CHAPTER 9

Marketing Practices of Islamic Financial Institutions

9.1 Introduction

The Shari'a provides a roadmap for every aspect of human life; it emphasises respect of God's creations and dictates a set of guidelines and values which govern business dealings, social interactions, and even human impact on the environment. Islamic values include justice, the equitable distribution of wealth, equity among humans, the fulfillment of contracts, as well as the prohibition of cheating and fraud.

The Islamic finance industry, which is governed by Shari'a, has become an integral part of the global financial system. It has been growing at an impressive compound annual growth rate of about 15% and has a presence in more than fifty countries, with assets estimated to surpass one trillion US dollars. However, this growth has not been without its problems; there are continuing criticisms of the industry: are products truly Shari'a-compliant, the dominance of Western multinationals in the industry (raising questions about objectives and authenticity of the industry), its neglect of serving the average Muslim customer, and the focus on products which do not employ profit-loss sharing (PLS) mechanisms. In this chapter, we highlight Islamic financial institutions' (IFI) marketing practices, determining their level of compliance with the ethical values of Shari'a.

9.2 Comparison of conventional and Islamic marketing

The American Marketing Association defines marketing as "the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organizational objectives."
Morphitou and Gibbs (2008) point out that marketing "seeks to satisfy a customer's need within his spiritual and physical well-being." [1] The authors point out that the conventional system is self-interested; it calls on the buyers to beware, in contrast with the Islamic system that obliges the seller to beware and to disclose all information in a sales transaction.

Islamic marketing is comparable to ethical marketing. It is governed by the Shari'a which provides a set of ethical rules that govern business and trade, and emphasises corporate social responsibility. Instead of maximising profits, Islamic marketing calls for truthfulness, trust, honesty, equity, mercy, justice, transparency, and fairness to every party involved in a transaction.

Alom and Haque (2011) point out that conventional marketing is based on "wants": the company wants profit and customers want satisfaction of their desires. In contrast, Islamic marketing is based on "needs" because Muslims are encouraged to consume moderately to satisfy needs rather than material wants, with a restriction that products and services should be Shari'a-compliant. [2] Elfakhani et al (2007) point out that in most countries there are no coherent standards of Islamic marketing regulations. [3]

Kotler et al (2009) comment that conventional marketing is criticised for "charging high prices, deceptive practices, high pressure selling, shoddy or unsafe products, planned obsolescence, poor services to disadvantaged consumers, false wants and too much materialism, too few social goods, too much political power, and creating undue competition."[4] In contrast, Islamic marketing calls for a balanced relationship between the seller and the buyer, and between material and spiritual needs, while respecting the wellbeing of others and upholding ethical values of the Shari'a. Fear of government prosecution restrains conventional corporations from activities such as false advertising or developing harmful products. Islamic marketing adds a second level of accountability which is before God.

[1] Morphitou, R & Gibbs, Paul (2008), "Insights for Consumer Behaviour in Global Marketing: an Islamic and Christian comparison in Cyprus", http://www.escp-eap.net/conferences/marketing/2008_cp/Materiali/Paper/Fr/Morphitou_Gibbs.pdf

[2] Alom, M and Haque, S. (2011) " Marketing: An Islamic Perspective" World Journal of Social Sciences, Vol. 1. No. 3. July. Pp. 71-81

[3] Elfakhani, S. M., Zbib, I.J. and Ahmed, Z. (2007) " Marketing of Islamic financial products" Handbook of Islamic banking, © M. Kabir Hassan and Mervyn K. Lewis 2007, Published by Edward Elgar Publishing Limited Glensanda House

[4] Kotler et al(2009) "Marketing Management-A South Asian Perspective" 13th Edition, Pearson Prentice-Hall, India, p.14.

9.3 The Islamic marketing mix

Marketing a product or a service requires decisions about four marketing aspects: product, price, promotion and place. These are referred to as the marketing mix. In what follows, we review the marketing mix that is acceptable to the Shari'a.

a. Product characteristics

Products have to be compliant with Shari'a, in terms of raw materials and processing, and they cannot be harmful to the body or the mind. Additionally, the sale transaction or contract has to comply with Shari'a. In an Islamic transaction the seller should be transparent by disclosing the product quality and revealing any defects to the buyer, whether obvious or hidden, otherwise the transaction would not be blessed by God.

Morphitou and Gibbs (2008) point out that the repackaging of a forbidden activity does not change its nature. For instance, in a murabaha transaction, an Islamic bank buys a property, marks up the price, sells it to a client for a higher price, and charges her/him to be paid in installment payments. Critics of the Islamic finance industry claim that the markup is actually riba repackaged as the markup; however the industry's defence is that both parties share the risk, unlike a conventional mortgage, and therefore this is not a valid criticism.

b. Price

Healthy competition is encouraged by Shari'a, and this does not prohibit the determination of a fair price in the market place through the forces of demand and supply, as long as the interests of both the buyer and the seller are protected. Unjust prices are considered to be illicit and deceitful by Shari'a. The Prophet Muhammad (Peace be upon him) is quoted as having said: "Those who cheat us, are not from us." The Shari'a also prohibits price discrimination among people, such as between Muslims and non-Muslims, or between bargainers who are good at negotiating a lower price and non-bargainers who just pay the price set by the seller, since it is considered as a form of riba.[5] Any increase in a product's price should be justified by an increase in quality or quantity. Moreover, price fixing through collusion agreements is forbidden (haram). Wilson (2006) points out that overcharging customers through a monopoly is condemned in Islam. [6]

c. Promotion

Shari'a prohibits gharar which was defined by Kamali (1999) as fraud, adding that gharar in transactions has often been used in the sense of risk, uncertainty and hazard. In any contract, the vagueness or ignorance of the characteristics of the objects of the contract is considered to be deceitful. [7]

The exaggeration in describing the traits of a product is prohibited by Shari'a because it can be deceitful. Promotion campaigns should be ethical and should not manipulate or pressure customers to submit to emotional factors, such as Shari'a-sensitivity, fear, or sexual appeal. Rather reason, preference and need should justify the decision. Islam promotes moderation in everything, thus false statements that promote reckless spending and extravagance are forbidden.

d. Place (distribution)

Shari'a prohibits exploiting people through hoarding goods for the purpose of raising prices. In addition, it bans price manipulation through controlling the distribution channel.

9.4 Market segments in the Islamic finance industry

JWT, the largest advertising agency in the USA, put the global Muslim consumer market at USD2.7 trillion, and projects its growth to USD30 trillion by 2050.[8] This creates huge potential for the forumulation of vast marketing campaigns. In the Islamic finance industry, the consulting giant Ernst and Young identified the preference for four classes of investors among Muslims, based on their degree of Islamic orientation:

a. Preference for conventional products: These investors choose only tried and tested conventional offerings regardless of performance and service quality. They generally do not have sufficient knowledge of the Islamic industry.

b. Value seekers: They will always select the best value investments regardless of Shari'a compliance. They typically invest with strong brand name players.

c. Preference for Islamic over conventional products offering the same return: Shari'a-compliance is secondary to return; it is considered a bonus feature. These investors typically seek strong brand names and competitive returns.

d. Islamic-only products: These investors typically sacrifice return for Shari'a-compliance, do not consider conventional investments, and favor pure Islamic investment providers.

Interestingly, Rushdi Siddiqui, Director of the Dow Jones Islamic Index, estimates that only 1% of Muslims would be interested in Islamic finance, since most are struggling with survival issues and are in the midst of poverty, famine, and civil wars. Siddiqui estimates that only 66% of Western Muslims would be interested in the Islamic finance market. This figure includes 33% who are interested in complying with Shari'a, and 33% who "would opt for it if the performance story and pricing was really sound." [9]

The industry has however been accused of targeting a very narrow investor segment. Most players have been violating Shari'a objectives by catering to the needs of wealthy Muslim investors only. There is a serious shortage on the supply side for serving average Muslims who are waiting for competitive Shari'a-compliant investment solutions.

9.5 Islamic financial institutions' marketing mix

Islamic financial institutions face several challenges in the area of marketing. They have to "re-invent the wheel" when it comes to developing new marketing strategies as they aim to mainly serve a new market segment, the "Shari'a-sensitive" customers. In addition, being an infant industry, they have to compete with conventional banks

[5] Saeed, M., Ahmad, Z.U. And Mukhtar, S.M. (2001) "International marketing ethics from an Islamic perspective: A Value Maximization Approach",Journal Of Business Ethics, 32: 127-142; Journal Of Retailing, 73(2): 171-183.

[6] Wilson, R. (2006), "Islam and business" Thunderbird International Business Review, 48 (1), 109–123.

[7] Kamali, M.H (1999) 'Uncertainty and Risk-Taking (gharar) in Islamic Law', IIUM Law Journal, 7(2)

[8] JWT (2007) "Study Reveals One of America's Biggest Hidden Niche Markets" JWT, New York, NY.

[9] Economics Week (2011) "Research and Markets; Islamic Asset Management Industry & Investment Analysis - Islamic Asset Management Industry Moves Beyond Borders & Religion", Anonymous, Atlanta: Feb 11, pg. 246

which have been around for centuries, have strong brand names and are heavily regulated.
In what follows we focus on the marketing mix, in order to assess Islamic financial institution's compliance with Shari'a.

a. Islamic financial product development

Strong competition from the conventional sector is blinding IFIs and diverting them away from their intended path. Some IFIs claim that they cannot afford to distance themselves too much from conventional products which are supported by strong brand names.

The growth of the industry has happened much faster than universities' ability to produce capable graduates.[10] This has meant that the Islamic finance industry is largely comprised of individuals that have a background in the conventional sector. An added concern is the difficulties in finding Islamic finance experts, technically proficient to work on complex, financial transactions.[11] The former group consists of people who are "inventing" Islamic equivalents of conventional financial products that are based on riba. This is a slippery slope because it leads to re-engineering or "Islamising" conventional products to make them Shari'a-compliant as opposed to identifying a customer need and developing new products that are based on Shari'a.

Jabaly et al (2013) criticise Islamic banks for acting as lenders rather than entrepreneurs, and point out that most banks have been focusing on non-PLS modes of financing such as murabaha, rather than PLS modes of financing (mudaraba and musharaka). Elfakhani et al (2007) note that Islamic banks during their formative years focused on short-term lending rather than supporting long-term profit sharing activities due to the "pressure" to perform and to offer viable alternatives to conventional products. The authors advise Islamic banks to "carry out their intended responsibilities to fund longer-term projects" now that they are more stable and mature.

According to Attallah and Ghoul (2011),[12] some Islamic financial products "may be Shari'a-compliant in form but not in substance, and may be consistent with the letter but not the spirit of Shari'a." The same source argues against "Islamic" products which might involve indirect riba, deception, exposure to leverage, a high probability of a loss, risk amplification, speculation, and a delinkage with real economic activities. The authors opine that innovation is needed and encouraged in Islamic finance as long as Shari'a spirit is preserved.

Ghoul (2011) further argues that the lack of standardisation of Shari'a interpretation and the absence of a globally recognised and centralised Shari'a certification body has been causing chaos in product development in the Islamic finance industry and impeding its sustainable growth.[13]

On the other hand, there have been some criticisms of western financial institutions' dominance of the product development effort.[14] Raphael de Ricaud, Head of Islamic finance at Rothschild, believes that Islamic finance has lost a bit of its originality and peculiarity, and is paying the price for being appropriated by conventional banks "having been taken over by conventional banks."[15] Indigenous IFI's are being urged to assume full responsibility for product development.

We now discuss briefly some violations of Shari'a tenets that are prevalent in Islamic financial product development:

- **Combining two contracts in one product:** The combination of contracts is a common mechanism in structured product development in Islamic finance. Its concept raises legal concerns due to legal pronouncements from the Prophet that forbid two contracts in one deal.[16] Osama (2008) criticises the actions of product developers that are circumventing Shari'a prohibitions.[17] He points out that some developers are "breaking down the overall questionable transaction into two segments - each of which, individually, being Shari'a compliant - whose combination ends up recreating the overall effect of the forbidden transaction." He adds that "creating a complex instrument by breaking down the component transactions defeats the whole purpose" of Shari'a prohibitions and objectives.
- **Islamic products' opacity:** Warren Edwards warns Muslim investors against some "Islamic" structured products because "whatever is inside would be invisible to the investor and could be related to gambling, alcohol stocks, money market funds, interest bearing bonds or other activities which are haram." Edwards also recommends checking whether funds from Islamic transactions have been commingled with the proceeds of conventional banking. [18]

b. Pricing of Islamic financial products

Ghoul (2012) notes that "Islamic" financial products have higher prices compared to equivalent conventional products. This has been referred to as the "Shari'a premium" or "the cost of going to heaven."[19] Examples of costs are the fees paid to Shari'a scholars who issue certificates and fatawa of Shari'a-compliance, as well as salaries of product "engineers" and lawyers. The high compensation which some Shari'a scholars receive has been very controversial.

Another cost arises from the need to monitor Islamic financial products for continuous compliance with Shari'a. To illustrate, a company in which a Muslim is allowed to invest should not be paying interest charges or earning interest income. It would become non-compliant in case it earns interest income at a later time, and thus periodic monitoring of the company's financial statement is required. [20]

Haron and Azmi(2006) point out that the "majority of customers do not use religion as the main factor when establishing a relationship with Islamic banks… most customers still seek the highest return and lowest charges imposed when deciding which bank to place a deposit or obtain funding from."

To conclude, the pricing of Islamic financial products

[10] Ghoul, W. A, (2011) "The Standardization Debate in Islamic Finance: A Case Study" presented at the 8th International Conference on Islamic Economics and Finance,Sustainable Growth and Inclusive Economic Development from an Islamic Perspective, organized by Qatar Foundation and the Islamic Development Bank. Doha, Qatar, 19-21 December 2011, http://conference.qfis.edu.qa/app/media/278

[11] Jabaly, R. Ameri, S. and Ghoul, W.A (2013), "Islamic Banks' Marketing and Communication Tactics: Towards a Better Reception and Perception" Forthcoming paper.

[12] Attallah, C and Ghoul, W (2011) "Wa'd-based total return swap: Shari'a-compliant or not?" Journal of Derivatives, USA, Vol. 19, No. 2: pp. 71–89, DOI: 10.3905/jod.2011.19.2.071Winter 2011, available at http://www.iijournals.com/doi/abs/10.3905/jod.2011.19.2.071

[13] See ft note 10

[14] Ghoul, W (2011) "The Dilemma facing Islamic finance and lessons learned from the crisis" Journal of Islamic Business, Economics and Finance, March 2011, available at www.ibtra.com

[15] Wigglesworth R (2009) "Islamic Banks: Real Estate Exposure May Be Largest Threat", The Financial Times Limited, May 5

[16] Arbouna M.B.(2007) "The combination of contracts in Shari'a: A possible mechanism for product development in Islamic banking and finance", Thunderbird International Business Review. Hoboken: May/Jun. Vol. 49, Issue 3; pg. 341

[17] Osama, A. (2008), "An Outsider's View on Islamic Finance" Harvard Islamic Finance Forum" Posted on May 28, available at www.dinarstandard.com/finance/HarvardFin051908.htm

[18] Islamic Derivatives and Structured Products; It's niyya that counts" 01 January, www.newhorizon-islamicbanking.com/index.cfm?section=lectures&id=10995&action=view

[19] Ghoul, W.A. (2012), " An Appraisal of the Islamic Financial Industry's Compliance with the Ethical Standards of Islamic Marketing", IBA International Conference on Marketing, May 5-6, 2012, http://ibaicm.iba.edu.pk/conference_program.html

should be competitive with conventional products. Husain (2007)[21] quotes Dr. Akram Laldin, Chairman of the Shari'a Advisory Committee of HSBC Amanah Malaysia: "Scholars look at three basic areas when assessing the compliance of products: belief, legalilty and morality . . . products could fairly easily comply with Islamic law but it is more difficult to ascertain whether they comply with the morals of Islam. The price of a product may not be controversial from a legal perspective but if the product costs more than an equivalent conventional product, it may not fulfill Islam's moral obligations of fairness and social equity."

c. Promotion of Islamic financial products

Conventional banks typically count on brand recognition when launching new products. In contrast, IFI's short track record causes difficulties in promotion. On the other hand, IFI's niche is serving the recently discovered market segment of Shari'a-sensitive customers. They need to put in more effort in promotion and distribution. Development of brand new products means difficulties in customers' understanding of the terminology and product characteristics. It is a well-known fact that Islamic product terminology is not straightforward, partly due to the use of Arabic names.

On the other hand, the Islamic finance industry is accused of being a copy-cat of the conventional financial industry, and of endorsing conventional products which are re-engineered or "Islamised" and given Arabic-sounding names, such as "amana", in order to lure Muslims into paying for the more costly "Islamic" alternatives.[22]

"Islamised" versions of conventional banking products have been causing a lot of controversy. Proponents of such a trend approve of the brand recognition associated with're-engineered' or 'Islamised' products; however this has been taking the Islamic finance industry away from its real objectives, and causing a lot of skepticism.

Elfakhani et al (2007) note that Islamic banks typically count on word of mouth for promotion; they distribute flyers among attendees of mosques, Islamic educational institutions and Islamic centers. Jabaly et al (2013) point out that Islamic banks are now relying on conventional public relations agencies; this leads to problems in the reception and perception of marketing messages. They add that Islamic banks are restricted in their promotion activities because Shari'a prohibits aggressive advertising.

The authors interviewed Islamic banks' employees and concluded that successful marketing requires a highly trained team. Critics advise the industry to start by training the employees who will in turn educate the clients.

d. Place (distribution) of Islamic financial products

Western financial giants currently dominate the Islamic finance industry, but they are mainly interested in finding "another distribution channel for their products and services"; they save time and cost by re-engineering conventional products into 'Islamic' versions.[23]

9.6 Conclusion

The above discussion has demonstrated that Islamic financial institutions are not being exactly true to the mission and objectives of Shari'a. Their products are not all Shari'a-compliant, prices are higher than conventional counterparts, and promotion efforts involve ambiguity in disclosing product characteristics. We end by noting that Shari'a aims to benefit and protect all humanity not only Muslims; its guidelines provide a framework for developing products that should be attractive to people of any religious belief. Marketing approaches could focus on the ethical value of products as much as, if not more than, their focus on compliance with Shari'a, this would increase market share, and thus reduce the need for cutting corners through violating Shari'a tenets.

[20] Ghoul, W. and K, Paul (2007) "MRI and SRI Mutual Funds: A Comparison of Christian, Islamic (Morally Responsible Investing), and Socially Responsible Investing (SRI) Mutual Funds", Summer 2007, Journal of Investing, Vol. 16, No. 2, pp. 96-102DOI: 10.3905/joi.2007.686416, available at www.iijournals.com/JOI/default.p?Page=2&ISS=23858&SID=686416

[21] Husain, Ahmad Sanusi (2007) "Islamic Scholars Call for More Attention to Morals than Law" Available at: www.gifc.blogspot.com/search/label/Islamic%20finance.

[22] El-Gamal, Mahmoud A. (2001) "Incoherence of Contract-Based Islamic Financial Jurisprudence in the Age of Financial Engineering" Available at www.ruf.rice.edu/~elgamal/files/Incoherence.pdf

[23] Wong Raphael (2009), "More Than Just Sukuk", www.islamicfinancenews.com, Vol. 6, Issue 32, pg 12, 14th August . Retrieved June 1, 2011