

The Effect of Conventional Bank's Interest Rate & Islamic Bank's Profit Rate on Investment & Return: An Empirical Investigation in Bangladesh

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ABSTRACT

Since depositors are motivated by returns, it is important for Islamic banks management to understand the extent that rates of return on deposits influence their customers' decision to deposit. The main objective of the study is to explore the degree of influence of conventional bank's interest rate on Islamic bank's profitability and vice-versa. It has been seen from 2005 to 2011 that the rate of interest declared on deposit by conventional banks has a negative impact on profitability of both types of banks in Bangladesh. Rate of profit declared on deposit by Islamic banks is positively related with their profit earned but negatively related with profit earned by conventional banks. We see that rate of interest declared on deposit by Conventional Banks is positively related with their deposit volume but negatively related with Islamic Bank's deposit. On the other hand, rate of profit declared on deposit by Islamic Banks is negatively related with deposit levels of both types of banks. The survey result shows that almost 85% of the respondents are choosing Islamic banks only from their religious point of view and more than 60% of the sampled Islamic bank customers are reluctant to leave the bank even if conventional banks offer better interest rates.

KEYWORDS

Interest rate • profit rate • Islamic banks • Conventional banks • Investment • Return

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1. INTRODUCTION

The objectives of Islamic financial institutions comply with the goal of Islamic economy. After nearly four decades of their establishment, Islamic banks have managed to position themselves as financial institutions not only playing important role in resource mobilization, resource allocation and utilization but are actively involved in the process of implementing government monetary policy. Like conventional banks, Islamic banks also depend on depositors' money as a primary source of funds. Islamic Bank Bangladesh Limited (one of the Islamic banks in Bangladesh) for example, had total deposits amounting to 88% of total liabilities and shareholders' equity as at the end of December 2011. Since depositors' money is a primary source of funds, it is necessary for the management of Islamic banks to know the factors that influence customers' decision making in depositing their money with Islamic banks. With the exception of a study conducted by Metawa and Almossawi (1997) which shows religion as a factor of customers' choice of Islamic bank in Bahrain, other studies proved otherwise. The evidence from studies conducted in Sudan and Turkey, for example, shows that religion is not the main reason for customers selecting Islamic banks (Erol and El-Bdour, 1989). Similarly, studies conducted in Malaysia and Singapore find both religion and profit are the reason for people maintaining their relationship with Islamic banks (Haron et al., 1994; Gerrad and Cunningham, 1997). Since depositors are motivated by returns, it is important for Islamic banks management to understand the extent that rates of return on deposits affect their customers' decision to deposit. Investment opportunity utilization mainly depends on the volume of deposit.

Interest rate has long been recognized not only by classical and neo-classical economists but also by contemporary

economists as one of the factors that determine the level of savings in the economy. Although there are cases of inconsistent findings, it is an accepted opinion that the interest rate has a positive relationship with savings. In other words, customers are guided by the profit maximization theory. Since there is no pre-determined rate of return involved in Islamic banking system, it is unknown whether Islamic bank customers are subjected to the normal conventional theory of economic behavior. If this assumption is true, a conclusion can be made that both interest rate of deposit accounts of conventional banks and rate of profit declared by Islamic banks have a strong relationship with the amount of deposits of Islamic banks. This in turn has an effect on the level of investment of Islamic banks.

Therefore, the management of Islamic banks is bound to follow the market rate when declaring the rate of profit to their customers, vice versa. Using Adaptive Expectation Model, the aim of this paper is to examine the effect of interest rates of deposit account facilities of conventional banks and past dividend rates on funds deposited by customers on the level of investment of Islamic banks of Bangladesh. Investment is an essential function for any commercial bank through which return is generated, employment opportunity is created, and productive activity is increased and also contributed to overall socio-economic development of the country. Levels of investment of Islamic banks are affected by interest rate and profit rate to a large extent.

The main objective of the study is to explore the degree of influence of conventional bank's interest rate on Islamic bank's profitability and vice-versa. The specific objectives are as follows.

First, this study explores the relationship between interest rate of Conventional banks and Deposits of Islamic banks and the effect of Profit rate declared by Islamic banks on deposits of conventional banks. Second, this study analyzes the relationship between Deposits of Islamic banks and investment volume of Islamic banks and vice-versa. Finally, this study analyzes the impact investment volume of Islamic banks on the profit rate of Islamic banks and vice-versa.

2. LITERATURE REVIEW:

Islamic finance is free from interest, which is the backbone of Conventional banking and financial systems. Islam prohibits interest, known as *riba*, not as law of the land, but as divine orders leaving no space whatsoever to argue or put a case forward otherwise (Al-Omar)⁵. It is compulsory for Muslims to completely evade *riba* in their commercial and non-commercial daily activities. The Islamic banking and finance is a system designed to allow Muslims to deal with their financial affairs in accordance with their belief. The

theoretical model is appealing and is carefully designed to avoid interest and other prohibition, however, accomplishment of the Islamic banking and financial system has not always been successful in practice (Shepherd, 1996).

Conventional bankers have learned that deposit pricing can be used to shape the kind of customer base each bank can best serve. Changing deposit prices affect not only spread between bank loan rates and deposit interest rates but also customer balances and deposit mix decisions, which in turn, influence both bank growth and profit margins (Edmister, 1982). As Rose (1991) points out, deposit pricing is best used to protect and increase bank profitability, rather than to simply add more customers and to take market share away from competitors. Indeed, when new deposit plans are introduced, its biggest appeal and the greatest chance for success lies with those customers who already hold deposits with the bank. And even those customers the bank already has will not automatically pay higher prices for deposit services. They will pay no more for a deposit than the total of its benefits to them and will go elsewhere when the value of those benefits falls below the deposit's price or if a competitor offers a significantly better package of services.

In summary, two important elements have emerged from this overview. First, the acknowledgement by conventional banks that those who are willing to part with their monies must be rewarded. Second, the recognition that different types of deposits carry different amount of returns or rewards. Therefore, if the management of Islamic banks believes that the attitudes of depositors of Islamic banks are indifferent to those of conventional banks, the same rates of return will be rewarded with rates of conventional banks. There are several serious repercussions if the management of Islamic banks believes that depositors at Islamic banks possess similar attitudes to those at the conventional banks. The interest rate will continue to have an influence on the operations of Islamic banks as long as this thought remains in the mind of their management. Findings of Metwally (1997), for example, confirmed that conventional and Islamic banks offer their depositors similar returns.

The empirical literature related to mimicking of the deposit return is very rare. One of them was Chong and Liu (2009), who examined the relation between the rate of return on deposits and interest rate of the conventional banks as they might not always be the same. They found that changes in the conventional bank deposit rate caused changes in the rate of return. When rate of return is deviated far above (or below) the bank deposit rate, it will be adjusted towards the long term equilibrium level and vice-versa. Nienhaus (1983) noticed that the Islamic bank used the interest rate as a benchmark rate to calculate, their profit and loss sharing ratio. Haron (2004), however found clear evidence that Islamic banks truly benchmarked interest rate

to fixing both charges to creditors and reward to depositors.

El-Gamal(1997) argued that the transactions in Islamic banks such as time deposits and saving deposits were not purely Islamic. The return on Islamic bank deposits had a high correlation with market interest rate and even tended to be lower than market rate (Bank Negara Malaysia 1994). Khan (19995) also argued that mimicking and interest rate was still acceptable in the short term for Islamic banks to make them competitive. Hopefully, this would be gradually replaced with a more sharia-compliant banking system later on. Nonetheless, Ahmed (1992) disagreed with that argument and wished to transform the economic system instantaneously to be an Islamic economic system.

A number of empirical studies is focusing on dual banking system underline that the interest rate strongly affects Islamic banking system. The probable reasons cited in these studies of such an impact include influence by interest rates upon deposits, the encounter with negative fund gap and deprivation from arbitrage opportunities. It was found in many empirical studies that the change in interest rates may affect not only the deposits in conventional banks, but also the deposits reserved in Islamic banks (Haron and Ahmad 1994). The arguments for the individuals to favor Islamic banks as institutions collecting deposits consist of religious and economic factors that a growing number of studies pay attention to. Erol and Bodur (1989) and Gerrard and Cunningham (1997). Most of these studies summon up that economic factors are as important as religious factors for the depositors. If interest rates is significant over Islamic banking deposits, this means that the positive impact of interest-free banking upon financial stability is restricted. Islamic banking units are influenced by interest rates because they are subjected to negative fund gap. Rosly (1999) demonstrates in a study where the influence of change in the interest rates in Malaysia upon one Islamic bank and 5 conventional banks is revealed that increase in interest rates subjects the Islamic banks to negative fund gap, reducing their rate of profitability. Because they suffer from over-dependency on fixed rate asset financing (such as al-bay’bithaman ajil and Murabahah), funds gap will always be negative where all Islamic liabilities are interest-sensitive. Rosly (1999) further explains that Bank Islam Malaysia appears to be the only bank suffering from a decline in profitability while conventional banks increase interest margins, suggesting that Islamic banks are negatively affected by changing in the interest rates.

3. METHODOLOGY OF THE STUDY:

This study uses all conventional and Islamic commercial

banks. Convenience sampling method was applied for the selection of respondents. In the study, the sampling technique was Stratified random sampling. Here, five major types of respondents were under focus such as follows:

TABLE 1: Sample size

No.	Category of respondents	Sample size
1	Deposit holders of Islamic banks	70
2	Deposit holder of conventional banks	70
3	Islamic bank’s investors/ entrepreneurs	60
4	Officials of Islamic banks	60
5	Officials of conventional banks	60
Total		320

SELECTION OF ISLAMIC BANKS: In the study, seven full-fledged Islamic banks and 7 conventional banks from 2005 to 2011 have been selected.

SELECTION OF CONVENTIONAL BANKS: Simple random sampling techniques will be applied in selecting conventional commercial banks. Among conventional commercial banks seven banks taken as a sample for the implementation of the study.

This study adopts the ‘Adaptive Expectation Model’ to measure the effects of rate of profit declared by Islamic banks on the level of deposits placed by their customers. A general statement of the model is represented by:

$$Y_t = a + b X^*t + ut$$

Where the variable X^*t is the anticipated (or expected) value of the variable X , and it is assumed unobservable. The anticipated value X^*t is assumed to be a weighted average of the previous period’s anticipated value, and the realization of the previous period. The rates of interest for various deposit facilities available at conventional banks are also included in the model with the objective of measuring the effect of this variable on the level of deposits of Islamic banks. The following equations are used to validate the objective of this study. They are,

- $It = a + b Ip^*t + ut$ (1)
- $It = a + b Ip^*t + d FDrt + ut$ (2)
- $ISDt = f + g ISDp^*t + ut$ (3)
- $ISDt = f + g ISDp^*t + h SDrt + ut$ (4)

Where It is the investment amount of Islamic banks for a period of t , Ip^*t is the expected rate of profit of Islamic investment deposits, $FDrt$ is the interest rate for fixed deposit of conventional banks at t period, $ISDt$ is the amount of savings deposit of Islamic banks, $ISDp^*t$ is the

expected rate of profit of Islamic savings deposit facility, and SD_{rt} is the rate of interest of conventional banks' savings deposit facility. The primary data were collected by using questionnaire and interviews. The secondary data were collected through the annual report, internet; books, journals, related studies and other sources of information, etc.

3.1. DATA ANALYSIS & FINDINGS:

With the objective and research question of the study, we explore the impact of the interest rate of conventional bank on the profit of Islamic Bank and simultaneously the same thing for Conventional bank. As designed in the methodol-

ogy the impact of the interest rate of conventional bank on the profit of Islamic bank as well as the impact of the interest rate of Islamic bank on the profit rate of conventional bank, we use Adaptive expectation model. This study we use two-stage model to find the impact.

As per the frame of the models, the study has devised a number of endogenous variables, independent variables and instrumental variables for carrying out different models to evaluate the impact of interest rate on profit for both conventional and Islamic bank. The summary values for the main variables used in our analysis are shown, separately for Islamic bank and conventional bank in table 1. The average rate of profit declared at deposit for Islamic bank is significantly higher than the Conventional bank.

TABLE 1: summary statistics for the main variables

Variables	Islamic Bank (Mean \pm SD)	Conventional Bank (Mean \pm SD)
Average Investment	60801.73 \pm	64587.02 \pm 34813.47
Average rate of profit declared at deposit***	8.79 \pm 1.49	7.94 \pm 1.39
Average amount of deposit	62523.39 \pm 72727.04	61223.55 \pm 31118.50
Average Fixed amount of deposit	54720.59 \pm 63142.46	48736.37 \pm 26414.20
Average rate of Interest against loan and	13.67 \pm 1.30	13.15 \pm 1.12
Average amount of Profit earned	7705.18 \pm 8061.44	8583.79 \pm 4400.80
Average employee per Branch***	26.61 \pm 7.74	22.49 \pm 3.01

*** significant at 1% level, ** significant at 5% level.

As in the methodology the impact of interest rate both the Islamic and conventional bank on the profit are explored by the help of instrumental variables (IV) regression. The study assumes that rate of profit declared at deposit is an endogenous variable since the interest rate offered to the customer is depending on some unobserved characteristic that may impact on the outcome variable.

To deal with the endogeneity problems three instrumental variables are considered preliminarily, namely rate of Interest against loan and advances both for Islamic bank and Conventional bank and average employee per Branch. The primary examination reveals that the instrument has a significant correlation with endogenous variable ($r=0.71, 0.26, 0.49$) and poor correlation for the rate of Interest against loan and advances of Conventional bank ($r=-0.04$) and average employee per Branch ($r=0.11$) but significant correlation with the rate of Interest against loan and advances both for Islamic bank ($r=-0.45$) with the dependent variable. In order to assess the impact of instrumental variables on endogenous variable (rate of profit declared at deposit), separate regression analyses have been carried out first, and the findings indicate that all the instruments have

high F-value ($F=49.05$ for interest rate against loan and advances for conventional bank, $F=14.56$ for the average employee per branch) except interest rate against loan and advances for Islamic bank ($F=3.34$). So interest rate against loan and advances for Islamic bank does not incorporate as an instrumental variable. As a result, the instrumental variable regression analysis has been performed by considering two instruments- interest rate against loan and advances for conventional bank and average employee per branch.

In addition, the study considered number of independent variables such as the amount of the deposit for both IB & CB, Fixed amount of the deposit for both IB & CB, amount of Profit earned for both IB & CB. The analysis has performed two-stage least squares regression with the above mentioned instrumental variables that are assumed to be uncorrelated with the error terms to compute estimated values of the endogenous variable in the first stage, and then uses those computed values to estimate a linear regression model of the dependent variable in the second stage. Since the computed values are based on variables that are uncorrelated with the errors, the results of the two-stage model are optimum. After conducting the 2SLS regression, Sargan

N*R-sq test has been performed to test whether the instruments are uncorrelated with error terms (overidentifying the restrictions). The test indicates that all the instruments are uncorrelated with the disturbance term. In order to obtain the robust estimates, the generalized method of moments (GMM) estimation technique of IV regression has been adopted.

3.2 ESTIMATES OF THE COVARIATES UNDER IV REGRESSION

From the above table, we see that Rate of interest declared on deposit by CB is negatively correlated with an investment volume of Islamic Banks but positively correlated with an investment volume of Conventional Banks.

TABLE 2: Estimates of the covariates under IV regression:

Variables	IB		CB	
	Coef.	P>z	Coef.	P>z
Rate of interest declared on deposit by CB	-160.83	0.910	2706.21	0.004
Rate of profit declared on deposit by IB	-1136.53	0.500	-1101.24	0.199
Total amount of deposit at IB	1.31	0.028	0.19	0.544
Total amount of deposit at CB	0.26	0.588	1.09	0.000
Rate of Interest charged against loan and advances by CB			-882.08	0.313
Rate of profit charged against loan and advances by IB	631.65	0.622		
Average employee per Branch at CB			-980.58	0.001
Average employee per Branch at IB	130.43	0.600		
Fixed amount of deposit at IB	-0.79	0.276	-0.29	0.432
Fixed amount of deposit at CB	-0.22	0.714	-0.15	0.460
Amount of Profit earned by IB	2.25	0.161	0.64	0.298
Amount of Profit earned by CB	0.11	0.926	0.78	0.058
Constant	-3577.05	0.819	18780	0.088
No. of observations	49		49	
F-test	211.64 (P=0.000)		238.86(P=0.000)	
R-squared	0.97		0.99	
Tests of overidentifying restrictions:				
Sargan N*R-sq test statistic	0.419 (P=0.52)		2.36 (P=0.12)	
Hansen-J-Statistic	0.691 (P=0.41)		2.23(P=0.14)	
Test for endogeneity of No. of Migrants (H₀: Regressor is exogenous)				
Wu-Hausman F-test	3.06795 (P=0.08)		0.30 (P=0.59)	
Durbin-Wu-Hausman	3.75186 (P=0.05)		0.39 (P=0.53)	

DEPENDENT VARIABLE: Total Investment of IB, Total Investment of CB, Independent variables: Amount of deposit for both IB & CB, Fixed amount of the deposit for both IB & CB, amount of Profit earned for both IB & CB, Instrumental variables: Interest rate against loan and advances for conventional bank and Average employee per branch.

One percentage point increase in interest rate declared on deposit by Conventional Banks cause BDT 160.83 million decreases in investment volume of Islamic Banks and 2706.21 million BDT increase in investment volume of Conventional Banks and vice versa. On the other hand, rate of profit declared on deposit by Islamic Banks is negatively correlated with an investment volume of both Islamic Banks

and Conventional Banks. One percentage point increase in the profit rate declared on deposit by Islamic Banks cause BDT 1136.53 million and 1101.24 million decrease in investment volume of Islamic Banks and Conventional Banks respectively.

It is seen that amount of the deposit at Islamic Banks is positively correlated with an investment volume of both

types of Banks. If BDT one million deposit increases at Islamic Banks then it results BDT 1.31 million increases of investment by Islamic Banks and BDT 0.19 million increase of investment by Conventional Banks and vice versa. It is also seen that total amount of the deposit at Conventional Banks is positively correlated with an investment volume of both types of Banks. If BDT one million deposit increases at Conventional Banks, investment volume of Islamic Banks and Conventional Banks increase by 0.26 million BDT and 1.09 million BDT respectively. Lending rate of Conventional Banks is negatively related with their investment volume, but that of Islamic Banks is positively related. One percentage point increase in interest rate on loan & advances cause BDT 882.08 million decreases in investment volume of Conventional Banks. On the other hand, rate, one percentage point change in rate of profit charged against loan and advances by Islamic Banks cause BDT 631.65 million changes in their investment volume to the same direction.

It is observed that fixed amount of the deposit at Islamic Banks has a negative impact on investment level of both types of banks. BDT one million increases of time deposit

at Islamic Banks results in BDT 0.79 million decrease in their investment volume and BDT 0.29 million decrease in Conventional Bank's investment volume. The same behavior is shown by the Conventional Bank's fixed amount of the deposit. BDT one million increases of time deposit at Conventional Banks results in BDT 0.15 million decrease in their investment volume and BDT 0.22 million decrease in Islamic Bank's investment volume. It is revealed that impact of change in level of fixed deposit on investment level is more in case of Islamic Banks. Amount of profit earned by banks is positively related with investment level of both types of banks. BDT one million profit increase of Islamic Banks cause BDT 2.25 million increases in their investment volume and BDT 0.64 million increase in Conventional Bank's investment volume. BDT one million profit increase of Conventional Banks cause BDT 0.78 million increases in their investment volume and BDT 0.11 million increase in investment level of Islamic Banks and vice versa.

From the above table, we see that Rate of interest declared on deposit by Conventional Banks is positively related with their deposit volume but negatively related with Islamic Bank's deposit. One percentage point increase

TABLE 3: Estimates of the covariates for the Interest rate declared

Variables	IB		CB	
	Coef.	P>z	Coef.	P>z
Rate of interest declared on deposit by CB	-72.28344	0.989	6551.755	0.090
Rate of profit declared on deposit by IB	-11981.26	0.022	-4392.015	0.212
Average employee per Branch at CB	-	-	-4109.134	0.042
Average employee per Branch at IB	6031.341	0.000	-	-

DEPENDENT VARIABLES: Total deposits by IB & CB

in deposit rate by Conventional Banks results in BDT 6551.755 million increases in their total deposit but BDT 72.28344 million decreases in Islamic Bank's deposit. On the other hand, rate of profit declared on deposit by Islamic Banks is negatively related with deposit levels of both types of banks. One percentage point increase in deposit rate by Islamic Banks results in BDT 11981.26 million and BDT

4392.015 decreases in deposit of Islamic Banks and Conventional Banks respectively.

From the above table, we see that the amount of investment by both types of banks is positively related with their respective amount of profit. BDT one million extra investments by Islamic Banks generate an extra amount of profits of BDT 0.1146711 million. In the case of conventional

TABLE 4: Estimates of the covariates for Profit

Variables	IB		CB	
	Coef.	P>z	Coef.	P>z
Total amount of investment by IB	.1146711	0.000	-	-
Total amount of investment by CB	-	-	.1027414	0.000
R-square	0.94		0.66	

DEPENDENT VARIABLES: Amount of Profit earned by IB & CB

banks, the marginal amount of profits is slightly less which is BDT 0.1027414 million for additional BDT one million investments. The R-square value shows that the influence of the independent variable is significant in both the cases.

From the above table, it is seen that rate of interest

declared on deposit by conventional banks has a negative impact on profitability of both types of banks. One percentage point increase in deposit rate by conventional banks results BDT 113.2046 and 294.0213 million decreases in profit by Islamic banks and conventional banks respectively.

TABLE 5: Estimates of the covariates for Interest rate on deposit

Variables	IB		CB	
	Coef.	P>z	Coef.	P>z
Rate of interest declared on deposit by CB	-113.2046	0.580	-294.0213	0.416
Rate of profit declared on deposit by IB	226.224	0.204	-56.63193	0.856
Total amount of deposit by IB	.0850048	0.000	.0604463	0.017
Total amount of deposit by CB	-.0066082	0.890	-.0359225	0.669
Total amount of investment by IB	.0238302	0.138	-.0441219	0.120
Total amount of investment by CB	.0229226	0.613	.12713	0.117
Average employee per Branch at CB	-100.6368	0.324	247.0001	0.172
Average employee per Branch at IB	-.381905	0.993	-154.7025	0.053
Constant	1048.92	0.711	2869.256	0.567
No. of observations	49		49	
F-test	213.94 (P=0.000)		15.95 (P=0.000)	
R-square	0.97		0.74	

DEPENDENT VARIABLES: Amount of Profit earned by IB & CB

Rate of profit declared on deposit by Islamic banks is positively related with their profit earned but negatively related with profit earned by conventional banks. One percentage point increase in deposit rate by Islamic Banks results in BDT 226.224 million increase in their profit but BDT 56.63193 decreases in Conventional Bank's profit. Next, we observed that the deposit level of Islamic Banks has a positive influence on profitability of both types of banks. Additional BDT one million of deposit created by Islamic Banks generate BDT 0.0850048 million to their profit.

The opposite behavior is shown in the case of conventional banks. Deposit level of conventional banks negatively related with profitability of both types of banks. BDT One million increases in deposit by conventional Banks results in BDT 0.0066082 and BDT 0.0359225 million decreases profit earned by Islamic Banks and Conventional Banks respectively. Although number of employees per Branch at Conventional Banks has positive impact on their profitability but the scenario is different in the case of Islamic Banks. Each additional employee of Conventional Banks contribute BDT 247.0001 million to their bank's profitability, but each additional employee of Islamic Banks reduce BDT 0.381905 million of bank's yearly profit.

3.3 ROBUST TESTS

I. H0: Religious point of view regarding banking activities of Islamic Bank is independent of Shifting Islamic bank to conventional bank for interest rate

According to the significance level of table in Appendix, Null (Ho) Hypothesis is rejected. So, it there is a strong association between religious point of view and Shifting of a bank. It means that, the customers of Islamic banks are very much religious intensive instead of profit rate of other services offered by conventional banks.

II. H0: Religious point of view regarding banking activities of Islamic Bank is independent of conventional bank rather than Islamic Bank.

According to the significance level in table in appendix, Null (Ho) Hypothesis is rejected. So, it there is a strong association between religious point of view and Shifting of a bank. It means that the religious point of view is strongly related with the selection procedure of Islamic bank. It is also true according to our survey. In the above figure in table 8 in appendix, it can be claimed that almost 85 % of the respondents are choosing the bank on

the basis of Islamic believes for selecting a bank.

III. H₀: The profit rate scheme announced by Islamic Bank and Customer retention are positively related.

According to the table in appendix As significance level is high, Null (H₀) Hypothesis is rejected. It means that people are not sensitive to the offer of Islamic banks for example It is clearly depicted in table 10 that almost 60% of the sample group of people are reluctant to leave the Islamic bank even if the conventional bank offers something more than that.

4. CONCLUSION:

Theoretically, Islamic banks should give Islamic return on deposits based on predetermined profit-and-loss sharing (PLS) ratio. Under PLS principle, the Islamic return is uncertain and post determined depending on profits and performance of the business. Indeed, it may not imitate the volatility of interest rate on deposits. This is because, unlike Islamic banks, the conventional banks pay interest on deposits according to a predetermined interest rate. As a result, the conventional bank depositors receive a certain and predetermined interest on depositors.

It can be concluded that the Islamic bank and Conventional banks are both interrelated in the money market. As our paper finds that the impact of conventional interest rates is not playing highly significant role on the investment and return on the Islamic banks mainly due to the customers beliefs and strong supports for the Islamic banks. The paper also proves that the customers of Islamic banks are irrespective to the changes of conventional interest rates and offerings. The further studies are needed to find out more reasons for the customer's choice and the risk and return relation between these two types of banking.

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APPENDIX: Religious point of view of banking activities of Islamic Bank

Hypothesis test-1:		Religious point of view banking activities of Islamic Bank				Total	Asymp. Sig. (2-sided)
		Strongly Disagree	Neither Agree nor Disagree	Agree	Strongly Agree		
Leave the Islamic Bank if profit rate less than conventional Bank	Strongly Disagree	11	1	22	31	65	.000
	Disagree	8	7	55	64	134	
	Neither Agree nor Disagree	6	21	23	62	112	
	Agree	0	0	3	0	3	
	Strongly Agree	0	0	6	0	6	
Total		25	29	109	157	320	

Hypothesis test- 2		Religious point of view banking activities of Islamic Bank				Total	Asymp. Sig. (2-sided)
Transactions with conventional bank rather than Islamic Bank	Never	15			28	80	.000
	Rarely	5	7	34	31	77	
	Occasionally	4	15	33	69	121	
	Frequently	0	4	5	19	28	
	Very Frequently	1	1	2	10	14	
Total		25	29	109	157	320	

Hypothesis- 3:		Leave the Islamic Bank if profit rate less than conventional Bank				Total	Asymp. Sig. (2-sided)
Scheme of the profit rate provided by Islamic Bank	Not at all Satisfactory	4	0	13	6	23	.000
	Slightly Satisfactory	24	5	25	0	54	
	Somewhat Satisfactory	14	85	41	3	143	
	Very Satisfactory	23	44	21	0	88	
	Extremely Satisfactory	0	0	12	0	12	
Total		65	134	112	9	320	