

The Impact of Compatibility and Perceived risk on Customers' Acceptance of Islamic banking in Nigeria

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Abstract : This study reported the impact of compatibility and perceived risk on the acceptance of Islamic banking products and services among customers in Nigeria. A total of 401 returned and useable questionnaires were used for the analysis. The use of PLS-SEM technique was employed in analyzing the data. The result suggests that compatibility plays an important role in the acceptance of the products and service provided by the Islamic bank in Nigeria. Compatibility explained 36% variance of the acceptance of Islamic banking products and services. Perceived risk was found to have a strong negative effect on the acceptance of the Islamic bank products and service with 28% variance of the adoption being explained. The overall model was found to have a moderate predictive power.

Keywords: Compatibility, perceived risk, Islamic Banking, Acceptance, Customers

I. INTRODUCTION

Islamic banking is structured based on the underlying principles that are strictly *shariah* compliant and hence provide ethical banking atmosphere that banned all sort of ethically questionable activities. All its products, services and activities must be based on *halal* (*Shariah* permissible) point of view. It is necessary to observe and make sure all the transaction of Islamic banks is free from interest, and other undesirable terms of investment (Dusuki & Abdullah, 2006). Accordingly, activities involving liquor, Polk, alcohol, tobacco, and advertisement considered ethically offensive are out of the canopy in which the Islamic banking sheltered. Engagement and dealings with desirable products that possess the positive attributes that are environmentally friendly, socially desirable, ethically responsible and morally sound remain the pivot activities of the Islamic banking.

Furthermore, any activity that is obviously prohibited by, or contradicts the moral value system of Islam could not be financed by Islamic banking, for example financing a brewery factory, casino, club and any activity that is apparently prohibited or detrimental to the society (Dusuki & Abdullah, 2006). In respond to this, four principles or categories in accordance with *shariah* and which Islamic banks would provide in replacement of interest-based were summarized to as: 1. Profit and loss sharing principles, example: *Mudarabah* and *Musharakah*. 2. Fee or charged based principles, example: *Murabahah* and *Ijarah*., 3. Free service principles, example: *Qard-Hassan*. 4. Ancillary services, example: *Wadiah*. (Hasan, 2014; Kamarulzaman & Madun, 2013).

Islamic banking system was established in Nigeria by incorporating Jaiz bank Plc as a Public limited liability company in 2003, but commenced business in January 2012 after obtaining its license in 2011. As the standalone Islamic bank in the country, the Jaiz bank provides an array of financial services in accordance with the *shariah* provision which is compatible with the belief and values of quite a number of financially excluded millions of people in the country (Dogarawa, 2012). Within the short period of its operation, the bank was able to attain a break-even in 2014 as against the loss reported by the bank in 2012. The profit before tax reported in the 2014 accounting period N157.7m indicate the success of the nascent institution in the country. The bank is moving toward enhancing the economic development of the country Nigeria through their contribution to the nation's fiscal, and having presently employed over 400 staff (Annual report, 2014). The bank recorded a

growth rate of 24% in the year 2014 from ₦33.9b in 2013 to ₦42b in 2014 and the number of customers enjoying financing from the bank rises to 1076 in 2014 from 375 in 2013 (Annual report, 2014).

Gaining customer confidence is the expectation and desire of a company that provides product and services like Islamic bank; to achieve this, the products and services need to be structured and align to customers' values and belief. Those products and services that are compatible with the customers' values and belief are easily patronized as against the one that provides otherwise. It is difficult to convince or change one's view from using a particular system he is accustomed to, but it is easy when the new system or products and services proves to be more compatible with one's belief and values.

II. OBJECTIVE OF THE STUDY

The examinations of the extant literature shows that many variables were investigated with regards to their contribution to the acceptance of Islamic banking products and services (Abduh & Omar, 2012b; Amin, 2012; Amin, Abdul-Rahman, & Abdul-Razak, 2013; Echchabi & Aziz, 2012a; Mansour, Abdelhamid, Masood, & Niazi, 2010; Metawa & Almossawi, 1998; Naser, Jamal, & Al-Khatib, 1999; Thambiah, Ismail, Ahmed, & Khin, 2013). But these studies are mainly conducted in Asian, Middle East and European regions. In Africa particular in Nigeria such studies are scarce (Daud & Yussof, 2011). The few studies conducted in Nigeria were mainly on the awareness (Unegbu & Onuoha, 2013) challenges (Bello, 2014; Ibrahim, Malami, & Abdullahi, 2012; Imam & Zubairu, 2011) and viability of the Islamic banking in the country (Dogarawa, 2011; Yaqub & Bello, 2012). However empirical studies specifically involving the customers of the bank were limited. This study therefore deemed it important and timely to investigate the impacts of compatibility and perceived risk on the acceptance or usage (which is refers to adoption in this study) of Islamic bank products and services in Nigeria using the customers of the standalone Islamic bank in Nigeria, Jaiz bank Plc.

III. LITERATURE REVIEW

3.1 Compatibility

Compatibility is considered as an important factor in the studies of customers' adoption or usage of products and services, more especially those products and services that are considered new. Generally, compatibility is explained as the degree to which something new is perceived as consistence with the values, needs experience and belief of the users (Rogers, 2003). The products and services provided by Islamic banks, compared to those of the conventional banks, are considered new. Islamic banking is considered as a new idea by its users as the best way, methods and manner of conducting their financial transactions (Echchabi & Aziz, 2012a). Kotler (1994) posit that new products incorporate original products, products modification and products improvement. It also includes the products ready to be launch in to the market and those that are perceived as new in comparison to others by the potential adopters. Islamic banking as a new innovation is linked to adoption by potential customers who accept or reject the innovation, which means the success of Islamic banking defends solely on customers patronage (Yahaya, Yusoff, Idris, & Haji-Othman, 2014).

In the context of Islamic banking, compatibility implies to the extent to which Islamic banking products or services are consistent with consumers' needs, beliefs, values, experiences, and habits. This goes with the fact that individuals tend to align themselves with ideas which accord to their interests, needs, belief and existing attitudes (Rogers, 2003).

A research on Moroccans customers on the acceptance and usage of Islamic banking services by Echchabi and Aziz (2012a) found compatibility as a significant factor impacting on the customers' acceptance of the Islamic banking services. Similarly, Gerrard and Cunningham (2003) found that customers' adoption of online banking in Singapore was greatly influenced by this factor. Furthermore a meta-analysis conducted earlier by Tornatzky and Klein (1982) revealed that compatibility is widely associated with individuals' acceptance and usage of new products, services or idea. The more the products and services are compatible with the users' values and belief the more likely they accepted the products and services.

This has been proven by quite a number of studies that found belief, especially religious belief as a key factor to the customers' acceptance of the products and services. For example, considering the fact that Interest is outlawed by Islam; being belief mostly explain in religious perspective, which coincides with compatibility, has appeared as a great determinant of customers acceptance and usage of the Islamic banking and services. This study therefore, hypothesized that:

H1: Compatibility has a positive impact on the customers' acceptance of the products and service of the Islamic bank in Nigeria

3.2 Perceived Risks

The concept of perceived risk, generally used by consumer researchers, is based on consumer's perception associated with possible failure emanating from the uncertainty and adverse consequences of buying and or engaging with a product and services (Howcroft, Hamilton, & Hewer, 2007; Srivastava & Sharma, 2011; Straub, 1989). This means the fear of the negative outcome arising from the use of the product or a service which is expected to affect the buying behavior negatively. Furthermore Cox and Rich (1964) define Perceived risk as the nature and the amount of the uncertainty faced by the consumer in his effort to make use of a particular product or service. Risk and uncertainty were used synonymously even though variation between the two exists (Peter & Ryan, 1976). Whereas risk connotes known probability, uncertainty does not have a known probability of occurrence (Knight, 2012)

The risk is inevitably part of a business and hence, businesses as well as the consumers are faced with different risks profiles. Both the business and the consumers are therefore expected to take steps to identify, estimate the likelihood and consider how to manage the risk (Mirakhor, 2000). Islamic banking does not accommodate interest with conferred risk on one side at the detriment of the other. In compliance with *shariah*, trading is permitted but interest was banned and therefore, Islamic banks involve risk sharing in trade and investment and as such perceived risk is pertinent and is expected to play an important role in trade and investment decision of Islamic banking consumers. This is because the innovation considered or perceived by the adopters as rewarding and with less risk and uncertainty are more rapidly adopted compared to the more risky and uncertain one (Fliegel & Kivlin, 1966). In Islamic banking where the customer cannot foresee the consequence of their purchase decision and where the outcome is solely based on the prosperity of the bank related to its performance, the perceived risk is capable of affecting the customers' decision.

Kamarulzaman and Madun (2013), opined that sharing the risk of trading and investment is aligned to the principle of Islam. They maintained that money lender by participating in the business of the money-borrower has to assume the risk associated with the outcome of the business because in Islam, lender and borrowers' relationship supersede that of creditor-debtor relationship. Basically, business growth is tied to risk sharing which Islam always encourages without compromising the welfare of either party (Kamarulzaman & Madun, 2013). In the same vein, Ghayad (2008) maintained that, Islam allows the owners of capital a share in a surplus which is uncertain. Investors in the Islamic order have no right to demand a fixed rate of return. No one is entitled to any addition to the principal sum if he does not share in the risks involved. Giving the inevitability of risk in the business dealing of Islamic banking involving the customers mostly using investment account, the perception of risk is expected to play an important role in determining the adoption of Islamic banking.

In Islamic banking product dealing, there is generally little uncertainty associated with opening a savings or current account and consequently there no much effort required of the customers in monitoring its outcome (Howcroft et al., 2007). However with regard to investment account where the outcome is uncertain, the customers are exposed to the risk which is expected to play a role in customers' decision with regards to their engagement with the bank. Hence, this study hypothesizes that:

H2: Perceived risk has a negative impact on the customers' acceptance of the products and service of the Islamic bank in Nigeria

IV. METHODOLOGY

This study used a quantitative approach to test the acceptance of the Islamic banking products and services in Nigeria. A structured questionnaire was designed and administered to the customers of the standalone Islamic bank in Nigeria- the Jaiz bank Plc. in the four selected states in the northwestern region of the country. The customers of the bank in Kano, Katsina, Sokoto and Zamfara states were specifically sampled for the study. A total of 539 questionnaires were distributed, 443 were returned. 42 of the returned questionnaires were found incomplete and therefore exempted from the analysis. 401 of the returned questionnaire were found completed and useable for the analysis. The questionnaire was designed to the five point likert-scale ranging from 1=strongly disagree to 5= strongly agree. Partial Least Square- Structural

Equation Modeling (PLS-SEM) was used as the technique for the analysis. The use of Smart-PLS version 3.0 was employed and the output from the PLS algorithm and bootstrapped result were assessed.

V. RESULT, FINDINGS AND DISCUSSION

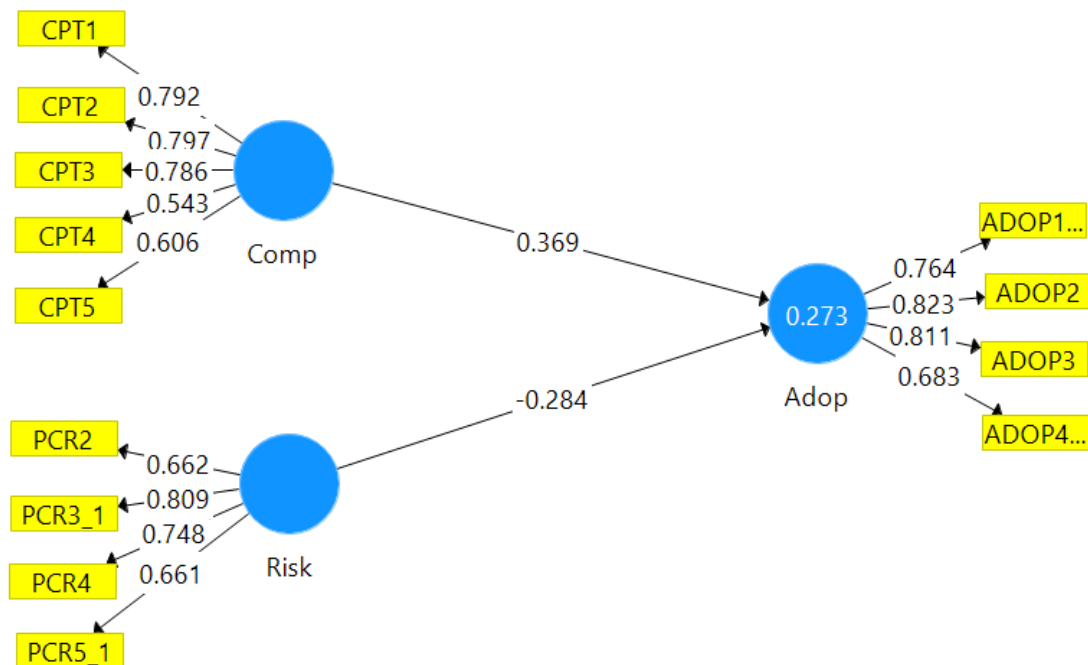


Figure 1: Path Model

5.1 Assessment of the Measurement Model

PLS algorithm was run to assess the reliability and validity of the measures. Initially, the items used for the model were 14. Compatibility and perceived risk constructs with five items each and acceptance which is refers to as adoption takes the remaining four items. However, after running the algorithm item PCR1 loading appeared very low and was deleted to get the required composite reliability and Average variance extracted (AVE) (Hair, Hult, Ringle, & Sarstedt, 2014). The rule of thumb provided that the average variance extracted should be 0.50 and above (Hair et al., 2014). As for the composite reliability the most widely acceptable minimum is 0.70 (Hair, Black, Babin, & Anderson, 2010; Hair et al., 2014; Nunnally, 1978). Table 1, shows that all the average variance extracted and the composite reliability values for entire constructs exceeded the minimum threshold of 0.50 and 0.70 respectively. This is an indication that internal consistency reliability was achieved. It also indicates that convergent validity was established (Hair et al., 2014).

Table 1: Reliability Assessment

Latent Construct	No. of Items	Average Variance Extracted (AVE)	Composite reliability
Adoption	4	0.596	0.855
Compatibility	5	0.508	0.835
Perceived risk	4	0.522	0.813

Source: PLS algorithm output

Discriminant validity assessment was done using two criteria; examining the cross loading of the indicators and comparing the square root of the AVE with the latent variable correlation (Hair et al., 2014). Firstly, the cross loadings examination shows that all the reference indicators loadings (figures in bold and italic, table 2.) are

greater than all their corresponding indicators loadings signifying that the constructs are distinct from one another (Hair et al., 2010). Secondly, using Fornell and Larcker criterion; the square roots of the average variance extracted (figures in bold table 3) were greater than the correlations of all the latent variables which is an indication of fulfilling the condition that the discriminant validity test is successful (Fornell & Larcker, 1981).

Table 2: Discriminant validity assessment

	Adoption	Compatibility	Perceived Risk
ADOP1_1	0.764	0.336	-0.275
ADOP2	0.823	0.369	-0.352
ADOP3	0.811	0.330	-0.298
ADOP4_1	0.683	0.339	-0.253
CPT1	0.360	0.792	-0.193
CPT2	0.352	0.797	-0.264
CPT3	0.335	0.786	-0.169
CPT4	0.168	0.543	-0.144
CPT5	0.320	0.606	-0.184
PCR2	-0.242	-0.239	0.662
PCR3_1	-0.322	-0.219	0.809
PCR4	-0.294	-0.165	0.748
PCR5_1	-0.243	-0.167	0.661

Source: PLS algorithm output

Table 3: Fornell-Larcker Criterion of Assessing Discriminant Validity

	Adoption	Compatibility	Perceived risk
Adoption	0.772		
Compatibility	0.446	0.713	
Perceived risk	-0.384	-0.271	0.723

Source: PLS algorithm output

5.2 Assessment of Structural Model

The structural model measures the overall predictive power of the model and it also measures the contribution of each independent variable and its impact in predicting the dependent variable. Tables 4 and 5 provided the result of the coefficient of determination (R^2) which presents the predictive power of the model. The R^2 value of 0.27 indicates that the model has a predictive relevance. This was considered as moderate in line with Chin (1998), who suggested that the R^2 values of 0.19, 0.33 and 0.67 in PLS path model signified as a weak, moderate and substantial influence of the model respectively (Chin, 1998).

Table 4: Coefficient of determination (R^2)

Endogenous variable	R^2
Adoption	0.273

Source: PLS bootstrapped output

Table 5 present the contribution of each of the independent variable in predicting the acceptance of Islamic banking product and services. The values under path coefficient are the variance of the dependent variable explained by each of the independent variables. Compatibility has the value of 0.36 indicating 36% variance explained of the dependent variable. The value of -0.28 implies that perceived risk is negatively related to the acceptance of Islamic banking products. It explains 28% variance of the dependent variable.

Table 5: Path coefficients

	Path coefficients	T Statistics	P Values
Compatibility -> Adoption	0.369	8.568	0.000
Perceived risk -> Adoption	-0.284	5.945	0.000

Source: PLS bootstrapped output

Hypothesis Testing

H1: Compatibility has a positive impact on the customers' acceptance of the products and service of the Islamic bank in Nigeria

Based on the result of the path coefficient, compatibility has the value of 0.36, t statistic= 8.56 and a p-value of 0.000. Hence the H1 is supported. This indicated that compatibility has a significant positive impact on the acceptance of the Islamic banking product and services among the customers in Nigeria. It signified that customers of the bank were attracted by the conformity of the products and services to their belief and values. They considered the products as preserving their faith and also satisfy the issue of human justice. This finding concord with the previous result in the literature where compatibility was found to play a significant role in customers' adoption of Islamic banking (Amin et al., 2013; Echchabi & Aziz, 2012a; Thambiah et al., 2013)

H2: Perceived risk has a negative impact on the customers' acceptance of the products and service of the Islamic bank in Nigeria

The result in table 5 above indicates the variance explained by the variable perceived risk as -0.28, t statistics=5.94 and a p-value of 0.00 this result supported the hypothesis 2 significant at 99% confidence level. It shows that perceived has a significant negative impact on the acceptance of the products and service of the Islamic banking in Nigeria. This means that customers are sensitive to the risk issue. The higher the perception of the risk the lower the customers are likely to continue their usage of the products. This finding is in agreement with the extant literature (Al-Fahim, 2012; Cunningham, Gerlach, & Harper, 2005; Zhao, Koenig-Lewis, Hanmer-Lloyd, & Ward, 2010).

Table 6: Effect size (f^2)

Variable	R-squared		f-squared	Effect size
	Included	Excluded		
Compatibility	0.273	0.148	0.17	Moderate
Perceived risk	0.273	0.199	0.10	Small

Source: PLS bootstrapped output

Thought the result and finding from the path coefficients indicated that compatibility and perceived risk both have a statistically significant relationship on the customers' acceptance of the product and services of the Islamic bank in Nigeria; the result was unable to present to us the effect size which indicates the impact of these variables on the dependent variable.

In this subsequent analysis therefore, the effect sizes with the predictive power of each of the independent variables were provided this indicates the impact of each of the independent variables on the dependent variable. An independent variable has a small, moderate and substantial predictive power when its effect size (f^2) is 0.02, 0.15 and 0.35 respectively (Cohen, 1988). The effect size is calculated by obtaining the R^2 of the endogenous variable through running the PLS bootstrapping the R^2 obtained is termed as " R^2 included" for its inclusion of all the endogenous variables. Then removing a particular endogenous variable and returning the analysis again, the R^2 obtained while excluding a path from the model is termed as " R^2 excluded" for its exclusion of one of the path. These results are subsequently used to calculate f^2 using Cohen's (1988) formula

$$f^2 = \frac{R^2_{\text{included}} - R^2_{\text{excluded}}}{1 - R^2_{\text{included}}}$$

Using the above formula, the effect size of compatibility and perceived risk as shown in the table 6 above are 0.17 and 0.10 respectively. This according to Cohen (1998) signified that compatibility is having a moderate

predictive power while perceived risk is having a small predictive power. This signifies the impact of these variables in the acceptance of Islamic banking products and services in Nigeria.

VI. CONCLUSION

This study provided the assessment of the impact of compatibility and perceived risk on the acceptance of the Islamic bank products and services in Nigeria. Each of the variables was found to be one of the factors that significantly impacted on the acceptance of the products and services provided by the Islamic bank in Nigeria. Whereas compatibility has a significant positive influence, perceived risk on the other hand has also a significant but negative influence on the acceptance of the products and services provided by the bank.

Notwithstanding the contribution of this study in furnishing us with the information on the extant of the contribution of these variables on the acceptance of Islamic banking in Nigeria, some of the limitations of the study include its failure to incorporate other variables that could also explain the acceptance of IBP. Future studies should therefore consider exploring the treasure of other variables like demographic variables of the customers and other personality traits like attitude and trust. Perceived government support could also be examined to see whether it has any impact on the customers' acceptance of the Islamic bank products in Nigeria.

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