SMEs Behavioral Intention towards Usage of Financial Products: A Comparative Study of Islamic and Conventional Banks in Pakistan

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ARTICLE DETAILS

ABSTRACT

Purpose: This study has emphasized that understanding SMEs’ financial behavior towards Islamic/conventional banking products is prerequisite for policy makers and managers of banking and non-banking financial institutions.

Design/Methodology/Approach: A conceptual framework has been discussed in present study to understand financial behavior of SMEs towards adoption of conventional or Islamic financial products. Moreover, to identify the determinants of SMEs owner-managers behavioral intention which influence their financial decisions towards adoption of Islamic/conventional banking products.

Findings: Prior research highlighted that for growth and development of SME sector it’s vital to fulfill their financial needs. In Islamic countries like Pakistan a large population of SME owner-managers interested towards Islamic financial products, however, current study has presented a conceptual framework and after examining these determinants study will explore which factors influencing SMEs intention to adopt Islamic/conventional financial products.

Implications/Originality/Value: The study will help the global and Pakistan banking industry (both Islamic and conventional) to look into the areas which are ignored and need attention, which is necessary for the growth of both sector of banking industry as well as for the growth of SMEs.

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Introduction

As a vital facility to promote the business processes banking importance is continuously increasing. Both Islamic and conventional banks are playing an important role in entrepreneurship and business growth. Banks take deposits from general public and offer various financial products to entrepreneurs for enhancing their investment and operational
activities which are compulsory for a healthy economy. For the promotion of business activities banks operate as intermediary link between depositors of savings and funds seeking businesses as depicted in Figure 1.

**Figure 1:** Role of banks in business and entrepreneurship development  
(Source: Ashfaq Ahmed, Thesis 2006)

Experts and practitioners considered SMEs as nursery of entrepreneurship in economy, and meeting their financial needs is vital for development and growth of this sector and new venture creation. Growth and development of SMEs also dependent to a major extent on availability of suitable financial products in line with their specific needs and wants (Mohsin, 2015). Understanding SMEs’ financial behavior, therefore, towards various financial products is prerequisite for policy makers and managers of financial institutions. According to IFC, (2014), both firm level determinants and personal characteristics of owner-manager influence firms’ financial behavior to use/adopt financial products. Within SMEs, owner manager assumes the dominant role in the firm’s decision making process as against the large firms where decision making is more formalized and is less influenced by socio-psychological factors of the owners/shareholders. Thus, personal characteristics of owner-manager and his/her cognitive factors dominantly influence the firm’s use and adoption of financial products i.e. their financial behavior. On part of the banking sector, importance of marketing and understanding consumer behavior is rising in financial institutions in post 2009 financial crisis (Abdulsaleh, 2013). There is growing concern in banking industry both Islamic and conventional for understanding socio-psychological factors influencing owner-manager’s decision making in SMEs regarding use/adoption of various financial products (IFC, 2015).

**Consumer Behavior in Banking Products: Customer Intentions to Use**
Researchers explored the area of customer behavioral intentions in different contexts. Several studies conducted by the researchers on intention to use, behavioral intention and purchase intention in different countries. To understand all the aspects of this area, Fishbein and Ajzen (1975) came up with the Theory of Reasoned Action (TRA) in which they studied the relationship of attitude and behavior. The outcome of this theory was excellent and after that researcher’s considered intention as determinant of behavior (Gumel and Othman, 2013). Along with the appreciation, some researchers also criticize this theory. As they argued that volitional factors are missing which are important to predict the human behavior and also they found inconsistencies in the variable of subjective norms (Gumel et al, 2015). To fill this gap in Ajzen (1991) modified the theory with the name of Theory of Planned behavior (TPB). This study added the component of perceived behavioral control as volitional factor to predict the behavior of customer (Gumel et al, 2015). Theory also explained that intention influenced by attitude and behavior (Laksamana et al., 2013). Taylor & Todd, 1995 criticized the TPB as the multidimensional constructs are not included in the theory. In 1995, Taylor & Todd extended the theory of planned behavior with addition of multidimensional constructs with the name of decomposed theory of planned behavior. According to the Taylor and Todd, 1995 the decomposed model is more explanatory and understandable with respect to relationships of theory (Gumel et al, 2015). Davis (1989) developed the model with the name of Technology Acceptance Model (TAM) for the measurement of adoption and use of information system.
Most of the studies related to intentions used the theories of TRA and TPA and technology based studies frequently used the TAM model.

Within financial sector, these theories have been applied in research studies aimed at understanding customer intention to use/adopt various financial products. A number of studies, both conceptual and empirical, in the banking industry have studied customer intention to use in context of Islamic and conventional banking (Mian and Rizwan (2013), Thakur and Srivastava (2013), Shanmugam (2014), Nguyen (2014), Ya’gobi (2015).

Within conventional banking, many of these studies have analyzed consumer behavior in banking by studying customer intention to use and adopt various conventional banking products Thakur and Srivastava (2013), Cheng et al. (2013), Salciuviene (2014), Shanmugam (2014).

Along with the conventional banking, many studies also analyzed the consumer behavior by studying customer intention to use and adoption of Islamic banking products like home financing (Diminishing Musharaka), Murabaha, Ijara, and mobile phone banking. Echchabi and Olaniyi (2012), Gumel and Othman (2013).

Sun et al. (2011) test the influence of religion on Islamic phone banking services. The research model of the study is based on TAM and find out that non-Muslims and casual religious Muslims are more concerned about perceived usefulness but the devoted Muslims emphasized on perceived self-expressiveness and subjective norms. A study on patronization behavior of IB customers in Malaysia conducted by Echchabi and Olaniyi, (2012) utilized TRA as underlying theory of their research. Aim of the study was to find out the determinants that influence customer intention to adopt IB products and services in Malaysia. The study find out the significant positive influence of normative belief and motivation to comply on subjective norms and also positive influence of attitude and subjective norm on adoption of IB services. The study findings suggested that banks can consider three factors of normative belief, subjective norm and motivation to comply while convincing their customers towards adoption of IB products and services. By studying the model of TRA Hanudin (2012) conducted research on customer intention to use Islamic credit card in context of Malaysia. The study revealed that attitude, subjective norms and perceived financial cost are the primary factors in intention to use. A conceptual study on adoption of IB services conducted in Nigeria by following the TPA model finds out the relationship of consumer innovativeness with intention to use and the three other variables of attitude, social influence and perceived behavioral control. Innovative consumer have ability to adopt earlier than the others, as the customers with low innovativeness look for more information and advice from others (Gumel and Othman, 2013).

Above all studies on customer intention are conducted on international level. However, in Pakistan, the area of customer’s intention or specifically SMEs owner-manager behavior to use banking products has been studied by few researchers. To fill in this gap current study has explored financial behavior of SMEs towards adoption of financial products.

Financial Behavior of SMEs towards Banking Products in Pakistan: Ijara (Islamic) and Leasing (Conventional)

Small and medium enterprise (SME) is the key sector in developing countries for employment creation, poverty alleviation, fair distribution of income, development of private enterprises and growth of economy. Globally SMEs are providing 50 % of employment and 90% of businesses (IFC report, 2012). In Pakistan, SMEs are positively contributing in job creation, GDP growth, industrial productivity and export earnings and supporting sustainable growth (Khan, 2015). According to the report of SMEDA in Pakistan 90% of enterprises are SMEs and contributing in GDP nearly to 40% and 80% of employ in non-agricultural labor force (http://www.smeda.org).

State bank of Pakistan (SBP) paying attention towards this important sector, as the SME
financing (domestic) increased and stood at Rs. 8.051 billion as compared to last year Rs. 6.625 billion (SBP Quarterly SME finance review, 2021). The overall financing of SMEs facility-wise working capital showing the highest with Rs. 351.61 billion, fixed investment Rs. 130.45 billion and trade finance Rs. 42.04 billion.

In a comparison of conventional and Islamic banks, difference is not much as compared to previous years. The top of the list among banks are domestic private banks with share of Rs. 344.80 billion, public sector commercial banks Rs. 128.37 billion and Islamic banks stood at Rs. 38.23 billion even lower than previous year, as in 2020 it was at Rs. 40.16 billion (SBP Quarterly SME finance review, 2021). Statistics shows lower share of Islamic financing for SMEs as compared to conventional financing. It revealed that in Islamic banking portfolio SME is the most neglected sector.

Islamic banks are not trying to grab this opportunity as the SME population with religious thoughts are the target market for Islamic banks because only 11% SMEs are well-served with respect to financing and 22% SME avail the financing facilities from Islamic and conventional banks and less than 20% of their demands fulfilled by the banks. As well as 67% of SMEs are still waiting for the financing facilities, in which major portion is stick to religious beliefs (World bank, 2017).

Islamic banks are offering different mode of financing to SMEs like Musharaka, Murabaha, Ijara and Istisna as Islamic financing the major share of 58% based on Fixed-return mode of financing (Diminishing Musharaka, Murabaha, Ijara, Istisna and Salam) (SBP KAP, 2014). Two major products Murabaha and Diminishing Musharaka have 40.6% and 30.8% share in Islamic financing and the third largest product is Ijara. Conventional banks are offering long-term, medium term, short term financing and leasing. In Pakistan, CBs and other financial institutions are offering the leasing facility and are the core customers of SMEs (Murad, 2008). Both Islamic and conventional banks feel hesitant while financing to SME due to non-availability of documents related to business, tax, credit history etc. (IFC, 2015).

In Pakistan, owners of SMEs are based in three large cities Lahore, Karachi, Faisalabad, contributing 50% of total SME financing of country, these are mostly owners of medium sized enterprises. The IFC, (2015) report of Islamic banking opportunities across small and medium enterprises Pakistan revealed that only 11% SME owners are well served customers of IBs and CBs, out of 22% of SMEs who are able to access the finance facilities less than 20% are satisfied. According to the IFC report, 2014, 67% of SME owners/manager are not satisfied with the current financing options of banks and not getting any finance facilities. One of the reason behind this situation is strong religious beliefs of SME owners/managers, report statistics exposed that from last five to 6 years this issue is growing as 20 to 25% SME owners/managers have strong religious beliefs and they are getting form financing but not satisfied. Although, it’s an opportunity for IBs to increase their customer portfolio but IBs are not exploring the SME sector, either not able to provide the required products and services or not giving attention to this sector. According to the statistics of SBP report, 2014 SME is the most neglected sector in IBs as financing ratio to corporate sector is 71.8% and to SMEs is only 5.1% which is very low. Researchers are not exploring this area as very few studies regarding attitude of firms towards Islamic banking and adoption of Islamic banking on firm level are available on international and national level (Gait, 2008). A study in Australian context conducted by the Jalaluddin and Metwally (1999) regarding attitude of small business firms towards profit/loss sharing methods of IBs. Results of study revealed that in this decision factor of religion is not relevant and other related the factors are interest rate, business risk and expected rate. Jalaluddin (1999), conducted similar study and find out with the non-Muslim respondents that profit/loss sharing method is an alternative in conventional banks is debt finance. The reasons for not obtaining the profit/loss sharing method were lack of product knowledge and terms and conditions of method. In Pakistan a study conducted by Ellahi et al. (2010) and concluded that 60% of SMEs are interested in Islamic financing, 35% prefer IBs because of religion factor and
removing 5% due to other reasons like service quality etc.

Available literature of marketing of financial services has grown exponentially, especially focusing on understanding consumer behavior towards various banking products of Islamic and conventional banking. Yet these studies have been focused only on individual consumer’s behavior and seldom have studied the buying behavior of business consumers such as SMEs. As has been discussed previously, owner-manager in SMEs assume a decisive role in the decision making process of firm. Yet their cognitive factors determining the behavioral intentions to use/adopt banking products are largely understudied in a cohesive manner. Both banking sectors Islamic and conventional and various financial institutions are providing wide range of products to SMEs globally as well as in Pakistan. But conventional banks are more competitive than the Islamic in financial market. SMEs constitute only around Rs. 38 billion of total loan portfolio of Islamic banks in which the three main products with respect to market share are Murabaha, Diminishing Musharaka, and Ijara (SBP, 2021). Studies on various banking products such as diminishing Musharka (home financing), Islamic personal financing, Islamic credit card, Murabaha, Islamic mobile banking services etc. in context of usage/ adoption are available. Yet there is seldom any study available that may explain consumer behavior in context of leasing/Ijara, which is the third largest product for SMEs in Pakistan.

To sum it up, this study seeks to analyze the cognitive decision making process of owner managers of SMEs and explain the impact of various socio-psychological factors of owner managers that influence their intention to use banking products such as leasing under Islamic and conventional banks in Pakistan.

**Research Questions**

The research problem described above needs to be translated into specific research questions that are to be answered by this research study. To examine the cognitive determinants of SMEs owner-manager’s intention to use Islamic and conventional banking products, following are research questions that are identified.

1. How does attitudinal factors (awareness, perceived risk) of owner-manager of SMEs his/her intentions to use Islamic and conventional banking products in Pakistan?
2. To what extent, subjective norms (religious beliefs, social beliefs) of owner-manager of SMEs towards Islamic and conventional banks influence his/her intentions to use Islamic and conventional banking products in Pakistan?
3. How does perceived behavioral control of owner-manager of SMEs towards Islamic and conventional banks influence his/her intentions to use Islamic and conventional banking products in Pakistan?
4. Are these cognitive determinants of SMEs owner-manager usage intentions same or different in Islamic and conventional banking in Pakistan?
Conceptual Framework

Figure 2. Research Framework

Prepositions

Preposition 1. Attitude positively effect SMEs owner-manager intention to adopt Islamic/Conventional financial products

Preposition 2. Awareness positively effect SMEs owner-manager attitude towards adoption of Islamic/Conventional financial products

Preposition 3. Perceived Risk negatively effect SMEs owner-manager attitude towards adoption of Islamic/Conventional financial products

Preposition 4. Subjective norms positively effect SMEs owner-manager intention to adopt Islamic/Conventional financial products

Preposition 5. Religious beliefs positively effect SMEs owner-manager subjective norms towards adoption of Islamic/Conventional financial products

Preposition 6. Social Beliefs positively effect SMEs owner-manager subjective norms towards adoption of Islamic/Conventional financial products

Preposition 7. Perceived Behavioral Control positively effect SMEs owner-manager intention to adopt Islamic/Conventional financial products

Attitude

Attitude is an individual’s assessment regarding impact of implementing a particular behavior or habit that result in either a favorable or an unfavorable belief. The unfavorable assessment hinder that intention, however, favorable assessment enhance the probability of performing behavior (Adam et al, 2016). John et al. (2014) explained attitudes as likes and dislikes of a person. Additionally, study confer that it depends on situation or object as attitudes may be neutral, positive, or negative. It is a psychological tendency that can be evaluated through a person favor or disfavor degree (Hsiao et al, 2013). Scholars also consider attitude as a complex construct because they hold a multidimensional view of attitude. The multidimensional view of attitude consist of three components, which are;

1. Affective (feelings of an individual toward some target evaluation);
2. Cognitive (refers to knowledge, beliefs, opinions and thoughts about the target)
Studies examined the determinant of attitude in various context such as Amin et al., (2011), study found attitude as the most significant determinant which influence consumer intention towards usage of Islamic finance. Similarly, Hanudin, (2012) examined the influence of consumer attitude towards usage of credit card by applying theory of reasoned action, findings of study revealed attitude as the key influential factor towards behavioral intention. Studies of Wahyuni, (2012) and Ya’gobi and Rad concluded the same results and highlighted the consumer attitude high influence on behavioral intention to use financial products and services.

**Awareness**

Awareness is an important determinant of customer intention, as it’s a first step towards adoption or purchase of products and services. Awareness is concern about and well-informed interest in a particular situation or development” (Tara et al, 2014). The concept of awareness attempts to explore that how customers establish knowledge of products and services and to what extent they are lacking of information about it. The importance of awareness to predict consumer behavior towards adoption/usage of products and services highlighted scholars in their studies. A considerable number of studies in various contexts explored awareness as dependent variable, also some examined direct relationship of awareness with consumer behavioral intention and actual behavior (Ismail et al., 2012; Ringim & Yussof, 2014).

**Perceived Risk**

Perceived risk plays an important role in trade and investment decisions of formal financing customers. Perceived risk has been defined as individual subjective expectancy of suffering a loss in pursuit of a desired outcome. Moreover, its consumer belief about the possible uncertain negative outcomes from any purchase transaction (Kamarulzaman & Madun, 2013). Additionally, in explaining consumers behavior perceived risk is a strong determinant, because consumers are conscious to avoid mistakes in order to maximize purchasing utility (Yahya et al. 2014).

**Subjective Norms**

Subjective norms are the social values and their pressure which effect decision making and behavioral intention of an individual. Moreover, it’s assessment of a person regarding social and religious pressure of whether to perform a behavior or not (Schlaegel & Koenig, 2014).

**Religious Beliefs**

Religion is a cause, principle, or a system of beliefs, practices held to with ardor and faith. Moreover, religion is a psychological connection and dominant emotional relationship to things (Mukhtar & Butt, 2012). Scholars considered religion as one of the critical factor which effect an individual perception while selection of financial products and services. Moreover, religiosity among other influential factors have highest rank which influence consumer behavioral intention (Amin et al, 2011; Sun et al. 2011; Tara et al, 2014). Also, in Pakistan 25 percent of SMEs owner-manager want to use Islamic products and services which must be according to Islamic rules and principles (IFC-2014). A current study in context of SMEs intention towards Islamic products highlighted the importance of religious obligation by postulating as attitudinal factor (Jaffar & Musa, 2013). Study suggested that to get favorable attitude of SMEs owner-manager towards financial products it’s necessary for financial institutions to follow Shariah principals.

**Social Beliefs**

Social belief is a perception of an individual regarding others that he/she believes should exercise (Amin et al, 2011). In a society, people take their decisions carefully because of social pressure, as for some decisions society appreciate an individual and for some he/she face criticism. It varies because in different cultures and societies people behave and react differently, sometime normal or sometime extreme reactions. Similarly, in Pakistan people are divided in various groups and societies, so, they follow and behave as per that circle rules and regulations. In line with current study, researchers also found that individuals behavior to adopt some product/service significantly affected by people surrounding them such as friends, family
and referrals etc. (Pentina et al., 2012). People usually appreciate those decisions which are acceptable as per their faith and values such Islamic financial products usage or adoption. Subjective norms or social influence have been found as the most influential factors towards adoption of Islamic financial products (Ali & Raza, 2015).

**Perceived Behavioral Control**

The construct of Perceived Behavioral Control (PBC) can be defined as an individual perceived control over the performance of a particular behavior (Ajzen, 2011). It’s a perception of ease and difficulty to perform the behavior (Schlaegel & Koenig, 2014). Though, self-perception varies according to self-efficacy of an individual and nature of study. Self-efficacy is an individual confidence in being able to perform a behavior (Adam et al., 2016). The PBC construct contains all psychological and external factors that can affect the intention of an individual towards the behavior (Chang & Zhu, 2011). Construct of PBC is exclusive as it serves in two case 1) predictor variable of intention and 2) direct determinant of behavior (Ajzen, 2011). It actually reflects a person’s beliefs about his/her control of the potential outcomes of taking any decision and the ability to overcome potential external constraints in the process. Additionally, if an individual have a high degree of control on his/her behavior then intention is sufficient predictor of the individual exerting effort and taking action to achieve goals.

**Conclusion**

Given the vital role of SMEs in inclusive economic activity and entrepreneurship, their needs and access to banking products is getting attention of policy makers and managers at of Islamic and conventional banks. This research questions posed in this study seek to better understand financial behavior of owner managers of SMEs towards Islamic and conventional banking products and thereby enhance banking sector’s marketing strategy. The existing literature explored that there is a tough competition between both Islamic and conventional banking in context of SME sector. SMEs are the key contributors in sustainable GDP and also essential for the growth of countries. Therefore, it’s necessary to find out the cognitive factors of SME owner-manager which effect their financial decision making while adoption of Islamic and conventional banking products in Pakistan. Study will explored the factors influence SMEs owner-manager behavioral intention towards adoption of conventional or Islamic financial products. Moreover, highlight the preference and interest of SMEs in selection of financial products in Pakistan.

**Practical Implication**

On practical front, major contribution of this study is that this area in not much studied in context of Pakistan and seldom study on cognitive factors of SME owner manager with comparison of Islamic and conventional banking is available in Pakistan. The study will also help the global and Pakistan banking industry (both Islamic and conventional) to look into the areas which are ignored and need attention, which is necessary for the growth of both sector of banking industry as well as for the growth of SMEs. As after understanding the financial behavior of SMEs banks can designed their products according to the needs and demands of SMEs. This study will also help the government as can identify the major financing issues facing by the most important sector of the country. Also help out the central bank of the country to work on new policies and procedures in order to make easy access of finance for the SME sector from both Islamic and conventional banks. As well as Islamic banks can target the SME sector population who are more influenced by the religion factor, also IBs can enhance their product range and modernize their systems. Conventional banks can also work on the products according to the demand and can swift their process of providing facilities in order to satisfy the consumer.

**Scope and Limitation**

The study focuses only the socio-psychological factors that influence owner-manager’s behavioral intentions to use Islamic and conventional banking products among SMEs. Firm
level determinants of SMEs’ use and adoption of various banking products are beyond the scope of this study. The study is limited to the small and medium-sized firm owner-manager cognitive factors in Pakistan, the corporate firms are not included. The study is exploring the banking industry both sectors Islamic and conventional in context of SMEs in Pakistan.

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