finance, the major funds were obtained from the short-term mark-up deals. This deal produces a minimal or thin profit margin to support overheads and also to produce sufficient profit to satisfy the bank and the depositors.

Another challenge that Islamic banks faces is the degree of competition. There is no doubt that Islamic banking is expanding, consequently it has become more competitive than before. Conventional banks around the world have also started to offer Islamic financial instrument to Muslim people, especially those living in non-Muslim countries. HSBC and Citibank are two major examples of conventional banks that offer Islamic financial products. These banks have set up a department dealing specifically with Islamic financial instruments that have a separate 'windows' in their operation. In terms of brand and marketing, these banks are in a better position to introduce new financial products compared to new entrants such as the Islamic banks (Warde 2000).

Islamic banks face difficulty in developing new instruments as they are hampered by religious constraint. Even if they manage to introduce a new instrument, it will take a considerable time before it will be used. This is because there are sometimes gaps in communication between the bankers and the scholars regarding different perspectives or views towards the Islamic banks operation (Wilson, 2000).

In the case of the United Kingdom, there is an increasing number of non-financial institutions already supplying financial instruments as a result of the government lowering the entry and exit barriers in the market. Well-established retailers such as Tesco and Sainsbury provide their customers with financial services such as loans and insurance. This phenomenon has introduced competition for financial institutions as more non-financial institution players have entered the market providing the same services (Naser, Jamal & Al-Khatib, 1999). As a result from this economic liberalisation, competition among domestic players has increased and it has opened up markets to the entry of foreign competitors (Wilson, 1999 & 2000). Now Islamic banks face competition not only from the conventional banks but also from non-financial institutions. This has increased pressure for the Islamic banks and they therefore have to reconsider their strategy in order to stay competitive and survive in the future.

The third challenge faced by Islamic banks is their relationship with the regulatory authorities. The importance of this issue is concerned with the supervision of banks following the bank crises faced by the banking industry for the past decades. According to Mohsin Khan (Khan, 2000), the Islamic financial institution needs to establish a strong legal system. He also mentions that there is a lack of well-defined regulatory and supervisory framework that look specifically into licensing requirements and prudential regulations, including minimum capital and liquidity standard.

This is especially true in the case of Bank of Credit and Commerce International when the regulatory authority failed to define the nature of business the organizations are conducting. This led to the collapse of the institution and a large loss to depositors; above all gave a bad impression to Islamic financial institutions as a whole. Thus the projection of the true image of Islamic banking will be tarnished and the idea of it to be accepted internationally will be laid on the line (Qayum, 2000). Financial fraud in the guise of Islamic banking has also thickened the image of non-viable in the eyes of investors. There are 70 cases reported in Pakistan and 50 in Egypt where the companies misappropriated the public money and fled the country (Lawai, 2000).

In order to prevent similar incidents from happening, the Bank of England has implemented tighter regulations on all financial institution operating in the United Kingdom. This includes the depositor protection scheme under the Banking Act of 1987, which clearly violates the *Shariah* principles of profit sharing finance. The problem with Islamic financial system practices is that the *Shariah* advisors will not accept guarantees of deposit value. It should be in the risk-sharing situation. However, the deposit protection scheme implemented by the Bank of England is not a complete protection scheme. The Bank of England will only cover 75 percent of the first £20,000 deposit. In terms of the operation, the Bank of England stresses that the key criteria for any institution accepting deposits must have adequate capital and liquidity, well-disciplined staff, a good business plan and the managers must be 'fit and proper' to conduct the business (Wilson, 1999 & 2000). This gives opportunities for the Islamic bank to develop instruments and an operating system that satisfies the requirement of regulatory authorities in the United Kingdom.

METHODOLOGY

Surveys were carried out in the area of Loughborough, Leicester, UK. Loughborough was chosen because of several reasons.

The first reason is, Loughborough has a quite a number of ethnic minorities, the majority of which are Muslims. Most of the ethnic minorities are from Indian sub-continent such as Bangladesh, Pakistan and Africa. The number of Asians, mostly students, is also growing. Most of them are international students enrol on programmes lasting more than a year, which in the meantime they may require some financial services. A number of 250 questionnaires were distributed among Muslims in Loughborough. The questionnaire was distributed among Muslims who are permanent residents in the United Kingdom. In order to differentiate between permanent and temporary residents, the researchers assumed that those who have bought a property in the United Kingdom can be classified as permanent residents. However the researcher also accepts Muslims staying in Loughborough who have intended to become permanent resident and buy a property in the town. For example, a number of students intend to stay and some of them have already bought a house in the town. People, who have purchased property as an investment, are included in the groups. The interviews were conducted in places frequently visited by the Muslims: Mosque, Halal shops, Bookstores selling Islamic books, Muslims gathering occasions, Halal restaurant, walking in the streets and interview those who wear skull caps and head scarves, and finally through Muslim addresses. There were 128 useable responses, accounting for approximately 51% response rate.

FINDINGS AND DISCUSSIONS

The response shows positive feedback to have Islamic mortgages in the area. Muslims who owned property with mortgages are willing to shift their current mortgages to the Islamic based ones.

Regardless of their knowledge of Islamic finance, 64.1% of total respondents were willing to close their existing account and open new account with the new Islamic institution and 31.3% would keep two separate accounts. Those who choose to keep two separate accounts are probably not confident with the service and would rather hold on to their existing account before shifting to the new Islamic bank. This concludes that the attitude of Muslims in Loughborough towards Islamic finance products is positive and encouraging. However, despite of the positive attitude, most Muslims in Loughborough did not have basic understanding of Islamic finance. With no financial firm offering Islamic finance in Loughborough, it makes it a lot harder for them to understand the operation of Islamic bank.

The levels of education did not contribute to the understanding of the Islamic finance. This is understandable, because most of the Muslims are not trained in the field of Islamic studies let alone Islamic economics or banking. 85.7% of respondents with higher degree qualification have never heard of Islamic finance, whilst only 27.5% respondents with secondary level qualification have never heard of it.

Hence it is important to educate the Muslim living outside the Islamic world with the knowledge of Islamic finance. This will initiate more interest in dealings with Islamic financial products and can create more demand for the products. Even though recently there are institutions like The Islamic Foundation in Leicester and Loughborough University offering Islamic finance courses, it would not be able to fully educated people in practice unless there is an Islamic financial institution in the area where they can deal with.

CONCLUSIONS

Attitudes of Muslims living in Loughborough towards Islamic finance products are of a positive one. Despite the limited knowledge of these products or of the Islamic financial system as a whole, they are willing to engage themselves in the Islamic financial system and products. Suffice to say that the demand for the Islamic financial products are high even outside the Islamic world, although it is naïve to generalise the attitude of the Muslims in Loughborough as representing the attitude of the overall Muslims in the U.K. let alone Muslims outside the Islamic world. Nevertheless, the notion that these Islamic financial products appealed to this community cannot and should not be discounted. The market of Islamic financial products is much bigger than just in the Islamic countries or country with its majority people are Muslims. However without proper channel of marketing strategy, the Islamic banks may face difficulties especially in attracting funds from the customer. Islamic financial institution may also need to pay more attention in educating the customer and giving more advice to them. Research and development is also essential to the development of Islamic banks in order to compete with the conventional bank. As such new financial products should be developed and can be accepted, not only to Muslim, but also to non-Muslim customers.

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