

Impact of Demographic and Socioeconomic Profile on Libyan Firms' Attitudes Towards Islamic Methods of Finance

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Abstract

This paper investigates the impact of demographic and socioeconomic profiles on Libyan business firms' attitudes towards potential use of Islamic methods of finance. A sample of 296 firms is surveyed using phone interviews during December 2007 and January 2008 to gather information on their demographic and socioeconomic profiles as well as their attitudes towards Islamic methods of finance. Descriptive statistics is used to indicate the main characteristics of the sample and potential use of Islamic methods of finance. The results indicate that over two-third (72.3 %) of Libyan firms are potential users of Islamic methods of finance. Discriminant analysis is used to indicate which of these profiles has significant impact on the attitudes of Libyan business firms towards Islamic methods of finance. This analysis illustrates that share capital, total assets, business experience and number of partners is the most important factors in discriminating between the two groups of business firms (potential users and non-potential users of Islamic methods of finance).

Keywords: Islamic methods of finance; demographic profiles; attitudes; Libya.

1. Introduction

Islamic finance comprise of financial institutions, products and services designed to comply with the central tenets of *Sharia* (or Islamic law). The

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current Islamic finance movement is now over three decades old. However, the conceptual development of Islamic finance first took place between the late 1940s and the mid-1970s. The huge influx of petrodollars into Middle Eastern economies in the 1970s and 1980s provided major impetus to the establishment of several large Islamic banks in the region. Other Muslim countries imitated these breakthrough developments and gradually established their own Islamic financial institutions. Islamic banking and finance made steady progress over the intervening decades. However, it has now emerged as the fastest-growing segment of global finance in recent years owing to consistently high oil prices in international markets and increasingly favorable socio-political and economic conditions across the globe. Islamic banking and finance is now flourishing in Africa, Asia, Europe and North America, with the Middle East, South Asia and South-East Asia as the main emerging centers (Khan, Bhatti, Wilson and Natt, 2008).

While many Muslim and non-Muslim countries have been practicing the Islamic methods of finance in their financial institutions, Libya has not yet introduced these methods of finance on a formal basis in the form of Islamic banks. This could be seen as unusual because most if not all Libyan population is Muslim (General Information Authority, 2007). Therefore, it is of interest to investigate the possibility of applying Islamic methods of finance in case of Libyan business firms who usually obtain finance from conventional banks on fixed or variable rates of interest. These firms have to pay back the principal borrowed along with its stipulated interest at the end of the specified period. They are also supposed to make these payments as per contract even if they suffer heavy losses in their business projects. This may cause a great deal of hardship on the part of the borrowers, especially at times of economic slowdown. However, Islamic methods of finance being interest-free are profit and loss based modes of finance and could possibly be preferred by the borrowers, especially in a Muslim country like Libya.

This paper examines the impact of demographic and socioeconomic profiles on the attitudes of Libyan business firms towards the potential use of Islamic methods of finance. More particularly, this paper attempts to explore the importance of the demographic and socio-economic profiles on the

attitude of Libyan business firms towards the potential use of Islamic methods of finance. Section 2 of the paper proceeds with a literature review related to the findings of previous studies regarding the use of Islamic finance. Section 3 includes brief information about the research methodology used to achieve the objectives of this study. Descriptive statistics for the main characteristics of the sample and the potential use of Islamic methods of finance are provided in section 4. A discussion of empirical results using Discriminant Analysis is indicated in section 5. This paper ends with some concluding remarks in section 6.

2. Review of Literature

Although the attitude of retail consumers towards Islamic financial institutions and products has been studied by researchers in Muslim and non-Muslim countries alike (Erol and El-Bdour, 1989; Erol, Kaynak, and El-Bdour, 1990); Omer, 1992; Haron, Ahmad and Planisek, 1994; Metwally, 1996; Gerrard and Cunningham, 1997; Al-Sultan, 1999; Hamid and Nordin 2001; Bley and Kuehn, 2004; Dusuki and Abdullah, 2007; and Rammal and Zurbruegg, 2007), relatively little inquiry has been made into the attitudes of business firms towards Islamic methods of finance:

Metwally (1996) and Al-Sultan (1999) report that even though Kuwait is a predominantly Muslim country, majority of businesses were inclined to deal with conventional banks rather than the Islamic banks and these business firms ranked the size of a bank's assets to be the primary factor in the bank selection process. In contrast to business firms, strong preference for Islamic methods of finance seems to have been revealed by Kuwaiti retail consumers. Similarly, Edris (1997) reports that business firms in Kuwait preferred to obtain financial services from banks that were large and reliable, whereas the Islamic method of finance was ranked fifth among the bank selection criteria.

Jalaluddin and Metwally (1999) surveyed 385 small businesses in Sydney and enquired about their opinion on the probability of applying profit/loss sharing modes of financing as advocated by Islamic finance. Their

main conclusion was that factors other than religion may motivate small business firms to use Islamic-like financial services. In Malaysia, Ahmad and Haron (2002) surveyed 45 current corporate customers on their attitudes towards Islamic products and services. Their major finding was that economic factors, such as profitability and the quality of service, were more significant than any religious concerns.

To conclude this section, though the impact of demographic and socioeconomic factors on retail consumers' attitude towards Islamic banking and products has been studied by some including Hegazy (1995); Metawa and Almossawi (1998); Naser, Jamal and Al-Khatib (1999); Metwally (2002); Zainuddin, Jahyd and Ramayah (2004) and Okumkus (2005), there are no empirical studies in the literature that focus on the impact of demographic profiles on business firm's attitudes towards Islamic methods of finance (Gait and Worthington, 2008).

3. Methodology

A questionnaire was designed to collect data from a sample of Libyan business firms. The respondents were requested in the first part of the questionnaire to indicate their knowledge about the existence of Islamic banks and their methods of finance. The second part of the questionnaire was used to discern the respondents' attitudes towards Islamic methods of finance. The questionnaire also collected information on the demographic and socioeconomic profile of the firms, including firm size, organisational structure, ownership, and industry etc. Unfortunately, despite best efforts only 296 complete questionnaires were obtained, therefore, the incomplete questionnaires were removed from the sample.

Descriptive analysis is used to indicate the main characteristics of the sample and potential use of Islamic methods of finance by Libyan business firms. Discriminant Analysis is used to determine which of the demographic and socioeconomic profiles account for the most significant impact on Libyan business firms' attitudes towards the potential use of Islamic methods of finance.

4. Descriptive Statistics

4.1 Main Characteristics of the Sample

Table 1 shows the main characteristics of the sample, it is shown that more than 40 percent of the firms have business experience of 4 to 5 years. Over one third (32.1 percent) of the respondents have total assets between LYD101,000 to LYD300,000. Similarly, majority of the business firms have liabilities between LYD50,000 to LYD100,000. However, there are no firms having liabilities of more than LYD300,000. Majority of the respondents have share capital of more than LYD50,000 with number of employees ranging from 5 to 20 persons. Most firms interviewed (96.6 percent) are joint ventures and partnerships, whereas 3.4 percent are family businesses. Similarly 37.2 percent of the firms are established by partners ranging from 10 to 20 persons.

4.2 Potential Use of Islamic Methods of Finance

Libyan business firms' as respondents were asked to indicate their intention of using Islamic methods of finance. This information about the Libyan business firms' potential use of Islamic methods of finance is summarized in Table 2. It is noted that over two-thirds of the Libyan firms (72.3 %) happen to be the potential users of Islamic methods of finance. From these potential users, 55.6 percent were partnerships and almost 73.4 percent of the potential users had total of assets between LYD101,000 to LYD 500,000. Approximately, 50 percent of these potential users had business experience as long as 4 to 5 years with share capital between LYD50,000 to LYD100,000 and liabilities between LYD50,000 to LYD100,000. In addition, majority of these business firms (80 percent) have been established by less than 20 partners.

However, 27.7 percent of the respondents were not potential users of Islamic methods of finance and majority of them had share capital greater than LYD100,000. Also, and noticeably most of them (73 percent) had total

assets greater than LYD500.000 and business experience of more than five years, while majority of these non potential users were joint ventures.

5. Empirical Results

In the second part of this study's questionnaire, the respondents were asked to indicate their firms' profile i.e professional status, business experience, total assets, total liabilities, share capital, number of employees, business type and number of partners. In addition, they were asked about their intention of using the Islamic methods of finance. Discriminant Analysis was performed on eight variables that represented firms' profiles as explanatory variables. The primary goal was to determine which of these eight variables accounted for the most significant and strong impact on the Libyan firms' attitudes towards the potential use of Islamic methods of finance. The potential use of Islamic methods of finance is used as the dependent variable. Thus, the respondents were divided into two groups, those who were potential users of Islamic methods of finance and those who were not. The results of discriminant analysis are discussed as below.

Table 3 gives discriminant analysis results that include information about the mean and standard deviation for the two groups. The group means suggest that the two groups are widely separated in terms of value of share capital and total assets. Differences between the two groups are smallest for professional status and number of employees. The Wilks' lambda statistic in Table 3 is the proportion of the variance not explained by differences between the groups. Because all the Wilks' lambda values are smaller than 1, most observed variability can be attributed to the differences between groups (Norusis 2006). Moreover, the significance of the univariate ratios show that, when the predictors are considered individually, all predictors significantly differentiate between the two groups (Metwally 2000). The pooled within-groups correlation matrix at the end of Table 3 is obtained by averaging the separate covariance matrices for the two groups and the correlation matrix is computed from the pooled-covariance matrix. This matrix indicates

remarkably low correlations between the variables therefore; multicollinearity is not a serious problem in the data set (Norusis 2006).

Table 4 indicates the significance level of *Box's M* which suggests that the null hypothesis that the covariance matrices are equal is rejected. This is confirmed also by the logs of the determinants of the variance-covariance matrices shown in Table 4. The logs of the determinants are quite different in value between the two groups.

The eigenvalue in Table 5 is remarkably large (2.023), accounting for 100% of the explained variance. The canonical correlation is another measure of the degree of association between the discriminant scores and the groups. The canonical correlation of the discriminant function is about 0.82. The square of this coefficient shows that 67.2% of the variance of the dependent variable is explained or accounted for by this model (Norusis, 2006 and Metwally, 2003). The Wilks' lambda associated with the discriminant function in Table 5 is 0.331 which is the ratio of the within-groups sum of squares to the total sum of squares. This can be transformed to a chi-square value of 320.827, which is statistically significant at the 0.0 level of significance, with degrees of freedom equal to the number of predictor variables. Therefore, the null hypothesis that the potential users of Islamic finance have the same average discriminant function score in the population is rejected (Norusis, 2006 and Malhotra and Birks, 2003).

The absolute magnitude of the standardized canonical discriminant function coefficients in Table 6, suggests that share capital (0.954), business experience (0.642), number of partners (0.240) and total liabilities (0.133) are the most important variables in discriminating between the two groups of business firms (potential users and non-potential users of Islamic methods of finance).

However, this magnitude of the standardised coefficients takes into account the other variables of the model when the relative contribution of the

variables is compared (Norusis, 2006). According to Norusis (2006), to know the association of the individual variables with the discriminant function ignoring other variables, it is best to use the structure matrix. Thus, another way to assess the relative importance of the predictors can also be obtained by examining the structure correlations between the values of the function and the values of the variables.

The structure matrix results mentioned in Table 6 indicate that share capital (0.753), total assets (0.594), business experience (0.537) and number of partners (0.396) have stronger impact on Libyan business firms' attitudes towards Islamic methods of finance. The group centroids in Table 6 show the unstandardised canonical discriminant functions evaluated at the group means. As shown, group 1 (non-potential users of Islamic methods of finance) has a positive value while group 2 (potential users of Islamic methods of finance) has a negative value. Since the sign associated with the value of share capital, total assets and business experience in both standardised canonical discriminant function coefficients and structure matrix are all positive, this suggests that a firm having larger share capital, assets and relatively longer experience will be among those who are not potential users of Islamic methods of finance. Therefore, Islamic methods of finance will be preferred by those firms that have smaller share capital, assets, and limited experience.

The classification matrix at the end of Table 6 gives a hit ratio of 96.6% which indicates a highly significant classification for most cases included in the sample. In other words there are only ten cases that are misclassified and this is acceptable when one group is much smaller than another group (Norusis, 2006).

6. Concluding Remarks

The main conclusion drawn from this study is that most business firms, in particular small businesses in Libya prefer to adopt Islamic methods of

finance for their business concerns. Apart from that business firms that are already availing Islamic finance are not only the ones with little business experience but are also smaller in size. Their assets size is small and the work force employed is also small. Moreover, these small businesses have a lower level of outstanding debt and have fewer business partners who own the business. In the light of our findings, it may be suggested that Islamic finance can play a crucial role in the development of small and medium sized enterprises in Libya.

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Table 1 Main Characteristics of the Sample

Variables	Frequency	%	Variables	Frequency	%	Variables	Frequency	%
Professional Status			301,000 to 500,000	83	28	Number of Employees		
Trading	12	4.1	More than LYD 500,000	71	23.9	Less than 5 persons	84	28.6
Manufacturing	50	16.9	Total of Liabilities			5 to 10 persons	123	41.5
Importing and exporting	60	20.3	Less than LYD 50,000	96	32.4	11 to 20 persons	76	25.6
Construction	66	22.3	50,000 to 100,000	160	54	More than 20 persons people	13	4.3
Transport and storage	20	6.7	101,000 to 200,000	36	12.2	Business Type		
Services	78	26.3	201,000 to 300,000	4	1.4	Family business	10	3.4
Others	10	3.4	More than LYD 300,000	-	-	Joint venture	155	52.4
Business Experience			Share Capital			Partnership	131	44.2
Less than 1 year	9	3	Less than LYD50,000	81	27.4	Number of Partners		
2 to 3 years	86	29	50,000 to 100,000	116	39.2	Less than 10 persons	90	30.4
4 to 5 years	122	41.3	101,000 to 200,000	46	15.5	10 to 20 persons	110	37.2
More than 5 years	79	26.7	201,000 to 300,000	17	5.7	21 to 30 persons	21	7.1
Total of Assets			More than LYD300,000	36	12.2	More than 30 persons	75	25.3
Less than LYD 50,000	2	0.8				Number of Employees		
50,000 to 100,000	45	15.2				Less than 5 persons	84	28.6
101,000 to 300,000	95	32.1				5 to 10 persons	123	41.5

Table 2 Libyan Business Firms' Potential Use of Islamic Methods of Finance

Variables	Frequency	%	Potential user	%	Not potential user	%
Potential Use of Islamic Methods of Finance						
Potential User	214	72.3	214			
Not Potential User	82	27.7			82	
Professional Status						
Trading	12	4.1	9	4.2	3	3.7
Manufacturing	50	16.9	33	15.5	17	20.7
Importing and Exporting	60	20.3	41	19.1	19	23.2
Construction	66	22.3	49	22.9	17	20.7
Transport and Storage	20	6.7	12	5.6	8	9.7
Services	78	26.3	64	29.9	14	17.1
Others	10	3.4	6	2.8	4	4.9
Business Experience						
Less than 1 year	9	3	9	4.2	0	0
2 to 3 years	86	29	84	39.3	2	2.4
4 to 5 years	122	41.3	103	48.1	19	23.2
More than 5 years	79	26.7	18	8.4	61	74.4
Total Assets						
Less than LYD 50,000	2	0.8	2	0.9	0	0
50,000 to 100,000	45	15.2	44	20.6	1	1.2
101,000 to 300,000	95	32.1	93	43.5	2	2.4
301,000 to 500,000	83	28	64	29.9	19	23.2
More than LYD 500,000	71	23.9	11	5.1	60	73
Total Liabilities						
Less than LYD 50,000	96	32.4	88	41.1	8	9.7
50,000 to 100,000	160	54	112	52.4	48	58.6
101,000 to 200,000	36	12.2	14	6.5	22	26.8
201,000 to 300,000	4	1.4	0	0	4	4.9
More than LYD 300,000	-	-	-	-	-	-
Share Capital						
Less than LYD50,000	81	27.4	80	37.4	1	1.2

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50,000 to 100,000	116	39.2	105	49.1	11	13.5
101,000 to 200,000	46	15.5	24	11.2	22	26.8
201,000 to 300,000	17	5.7	5	2.3	12	14.6
More than LYD300,000	36	12.2	0	0	36	43.9
Number of Employees						
Less than 5 persons	84	28.6	69	32.3	15	18.3
5 to 10 persons	123	41.5	88	41.1	35	42.7
11 to 20 persons	76	25.6	52	24.3	24	29.3
More than 20 persons	13	4.3	5	2.3	8	9.7
Business type						
Family business	10	3.4	8	3.7	2	2.4
Joint venture	155	52.4	87	40.7	68	83
Partnership	131	44.2	119	55.6	12	14.6
Number of partners						
Less than 10 persons people	90	30.4	82	38.3	8	9.7
10 to 20 persons	110	37.2	91	42.5	19	23.2
21 to 30 persons	21	7.1	16	7.5	5	6.1
More than 30 persons	75	25.3	25	11.7	50	61

Table 3 Group Statistics, Tests of Equality of Group Means and Pooled Within-Groups

Groups		Mean		Std. Deviation		Valid N (listwise)	
		Unweighted	Weighted	Unweighted	Weighted	Unweighted	Weighted
Not potential user	Professional Status	3.829		1.616		82	82
	Business Experience	3.719		.503		82	82
	Total of Assets	4.670		.589		82	82
	Total of Liabilities	2.268		.703		82	82
	Share Capital	3.865		1.162		82	82
	Number of Employees	2.329		.903		82	82
	Business Type	2.134		.408		82	82
Potential user	Number of Partners	3.182		1.101		82	82
	Professional Status	4.112		1.640		214	214
	Business Experience	2.607		.702		214	214
	Total of Assets	3.182		.855		214	214
	Total of Liabilities	1.654		.598		214	214
	Share Capital	1.785		.731		214	214
	Number of Employees	1.957		.800		214	214
Total	Business Type	2.514		.571		214	214
	Number of Partners	1.925		.961		214	214
	Professional Status	4.033		1.636		296	296
	Business Experience	2.915		.821		296	296
	Total of Assets	3.594		1.033		296	296
	Total of Liabilities	1.824		.686		296	296
	Share Capital	2.361		1.276		296	296
Number of Employees	2.060		.845		296	296	
Business Type	2.408		.557		296	296	
Number of Partners	2.273		1.148		296	296	

	Wilks' Lambda	F	df1	df2	Sig.			
Professional Status	.994	1.777	1	294	.184			
Business Experience	.631	171.637	1	294	.000			
Total of Assets	.583	209.870	1	294	.000			
Total of Liabilities	.839	56.414	1	294	.000			
Share Capital	.466	337.446	1	294	.000			
Number of Employees	.961	11.854	1	294	.001			
Business Type	.907	30.309	1	294	.000			
Number of Partners	.759	93.438	1	294	.000			
Correlation	1	2	3	4	5	6	7	8
Professional Status (1)	1.000	.094	-.160	-.066	-.123	-.091	.092	-.072
Business Experience (2)	.094	1.000	.071	.075	-.102	-.044	-.037	.005
Total of Assets (3)	-.160	.071	1.000	.626	.679	.096	-.246	.527
Total of Liabilities (4)	-.066	.075	.626	1.000	.434	.043	-.213	.375
Share Capital (5)	-.123	-.102	.679	.434	1.000	.111	-.256	.652
Number of Employees (6)	-.091	-.044	.096	.043	.111	1.000	-.077	.079
Business Type (7)	.092	-.037	-.246	-.213	-.256	-.077	1.000	-.210
Number of Partners (8)	-.072	.005	.527	.375	.652	.079	-.210	1.000

Table 4 Test Results and Log Determinants

Box's M		188.929
F	Approx.	5.046
	df1	36
	df2	85246.131
	Sig.	.000
	Rank	Log Determinant
Groups		
Not potential User	8	-6.382
Potential User	8	-5.467
Pooled within-groups	8	-5.076

Table 5 Eigenvalues and Wilks' Lambda

Function	Eigenvalue	% of Variance	Cumulative %	Canonical Correlation
1	2.023	100.0	100.0	.818
Test of Function(s)	Wilks' Lambda	Chi-square	df	Sig.
1	.331	320.827	8	.000

Table 6 Standardized canonical discriminant function coefficients, structure matrix, functions at group centroids and classification results

Standardized canonical discriminant function coefficients		Function		
		1		
Professional Status		.001		
Business Experience		.642		
Total of Assets		.102		
Total of Liabilities		-.133		
Share Capital		.954		
Number of Employees		.078		
Business Type		-.006		
Number of Partners		-.240		
Structure Matrix		Function		
		1		
Share Capital		.753		
Total of Assets		.594		
Business Experience		.537		
Number of Partners		.396		
Total of Liabilities		.308		
Business Type		-.226		
Number of Employees		.141		
Professional Status		-.055		
Functions at Group Centroids		Function		
Groups		1		
Not Potential User		2.290		
Potential User		-.877		
Classification Results		Predicted Group Membership		Total
		Not Potential User	Potential User	Not Potential User
Original	Count	Groups		
		Not Potential User	Potential User	
		79	3	82
		7	207	214
%		96.3	3.7	100.0
		3.3	96.7	100.0
A 96.6% of original grouped cases correctly classified				