EFFECT OF CREDIT CARDS ON CUSTOMERS’ SPENDING BEHAVIOR: A COMPARATIVE ANALYSIS OF ISLAMIC AND CONVENTIONAL CREDIT CARDS

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Abstract

Purpose – The main purpose of this paper is to understand the attitude of Malaysian credit card holders towards spending and settlement behavior. It also attempts to highlight the effect of Islamic credit cards on the spending behavior of customers in comparison to that of conventional credit cards.

Design/methodology/approach – Data were collected using a structured questionnaire, distributed among the holders of conventional and Islamic credit card holders. A total of 200 questionnaires were distributed among the respondents in Klang Valley of Malaysia. The data collected were analyzed using Statistical Package for Social Science (SPSS). First, descriptive analyses were conducted followed by reliability tests and factor analysis.

Findings – The findings of this research revealed that there is no effect of religion on the usage of credit card whether Islamic or conventional. Further, it is also found that conventional credit cards outweigh Islamic credit cards. It might be due the fact that Islamic credit cards are new compared to conventional counterpart.

Research limitations/implications - Given that this research is quantitative, there is a need to embark on in-depth study (qualitative) to understand the effect of credit cards on customers’ spending behavior in much better way.

Practical implications – The results of this study give clear indications that there is a great need for the Islamic banks to enhance their credit card marketing in terms of the benefits it offers to the customers, particularly, the consideration to avoid riba in the transactions.
Originality/ value – This study is a novel attempt to test the impact of credit cards on spending behavior of customers along with the comparison of Islamic cards with conventional cards.

Keywords – Credit cards, spending behavior, Islamic banks, conventional banks, Malaysia

Introduction

Mobil Oil, USA card issued in 1914 is considered the first credit card used to eliminate the need for carrying cash. Meanwhile Diners Card issued in the 1950s was the first company implemented service for businessmen to purchase meal on an expense account. Thus since the early 1950s, credit card has been widely used especially in developed countries as payment system for transfer of funds. It has become a norm for everyone to purchase an item without the need for carrying large sum of paper money. Payment for goods and services through internet using credit cards has also gained acceptance worldwide. By 2004 the average consumers in United States of America held 5.5 million of credit cards while and average consumers in South Korea held 3.6 million credit cards (Yahoo, 2005).

In Malaysia the credit card lending is growing at a compound annual growth rate (CAGR) of 50.4% per annum for 7 years from 2005 to 2012 (BNM, 2012). One of the significant contributions to this trend is that Malaysian consumers have displayed a positive move towards credit card facility. They are able to grant loans for themselves. Meaning, they can obtain funds easily via credit card than personal loans with many documents formalities being relaxed. As a result, credit cards issued from January till February 2012 rose to 10.1 million (BNM Report, 2012).

The last two decades have witnessed increasing proliferation of Islamic credit card, which different from the conventional Credit card which operates on loan basis and charges interest. Islamic Credit Card provides the same benefits as conventional Credit card but is fully compliant with Shari’ah principles. Over the years, Islamic credit card has become attractive to both Muslims and nonMuslims.

Credit cards have several positive effects on customer spending behavior reaping for them many advantages and benefits. For instance, the secure mechanism of credit card payment has gained trust and popularity worldwide. On the other hand, even though it has become a normal practice to own credit cards for variety of reasons, its impacts are still questionable both in developed and developing countries. These cards also have several negative effects such as for example default, fraud, overspending and lack of awareness. Studies show that these effects have multiplied in size especially from the early 2000s.

The significant growth of credit cards as an easy paying instrument has resulted in an undiscerning expenditure by customers with numerous impacts. Arguably, one of the major culprits for the ongoing financial crises is the extensive grant of credit to the people. It was reported that the next financial crises could be caused only by the compulsive buying nature of credit card (Business Week, 2011). The early signal of the impact of credit card is excessive buying behavior which compels customers to purchase out of their common needs. Relaxed source of obtaining credit and obsessive
purchasing without any control has created various concerns such as inflation due to excessive shopping and thus over leveraging of debt (BNM Report, 2010). Many Malaysian consumers have shown changes in their behavioral pattern. Since credit card encourages reliable and independent usage of credit by cardholders to meet their future consumption in advance; this has given rise to debt default by indiscipline users. Hence, excessive debt can trigger excessive default rates and writing off capital which finally can result into the vulnerability of the financial system and the stability of the economy (Zafar U et al, 2010).

In Malaysia, the credit card lending is growing at a compound annual growth rate (CAGR) of 50.4% per annum in the past 7 years since 2005, which is the major concern of regulatory authorities to lower down the debt ratio. In the year 2009, it was reported that out of the 11.41% of the total loans outstanding, consumer credit accounted for 1.35%. Out of this total loan, nearly 6.43% of the amount outstanding has been written off as non-performing loans. There is yet a shocking trend of increasing number of credit card holders finally going through a bankruptcy stage (Bank Negara Malaysia, 2011).

A few studies have examined the customers’ attitude their spending behavior when using credit cards. Most of these studies, however, have focused on the customers’ behavior of conventional credit card holders. Their focus has not taken into consideration the popularity and common usage of Islamic credit card by the public as an alternative to conventional credit card, given the wide acceptance of Islamic banking practice in Malaysia. It would be interesting to see the pattern of behavior among the users of Islamic credit cards. It is anticipated that these users will be highly disciplined since Islamic banking products are based on ethical values. This study therefore, seeks to investigate whether the excessive buying behavior or compulsive purchasing trend via credit has also penetrated into the Islamic credit card holder and if it is in the affirmative, then to what extent do such behaviors of Islamic credit card holders differ from their counter parts, the conventional credit card holders. This study therefore aims to achieve the following salient objectives:

1. Investigate the effect of Islamic and conventional credit cards on customer spending behavior
2. Conduct a comparative analysis on the effects Islamic and conventional credit cards on customer spending behavior

This study is considered a pioneering work in the area of Islamic banking in that it offers comparative empirical analytical study on both conventional and Islamic credit card holders in Malaysia. The findings of the study are expected to be significant not only as an additional stock to the existing literature but also to policy makers i.e., regulators, various stake holders like shareholders, bank managers, and Muslim Ummah in general. The Shari’ah compliance aspect of the study is relevant to both types of consumers. Regulators can make use of the quantitative and qualitative aspects of credit card spending behavior to gauge the future financial indebtedness of the public.

The paper is divided into five sections including the introductory section. The second section reviews the related literature on the subject. The third section discusses methodology used and the fourth
section presents the results and their discussion. The final section concludes the study and makes suggestions for future research.

Review of the Related Literature

The Effect of Credit Card on Economic Agents

Credit card seems to replace cash as a medium of exchange. According to APACS’s annual report (2004), approximately two third of adults have credit cards and, owning multiple cards has become a phenomenon in the UK. Credit does raise the standard of living, help in managing emergency cases, ease customers spending and increase expand market for business (Mishler and Cole, 1998). There are eight reasons why people hold credit card: superior point’s scheme, superior pricing, designation of credit card, promotions and offer, loyalty towards bank, prestige, credit limit enhancement and facilitates debt management, (P. Gerrard, S. Worthington and James F. Devlin, 2006). According to HESSA (2009), credit card encourages people to borrow more but create problems in the future as well. If an individual is not able to pay promptly, it has an impact for him or her to get a job, take other loan or automobile insurance because creditors tend to check customer’s financial history. Consumers’ way of life has been affected because of the philosophy, “buy now and pay later”. The behavior towards credit card use differs from one customer to another depending on their level of responsibility (R.A. Feinberg, 1986). According to Galanoy (1980), credit card has a correlation with spending. Customers will spend more if they have credit cards (Burman 1974; Mathews and Slocum 1968). Furthermore, the use of credit cards as main medium of exchange the vibrancy of credit card markets in developing countries are some of the factors influencing the credit card industry (Sook Yee Choo 2005).

Perception of society towards Islamic banking

Islamic Banking function is the same like conventional banking. However the difference between them is that conventional banking products are interest based. The demand for Islamic banking in Malaysia started since 1962 upon the establishment of Tabung Haj as non-bank financial institution. In July 1983, the first Islamic bank, Bank Islam Malaysia Berhad (BIMB), was established and the Malaysian authorities thereafter introduced an Interest free banking scheme. Over the years, Islamic banking in Malaysia has offered several products and services to customers. These products of recent have included Islamic credit cards. Some Islamic banks market shares have been increasing tremendously for few years after offering Islamic credit cards using a combination of contracts such as Bai al Inah and Qard Hassan, (Mohd Dali and Mohd Rais 2006). Islamic bankers and shari’ah experts need to rethink of their current approach when developing new Islamic banking products and they should be able to offer more authentic and Islamic financial products since the decision to legalize the bay’ al-Inah demonstrates such pragmatic orientation, (Amir Shaharudin n.d).

Conventional and Islamic Credit Card
The rising income and the increase in the purchasing power of the household are among the most significant factors increasing demand for credit card facilities from 1980 to 1999 (Kara et al, 1994). There has been a push towards the supply of consumer finance that includes personal loan, house mortgage, credit cards and auto loans due to increased liquidity of banks. In Pakistan, it is stated that consumer-financing forms more than 25% of the total private sector credit (Economic survey, 2006-2007). According to H.Kazmi, (2007) the mortgage loans and credit card debts have the highest growth during the last couple of years. Consumers have different incentives searching for lower interest rate terms and different motives for holding cards, (Kim, F. Dunn, and E. Mumy 2005). Some Pakistani consumers need proper segmentation since there are different explanations for the use of credit card. The highest default within the consumer portfolio increased from 1.4 percent in December 2006 to 3.7 percent in March 2007 as the gap between the consumption and saving is increasing at the expense of financially insecure customers, who are unable to make the payments and have to pay penalties, (Ghani 2007). Islamic credit card offers more value of money, offer low penalty rate, free bonus point, more looks fancier and gives annual fee waiver. Charge card, is one of types of Islamic card where its convenience to the buyer, security wise and cost effective are considered to benefit the user and customer has to pay all the debt in one shot (Mohd. Ma'sum Billah, 2001). This situation is unprofitable for the bank that only charges membership fee for the service provided (Middle East Banker, 2005). According to Alhassan G. Abdul-Muhmin (2007). Credit card ownership in Saudi Arabia is higher among women even though it is positively related to income, education, age, and attitude toward debt.

Customer Perception towards Islamic Credit Card

Islamic scholars differed in their opinion on the precise term for credit card, whether it is ‘qard’ or ‘I’timan’. Eventually, the Islamic Fiqh Academy later agreed on the precise definition of the credit card in the year 2000. Islamic Fiqh Academy has defined it as a document and is called it as “AlI’timan” as referring to the credit card transaction in Islam instead of Al-Qard, (Ruzian Markom 2011).

The Islamic credit card adds value and attracts customers, both Muslims and non-Muslims due to its features and beneficial services to the customers because of the concept, application and low cost compared to conventional one. There is a significant difference between Islamic credit card in terms of buying goods and rendering services. Gradually, the demand for the Islamic Credit Card is increasing because of the interest free elements and its compliance to Shari’ah rules and regulations. People start shifting their credit card preferences towards Islamic Credit Card. This has forced conventional banks to improve their product to satisfy the customer’s needs and preferences (Mohd Dali et al. 2008). According to Phoon (1993), Islamic banking product is still new and there is a mixture of curiosity and skepticism among customers. Getting more people to use Islamic Credit Cards can pose a stiff challenge to conventional credit cards which is competing by offering attractive benefits and incentives (Kaynak et al, 1995). Islamic banking should review its strategic planning in order to achieve its missions and objectives by focusing on their target market, study the external opportunities, threats, increase their promotion strategy to enhance the customer’ awareness as
well as internal strengths and weaknesses to get more customers (Norudin & Zull Nikli, 2005). According to Adil Manzoor Bakhshi (2006), there is a bank in UK which offers credit card that is Shari’ah Compliant even though the Muslim population in UK is two million. In fact, Muslims need to look forward to such products that are in line with their belief. It is argued that credit card transaction is not the best way to generate profit and Malaysian IFIs should oversee business operations and the models should be reviewed from time to time towards more Shari’ah inspection and audit (Azman Mohd Noor and Rafidah, 2010). Islamic Credit card holders have correlation with religion and their interest to go into debt seems to be tamed compared to conventional credit card holders (Nazimah Hussin 2011).

Hypotheses

Following the above discussion, this study has developed hypotheses in line previous findings in the literature. The General business level hypothesis states that wherever the benefits and values are achieved at lower expenses by the consumer, the higher the prospect of its marketability and turn over. On the other hand, in a traditional Islamic economics perspective, higher Shari’ah compliance would force the customer to select the same product even at a high cost. Thus, in view of this ideal situation, it is easy to construct the hypotheses as follows:

H1. There is a significant association between conventional credit card holders and Islamic credit holders spending behavior across Malaysia.

H2. There is affirmative relationship between the psychographic variables and the spending behavior attitude of conventional and Islamic credit card holders in Malaysia.

H3. The Islamic credit card holders enjoy better benefits than the conventional credit card holders.

H4. The Islamic credit card holders are in better place in terms of the conceived risk involved in the operation than conventional one.

Research Methodology

The sample for this study was selected from among a population in Klang Valley representing people age 19 years old and above. According to Senator Datuk Raja Nong Chik Raja Zainal Abidin, Klang Valley has 6 million people representing 20 percent of Malaysia’s total population. The sample size is 200 respondents representing approximately 0.003 percent of the population which is around 6 million. Those who have career were represented as the respondents because they meet the required criteria, using credit card either conventional or Islamic. Based on the convenience selection criteria for each credit card were consisting of 64 percent female and 36 percent male for conventional and 40 percent male and percent 60 female for Islamic credit card.
This research purposely chosen Klang Valley area because the researcher believes that most of credit card holders living in this area represent the high-income group in an area characterized as business centre and some people would survive by using credit card as their income does not allow them to fulfill their needs. According to Household Income (2012), average monthly household income in Klang Valley has increased and stood at RM 5488.

A survey was conducted in order to get data from customers of credit card as the researcher understands that it is not easy to take their time as they are busy with their daily business activity. The structured questionnaires were developed based on literature review and objective of the study which contained Likert scale and are open ended questions. The open ended questions represent respondent’s demographic profile; gender, marital status, sex, income, age, education, career, race and reason for holding credit card, conventional and Islamic credit card. For the next section, all questions used are five-point Likert scale as “1 = Strongly Agree, 2= Agree, 3 =Slightly Agree, 4= Disagree and 5= Strongly Disagree”. These questions are meant to gather data on their spending behavior from items such as monthly income spent, benefits and quality service provided, risk and faith. The researcher believes it can measure card holder’s perception and action while using credit card.

In answering the questions, the respondents were assured that the researcher would not reveal the answers and their names and other responses would not be solicited. The respondents were been given almost 5 minutes to fill up the questions according to their perception. Some respondent were approached face to face and some through Google document online. The questionnaires responses gathered through online were 50 and the rest were through face to face. As it is not convenience for researcher to find respondents the researcher used Facebook and email by creating link to the Google document to ease the search for respondents.

The data collected were analyzed using the Statistical Package for Social Science program (SPSS). Descriptive analysis has been used as to compare the outcome from the two types of credit card. Factor analysis was also used in order to enhance the validity and reliability of the variables (Dusuki and Abdullah, 2006). The dependent and independent variables involved in this analysis included perception, benefits, perceived risk, quality and service and faith to spending behavior. Other analyses conducted are descriptive analysis, reliability, frequency distribution and Friedman test. The descriptive analysis provided a result of frequency distribution. The descriptive statistics provided mean and standard deviations for the interval scaled independent and dependent variables depending on the Likert scale given. The results would show whether the mean for each variables was high or low and the researcher analyzed the descriptive statistic of the customers on their perception for each item measured. Reliability analysis measured the stability and consistency of each variable.

Findings and Data Analysis

The respondents are sample from Klang Valley area holding credit card either Islamic Credit Card or Conventional Credit Card. A total of 200 respondents were collected whereby 100: 100 for each type...
of credit card. The questionnaire’s section of respondent’s profile gathered information in relation to gender, marital status, sex, income, age, better educated, career, race and reason for holding each type of credit card, conventional or Islamic credit card. From the data outcome the respondent were predominantly female for both type of credit card 64 female and 36 male for conventional and 60 female and 40 male for Islamic credit card. It is perhaps because of the majority of women’s population in the Malaysia.

Most of the respondent are married, 63% for Islamic credit card, 58% for conventional. One of the noteworthy factor is that most of the respondent are Malay constituting 87 Islamic and 71 conventional. It is also established that more than half of them hold above the undergraduate degree. The age profile varies with half of the total respondents ranging from 30-39 accounting for 43% for Islamic and 48% for conventional. It is followed by the range 20-29 which nearly accounts for 42% Islamic and 32% of conventional. Same goes to income. The highest type of holders are the one who receive income around RM3001 to 5000 and next highest is less than 3000 for both types of credit card. This may be reasonable as the holders are searching for best financial sources that offer great benefit and help them to buy luxury goods or to survive as they just got a job, not promoted to high level and having children.

The result reported that the private company servants represented the highest percentage of the respondents, which consisted of 63% for Islamic and 78% for conventional. It must be because of promotion from bank from time to time around the city or from the organization itself for example for those working in a bank; they have been offered to have a credit card as one of benefits since the interest for staff is low.

Majority of the respondents were well educated with 39 respondents for Islamic and 48 respondents from Conventional. This is a positive tendency that they understand the questionnaire given as the higher education level holders possessed the higher awareness and better understanding of the difference between both cards. There are 99% respondents holding Islamic credit card but 93% percent of them really use it. It means they are really eager to use Islamic credit card because they believe in its significance and the Shari’ah compliant aspect of it. But for conventional only 64% holding credit card but 60% of them are willing to use conventional credit card and the rest think about Islamic credit card.

Some of them still stick with conventional because of the long time period they had been using it, approximately more than 5 years without facing any problem, besides being easy to purchase and convenient to buy goods. One of the possible arguments in this regard can be the inability to understand the conceived risk involved in the operation of Islamic credit card which may obstruct the respondents to transfer it into Islamic mode of credit card. Some researchers even shared with respondents that Islamic bank has poor promotion and rumors says that some places such as hotel will cancel the transaction if the customers use Islamic credit card instead of conventional. We will look at the reason from the outcome of likert scale. Most of respondents, 66 percent wanted to use credit card because it is easy for them to purchase good. The same goes to conventional whereby 64 percent provided the reason to purchase goods and services.
The result of the descriptive statistics shows that both credit card respondents agree that credit is a common source of money: 37% agree for Islamic credit card and 48% agree for the conventional. Both types of respondents disagree that they spend more than 30% of credit limit to buy goods every month. While approximately half of both credit card holders agree to consume more and save less by using credit card. There is a balanced view from both holders who regard the card they hold as the best compared to the other.

Conventional holders enjoy the benefits of paying credit card after due date more than Islamic credit card since the result shows 68% for conventional holders and 56% for Islamic holders. Half of each credit card are happy with the benefits of their card and believe it acceptable worldwide since: 86% for respondents of Islamic and 80% for conventional. 72% of Islamic holders and 69% of conventional agree that their cards are useful during festival. Meanwhile 86% of Islamic card holders and 70% of conventional card holders believe their transactions are done quickly using credit card. 61% of Islamic holders and 53% of conventional holders agree their bank offer many rewards and discount. From these questions, most of Islamic credit card holders like the rewards given by Islamic bank while conventional card holders like the time of the due date of payment.

For the perceived risk it is slightly higher for conventional card holders than Islamic card holders in problems such as fraud. Some conventional card holders face those problems while using credit card. For example 42% of conventional holders agree that fraud cases threaten them to use credit card compared to Islamic credit card which is 38%. But conventional card holders believe their bank can handle the problem since 52% agree that the card is secured compared to 47% for Islamic card holders. 69% of Islamic credit card holders agree that they are unable to pay the debt compared to 45% of Conventional holders.

For quality and services, conventional holders are happier than Islamic credit holders since each item of the question ranks conventional card holders higher than Islamic card holders. For example; 62% of conventional card holders agree that they have been treated well by Conventional staff when they face problem compared to 50% of Islamic credit card holders.

In term of faith, it's quite surprising that the result shows that Islamic card holders and conventional card holders subscribe to their credit cards not because of religious consideration. Only 27% of Islamic card holders and 53% of conventional card holders agree they hold their cards due to religious conviction. Looking back at races, most of the respondents are Malays who are Muslims. They believe riba is involved in Islamic credit card as represented by 31% of the respondents and for the conventional card holders half of them know that interest is involved in their card. Few Islamic credit card holders believe that Islamic credit card has good reputation (28%) and in their best interest (35%). For conventional respondents, it is 42% and 59% respectively.

The result from Friedman test was also analyzed. The mean represents variables that have been chosen highest in dimension. The results show Islamic credit card holders spend less than conventional card holders since they notice that Islam discourage bad debts and loan. Islamic credit card holders agree that the benefits of Islamic credit card are quite good and conventional holders chosen natural as the mean is 3.26. For perceived risk conventional holders believe that the card
they are holding is risky, they score 4 on Friedman test compared to 3.85 for Islamic card holders that see less risk for fraud. In terms of quality, conventional holders feel that the service they get is better than Islamic holders. Lastly, both disagree that they are using credit card because of religious conviction as Muslim card holders believe that disguised riba do occur in their credit card especially Conventional. As a conclusion, the reason they spend money by using credit card isn’t related to religion but to benefits, risk and quality given.

Specifically, all the reasons discussed above reflect lack of understanding and information among the public about Islamic credit card. Hence, there is wider scope of educating the client about the service and product of Islamic banking in general and Islamic credit card facility in particular. This can be achieved only if the Islamic banking system courses are also included in the primary and secondary school level curriculum.

This study has some limitations. Firstly, the data for this study were collected from only one area called Klang Valley that is overwhelmingly led by Malay majority consumers. Hence the findings cannot be generalized to other geographical areas. Furthermore, the factors explaining the consumer credit spending are also beyond the scope of this research. Future studies should look into longitudinal research, as it can be used to measure the changes in the use of credit cards over time. Future research can also investigate further other factors that influence consumer behavior from the use of e credit cards.

Conclusion

With the extensive growth of Islamic banking in the Malaysian region as an alternative to the conventional banking, the consumer has wide option to choose for availing micro credit through credit card. Credit card is seen to exhort the consumer behavior towards excessive purchasing or compulsive buying. Islamic credit cards being recently introduced and marketed is seen to gear a competitive advantage over the conventional credit card (Mohd Dali 2010). Hence, this study provides a fresh empirical result to show the effect of Islamic credit card on consumer spending for both conventional and Islamic credit card holders. It is found that most consumers are ready to shift to Islamic credit card, with the exception of few who still believe in conventional credit card because of the long banking experience that is better equipped with proper channel of security management and its operation. The study shows that Islamic credit holders spend less than the conventional credit holders in the short run because the former acknowledge that Islam abhor excessive debt obligation. Hence, users tend to discourage bad debts and over loan obligation towards themselves. Islamic credit card holders agree that the benefits of Islamic credit card are quite good and the conventional card holders also see the same on their part. The conventional holders assume the perceived risk of fraud through hacking or any fault through the online payment mechanism far more than Islamic credit card holders do. In terms of delivering quality services, conventional holders show preference over Islamic holders. Lastly, Religious factor seems to be significantly absent in influencing the decision of the consumers towards selecting the credit card of their choice. Hence, the reason they spend money using credit card isn’t related to religion but to the benefits, risk and quality they avail.
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