Demand and Supply Conditions of Islamic Housing Finance in the United Kingdom: Perceptions of Muslim Clients

By

Mohammed Elkhatim Mamoun Tameme

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Declaration

I, the author of this thesis, declare that this thesis and the work presented in it are my own and have been generated by me as the result of my own original research. No part of the work that appears in this study has been submitted in support of an application of any other degree qualification in this or any other university. Where other sources of information have been used, they have been acknowledged.

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Mohammed Elkhatim Mamoun Tameme

Abstracts

An important aspect of Islamic finance in the retail market has been the introduction of mortgage products for housing finance. These are offered by a number of banks in the UK. The aim of this research is to examine the characteristics of the UK market for Islamic mortgages and to analyse the activities of the major institutions involved. Supply and demand conditions are explored.

This study evaluates the development of Islamic housing finance in the United Kingdom by focusing on the following main areas: First, it investigates whether there is any effective demand for Islamic Mortgages in the UK. Second, the study evaluates the perceptions of UK Muslims towards various aspects of Islamic mortgages and provides an empirical assessment of these perceptions. Also, the study analyses how Muslim client attitutes and the overall environment affects preferences for Islamic mortgage products. Third, it investigates the factors which might encourage or discourage home-buying among UK Muslims. Fourth, it investigates the current structures of Islamic mortgages and examines whether these play a role in helping low-income groups from the Muslim community to achieve home ownership. Fifth, it investigates the current practices surrounding Islamic mortgages to identify the obstacles and factors influencing decision making with the aim of suggesting possible remedies. The study also evaluates accessibility issues with the objective of defining effective ways of raising awareness in the Muslim Community. It also discusses the marketing of Islamic mortgages and investigates the importance of product awareness by bank staff. Furthermore, it explores in detail the role of religion, Muslim households' consumer preferences and the prospects for Islamic banks cross-selling mortgage products to Muslim customers. Finally this study investigates the factors influences clients' choices of Islamic mortgage providers.

In fulfilling its aims and objectives, this study has utilized both primary and secondary data from the UK. A survey questionnaire was conducted among the Muslim community in London. Non-parametric procedures and tests have been used to analyze the data collected.

The findings of the study demonstrate that there is a gap in home ownership among British Muslims compared to the general public, which is determined by affordability, financial exclusion and information gaps. In addition, this study found that there is substantial potential demand for Islamic mortgages in the UK, which requires effective but also sound marketing strategies. Perception and opinion analysis also indicated that wider social factors and lifestyle choices may be increasing the demand for Islamic mortgages. Moreover, the findings also demonstrate that perceptions of Islamic mortgages are similar between different ethnic and tenure groups. Some Muslim ethnic groups are more willing than others to take on an Islamic mortgage even if it is more expensive than a conventional mortgage.

The study concludes that the prospects of Islamic mortgages in UK are promising and, unlike conventional bank mortgages, they are not financed by borrowing from wholesale markets, but rather from Islamic deposits. Islamic housing finance has proved sustainable, and has not been subject to the problems associated with sub-prime defaults. On the other hand a careful risk appraisal by Islamic institutions providing housing finance has made it more difficult for low-income Muslims or those with less secure employment to obtain *Shariah*-compliant mortgages.

Dedication

I dedicate this work to my loving mother Hajah Lylah, my guiding father Sheikh Mamoun who is a source of inspiration for me, my caring wife Shaza and my wonderful son Mustafa.

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All Praise to Allah *Subhanahu Wata'ala* for his help, blessings and guidance, which has enable me to undertaken and completed this humble work.

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Ameen.

Mohammed Tameme

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Chapter 1

INTRODUCTION

1.1 AN OVERVIEW OF THE RESEARCH BACKGROUND

Traditionally, housing finance has been particularly dependent on the individual attributes of each country's financial, legal and policy systems. The outcome has been that different countries tend to have quite different patterns of ownership, property rights and funding in terms of the institutions involved, the instruments employed, the legal positions of owners, occupiers and financiers and the importance of government with respect to taxation, subsidy and regulation.

Housing provision and policy is in the main outside the remit of the European Union because it is a local asset traded on nationally-based markets. However, the provision of housing and its finance does have a direct impact on a country's relative trading position. Moreover, housing finance is increasingly an intrinsic part of the overall finance system and thus of the single market.

The traditional world of finance, dominated by commercial interest-based banking, could raise potentially troublesome theological issues for Muslims. However, Islamic finance has thrived in the new world, with its downgrading of interest income, financial innovation and blurring of distinctions between commercial banking and other areas of finance. The downgrading of interest (and the concomitant rise of fees as a major source of revenue for financial institutions) has allowed Islamic bankers to side-step the controversial issue of *riba*. Deregulation has fostered the creation of tailor-made Islamic products. Until the 1970s financial institutions were able to sell only a narrow range of financial products. With the lifting of constraints on products that could be devised to suit every need, religious or otherwise, Islamic products could be created.

The Islamic financial services industry has recorded phenomenal growth in recent years. A recent report by the Financial Times estimates the size of the Islamic finance industry at $750 billion. The report breaks up the industry into Islamic financial institutions with estimated combined assets of $250 billion, 250 Islamic mutual funds operating with US$300 billion of assets and another US$200 billion estimated to be held in the Islamic windows of conventional banks (Tett, G. 2006). The essential feature is that it is interest-free. Islam prohibits Muslims from taking or giving interest *(riba)* regardless of the purpose for which such loans are made and regardless of the rate at which interest is charged. The prohibition of *riba* is mentioned in four different sections of the Qur'an. The first emphasizes that interest removes God's blessings from wealth. The second condemns it, placing interest with wrongful appropriation of property belonging to others. In the third reference Muslims are instructed to stay clear of interest for the sake of their own welfare and the fourth establishes a clear distinction between interest and trade, urging Muslims to take only the principal sum and to forgo even this sum if the borrower is unable to repay. It is further declared in the *Qur'an* that those who disregard the prohibition of interest are "at war with God and His Prophet" (Usmani, 1999). The prohibition of interest is also referred to in no uncertain terms in the *Hadith* (sayings of the Prophet Mohammed). The Prophet condemned not only those who take interest but also those who give it and those who record or witness the transaction, saying, "They are all alike in guilt".

From small beginnings in the mid-1970s, Islamic banks today offer a wide range of products: from basic *Shari'a*-compliant retail products, to insurance, mortgages, investment instruments and large-scale project financing. Although Islamic banking remains rooted in the Muslim world, *Shari'a*-compliant products are increasingly on offer in Europe and North America. The industry has been supported at product level by central banks. Following the lead of Malaysia's Islamic Central Bank (Bank Negara) in 2001 the Bahrain Monetary Agency introduced its own *Shari'a*-compliant government bills (a three-month paper known as *sukuk al-Salam*) in an effort to meet Islamic banks' short-term liquidity needs.

Islamic finance gained important momentum in the 1990s, and is now recognised by financial institutions and regulators all over the world. The Islamic financial services industry is the fastest growing component of the international financial services industry, with an annual rate of growth ranging between 15 to 20 percent. It is interesting to note that almost all major multinational banks such as Citigroup, HSBC, BNP Paribas, UBS, Credit Agricole, and Standard Chartered offer Islamic finance. London is one of the main wholesale transacting centres outside the Middle East for this market, yet it is ironic that little by way of Islamic financial products is available to Muslims in the UK. There are thought to be about 1.8 million Muslims in the UK making up three percent of the population. Around 50 percent of these are estimated to reside in the London area. There are also estimated to be about half a million regular Muslim visitors to the UK (Duckers, 2002). In addition, 300,000 Muslim adults in the UK have annual incomes in the range of £30,000 and over (Datamonitor, 1999). A considerable number of Muslims living abroad, mainly from the Middle East, have expressed their desire to own properties in Britain mainly as holiday residences but have been reluctant to embark on an interest-bearing financing facility.

The largest volume of Islamic financing business which is registered in the United Kingdom at present originates in Muslim countries, largely from the Gulf, although there is a large potential domestic market, which is only just beginning to be tapped. The attraction of London for Gulf clients, which include all the major Islamic banks, is the breadth of specialist financial services offered, the depth of the market and the solidity of the major banks, which include all the leading global players. In addition to this, London is nearer to the Middle East than New York, and in a convenient time zone for communications.

Most Gulf businessmen and bankers have English as their second language, and many have long-standing connections with the United Kingdom, where they and their families enjoy spending time. The Arab community in central London is one of the most affluent in the world, and there are many Arab restaurants and hotels which are used to catering for the needs of Muslim visitors. London is also the second most important centre for the Arab media after Cairo, with its own Arabic newspaper and magazines and an Arabic satellite television channel.

So far Islamic finance is flourishing in Europe and many major European banks perceive it as a profitable opportunity to generate new business rather than as a threat to existing business. Islamic finance is about widening choice and in particular about providing non-interest-based finance alternatives (Wilson, 2007). Islamic financial products are available in the UK from a number of high street banks which offer current accounts and mortgages tailored for Muslims. The UK is home to the first wholly *Shari'a*-compliant retail bank in the West, the Islamic Bank of Britain, which was authorized by the Financial Service Authority (FSA) in 2004. The Council of

Mortgage Lenders (CML, 2002) has concluded that Muslims are the fastest growing community in the UK and, as such, emerge as a key yet untargeted market for financial products and services. Datamonitor (2005) quantifies the value of the UK Islamic mortgage market at £164 million; growing at an average annual rate of 68.1 percent since 2000, in comparison with the total mortgage market's average growth of 16.2 percent. A working party, comprising of practitioners and representatives of the Muslim Council of Britain (MCB) and Union of Muslim Organisations (UMO) has been formed with the blessing of the Governor of the Bank of England. This party has prepared a report on the issues of concern and has met several of the officials, regulators, departments and ministries to work out acceptable solutions. The Islamic mortgage market began to take off and more lenders entered the market after the labour government abolished Stamp Duty which had seriously hampered the market.

Many people have argued that Muslims have taken advantage of existing products and are unlikely to abandon them for the new *Shari'a*-compliant products. However, anecdotal evidence suggests that many people would switch to *Shari'a*-compliant products if they were properly structured and competitively priced. Certainly, new buyers would seriously explore these facilities. As the range and scope of these products grows, the whole saving and borrowing pattern of UK Muslims is likely to change, and as the volume of financing increases the underlying ethical base of Islamic financial products would begin to make its mark on the market. At that point, many non-Muslims would also be attracted to these products. In time, these products could provide a valuable bridge between different communities and interest groups in the UK.

There is a paucity of research on Islamic home financing in Islamic finance literature in general and with reference to the United Kingdom market in particular. Even the few studies that exist on the topic are mainly concerned with the supply aspect and working mechanisms of the mortgages models. CML (2002) with a group comprising community representatives and industry professionals prepared a report for discussion with the Governor of the Bank of England to help identify barriers, which could prevent the wider availability of Islamic home finance in the United Kingdom. The report shows that the highest earning group falls within the 35 to 44-year-old age band. This is the stage where the need for consumer finance products is greatest as it coincides with individuals settling down, having families and aiming to address long-term stability and security issues. The study also indicates that Islamic mortgage products may well be attractive to ethical investors. By contrast, Dar (2002) argues that British Muslims have shown a strong desire for Islamic mortgages, but it is not a simple matter of inferring from this that there is an effective demand for any Islamic financial product, rather that there is a need to study the structure of demand for Islamic finance in the United Kingdom at grassroots level. Dar (2004) also found in another later study that while there is no huge demand for Islamic finance at present in the United Kingdom, it is certainly growing and expected to further increase if correct marketing measures are adopted. Matthews et al (2003) examines some micro economic and financial aspects of Islamic housing finance. The system of Islamic mortgages is compared to the conventional system using illustrations from banking practices in the United Kingdom. According to Matthews et al (2003) the core differences between the two systems are found to be that equity ownership is shared under an Islamic system whereas this is not the case under a conventional system.

Datamonitor (2005) quantifies the value of the United Kingdom Islamic mortgages market at £164 million, growing at an average annual rate of 68.1 percent since 2000, in comparison to the total mortgage market's average growth of 16.2 percent. The report indicates that the Islamic mortgages market began to accelerate and more lenders entered the market, after the Labour Government abolished the Stamp Duty which had seriously hampered the market. This is in line with Housby (2005) who believes that the developments in Islamic finance products in the UK during the first few years of the twenty-first century were the product of government policies related to its own political objectives. This confirms the study of Wilson (2006) which examines the experience of Islamic banking in the United Kingdom since 1980, focusing on wholesale operations and retail consumer finance products. Wilson (2006) concludes that the UK government is determined to create a level-playing field for *Shari'a*-compliant products and encourage more competition in the market for Islamic financial services, reducing prices and margins, and making Islamic products more affordable.

1.2 STATEMENT OF THE PROBLEM

Most people in the United Kingdom, including Muslims, want to own the home they live in and are prepared to take out substantial mortgages to do so, with this becoming their biggest single financial obligation. As conventional mortgages are based on interest on the amounts borrowed, the challenge in Islamic finance was to develop acceptable *Shar'ia* compliant alternatives.

The concept of Islamic Housing Finance has become important in both providing permanent housing to the lower and middle class Muslim communities and mainstream Islamic banking systems. My aim in this study is to point the reader towards what I perceive to be the most important theoretical and practical issues associated with the design and construction of Islamic mortgages.

1.3 AIMS AND OBJECTIVES

The aim of this research is to explore the ways and means of Islamic housing finance by focusing on supply and demand conditions in the UK through the perception of Muslim clients. The study also attempts to explore the potential of the industry and the perceived problems associated with Islamic housing finance experience to recognise the obstacles and factors influencing decision-making in order to suggest possible remedies. Furthermore, the study aims to examine the factors determining the potential market for Islamic housing finance and the factors hampering the realisation of the market in the United Kingdom.

To shed light on these issues this study undertakes an empirical research on Islamic housing finance in the United Kingdom, focusing on the following main objectives: First, it investigates whether there is any effective demand for Islamic Mortgages in the UK. Second, the study evaluates the perception of Islamic Mortgages among UK Muslims and provides an empirical assessment of those perceptions. Third, it identifies the Islamic finance products offered by the high street banks in the UK. Fourth, the study investigates the current structures of Islamic mortgages and whether they play a role in helping low-income groups of the Muslim community to achieve homeownership and it also investigates the current practice of Islamic Mortgages in order to highlight marketing issues and recognise the obstacles and factors influencing decision-making and the realization of the market potential and suggest possible remedies. Hence, the topics in which the investigations focused were mainly a perception of the Muslim Communities in the United Kingdom.

After providing empirical evidence, which could be useful in provoking an informed debate on Islamic housing finance in the United Kingdom and elsewhere, the research draws a road map of Islamic housing finance and highlights the necessary policy to improve Islamic housing finance. It concludes by suggesting recommendations for a better and healthier Islamic financial market.

1.4 RESEARCH QUESTIONS

The following questions are proposed to guide the collection, analysis and interpretation of data in line with the research aims and objectives. It is expected that the research will, in the end, provide answers to these questions to ensure the research is designed accordingly. In particular, the study seeks answers to the following questions:

1. What are the challenges and prospects of home ownership for the Muslim community in the UK?
2. What factor/s might encourage/discourage home buying in the Muslim community?
3. Is there any effective demand for Islamic Mortgages in the UK?
4. What are the factors for choosing Islamic mortgages?
5. What is the perception of Islamic Mortgages among UK Muslims?
6. Do current structures of Islamic mortgages help low income groups in the Muslim community to achieve home-ownership?
7. What are the best marketing strategies for financial institutions to promote Islamic mortgages among the Muslim Community?

8. What is the level of knowledge about Islamic mortgages within the Muslim Community?

9. What mode of finance for Islamic mortgages is preferred by Muslims in the UK?

10. Do Muslims prefer to be financed by a branded high street bank rather than other small banks?

11. What are the main choice criteria by which Muslims choose between Islamic mortgage providers?

12. Does importance of the choice criteria vary with respect to the ethnicity and type of tenures factors and if so, what are the main marketing implications?

1.5 RESEARCH METHOD

The principal method used to gather primary data in response to the research questions is a questionnaire survey of Muslim households in London. A period of about three months was spent carrying out this fieldwork, and the objectives were three-fold: to collect all possible and available primary information about Muslim households in London; to obtain information on Islamic Mortgage providers; to gather all available related secondary information pertaining to the research work including different types of reports and articles.

This research is regarded as being explanatory and evaluative since it attempts to investigate the trend, demand, products, preferences, perceptions, obstacles and prospects of Islamic Mortgage in the United Kingdom. It mainly uses a sample survey as this was thought to be the most suitable way of achieving the research objectives, especially based on the nature of the data required and the purpose for which it was to be used. The study uses a combination of a review of the literature and a survey investigation approach, which offers the most appropriate and satisfactory methodology in carrying out this research.

Data from an area of East London which represents the Muslims community is used to answer the research questions. The researcher used mainly primary data to suit the nature and purposes of the research, which was to elicit respondents' opinions, perceptions and attitudes. The survey approach using a questionnaire is thought to be the most appropriate technique in collecting the intended primary data. Also the investigation of this study is based on secondary data obtained from journals, magazines, the web, reports and books.

1.6 LIMITATIONS OF THE STUDY

Like any other research projects, this research has its limitations. They are:

a. The ability of the respondents to comprehend the questions asked. The respondents' comprehension of the questions in the questionnaire could be at various levels, whether low or high. There is a limitation in knowing whether the respondent has been diligent enough to ask, if in doubt, via personal email and mobile phone, through contact information given at the introduction of the questionnaire for correspondence purposes, or if the respondent had any questions to ask.

b. The diligence of the respondents in answering the questionnaire all the way through, honestly and earnestly, instead of simply for the sake of putting down an answer.

c. The data collection method was limited to the survey questionnaire without including other methods, for example focus groups and semi-structured interviews.

d. It would have been more beneficial if more respondents were surveyed. However, due to a limitation of the resources, budget and time, this was not possible.

e. This study will be on Islamic housing finance in the United Kingdom only.

f. The measures introduced in this study could be refined and made more robust. This will be the subject of later studies.

In addition to the limitations mentioned above a number of difficulties were encountered during the course of this research. These include:

a. Getting More Respondents

There was difficulty in getting respondents to fill in the questionnaire. Respondents might have been put off by the questionnaire being rather long and containing personal financial information. It would have been better if more questionnaires were completed, but there was a time and budget constraint. It was not possible to stay in London for longer than three months and therefore it was also not possible to get more respondents. However, it was still satisfying to have 250 of the questionnaires that had been sent out returned.

b. Analysing

There was also difficulty in analysing some of the respondents. Sometimes, there were people who did not fill in the questionnaire properly, for example, instead of noting down the ranking numbers to the answers given they just ticked the appropriate answers. Or sometimes they skipped some of the questions. The researcher did not notice this mistake when the questionnaires were given back to him so by the time the questionnaires were finally looked at, it was difficult to trace the respondents as they were not asked to give their names for reasons of anonymity.

The results of the survey are generally applicable to the rest of the Muslims in the United Kingdom, based on the fact that the British Muslim community is homogeneous and any segment of the population should be a fairly accurate representation of the Muslim population as a whole in the United Kingdom.

1.7 STRUCTURE OF THESIS

The plan of the research work is spread over nine chapters, including the introduction, with the chapters covering a number of interrelated topics.

Chapter 1: Introduction – a brief mention of the background of the research which highlights the importance of housing finance, the development and fast growth of

Islamic finance and emergence of Islamic mortgages. There is also a section on the focus of this research which lists the research questions that it attempts to answer and also states the research method used in data collection. The aims and objectives were also stated in order to understand what this research hopes to achieve. Lastly, the significance of the study is also mentioned to enable the reader to appreciate the importance of conducting this research.

Chapter Two: Housing Provision and Financing: A Literature Review - This chapter provides an overview of housing finance systems in general and homelessness in the EU in the context of the EU's concern with social cohesion and exclusion. It also covers the definition and nature of homelessness; the extent to which it exists; reasons why it exists; the characteristics of homeless people and trends in the homeless population; and rights and services for the homeless. The main theme of the chapter is to identify similarities and distinctions in the national homelessness situations across the EU. The chapter ends with a discussion of the implications of this analysis for the role of the EU in tackling homelessness in the member states.

Chapter Three: Islamic Home Finance Principles and Practice - The main objectives of this chapter, which covers theoretical and practical issues, is to explore the ways and means of providing Islamic housing finance. It discusses the principles of the Islamic financial system and contracts. This chapter also attempts to explore and discuss technical issues relating to *Fiqh* as well as economic aspects of Islamic housing finance to clarify the modes and instruments suitable for this purpose endorsed by *Shari'a.* It provides an overview of the application of Islamic housing finance across the world and also discusses the role of the *sukuk* in Islamic housing finance and covers the regulatory, legal and financial obstacles.

Chapter Four: Islamic housing Finance in the UK: the Supply Side - The aim of this chapter is to assess the supply of Islamic housing finance in the United Kingdom. A brief overview of Islamic housing finance in the UK is provided, together with detailed discussions of the relevant financing techniques. In addition, this chapter discusses the remaining legal and regulatory issues involving the Financial Services Authority, as well as tax matters involving Her Majesty's Treasury. The market experiences have been examined and the products and services offered by Islamic windows of the high street banks and the wholly British Islamic Bank have been compared. The political economy of Islamic housing finance in the UK has been monitored and finally the prospects and future of Islamic housing finance in the United Kingdom have been studied.

Chapter 6: Sample Characteristics and Homeownership among British Muslims- This chapter aims to present the demographic and the work related characteristics of the Muslim households who responded to the questionnaire conducted by this study. It also provides personal information about the Muslim households in UK including gender, age, marital status, ethnic origin and qualifications. In order to conduct the data analysis for the primary data descriptive statistics were employed in this chapter. Basically this chapter responds to research questions 1 and 2.

Chapter 7: The Market Potential - This chapter aims to cover, explore and evaluate the development of the demand for Islamic mortgages in UK. In doing so we can make particular use of empirical evidence, drawn from the questionnaire, for Muslim households seeking Islamic mortgages in the east London area. This chapter also provides the results of the cross tabulations and statistical tests and mainly focuses on responding to research questions 3, 4, 5 and 6.

Chapter Eight: Marketing Strategies – This chapter mainly discusses the marketing issues which Islamic mortgage providers need to consider when promoting Islamic mortgages among the Muslim community in the United Kingdom. The chapter responds to research questions 7, 8, 9, 10, 11 and 12.

Chapter Nine: Conclusion – This chapter presents a summary of the findings of the research questions. These findings are discussed and recommendation policies have been derived on the supply side and the demand side and general recommendations for the policy makers have been suggested on theoretical, institutional and practical levels. Also, questions arising from this study are used to propose an agenda for future research.

Chapter 2

HOUSING PROVISION AND FINANCING: A LITERATURE REVIEW

2.1 INTRODUCTION

In this chapter, I will provide an overview of housing finance systems in general and homelessness in the European Union in the context of the EU's concern with social cohesion and exclusion. I will look at: the definition and nature of homelessness; the extent of homelessness; explanations of homelessness; the characteristics of homeless people and trends in the homeless population; and rights and services for the homeless.

The main purpose of the chapter is to identify similarities and distinctions between the national homelessness situations across the EU. There is a particular focus on the quite different ways in which it is conceptualised and explained in different countries, and whether these distinctions reflect genuine differences in the phenomenon or simply different political and scientific perspectives. The chapter ends with a discussion of the implications of this analysis for the role of the EU in tackling homelessness in the member states.

2.2 HOUSING FINANCE SYSTEMS: AN OVERVIEW

The phenomenon of regular patterns of housing and land uses centred on urban developments has been commented upon by economists since the 1760's (Steuart 1769, Van Thunen 1875, Schumpeter1954). In the first phase of major industrial development their interest centred on agricultural land use patterns around cities and the geography of intra-urban land uses (Hurd, 1903) cited by (Merrett.A.J,1965). Early neoclassical economists were mostly concerned with housing. It was only in the 1920's that researchers began to focus on urban economics, land economy and housing economics.

As a result of academic and policy pressures relating to North American cities the sub-discipline now known as urban economics was established, which emphasises two major strands of residential structure of the city:

1. The large scale inductive and deductive studies concerning the social or ecological structure of cities undertaken in Chicago (Robson, 1969; Timms, 1971).

2. The development of land economy as a discipline to describe and explain the economic operation of housing and land markets (Ratcliff, 1949).

The services provided by houses over an individual's lifetime make them assets which provide security and are also an investment. These services include shelter, comfort, independence and privacy. They can exist in a number of combinations and in varying quantities. For example, owner occupiers benefit from investment characteristics which do not exist for tenants of rented accommodation In addition, shelter services can offer very basic protection from the elements, or can provide luxuries including central heating or air conditioning and large and numerous rooms *etc.* Housing is a diverse commodity, the services of which can be accessed to varying degrees and in a range of combinations. The complicated nature of the housing sector renders it a challenge as it involves sociology, geography, demography, architecture and political forces, and takes into account fundamental trends in economics, problems of finance, the risk of illiquidity and matters relating to valuation. The fact that all institutions own commercial real estate somewhere in their portfolios warrants an accurate understanding of factors which can influence the value of real estate, such as market forces, and the idiosyncratic nature of a particular property, including its location history, visibility, and the neighbours (Booth, Cashdon, and Graff 1989).

Social stability and economic development are greatly influenced by housing finance which provides individuals the means to purchase an asset which will represent their largest single investment. According to the World Bank, 40 percent of households' monthly expenditure is taken up by housing worldwide. This accounts for between 75 and 90 percent of household wealth worldwide and represents up to six times their annual income (WB stat.2001). In terms of economic development, housing as a durable asset investment accounts for between 15 and 35 percent of aggregate investment worldwide (WB stat 01). In addition to providing benefits for individuals housing supports a wider economic. Worldwide, five percent of the labour force is involved in residential construction and four percent in real estate services (WB stat. 2001).

Attitudes to housing finance differs from country to country according to cultural values, financial systems and varying government policies, bringing diversity in terms of home ownership, mortgage debt, house prices, inflation rates, and so on. The different financial, legal and policy systems in particular affect housing finance. For this reason we can see very different patterns of ownership, property rights and all aspects of financing

As a local asset traded on nationally-based markets, housing provision and policy is not subject to European Union policy. . Nevertheless a country's trading position is directly affected by housing provision and finance. Housing finance is also increasingly an intrinsic part of the overall single market.

In 1984 the European Community looked at the potential standardisation of housing finance in relation to a draft directive on mortgage credit (Commission of the European Communities 1984). A report by the House of Lords Select Committee at that time concluded that harmonisation and mutual recognition of finance institutions, and indeed savings and mortgage instruments, were only a small element in the overall question of effective competition. Housing and its finance were seen to be fundamentally grounded in the different nature of legal systems and institutional structures as much as in taxation and subsidy policies or the right to trade and operate across borders. Without greater convergence across the whole range of factors, they argued, housing finance systems would be likely to remain quite separate and to continue to develop in different ways (House of Lords Select Committee on the European Communities, 1985). In the end the draft directive came to nothing and the whole question of housing finance became subsumed into the wider question of banking regulation, which was itself addressed through the Second Banking Directive in 1989 (Commission of the European Communities 1989; British Bankers' Association 1990).

2.3 HOMELESSNESS AND SOCIAL EXCLUSION

'Social cohesion' became an objective of the European Community by virtue of the Single European Act 1987 (Article 130 A-E). This has since been interpreted as a competence to combat 'social exclusion' (House of Lords 1994). The European Commission argues that social exclusion is a more dynamic concept than poverty, referring to processes as well as outcomes, and is also broader, relating to marginalisation in all aspects of social, political and economic life, as well as income deprivation. The House of Lords Select Committee on the European Communities provides a useful summary:

Income poverty and social exclusion is not co-terminus; poor housing and health care, unemployment and lack of training, old age and single parenthood may all interact and react with low income to restrict economic and social opportunities with the result described as social exclusion. (House of Lords l994: 7)

Homelessness is perhaps the most extreme manifestation of social exclusion, representing the denial of a fundamental requirement of social integration: adequate shelter. Therefore as a marginalised groups the homeless are entitled to help, under European Union programmes, to combat social exclusion. However to qualify for funding from these Structural Funds a homelessness project must combine education, training or work creation with accommodation, and must not be concerned solely with the re-housing of homeless people. EU funding has been granted for homelessness projects under the Horizon programme which provides training and job creation for disadvantaged groups. Funds have also been secured for the Foyer hostel network, which offers accommodation and training to young people (Stephens *et al.* 1997). However such EU assistance to homeless people has thus far been very limited in scale.

The United States of America does not, contrary to some assertions, exhibit an unusually large mortgage sector, relative to its GDP, when compared to Canada. Measuring the relative size of the domestic mortgage market in terms of the value of outstanding residential mortgage debt to GDP, the relative size of the residential mortgage market in the USA (53 percent) exceeds that in Canada (43 percent) even though several other developed countries have higher percentages (see Courchane and Nickerson, 2001).

No country matches the USA in commonly offering both a 30-year term to maturity and a mortgage rate fixed over the life of the loan and Canada has only recently introduced any instrument comparable. The average period of time over which the mortgage rate is fixed in Canada is considerably shorter than that in the USA, whether the mortgage is adjustable rate (ARM) or fixed rate (FRM). Over all types of mortgages the average mortgage term length in Canada is only three to five years, substantially shorter than that most commonly found in the USA (30 years).

Loan-to-value (LTV) ratio requirements are similar in both countries, though Canada was much later than the USA in allowing for ratios higher than 75 percent. Both countries require mortgage insurance for high LTV mortgages, though borrowers can often avoid this by taking a first mortgage at 75 or 80 percent LTV and a second mortgage (home equity line or line of credit) for the remainder.

Rates (and spreads) remain relatively lower in the USA than in Canada. As of 11 November 2001, 30 year fixed rates in the USA averaged only 6.56 percent (the spread over ten year treasuries was at about 1.33 percent). The longest fixed term that could be found in Canada (at Royal Bank) was 25 years, and this came with a large price differential relative to the USA. However, ignoring fixity of term, rates were generally higher on Canadian mortgages, while ten year treasury bond rates remained similar across the two countries, leading to relatively higher priced mortgages, in investment terms, in Canada than in the USA.

Even with the difference in rates and terms, Canada has a rate of homeownership quite comparable to that of the USA. In a survey of 20 developed countries, most countries have rates from approximately 10 to 30 percentage points lower than that of the USA. However, in 2000, the rate of homeownership in Canada was 64 percent, while that in the USA was 67 percent. Owner-occupancy rates were similar: 64.7 percent in Canada and 67.1 percent in the USA.

What explains this difference? Clearly Canadians pay relatively higher mortgage rates, often seem to require relatively higher down-payments, and bear much more interest rate risk than US homebuyers. In addition, Canadian homeowners lack the income tax incentives provided to Americans through home mortgage interest deductibility. Still, as evidenced by the high rate in Canada, homeownership is clearly valued. In this paper we will explore some of the historical trends in public policy relating to housing, and some of the characteristics of the economies in the two countries, in an attempt to account for the similarity of homeownership rates, in the face of decidedly different costs.

2.4 PUBLIC MORTGAGE AND HOMEOWNERSHIP ASSISTANCE PROGRAMS

In this section I will detail and contrast the housing policies in the USA and Canada that have resulted from specific public policy objectives in the two countries. While many of the programs still extant in the USA resulted from Great Depression policies, Canadian homeownership programs tend to have been more recent.

2.4.1 United State of America

Many of the programs that we observe today in housing finance markets in the USA have evolved from public policy programs established during the Great Depression. During this time much focus was placed on ensuring that every American had the possibility of homeownership. The National Housing Act of 1934 (and its 1938 amendments) states, “The Congress affirms the national goal that every US family be able to afford a decent home in a suitable environment”. An enabling factor was the incentive provided in the tax code in 1913. The code stipulated that mortgage interest would be a deduction against income taxes for all tax-paying Americans who chose to itemize deductions. This deduction remains one of the largest for the majority of homeowners today.

The Depression programs followed the tradition of the Federal Farm Loan Act of 1916. That act focused exclusively on providing credit for farm mortgages, but it established the practice of using credit support to affect public policy agendas in mortgage markets. This is clearly not the only means available to support policy.

Housing policy in the USA has been comprehensive in its objectives for decades. A small part of statement 42 USC §12702 has been extracted here:

> The objective of national housing policy shall be to reaffirm the long-established national commitment to decent, safe, and sanitary housing for every American by strengthening a nationwide partnership of public and private institutions able to provide every American community with a reliable, readily available supply of mortgage finance at the lowest possible interest rates.

Clearly housing matters; this statement of policy includes aspects of mortgage finance (including rate determination), of federal assistance, of social policy and of income re-distribution. Where did this comprehensive emphasis on housing policy come from? When the National Housing Act was passed in 1934, mortgage markets were troubled in many respects. Over two million construction workers became unemployed. Mortgage loan terms were difficult, often requiring 50 percent LTVs with terms of only three to five years, followed by balloon payments. Only four in ten households owned homes.

After the Federal Farm Loan Act of 1916, further assistance for farm lending came from the establishment of the Federal Home Loan Bank System (FHL Bank System) through the Federal Home Loan Banks Act (FHLB Act) in 1932. The FHL Bank System was established by Congress to increase liquidity in mortgage markets by providing a source of short-term funds (advances) to approved primary mortgage lending institutions (savings and loan associations). Originally, only thrift institutions (savings and loan associations and savings banks) and insurance companies were allowed to be members of the FHL Banks. The FHLB Act also established the Federal Home Loan Bank Board, a regulatory agency intending to supervise the mission and safety and soundness of the Federal Home Loan Banks (FHL Banks). The FHL Banks have acted traditionally as sources of short-term credit for member institutions, which primarily held portfolios of long-term residential mortgage loans. Hence, the mechanism used for effecting housing policy in this instance was through the provision of low cost funding to the actual originators (the FHL Bank members) of the mortgages.

In 1933 another housing act, the Home Owners' Loan Act, provided for chartering and regulation of the savings and loan institutions (S&Ls). These institutions were the primary lenders to homeowners during this period. Several other primary housing agencies were established during the Great Depression including, under the National Housing Act of 1934, the Federal Housing Administration (FHA). Its mission was to improve both housing standards and conditions and to provide “adequate” home financing through the insurance of mortgages. It was also intended to stabilize the mortgage markets. When the Department of Housing and Urban Development (HUD) was established in 1965, FHA was consolidated into HUD. While its mission today has broadened, its focus is housing. In particular, its mission currently includes contributing to the building and preservation of healthy neighbourhoods and communities, maintaining and expanding homeownership and rental housing, and stabilizing credit markets during economic disruptions. FHA pioneered the long term amortizing loan, instrumental in the prevalence of the 30-year fixed rate mortgage in the USA. FHA continues to insure mortgages, insuring over 24 million since 1934, including 38,000 multifamily apartment projects.

While broader in scope than just housing support, the Federal Deposit Insurance Corporation (FDIC) was another Depression program created in 1933. The intent was to support the financial institutions that fund housing. Its express mission was, and remains today, to maintain the stability of and public confidence in the nation’s financial system, through its insurance of deposits and its supervision of safety and soundness at state non-Federal-Reserve-member banks. Since its establishment, the USA has not witnessed bank panics such as those observed during the Great Depression, and it is in some large measure due to this that the funds are available to lend to homeowners.

While the programs above pertained to the primary market for mortgages, the Great Depression also led to the creation of a secondary market. Congress created Fannie Mae in 1938 to support housing through the purchase of FHA-insured loans. In fact, at its inception, Fannie Mae was part of the FHA. It channelled funds through mortgage originators of FHA loans, targeting investment funds to housing. While today Fannie Mae is private (as of 1968) and does not receive government funding, its mission focuses on increasing the affordability and availability of homeownership for low-, moderate-, and middle- income Americans. Fannie Mae and the FHL Bank System are two of the government-sponsored enterprises (GSEs) that comprise the secondary mortgage market in the USA. The third, Freddie Mac, was established in 1970 as the Federal Home Loan Mortgage Corporation (FHLMC) and is subject to the same mission and safety and soundness regulation as is Fannie Mae. Their mission regulator is HUD, while their safety and soundness regulator, as of 1992, is the Office of Federal Housing Enterprise Oversight (OFHEO). All three of the GSEs support housing through the mortgage finance mechanism of providing funding to other institutions that actually originate the home loans. However, only the FHL Banks can also originate mortgages.

Additional federal programs provided some support for the housing and mortgage markets in the USA. For example, the Veteran's Administration (VA) was established in 1944 under the Serviceman's Readjustment Act, to enable servicemen returning from the war to obtain low cost housing funds. The Farmer's Housing Act (FmHA), later the Rural Housing Service (RHS), provided farm and rural housing loans. The establishment of HUD in 1965 moved many of these programs under a central administrative authority. Ginnie Mae, established through the Government National Mortgage Association (GNMA) (1968) served low- and moderate-income borrowers and guaranteed FHA, VA and RHS loans, essentially assuming the credit risk and providing an incentive to lenders to fund these loans relative to conventional (non-government-insured) loans.

While the above discussion only briefly mentions a few of the many public policy programs and objectives that support and finance housing in the USA, even this brief discussion highlights the importance that public policy has placed on homeownership. Much of the US public policy focus has been on public and private partnerships that focus on the supply side of funding – not direct subsidies to homeowners.

2.4.2 Canada

The Canadian federal government supports homeownership through the Canadian Mortgage and Housing Corporation (CMHC), a federal crown corporation (similar in some respects to a US government-sponsored enterprise) that was created in 1954 to be the Canadian government's national housing agency, established to provide access for Canadians to a wide choice of quality, affordable homes. The broad mandate of the CMHC is to promote the construction of new houses, the repair and modernization of existing homes, and the general improvement of the living conditions for Canadians. The focus has been, and continues to be, on the supply of housing units in the private sector, with the approach being on introducing a series of programs designed to make homeownership a practical option and to assist in reducing the likelihood of mortgage defaults. This is significantly different from the federal government support in the USA that focuses more on market financing and market stability and much less on direct schemes to assist homeowners to acquire and remain in homes (Carter, 1997).

The timing and evolution of public policies toward housing were quite different in the USA and Canada. There were two key reasons why no national housing policy existed in Canada until recently. First, Canadians shared roughly similar housing circumstances, so that few thought they were disadvantaged. In fact, the prevalent social perspective was that financial difficulties implied moral degeneracy (Anderson, 1992). Second, governments had limited funds with which they could intervene, even if desired. The Canadian federal government only chose to become involved in housing matters after the Halifax ship explosion in December 1917 that killed over 1,600 people and virtually flattened the city. At the end of the First World War, the Canadian federal government provided approximately $25 million in loans for housing. The first national housing program, which lasted from 1919 to 1923, provided over 6,200 dwelling units in 179 municipalities, but was regarded as wasteful and inefficient (Anderson, 1992). During this period, the government's general tenet indicated a preference for reliance on the private market to provide housing.

Just as in the USA, the Great Depression brought serious housing shortage problems. Subsequent to several government reports, the Dominion Housing Act (DHA) of 1935 authorized the Minister of Finance to join with lending institutions or local housing authorities to loan funds for new housing construction, but not for renovation of existing housing stock. The Bill introduced the concept of blended payment mortgages, risk absorption by the government and longer amortization periods. Notably, the DHA did not establish a national housing agency despite numerous discussions in Parliament, and it capped the mortgage interest rate at 5 percent, despite numerous complaints from lending institutions (Hulchanski, 1990). In 1937 the Canadian government introduced the Home Improvement Loans Guarantee Act that allocated funds for renovations. This program persisted until the late 1980s but with very limited success.

In 1938, just a few years after the US NHA was passed, Canada passed its first National Housing Act (NHA) reaffirming the DHA while making available far more funds for loans. In 44 months there were 15,000 loan applications (Anderson, 1992). Further legislation just before the Second World War provided for the Central Mortgage Bank, operated by the Bank of Canada, which permitted any financial institutions to join by agreeing to keep mortgages for farms at rates not to exceed 5 percent and on homes not to exceed 5.5 percent. Though only short-lived, the Central Mortgage Bank was the precursor to the CMHC, and reaffirmed that, in Canada, the government intended to confine itself to activities in the housing market that avoided conflict with the private sector.

No further housing legislation was introduced until 1944, apart from the creation of Wartime Housing Limited in 1941 (similar to the US VA), whose mandate was to assist in housing munitions workers and their families. In 1944, the Curtis Report, one of several reports requested by the government on housing issues recommended, among other things, that equity for mortgages be reduced to 10 percent from 20 percent and that the government provide mortgage insurance to assist middle- and low-income families to qualify for loans. The subsequent 1944 NHA fell far short of the recommendations as it only provided initiatives for new housing construction in the post-war period. The government moved closer to a national housing policy with the 1945 Central Mortgage and Housing Act that allowed for a crown corporation that would serve as an instrument for public housing policy and an administrator of federal housing funds. The first task of the CMHC, similar to the US VA, was to house the families of veterans. However, the chronic shortage of affordable housing remained and there were still insufficient mortgage funds available.

The housing situation deteriorated even further following the post-war baby boom coincident with high immigration. Immigration in 1952 increased more than ten-fold and totalled 221,000 relative to only 15,000 in 1945. The 1954 NHA attempted to address the housing finance shortage by enabling chartered banks, for the first time, to provide government mortgage loans, with CMHC providing mortgage loan insurance. This insurance program, financed by borrower premiums, is still intact. This compares, broadly, to the provision of mortgage insurance by Ginnie Mae on FHA, VA, and RHS loans in the USA. The new Act was successful – in one year the number of new loans jumped by more than a third, and between 1954 and 1956, banks provided mortgages for more than half of the homes built under NHA.

The insurance is available for both new homes and existing units, though initially it was only for new homes. Currently, a loan-to-value ratio of 75 percent is the cut-off for the requirement for default insurance (compared to the 80 percent cut-off in the USA); the introduction of this programme increased mortgage funding under NHA, mainly from banks that had been reluctant to enter the government mortgage market. The total value of outstanding mortgages insured by CMHC exceeded $200 billion in 2000 (CMHC, 2001), and over 460,000 mortgages were insured in that year.

While chartering banks for residential lending under NHA was initially successful, by 1957, which marked an economic downturn as well as the end of a long era of a Liberal Canadian government, the banks were failing to provide adequate mortgage funds as a result of the (then) 6 percent legislated ceiling on mortgage interest rates. In the decade from 1957 to 1967, the CMHC funded more homes than did the banks. This led the government to introduce a new formula for setting the NHA mortgage interest rate in 1966, and finally led to deregulation of interest control in June 1969, so that the only difference between NHA and conventional loans was the default protection provided by the mortgage insurance for the NHA loans (Hulchanski, 1990). These initiatives followed a slump in housing starts. Simultaneously, the term for NHA loans was reduced from 25 years to five years, and then to three years in 1978. This reduced the interest rate risk of lenders and so provided an incentive for private sector funding of mortgages; but it simultaneously shifted the interest-rate risk to borrowers, while providing them with a range of term options to help limit the risks. Clearly both of these changes were made to persuade lenders to become more vigorous participants in housing finance. It is unclear why both changes were made simultaneously but clearly both benefited the banks and imposed costs on homeowners.

Various programs were implemented during the 1970s and 1980s, periods of high and unstable interest rates, to assist homeowners in meeting their payment schedules and to protect them from the rapidly rising rates, which were seriously impacting payments, given the short-term loans commonly offered by institutions. Home buying in urban areas became especially difficult, even for two-income families, with the unprecedented house price inflation. For example, between 1972 and 1974, the average multiple listing service (MLS), sale price increased from $26,595 in 1972 to $41,057 in 1974, a rise of 54 percent (Fortin and Leclerc, 1999) while the average Canadian salary increased by only 22 percent (Hulchanski, 1990). Fortin and Leclerc estimate the change in the real housing price between these two years at 29 percent. Further evidence of the homeownership crisis is given by the decline in the CMHC's measure of the percentage of renters of prime home-buying age (25 to 44 years old) able to buy the average-priced house. This index fell from 50 percent in 1971 to 17 percent in 1975 and to 7 percent in 1981 (CMHC, 1985).

The Assisted Homeownership Program (AHOP), introduced in 1973 when over 36 amendments were made to the NHA, provided borrowers with monthly payments from CMHC intended to equate their net monthly mortgage payment to that which would result under an 8 percent per annum interest rate. These interest reduction loans were secured by a second mortgage, but were interest-free for five years. The provincial governments also assisted by augmenting the grants received by first time homeowners enrolled in AHOP. The program was discontinued in 1978 as a result of high default ratios in regions where house capital appreciation was not sufficient to cover the high ratio first mortgage and second mortgage debts (Jones, 1998). Over 94,000 households enrolled in the program (Hulchanski, 1990). In 1974 another program was instigated that provided cash grants for down payment assistance (First Time Home Buyer Grant Program). In 1972, lenders were required to consider any or all of a spouse's earnings, rather than the 50 percent limit imposed in 1968 (Carter, 1997).

The CMHC and provincial governments also tried other programs to alleviate the real payment tilt burden and assist the housing market during the early 1980s slump. The gross debt service ratio used in the loan underwriting process was gradually increased from 23 percent of gross income in 1945 to 32 percent in the early 1980s (Carter, 1997). The Canada Mortgage Renewal Program (CMRP), introduced in September 1981, provided assistance to those renewing loans in the form of grants and deferred interest options. This was curtailed in late 1983 with the CMHC replacing it in 1984 with the Mortgage Rate Protection Program (MRPP) that provided insurance protection from interest rate increases to those holding NHA mortgages. Perhaps not surprisingly, given its implied catastrophic risk, the program was prohibitively costly to the loan holder (a flat premium of 1.5 percent of the loan) and restrictive in benefits (e.g. a $70,000 maximum loan size, 12 percentage point cap on interest rate increases). Predictably, given declining interest rates, few borrowers have availed themselves of the protection (Lea and Bernstein, 1995; Jones, 1998).

An alternative approach to promote homeownership from these mortgage-based plans (e.g. low-down payment and government insurance), encourages household savings for down payments. Unlike the USA, the Canadian government has used several such schemes over the years. The Registered Home Ownership Savings Plan (RHOSP), begun in 1974 and ended in a tax reform measure by the Conservative government in 1985, enabled renters (each spouse in the case of a married couple) to establish a RHOSP account in which deposited funds (limited to $1,000 per annum) were tax deductible and the interest earned was free of income tax. Participation peaked around 20 percent for renters aged 25 to 29 years and then declined with age, though over time a greater proportion of households with heads aged 35 to 39 participated. Contributors to RHOSP had higher median incomes than non-contributors, so the program likely benefited higher-income households more than lower-income households (Engelhardt, 1997). Moreover, Engelhardt (1996) shows that most contributions to this savings program constituted new net savings, which leads him to recommend the use of such a targeted tax-based savings program for the USA, assuming that household behaviour for the USA is similar to that for Canadians. However, a variety of very low down payment programs are available for homeowners in the USA. Targeted savings plans impose clear costs on the federal government (foregone tax revenues) and were necessitated by the lack of program offerings provided by the private lenders in Canada.

Similar assistance plans included the Canada Homeownership Stimulation Plan (CHOSP), introduced during the 1982 downturn, which provided $3,000 cash grants to help with home purchases, and the Canada Home Renovation Plan (CHRP), also begun in 1982 to further stimulate residential construction, which made available up to $3,000 in a cash grant. These programs, though popular, were expensive and typically failed to assist lower-income households. CMHC (1986) estimates that the CHOSP cost $800 million and CHRP $230 million. Furthermore, Dowler (1983) reports that the RHOSP costs about $100 million per year.

The federal government introduced the Home Buyers' Plan (HBP) in 1992 to assist would-be homeowners raise sufficient down payment funds. It allows Canadians to withdraw up to $20,000 from their RRSPs (Registered Retirement Savings Plans). It is difficult to ascertain whether the program has resulted in simply a transfer of funds from RRSP savings to homeownership or in a net gain in tax-sheltered savings. In 1992, the CMHC extended its insurance program through the introduction of the First Home Loan Insurance (FHLI) program, allowing first-time homebuyers to have 95 percent LTVs and still qualify for CMHC insurance.

Apart from these described savings programs, the government has not used the tax system to stimulate homeownership, except to exempt the family home from capital gains tax in 1972, thereby enabling homeowners to fully benefit from capital appreciation. The foregone revenue from tax exemption of capital gains on houses is estimated to be well in excess of $1.5 billion annually. Unlike the USA, Canada does not allow homeowners to deduct mortgage interest and property tax payments from taxable income, despite this being in the election platforms in 1978 and 1989.

While there is much debate in both political and academic circles on mortgage interest deductibility (e.g. Green and Vandell, 1999; Dreier, 1997; Voith, 1999; Bourassa and Grigsby, 2000 and the associated comment articles Weicher, 2000; Vandell, 2000), the Canadian government remains unconvinced even though some research suggests that the demand for mortgage debt is highly responsive to changes in the mortgage interest deductibility (e.g. Follain and Dunsky, 1997. Unlike Canada, the USA continues to allow home mortgage interest deductibility for several reasons. Congress believes that the tax concessions encourage homeownership; that eliminating the deductions may cause a significant drop in the market value of homes (e.g. Capozza *et al.*, 1997); that distortions in the tax code may increase rather than decrease (e.g. Woodward and Weicher, 1989) if the deductions are eliminated; that the volume of housing construction is higher with the deductions than without; and finally, Congress may be persuaded by the political lobbying of several housing trade associations (Bourassa and Grigsby, 2000).

In summary, while the Great Depression engendered National Housing Acts in both the USA and Canada, the subsequent approaches of public policy towards housing differed significantly in the two countries. The USA focused on stimulating the provision of funds to housing through the establishment of government-sponsored enterprises (FHL Banks, Fannie Mae, and Freddie Mac) but without interference in pricing mechanisms (such as interest rate caps). Canada had more limited success in targeting funds to housing, partly because they capped prices that private institutions could charge for mortgages. The USA uses the tax code to stimulate homeownership, Canada does not. Rather, it attempts to stimulate private investment in housing through support of housing savings programs. Finally, the secondary market in Canada is much less well established than that in the USA, certainly implying that the availability of funds for housing depends more on just a few large lenders (given the concentration of banking in Canada) than on funds raised through global capital markets. In spite of these considerable differences, both countries have achieved notable success in attaining high homeownership rates.

2.5 DEFINITION AND FORMS OF HOMELESSNESS IN THE EU

There is a wide range of official and unofficial definitions of homelessness employed within the EU, reflecting different national perspectives on the issue, and the views of various commentators whose interests are served by either minimising or maximising the scale of the problem. In the absence of any agreed common definition of homelessness, the European Federation of National Organisations Working with the Homeless (FEANTSA) offers the following working definition:

1. People who are roofless.
2. People who are living in institutions because they have no other place to go.
3. Those living in insecure accommodation.

4. Those living in entirely substandard or inappropriate accommodation (Harvey 1994).

This definition offers a useful broad outline but is clearly open to a great deal of subjective interpretation. For instance, how 'substandard' must accommodation be to constitute homelessness? One must always be careful in attempting to include all groups who may legitimately be regarded as homeless, so that the term does not become over-extended to the point where it includes everyone who is not adequately housed, and therefore becomes entirely useless. The above typology also fails to capture the dynamics of homelessness; it does not distinguish, for instance, between the completely dissimilar situations of the short-term and the chronically homeless. Furthermore, it is clear that the concept of homelessness, like 'home' from which it is derived, is not a purely housing based concept and has social and psychological dimensions, which are not acknowledged in FEANTSA's definition. However, it must be conceded that any definition, which attempts to incorporate all these meanings of homelessness, will be too complex and abstract to be of any practical use, and it is perhaps inevitable that a working definition be reduced to the housing dimension.

One further point should be made regarding the definition of homelessness. FEANTSA, like many other commentators, has argued that homelessness is a relative rather than absolute term, to be judged by the standards prevailing in a particular society at a particular time (Daly 1992). This position seems sensible, and sits well with the concept of social exclusion. However it would appear to undermine FEANTSA's call to the national governments of the EU to adopt a common definition of homelessness, given the still widely varying housing and social conditions found across Europe.

We now turn to the specific types of accommodation occupied by homeless people in the EU, and the similarities and differences between countries in the form which homelessness take.

Rooflessness is apparent in major cities throughout the EU, but there are some important differences between northern and southern Europe. Significant numbers of 'street children' and roofless families can be found in Spain, Portugal, and Greece, and in some parts of Italy. In the northern countries most roofless people are single adult males, although single women and young people form an increasing proportion of rough sleepers. Roofless children or families are exceptional in northern Europe (Drake 1994).

There are many types of homeless accommodation common to most countries in the EU. Hostels, bed-and-breakfast hotels and guesthouses provide shelter to homeless people throughout Europe. In all member states there are homeless people squatting in disused buildings and living in caravans and tents because they have no proper accommodation. Similarly, in all countries within the EU there are people staying in institutions such as psychiatric hospitals and prisons who should be considered homeless because they have nowhere to go on their release. Indeed, many of these people will have become institutionalised because of their homeless situation.

In all member states of the EU there are people living in severely overcrowded accommodation, or sharing housing with friends and relatives on a permanent or temporary basis because they have no home of their own. However it may be that cultural and social conventions differ from country to country within Europe so that conditions which are commonplace and socially accepted in one member state may be viewed as extreme deprivation and therefore homelessness in another.

2.6 SOURCES OF HOUSING FINANCE FOR OWNER-OCCUPATION

It has often been predicted that globalisation in finance markets in general, liberalisation in housing finance in particular, and the completion of the European internal market would all tend to result in standardisation of financial institutions and mortgage instruments (Miles 1994). In part the differences are ones of nomenclature; for instance is a mortgage bank distinct from a housing bank in any other sense than the first covers a wider range of land-based assets than the second?

Historically there have been two big substantive differences and one great similarity. The differences concern whether funding for private housing has, on the one hand, been through direct retail institutions or, on the other, through often state-owned ,intermediaries providing matching bonds. Second, but strongly linked to the first, is the question whether government provides direct assistance, usually in the form of interest subsidies, often tied to new provision or investment in housing? The similarity has been in the extent to which there has been a special circuit of housing finance which has directed funds towards housing investment or transactions and provided them at below-market-rates through regulation, tax benefits and sometimes subsidy. In many ways it is this similarity that has been disappearing over the last decade, as much as the differences.

In all European countries there has been emphasis on deregulation of the financial system overall which has in turn entailed some integration of housing finance into the general market. In most countries there has also been greater emphasis on privatisation including, where relevant, changing the status of state-owned banks. So far, however, the outcome has been quite different between countries with at one extreme, notably in France, Germany and particularly Austria, the continuation of a special circuit of housing finance, still usually linked to government assistance and/or guarantee, and at the other, notably in the UK, Spain and other countries that tend more to utilise retail banks, an open finance system almost entirely non-specific to housing. So instead of all countries having a special circuit there are now very real differences in the extent to which housing finance has been integrated into the overall finance market.

2.6.1 Government support to owner-occupation

Table 2-1 Government support to owner-occupation in EC Countries

Country	General	Targeted	Change in level of support
Finland	Tax relief at 28% (30% first time buyers)	Young first time buyers, contractual savings	Declining
Sweden	Tax relief at 30%, interest subsidies being phased out	New improvement investment	Declining
Norway	Tax relief at 28%, low imputed income	Housing allowance, contractual	Declining
Denmark	Tax relief (reducing) low imputed income	Saving None	Declining
Netherland	Tax relief at marginal tax rate	Low income earners before 1993	Declining
Germany	Interest rate subsidies, depreciation allowances	Tax credit for families, improvement	Stable
Austria	Interest rate subsidies, no tax relief	Low income, young, investment	Stable
Ireland	Tax relief declining rapidly from 48%	New investment	Declining higher incomes, stable lower incomes
UK	Tax relief declining rapidly from 48%	Low income (very limited improvement investment)	Declining
France	Tax relief (restricted), interest rate subsidies	Contractual savings low income, young, first time buyers,	Declining
Spain	Tax relief	New/improved 80% of total, so not really targeted	Declining

Sources: European Mortgage Federation, Brussels.

Looking next at the differences, in all the countries that we examined that had used interest rate subsidies to encourage investment there have been moves to reduce the extent of interest rate subsidies, either to phase them out altogether or to limit them to particular forms of investment (such as rehabilitation) or particular locations (such as urban regeneration areas). In some cases these benefits have been restricted to rented and particularly social rented housing. At the same time in almost all the countries that had provided mortgage tax relief for borrowing for owner-occupation that relief has either been abolished or restricted. The most important exception here has been the Netherlands which continues to provide full deductibility at the marginal tax rate in all sectors, while at the same time taxing imputed rents (Table 2.1). The tendency towards convergence that has emerged here is that, for tax purposes, the majority of countries now treat owner-occupied housing as consumption good, while treating rented housing as an investment good.

An important aspect of mortgage funding in many countries has been the role of contract saving. Traditionally, specialist institutions have provided lower rates of interest to small, usually younger, savers in return for access to below market priced mortgage funds-with or without an additional subsidy from government. In Britain and other countries where there has been a strong emphasis on deregulation this special circuit has disappeared, generating a much wider range of options for the saver and market-priced mortgages for the borrower. This tends to result in earlier owner-occupation and higher levels of borrowing compared to the previous constrained systems. In Germany and Austria, on the other hand, the Bausparkassen remain central to the mortgage system, although the proportion of finance provided through contract savings has fallen considerably in the last few years in the face of financial liberalisation. The same is true of France, where the form of finance is tightly linked to the extent of assistance provided by the government which, in turn, tends to be more strongly income related than in the past.

Both Norway and Finland have lately introduced contract savings schemes within a liberalised finance market, to assist entry into owner-occupation for marginal purchasers. In this context contract savings have three distinct roles: to signal the household's preparedness to meet its contractual obligations, to reduce the financial risks involved in providing funds to marginal buyers and to target assistance through a form of matching grant. It remains to be seen whether this revival in contract savings is sustainable in the face of competition from institutions prepared to provide higher loan-to-value ratios, unless large-scale government assistance is also on offer. Once again, it reflects in some ways a growing divergence in approach-but linked to different means of targeting government assistance, rather than to market factors.

In the more market-oriented systems of the United States, Australia and Britain, on the other hand, there are general bankruptcy and foreclosure laws, which are applied to housing in the same way as to other assets. Even so, housing is still regarded as special, in part because foreclosure is seen as a social problem and in part because the process is very expensive and therefore, if possible, should be avoided from the point of view of borrowers and lenders alike.

Perhaps for this reason, whatever the formal rules, restructuring debt is by far the most usual practice in the face of growing arrears. In some countries this is forced upon institutions because the courts do not apply the formal enforcement powers and it is therefore almost impossible to obtain possession. In others it is more a business decision based on the relative costs of different approaches. In either case these conditions affect the ways in which contracts operate and therefore the costs of borrowing.

Higher proportions of owner-occupiers and more liberal finance markets have undoubtedly brought the question of arrears and foreclosure to the forefront of discussion-although the upswing in most economies observed in the mid-1990s has reduced the immediacy of concerns. What is also clear is that so far these arrangements are seen as entirely a national concern and there is no sign of any formal convergence in approach.

2.6.2 Financing Social Housing

The provision and financing of social housing is also of relevance to the question of convergence in that it provides different opportunities. So far, however, the methods by which social housing is funded are seen as aspects of national policies of little direct relevance to the question of convergence. Even so it is worth noting some consistent trends.

The majority of social housing finance is still provided by the state, or involves important government guarantees. There have, however, been very significant changes in the ways that governments assist provision. In particular, there has been a growth in the use of arm's-length organisations, to the point where some countries have no municipally-owned housing at all. Most such organisations remain locally based and continue to have strong links with the local authority; sometimes, as in the Netherlands and France, involving guarantees by that authority, but the finance, excluding subsidy, comes from the private sector. In the UK new social housing provision has shifted from local authorities to housing associations, involving increasing proportions of private funding. In addition there is a growing emphasis on transferring existing stock to associations or local housing companies through privately funded buy-outs.

In France there have been fewer structural changes, in part because social housing has always been more flexibly structured with organisations sometimes being controlled by municipalities and sometimes by independent bodies. Germany is once again atypical in defining social housing not by ownership but by the nature of the subsidy provided together with the contract between the relevant landlord and the government. Private landlords may provide social housing for the period of subsidy, usually thirty years, and are then able to let the accommodation on the open market. Austria, while operating in a way similar to Germany, maintains stronger government involvement.

The tendencies across Europe away from both general and open-ended subsidies towards both targeting and certainty of commitment are clear (Turner *et al.* 1996). The Netherlands has gone furthest by rolling up all existing open-ended subsidies into a single grant, together with insurance and guarantees. A number of countries are beginning to limit interest rate subsidies to improvement investment instead of new building: Denmark and France are good examples here. Up-front grants are also becoming more usual, especially for rehabilitation. Britain has been at the forefront of both cash-limiting and location targeting, with housing associations bidding for grants on the basis of cost as well as need. Thus the emphasis has moved towards greater integration of social housing into the private finance system as well as increasing restrictions on the extent of subsidy. In this context there have certainly been elements of convergence in policy terms.

The other major tendency has been towards person-related, rather than dwelling-related, subsidies. In some countries these are available in all tenures; in others, such as the Netherlands, the UK and Denmark, only in the rented sector. The forms of this assistance vary greatly between countries, but the move towards assisting lower income households rather than directly encouraging the supply side is general. In principle this can allow rents to better reflect the resource costs involved, but there is a long way to go before this becomes the norm.

Overall there is some evidence of convergence with respect to social housing policies and in terms of the mechanisms used for assisting lower income households to obtain adequate accommodation. These tendencies do not arise specifically from the development of the Union, but more from wider pressures on governments to control their expenditures and to target what assistance remains towards particular groups and locations. This second strand of policy has more to do with regional than financial policy, but is no less important in the longer term.

2.7 CONCLUSION

The extent of convergence, in terms of financial institutions and instruments, remains relatively limited. What matters, however, is not whether each country operates in the same way, but whether households and providers in each country have similar opportunities and are equally able to benefit from any comparative advantage. The ways to analyse this are through the examination of outcomes - can people obtain housing finance on similar terms where similar risks are involved? - rather than looking at whether or not they do this through similar instruments and organisations.

The evidence of the last few years is that the pressures of deregulation have affected housing finance markets throughout the world. In some cases the impact has been to remove any special circuit and to address the resultant risks through insurance. In others the liberalised market is tending to compete away the benefits associated with the special circuit of housing finance. There are, however, very different pressures in the different countries, arising in particular from the nature of government involvement: Are specific subsidies still being provided? Is the government prepared to guarantee loans? Are tax benefits available for particular types of housing? Where the answers to these questions vary, not only will instruments and institutions differ but so also will costs prices and access.

There is considerable evidence of change. There is also considerable evidence that systems are still in transition, generating further differences as well as convergence. The fundamentals of the legal definitions of property rights and their enforcement show no signs of modification. When and if convergence in this context does occur the reason for it will not be housing related but will be the result of far more general tensions.

Overall the evidence suggests that it is the wider economic and global pressures that are the engines of change. What is required now is detailed empirical evidence on the costs and availability of funds across countries as well as on access and profitability among organisations in the finance market. Such evidence is likely to show that there is a long way to go before there is a level playing field in housing finance.

Chapter 3

ISLAMIC HOME FINANCE: PRINCIPLES AND PRACTICE

3.1 INTRODUCTION

The Islamic financial services industry has recorded phenomenal growth in recent years; Islamic finance has grown rapidly across the world, conservatively estimated at 10-15% a year (Sole, 2007). A recent report by the Financial Times estimates the size of the Islamic finance industry at $750 billion. The report breaks up the industry into Islamic financial institutions with estimated combined assets of $250 billion, 250 Islamic mutual funds operating with US$ 300 billion of assets and another US$200 billion are estimated to be held in the Islamic windows of conventional banks (Tett, 2006). From small beginnings in the mid-1970s, Islamic banks today offer a wide range of products: from basic *Shari'a*-compliant retail products, to insurance, mortgages, investment instruments and large-scale project financing. Although Islamic banking remains rooted in the Muslim world, *Shari'a*-compliant products are increasingly on offer in Europe and North America. The industry has been supported at product level by many central banks. Following the lead of Malaysia's Islamic Central Bank (Bank Negara) in 2001 the Bahrain Monetary Agency introduced its own *Shari'a*-compliant government bills (a three-month paper known as *Sukuk al-Salam*), in an effort to meet Islamic banks' short-term liquidity needs.

The main objective of this chapter, which covers theoretical and practical issues, is to explore the ways and means of providing Islamic housing finance. Section 3.2 discusses the principles of the Islamic financial system, and briefly overviews the prohibition of *riba* and *gharar*. Islamic financial contracts are discussed in section 3.3 which covers equity contracts (M*udarabah* and *Musharakah*) and the debt contracts (*Murabahah, Ijarah, Ijarah wa Igtina* and *Istisna*). Section 3.4 provides methods and structures of Islamic home finance and attempt to explore and discuss technical issues relating to *Fiqh* as well as the economic aspects of Islamic housing finance to clarify the modes and instruments suitable for this purpose indorsed by *Shari'a*. The application of Islamic housing finance across the world is overviewed in section 3.5

through various actual experiments from mainly Muslim countries, where housing finance varies from underdeveloped to relatively develop and from minority Western countries where Muslims are in the minority, where housing finance development has been discussed. Section 3.6 discusses the role of the *Sukuk* in Islamic housing finance. Section 3.7 looks at the legal and financial obstacles and the way forward, as well as the infrastructure finance from a conventional as well as from an Islamic prospective.

3.2 PRINCIPLES OF AN ISLAMIC FINANCIAL SYSTEM

The basic framework for an Islamic financial system is a set of rules and laws collectively referred to as *Shari'a*, governing economic, social, political, and cultural aspects of Islamic societies. *Shari'a* originates from the rules dictated by the *Quran* and its practices, and explanations rendered by the Prophet Muhammad known as *Sunnah*. Scholars provide further elaboration of the rules in Islamic jurisprudence within the framework of the *Quran* and *Sunnah*. The basic principles of an Islamic financial system can be summarized as follows:

3.2.1 The Prohibition of *Riba*

Prohibition of *riba*, a term literally meaning "an excess" and interpreted as "any unjustifiable increase of capital whether in loans or sales" is the fundamental principle of the system. More precisely, any positive, fixed, predetermined rate tied to the maturity and the amount of principal (i.e., guaranteed regardless of the performance of the investment) is considered *riba* and is prohibited (Tahir, *et.al.1999*). *Shari'a* does not consider money as a commodity such that there should be a price for its use. Money is a medium of exchange in an asset-oriented economy, and a store of value. However, the term *riba* or interest is used in the *Shari'a* in two senses, *riba-an-nasiah* and *riba-al-fadl*. *Riba-an-nasiah* refers to the time allowed to the borrower to repay the loan in return for addition (financial increment) (*nasiah* is related to the verb *nasa'a*, meaning to postpone, defer or wait). It makes no difference whether the return is a fixed or a variable percentage of the principal, an absolute amount to be paid in advance or on maturity, or a gift or service to be received as a condition for the loan.

The general consensus among Islamic scholars is that *riba* covers not only usury but also the charging of "interest" as widely practiced, in conformity with this consensus, the Islamic *Fiqh* Academy of the Organization of Islamic Countries (OIC) issued resolution No.10 (10/2), on the prohibition of interest (Islamic *Fiqh* Acdemy,2000).

Riba-al-fadl, on the other hand, is related to transactions involving homogeneous goods. *Riba-al-fadl* arises if gold, silver; wheat, barley, dates and salt are exchanged against themselves with unequal proportion. That is, they should be exchanged on the spot and be equal and alike, otherwise any change in transactions will create *riba-al-fadl*. For a more detailed discussion see for example resolution number 42(4/5) for the Islamic *Fiqh* Academy. However, it is permissible for the debt (*gard hassan*) in the case of inflation and change of currency value to be paid in terms of means other than the currency that will encounter a fall in value (for a full discussion see resolution number 115 (9/12) of the Islamic *Fiqh* Academy, 2000).

This prohibition is based on arguments of social justice, equality, and property rights. Islam encourages the earning of profits but forbids the charging of interest because profits, determined ex post, symbolize successful entrepreneurship and creation of additional wealth whereas interest, determined ex ante, is a cost that is accrued irrespective of the outcome of business operations and may not create wealth if there are business losses. Social justice demands that borrowers and lenders share rewards as well as losses in an equitable fashion and that the process of wealth accumulation and distribution in the economy be fair and representative of true productivity.

Because interest is prohibited, suppliers of funds become investors instead of creditors. The provider of financial capital and the entrepreneur share business risks in return for shares of the profits.

Money is treated as "potential" capital -- that is, it becomes actual capital only when it joins hands with other resources to undertake a productive activity. Islam recognizes the time value of money, but only when it acts as capital, not when it is "potential" capital.

3.2.2 *Gharar*

There are many definitions of *gharar*. According to Al-Darir (1997) *Gharar* covers both the unknown and the doubtful, as the definition proposed by *Al-Sarakhsy*: *"Gharar* obtains where consequences are concealed. This is the view favoured by most jurisprudents.

The scholars of the *Maliki* school of *Fiqh* have widened the scope of their discussion of *Gharar*. In summary they have laid dawn the basic classification of the principles covering all elements of *gharar* as follows:

I. *Gharar* in the terms of the contract, means that the contract has been concluded in words that imply *gharar, i.e.* the *gharar* relates to the essence of the contract and not to its object. This includes the following types of sales:

1) Two sales in one.

2) Down-payment *('arboon)* sale.

3) "Pebble", "touch" and "toss" sale.

4) Suspended *(mu'allaq)* sale.

5) Future (*mudhaf*) sale.

II. *Gharar* in the object of contract is where the effect and outcome of the contract are covered by the provisions manifested. In a contract of sale, the object covers both the item sold and the price. *Gharar* in these two can occur in any of the following cases:

1) Ignorance of the genus of the object.

2) Ignorance of the species of the object.

3) Ignorance of the attributes *e.g.* selling the unborn animal without its mother

4) Ignorance of the quantity of the object.

5) Ignorance of the specific identity of the object.

6) Ignorance of the time of payment in deferred sales

7) Inability to deliver the object.

8) Contracting on a non-existent object.

9) Not seeing the object

An Islamic financial system discourages hoarding and prohibits transactions featuring extreme uncertainties, gambling, and risks. Not every level of risk is *gharar,* as stated by *Ibn Taymiah:* "it is well known that Allah and his Messenger did not forbid all kinds of risk" (cited by Al-Misri 1993, p. 35). Risk exists in all economic activities. It is only when risk exceeds a certain level that a transaction is considered illegal. This concept helps us to understand why some contracts are prohibited in Islam.

Islam upholds contractual obligations and the disclosure of information as a sacred duty. This feature is intended to reduce the risk of asymmetric information and moral hazard.

Only those business activities that do not violate the rules of *Shari'a* qualify for investment. For example, any investment in businesses dealing with alcohol, gambling, and casinos would be prohibited.

3.3 ISLAMIC FINACIAL CONTRACTS

The contract is the very essence of transactions, without which the transactions are void of legal consequence. Islamic commercial law, known as *fiqh al-mu'amalat* in *Shari'a* law has laid down fairly detailed regulations leading to the formation of contracts. Conversely, Islamic commercial law is rich of various transactions useful for meeting people's need in various situations.

In Islamic jurisprudence there are four basic rules for judging the validity of conditions in a contract (Kamali, 1996) .These are:

1) A condition that is not against the contract is a valid condition.

2) A condition that seems to be against the contract but conforms to market practice is not void, provided that its invalidity is not proven with the clear injunctions of the *Holy Quran* and *Sunnah*. For example 'A' buys a washing machine on condition that the seller will provide him with a three-year guarantee and one year's free service. This type of condition does not invalidate the contract.

3) A condition that is against the contract and does not conform to market practice but is in favour of one of the contractors or subject matter is void. For example if 'A' says he will sell a bike on the condition that he will use it on a fixed date every month, this contract will be void.

4) A condition which is against the contract does not conform to market practices and is not in favour of either contractor, is not a void condition.

Sometimes a void condition invalidates the contract and sometimes it does not, nevertheless, the condition itself is null and void.

To elaborate on this, Islamic jurists and scholars have written that compensation (*uqood muawadha*) like sales, purchases and lease agreements, become void by setting a void condition. However, non-compensatory (voluntarily) agreements *(uqood ghair muawadha*) like loan contracts *(qard-hassan*) do not become void because of void conditions. The void condition, on the other hand, itself becomes ineffective. For example if 'A' gives 'B' a loan with a condition of premium at the time of repayment, this condition of interest is void. However, this condition does not invalidate the contract, therefore all transactions made with this borrowed money, will be valid. But the condition of interest itself is revoked; therefore 'B' is not liable for the payment of interest.

In Islamic jurisprudence, some contracts are such that rights and obligations are also attached to the Agent making the contract on behalf of the Contracting Party e.g. a Sales Contract, *Ijarah, Istisna*, *Salam* etc. While in other contracts, like the marriage (*ikah*) contract, only the Principal has all the responsibilities, rights and obligations.

3.3.1 Equity Contracts

The main equity-like contracts used in Islamic finance are:

3.3.1.1 Mudarabah

An agreement made between a party, which provides all of the capital for a project and another party, the *mudarib*, or entrepreneur/project manager. Profits from the project are distributed according to a pre-determined sharing ratio but any losses are borne solely by .the provider of the capital. The provider of the capital has no control over the management of the project.

3.3.1.2 Musharakah

Musharakah is a financing technique involving a partnership between parties who provide capital for the financing of a project. The parties share profit on a pre-agreed ratio, but losses are shared on the basis of equity participation. One or more parties can carry out the management of the project.

3.3.2 Debt Contracts

The main debt-like contracts are:

3.3.2.1 Murabaha

Murabaha is a contract between the financial institution and its client for the sale of goods at a price that includes a profit margin agreed by both parties. As a financing technique, it involves the purchase of goods by the financial institution as requested by its clients. The goods are sold to the client with a mark-up. Repayments, usually in instalments, are specified in the contract.

3.3.2.2 Ijarah

An *Ijarah* is a leasing contract under which a financial institution buys and leases out equipment required by its clients for a rental fee. The duration of the lease and rental fees are agreed in advance. Ownership of the equipment remains in the hands of the financial institution. The contract is a classical Islamic financial one, now in increasing use worldwide and identical to a full-payout financial lease

3.3.2.3 Ijarah wa Igtina

An *Ijarah wa Igtina* is a lease/hire purchase contract similar to *Ijarah*, except that there is a commitment from the client to buy the equipment at the end of the rental period. It is agreed that at the end of the lease period the client will buy the equipment at an agreed price from the financial institution, with rental fees previously paid constituting part of the price.

3.3.2.4 Istisna

Istisna is a contract for the acquisition of goods by specification or order, where the price is paid progressively in accordance with the progress of a job. This is practised, for example, for purchases of houses to be constructed where payments made to the developer or builders are according to the stage of work completed.

3.4 METHOD AND STRUCURE OF ISLAMIC HOME FINANCING

Housing constitutes a fundamental and important part of basic human needs, in addition to food and clothing. Nonetheless, it has several features which make it more important than the other two needs. Firstly, the expenditure on housing is much larger in absolute amounts than on food and clothing. Secondly, housing is a fixed asset; hence, expenditure on housing acquires the character of an investment because of its long-term nature. Thirdly, and doubtless most importantly, housing is and has been a vehicle of economic development as it generates demand for different basic industries, such as, steel, cement, other building materials and fixtures etc.

> It is *Allah* Who made your habitations homes of rest and quiet for you; and made for you, out of the skins of animals, (tents for) dwellings, which ye find so light (and handy) when ye travel and when ye stop (in your travels); and out of their wool, and their soft fibres (between wool and hair), and their hair, rich stuff and articles of convenience (to serve you) for a time. (016.080, Yusuf Ali, the meaning of the *Qur'an* Translation)

Aisha was quoted as saying that the Prophet Muhammad, God's peace and blessings be upon him, said: "There are three forms of happiness: a good wife, a spacious home and a fast beast of burden" (Reported by *Ahmad*, *al Bazzar* and *al Tabrani in al Awsat*) cited by (Othmani, 1995).

In spite of its positive significance, housing finance has neither received much consideration as a theoretical issue of Islamic banking nor could it manage to get its due share as an Islamic banking operation. The Islamic banking system has come to realize the fundamental issue of housing finance as an integral part of its general concern about achieving economic and social well being of Muslims. A group of *Shari'a* scholars, Islamic bankers, economist and policy makers gathered together for a Workshop on "Islamic Banking Modes for House Building Financing" organized in Khartoum (Sudan) during Rabi Thani 1412H (October 1991) in a collaboration between the Islamic Research and Training Institute (IRTI) of the Islamic Development Bank (IDB) and the Sudanese Estates Bank. They identified the following methods of finance that are consistent with Islamic *Shari'a* and that could be adopted by financial institutions in Islamic countries and elsewhere.

3.4.1 Instalment Sale

Under this method the financier sells a house he owns to a client and receives the value in deferred, mutually agreed-upon instalments. This technique can take one of two forms; the first is where the contract does not indicate the original cost of the house and the profit margin separately. The total value for which the house is sold is divided into instalments. This case could be denoted as an instalment sale. If, however, the contract refers to the original cost and the profit margin separately, this is *Murabahah*. The instalment sale can be for the whole or only part of the property.

A client who cannot afford to purchase a house alone may be in a position to pay part of the cost. The financier could in this case pay the remaining part of the cost and share the ownership of the house with the client. The financier can then sell his share to the client for a profit on a deferred payment basis (Othmani 1995).

This technique can be applied through the construction of houses by government-owned institutions (e.g. banks and companies), private investment institutions, or capable individuals and offering them for sale to the public through instalment sale techniques. In applying this method, the *Shari'a* controls governing the exercise of instalment sale as stated in Resolution No. (51/2/6) of the Islamic *Fiqh* Academy (2000) should be taken into account. These controls include the following:

The instalment price of a sold property may be set at higher than its cash price. It is permissible to indicate the cash price together with the price to be paid in instalments over a specific period of time. However, the sale is not rendered valid unless the parties have decided whether the sale will be in immediate payment or in instalments. If the sale is implemented while the parties are still hesitating between an on-the-spot and a deferred sale, then the transaction is null and void according to *Shari'a*.

In the instalment sale contract, it is prohibited to separate the return for accepting deferred payment from the cash price in such a way that it becomes directly linked to the duration of the transaction whether or not the parties agree to calculate this return according to a certain rate or the prevailing interest rate in the market.

If the debtor fails to pay the agreed instalments, it is not permissible to charge him any amount in addition to the principal, whether or not an advance condition was made to that effect; since such an additional amount constitutes prohibited *riba.*

It is prohibited that a solvent debtor delays the repayment of due instalments. However, it is not permissible to provide in the agreement for compensation to be paid in the case of delayed payment.

In an instalment sale, it is permissible for the seller to impose earlier payment of instalments if the debtor delays the payment of some instalments, despite his agreement to that condition at the time of concluding the contract.

The seller has no right to maintain ownership of the sold property after the sale has been effected. He may, however, make a condition requiring the purchaser to mortgage the property as collateral for payment of deferred instalments.

The instalment sale may be concluded on the basis of an agreed price, irrespective of the initial cost incurred by the seller for acquiring the property (i.e. through bargaining). It is also permissible to conclude the instalment sale (as in *murabahah)* by agreement to give the seller a certain profit in addition to the actual cost he has incurred.

This financing technique may be applied for purchasing houses which are already built or those to be constructed at the cost of the financier, taking into account the preferences of the prospective buyer as regards the specifications of the house. Alternatively, the financier may authorize the prospective buyer to supervise the construction of the house, and then sell the house to him through *Musawamah* or *Murabahah*

Among the financing techniques that are based on deferred sale and which should be considered by governments and charitable organizations, is the construction of houses to be sold to those in need of them on the basis of the actual cost without any profit added, *i.e.* through *tawliyah* sale.

3.4.2 Hire Contracts on a Deferred Payment Basis

Deferred sale in Arabic is known as *Bay' Mu'ajjal* or *Bay' Bithaman a'Ajil.* It is permissible, in a sales contract, to make provisions for the immediate delivery of goods while postponing the payment of the price to a later date. In such an event, it is permitted to charge a higher price than the prevailing market price.

This method is appropriate for individuals who have secured the land and the construction materials and want to enter into an agreement with contractors willing to deliver them the construction service against deferred payment.

3.4.3 Diminishing *Musharakah*

Sometimes called Decreasing *Musharakah,* in Arabic *Al-Musharaka al-Mutanakissa* or *Al-Musharaka at Tanazoleya,* is where one partner in the contract can withdraw gradually from the project or business by selling part of their share to the other partner. Hamoud (1974), was the first to propose the concept of Diminishing *Musharakah* or, in Arabic, *Musharakah Myantahi bi al Tamlik (Musharakah* which ends in transferring ownership to one party - the entrepreneur), when he realized the limitation of using *Mudarabah* and *Musharakah* by the Islamic Bank on a large scale for a very long time. This proposal was subsequently discussed and approved as a permissible mode of financing by the First International Conference on Islamic Banking, held in Dubai, from 23-25 *Jamad al Thani* 1399H (1979) (Abdallah, Ahmad Ali, 1991).

Decreasing *Musharakah* entails three contracts: partnership (*Shirakit-ul-Milk*), *Ijarah* (lease), and sale contract and it takes place when a financing body enters into a partnership contract with individuals who can contribute to the construction costs by providing cash and/or the land. . The house, when completed, becomes the joint property of the beneficiary client and the financing body. The latter then sells its share to the former against lump sum deferred payment or instalments. Upon the payment of the final instalment ownership of the house is transferred to the beneficiary client.

Diminishing *Musharakah* can also be affected with regard to ownership of the building, only while the beneficiary owns the land. Both the financing body and the beneficiary client could bear part of the cost of the building, which will be jointly owned by them according to their shares. The financing body then sells his share to the beneficiary client against lump sum or installed deferred payment.

Diminishing *Musharakah* may take the following forms:

On the basis of a partnership agreement, the financing body and the beneficiary client may buy the house, which becomes their joint property, according to the rates of their contribution to the cost of the house.

The financing body then leases its share to the beneficiary client for a specified periodic rent.

The share of the financing body in the ownership of the house is divided into shares. The beneficiary client, according to the agreed schedule, buys one of these shares at a specified price and the total number of shares of the financing body decreases. Proportionately, the rental amount is reduced, and the share of the beneficiary client in the ownership of the house increases until he has complete ownership of the house; at that point both the partnership agreement and the lease contract come to an end.

In Decreasing *Musharakah* where partnership, leasing and sale are involved, no contract should be made a pre-condition of another. The flawless method of decreasing *musharaka* which adheres to *Shari'a* requires that the three contracts should be concluded in their due time and independently. However, both the financing body and the beneficiary client may reach, through promises, an understanding on the entire process. It is generally believed that a promise to do something creates only a moral obligation on the promisor, which cannot be enforced through courts of law. However, there are a number of Muslim jurists who declare that promises are enforceable, and the court of law can compel the promisor to fulfil his promise, especially, in the context of commercial activities. Some *Maliki* and *Hanafi* jurists can be cited, in particular, who have declared that the promises can be enforced through courts of law only for the extend of losses arising from the promise in cases of need (for full *Fiqh* discussions see Othmani 1995). The Muslim jurists allowing this arrangement have based their views on the principle that "the promise can be made enforceable in a time of need".

One could raise an objection that if the promise of resale has been taken before entering into an actual sale, it practically amounts to putting a condition on the sale itself, because the promise is understood to have been entered into between the parties at the time of the sale, and therefore, even if the sale is without an express condition, it should be taken as conditional because a promise in an express term has preceded it.

This objection can be answered by saying that there is a big difference between putting a condition on the sale and making a separate promise without making it a condition. If the condition is expressly mentioned at the time of sale the sale will be valid only if the condition is fulfilled, meaning thereby that if the condition is not fulfilled in future, the present sale will become void. This makes the sale transaction contingent on a future event, which may or may not occur. It leads to uncertainty (*gharar)* in the transaction, which is totally prohibited in *Shari'a.*

On the other hand, if the sale is without any condition, but one of the two parties has promised to do something separately, then the sale cannot be held to be contingent or conditional to the fulfilling of the promise. It will take effect irrespective of whether or not the promisor fulfils his promise. Even if the promisor backs out of his promise, the sale will remain effective. The most the promisee can do is to compel the promisor, through a court of law, to fulfil his promise and if the promisor is unable to fulfil the promise, the promisee can claim actual damages he has suffered because of the default. This makes it clear that a separate and independent promise to purchase does not render the original contract conditional or contingent; therefore, it can be enforced.

On the basis of this analysis, Diminishing *Musharakah* may be used for house financing with the following conditions:

The agreement of joint purchase, leasing and selling different units of the share of the financier, should not be tied-up together in one single contract. However, the joint purchase and the contract of lease may be joined in one document whereby the financier agrees to lease his share, after joint purchase, to the client. This is allowed because, as will be explained later, *Ijarah* can be affected for a future date. At the same time the client can sign a one-sided promise to purchase different units of the share of the financier periodically and the financier may undertake that when the client will purchase a unit of his share, the rent of the remaining units will be reduced accordingly

At the time of the purchase of each unit, the sale must be carried out by the exchange of offer and acceptance at that particular date.

It is be preferable that the purchase of different units by the client is implemented on the basis of the market value of the house as prevalent on the date of purchase of that unit, but it is also permissible that a particular price is agreed in the promise of purchase signed by the client.

3.4.4 Leasing Ending with Ownership

This mode of finance is called *Ijarah wal Iqtina`*. The basic idea behind this system is that an asset is given to the client on lease at an agreed rental. At the same time, the lessee is allowed to purchase the asset at an agreed price. It has been allowed by a large number of contemporary scholars and is widely acted upon by Islamic banks and financial institutions.

This mode of financing consists of both leasing and sale contracts. At the end of the lease period, the property is sold, completely or in instalments, to the beneficiary. This technique is similar to that of decreasing *Musharakah* with the exception that here there is no prior joint ownership of the property.

The validity of this agreement is subject to two fundamental conditions as set by the Resolution No.110 (4/12) of the Islamic *Fiqh* Academy (2000):

Firstly, the agreement of *Ijarah* itself should not be subjected to signing this promise of sale or gift but the promise should be recorded in a separate deed.

Secondly, the promise should be one-sided and binding on the promissory only. It should not be a two-sided promise binding on both parties because in that case it would be a full contract implemented to a future date which is not allowed in the case of sale or gift.

In this system *Shari'a* requirement should be observed throughout the lease time. These requirements require that the owner (lessor) bear all the responsibilities relating to the property he owns, such as maintenance and the like, until the lease ends with him selling the property to the beneficiary client.

This type of contract may also be terminated at any time, provided that the lessee covers any resultant costs incurred by the owner (financier). It is also possible to agree on terminating the lease agreement in order to enter into an instalment sale contract.

The sale contract should be completed at the end of the deal, and not at the beginning of the lease period.

3.4.5 *Istisna'* (*Mugawalah*) Contracts

Istisna is the sale of a well-defined article to be delivered in the future and not the sale of a service (Al Baberti 1316H, cited by Abdalla, Ahmed Ali 1995).

Financing *Istisna*' can only be done by means of two parallel contracts whose subjects are exactly the same: the first contract is between the financier and the party who needs the contracted things; the second contract is between the financier and the contractor who actually manufactures constructs or builds the contracted things; the price difference is the profit of the financier, and the two contracts are linked by proxy or agency agreement. According to many schools of *fiqh Istisna'* is a permissible practice that does not conform to '*Qiyas'*.

This mode of house financing is suitable for middle- and low-income groups who own the land but cannot afford the construction cost. Hence, the one who owns the land can engage in a contract with the financing body to build him a house according to certain specifications, in return for an agreed cost. That cost can be repaid in instalments or in full upon completion of the house. The payment of instalments by the client may start, in this case, right from the day when the contract of *Istisna*' is signed by the parties, and may continue during the construction of the house and continue after it is handed over to the client. As a security the financer may keep the title deeds of the house or land, or any other property of the client as collateral, until the client pays the last instalment.

According to *Sheikh* M.Taji Usmani (2000) for this contract to be valid as an *Istisna*' the financer must provide the building material; otherwise it will be an *Ijarah* contracts. In order to close the back door to *riba* in the *Istisna*' code of financing, it is not permissible in *Shari'a* for the financial body to appoint the client to carry out the construction work on his behalf.

Many contemporary scholars like Dr. *Wahbah al Zuheili* (2003) and *Sheikh Siddiq al Dharir* (1997) consider the *Istisna*' contract to be binding for the two parties once concluded. The binding nature of the *Istisna'* contract means it involves no *gharar* and is more acceptable (Siddiq al Dharir 1990).

For competitive pricing for *Istisna'*, it is highly recommended that financial institutions catering for housing finance establish subsidiary real-estate companies to provide construction materials and services to clients at a sensible cost (Salama, 1991).

3.4.6 Participation in a Housing Fund on the Basis of *Musharakah* or *Mudarabah*

This mode of housing finance operates when the client buys a number of shares in a housing finance portfolio on the basis of either *Musharakah* or *Mudarabah.* With these portfolio shares, the client will be at liberty to get a house from the financial body. Moreover, the client may pay the outstanding amount of the cost of the house or otherwise rent the bank‘s share according to a formula similar to that of Decreasing *Musharakah.*

3.4.7 Interest Free Loan (*Qard Hassan*)

Loan (*Qard*) is defined as the transfer of ownership of an asset or money from the original owner to others on condition that the asset or money will be returned to the owner in the same condition/form and to the same value as when it was first received by the other party from the owner.

A loan in Islam is a contract, which is based on the concept of mutual help (*tabarru*) and contemplation for others' well being-especially those in need (*Al-Mughni*, *Ibn Qudamah*, 4/353 cited by Ali, 1995). Thus, Islam highly encourages the practice of *Qardul Hassan* as stated in the *Hadith* of the prophet Muhammad *S.A.W* "One who releases his brother from difficulties, *Allah* will release him from the hardships in the hereafter" (*Sahih Muslim*). In another *Hadith* our Prophet (peace is upon him) said:

> When God took me for a journey by night (from the Sacred Mosque to the Farthest Mosque). I found written on the Gateway to the Garden the reward of *Sadaqah* is ten-fold; while that of *Qard is* 18 times its actual worth. I asked *Jibril* why *Qard is* better than *Sadaqah*. He answered because the petitioner may ask for what he owns, but the borrower is prompted by his need to borrow (*Sunan Ibn Majah*, cited by Abdallah, Ahmed Ali, 1995).

Loans are one method of house financing based on cooperation, interdependence and for the sake of *Allah*. As such; interest-free loans are not instruments for investment. Governments, institutions, charitable organizations and capable individuals should pay attention to this method for the benefit of those who cannot secure houses with their own means. House financing through *Qard Hassan* has been practised in different parts of the Muslim World by informal associations (*gamaiyah*), *e.g.* in Egypt and the Muslim community in India. Recent research integrates the mortgage design with the existing mainstream literature on housing finance, suggesting that the *Qard Hassan* facility is more efficient than the traditional interest-bearing mortgage facility. This implies that *Qard Hassan* is also more efficient than *Murabahah* and *Ijarah* (Ebrahim, M.Shahid, 2009).

The *Shari'a* ruling is that a loan is to be repaid without any extra amount other than the principal. Nerveless, if extending a loan entails some administrative cost, then it is permissible to have the cost borne by the borrower so that the lender gets the same amount he lent. The borrower should not be asked to make any extra payments other than the actual cost incurred as a result of giving him the loan. The *Shari'a* verdict in this relation is that the lender must not gain any benefit in return for extending the loan.

The resolution of the International Jurists Assembly under the Accounting and Auditing Organization for Islamic Financial Institutions (AAOFI) (http://www.aaoifi.com) mentions that all kinds of benefit or increase (from the borrowed amount) agreed by both borrower and loan giver, made conditional in the contract upfront, or charged upon late payment, in the form of money, things or any benefit, are strictly prohibited and considered as *Riba*. (*Shari'a* Standard, AAOIFI, page 336).

It is further stated in AAOIFI standards, which is online in the Resolution of International *Fiqh* Academy in its third assembly in 1986 that the charging of service cost is allowable with the strict condition that it is an actual cost. The resolution has mentioned further that any charge in excess of the actual cost is prohibited and thus the Islamic jurists unanimously agreed at the assembly that the formula used to calculate the cost must be appropriate, exact and accurate. Moreover, indirect costs such as employment expenditure, office rental and expenses and other liabilities are not inclusive in the actual cost of financing.

3.4.8 Assistance from Governments and Charitable Organizations

Housing is regarded as a basic human need in Islam, which the state should provide in an adequate form to all citizens. The Prophet, peace be upon him, was clear about housing public servants. The caliph Omar's insistence that governors' houses should have no gates suggests that such houses were regarded more as public offices than private residences. Islamic Scholars, like Ibn Hazm include housing among the basic needs to which every Muslim is entitled; the others are food, clothing, medical care, transportation and house-help for invalids or the disabled. At the same time, the human right to housing is explicitly set out in the Universal Declaration of Human Rights, the International Covenant on Economic, Social and Cultural Rights, and other widely-adhered-to international human rights treaties and declarations. Article 11 of the International Covenant on Economic, Social, and Cultural state 'The State's Parties ... recognize the right of everyone to an adequate standard of living for himself and his family, including adequate food, clothing and housing, and to the continuous improvement of living conditions...."

Hence, a person who cannot afford to acquire his own house should be provided with a home by the state. This would be secured either from the *Zakah* fund if he deserves *Zakah*, or the state should sell him the house at cost price without any profit, or give him an interest free loan. Likewise, charitable organizations, in addition to providing food, clothing and medication, should include housing and help for securing it as one of their concerns. Also Resolution No (50/1/6) of the Islamic *Fiqh* Academy concerning real estate financing dealt with these issues.

Table 3.1 Comparative Analysis between Different Typology of Islamic Mortgages Models

	Murabahah	***Ijara wa iqtina***	***Diminishing Musharakah & Ijarah***
Role of the Bank	Buys and then sells property to the client	Buys and then rents property to the client	Buys jointly & then rents its share to the client
Payments Term	15 years	25 years	25 years
Maximum Finance – Value Ratio	Up to 80%	Up to 80%	Up to 80%
Mortgage Type	Fixed	Variable or Fixed	Variable or Fixed
Profit Rates	Profit is achieved by increasing the purchase Price of the property.	Monthly payments include a lease payment (rent) and an on account payment towards the cost of buying home. The amount of the lease payment is reviewed annually and includes the lender's profit.	Each monthly payment includes a charge for rent and a charge that buys a small proportion of the house itself.
Right to sale or repayment	Allowed, & the customer gets the full benefit of any rise in the value of the property.	Allowed, & the customer gets the full benefit of any rise in the value of the property.	Allowed, & the customer gets the full benefit of any rise in the value of the property.

Continue Table 3.1 Comparative Analysis between different Typology of Islamic Mortgages Models.

	Murabahah	***Ijara wa iqtina***	***Diminishing Musharakah & Ijarah***
Home improvements	Allowed to make	Allowed to make	Allowed to make
Taxes and insurance	Not included in the purchase price	Usually included in cost of lease	Usually included in cost of lease
Refinancing	Not available	Available	Available
Payment – Income Ratio (Multiplier)	Allows 2.5 times annual income in case of a sole applicant. For joint applicants it allows 2.5 times the higher income plus 1 t imes the lower income or 2 times joint income.	3 times annual income in case of a sole applicant. For joint applicants it usually allows 3 times the higher income plus 1 times the lower income or 2.5 times joint income.	3 times annual income in case of a sole applicant. For joint applicants it usually allows 3 times the higher income plus 1 times the lower income or 2.5 times joint income.
Bank Risk (based on the length of ownership by the bank)	Low ownership risk	High ownership risk	Medium ownership risk
Penalty Payments	Available provided that it is repaid to charity after excluding actual losses & charges	Available provided that it is repaid to charity after excluding actual losses & charges	Available provided that it is repaid to charity after excluding actual losses & charges
Securitization	Not suitable for securitizations	Suitable for securitizations	Suitable for securitizations

Source: Researcher's compilation

3.5 APPLICATION OF ISLAMIC HOUSING FINANCE ACROSS THE WORLD

According to Islamic Research and Training Institute (IRTI), Islamic Development Bank and Islamic Financial Services Board (IFSB) report, Islamic home mortgages have grown rapidly over the last five years, with major providers of Islamic mortgages in a number of countries being licensed as non-bank financial institutions. The size of the industry estimated for 2005 was around US dollars 9-12 billion (IRTI & IFSB, 2006). However, house financing by Islamic banks varies and is in line with the economic environment of the respective countries. In Western Countries (North America, Europe, and Australia) where there is a mature and deep housing finance system, as well as a developed conventional mortgages market, there is a successful minority of experimentations of Islamic mortgages .At present there are four models of Islamic mortgage in practice, *Ijarah* (lease) based contract, Diminishing *Musharakah* (equity partnership) based contract, *Murabahah*-based contract, and the fourth model is designed on lines of cooperative societies, where members buy *Mudarabah* (equity) membership and assist each other in purchasing a home from the pool of the society's funds (Iqbal 2002).

On the other hand, in majority Muslim countries the housing finance status ranges from undeveloped (as in Yemen), small and dominated by the public sector (as in Algeria and Iran), small with potential (as in Morocco, Egypt and Lebanon) and relatively developed but still dominated by the public sector (as in Jordon). In these countries home mortgage finance facilities are almost missing for low- and middle-income groups and where demand for affordable housing is high and will remain high, reflecting pent-up demand and medium- to long-term demographics. A recent report by the IMF suggests that in these countries more widely available mortgage financing is a fundamental part of financial sector development and a crucial vehicle for increasing the depth and breadth of the financial sector (Buckley 2005). Hence, Islamic financial institutions provide home mortgages to Muslim majorities in developing countries, as well as to Muslim minorities in developed countries, contributing positively towards eliminating poverty and increasing growth in the Muslim World as well as eliminating 'social exclusion' among the Muslim community in the developed world.

3.5.1 North America

Housing Finance in North America is very deep; the rate of mortgage loan to the GDP is very high (58 percent in US and 43 percent in Canada) while home ownership is 69 percent for US and 67 percent for Canada (Social Bank, 2007). Islamic home financing in North America was spawned from a grassroots of the growing Muslim community. Islamic home financing is a potential source of business for financial institutions, which tend to serve socio-economically diverse customer bases and identify a strong growth prospective among Muslims in professional occupations.

3.5.1.1 Islamic banks

The fully fledged Islamic bank, University Bank – University Islamic Financial Corporation in North America was established in late 2005. University Bank offered Islamic finance products only after brokers and real estate agents made them aware of this niche market back in July 2003. In an attempt to expand its Islamic home finance business nationwide, University Bank in December 2005 formed a subsidiary, University Islamic Financial Corporation, to focus solely on selling its line of Islamic home finance products, profit sharing deposit accounts, and shares of Islamic mutual funds (Chiu, 2006).

3.5.1.2 Finance companies (houses)

In Canada, the Islamic Cooperatives Housing Corporation was the first Muslim financial institution in Canada as well as the whole of North America.: It began in 1981 by pooling money from members of the local Muslim community and it introduced the *Musharakah Mutanaqisah* financing model. The ICHC's system works as follows: if a customer wants to buy a house, they have to pay a minimum of 25 percent as a down-payment and the co-op buys the property. Instead of mortgage payments, the resident pays the co-op a fixed sum of money each month, including a 20 percent administration fee. Eventually, the resident pays off their debt entirely and the property is transferred into his/her name (Efron, 2005).

Islamic home financing was first offered to the Muslim community in the United States in 1986-87 by two companies in California: Muslim Savings and Investments (MSI, now headquartered in Texas) and American Finance House-*LARIBA* (Los Angeles Reliable Investment Bankers Associates). LARIBA was the first company to offer diversified retail financing services to the community in all fields. It first offered Islamic mortgages using the *Murabaha* (cost-plus) model in 1987, it later moved to using *Musharakah Mutanaqisah* in 1990 (Abdur-Rahman, 2000).

There is an unconfirmed total of 10 Islamic finance houses operating in North America with five operating in Canada and five operating in the United States

3.5.1.3 Commercial banks with Islamic windows

In response to this growth, new companies entered the market. The most important of these in mid-1997, the United Bank of Kuwait (UBK) started financing mortgages using the lease-to-purchase model (*Ijarah wa Iqtina*) in a program called *Manzil*. The United Bank of Kuwait was a conventional bank with an Islamic window, but more significantly the United Bank of Kuwait's entry into this market was marked by banks' willingness to deal with the legal and regulatory framework of North America head on, paving the way for future development in Islamic financing in North America.

Prior to 1997, no bank in the U.S. offered formally-structured Islamic financing that was both publicly approved by a U.S. regulatory agency, and approved by a board of Islamic scholars. In the late 1990s the New York branch of the United Bank of Kuwait (now closed) paved the way for financial institutions that currently offer Islamic financial products. In 1997 and 1999, the Office of the Comptroller of the Currency issued two interpretive letters permitting a New York branch of the United Bank of Kuwait to offer its Islamic home financing products to Muslim customers. The interpretive letters have since been the premise for determination by certain regulatory agencies as to whether an Islamic finance product is compliant with U.S. banking regulations and can be offered by a financial institution.

HSBC, the only large bank offering Islamic home financing and other *Shari'a*-compliant products in the United States, focuses its Islamic finance activity on the state of New York. Since 1998, HSBC has offered Islamic finance products and services. The HSBC home financial product is entitled *Murabaha* Home Finance, and is also known as "cost-plus financing'.' It differs from conventional lending in that it is based on the idea of selling something at an agreed-upon profit with payment over a period of instalments that can range from 10 to 30 years

Devon Bank in Chicago is a privately-owned community bank involved in Islamic finance which developed largely as a result of their locations in multi-ethnic neighbourhoods with high concentrations of Muslims. Devon Bank offers its products both inside and outside of Illinois. It offers Islamic home, construction, and small business financing. Home financing is offered through either the *Murabahah* or *Ijarah* model. Devon Bank offers commercial *Murabahah* and *Ijarah* transactions for real estate acquisitions to business customers.

3.5.2 Australia

Muslims in Australia, according to the 2001 census account for 1.5 percent of the population mainly concentrated in Sydney and Melbourne. Currently Islamic home finance is provided by the Muslim Community Credit Union Ltd (MCCU) and the Muslim Community Co-operative (Australia) Ltd (MCCA).

3.5.2.1 Muslim Community Co-operative (Australia) Ltd (MCCA)

MCCA is the first Islamic financial institution and was established in February 1989**.** It operates as a co-operative and offers investment accounts and Islamic home finance.

MCCA has more than 69,000 members in Victoria and New South Wales. The size of its business is more than A$120 million annually in Islamic home finances. MCCA currently offers four models of home finance products *Ijarah*, *Murabahah, Tamleek* (based upon purchase by agency), and *Ijarah Muntahiya bi-Tamileek (Ijara wa Igtina).* It can finance for purchase, refinance or construction (*tameer*) of a home according to the appropriate mode of financing. The term of financing up to 30 years, the co-operative pays up to 95 percent and first registered mortgages over the house (collateral) as security (MCCA, 2006).

The MCCA has recently obtained registration as a credit union under the name of the Muslim Co-operative Credit Union (MCCU). As a credit union, the organization is able to expand its operations and offer retail banking services (Mirza & Halabi, 2003).

3.5.3 United Kingdom

The UK has a growing Muslim population, estimated at 1.8 million, representing approximately 3 percent of the country's population. The removal of the double stamp duty (the house purchase tax) in 2003 increased the demand for Islamic home finance and made it more attractive for new players to enter the field. The Financial Services Act 2005 gives the Financial Services Authority (FSA) responsibility for regulating Islamic home finance. Scholars and Islamic banking practitioners consider *Ijarah* and *Murabahah* to be the most suitable methods for home financing in the UK. Islamic home finance services provided by fully fledged Islamic banks, High Street commercial banks with an Islamic window and financial companies (houses).

3.5.3.1 Islamic banks

The Islamic Bank of Britain (IBB) was granted a full banking licence by the UK regulator in August 2004 two years after it launched an application with the support of leading Islamic banks and financial houses in the Gulf in 2002. The first retail branch was opened in the Edgware Road in London the following month. The bank's head office and operational centre is located in Birmingham, the second largest city in the United Kingdom, which has a major concentration of the country's Muslim population (Wilson 2005). The bank has eight branches in London, Birmingham, Manchester and Leicester. The bank launched Islamic home finance in 2005, teamed up with *Alburaq* and Bristol & West Building Society. The bank implements the Diminishing *Musharakah* mode of financing over a 25-year term, contributing up to 90 percent of the home purchase price.

3.5.3.2 Commercial banks with Islamic windows

The United Bank of Kuwait (UBK) now the *Ahli* United Bank paved the way for Islamic mortgages in the UK, when it first introduced Islamic mortgages based on *Murabahah –Manzil* Home Plan in 1997 and *Ijarah–Manazil* Home Plan in January 1999. However, UBK has signed an agreement with West Bromwich Building Society to distribute *Al-Manzil* in the UK (Parker, M., 2002).

A parallel agreement was accomplished between *Alburaq*, a subsidiary of the Arab Banking Corporation, and the Bristol and West Building Society, a subsidiary of the Bank of Ireland for the distribution of Islamic mortgages in England (Smith, D 2004).

In July 2003, HSBC bank became the first UK high street bank to offer Islamic home finance through its dedicated *Amanah* Islamic finance division. *Amanah* Islamic home finance products, initially offered in Bradford, Cardiff, Birmingham and London branches, are currently offered in more than 84 branches. The model is based on the Diminishing *Musharakah* method of home finance.

In March 2005 Lloyds TSB entered the market with 17 branches across the UK including London, Luton and Birmingham. The product was based on the

Diminishing *Musharakah* method designed by *Alburaq* and Bristol and West Building Society.

3.5.3.3 Finance companies (houses)

The *Ansar* Finance group is an Islamic community collective established in 1994 in Manchester to provide '*halal*' borrowing and investment to its members among the UK Muslim Community. In February 2000 *Ansar* Finance Group (afg) launched *Ansar* Housing Ltd (AHL) to provide Islamic home finance to AHL's members using the same system as the Islamic Housing Co-operation in Canada. AHL managed to purchase 14 properties under the scheme, but due to recent government legislations regarding Islamic home finance products AHL stopped providing this service until it receives an authorisation from the FSA.

There are a number of independent online companies 'Islamic mortgage supermarkets' which assist customers to evaluate and select a '*halal*' mortgage that suits them, *e.g. Halal*mortgage.co.uk and Islamicmortgages.com.

3.5.4 Malaysia

Malaysia is viewed as providing an adequate Islamic financial model; the mortgage market is relatively developed, representing nearly 22% of the GDP. Islamic home finance is usually based on *Bai Bithaman Ajil* (Deferred Payment Sale) with two types of *Takaful* (Islamic insurance) covering the house owner, *Takaful* plan and *Takaful* Mortgage Reducing Term Assurance (ARTM). The former provides cover for the house against loss or damage, and the latter provides full settlement of the outstanding balance of the house in the event of permanent disability or death (Seow, 2005).

3.5.4.1 Bank Islam Malaysia

The first Islamic bank in South-east Asia started on July 1983, has been listed on the Kuala Lumpur Stock Exchange since January 1992, and by 2005 it had 85 branches across the country, with over 50 products on offer. Its home financing is based on *Bai' Bithaman Ajil* (Deferred Payment Sale) contracts by pre-arranged monthly instalments. The rates for home financing vary according to LVR and the term involved, but for the first year charges only amount to 2.8 per cent and for the second year 6.0 per cent as the bank allows for new homeowners having to buy furnishings and other household items that might limit their capacity to repay. For years 3 to 10 the bank charges are 7.5 per cent for home finance for amounts up to US$65,790 for 100 per cent financing and 7.3 per cent for 80 per cent financing given the lower risks involved. For financing exceeding US$65,790 the rates increase to 8.0 per cent and 7.8 per cent respectively. Rates rise by 0.1 per cent for periods exceeding 10 years, and a further 0.1 per cent for periods exceeding 20 years (Wilson, 2005).

3.5.5 Gulf Cooperation Council (GCC)

In 2002 the authorities in the UAE allowed foreigners to buy properties on a freehold basis, due to the fact that one in ten residents is foreign. This has given an immense boost to the residential real estate and mortgage market. In Dubai alone there are 16 mortgage lenders which intensify the competition in the mortgage market. The biggest players in the field are Tamweel a subsidiary of Dubai Islamic Bank; Amlak, a subsidiary of Emmar Properties and HSBC bank. The size of the market is reported to be about $2.3 billion, 4% of UAE's gross domestic product (GDP) (Bergsman, S 2006).

Like Dubai, in 2005 Qatar's government allowed homeownership to non-Qatari national residents which created a demand for mortgages.

Saudi Arabia, a good example of a rich Muslim state, established the Saudi Estate Development Fund and through continuous government support provided easy loans to a large sector of the population. In addition to this, the Saudi government has built many housing schemes in major cities of the Kingdom. Survey study suggests that most Saudi citizens would not be prepared to consider an interest-bearing loan, for religious reasons. However, all the Islamic alternatives suggested gained support (Al Tasan, HAS, 1998). However, Analysts forecast that by 2015, in the GCC countries, a significant proportion of conventional financial services are expected to become *Shari'a* compliant.

3.5.5.1 Dubai Islamic Bank (DIB)

Dubai Islamic Bank provides home finance to UAE nationals who have secured a grant or a loan through the government's housing programme. This is known as the *Sakan* finance scheme, which covers finance of up to US$95,000 for the purchase of homes, the repayment period ranges from 12 to 108 months. The scheme is based on the *Murabahah* method, with fixed monthly payments. When the finance period is longer the scheme is based on *Ijarah* mortgages.

Al Rajhi Banking and Investment Corporation in Saudi Arabia offers home finance for Saudi citizens with no advance payment facilities for up to a 15-year term.

3.5.5.2 Kuwait Finance House (KFH)

KFH offers home finance on a *Murabahah* basis over a 15-year term with fixed instalments (10 instalments/year).

It also offers *Ijarah* with option to own (*Ijarah wa Iqtina*), with monthly instalment (10 instalments/year) over a 10-year term. Once finance is approved the client has to open a current account at KFH and permanently transfer his salary into it. It also has an international real estate services for its clients in different countries including the UK.

3.5.6 Jordan

Jordon was one of the first countries in the Middle East to introduce the housing finance system in the early 1980's; housing finance volume represents 11 percent of the GDP. Jordan's housing finance systems benefit high- and upper-middle income groups. Lower income groups usually do not have access to home finance, due to weak involvement in the formal finance system, irregularity of income flows and lack of guarantees.

3.5.6.1 Jordon Islamic Bank

The JIB finances housing through the following methods:

Murabahah lilamir Bilshri'a Financing: Granting the financing of the purchase of building materials (including structure and finishing), the purchase of flats, houses and plots of land, for a period of up to 120 months on condition that the monthly instalment is not more than 40 percent of the client's income. It is guaranteed by transferring his salary if he is an employee and suitable guarantees and real estate mortgage for the interest of the Bank.

Ijara wa Iqtina (leasing purchase): Purchasing ready-made flats or houses and renting them to the lessee for a period of up to 25 years in such a way that the monthly rental suits the lessee with a ratio of no more than 40 percent of his income. The down-payment of the price of the real estate must not be less than 20 percent, with an acceptable guarantor in the Bank. The Bank assigns the ownership of the real estate to the lessee at the end of the specified period, providing that he fulfils the conditions of the signed contract with the Bank.

3.5.7 Pakistan

Housing finance in general is undeveloped in Pakistan; its share is less than 1% of the country's GDP. The affordability is very poor with nearly 95 percent of the people falling below the mortgage affordability of Rs 30 lac (hbfc. pak, 2006). Commercial banks focus on high net worth clients. The *Shari'a* compliant method uses their rent sharing with flexible weightage to bank's funds or buy-back cum mark-up (Siddique, 1985). The House Building Finance Cooperation state-owned cooperation provides financial assistance for the construction and purchase of houses, development of land, as well as for repair and re-construction. HBFC's latest introduction is the non-interest bearing new schemes of *Shandaar Ghar* Scheme *(Murabahah*)-2001 & *Ghar Aasaan* Scheme *(Musharakah)-2002* which are *Shari'a* compliant have attracted attention.

3.5.8 Iran

The housing finance system in Iran is small and dominated by the public sector. It represents three percent of the GDP. House prices are very high due to the house and land policies, which creates a severe affordability problem. Islamic home finance in Iran is based on instalment sale, civil partnership, hire purchase, *Qard al –Hassanah*, direct investment and *Jo'alah* (Hedayati, 1993). Iranian commercial banks are empowered by the central bank of Iran to construct low-cost housing and sell it to applicants under the instalment sales system. Under the Usury-Free Banking Law of 1983, Iranian banks are authorized to provide various kinds of services and charge a commission for these services.

3.6 THE ROLE OF SUKUK IN HOUSING FINANCE

Sukuk is the Arabic name for a financial certificate that is popularly perceived as a *Shari'a*-compliant bond. According to AAOIFI Standard 17 *Sukuk* are asset-backed trust certificates evidencing ownership of an asset or its usufruct. These certificates are based on *Istisna*, *Ijarah*, *Mudarabah*, *Musharakah*, *Murabahah* and *Salam* but share with conventional bonds marketability, rateability, enhanceability, and versatility (Wilson 2006).

Innovations of highly structural *Sukuk* deals for Islamic home finance instruments as securities tradable in the secondary market is very important for the future of the Islamic home finance industry. As the current trend in housing finance is creating a secondary market for a number of reasons, *e.g.* accessing the capital market in order to expand the flow of funds to the housing sector and improve risk management for lenders and expanding competition in the market. Secondary market institutions are not appropriate vehicles for subsidizing mortgage credit and expanding access to mortgage credit can be better addressed through mortgage design and direct income or down payment support for target group borrowers (Lee, M 1998).

In the United States Freddie Mac started to finance Islamic mortgages in March 2001 for Lariba Company with a $1 million pool of *Ijarah wa Iqtina* contracts. It has securitized, over $100 million of Islamic home finance contracts financed by Freddie Mac (Salam, S 2002).

Cagamas Berhad, the National Mortgage Corporation, was established in 1986 to promote the secondary mortgage market in Malaysia. In March 1996 Cagamas Berhad issued the first mortgage *Mudarabah Sukuk* in the world. It combines two basic concepts: *Bai' al Dayn* (sale of debt or debt trading) and *Mudarabah* (profit sharing). The proceeds of the *Sukuks* are utilized by Cagamas to purchase "Islamic housing debts" on the basis *of Bai' al Dayn* (Cheng, H .S. 1999).

In the UAE the Emirates National Securitization Corporation (ENSeC) was created to facilitate the development of the secondary mortgage market in Dubai. Amlak Finance in 2005 launched an *Ijarah Sukuk* backed by $200 million in Islamic mortgages (Bergsman, S 2006).

Zamzam Tower or *Abraj AlBait, Makkah* is a landmark transaction structured to the international standards of *Sukuk al Mudarabah* for real estate developed by *Munshaat* Real Estate Company in KSA.

The Jordanian Government, with the help of the World Bank, has created secondary mortgage facilities (SMF). It is the first in the Middle East, is privately owned, is sponsored by the government and it functions as a refinancing facility relying on mortgages collateral (Douglas, B. Diamond 1998). The *Muqaradah Sukuks i.e.* securitizations of the *Mudarabah* contracts were floated by the Ministry of *Awqaf* in Jordan in 1988.

3.7 OBSTACLES AND THE WAY FORWARD

Islamic home financing has encountered a set of legal and financial obstacles, which have jeopardized its growth and development; these obstacles, can be summed up as follows:

3.7.1 Legal Obstacles

A suitable legal, institutional and tax framework is a necessary requirement for establishing sound financial institutions and markets. Islamic law offers its own framework for the operation of commercial and financial contracts and transactions. Nonetheless, commercial, banking and company laws suitable for the operation of Islamic banking and financial contracts do not exist in many countries.

Inflexible interpretation of laws as regards the case of Islamic mortgages requires the bank, according to *Shari'a* law, to own the property first and then transfer it to the client's name. Thus Islamic mortgage contracts are treated as buying and selling properties in most of the countries and hence are taxed twice.

In the absence of Islamic banking laws the enforcement of Islamic mortgage contracts in courts may require additional effort and cost, for example unavailability of sufficient tax incentives and multiplicity of taxes on houses and real estate such as the income tax, roofed spaces. Islamic banks emphasise the form of Islamic contracts over substance, regulatory in some countries like the USA which overlook the form of the contract and rely upon substance that may be problematic.

International acceptance of Islamic financial contracts requires them to be *Shari'a*-compatible as well as acceptable under the major legal regimes such as Common law and Civil law systems.

3.7.2 Financial Obstacles

These are the obstacles related to the supply and demand of Islamic mortgages such as:

The ability of the bank to balance the terms of maturity of the funds invested in housing finance, which are usually of a long term nature, with the terms of deposits with the bank, which are mostly of a short and medium term nature.

The ability of the bank to reconcile between maximising the profit of the shareholders, and its ability to provide low-cost housing finance to its clients.

Under some countries regulations Islamic mortgage products attract 100 percent risk weightage *e.g. Ijarah* mortgages. In other words, an Islamic bank has to set aside the full amount of the property to cover the full value of the house, in case the buyer cannot afford to pay the rent, whereas a conventional mortgage has a risk weighting of only 50 percent (Tran, 2002).

Hyper inflation conditions hinder the operation and the development of Islamic housing finance in many ways by the increasing cost of the housing units, which is not matched by an increase in household income, in which case of defaults may be encountered. These conditions also have an impact on the rate of return to be charged by some Islamic mortgage contracts e.g. *Murabahah* (Salama, 1995).

Proponents of Islamic banking view these institutions as viable alternatives to interest-based banks in the markets in which they operate. They argue that Islamic profit-and-loss-sharing contracts efficiently allocate capital to long-term productive investment

Moreover, the mission of Islamic financial institutions best serves small entrepreneurs and rural businesses that do not have access to credit in the mainly urban-based conventional banking system. For these reasons Islamic banking may be an engine of growth and development in Islamic countries.

In most countries, however, the Islamic finance sector has yet to live up to these expectations. First, it is not clear from the statistics available if the Islamic sector has continued to grow apace after rapid expansion in the 1980s. For example, Aggarwal and Yousef (2000) cite the experience of Faisal Islamic Bank (FIBE). FIBE was founded in 1979 and today ranks as the third largest Islamic bank in the world and Egypt's sixth largest commercial bank. FIBE's total assets grew rapidly from 1979 to 1985 at a rate of over 50 percent but thereafter declined in both nominal and real terms. Similarly, FIBE's market share of total deposits grew from three percent in 1979 to 7.3 percent in 1983 but subsequently showed little growth.

In the countries of the Gulf Cooperation Council, home to four of the world's five largest Islamic banks, the Islamic banking sector grew at an estimated 10 percent a year in nominal terms during the first half of the 1990s. However, inflation in the region was almost as high as this on average, thus growth in real terms was significantly lower. Conventional banking still dominates in the Gulf and the Islamic sector represents less than 10 percent of the deposits of the total banking system in the Gulf countries overall.

Second, Islamic banks can be characterized as heavily concentrated in mark-up instruments that are used chiefly for short-term trade finance and the portfolio share of longer term financing instruments in these institutions is rather small. Aggarwal and Yousef (2000) examined the flow of new mark-up financing versus term financing by profit-and-loss sharing instruments for FIBE, the Jordan Islamic Bank, Bank Islam Malaysia (BIM), and the whole of the Iranian banking system, which is entirely Islamic. For all these institutions, short-term mark-up financing consistently composed more than 50 percent of total new financing flows. For the BIM, mark-up financing averaged over 95 percent of total new financing for the period 1983 to 1994. Moreover, in Pakistan, mark-up finance composed an estimated 85 percent of the total financing of Islamic banks in this country.

Third, there is some evidence that Islamic bank portfolios appear to be concentrated in trade; retail, finance, and service sector investments, rather than the more productive capital-intensive industrial sectors of the economy. In Egypt, 90 percent of Islamic bank portfolios are in the trade and services and financial sectors whereas the comparable concentration for Egyptian commercial banks is only 63 percent. Islamic banks' exposure to agriculture and industry represents 10 percent of their portfolios compared to approximately 30 percent for commercial banks in Egypt. In Iran, where credit allocation is determined by regulation, lending targets to the retail trade and services sectors are consistently overrun while shortfalls are realized against lending targets for the industry and agriculture sectors. In Malaysia, the Bank Islam Malaysia committed only 10 percent of its total financings to manufacturing over the period 1983 to 1994, compared to 34 percent for other Malaysian commercial banks.

Several factors can constrain the growth of Islamic finance. First, the macroeconomic environment needs to improve further in many countries where Islamic finance is prevalent, notably in the direction of trimming public sector debt and deficits and reducing levels of regulations.

Islamic investors, however, are thinking globally and are investing in sophisticated instruments in countries, which have a more stable macroeconomic environment, such as the United Kingdom and the United States. Second, better accounting standards are needed to aid investment transparency in new products, whether conventional or Islamic. Third, greater operational efficiency is required in the financial system in the areas of asset quality and prudential management both within and outside the Islamic banking sectors. Islamic banking doctrine would benefit from harmonization and mutual recognition of terms and standards across markets and countries. This would lower transaction costs and help to unify national and regional capital markets.

3.7.3 International Finance Corporation (IFC) Activities in Infrastructure Finance

One of the types of project finance for which Islamic financing might be appropriate is infrastructure finance. IFC has been involved in the financing of more than US$7 billion for infrastructure projects costing more than US$30 billion in developing countries, and has played an active part in private participation in promoting the spread of private participation in the infrastructure sector. As a corporation, IFC has devoted about one-third of its total financing worldwide to infrastructure investments.

While opportunities are greatest in power telecommunications, IFC projects in transportation and utilities, including roads, ports, and water, are also increasing.

Demand has increased for IFC financing of infrastructure projects as developing country governments continue to liberalize sectors such as telecommunications, transportation, and power. This growth in demand is the result of decisions by many governments to broaden opportunities for private investors, and the difficulties of mobilizing funds and structuring transactions for large infrastructure projects. IFC has worked in countries seeking to undertake their first private infrastructure projects, as well as in countries that have some experience with private investors but still have difficulty in mobilizing funds. IFC complements its direct project support with technical assistance to governments and project sponsors. Through this dual strategy, IFC leverages its relatively limited resource base, with particular emphasis on achieving high funds mobilization ratios, demonstrating successful projects, and sharing lessons gathered from its experience.

The demand for IFC financing of private sector infrastructure projects will continue to increase especially in countries where sustained non-inflationary growth is needed to improve the standard of living.

3.7.4 Islamic Investment in Infrastructure Finance

It is reasonable to ascertain whether Islamic instruments could be helpful in mobilizing the large sums that are currently held in short-term Islamic investments for investment in private sector infrastructure projects. Several factors suggest that Islamic finance can make a potentially significant contribution to financing the large infrastructure investment needs that have been identified. First, in providing basic social goods such as power, water, transport, and communications services, infrastructure projects fit well with the perceived social responsibility that is an essential feature of the Islamic finance industry. Investing in socially valuable services accords better with the principles of *Shari'a* than does, for example, lending to finance the consumption of luxury goods. Second, limited recourse or non-recourse project financing structures represent a form of asset-based financing that is consistent with Islamic law at a general level. Despite the often-complex financial claims that constitute these structures, project investors typically share in the asset and cash flow risks or projects in ways that investors are required to under Islamic law.

Islamic banking and finance institutions offering financial products consistent with Muslim religious beliefs grew rapidly during the 1980s and into the 1990s. Islamic financial products encompass a range of asset-based and profit-participating contracts that are generally well-suited to financing economic development. Leasing funds pioneered by ANZ and IFC are well-adapted to many of the constraints facing borrowers and lenders in the developing regions of the Islamic world. Leasing funds also provide both borrowers and investors with *Shari'a*-based financial claims. There is therefore the potential for significant future growth in this market. However, it is the asset-based project finance markets and socially valuable infrastructure projects in particular that perhaps holds the greatest promise for the mission of Islamic financial institutions.

To sustain the future growth prospects for the Islamic finance sector and to attract international capital inflow, further progress in macroeconomic stability and financial sector reforms are needed in many countries where Islamic finance is prevalent. Notably, greater efficiency is generally needed in the areas of asset quality and prudential management. Islamic instruments can be mobilized to deliver on these institutional efficiency gains, with very little in the way of incremental costs entailed, to provide the governance structures that Islamic law mandates.

3.8 CONCLUSION

There are many economic, social and demographic factors which push the housing problem to the forefront of development priorities. Therefore, Islamic *Shari'a* has given much consideration to this subject by recognizing that the provision of decent housing facilities for all citizens falls within the responsibilities of the state.

Based on the theoretical and technical *Fiqh* issues discussed in this chapter as well as the case studies across the world certain financing techniques can be used in Islamic housing finance. These include: *Istisna'*, Decreasing *Musharakah*, housing funds, instalment sale, interest-free loans deferred-payment sale, *Musharakah*, *Murabahah etc.* But this should be examined with a view to selecting those which are more suitable to the economic conditions of the country in which they need to be implemented.

Shari'a scholars, bankers, academics and policy makers need to cooperate with each other and coordinate their efforts, in order to subject these techniques to a process of careful scrutiny and refining so as to make them tolerable and appealing to both the bank and the customers without violating the *Shari'a* and the proper banking requirements.

Chapter 4

ISLAMIC HOUSING FINANCE IN THE UNITED KINGDOM: THE SUPPLY SIDE AND REGULATORY ISSUES

4.1 INTRODUCTION

The largest volume of Islamic financing business carried out in the United Kingdom at present originates in Muslim countries, largely the Gulf. However, there is a large potential domestic market which is only just beginning to be tapped. The attraction of London for Gulf clients, which include all the major Islamic banks, is the breadth of specialist financial services offered, the depth to the market and the solidity of the major banks, which include all the leading global players. London is nearer to the Middle East than New York, and in a convenient time zone for communications.

Most Gulf businessmen and bankers have English as their second language, and many have long-standing connections with the United Kingdom, where they and their families enjoy spending time. The Arab community in central London is one of the most affluent in the world and there are many Arab restaurants and hotels used to catering for the needs of Muslim visitors. London is also the second most important centre for the Arab media after Cairo, with its own Arabic newspaper and magazines and an Arabic satellite television channel.

The aim of this chapter is to assess the supply of Islamic housing finance in the United Kingdom. A brief overview of Islamic housing finance in the UK is provided with detailed discussions of the relevant financing techniques. Fortunately, a number of barriers that have prevented the wider availability of Islamic housing finance in the UK have been removed. Nonetheless, this chapter discusses the remaining legal and regulatory issues involving the Financial Services Authority, as well as tax matters involving Her Majesty's Treasury. The market experience has been examined, focusing on what HSBC Amanah and the Islamic Bank of Britain (IBB) have to offer so as to compare the products and services offered by Islamic windows of the High Street Banks with those of the British Islamic Bank. The political economy of Islamic housing finance in the UK has been monitored and finally the prospects and future of Islamic housing finance in the United Kingdom has been studied.

4.2 PERMISSIBILITY OF CONVENTIONAL MORTGAGES UNDER NECESSITY

In 1999, Shaykh Yousif al-Qaradawi ruled for the European Council for *Fatwa* and Research that Muslims living in the UK or in the West in general are permitted to take up a conventional mortgage to buy a home, provided that: the home to be bought is for the buyer and his household. The buyer must not have another home and must not have any surplus of assets that would enable him to buy a home by any means other than a mortgage (ECFR, Fatwa (26) Resolution 2/4).

The ECFR stresses that bank interest is *riba*, but its resolution is based on the following two principles:

First, the verdict of Abu-Hanifah, which claims that it, is permissible for Muslims to trade with usury and other invalid contracts in countries other than Islamic countries. *Shari'a* does not require Muslims to establish the civil, financial and political status of *Shari'a* in a non-Muslim country, as this would be beyond their capabilities. Allah (*swt)* does not require people to do things that are beyond their capacity.

Secondly, the principle of *darurah*, or necessity, when there is no other alternative. There is a well-known rule in *Fiqh* which states that extreme necessity makes unlawful matters lawful. This rule is derived from five *Quranic* texts, amongst them "And He has not laid upon you in religion any hardship" (Quran 22:78).

The ECFR stresses that what has been made permissible due to extreme necessity must be handled with great care and taken in measure. For example it should be restricted to the category of people who are in real need of a house and if European banks observe the needs of Muslims and offer *Shari'a*-compliant or alternative financing this resolution will be void (Altikriti & Howard, 2008).

4.3 UK ISLAMIC FINANCIAL MARKET CHARACTERISTICS

In 2002 Sir Howard Davies, the then chairman of the Financial Services Authority in the UK, assumed that there was a gap in the market for retail sector Islamic banking products which would cater for nearly two million UK Muslims. The Muslim population represents 50 percent of all UK ethnic minorities with approximate savings of about £1 billion and more than 500,000 Muslims visited Britain in 2001, spending nearly £600 million (Duckers, 2002). There is a considerable number of Muslims living abroad, mainly from the Middle East, who have expressed their desire to own properties in Britain, mainly as a holiday residence, but are reluctant to embark on an interest-bearing financing facility. For these investors an Islamic home financing scheme would offer the opportunity to own a property in Britain. According to market research analysts Datamonitor, the 5,000 richest Muslims in the UK have liquid assets of more than £3.6 billion. Datamonitor research (1999) estimates that 300,000 Muslim adults in the UK have annual incomes in the range of £30,000 and over (see Table 4.1). This means that approximately 25 percent of all adult Muslims are excellent potential customers for banking and financial products (Mathew, 2003).

A large number of British Muslims, perhaps in excess of 100,000, have small businesses. These include neighbourhood food stores which compete with the dominant supermarket chains by being in more convenient locations for those who do not have cars or cannot drive. There is also a significant number of Muslim-owned textiles and clothing manufacturing businesses, which have a lower labour cost base than their competitors, although they may have been adversely affected by the minimum wage legislation introduced in 1999.

Bangladeshi immigrants have been particularly active in the restaurant and catering business and account for up to twenty percent of the total number of restaurants nationally. All these groups have small business financing needs, mainly to cover mortgages on premises, inventory, and stock finance and equipment purchases.

4.4 PRODUCTS STRUCTURE IN THE BRITISH RETAIL MARKET

In the Muslim World Islamic finance practitioners and *Shari'a* Scholars have developed a number of ways in which to provide finance and banking facilities for the purpose of financing a home, without resorting to interest, which are *halal* - that is permissible within the *Shari'a* law. The financing techniques and methods which have been discussed in Chapter Three are broadly based on profit- and loss-sharing contracts, lease-to-own contracts or cost plus mark up contracts. *Shari'a* scholars and Islamic bankers identified *Ijarah* (lease) and *Murabahah* (cost-plus mark up) as the most suitable techniques to facilitate affordable homeownership in the UK (Thomas, 2006). Both structures will necessarily operate in a different way to a conventional mortgage loan. However, the risks to the financier remain very similar to those to financiers providing conventional mortgage finance, the risks being primarily of affordability and asset value, *i.e.* house prices (Thomas, 2006).

4.4.1 *Murabahah* Based Mortgage

Under the *Murabahah*-based mortgage the bank buys the dwelling from the vendor at a price agreed between the customer and the vendor. The bank then directly sells the dwelling on to the customer at an agreed mark-up price. This mark-up price is calculated taking into account the length of time allowed to the customer to repay the original purchase price (Thomas, 2006). The mark-up can be compared economically to the conventional fixed interest rate. This arrangement is considered to be permissible by *Shari'a* law because the bank is taking the title of the property and assuming the risk.

In practice the principle operation of *Murabahah* is as follows:

1. The client selects the property s/he wishes to buy and agrees the price with the vendor in the normal way.

2. The client approaches the bank for financing. The bank undertakes normal underwriting procedures and an independent valuation of the property.

3. The bank instructs its own solicitors to investigate the title to the property in the standard way.

4. Once these preliminary steps are completed, including legal confirmation of the title of the property, the bank contracts to buy the property from the vendor at a price agreed between the vendor and the client.

5. The bank agrees to sell the property to the client under a deferred purchase agreement by way of sub-sale at an agreed mark-up price.

6. On completion, the bank sells the property to the client by way of sub-sale at the agreed mark-up price under a deferred purchase agreement.

7. The customer takes over the legal title of the property and becomes the registered proprietor of the property at the Land Registry, and the bank is secured by a first legal charge over the property.

8. The *Murabahah* contract records the sale between the bank and the client.

9. The client makes regular monthly payments until the purchase price is paid.

The main features of the *Murabahah* mortgage are very rigid and only suitable for a new purchase; it is not suitable for re-finance. It is usually used for short-term financing. The monthly instalments are fixed and do not alter throughout the payment term.

The bank reduces its immediate financial exposure in the *Murabahah* mortgage by taking the first instalment of the purchase price, usually 10-20 percent of the property value on the day of completion of the contract.

The bank can re-possess the property and exercise the power of sale contained in the first legal charge if the client defaults on payment or breaches the terms of the contract.

4.4.2 *Ijarah* Based Mortgage

Under the *Ijarah*-based mortgage the property is purchased by the bank and sold to the client at the same price with payment being spread over an agreed term. The bank leases the property to the client on an agreed rental basis. Economically this could be compared to a conventional mortgage loan with variable interest rate (Thomas, 2006).

There are two slightly different models based on *Ijarah* contract: *Ijarah wa Iqtina* (lease-to-own) and Diminishing *Musharakah* and *Ijarah*. There is very little difference between them, however the following points should be considered:

I. Both models could be used for establishing a co-operative, but in practice only *Ijarah wa Iqtina* conforms to the structure of a co-operative.

II. The bank and the client engage in joint ownership in both models. However, the legal title remains with the bank in the case of *Ijara wa Iqtina* and is shared between the bank and the client in the case of Diminishing *Musharakah and Ijarah* (Dar, 2002).

In practice the principle operation of *Ijarah* is as follows:

1. The client chooses the property s/he wishes to buy and agrees the price with the vendor in the usual way.

2. The client approaches the bank for financial assistance and the bank undertakes standard underwriting enquires and independently values the property.

3. Once these introductory steps are concluded, including legal confirmation of the title of the property, the bank will buy the property from the vendor, taking the legal title.

4. The client signs an agreement with the bank to purchase the property over a specified time.

5. The client signs a lease detailing tenancy rights and explaining the relative responsibilities of the respective parties.

6. The client makes regular monthly payments, comprising both payments towards the capital (purchase price) and rent.

Ijarah is suitable for new purchase and refinancing. The bank reduces its exposure to the property by requiring a down-payment of 10-20 percent of the property value. The bank can evict the client for failing to make payments of rent under the terms of the lease. The original term of the lease is generally at least seven years. This avoids placing on the bank the obligation of repairs, under Section 11 of the Housing Act 1985. The rent is assessed annually and is adjusted to reflect the payments the client has made to the bank. The rent might be subject to review by a mutually-acceptable arbiter or determined by reference to LIBOR, base rate or other benchmarks plus a profit margin. Bench-marking the rent to LIBOR is accepted by many *Shari'a* scholars. The client will take the benefit of any capital gain of the property and bear any decrease in its value.

Table4-1 Comparison between Conventional and Islamic Mortgages

	Conventional Mortgage	**Islamic Mortgage**
Instruments	The lender advances funds to the borrower and charges [interest] for the mortgages loan.	Based on trade [*Murabahah*] and leasing [*Ijarah*], Islamic mortgages are interest free.
Eligibility	Credit references, stable sources of income to be able to return the loan before the age of 65 qualify to apply.	Credit references, stable sources of income to be able to pay the purchase price before retirement age qualify to apply.
Property qualification	Generally the lender has no lower limit to the property value.	Minimum value for the chosen property must be £50,000.
Loan to Value (LTV)	Up to 125% of the property value.	Up to 80% of the property value
Insurance	Life insurance and building are mandatory in most cases.	There is no compulsory life and building insurance required.
Risks	Lender never owns the property.	The bank puts itself in the position of owner of the property. Higher risks.
Term	Payment term up to 40 years.	*Murabahah* up to 15 years minimum 5 years *Ijarah* up to 25 years minimum 7.5 years
Income Multiplier	Income Multiples Up to 5 times primary annual income sole applicant.	*Murabahah* 2.5 times primary annual income *Ijarah* 3 times primary annual income sole applicant
Fee	Arrangement fee generally up to £500.	Arrangement fee of 0.75% of the property value less the first payment.

Sources: Review of Islamic Economics (No. 12&14)

4.5 BARRIERS TO THE DEVELOPMENT OF ISLAMIC HOUSING FINANCE IN THE UK

In the last few years there have been combined efforts by the government and the financial services industry to remove some of the obstacles. In 2001 a working party was set up to deal with this matter, chaired by Andrew Buxton, a former chairman of Barclays Bank and director of the Bank of England. Also involved were representatives of the Treasury, the Financial Services Authority (FSA), several banks, the Muslim Council of Britain and some other Muslim organizations. The working party identified the main hurdles, affecting the development of Islamic home finance in the country as follows:

The inability to use either *Murabahah* or *Ijarah* to assist with house purchases, under right-to-buy or other various public sector homeownership initiatives, because the financier is the original buyer and hence does not qualify.

The additional Stamp Duty burden when finance is provided following the principles of either *Ijarah* or *Murabahha* still applies to Islamic mortgages provided by companies (The new regime only exempted banks & building societies).

The adverse regulatory capital weighting treatment for the financier when home finance is provided following the principles of *Ijarah*, the financer is required to hold higher capital weighting in this model.

The inability to obtain financial assistance from the State in cases of financial hardship as the aid is based on interest.

There are other issues related to supply problems which may deter the banks from considering Islamic home finance products, such as:

The additional legal costs which may be incurred, in comparison with conventional mortgage finance

The uncertain legal interpretation, in the UK, of the *Ijarah* and *Murabahah* contracts in the event of their enforcement

All these and many others are genuine problems which are considered in further detail in the light of the joint documents prepared by Barclays Group, HSBC, Union Bank of Switzerland, iHilal UK, and United Bank of Kuwait in 2001 as follows:

4.5.1 Public Sector Homeownership Initiative

The Government launched the Low Cost Home-ownership (LCOH) programme in the 1980's, which consists of a number of schemes with different characteristics and objectives. One of the main objectives of LCOH is to encourage sustainable home-ownership; and enable first time buyers to get a foot on the property ladder (Bennett, 2002). There is a range of public sector home purchase assistance schemes available in the UK targeted at those attempting to get on the homeownership ladder, the majority of which are aimed at tenants in public sector rented accommodation. These include: Right to Buy (RTB), Right to Acquire (RTA), Rent to Mortgage, Voluntary Purchase Grant Scheme (VPG), Home Buy Scheme, Cash Incentive Scheme (CIS), and Conventional Shared Ownership.

4.5.1.1 The right to buy

The Right to Buy means that qualifying tenants can buy their homes by paying the full purchase price at once. They receive a discount of between 32 and 60 percent for a house and between 44 and 70 percent for a flat. Any secure tenant of a District Council, London Borough Council, County Council or other similar body, non-charitable housing association or other registered social landlord or a housing action trust has the right to buy. Tenants may qualify to buy their own home if they have spent a total of at least two years as a tenant of their present landlord, with another right to buy landlord, with a qualifying public body or in accommodation provided by the armed forces.

Secure tenants of a registered social landlord, such as a housing association, do not have the normal right to buy but may have the "right to acquire". If they used to be a secure tenant but stopped being one because their home was transferred to a housing association, they may have a conserved right to buy.

The Bank of England Working Party took the view that current legislation does enable local authorities to allow tenants to buy their homes with Islamic finance. The Office of the Deputy Prime Minister prepared appropriate guidelines for local authorities in this regard.

4.5.1.2 The right to acquire

The Right to Acquire is a scheme introduced by the Housing Act 1996 giving eligible tenants of registered social landlords (formerly known as housing associations) the legal right to purchase the dwelling they currently rent with assistance discount ranging from £9,000 to £16,000 depending on the area in which the property is located. The right applies to properties publicly funded after 1 April 1997 for tenants with over two years as a public tenant before 18 January 2005. This was extended to five years for new tenants from 18 January 2005 by the Housing Act 2004 (Housing Cooperation, 2006).

4.5.1.3 Rent to mortgage

Rent to Mortgage facilities assist those who want to buy their home but do not have the funds to pay for it outright. Rent to Mortgage permits tenants to buy their home on a mortgage with repayments nearly equal to their rent. Initially they pay a lump sum which is less than the Right to Buy price. Tenants can take out a mortgage from a building society or bank and the repayment of the mortgage will not be more than the rent now paid each month. If they sell the property in the future they pay the landlord's part of what it is worth at that time. Under this scheme, the landlord - the council or housing association - keeps a share of the property. The landlord’s share is a percentage of the value of the property. Landlords first work out the discount as if the tenant was going to buy outright. Then they work out the Right-to-Buy price for the property. But when the tenant buys on Rent to Mortgage terms, they do not pay the full price at once. First they make an initial payment linked to the amount of rent, and then they pay the rest of the purchase price later. The discounts on the initial payment and on any later payments are at different rates (Communities Scotland, 2006).

4.5.1.4 Home buy

This scheme was first introduced in England in 1999 to replace the Tenants' Incentive Scheme (TIS) and the Housing Corporation-funded Do-It-Yourself-Shared-Ownership Scheme (DIYSO). This scheme enables social housing tenants and others in priority need on the waiting list to buy a home on the open market utilizing an interest-free equity loan equal to 25 percent of the purchase price on offer to them. The objective of this scheme is to release existing social lettings which can then be re-let to people in need of housing in areas where there is a shortage of social housing. Tenants can buy the house of their choice. They pay 75 percent of the market value and receive a loan for the balance, paying back 25 percent of the property value if and when they decide to sell (Housing Cooperation, 2006).

4.5.1.5 Cash incentive scheme *(CIS)*

This scheme is a grant which facilitates buying a property from the private sector. Tenants have no mandatory right to this grant; it is a matter for the local authority to decide. The size of grant payable is set by local authorities, but must be within parameters set by the Government - up to 80 percent of the average Right-to-Buy discount for London, the South East and Eastern regions and £10,000 elsewhere. All grants must be means-tested (Communities and Local Government, 2006).
The objective of the Cash Incentive Scheme is to free up social housing accommodation for letting to those in housing need whilst encouraging owner-occupation especially in areas where there is a shortage of social housing.

4.5.1.6 Voluntary purchase scheme

Tenants of housing associations built before April 1997 who do not qualify for the Right to Acquire may be able to apply to buy the home they rent at a discount. The tenants have no mandatory right to this scheme as it is up to landlords to decide whether to take part in the scheme.

4.5.1.7 Conventional shared ownership

This scheme enables housing associations or any Registered Social Landlord (RSL) to build new or acquire existing houses and refurbish them for sale on Shared Ownership terms. The customer buys a share - usually between 25 and 75 percent - and pays rent on the remainder, the remaining share being purchased over time or on subsequent sale of the property. This is targeted to help those in housing need who would otherwise be unable to buy a property outright.

In spite of the Government's wide-ranging homeownership initiatives, Muslim households who might qualify for such assistance and wish to participate through Islamic mortgages would be disqualified from buying their homes utilizing these initiatives because of the required "third party" involvement by the financier in the purchase process. The relevant legislation covering these schemes (e.g. Housing Acts 1985 and 1996) does not allow disposal to a third party. This eliminates the discount benefits for potential Islamic mortgage customers.

To enable Muslim households and Islamic mortgage customers to utilize the Low Cost Home Ownership initiatives, and to qualify the financier to participate as a third party in the ownership, wholly or partially, the Housing, Planning and Regeneration Division within the Office of the Deputy Prime Minster needs to amend the regulation and legislation or maybe introduce a specific initiative for this purpose.

4.5.2 Stamp Duty Land Tax (SDLT) (successor to stamp duty)

In the UK, Stamp Duty is payable on conveyances and land transfers where the consideration is in excess of £60,000. Both the *Ijarah* and *Murabahah* methods of finance therefore give rise to the payment of additional sums of Stamp Duty not normally associated with 'conventional' mortgage finance. This is because in Islamic methods of financing, the asset (the house) must be purchased and sold by the financier in order to create the finance and the profit for the financier. The sale transactions according to *Shari'a* must be genuine and must give rise to an actual change of ownership.

Until the end of 2003 Stamp Duty was payable double if not three times on Islamic mortgage products. Under *Ijarah* Stamp Duty was paid once when the bank completed its purchase and again on the sale to the customer and possibly also on the *Ijarah* lease. The *Ijarah* charge for Stamp Duty was particularly heavy on a re-finance. There was no Stamp Duty on the typical re-financing of a conventional mortgage.

In *Murabahah*, whilst the sale of the property from the bank to the customer is sometimes by way of sub-sale to minimize the liability to Stamp Duty, the customer still paid stamp duty on the higher price agreed to be paid to the bank. The higher price under *Murabahah* could push the customer into the next Stamp Duty band.

Nonetheless, the Finance Act, 2003 has, to a great extent dealt, with the problem of double/multiple SDLT payments on Islamic mortgage products. The Government's aim is to put Islamic mortgage products on a level playing field with conventional mortgage products. Section 72 of the Finance Act, 2003 relates to *Ijarah* and Section 73 to *Murabahah.*

The relief was only available where land was leased or resold to an individual and the financial institution had to be a bank or building society or a subsidiary of either as defined. Hence, whilst *Ijarah* and *Murabahah* mortgages were available for use by companies, the SDLT relaxation did not apply to company acquisitions. The SDLT provisions were extended in 2005 to equity sharing arrangements, and in 2006 to companies (HM Treasury, 2008).

4.5.3 Regulatory Capital Weighting

There was concern under Basel 1 as *Murabahah*-based home finance products were considered to have the same risk as conventional mortgages, risk-weighted at 50 percent. However, *Ijarah*-based products were risk-weighted at 100 percent. This is essentially because the transaction is equivalent to a lease and leases are weighted at 100 percent. This assumes that the house remains the property of the bank throughout the term of the transaction and is treated as a fixed asset on its balance sheet. In other words the Islamic mortgage provider has to set aside the full amount of the property to cover the full value of the house, in case the buyer cannot afford to pay the rent, whereas a conventional mortgage has a risk weighting of only 50 percent (Tran, 2002). . Because of 100 percent weighting Islamic mortgage pricing was significantly higher than the conventional mortgage rate. The definition of capital and the risk weight assets in Islamic banking does not fit with the Basel formula.

The Basel Committee develops general principles that can be applied to a wide range of banks. It is up to national authorities to determine how to apply these principles to local financial institutions.

Basel II, due to its wider range of options, might be easier to apply to Islamic banks than Basel I. The Basel Committee does not have the necessary expertise to determine how best to apply Basel II to *Shari'a*-compliant banks. Hence, more flexible treatment has been given under the EU Capital Requirements Directive, and the new Accord, Basel II; the risk weights of all three products are the same in the UK, set at 35 percent, under the standardized approach (Anile, *el.al* 2007).

4.5.4 Social Security Support

Government support in case of financial hardship is often available under a conventional mortgage product. The payment of income support for mortgage interest (ISMI) is rooted in a scheme which looks specifically at the interest charged on a mortgage.

Benefit assistance is based on calculating the interest due on a person's capital balance outstanding when they make a claim for benefit. For administrative ease the Department for Work and Pensions (DWP) uses a standard interest rate based on the average building society interest rates published monthly in 'Financial Statistics', an official publication of the Office for National Statistics.

The legislation relating to housing cost payments includes Income Support

(General) Regulations 1987/1967 Schedule 3; Jobseekers' Allowance Regulations

1996/207 Schedule 2, Social Security (Claims and Payments) Regulations

1987/1968 Schedule 9A and Regulation 34A and Social Security Administration Act 1992 Section 15A (Jeffrey Green Russell, 2004).

Consequently the DWP, through its Financial Support Change team, has indicated that, neither *Ijarah* nor *Murabahah* would appear to qualify the claimant for support in the same way as a standard interest-bearing mortgage. As Islamic mortgages do not involve interest payments, the ISMI regulations will need to be revisited to ensure that these mortgages can be sustained through benefit payments in the event of financial hardship.

Nonetheless, the Office of the Deputy Prime Minister is working with the Department of Work and Pensions in consultation with the Council of Mortgage Lenders (CML) to facilitate legislative amendment to provide such support. With many banks currently providing Islamic mortgages, it should be possible to assess the average mark-up on each loan transaction. The provision of financial support under Islamic mortgages requires changes in the relevant legislation or new policy orders to facilitate default support payments by the Department for Work and Pensions.

Muslims may well not hold conventional mortgage support products, such as sickness and unemployment protection and life assurance as these products may not be *Shari'a* compliant.

4.5.5 Separate Legal Representation

With a conventional mortgage loan, the bank and the customer usually instruct a single solicitor to act for them both, subject to provisions of Rule 6 of the Law Society's Practice Rules. In the case of Islamic mortgages the appointment of two sets of solicitors would be required to ensure the customer receives independent legal advice on the nature and content of the contracts, thus making the product more expensive. The problem with Islamic mortgages is that the bank effectively becomes the vendor of the property to the purchaser (borrower), thus immediately giving a *prima facie* conflict of interest.

Rule 6 is a Practice Rule, it is down to a solicitor's own judgement to decide whether he is within Rule 6 or not. Nonetheless, the form of the transaction would appear to give an obvious conflict of interest and it would in such circumstances be debatable whether the bank could rely upon the solicitor’s indemnity policy when it knew that the solicitor might be acting in breach of the Practice Rules.

The Bank of England Working Party discussed this issue with the Law Society as to whether or not Rule 6 could be changed to facilitate single legal representation. The law society is considering the matter, and this may involve providing solicitors who are not familiar with Islamic mortgages with appropriate guidelines. It may also require changes to the documentation of transactions such as the form of the Certificate of Title (George, 2003).

4.5.6 Enforceability of Contracts

Islamic mortgage contracts are governed by English law, therefore the structure of the documentation is invariably in accordance with the law in England and Wales. Nonetheless, substantive provisions in contracts are carefully drafted to comply with interpretation of *Shari’a* Law.

Banks are very concerned as to the enforceability of the rights and obligations granted and imposed by their documentation, particularly if a default occurs. Courts should enforce the contract using normal contractual principles if disputes arise.

The English courts are exclusively concerned with the contractual documentation. Where both parties have signed an agreement, believed to be *shari’a* compliant by their own *shari’a* boards, they cannot appeal to another potentially conflicting *fatwa* issued by scholars who were not party to the agreement. In the court case between the Shamil Bank of Bahrain and Beximco Pharmaceuticals of Bangladesh over the failure of Beximco to make a payment under a *Murabahah* agreement, the case was taken to the High Court in England as the agreement was signed under English law. Norton Rose acted on behalf of Shamil Bank, and the High Court judged in its favour. Beximco subsequently appealed, but the Court of Appeal upheld the judgement made by the High Court in 2004, with Beximco ordered to make the payments and cover all legal costs (Lovells, 2004).

The ownership of the property by the bank also has implications for the bank when endeavouring to deal with customers in default, as the provisions of the Landlord & Tenant Act 1985 (as amended) could apply to the bank as landlord of the premises. This could have a cost implication when dealing with issues such as maintenance and might also lead to different interpretations in court over the ability of a "lender landlord" to take property into possession with a sitting tenant. This could change the nature of Islamic mortgages into ongoing management responsibilities and unclear secure possession rights.

The recommendation of the Bank of England Working Party regarding this issue is that suitable specialist legal opinion should be required to clarify potential liability in utilising Islamic mortgage models as pertaining to the Landlord and Tenant Act. This information should be sought from the Department for Transport, Local Government and the Regions (DTLR) and the Housing Department of the Welsh Office. The Government could consider amendments to the relevant statutes and legislation to prevent any inappropriate obligations outside the spirit of Islamic mortgages.

4.5.7 Insurance

Conventional insurance is considered not to be *Shari'a* compliant for three main reasons:

1) It violates the prohibition on *gharar* (uncertainty).
2) It amounts to *maysir* (gambling).
3) Insurers' underlying funding activities are *riba*-(interest) based.

Banks offering Islamic financial products may not generally insist on customers having life insurance or mortgage protection although they will insist on property insurance.

With *Ijarah* the bank owns and usually insures the property itself, whereas with *Murabahah* the customer usually asks the bank to insure via its block policy.

There are limited *Takaful* policies in the market. HSBC *Amanah Takaful* and *Salaam* Insurance Company are the only ones known in the market however it is hoped that in the future a range of acceptable *Takaful* policies will become available.

Takaful is a *Shari'a*-compliant form of insurance based on the principle of mutuality. The growth of *Takaful* products in the UK could help to develop the Islamic mortgage market. As with conventional finance firms Islamic firms would then be able to offer a combined package to prospective homebuyers.

4.6 FUTURE CHALLENGES AND ISSUES

It is clear that much more work is needed in the near future for the development of the Islamic mortgage market in the UK and to remove barriers to growth in areas with the likes of standardization, awareness and skills (HM Treasury, 2008). It is a duty of the Islamic finance industry to take these issues forward.

4.6.1 Standardization

The lack of standardization for Islamic mortgage products is likely to increase their cost and reduce their competitiveness in relation to conventional mortgages. The lack of standard practices in any industry can be a barrier to development. Hence, the Islamic finance industry has to address the challenges of standardization for Islamic mortgage products within the framework of the *Shari'a.* Better standardization of Islamic mortgage products will bring many benefits to the market. It will reduce the transaction cost thereby enabling banks to offer affordable prices to the consumer. It will also improve the standard of documentation, mitigate the risks of the legal challenge and reduce the workload for the *Shari'a* scholars, of which there is a shortage. Standardization would increase confidence in Islamic mortgage products, provide confidence in Islamic mortgage providers and provide extra information which would make the decision-making process easier for customers.

There has been some good but limited progress made towards standardization by international Islamic standard setters such as the Accounting and Auditing

Organization for Islamic Financial Institutions (AAOIFI), Islamic Financial Services Board (IFSB) and the International Islamic Financial Market (IIFM). Further progress is required to create a set of robust and accessible term-sheets for the main Islamic products.

In the UK many of the preferred forms of documentation for Islamic mortgages have been arranged by individual banks themselves, which increases the costs to that firm of bringing a product to market. This can result in a certain degree of commercial pressure to protect this work. Nonetheless, for the sake of practicality greater standardization is likely to occur alongside further growth in the size of the industry.

4.6.2 Awareness

For Islamic finance to expand, it is very important that more consumers and investors are made aware of the products available and understand them. In addition to that the Islamic finance sector needs to give consumers confidence about the authenticity of products and the manner in which they are regulated.

Recent progress has been made in this matter by individual banks' marketing materials, seminars and conferences, together with the establishment of the Islamic Finance Council in Scotland. This is an industry-led organization which aims to promote Islamic finance. There is also a proposal to create an Islamic Finance Transparency Standard by the Muslim Council of Britain (MCB), in association with the Islamic Finance Council and the Utrujj Foundation. The proposed standards seek to give consumers increased confidence in the *Shari'a*-authenticity of Islamic finance retail products.

HM Treasury has agreed with the Home Office and the Department for Communities and Local Government (DCLG) to explore the scope for using their contacts and distribution channels to circulate information on Islamic finance to ensure that it reaches a wider audience of the Muslim community in the UK.

4.6.3 Skills

A stable flow of properly-qualified staff is vital to the survival of any industry. There are extra aspects which impact upon Islamic financial services in particular. First, this is a relatively new sector that requires specialist training which takes time to set up. Second, the industry is underpinned by what is currently a very limited number of *Shari'a* scholars who decide whether firms and products are indeed compliant with *Shari'a* law. Coordination between the Islamic Finance Industry and the educational and training providers of Islamic finance skills is very important for the sectors.

4.7 EVALUATING THE MARKET FOR ISLAMIC HOME FINANCING

The size of the Islamic mortgage market in the UK is estimated at only £500m compared with over £1.1 trillion for the general mortgage market. There are around nine or ten regulated financial institutions, including major high street banks, providing Islamic retail products. However the FSA has received a number of applications to offer Islamic mortgage products by existing providers and more than 50 applications by intermediaries to enter the Islamic mortgage market (Ainely, *et.al*, 2007).

Although the now defunct Al-Baraka International Bank initiated Islamic housing finance in Britain (Wilson, 1999) HSBC became the first large British-based banking chain to offer a range of Islamic mortgage products as part of its global growth strategy, having gained the approval of its *Shari'a* Board and United Kingdom banking regulators. Amanah Home Finance is based on the Diminishing *Musharakah* mode of financing. If the customer already has a traditional interest-based mortgage, the product allows him to refinance his property.

After the Al-Baraka Bank went back to being an investment company it stopped offering housing finance and since 1997 the Ahali United Bank (the successor of United Bank of Kuwait) has offered the *Manzil* home purchase plan, based on *Murabahah* and *Ijarah* mortgages. The latter being the equivalent to a variable rate mortgage, while repayments and the mark-up for the *Murabahah* mortgage were fixed. These products distributed through the network of the West Bromwich Building Society and perceived as expensive. *Shari'a*-compliant mortgages became more competitive in the United Kingdom after the Chancellor of the Exchequer abolished the Double Stamp duties on them in 2003.

Following the Stamp Duty relief, ABC International Bank (Arab Banking Cooperation) and Bristol & West plc, an English subsidiary of the Bank of Ireland with a substantial branch network, including in areas with significant Muslim populations present introduced Alburaq Islamic Home Finance (Smith, 2004). *Alburaq* Home Finance is based on the principles of *Ijarah* and Diminishing *Musharakah*, and was distributed through Lloyds TSB bank chains and the Islamic Bank of Britain (IBB) until recently but now IBB offers its own Islamic mortgage products. The Arab Banking Corporation has a large base of *Shari'a*-compliant deposits, which can be used to finance Islamic mortgages, unlike Lloyds TSB as, although it is one of the largest banks in the United Kingdom with enormous deposits, these are conventional and pay interest, and hence cannot be used to fund *Shari'a* compliant mortgages.

United National Bank (UNB) also offers Islamic mortgages based on *Ijarah* principles. Although United National Bank originated in Pakistan, it is a UK-registered bank that is authorised and regulated by the Financial Services Authority (FSA).

This section will discuss the histories of, HSBC Amanah and the Islamic Bank of Britain (IBB) to compare the products offered by Islamic windows of High Street Banks with those of the stand-alone British Islamic Bank.

Table 4.2 Comparative Analysis between Different Suppliers of Islamic Mortgages in UK

Bank	**Notes**	**Product Offered**	**Maximum FTV**	**Application Fees**	**Maximum Term**	**Income Multipliers**	
						Sole Appli-cant	Joint Applicant
Alburaq	Various products available via Bank of Ireland, Lloyds TSB and others	*Ijarah* & Diminishing *Musharakah*	90%	£ 299	To finish at age of 65 years	4.5 times	4.5 times plus 1 times second or 4 times joint
HSBC Amanah	Only sold in HSBC branches	Dimishing *Musharakah*	90%	£ 275	30 years	Applicants can make one application + maximum of 6 incomes can be taken into account when assessing an application , Salary multipliers not used but affordability calculate using earnings & outgoings	

Continue Table 4.2 comparative Analysis between different Suppliers of Islamic Mortgages in UK

Bank	Notes	Product Offered	Maxi mum FTV	Applica-tion Fees	Maxi mum Term	Income Multipliers	
						Sole Appli-cant	Joint Applicant
Islamic Bank of Britain	8 Branches (4 in London)	*Ijarah* & Diminishing Musharakah	80%	£ 299	30 years	Income from up to 4 applicants can considered	
Ahli United Bank	1 Branch-2product options avilable	*Murabahah*	73%	0.75% of finance amount	15 years	2.5 times	3 times higher + time 2nd or 2 times combined
		Ijarah	73%	0.75% of finance amount	25 years	2.5 times – 3 times (depending on product)	3 times higher +1 times 2nd or 2.5 times comined
United National	5 Branches (1 in Scotland)	*Ijarah* & Diminishing Musharakah	80%	Not avilable	25 years	3 times	3 times higher + 1 or 2.5 times combined

Source: Mortgage Gazette, 2008

4.7.1 HSBC *Amanah* Finance

HSBC *Amanah* was founded in 1998 when selling to ethnic minorities was a niche market with little investment from large national and international banks (Shanmuganathan, 2004). They recognized the market potential of the global Muslim community which was relatively under-served. HSBC had enormous experience in developing a range of Islamic products and services in the Middle East, Malaysia, Indonesia and the United State.

In July 2003 HSBC became the first UK high street bank to offer an affordable *Shari'a*-compliant mortgage, initially offered in Bradford, Cardiff, Birmingham and London branches, and now in more than 84 branches. The launch of its Islamic finance products was welcome news for many thousands of Muslims. Their mortgages were seen by some as more expensive, but the terms have become more favourable as they have sought to increase their market share. Also, when HSBC offered Islamic mortgages in the high street it shifted its status from a niche product and gave it mainstream credibility.

Iqbal Khan the then head of the Amanah Finance states that his company set up cross-border teams which encouraged sharing knowledge to achieve integration with other Muslim markets, for example Saudi Arabia which is a homogeneous market and Malaysia which has diversity, cited by (Shanmuganathan, 2004).

Furthermore, he argues that the UK market was recognized by HSBC Amanah as an important market in which to establish its credibility and visibility, as its success would impact on Muslim minorities living elsewhere. As a result HSBC invested heavily in training hundreds of managers who were involved with the scheme to educate them about Islamic mortgage products, Muslims' lifestyle and cultural values (cited by Shanmuganathan, 2004).

Having initially operated in wholesale Islamic finance, Amanah finance already had a global *Shari'a* advisory board consisting of eight scholars from the Gulf countries, Malaysia and Pakistan which regularly reviewed its products and transactions. In addition to the central *Shari'a* committee the operation in the United Kingdom was supervised by a regional *Shari'a* committee consisting of three scholars, none of them British Muslims.

Amanah home finance is based on the Diminishing *Musharakah* method of financing so HSBC buys the property jointly with the customer. Typical first time buyer financing is 90 percent the bank's share (90% LTV) and 10 percent the customer's share (10% deposit). The property will be held by HSBC trust company as a third party during the financing term, typically 25 years. The rent rate is linked to LIBOR, which is reviewed quarterly every year and will not be more than 2.5 percent above the Bank of England Base Rate. The customer can make a lump-sum payment of a minimum of £5,000 to increase his share in the property (HSBC, 2009). The monthly repayment consists of three elements; contribution towards the purchase price to increase the customer's shares in the property, rent for the use of the bank's share in the property plus any other charges if applicable.

The bank charges an application fee and a valuation fee which are non-refundable and building insurance is a mandatory requirement and must be paid by the customer. The bank offers an alternative *Shari'a* compliant insurance (Home *Takaful*) to cover buildings, contents and personal possessions. To qualify the property should be freehold or leasehold of at least 50 years (HSBC, 2009).

4.7.2 Islamic Bank of Britain

The Islamic Bank of Britain (IBB) was granted full banking license by the UK regulator in August 2004, two years after it lodged an application, with the support of leading Islamic banks and financial houses in the Gulf, in 2002. The first retail branch was opened in the Edgware Road in London the following month. The bank's head office and operational centre is located in Birmingham, the second largest city in the United Kingdom, which has a major concentration of the country's Muslim population (Wilson 2005). The opening of the first branch of the Islamic Bank of Britain (IBB) attracted much media attention and was well received by Muslims wishing to extend the choice of financial product available to them, tailored to their needs and compliant with their faith. The bank now has eight branches in London, Birmingham, Manchester and Leicester. According to recent report, the IBB had over 50,000 accounts and some 42,000 customers (IBB annual report, 2006).

The Bank launched Islamic home finance in 2005, teaming up with Alburaq and Bristol & West Building Society. It implements the Diminishing *Musharakah* mode of financing over a 25-year term, contributing up to 90% of the home purchase price.

The IBB decided to distribute and fund its own Islamic mortgage product, the Home Purchase Plan, from its own funds and its customers' deposits which were managed purely according to the *Shari'a* and on an ethical basis (Choudhury, 2009). The Home Purchase Plan is approved by the IBB's *Shari'a* supervisory committee, which consists of three scholars, one of whom is a UK resident.

The Islamic Bank of Britain's *Shari'a*-compliant Home Purchase Plan is based on the Islamic financing principles of *Ijarah* (leasing) and Diminishing *Musharakah* (partnership). The bank and the customer will have joint ownership of the property as explained earlier. The term is up to 30 years and the rent rate varies according to the Finance–to-Value ratio, which will be reviewed twice a year and will not be more than 3.5 percent above the Bank of England Base Rate (IBB, 2009). Income from up to four people from the same household can be taken into account, but customers' income and expenditure will be assessed.

IBB focuses on brand and products/services. It has expanded its portfolio of products considerably and has put a lot of effort into promoting the IBB brand as a fully fledged British Islamic bank through direct and indirect marketing channels. It is trying to differentiate itself from other players (Choudhury, 2007).

The Islamic financial market in the UK was culturally diverse, there was a lack of market intelligence data and there was competition from mainstream players. Hence, it was not easy to establish a single marketing strategy. In fact, word of mouth proved to be the most powerful means of attracting new customers.

IBB is a new bank and is fairly small compared with other UK retail banks. This has some advantages, for example:

1) It has a simpler organisational structure;

2) There is the opportunity to gain huge rewards in the long run by exploiting the pioneering role;

3) It is easier to implement staff reward schemes and to focus on the customers when building products and services;

4) It offers competitive pricing and simple terms and conditions for customers.

There are also disadvantages of being a small bank. For example:

1) Huge investment is required

2) There is lack of awareness about the brand and high marketing costs to promote it.

3) There is a need to avoid copying conventional banking products and techniques for fear of diminishing the value of the brand

4) It takes time to become profitable

5) There is a risk of failure of the business model.

4.8 THE POLITICAL ECONOMY OF THE ISLAMIC MORTGAGE

The Government has been very supportive towards Islamic mortgages and Islamic finance in general for its own political agenda. Although it has refused to extend the law against racial discrimination in employment, housing, and education to include religious discrimination, a key concern for Muslims (Islamic Human Rights Commission 1998), it has been fairly open to accommodating the cultural and religious needs of Muslims (Spencer, 2006).

At the domestic level demand for Islamic financial products is growing fast, maybe due in part to the apparent growth in religious awareness among many British Muslims in recent years. In the meantime, the Government, concerned with issues of social inclusion and integration, is actively encouraging banks to offer *Shari'a*-compliant financial products.

The United Kingdom has always been a main trading associate of the Muslim world. Trade volumes increased significantly with the Gulf Cooperation Council (GCC) countries in the 1970s following the oil-driven economic boom. Surplus funds from these countries and the rest of the Muslim world found their way into safe and stable environments in the UK to be managed by London-based banks.

In a speech to the conference, which was organised by the Muslim Council of Britain (MCB) in 2006, the then Chancellor Gordon Brown drew an explicit link between 'financial exclusion' and political/religious extremism, and called for the UK to become the international centre for Islamic finance. He said the UK was "well placed" to become a gateway for Islamic trade and finance (Wilson, 2006).

To achieve these political agenda the Government's approach to Islamic finance was characterized by three principles as stated by Ian Pearson the Economic Secretary to the Treasury: First, fairness - we must make every effort to create a level playing field between Islamic and conventional finance. Second, collaboration - development can be delivered most efficiently when it engages industry, community groups and the Authorities working together to achieve shared objectives. Third, commitment - whenever there is a role for Government to play, it will continue to do so (HM Treasury, 2008).

The Financial Services Authority (FSA) and the Bank of England have effectively supported Islamic mortgages and Islamic finance in general over the last ten years. The Bank of England together with the Treasury, representatives from Islamic finance industry and the Muslim community established a working group in the year 2000 to investigate the obstacles facing the industry. This led to legislation being introduced by the Treasury to enable the development of Islamic mortgages in the UK.

The Treasury, Revenue & Customs and the FSA abolished the double Stamp Duty for Islamic mortgages in 2003 and introduced many changes to the tax and regulatory systems to enable British firms to offer Islamic mortgages and other Islamic financial products.

In 2004 The FSA officially recognized Islamic finance by authorizing the Islamic Bank of Britain as a stand-alone Islamic retail bank and followed this by authorizing other investment banks and insurance companies, which are currently the only Islamic financial institutions in Europe. In the same year regulations were also extended to cover Home Purchase Plans (HPPs) a type of *Shari'a*-compliant mortgage (Diminishing *Musharakah*). This will provide fair competition for the HPPs in the mortgage market and the consumers of the Islamic mortgages will have the same level of protection and access to the compensation scheme as conventional mortgage consumers.

UK Trade & Investment (UKTI) started working actively in 2007 to promote London as a world hub of Islamic finance by setting up a separate group of practitioners, representatives from the Treasury and UKTI to produce a promotion strategy and to gauge both the implementation of the strategy and market changes.

The Treasury established an Islamic Finance Experts' Group (IFEG) in 2007 from leading experts in finance, legal and advisory firms, Government agencies and Muslim community groups. The IFEG provided advice to the Government on how best to support the development of Islamic finance in the UK.

4.9 CONCLUSION

There is a very good prospect for Islamic mortgages in the United Kingdom, providing that the demand is very well assessed and investigated and appropriate marketing strategies are carefully adopted. So far the emphasis has been on providing Islamic mortgages to Muslims living in England only, while there is a sizable Muslim population living in Scotland and Wales who are well settled and less mobile. The future of Islamic housing finance very much pivots on extending the current structure of Islamic mortgages for the average Muslims living in social housing who are relatively less well off compared to the general population. The Office of the Deputy Prime Minister integrated Islamic mortgages into the Right to Buy Scheme. However, for Islamic mortgage providers to assist the average Muslims in attaining home ownership utilizing public sector housing schemes a great deal of work needs to be done in this regard.

The recent favourable regulatory and tax changes by the Government for Islamic mortgages have attracted more banks to offer Islamic mortgages products. For example, the removal of double Stamp Duty provides a level playing field with conventional products. This has opened the door to new players and increased competition in the Islamic financial market. The regulation of the home purchase plan (*Ijarah* mortgages) became a reality and this increased customer confidence in Islamic mortgage products. The Government could share the responsibility with the banks for raising the awareness of Islamic mortgages among the Muslim Community. The regulation of Islamic mortgages and the authorization of a wholly Islamic retail bank and wholly Islamic investment banks represent recognition from the Government and the Financial Service Authority (FSA) regarding the importance of

Islamic mortgages and the Islamic finance industry in general. Considering this in a larger framework, it is true that British government has developed strategies with the aim of keeping London as an important Islamic banking and finance centre. It is hoped that this will provide further opportunities for Islamic retail banking and financing activities in the UK and also the development of new mortgage products to prevent financial exclusion which is also due to social exclusion.

Chapter 5

RESEARCH METHODOLOGY

5.1 INTRODUCTION

This chapter describes the research procedures for both primary and secondary data collection, especially the survey questionnaire, and considers the advantages and disadvantages of this approach. It also describes the method of data analysis pursued in empirical analysis. The chapter discusses the main issues involved in survey design, data collection and data analysis. Furthermore, it provides an outline of the research methods used in the fieldwork and also presents a description of the study sample and the statistical techniques used to analyse the data.

The term ‘methodology’ refers to the overall approaches and perspectives of the research process and is concerned with issues such as the collection of certain data; the rationale for the collected data; the data collection process and data analysis (Stacey, 1969).

There is a paucity of research on Islamic housing finance in the Islamic finance literature in general and with reference to the United Kingdom market in particular. The few studies that do exist on the topic are mainly concerned with the supply aspect and working mechanisms of the financing models. Hence, this study aims to provide an empirical investigation of Islamic housing finance in the United Kingdom.

The significance of this study stems from the fact that although London is one of the main wholesale transacting centres for Islamic finance there is little in the way of Islamic financial products available to British Muslims. The study hopes to contribute to a better understanding among researchers, practitioners and the regulatory and overseeing agencies regarding both the need and the demand for such services. Furthermore, this study aims to provide an empirical investigation of how the United Kingdom’s financial regulatory policies have affected Islamic finance products in recent years.

It extends the existing literature on Islamic finance and housing finance in two directions. First, it applies methods that are scantly used to analyse the implications of introducing Islamic housing finance products in the United Kingdom. Second, it provides empirical evidence for a country for which little research has been conducted, to understand the nature and dynamics of Islamic housing finance modes. Consequently, there is a need for in–depth analysis of the effect of this practice. The study addresses the issue of Islamic finance practice in the United Kingdom to fill this gap in the literature. In this context, it departs from previous studies by using different techniques of analysis, evaluating the demand aspect (most of the previous studies concentrate on the supply aspect only) and uses fresh data and quantitative assessment of the policy and non- policy factors.

This research may be considered as one of the few pioneering studies in the field of Islamic housing finance in the United Kingdom and elsewhere. The principle aim is to comprehensively investigate Islamic housing finance in the United Kingdom to establish policies to improve its supply and determine the factors that correctly evaluate its demand.

Hence, an empirical study based on the experience of Islamic housing finance in the United Kingdom is presented in this research. The United Kingdom experience has been chosen for the following reasons:

i. the prospects of Islamic housing finance in the United Kingdom is very promising, as a non-discriminatory system of taxation and regulation will encourage more competition in the market for Islamic financial services, reduce prices and margins, and make Islamic products more affordable.

ii. London is one of the main wholesale transacting centres outside the Middle East for the Islamic finance market and has a quarter of a century of experience in Islamic finance. Hence, Western countries can learn a great deal from this experiment.

iii. Islamic housing finance in the UK is of special concern to the researcher, who has lived and worked among the Muslim community in this country for a long time.

5.2 RESEARCH DESIGN

The specific study designs used by researchers can affect the findings that are produced (Stacey, 1969). There are different research designs in social research, and according to Black (1999) research methodologies can be classified into four categories: historical research, descriptive research, experimental research and developmental-action research. What is going on (descriptive research)? Why is it going on (explanatory research)? The basic difference between descriptive and experimental research is that the former include observations that has already occurred, hence a researcher measures things as they are (Burns, 2000).

Stacey (1969) states that social research needs a design or a structure before data collection or analysis can commence. For Stacey the major approaches in social science include exploratory research, descriptive research, explanatory research, and evaluation research. Exploratory research attempts to understand a problem or area of study in a preliminary way. Research designs for exploratory research often rely on direct observation of a limited number of examples of what is to be studied. Although exploratory studies do not and are not intended to provide precise estimates of the prevalence of a problem or to test specific theories, they can be invaluable in mapping domains of study or clarifying the feasibility of specific research strategies and tactics Stacey, 1969).

Descriptive research usually attempts to examine a few well-developed constructs in detail in an effort to estimate the frequency with which certain behaviours or relevant characteristics occur in a given population (Black, 1999). Descriptive research is undertaken with the objective of describing relevant aspects of the phenomenon of interest from an individual, organisational, industrial and other perspective. Data collected through descriptive research can provide valuable information about characteristics of the groups and also about the relationships between the characteristics. There are two basic descriptive research studies: cross sectional and longitudinal. The former measures a population at one point in time, while the latter involves data collection at several periods in time. Besides descriptive research other research designs are exploratory and causal research (Ragin, 1994).

Explanatory research attempts to investigate the causes of particular phenomena, not simply to describe them. Such research carefully tests causal hypotheses. It also rules out rival explanations (Maxim, 1999).

According to Stacey (1969), evaluation research attempts to explore whether a given program is achieving its stated goals. Process evaluation examines whether the program is operating as planned, whereas outcome evaluation assesses whether the program achieves the impact or effects that were planned for it. This research is regarded to be an explanatory research and evaluation research since it attempts to investigate the trend, demand, products, preferences, perceptions, obstacles and prospects of Islamic mortgages in the United Kingdom. It uses a sample survey as it was thought to be the most suitable way to achieve the research objective especially based on the nature of the data required and the purpose for which it was to be used. The study uses a combination of literature studies and a survey investigation approach, which offers the most appropriate and satisfactory methodology in carrying out this study.

Data from an area of East London, which represents the Muslim community, is used to answer the research questions. The principal method used to gather primary data in responding to the research questions is a questionnaire survey of Muslim households in East London. A period of about three months was spent carrying out this fieldwork, and the objectives were three-fold: to collect all possible and available primary information about Muslim households in London, to obtain information about Islamic Mortgage providers; to gather all available related secondary information pertaining to the research work including different types of reports and articles.

The researcher used primary data mainly to suit the nature and purpose of the research which was to elicit respondents' opinions, perceptions and attitudes. The survey approach using a questionnaire is thought to be the most appropriate technique in collecting the intended primary data. Also the investigation of this study is based on secondary data obtained from journals, magazines, homepages reports and books.

5.3 RESEARCH METHOD AND DESIGN

There are two essential methodological approaches in social sciences: qualitative and quantitative. Quantitative research can be interpreted as a research strategy that emphasises quantification in the collection and analysis of data (Black, 1999). By contrast, qualitative research can be interpreted as a research strategy that usually emphasises words rather than quantification in the collection and analysis of the data (Miller, 1983).

In quantitative research, the researcher is ideally an objective observer who neither participates in nor influences what is being studied. In qualitative research, however, it is thought that the researcher can learn the most by participating and/or being immersed in the research situation. These basic underlying assumptions of both methodologies guide and sequence the types of data collection methods employed (Maxim, 1999). While quantitative research readily allows the researcher to establish relationships between variables, it is often weak when it comes to exploring the reasons for those relationships. A qualitative study can be used to help explain the factors underlying the broad relationships that are established (Remenyi, 1998).

For these reasons, we feel that a combination of the literature studies, case studies and a survey investigation approach offers the most appropriate and satisfactory methodology for this study. The approach of using two or more methods in combination is called triangulation. In social science triangulation is defined as the mixing of data or methods so that diverse viewpoints or standpoints cast light upon investigated subject (Creswell, 2003). Ragin (1994) argues that one of the principal aims of triangulation in social sciences seems to be to corroborate one set of findings with another. Triangulation reduces the risk of a researcher's conclusions reflecting only the systematic biases or limitations of a specific method (Black, 1999). Consequently, the researcher has used quantitative and qualitative approaches to analyse the data. In this study quantitative analysis is used to analyse the questionnaire responses, but at the same time qualitative attempt was made to interpret the results. In addition, qualitative and descriptive material provides the contents for the literature. Thus, this study benefits from triangulation.

On the other hand, one of the ways research designs can be classified is by the communication methods used to gather primary source data. There are two alternatives; first, we might observe conditions, events or subjects. Secondly, we might survey or question persons about various topics. Furthermore we wish to utilize both quantitative and qualitative data in our study. This has been necessitated by the fact that for certain issues to be analyzed only quantitative data is available, whereas other concepts have only data of a qualitative nature (Sekaran, 2003). However, we know that each method has strengths and weaknesses. For example, with primary sources, one collects precisely the information one wants. One can usually specify the operational definitions used and can eliminate, or at least monitor and record, the extraneous influences on the data as they are gathered. However, secondary sources also have their merits as they can be found more quickly and more cheaply (Crano, 2002).

Both primary and secondary data were used in the preparation of this study. The primary data was acquired through questionnaire surveys, while the secondary data was obtained from library references (books, articles and magazines), published research, related studies, statistical reports, banks' annual reports, government and Central Bank publications and periodical reports. In short, studies made by others for another purpose, represent secondary data. In this regard it is worth mentioning that data was often available in formats that suit government planning purposes, but do not cover broadly all the information required by this research. This highlights a need for reliable databanks within each sector, to provide complete and standardized information. Time series data relating to macroeconomic performance, monetary and financial aggregates and government policies was obtained from official sources including different FSA and CML reports and the economic survey of the Treasury and the Bank of England as well as other publications.

However, it must be noted that the study only focuses on the perceptions of the Muslim households seeking Islamic mortgages in an area of East London. Therefore, it does not include the Islamic mortgage providers' perceptions. In addition the qualitative data will not include any interviews with Islamic mortgage providers' employees.

5.4 RESEARCH INSTRUMENTS

The most popular quantitative technique is the survey, which can be administered by mail, telephone, face to face, or more recently by the internet (Miller, 1983). In order to collect the appropriate and necessary information for achieving the objective of the study, the questionnaire survey technique was used. It is reasonable to believe that a questionnaire is the most convenient and efficient way to obtain the information needed. The written questionnaire is typically more efficient and practical, and it allows for the use of a large sample (Oppenheim, 2000; Gillham, 2000; Barnett, 1991).

5.5 DATA COLLECTION DESIGN AND SURVEY TECHNIQUES

As for the empirical part of this study, the researcher used primary data mainly to suit the nature and purpose of the research which was to elicit respondents' opinions and attitudes. The survey approach using a questionnaire is thought to the most appropriate technique in collecting the intended primary data. It also allows quantitative analysis to be concluded in the testing of inferences and also it has the potential to generalise the findings (Ryan, 2002). A questionnaire is a highly-structured data collection technique in which each respondent is asked the same set of pre-formulated written question, to which respondents record their answers, usually within rather closely defined alternatives (Oppenheim, 2000).

Questionnaires are an inexpensive way of gathering data from a potentially large number of respondents. Often it is the only possible way to reach a number of reviewers large enough to allow statistical analysis of the results. Questionnaires assist the process of collecting data by asking all, or a sample of people to respond to the same questions (Miller, 1983).

The advantages of questionnaires include them being cost effective and easy to administer; they are easy to analyse through computer software packages; they provide access to hard-to-reach respondents; they are simple and quick for the respondent to complete and they preserve confidentiality; and there is no interviewer bias (Gillham, 2000; Dubois, 1992). Disadvantages of questionnaires include: them not being suitable for complex question patterns; data entry is time consuming; there can be errors in completion; and there is poor quality control due to the absence of the interviewer. The questionnaire can be conducted by post to the respondents or personally administrated as in face-to-face interviews and surveys, telephone surveys, self-administered surveys (mail and drop-off surveys) and more recently the internet, *ie* e-mail and the World Wide Web.

The mail survey only requires the researcher to post the questionnaire to the prospective respondents and wait until it is completed and returned. On the other hand, using a drop-off survey, the researcher approaches a prospective respondent, introduces the general purposes of the survey and leaves it with the respondent to complete (Oppenheim, 2000). Essentially, the objective is to gain the prospective respondent's cooperation. Normally, the researcher returns on the same day or the next day to collect the completed questionnaire. In this way a researcher can cover a number of survey locations in a single day with an initial drop-off and later collection (Miller, 1983).

This study mainly adopted the face to face survey and sometimes the drop off questionnaire approach.

5.6 THE ADVANTAGES AND DISADVANTAGES OF THE SELECTED SURVEY TECHNIQUES

A face-to-face questionnaire is better than a postal questionnaire. One of the problems associated with postal questionnaires is that people simply enter replies in the wrong boxes (Black, 1999). Human errors can easily go uncorrected when the respondent is alone (Miller, 1983). Operation of the face-to-face questionnaire as a suitable instrument for data collection is supported by the literature. For example, conventional evaluations of business support measures rely on a questionnaire survey of recipient firms in order to establish the direct benefits of policy (Black, 1999).

Hence, a face-to-face questionnaire has several advantages, and some disadvantages. In a face-to-face questionnaire, the researcher has the chance to explain the questions to avoid any misunderstanding and people may be more co-operative when all they have to do is talk. In this situation, the researcher and the respondent may feel more relaxed and the respondent may give more reliable information. In addition, a face-to-face questionnaire minimises missing answers and errors. Moreover, it helps to create an atmosphere of confidence between the parties, namely the researcher and the respondents. In addition, it gives the respondent the feeling that there is some interest being shown in them and their role in society (Black, 1999).

The main disadvantage of the face-to-face questionnaire is that with a wide geographical area and a large sample it can be very difficult to achieve good coverage (Dubois, 1992). This problem was solved in our study because we only concentrated on East London. Another disadvantage of this method is the high cost of training interviewers to minimize interviewer bias, for example differences in questioning methods and interpretation of responses. The objective of this study survey was to collect all possible and available primary information by pursuing the respondents to reveal their attitude towards Islamic mortgages based on their pre-interview awareness of Islamic mortgages. To achieve this objective the researcher avoided any direct questions on the religious affiliation of the respondents. The survey was conducted in the area with the highest Muslim population in the country and if, during the interview, a person was found to be non-Muslim the questionnaire was discarded. Another drawback is that respondents might feel uneasy about the anonymity of their responses when the questionnaire is conducted face-to-face. This problem was solved in this study by assuring the respondents that the data would only be used in aggregate to statistically compare different types of services provided and that their responses would remain confidential.

The drop off technique was used for three reasons (Brannen, 1992): First, it is suitable for collecting data about attitudes and opinions as suggested above, and has been extensively employed in many similar studies. Secondly, the self-administered approach is appropriate for covering a large number of respondent groups and at diverse geographical locations in East London as intended in this study. Finally, by using the self-administered approach the researcher was able to overcome several constraints of this study such as the unavailability and inaccessibility of information required to construct a sampling.

5.7 THE SURVEY STRUCTURE AND CONTENT

5.7.1 The Survey Structure

The researcher opted to design closed-ended rather than open-ended questions in the questionnaire design. The advantage of closed-ended questions is that they can be administered with little direct confrontation and the respondent can perform with greater reliability the task of answering the questions when response alternatives are given (Oppenheim, 2000). Closed-ended questions are also easier and relatively quicker to answer. In fact, they require no writing and quantification, since they are straightforward (Miller, 1983).

The kind of questions used and the construction of a questionnaire vary according to the type of information required. Thus, the questions have been phrased carefully in order to be certain that the desired information is secured. Many steps are involved in the construction of a questionnaire. The researcher begins with the research objectives, and then goes through the process of preparing the questions.

In this way the researcher can use appropriate statistical tests in evaluating the empirical findings of the study so as to encourage easy responses from the various respondent groups under study. It also enables uniformity and consistency throughout the data collection process.

The questions themselves are mostly ranking or multiple choice, in order to cover a wide range of possible responses. Answering these questions should not only be much quicker, but should evoke a higher response rate. Some of the other questions were open-ended, so that the respondents were not restricted in their answers or comments. It was considered that the questionnaire may be too long, but the risk of facing a lack of information made this inevitable.

The questionnaire was prepared in English. A total of 350 questionnaires were distributed to Muslim households in East London and only 250 were returned to the researcher, which is sufficient for statistical reliability. Householders were contacted in their homes, offices, mosques, community centres and on the street.

5.7.2 Questionnaire Content

The questionnaire was fairly comprehensive, consisting of 47 questions, covering a wide range of issues aiming to gauge respondents' attitudes towards Islamic mortgages. The questionnaire covered six pages and was divided into four sections (see Appendix for a sample of the questionnaire used in this study).

The objectives of the questionnaire were briefly stated in the questionnaire's covering letter, which also stated the confidentiality of all information provided and that such information was to be used for the purpose of the study only. To encourage target groups to participate and respond to the questionnaire the anonymity of respondents must be guaranteed by not asking them to identify themselves or their organisations.

The questionnaire contains four sections; the first section was designed to gather information about the respondents' personal profile including gender, age, marital status, educational qualification, managerial experience. The second part consists of questions about their financial situation. Home ownership and affordability is the title of the third section, in which the respondents had to give their opinions and perceptions about home ownership, determine what factors might encourage or discourage them to be a home owners and also to obtain a general idea about their ability to afford to be home owners. In the last section the questions were devoted to the Islamic mortgage. The respondents were given the chance to give any further comments. The questionnaire ended with a statement expressing that the identity of respondents would be treated in strict confidence and not revealed in the theses or any other publication. If a respondent wished to receive the conclusions of the study, however, they would have to supply their contact information.

5.8 SAMPLE DESIGN AND SAMPLING PROCESS

5.8.1 Population and Sampling Frame

A population is a group of persons, institutions, or events, which are the aggregate of all cases that conform to some designated set of specifications (Gillham, 2000). For instance, the term Muslim household used in this study defines a population consisting of all the Muslim households in East London.

The sampling frame is the list or other record of the population from which the sampling units are drawn. Note that not all members of the population of interest are included in the sampling frame. The sampling frame may be based on telephone directories, city directories, or membership lists of private organisations (Barnett, 1991).

Currently, there are 350,000 Muslim households in the UK according to the MCB and a total population of 1.8 million. While London consists of 607,000 Muslims, in East London - Tower Hamlets alone in which the questionnaire took place - there are 71,000 Muslims.

5.8.2 Size of the Sample

Different authors tend to give different guidelines concerning the minimum size of the sample. Rao (2000) states that a sample of more than 30 is thought to be a good estimate of the population. For this study the sample was much larger than 30. Sample sizes larger than 30 cases and smaller than 500 cases are considered suitable for most research. In this study, the sample is 250 cases. In addition, the larger the sample the more accurate the research, while increasing the sample size decreases the width of the confidence interval at a given confidence level (Jessen, 1978).

In order to minimize potential random error in the sample selection process, it was deemed proper to consider the appropriate sampling technique and the sample for the study (Population Centre, 1982). The method of data collection for this study was originally planned on the assumption that the ideal sampling frame as identified in any research methodology literature would be accessible to the researcher. In the case of this study the ideal sampling frame would be the lists of all Muslim households in East London. The availability of such lists would enable the researcher to sample the population through the use of a table of random numbers which could ensure random sampling and prevent bias. However, developing such an ideal sampling frame would have been almost impossible as time and resources were the main constraints to this study. Furthermore, to gain access to information on respondents' profiles was another critical issue.

To overcome some if not all of the difficulties mentioned above, the official statistics and general figures obtained from the UK census taken in 2001and the statistical data base for the MCB were the sources of reference when determining the sampling strategy. Another strategy adopted was to distribute the questionnaire randomly to Muslim households in East London using face-to-face and drop-off self administered methodology.

The Muslim population in London is one of the largest of all major European cities. After Christianity, Islam is the second largest religion practiced in London; according to the 2001 census, 607,000 people in the city identified themselves as Muslims, or 8.5 percent of the general population of approximately 7,172,000. The London Borough of Tower Hamlets in East London is home to the UK's largest Muslim community, accounting for over 36 percent of the population in the 2001 census, compared to eight percent for London as a whole and 2.7 percent nationally. The majority of these Muslims are Bangladeshi, primarily from the Sylheti region (speak Sylheti,) and a few are from other parts of Bangladesh. The rest of the local Muslim population includes Somalis, Pakistanis, North African Arabs and a few White British.

5.9 PRE-TESTING, PILOT VALIDITY AND RELIABILITY

It is regular practice to pre-test the questionnaire with a small sample prior to starting the survey proper as this minimises the problems that may arise when producing the final draft. Each survey questionnaire presents its own problems and difficulties before it reaches the final draft. Questionnaires have to be designed, and tried out, improved and then tried out again, often several times over, until it is certain that they can do the job for which they are intended (Oppenheim, 2000).

Validity is the strength of our conclusions, inferences or propositions. In short, were we right? Validity could be divided into two types: internal validity and external validity. External validity refers to the extent that the results of a study can be generalized, while internal validity refers to the degree to which a study exactly reflects or assesses the specific concept that the researcher is trying to measure. There are several types of internal validity: face validity, content validity, construct validity, predictive validity and concurrent validity (Kalton, 1983). Validity is more important; if a measure has a high validity, it must also have a high reliability. If it has a low validity, it is misnamed and misleading regardless of its reliability (Gillham, 2000). Reliability, on the other hand, is the consistency of the measurement, or the degree to which an instrument measures the same way each time it is used under the same conditions with the same subjects (Miller, 1983).

The real difference between reliability and validity is mostly a matter of definition. Reliability estimates the consistency of measurement, or more simply the degree to which an instrument measures the same way each time it is used in under the same conditions with the same subjects. Validity, on the other hand, involves the degree to which it is measuring what it is supposed to, more simply the accuracy of its measurement. It is my belief that validity is more important than reliability because if an instrument does not accurately measure what it is supposed to, there is no reason to use it even if it measures consistently (reliably) (Gillham, 2000). It has been widely recognized that reliability and validity of the instrument used can be improved by using the pre-test or pilot study.

As in any survey work the quality of the results depend to a great extent on the quality of the primary data collected from the respondents. Working on this premise, the researcher took all necessary measures to ensure that the data collected were of high quality in terms of accuracy and reliability. In order to check the content validity of the questionnaires the researcher contacted some experts in the field of Islamic finance and some academics.

The questionnaire was designed with two goals in mind: relevance and accuracy. A questionnaire is relevant if no unnecessary information is collected. Accuracy means that the information is reliable and valid. So the sequence and wording of the questions were designed in such a way as to promote accurate and informative answers from the respondents. Efforts were made to make the questions as short and clear as possible to avoid ambiguity, confusion, and vagueness. In addition efforts were made to avoid asking questions which were are beyond the respondents' capabilities or knowledge.

The pilot test for this study was conducted between June and August, 2006 through a convenience sampling procedure. At least three drafts were made before the final one. The questionnaire was piloted by distributing 10 drafts to Durham University postgraduate students in the first stage. In the second stage the questionnaire was piloted twice in order to make sure that the questions were easily understood. The first test was made by distributing 20 drafts of the questionnaire to some academics at Durham University as well as some bank staff, who participated in Durham Islamic Finance summer school 2006. The second test was made by sending the questionnaire to some educated Muslim households in Newcastle and London. Amendments were made following these two tests, in order to make the questionnaire clearer. Their comments and opinions provided valuable feedback. Their opinions gave strength to the final questionnaire. The final format was therefore established according to the maximum feasible amount of testing.

The pilot study was undertaken after correcting the initial draft of the questionnaire. This was to ensure that the testing of the questionnaire achieved its intended objective. Thus, once the initial draft of the questionnaire had been designed, each question and the questionnaire as a whole were tested and evaluated. One of the main objectives of pilot testing is to refine the wording, filtering, and ordering, and to control the length of the questionnaire and most importantly to calculate the variables validity and reliability test (Population Centre, 1982).

5.10 RESPONSE RATE

A visit was undertaken to London to collect the main field data. The major survey was conducted between January and March 2007. From a total of 350 questionnaires distributed, 270 were returned, of which 250 were fully completed, thereby yielding a response rate of about 77 percent. This response was considered large enough and sufficient for statistical reliability and generalisation (Population Centre, 1982). This high response rate undoubtedly improved the validity and reliability of the survey since the greater the response the more accurately it estimates parameters in the population sampled (Pallant 2002). Hence, no further attempt was made to increase the sample. The survey covered Muslim households of different ethnic backgrounds living in East London. Details of the number of questionnaires distributed and the response rate are summarised in table 5.1.

It should be noted that some of the questionnaires were eliminated because they contained too many missing items or some contradictions in the answers occurred either by mistake or by misunderstanding of the questions which could have affected the results of the study.

Table 5-1 Sample Breakdown and Response

	Ethnic Origin	Valid Response	Distributed Questionnaire
1	White	12	23
2	Indian	11	20
3	Pakistani	17	29
4	Bangladeshi	81	104
5	Black	42	53
6	Arab	59	71
7	Mixed	8	20
8	Other	20	30
	Total	250	350

5.11 ANALYSING THE DATA

5.11.1 Software for Data Analysis

Once the questionnaires had been collected and the data had been entered into the SPSS software and the data file checked for accuracy, the next step involved formatting the raw data into a form that could be used to conduct analyses and to test the research hypotheses. The researcher calculates the total scale score as an effective procedure which can be used to manipulate data sets (Allison, 2002). This results in a new variable at the end of the data set. If any items had missing data, the overall score would also be missing. The created variable, with its full details, was recorded for a clear guide to the study.

The Statistical Package for Social Sciences (SPSS) is possibly the most widely used computer software for the analysis of quantitative data for social scientists (Norusis, 2004). Using this powerful software all data assembled from the questionnaires' data for this research study were defined and entered by the researcher. Because of the nature of the data and research questions, descriptive statistical methods were used. These methods include frequencies, percentages and means, in order to clarify the differences between the different characteristics and performance.

5.11.2 Descriptive Statistical Technique

Once the data is collected, the first step is to describe it using statistical measures such as the mean and median (central tendency), and standard deviation (variation) (Haberman, 1974). The idea is that for a particular item on the questionnaire, we are computing the mean value that underscores the respondents' behaviour with respect to the stated research question and/or hypothesis.

5.11.3 Other Statistical Technique

Choosing the correct statistical technique to analyse data is a difficult part of the research process. When making this selection, a number of different factors have to be considered, such as the type of question, the type of scale, the nature of the data for each variable and the assumptions that must be met for each of the different statistical techniques. Identifying the statistical techniques used in other related studies should also help in choosing the correct one (Jessen, 1978).

There are a number of steps that can help the researcher to navigate through the decision-making process for the questionnaire. First, what questions does the researcher want to address? Any researcher should write a full list of all the questions he or she would like to have answered in his or her research. Some questions could be asked in a number of different ways. These alternatives can help to cover each of the areas of interest (Ragin, 1994). Second, what is the nature of each variable? Knowing the level of measurement for each variable is very important. Different statistics are required for variables that are categorical and continuous. Variables may be categorical (also referred to as nominal level data), ordinal data (rankings: 1^{st}, 2^{nd}, 3^{rd}), or continuous (also referred to as interval level data) (Jessen, 1978).

While the description of data gives some information and idea about the questionnaire, only testing gives a clear answer regarding a given question. The test generally depends on the nature of data to hand (Leach, 1979). The third step is, therefore, to decide the nature of statistical techniques as to whether a parametric or a non-parametric statistical technique will be used. Testing is critical in statistical analysis. Statistical techniques are classified into two main groups: parametric and non-parametric. Parametric techniques assume that the underlying distribution of scores is normal. In addition, each of the different parametric techniques contains other additional assumptions that must be checked before carrying out the analyses. Only non-parametric statistical techniques are used in this study (Sprent, 2001).

5.11.4 Statistical Tests

5.11.4.1 Chi-square for independence

The chi-square test for independence is used to determine whether two categorical variables are related. It compares the frequency of cases found in the various categories of one variable across the different categories of another variable (Gibbons, 1976). Two categorical variables with two or more categories in each are needed. The lowest expected frequency in any cell should be five or more for the main assumption. In addition, the significant value needs to be .05 or smaller, otherwise the result is not significant (Antonius, 2003).

5.11.4.2 Chi-square goodness-of-fit test

The chi-square goodness-of-fit test, also referred to as the chi square test for a single sample, is a non-parametric test employed in a hypothesis-testing situation involving a single sample with nominal and categorical data (Sheskin, 1997). The chi-square test for goodness of fit tests the hypothesis that the distribution of the population from which nominal data are drawn agrees with a posited distribution. The chi-square goodness-of-fit test compares observed and expected frequencies (counts). This test is basically the sum of the squares of the differences between the observed and expected frequencies, with each squared difference divided by the corresponding expected frequency. Two values are involved, an observed value, which is the frequency of a category from a sample, and the expected frequency, which is calculated based upon the claimed distribution. Goodness-of-fit tests test the conformity of the observed data's empirical distribution function with a posited theoretical distribution function by comparing observed and expected frequency counts (D'Agostino and Stephens, 1986).

The purpose of Chi-square goodness-of-fit tests is to see if the sample comes from the population with the claimed distribution. Another way of looking at it is to ask if the frequency distribution fits a specific pattern. The chi-square goodness-of-fit test has been used to differ between sample characteristics.

5.11.4.3 The t-test

The t-test is probably the most commonly used statistical data analysis procedure for hypothesis testing. There are several kinds of t-tests, but the most common is the "two-sample t-test" also known as the "student's t-test" or the "independent samples t-test".

The two-sample t-test is a simple test used for comparing the means of two samples (or treatments), even if they have different numbers of replicates. In simple terms, the t-test compares the actual difference between two means in relation to the variation in the data (expressed as the standard deviation of the difference between the means) to check whether this represents a real difference between the two populations or just a chance difference in our samples. By using the t-test statistic to determine a p-value we can see how likely it is that we could have gotten these results by chance. By convention, if there is a less than five percent chance of getting the observed differences by chance, we reject the null hypothesis and say we found a statistically significant difference between the two groups (Trochim, 2006).

5.11.4.4 One-way Analysis of Variance (ANOVA)

This is similar to a t-test, but is used with more than two groups to compare their mean scores on a continuous variable. It is called one-way because it measures the impact of only one independent variable on the dependent variable. It compares the variance between the different groups, with the variability within each of the groups. The variance between the groups is given by an F ratio. A large F ratio indicates that there is more variability between the groups. In this case, the null hypothesis that states that the population means are equal can be rejected (Sprent, 2001).

All the above statistics are calculated using SPSS that provides the value of the statistic and the critical value P. In general; the five percent level is widely accepted as a reasonable level of significance.

5.12 DIFFICULTIES AND LIMITATIONS OF THE STUDY

Like any other research project this research has its limitations. They are:

a. The ability of the respondents to comprehend the questions asked. The respondents' comprehension of the questions in the questionnaire could be at various level, whether low or high. There is a limitation in knowing whether the respondent has been diligent enough to ask, if in doubt, via personal email and mobile phone (contact details were given in the introduction of the questionnaire for correspondence purposes or if the respondent had any questions to ask).

b. The diligence of the respondents in answering the questionnaire all the way through honestly and earnestly, instead of simply for the sake of putting down an answer.

c. The data collection method was limited to the survey questionnaire without including other methods, for example focus group and semi-structured interviews.

d. It would have been more beneficial if more respondents were surveyed. However, due to a limitation of the budget and time, this was not possible.

e. This study will be on Islamic housing finance in the United Kingdom only.

f. The measures introduced in this study could be refined and made more robust. This will be the subject of later studies.

In addition to the limitations mentioned above, a number of difficulties were encountered during the course of this research. These include:

a. Getting More Respondents

There was difficulty in getting respondents to fill in the questionnaire. Respondents might have been put off by the questionnaire being rather long and containing personal financial information. It would have been better if more questionnaires were completed but there were time and budget constraints. It was not possible to stay in

London for longer than three months and therefore, it was also impossible to get more respondents. However, it was still pleasing to have 250 of the questionnaires returned.

b. Analysing

There was also difficulty in analysing some of the respondents. Sometimes, there were people who did not fill in the questionnaire properly; for example, instead of noting down the ranking numbers to the answers given, they just ticked the appropriate answers. Or sometimes they skipped some of the questions. The researcher did not notice this mistake when the questionnaires were given back to him so by the time the questionnaires were finally looked at, it was difficult to trace the respondents as they were not asked to give their names for reasons of anonymity.

The results of the survey are generally applicable to the rest of the Muslims in the United Kingdom, based on the fact that the British Muslim community is homogeneous and any segment of the population should be a fairly accurate representation of the Muslim population as a whole in the United Kingdom.

5.13 CONCLUSION

The methodology employed in this thesis aimed to obtain sufficient information to satisfy the basic requirements of the thesis. In the case of the questionnaire used the number of respondents should prove adequate for interpreting the situation. The final questionnaire benefited greatly from the pilot study, which proved invaluable for framing the appropriate questions. The aims and objectives that the survey method was trying to reach were also explained here. The way in which the survey method was administered and how the data was analysed were also discussed. Finally, like any other research project, there were limitations and difficulties encountered throughout, which were also noted in this chapter so as to give a true picture that all was not plain sailing.

Having presented the research methodology in this chapter, the next three chapters will be the empirical chapters. The next chapter, (chapter six), being the first empirical chapter, presents the profile analysis and sample characteristics of the survey and respondents.

Chapter 6

SAMPLE CHARACTERISTICS AND HOMEOWNERSHIP AMONG BRITISH MUSLIMS

6.1 INTRODUCTION

This chapter aims to present the demographic and the work-related characteristics of those Muslim households who responded to the questionnaire conducted as part of this study. It is crucial to know the demographic profile of the respondents, as well as their employment status, income, financial health and their banking commitments. Hence, this chapter will provide personal information about Muslim households in the UK including gender, age, marital status, ethnic origin and qualifications. The questionnaire contains a section on respondents' personal details as diverse biographic, demographic and educational factors were likely to influence the answers to the research questions of this study. This would also enable us specifically to understand the factors which determine the demand for Islamic mortgages in this country. In order to conduct the analysis of the primary data, descriptive statistics were employed in this chapter.

This chapter also aims to study, in detail, homeownership among British Muslims as a pre-requisite to correctly evaluating the demand for Islamic mortgages in the UK. The status of tenure within the Muslim Community has been investigated and different gaps in British Muslims' homeownership have been identified. The lure and aspiration for homeownership among British Muslims has been studied and obstacles and factors which translate this aspiration into actual homeownership are investigated in detail.

The final aim of this chapter is to study two aspects of the purchasing power of Muslim households: their ability to enter the housing market/pay a deposit and their ability to keep up repayments. By covering the above-mentioned issues this chapter will answer the two research questions: What are the challenges and prospects of homeownership within the Muslim community through Islamic Mortgages in the UK? And what factor/s might encourage/discourage home-buying within the Muslim community?

Table 6.1 Demographic Profile

	Valid	Frequency	Percent
Gender	Male	202	80.8
	Female	48	19.2
	Total	250	100.0
Age	25 and under	51	20.4
	26 – 35	80	32.0
	36 – 45	71	28.4
	46 – 55	32	12.8
	56 - 65	15	6.0
	66 and +	1	0.4
	Total	250	100.0
Marital Status	Married	138	55.2
	Single	97	38.8
	Other with children	11	4.4
	Other without children	4	1.6
	Total	250	100.0
Ethnic Origin	White	12	4.8
	Indian	11	4.4
	Pakistani	17	6.8
	Bangladeshi	81	32.4
	Black	42	16.8
	Arab	59	23.6
	Mixed	8	3.2
	Other	20	8.0
Qualification	No formal qualification	19	7.6
	GCSE/ O levels	42	16.8
	A levels	56	22.4
	Professional qualifications (in	24	9.6
	BA or B.Sc.	63	25.2
	MA or PhD	46	18.4
	Total	250	100.0

6.2 DEMOGRAPHIC PROFILE OF THE RESPONDENTS

Table (6.1) above provides the frequencies and percentage distribution of personal characteristics of Muslim households in Eastern London.

6.2.1 Gender

As can be seen from table 6.1 the distribution of males and females is uneven. The females represent only 19.2 percent of the total sample and 80.8 percent of the sample is male. This may be due to the fact that the number of male Muslims in London is greater than that of females. According to the 2001 Census there are 310,477 Muslim men and 296,606 Muslim women in London.

This gender profile may be attributed to migration history where, men with families migrate alone and the rest of the family follow at a later date. The fact that the respondents in this survey are mostly men reflects social factors whereby men deal with money and financial decisions.

6.2.2 Age

As table 6.1 shows, 32.0 percent of the respondents belong to the age group ranging between 26 to 35 years old while the percentage in the 36 to 45 years old group is almost 28.4 percent compared with 20.4 percent for those 25 years old and under and only 0.4 percent for those over 65 years of old .In general, the table indicates that the majority of respondents come from a relatively younger age group. This confirms earlier findings that the Muslim population is younger than the general population with only 3 percent of Muslims being over 65 (Sellick, 2004).

6.2.3 Marital Status

The majority of respondents (55.2 percent) were married compared with 38.8 percent who were single; this confirms the general assumptions that Muslim households are more likely to consist of a married couple with two or more children. The 2001 census showed that 28 percent of Muslim households were married with two or more children compared with 11 percent of the general population. However, six percent of respondents were either divorced or widowed. This reflects the Muslim culture that has a tendency towards early marriage. These findings may be attributed to the importance of marriage in Islam and to Islamic laws, which prohibit sexual relationships outside marriage.

6.2.4 Ethnic Origin

Table 6.1 shows that the majority of respondents were of Bangladeshi origin (32.4 percent) while the second largest group were those from an Arab background (23.6 percent) compared to 16.8 percent of black origin and 6.8 percent, 4.4 percent and 4.8 percent for those of Pakistani, Indian and White origin respectively. Muslims are a diverse population with nearly three-quarters of them describing themselves as Asian - 60 percent are Bangladeshi or Pakistani - but over 10 percent describe themselves as White. When Muslims first began arriving in Britain they were labelled under the Black category, which made it very difficult to understand the demographic profile of the Muslim community at that time. Ethnicity-based data does not give a complete understanding of all communities, especially the Muslim community, a community that transcends racial boundaries. There are particular issues faced by Muslims which are not identified or the true extent to which those issues arise is not properly investigated. For example, the case of the growing number of African Muslims in the UK who have been lost in the overall Afro-Caribbean racial categorisation; these African Muslims have many needs, which are often completely different to their non-Muslim Caribbean counterparts' needs and are more similar to those of Asian and Arab Muslims. As for White Muslims, according to the racial categorisation they do not even exist, since there seems to be a huge misconception that being Muslim requires an element of colour (Sacranie, 2002).

6.2.5 Education and Qualification Level

In general the respondents were well educated. Almost half of them had a university degree and/or postgraduate degree; 25.2 percent held a bachelor degree and 18.4 percent held a postgraduate degree. Those who had O level/GCSE, A level and professionals qualifications represent 17 percent, 22 percent and 10 percent respectively and only less than 8 percent had no formal qualifications. Therefore, it is possible to conclude that the dominant types of households are well educated.

In 2000, 30 percent of Pakistani students gained five or more good GCSEs, compared with 50 percent of the general population as a whole. Bangladeshi and Pakistani children with unemployed parents are more likely to enter higher education than their white counterparts (The Guardian, 2002).

6.3 INCOME AND EMPLOYMENT

Table 6.2 shows the income, employment and industry of the respondents.

Table 6.2 Income, Employment and Industry

	Valid	Frequency	Percent
Employment	Working, for how many years have you been working	198	79.2
	Retired, please specify how many years since you retired	10	4.0
	Neither	42	16.8
	Total	250	100.0
Income	10k and under	95	38.0
	11k - 20k	78	31.2
	21k - 30k	49	19.6
	31k - 40k	24	9.6
	Over 41k	4	1.6
	Total	250	100.0
Industry	Public sector	35	14.0
	Finance	12	4.8
	Self employed	43	17.2
	Management and IT	16	6.4
	Health	14	5.6
	Education	19	7.6
	Others	64	25.6
	Total	203	100.0
	Not applicable	47	

6.3.1 Employment and Industry

Nearly 79.2 percent of the respondents are working compared to 16.8 percent who are unemployed and less than five percent retired. Most of the respondents are self-employed 17.2 percent) 14.0 percent work in the public sector, while those who work in education represent 7.6 percent, management and IT 6.4 percent; finance sectors 4.8 percent, the health sector only 5.6 percent and others make up 25.6 percent.

The Greater London Authority in 2001 reported that there were 2,450 Muslim businesses in London; *i.e.* one in ten businesses in London were owned by Muslims. There were 8,500 Indian restaurants in the UK, of which roughly 7,200 were Bengali. However, the Bangladeshis and Pakistanis had two and a half times the unemployment rate of the white population. Twenty-five percent of Pakistani men were self-employed compared with 11 percent of white men, while 65 percent of Bangladeshis were semi-skilled manual workers compared with 23 percent among other ethnic minorities and 15 percent among white Britons.

These assorted messages are generally in line with previous research, such as Tariq Modood's definitive Policy Studies Institute Report, Ethnic Minorities in Britain (1997) which showed Bangladeshis and Pakistanis experiencing greater disadvantage whilst their fellow Muslims from India did much better.

6.3.2 Income and Financial Health

Despite the fact that Britain may have well over 5000 Muslim millionaires who control in total liquid assets of more than £3.6bn (The Guardian, 2002), table 6.2 shows that the majority of respondents are from the low-income group. 38 percent of them earned very low incomes, *i.e.* less than £10k per annum, 31.2 percent earned between £11k and£20k, nearly 20 percent were from the middle class income group, their earnings being in the range of £21k to £30k per annum, and those who earned more than £30k represented only 11.2 percent. This result was attributed to the fact that the majority of respondents were of Bangladeshi origin, which is the most disadvantaged ethnic group in the Muslim community.

Bangladeshi households have incomes at or below the national average compared with two-fifths for other ethnic minority households. Bangladeshi men earn £150 per week less than white men, while the difference is £115 for Caribbean men and £116 for Africans (BBC News, 2002, April12).

Table 6.3 Respondents' Relatives' Income

	Valid	Frequency	Percent
Cannot afford a deposit for mortgage	Yes	75	39.50
	No	115	60.50
	Not applicable	60	
	Total	250	100
Cannot afford repayment for mortgage	Yes	32	16.8
	No	158	83.2
	Not applicable	60	
	Total	250	100.0
Do not have good enough credit for mortgage	Yes	18	9.5
	No	172	90.5
	Not applicable	60	
	Total	250	100
The home buying process seems too complicated	Yes	27	14.2
	No	163	85.8
	Not	60	
	Total	250	100
Cannot find an Islamic mortgage provider	Yes	37	19.5
	No	153	80.5
	Not applicable	60	
	Total	250	100.0
Due to religious reasons, cannot take interest bearing mortgage	Yes	66	35.8
	No	122	64.20
	Not applicable	60	
	Total	250	100.0

Table 6.3 summarizes respondents' relatives' incomes. It shows that 54.3 percent of the respondents' spouses have no income at all while 37 percent of them have a low income, more than 95 percent of the household respondents' sons/daughters make no contribution at all and nearly 90 percent of the respondents have no other contributors to the household cost.

These finding are in line with earlier studies *e.g*. Dar (2004) found that 90 percent of Muslims in Leicester earned less than £20k per year and 78 percent earned less than £15k.

Table 6.4 Respondents' Financial robustness

Valid	Frequency	Percent
We can mostly afford what we want, and often have money left	79	31.6
We can mostly afford what we need, but there is not much left	136	54.4
We struggle to make ends meet.	35	14.0
Total	250	100.0

Respondents were asked how far their money stretched. Table 6.4 shows the findings of that question. More than half of the respondents (54.4 percent) said that they can mostly afford what they need, but there is not much left. Clearly these respondents are coping with their day-to-day spending, but they are on the verge of their finances getting out of control. The number of respondents who are coping with their daily spending and have money left over and who might want to build up savings and investments is 31.6 percent, while 14 percent struggle to make ends meet and cannot tie themselves to any financial commitments before they sort out their daily finances. Maybe a basic financial education and some information to make the most of their money are required in the community.

6.4 DEPENDENTS AND SPOUSE

Table (6.5) shows the respondent's number of children, dependents, spouse employment and spouse industry.

Table 6.5 Number of Children and Dependents

	Valid	Frequency	Percent
No of children	0	4	2.7
	1	54	36.2
	2	26	17.4
	3	38	25.5
	4	19	12.8
	5	4	2.7
	More than 5	4	2.7
	Total	149	100.0
	Not applicable	101	
No of Dependents	Less than 2	136	54.4
	2 - 4	98	39.2
	5 - 7	11	4.4
	Over 7	5	2.0
	Total	250	100.0
Spouse Employment	Working:	54	39.1
	Retired:	8	5.8
	Neither:	76	55.1
	Total	138	100.0
	Not applicable	112	
Spouse Industry	Public sector	10	18.5
	Self employed	14	26.0
	Management and IT	5	9.3
	Health	5	9.3
	Education	11	20.4
	Others	9	16.5
	Total	54	100.0
	Not applicable	196	

6.4.1 Spouse employment and Industry

Spouse's employment showed the majority of women (55.1 percent) to be neither working nor retired; according to their culture they are housekeepers. Large numbers of them (39.1 percent) are working, possibly influenced by the British culture or maybe, due to economic pressures, to make ends meet. Based on the 2001 Census 69 percent of Muslim females are economically inactive. This may be due to the nature of Muslim society where men are expected to shoulder the financial responsibility of the household, hence they are expected to undertake more remunerable work than women. In recent years Muslim women have become an absolute symbol of oppression, and distorted images of them permeate news coverage in the British Media. The Islamic Human Rights Commission has reported many cases of employers and educators using this image to excuse discrimination. Muslim women are denied many opportunities on the assumption that they will - if not on a whim then by force - get married, or have many children. Or they face the unspeakable dilemma of having to choose between employment and their Islamic dress. Muslims' customs show the apparent inappropriateness of their attitudes towards women. However, blaming Islam is to express ignorance both of Islam and of the historical struggle for the equality of women in Muslim societies. For instance, Islam grants women legal rights to domestic help at the expense of their husbands. Three of the four Sunni schools consider domestic chores outside the scope of a woman's legal responsibilities towards her husband. Contrast that with US polls showing that working women still do 80 percent of domestic chores (Yusuf, 2002). Although this issue is out of the scope of this thesis it has been highlighted because of the importance of a second income for a household in order to buy a home and to draw attention to the fact that Muslim women have the required skills to be employed and can contribute positively in homeownership.

Spouses working in the public sector and those who are self-employed, account for 25 percent of the spouses' respondents for each industry. Education came second with 16 percent of the spouses' respondents working in this field, while 9 percent work in the health sector, 4.5 percent in the management and information technology sector and 20 percent in other sectors.

6.4.2 Number of Children

It is clear from table 6.5 that the majority of respondents' households' *i.e.* 61.1 percent have two or more children, those who have only one child represent 36.2 percent and only 2.7% of the respondents have no children. These findings confirm the results of the 2001 Census, which, show that a third of the British Muslim population are children. This indicates that the total number of Muslims in the UK is likely to increase as these large groups of young people have children of their own. This will indeed be true if Muslims continue to have a higher birth rate than the general population, or at least continue to have children in the same pattern as in this survey *i.e.* more than two children each.

6.4.3 Number of Dependents

Table 6.5 also shows that of the respondents who have relatives who depend on them financially, the majority (53.2 percent) have no dependents or fewer than two dependents, 39.2 percent have between two to four dependents and only 6.4 percent have five or more dependents. The large number of Muslims permanently settling in the UK and the marrying of the two cultures for the second and third generations of the Muslim Community means that money transfers (*Hawala*) become fewer and fewer. The French academic David Garbin, cited in the Guardian (June 21, 2002), said that the financial relationship between Bengali families in East London and those in Bangladesh was rapidly changing. He referred to a report in 1995 which indicated that 20 percent of Bangladeshi families in East London were sending money to Bangladesh whereas in the 1960s and 1970s, 85 percent were remitting their savings. Many British Muslims may not need to send money abroad because either the entire family has joined them in UK or the family is well educated and they do not need money. Many observers predict that this tradition will eventually die out.

6.5 FINANCIAL SOPHISTICATION AND BANKING COMMITMENT

This section aims to measure the level of sophistication of the financial affairs of Muslim households by identifying respondents' banking commitments. Tables 6.6 and 6.7 show the respondents' banking assets and their banking liabilities respectively.

Table 6.6 Respondents' Banking Assets

	Valid	Frequency	Percent
Bank account	Yes	207	96.7
	No	7	3.3
	Total	214	100.0
Bank Type	A conventional bank	174	84.1
	An Islamic bank	11	5.3
	Both	22	10.6
	Total	207	100.0
	Not Applicable	7	
Current Acc	Yes	195	94.2
	No	12	5.8
	Total	207	100.0
	Not Applicable	7	
Saving Acc	Yes	69	33.3
	No	138	66.7
	Total	207	100.0
	Not Applicable	7	
Investment Acc	Yes	3	1.4
	No	204	98.6
	Total	207	100.0
	Not Applicable	7	

Table 6.6 shows that majority of respondents are financially sophisticated as 96.7 percent have a bank account, either with a conventional bank (84.1percent) or with an

Islamic bank (5.3 percent), or with both (10.6 percent). As most current accounts offered by conventional banks are interest free if they are not used for an interest-based loan they are permissible from the Islamic point of view. Therefore, more than 94 percent have this service compared to 33.3 percent who have a savings account, and less than 2 percent who have investment accounts.

Table 6.7 Respondents' Banking Liabilities

	Valid	Frequency	Percent
Overdraft Acc/Personal Loan	Yes	27	13.0
	No	180	87.0
	Total	207	100.0
	Not Applicable	7	
Debit Card	Yes	80	38.6
	No	127	61.4
	Total	207	100.0
	Not Applicable	7	
Credit card	Yes	51	24.6
	No	156	75.4
	Total	207	100.0
	Not Applicable	7	
Home mortgage	Yes	41	19.8
	No	166	80.2
	Total	207	100.0
	Not Applicable	7	
Islamic Home Mortgage	Yes	4	1.9
	No	203	98.1
	Total	207	100.0
	Not Applicable	7	

Table 6.7 shows the respondents' banking liabilities with only 13 percent having a personal loan or overdraft facilities, while 38.6 percent have debit cards and 24.6

percent have credit card facilities. Nearly 20 percent of respondents have conventional mortgage which contrasts with less than 2 percent who have Islamic mortgages. Among Muslim households 75 percent of owner-occupiers have a conventional home mortgage and only 8.3 percent have an Islamic home mortgage.

6.6 HOMEOWNERSHIP

This section aims to provide an overview of the level of homeownership among the Muslim Community in the UK and to answer the following research question:

Research question (1) what are the challenges and prospects of homeownership among the Muslim community in the UK?

According to the International Union for Housing Finance (IUHF), levels of owner-occupation in the UK are around 71 percent (BBC News, Februry13 2008). Although this is higher than North America (69 percent), Japan (61 percent), France (56 percent) and Germany (43 percent), compared to other developed nations it looks fairly average. Ireland, for example, has owner-occupation levels of 77 percent, Italy has 80 percent and Spain has 83 percent. The UK, in fact, is ranked 56th in the world's owner-occupation levels according to the IUHF (Politics.co.uk, 2007).

6.6.1 Tenure

Home-ownership has now been the preferred tenure amongst UK households for more than thirty years.

Table 6.8 Tenure and Type of Homeownership

	Valid	Frequency	Percent
Tenure	Own the house/flat you are living in	60	24.0
	Rent house/flat you are living in	190	76.0
	Total	250	100.0
Type of homeownership	Paying mortgage	50	83.3
	An outright owner	10	16.7
	Not applicable	190	
	Total	250	100.0

Table 6.8 above shows that the majority of respondents (76 percent) are renting the home they are living in compared to only 24 percent of respondents who own their home. It is a fact that there is a gap in homeownership among the Muslim community compare to the general public. According to a recent report about Muslims' housing experience in the UK only about half of Muslim households (51percent) are homeowners, compared with 71 percent of the general population. Muslims are more dependent on social housing than the general population (28 percent of Muslim households rely on social housing compared with 20 percent of the general public) and on private renting, 17 percent of the Muslim populations are in private rented accommodation against 10 percent of the general public (Sellick, 2004).

Table 6.8 shows that 83 percent of Muslim homeowners surveyed are paying mortgages on their homes and 17 percent of them are outright owners.

The issue of taking out a conventional mortgage affects Muslims today in a way that it did not affect their parents. For the first generation of Muslims the common solution of the housing problem was to buy a house outright. In the early 1960s this was fairly common practice even for the indigenous British citizen.

At that time Muslims were excluded from council housing because local councils normally required a minimum period of residence in the area before they became eligible for housing. In the 1970s nearly every council in the UK removed the residence qualification requirement which is one reason why the majority of Bangladeshis, who mostly arrived in UK in that decade, are living in council housing today compared to Pakistanis who arrived here earlier (Robinson in Clark et al 1984). The mechanism by which first generation Muslims achieved homeownership through outright purchase is referred to in several studies *e.g.* Halliday (1992) in his studies of Yemenis. He says that a group of people would club together to save a certain amount per week, thus over a certain period of time a total pool of a house price was available and would be used to purchase a house for the first member of the club. All the members would then continue to save until another house could be bought, and so on.

6.6.2 Understanding the Gap in British Muslim Homeownership

Respondents were asked in question 22 of the questionnaire: If you are a tenant what is the major reason why you have not bought a home? The findings of their responses are summarized in table 6.9. There is a clear gap in homeownership in the Muslim community, thus there is a need for an up-to-date development policy to help Muslims to enter the housing market.

From table 6.9 the following gaps can be identified:

6.6.2.1 Affordability Gap

There are two aspects of affordability, firstly the ability to enter the market, which includes raising a deposit, and secondly the ability to stay in the market, *i.e.* the repayment of a mortgage. These two facets are likely to be correlated and clearly a borrower needs to satisfy both aspects. For a more thorough examination, please see Vass (2003).

When the tenant respondents were asked what the major reason was for them not having bought a home the greatest affordability concern for British Muslims was the ability to raise a deposit; nearly 40 percent of them could not afford a deposit for a mortgage. However, having a comfortable monthly house payment is a lesser concern for British Muslims, as just 17 percent of the respondents could not afford the mortgage repayments.

Deteriorating affordability of home ownership has been a main cause of the reduction in first-time buyer numbers. In fact, it has been suggested that only 33 percent of new households in the UK could afford to buy on the basis of income alone, without some form of assistance (Bramley, 2004a).

6.6.2.2 Financial inclusion gap

The second barrier for homeownership in the British Muslim community is interest, as many British Muslims were unable to get their foot onto the property ladder as a result of interest-bearing mortgages being forbidden in Islam. Almost 36 percent of the respondents said that due to religious reasons, they could not take on an interest-bearing mortgage. The religious conviction of Islam embraces all aspects of a Muslim's life, including the way finance and business transactions are conducted.

One of the most essential and widely-understood doctrines of the religion is that the payment or receipt of interest is strictly forbidden. This means that conventional mortgage products are inappropriate for Muslims. "Some (Muslims) are wracked with guilt because they have broken Islamic law. While others' values are beyond question, they are more pragmatic in order to keep a roof over their family's head", said Iqbal Asaria, a former spokesman for the Muslim Council of Britain (BBC, July1 2003). On the other hand 20 percent of the tenant respondents said their major reason for not buying a home is that they cannot find an Islamic mortgage provider, even though there at least two high street banks – HSBC Amanah and Lloyds TSB – now offering Islamic home finance packages. 'Needs of British Muslims have been overlooked by the financial service industry'', says Syed Noaman Hasan, UK Head, Amanah Finance (Shanmuganathan, 2004). As mentioned earlier the Muslim community in the UK is proportionately the biggest segment of society using social housing. As discussed earlier in Chapter Four, there is an effort in process to adapt Islamic home finance for the needs of the local authority and social housing tenants. These efforts need to be encouraged and a required adaptation of regulations needs to be speeded up.

Table 6.9 Major Reasons Why Tenants Have Not Bought a Home

	Valid	Frequency	Percent
Cannot afford a deposit for mortgage	Yes	75	39.50
	No	115	60.50
	Not	60	
	Total	250	100
Cannot afford repayment for mortgage	Yes	32	16.8
	No	158	83.2
	Not	60	
	Total	250	100.0
Do not have good enough credit for mortgage	Yes	18	9.5
	No	172	90.5
	Not	60	
	Total	250	100
The home buying process seems too complicated	Yes	27	14.2
	No	163	85.8
	Not	60	
	Total	250	100
Cannot find an Islamic mortgage provider	Yes	37	19.5
	No	153	80.5
	Not	60	
	Total	250	100.0
Due to religious reasons, cannot take interest bearing mortgage	Yes	66	35.8
	No	122	64.20
	Not	60	
	Total	250	100.0

6.6.2.3 Information gap

The third main gap identified in this survey is the problem of accessing information, as 14 percent of respondents (see table 6.9) perceive the home buying process to be too complicated. This finding confirms earlier research reported to the housing cooperation by the Oxford Centre for Islamic Studies which showed that considerable sections within the Muslim community do not have easy access to information and services (Sellick, 2004). Females are particularly dependent on the men in their household for access to information and services; the elderly and newly-arrived migrants have language difficulties in accessing information and services. Policy-makers and relevant organizations have to ensure greater awareness about services provided by statutory and voluntary sector organizations, and more information in relevant community languages is needed to encourage greater take-up of services.

6.6.2.4 Credit Gap

Surprisingly credit is not a great concern for Muslim households as only 10 percent of respondents consider that they do not have good enough credit to be able to become a homeowner see table 6.9.

In the UK there are two systems for dealing with credit risk. One is private, where lenders insure high Loan to Value (LTV) loans through mortgage indemnity insurance (IM). This protects the lender against losses due to foreclosure and the cost is paid by the borrower.

The other system is the state system which offers limited protection through Income Support for mortgage interest scheme, which pays mortgage interest for borrowers who become unemployed or sick after a waiting period.

These two systems of mitigation of the risk do not benefit Muslim homeowners, simply because of the *riba* (interest) involved. There is a need for Islamic home insurance (Home *Takaful*), based on the concept of mutual cooperation in the sharing of risk, as an alternative for Muslims.

As far as the state system is concerned, there are two interesting examples, in Belgium and the Netherlands, where homeowners rely on the state for risk management

(Scanlon and Whitehead, 2004). Muslims homeowners may benefit if similar systems are adopted in UK.

In Belgium the state provides insurance against income losses. This system works when a borrower concluding a mortgage, can get ten years free insurance. If the householder becomes unemployed the insurance will make part contribution to repayment of the mortgage. The scheme is managed by large insurance companies on behalf of the government, which pays the cost of the insurance.

The second example is the Netherlands Mortgage Guarantee Scheme (NHG), which works as follows: The homeowner pays 0.3 percent of the mortgage amount for a guarantee from (NHG). This money goes into a fund to meet potential losses. Under its terms, the (NHG) will pay should the borrower be unable to meet interest or repayment obligations. The most important condition for the NHG is that the property cost is capped; it should not cost more than EUR 265,000, including all additional costs such as civil-law notary costs, commission and refurbishment (www.nhg.nl/ cited 2008).

6.6.3 Aspirations for Homeownership

Aspiration to live in owner-occupied housing in ten years time in the UK jumped from 62 percent in 1975 to a peak of 84 percent in 1991. Since then the ratio has levelled off and currently stands at 80 percent. A similar pattern is seen for householders' desire to own in two years time where the ratio jumped from 51 percent in 1975 to 72 percent in 2004 (Smith, J. 2004). In contrast the aspiration level to own a home in three years time in the Muslim Community is very low with only 32 percent wishing to own in three years time in this survey.

Table 6.10 Intention to Buy a Home in the Next Three Years

Valid	Frequency	Percent
Yes	61	32.1
No	47	24.7
Not sure	82	43.2
Not applicable	60	
Total	250	100.0

Chi-square 9.800 Asymp.sig. 0.007

As can be seen from table 6.10, when respondents were asked about their intention to buy a home in the next three years although the majority (43 percent) of respondents are not sure about their intention a significant number of them (32 percent) have a definite intention of buying a home within the three years. However 25 percent of the respondents have no intention whatsoever to buy a home in the near future. Since the chi-square level is lower than 0.05 then the null hypothesis will be rejected, therefore the differences between the options given to the respondents are not attributed to chance.

6.6.4 Aspirations for Homeownership by Age and Income

The cross tabulation between age and intention to buy a home in the next three years suggests that there is a correlation between the two. Since the significant value of the age factor is equal to the alpha value of 0.05 as in the chi-square test in table 6.11, this indicates that the attitudes to owning have changed within different age groups. In particular the cross tabulation table 6.12 clearly shows low aspirations in younger Muslims who are under 25 years and very dramatically low aspirations in the elderly. Nonetheless, aspiration is higher in the middle age groups, 44 percent and 43 percent for the age groups 46-55 years and 36-45 years respectively.

Table 6.11 Chi-Square Tests for Cross Tabulation of Age & Intention to Buy in the Next Three Years

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	18.278(a)	10	.050
Likelihood Ratio	17.849	10	.058
Linear-by-Linear Association	4.580	1	.032
N of Valid Cases	190		

Table 6.12 Cross tabulation of Households Who Aspire to Buy Their First Home in 3yrs time, by Age

			Intention to buy home in the next 3 years			Total
			Yes	No	Not sure	
Age	25 and under	Count	10	16	18	44
		% within Age	22.7%	36.4%	40.9%	100.0%
	26 – 35	Count	17	10	38	65
		% within Age	26.2%	15.4%	58.5%	100.0%
	36 – 45	Count	23	13	18	54
		% within Age	42.6%	24.1%	33.3%	100.0%
	46 - 55	Count	10	6	7	23
		% within Age	43.5%	26.1%	30.4%	100.0%
	56 - 65	Count	1	1	1	3
		% within Age	33.3%	33.3%	33.3%	100.0%
	66 and +	Count	0	1	0	1
		% within Age	.0%	100.0%	.0%	100.0%
Total		Count	61	47	82	190
		% within Age	32.1%	24.7%	43.2%	100.0%

The cross tabulation between income and intention to buy a home in the next three years suggests that there are correlations between the two, as the attitudes to owning have changed between different income groups. From table 6.13 the significant factor for income 0.04 is smaller than the alpha value 0.05; this indicates that there is a positive correlation between income and the aspiration for home-ownership.

We do not know from this survey how aspirations to buy translate into actual home-ownership. Nonetheless, it is likely that affordability constraints in the past few years mean that fewer households who aspire to home-ownership are able to make that a reality within the three years framework. For example, research by Bramley (2004b), suggests that only 33 percent of new households could afford to buy in 2004, well down on 2002 when 40 percent could afford to buy. However, it is clear that the reasons behind the home-ownership gap are likely to be different for different age groups.

Table 6.13 Chi-Square Tests for Cross Tabulation of Income & Intention to Buy in the Next 3Years

	Value	**df**	**Asymp. Sig. (2-sided)**
Pearson Chi-Square	16.090(a)	8	.041
Likelihood Ratio	16.734	8	.033
Linear-by-Linear Association	2.339	1	.126
N of Valid Cases	190		

Table 6.14 Cross Tabulation: Households Who Aspire to Buy Their First Home in Three Years Time, by Income

			Intention to buy home in the next 3			**Total**
			Yes	No	Not sure	
Income	10k and under	Count	17	28	32	77
		% Within	22.1%	36.4%	41.6%	100.0%
	11k - 20k	Count	23	13	31	67
		% Within	34.3%	19.4%	46.3%	100.0%
	21k - 30k	Count	13	3	14	30
		% Within	43.3%	10.0%	46.7%	100.0%
	31k - 40k	Count	8	3	4	15
		% Within	53.3%	20.0%	26.7%	100.0%
	Over 41k	Count	0	0	1	1
		% Within	.0%	.0%	100.0%	100.0%
Total		Count	61	47	82	190
		% Within	32.1%	24.7%	43.2%	100.0%

6.6.5 What Factors Encourage or Discourage Muslim Households from Buying

This section aims to answer the following research question:

Research question (2) what factor/s might encourage/ discourage home-buying within the Muslim community?

House prices have trebled to an average of £184,070 since the Labour Party came to power in 1997, providing millions of existing homeowners with surges in their personal wealth. As prices have risen, buyers have pushed themselves to the brink to get onto the property ladder. A monthly survey by Spicerheart Financial Services found that the proportion of borrowers taking out mortgages of 95 percent or more of the value of the property doubled from 9 percent to 19 percent between January and June 2007. If a person was in a position to buy, the general view was they should do so in order to avoid further house price inflation in the future. Nonetheless, recently house prices have fallen due to the lack of financing available, not a fall in demand. As the recession bites, mortgage shortages will be compounded by a fall in consumer confidence reducing demand and prices will fall still further. However the United Kingdom still faces a severe housing shortage and the current hiatus means this will simply get worse. The Labour government wants to improve affordability by increasing the supply of homes to 240,000 new homes a year by 2016, but with the 2008 credit crunch and collapsing house prices, those numbers will be impossible to achieve. Hence, the current downturn will result in severe house price inflation again by 2015 according to the estimation of the National Housing and Planning Advice Unit (Adams & Humber, January11 2009). In this climate of relative uncertainty it is helpful to be able to gauge Muslims' attitudes to buying and what might influence their decision to buy over the next three years.

Table 6.15 summarizes what factors might encourage households to buy their first home in the next three years.

Table 6.15 Factors Encouraging Home Buying in the Next Three Years

Valid	Frequency	Percent
More affordable house prices	39	20.5
Income rise	40	21.1
New job	16	8.4
House prices stable	8	4.2
Stamp duty reduced	2	1.1
Need to get foot on ladder	4	2.1
If get help with the deposit	12	6.3
Provision of Islamic mortgages (interest free	69	36.3
Not applicable	60	
Total	250	100.0

The respondents were asked what factors would encourage them to buy a home in the next three years. Most believe that the availability of Islamic mortgages is the most important factor, even more important than affordable house prices; more than 36 percent selected the provision of Islamic mortgages as the number one factor that would encourage them to buy a home in the next three years. More than 21 percent believe that if their income rises that will enable them to buy a home in the next three years. Nearly 21 percent believe that more affordable house prices are essential to buying a home in the next three years. Eight percent think that if they get a new job they might be encouraged to buy a home in the next three years. More than six percent think that getting help in paying the deposit for a mortgage would encourage them to buy a house in the next three years. The stability of house prices and the reduction of property taxes (stamp duty) are lesser encouraging factors for respondents to buy a home in the next three years.

Table 6.16 summarizes what factors might discourage households from buying their first home in the next three years.

Table 6.16 Factors Discouraging Home Buying in the Next Three Years

Valid	Frequency	Percent
High house prices	55	28.9
Can not save deposit	20	10.5
Income too low	32	16.8
Job insecurity	13	6.8
Expect house prices to fall	4	2.1
Stamp duty	1	.5
Non-provision of Islamic mortgages	49	25.8
None	16	8.4
Not applicable	60	
Total	250	100.0

When responding to this survey in early 2007, the Muslim tenants selected a number of factors that discouraged them from buying a home in the next three years. The majority of survey respondents (29 percent) considered the high house prices in the housing market to be the biggest hurdle to them becoming a homeowner even though prices are now falling, but even if the Government revives the market and restores the flow of mortgage funds to borrowers the issue of high prices is still valid. Twenty-six percent of respondents perceived the non-provision of Islamic mortgages to be the second major factor discouraging them from buying a home. While 17 percent of the respondents perceived too low income as a third factor discouraging home buying in the next three years. On the other hand 11 percent of the respondents would not be able to save the deposit to buy in the next three years. The fifth factor, considered by seven percent of the survey respondents as a barrier to buying a home in the next three years, was job insecurity. A very small number of respondents (only two percent) considered the expectation of a fall in house prices to be a discouraging factor in buying a home in the next three years and less than one percent considered stamp duty to be a discouraging factor of buying a home in the near future. Nevertheless 8 percent of the respondents saw none of the above factors as preventing them from buying a home in the next three years.

6.6.6 The Lure of Homeownership

British Muslims are unsurprisingly bullish on housing and homeownership. Half of Muslim households are homeowners; compared with 71 percent of the general population, but a significant proportion, nearly one third, are buying with a mortgage or loan despite concern among many Muslims about borrowing money on interest.

Table 6.17 Major Reasons to buy a Home

	Valid	Frequency	Percent
It is good long-term investment	Yes	157	62.8
	No	93	37.2
	Total	250	100.0
Paying rent is not good investment	Yes	99	39.6
	No	151	60.4
	Total	250	100.0
To live in a neighbourhood that you like	Yes	49	19.6
	No	201	80.4
	Total	250	100.0
Getting married and expecting children	Yes	44	17.7
	No	206	82.3
	Total	250	100.0
It provides the feeling of owning something of your own	Yes	61	24.4
	No	189	75.6
	Total	250	100.0
It is something you always dream of doing	Yes	38	15.2
	No	212	84.8
	Total	250	100
Encouraged by the discount in the "right to buy" scheme	Yes	14	5.6
	No	236	94.4
	Total	250	100.0

Table 6.17 summarizes the answers of the survey respondents when asked their major reason to buy a home.

63 percent of respondents said a major reason to own a home is that it is a good long–term investment. Similarly, 40 percent of the respondents cited the fact that paying rent is not a good investment as a major reason to own a home. In addition to being an excellent financial investment, British Muslims believe that owning a home also provides social benefits. In particular, they say owning a home provides them with a strong sense of personal satisfaction and accomplishment, as 24 percent of those who surveyed cited 'the feeling of owning something of your own' as a major reason to own a home. In fact, for some Muslim households the intangible satisfaction of homeownership is even more important than the monetary investment benefits. Twenty percent believe the major reason to buy a home is to live in a neighbourhood that you like. Change in family structure such as marriage and having children was cited by 18 percent as a major reason to buy a home. Fifteen percent of the respondents said 'it is something you always dream of doing''. The discount in the 'right to buy' registered much lower, with only six percent believing it to be major reason to buy a home.

Analysis of individuals' local activities confirms that homeowners invest considerably more in their local communities than do rental tenants. A study by Di Pasquale and Glaser (1999) discovered that homeowners are more likely to join organizations and to help solve local problems. Many studies have recognized that residential prices are significantly affected by community quality or what are often termed local amenities. However, when a rental tenant moves it is the landlord who benefits from the value of any improvement in local amenities, and therefore a homeowner tends to have a greater incentive than a renter to invest in the local community. A study by Haurin, Parcel and Haurin (2001), finds that homeownership benefits children, as judged by behavioural and educational performance. Homeownership is found to reduce behavioural problems in children, which in turn can lead to better-behaved children and less crime.

However, a minority of economists believe that home ownership imposes a crippling burden on the economy. For example Oswald (1999) argues that unemployment rates have risen most quickly in the nations with the fastest growth in home ownership. He states the fact that Spain has the highest unemployment, and also the highest rate of home ownership and in the 1950s and early 60s, the United States had the highest unemployment, and at that time had the highest rate of home ownership. This is in contrast with Switzerland which has the lowest unemployment, and the lowest rate of home ownership (Oswald, 1999).

6.7 AFFORDABILITY

As house prices have risen and the prospect of home-ownership accelerated away from the grasp of Muslim households, the issue of housing affordability has demanded the attention of lenders, financial advisers, and policy-makers.

Table 6.18 Affordability

	Valid	**Frequency**	**Percent**
Availability of the Funds for a deposit	Yes	32	16.8
	No	111	58.4
	Not sure	47	24.7
	Not applicable	60	
	Total	250	100.0
Proportion of income allocated to mortgage	Less than 10%	74	38.6
	10%- 19%	51	27.0
	20%- 29%	34	18.0
	30%- 39%	18	9.5
	40% and more	13	6.9
	Not applicable	60	
	Total	250	100.0
Preferences of lease hold over free hold	Yes	26	13.7
	No	71	37.4
	Not sure	93	48.9
	Not applicable	60	
	Total	250	100.0

6.7.1 Availability of Funds for a Deposit

It is very clear that there is an affordability problem as 58 percent of the surveyed respondents have no funds available for a deposit on a house. On the other hand only 17 percent have funds ready for a deposit to buy a home and 25 percent are not sure about their financial position. This result is due to the fact that, as we clearly stated earlier, in the Muslim household profile the majority of respondents are from Bengali ethnic origin, and have an income at or below the national average. Also, 90 percent of the household have no other contributors to rely on when raising a deposit. Hence, due to the limited opportunities to accumulate liquid wealth and the earning of relatively low wages the majority of respondents have no funds available for a deposit.

House price growth significantly outpaced income growth until recently. As a consequence, raising a large deposit is now a major constraint to becoming a homeowner. For example, the average UK house price was more than £186,000 in August 2005 (ODPM 2005a). This compared with prices of over £100,000 in 2000. Over this period as a whole, the growth rate has averaged nearly 14 percent a year. It peaked at 25 percent at the end of 2002, but has since fallen to around 3 percent. The strength of house prices reflects the low level of house building, which has been unresponsive to the rise in prices. As we can see from table 25 a major factor now putting off first-time buyers from making the decision to buy is the need to raise a deposit. This is essential in order to pay the difference between what banks are willing to lend on the basis of their assessment of the repayment and the price of the property. The typical first-time buyer now needs to raise a deposit of £17,000, equivalent to over 50 percent of gross annual household income, compared with £6,150, equivalent to around a quarter of annual income, in 2000 (CML, 2005). Nonetheless, because of the 2008 credit crunch house prices are falling but research shows that a high proportion of prospective homebuyers have postponed applying for a mortgage because they were afraid of redundancy.

6.7.2 Proportion of Income Allocated to Mortgage

Once again the affordability gap is the main obstacle to homeownership; mortgage repayment is quite difficult for most of the respondents (39 percent) who can allocate only less than 10 percent of their income to repaying a mortgage. The Council of

Mortgage Lenders Report in the 4th quarter of 2006 shows that a typical two-income British couple buying their first property would have had to commit 34 percent of their joint income to meet their initial mortgage payments, the highest level since 1990. In April 2005, 11 percent of loans to first-time buyers were taken out at over four times income, but by March 2007 this had risen to 21 percent.

The survey found that 90 percent of respondents who were potential first time buyers had no other source of help or assistance, so having high loan to value ratio (LTV) means that they have little room to manoeuvre in the early years of the mortgage; if their situation changes repayment of their mortgage becomes difficult.

6.7.3 Preferences of Leasehold over Freehold

When respondents were asked whether they preferred the cheaper option of leasehold over the more expensive freehold, in order to overcome the affordability problem, 49 percent were not sure about their preferences, and only 14 percent preferred a leasehold property.

Homebuyers like freehold ownership, but if the location is right, the freehold or leasehold tenure, may not be a problem except where the outstanding lease is too short. Property professionals will testify that preference for freehold property over leasehold is an inevitable conclusion. Also banks' preference for a property declines correspondingly with the term of the unexpired lease. By the same token, the value of the property drops because of the need to transfer the ownership of the leasehold properties. Also the possibility of the expired lease being replaced with a shorter renewed lease period offers little comfort to prospective homebuyers. Traditionally if a flat is offered for sale with a share of freehold this is more attractive to homebuyers than if it were sold as leasehold. Consecutive governments have recognized these issues and this has resulted in the introduction of extensive rights, primarily in favour of tenants. The tenants' right to purchase the freehold (collective enfranchisement), to extend their leases and to takeover the management of the building (right to manage), is set out in the 2002 Act (GD News, Autumn 2005).

6.8 CONCLUSION

There are clear gaps in homeownership among British Muslims, which can be identified as follows: First the affordability gap as the greatest affordability concern for British Muslims is the ability to pay a deposit. It has also been noted that the majority of Muslim households are able to allocate only less than 10 percent of their income to meet mortgage instalments. The second gap in homeownership among the British Muslim community is financial inclusion, as many British Muslims are unable to get their foot onto the property ladder due to the fact that interest bearing mortgages are forbidden in Islam. The third main gap identified in this survey is the problem of accessing the information about the housing and home buying process, as some of the respondents perceived the home buying process to be too complicated.

Aspiration for homeownership among British Muslims is not strong enough as just over a third of respondents aspire to own their home. There is a correlation between the aspiration for homeownership and age, as aspiration for homeownership is very high among the middle age groups and very low among the elderly. Also there is a positive relationship between the aspiration for homeownership and the respondents' income.

British Muslims have great confidence in homeownership, as the majority of them perceive it to be a good long term investment. They also perceive paying rent as a bad investment. In fact, for some Muslim households the intangible satisfaction of homeownership is even more important than the monetary investment benefits.

The issue of housing affordability has demanded the attention of lenders, financial advisers, and policy-makers. It is very clear that there is an affordability problem, as the majority of the respondents surveyed have no funds available for a deposit on a house. Also mortgage repayment is quite difficult for most of the respondents as many of them can allocate only less than 10 percent of their income to repay a mortgage.

After having seen the sample characteristics and homeownership among British Muslims the following chapters are devoted to the survey analysis. These include two aspects of Islamic housing finance in the UK, the market potential investigated in Chapter Seven and marketing strategies, studied in Chapter Eight followed by Conclusion and Recommendations in Chapter Nine.

Chapter 7

THE MARKET POTENTIAL FOR ISLAMIC HOME FINANCE IN THE UNITED KINGDOM

7.1 INTRODUCTION

The UK Islamic mortgages market has seen an impressive growth over the last five years. The Financial Service Authority (FSA, 2007) quantifies the size of the UK Islamic mortgages market at a value of £500 million; this indicates an average annual growth rate of more than 68.1 percent since 2000, in comparison with the total mortgage market's average growth of 16.2 percent. The report indicates that the Islamic mortgages market began to accelerate and more lenders entered the market, after the labour government introduced relief from Stamp Duty which had seriously hampered the market.

This chapter explores and evaluates the development of the demand for Islamic mortgages in the UK, making particular use of empirical evidence drawn from the questionnaire distributed to Muslim households seeking Islamic mortgages in the east London area, in the period of January to March 2007. This chapter also provides the results of the cross tabulations and statistical tests, mainly focusing on the following areas:

The size and demographic profile of the Muslim population in the UK are overviewed in section 7.2. Section 7.3 evaluates the demand for Islamic mortgages in the UK with a view to quantifying this demand. Two kinds of demand have been identified from the behaviour of Muslim households towards Islamic mortgages; these are discussed in detail in this section. Furthermore, this section tries to determine the factors that might influence this demand. Section 7.4 studies the perception of Islamic mortgages among British Muslims and provides an empirical assessment of those perceptions. Finally, section 7.5 provides a detailed discussion of the possibility of extending the current structure of Islamic mortgages to the low-income groups of Muslim households through Low Cost Homeownership schemes (LCHO).

7.2 SIZE AND DEMOGRAPHIC CHARACTERISTICS OF THE BRITISH MUSLIM POPULATION

There are over two million Muslims resident in the United Kingdom, mostly British citizens, the majority of whom have now been born in the country. According to Home Office estimates the Muslim population in the UK now constitutes the second largest religious community in the UK after Christians, with an estimated 760,000 practicing Muslims, most of whom observe the Sunni tradition at 1136 registered mosques every Friday (MCB, 2006). Also, 20,000 British Muslims travel to Mecca for *Hajj* (pilgrimage) every year according to the Foreign Office (cited by MCB, 2006). The community consists of 350,000 households, the typical family being twice as large as the average family size in the United Kingdom.

7.2.1 Origins of the Muslim Population

The Muslim population in the UK is predominately from the ethnic and cultural backgrounds of India (10 percent), Pakistan (38 percent), and Bangladesh (19 percent). Approximately 16 percent of UK Muslims are of Middle Eastern origin, with the remainder coming from Africa (13 percent), Europe (three percent), and other parts of Asia (one percent). Historically the ethnic groups originating from the Indian subcontinent have shown a higher rate of population growth, as compared to other groups in the UK, a trend that is likely to be confirmed anew by the Official Census in 2001 (Guardian, 2002,).

The population of Middle Eastern origin is heterogeneous. The longest established is a Yemeni community who date from seamen who settled in the late nineteenth and early twentieth century. Many have intermarried, and most have at best a limited knowledge of Arabic and have never been to Yemen, but Islam remains strong in this community. There is also a Turkish Cypriot community, mainly resident in north London, where the size of the community exceeds those remaining in Cyprus. There is also a small Arab community, mainly of Egyptian and Palestinian origin, but most are now also British citizens.

In addition to this there are also significant numbers of Muslim students who are temporary residents of the United Kingdom for the duration of their studies, the largest group coming from Malaysia. These and summer visitors, mainly from the Gulf region, represent a transient community, but many maintain British bank accounts and use other financial services, especially involving foreign exchange and money transfers.

Financial transfers to the Indian sub-continent have declined as the Asian community has become more settled in Britain and ties with distant relatives have weakened.

The Second and third generation Muslims from these ethnic groups are British nationals by birth. They have shown success in educational and professional achievements. An increasing proportion of those are professionals with university degrees working as doctors in general practice and hospital surgeons. In the private sector many work as lawyers or accountants and there is a rapidly-growing number of information technology specialists, notably in systems management. The group earning £30,000 or more per year is mainly made up of these educated professionals. Research indicates that these professionals are well aware of their religious and social roots. Thus, there is a natural preference among them to conduct their financial affairs in line with religious convictions and Islamic lifestyles.

Such groups require a wide range of personal banking services, their largest single outgoing being the mortgage on the property in which they reside with their families. Most have occupational pensions and are entitled to sickness benefits from their employers, but they require house and contents insurance and vehicle cover, and many have some form of endowment insurance.

7.2.2 Geographic Distribution of the Muslim Population

The distribution of Muslims in the UK falls into a number of well-defined regions in the South (London, Luton and Slough), the Midlands (Birmingham and Leicester), and the Pennines (Manchester, Lancashire, Leeds and Bradford), as well as smaller communities in Glasgow and in the Cardiff, Bristol and Bath areas. In some heavily-populated areas, such as Leicester and Luton for example, up to 20 percent of the population is Muslim. Indeed, within the next decade, as the Muslim population grows to above 50 percent, Leicester is set to become the first city in the UK with a Muslim majority *i.e.* ”ethnic majority’’ (Zawya.com, 2004).

Much of the Muslim population is centred on the South East of England, in Slough, and in North, West and Central London. Datamonitor estimates that eight percent of the population in Greater London is Muslim, amounting to approximately 725,000 persons. This means that over 40 percent of UK Muslims live in the Greater London area.

7.3 THE POTENTIAL DEMAND FOR ISLAMIC HOUSING FINANCE PRODUCTS

The main feature of home ownership in the UK is the high percentage of homes purchased through mortgage loans. Getting a mortgage is one of the biggest dreams for an individual in order to lead an economically secure life. There were around 11.5 million mortgages at the end of 2003 with a total stock of debt of over £740 billion (Miles 2004). It is estimated that the Muslim population in the UK secures five percent of total mortgages (Dar 2002). The UK Land Registry recently published the information that for the year 2007 the average value of residential property in the UK was £177,099. Taking this estimate into account, along with the Muslim share of the existing mortgage market, the total market for Islamic mortgages is potentially in excess of £10 billion. Robin Matthews (2003) estimates that half of British Muslims are anxious to be *Shari‘a*-compliant in respect of their mortgages and the potential market is still over £5 billion. Furthermore, if Malaysian Islamic mortgage market experiences are taken into account, the demand for Islamic mortgages from non-Muslims who believe them to be ethically motivated will be significantly high.

Datamonitor (2000) reported that of those British Muslims who earn more than £30,000 annually 184,000 had saving accounts, 141,000 had Investment Saving Accounts (ISA), personal equity plans (PEP), or Tax-Exempt Special Savings Accounts (TESSA) with a maximum investment of £7000. Also, 86,000 owned shares and 16,000 had purchased unit trusts. Nonetheless, the home ownership rate among British Muslims is relatively low compared to other communities in the UK. The main explanation for this low ownership rate is that there has been no availability of Islamic home finance. Muslim needs for Islamic home finance have been overlooked by the British financial service industry, and this has had an adverse effect on home ownership in the Muslim community.

Research suggests that an Islamic home finance product would offer an opportunity for the vast majority of the Muslim community to progress from the position of being inactive investors to becoming stakeholders and evolving as a community actively participating in the process of financial development in the country (e.g., Dar, 2002; Matthews, 2003; Wilson, 2007).

The following table gives an age and income analysis of British Muslims

Table 7.1 Analysis of Income and Age Groups of Muslims

Age Range	**Below £30k**	**Above £ 30k**
18 -24	244,470	56,138
25 - 34	154,421	61,453
35 - 44	194,977	95,515
45 - 54	149,122	55,758
55 - 64	108,259	22,972
65 and over	70,925	2,005
Total	922,174	292,941

Sources: Datamonitor, Policy Studies Institute, Labour Force Survey (1999).

The above table shows that the highest earning group falls into the 35-44 year old age group. This is the stage at which the need for long-term investments, mortgages, insurance, loans and credit coincides with individuals settling down, having families and aiming to address long-term stability and security issues.

In short, the earlier study (Datamonitor, 2005) shows that Muslims are the fastest-growing community in Britain and emerge as a key yet untapped market for financial products and services.

7.4 ASSESSING THE DEMAND FOR ISLAMIC MORTGAGES

This section focuses on assessing the demand for Islamic mortgages in the British Muslim community, with a view to quantifying that demand in this country and then determining the factors that might affect it. Despite the fact that many argue that there is significant demand for Islamic mortgages in the UK (Datamonitor, 2002) there are some indications which lead us to believe that the demand for Islamic financial products in general is limited. In other words it does not exist at grassroots level and it may prove to be a delusion. For example, the closure of *Al-Baraka* Bank and the poor take up of the *Halal* Mutual Investment in the 1990s might give the impression that the British Muslim community is not financially sophisticated and not fully aware of Islamic finance. There may not be the customary demand for Islamic financial services even in the in the main Muslim countries (see Ahmad and Haron, 2002; Erol and El-Bdour, 1989). Hence this section aims to answer the following research question:

Research question no (3) Is there any effective demand for Islamic Mortgages in UK?

To answer the research question the respondents were asked whether or not they would be willing to take out an Islamic mortgage. The results are presented in Table 7.1 below, which shows the willingness of the respondents to take out Islamic mortgages. It is very clear that there is a substantial demand for Islamic mortgages as 66 percent (39.6+8.4+18) of the respondents are willing to take out an Islamic mortgage in contrast with only nine percent (5+4) who are not. However, 25 percent are not sure. The significance of the chi square goodness-of-fit test is lower than 0.05 then the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data.

The basic idea behind this question in the survey is to find out how willing a Muslim household would be to take out or switch to an Islamic mortgage if they had a choice. This method is similar to Lancaster's approach to consumer preferences (Lancaster, 1996) which stresses that clients seriously consider the characteristics that make up a product before deciding to buy. Hence, willingness to take out or switch to an Islamic mortgage should provide a good indicator of demand for the Islamic mortgage.

Table 7.2 Willingness to Take Out an Islamic Mortgage

VALID	FREQUENCY	PERCENT
Yes, only if the cost are similar to or less than conventional	99	39.6
Yes, no matter the cost, even if it is much more expensive	21	8.4
Yes, if leading Islamic scholars have approved it	45	18.0
No, Islamic mortgages are not possible	13	5.2
No, whatever the difference between Islamic mortgage and con	9	3.6
Not sure	63	25.2
Total	250	100.0

Chi-sq 145 df 5 Asymp.Sig .000

From the results of the above table six types of attitude towards Islamic mortgage can be identified and differentiated. Applying the similar classification for the demand for the Islamic financial services (Dar, 2004) two kinds of demand are derived from these attitudes: those who responded positively that they are willing to take on Islamic mortgages generate an effective demand for the Islamic mortgage and those who responded negatively that they are not willing to take out Islamic mortgages generate an ineffective demand for Islamic mortgages.

7.4.1 Effective Demands

From the positive responses of respondents' attitudes towards Islamic mortgages (those who responded yes they are willing to take out an Islamic mortgage) we can distinguish and differentiate between three types of demand for Islamic mortgages, which are the conventional demand, the pending demand and the staunch demand.

7. 4.1.1 Conventional Demand

The conventional demanders would in general be hesitant to use Islamic mortgages, particularly if they are more costly. In this case the respondents consider the Islamic mortgage to be good and the conventional mortgage also to be good. Islamic mortgages and conventional mortgages are perfect substitutes for each other, only price matters. From table 7.2, above, 40 percent of the respondents are considered to be conventional demanders for an Islamic mortgage. Forty percent of the respondents stated that they would be willing to take out an Islamic mortgage only if the cost is similar to or less than a conventional mortgage. The respondents would demand an Islamic mortgage if it was sufficiently competitive vis-à-vis a conventional mortgage. The respondents considered religious and other factors in choosing an Islamic mortgage. Recent studies indicate that the religious factor is not enough to encourage Muslims to use Islamic banking facilities (Rosly and Abu Bakar, 2003). In this situation, however, the respondents consider an Islamic mortgage to be as good as a conventional mortgage. In this case Islamic mortgages and conventional mortgages are perfect substitutes for each other, only the price matters.

7.4.1.2 Pent-up demand

Pent-up demanders consider religious and other factors in choosing a mortgage product and would be expected to switch to an Islamic mortgage if it is sufficiently competitive vis-à-vis a conventional mortgage.

Table 7.2 shows that 18 percent of the respondents were considered pending demanders, as they would take an Islamic mortgage if leading Islamic scholars approved it. People buy Islamic mortgage products if they feel sure they are fully *Shari'a* compliant. *Shari'a* law plays a pivotal role in consumer confidence; in general greater coordination of the *Shari'a* standards would further enhance the profile of Islamic banking and attract more customers (Al Zaaibi, 2006). In the pent-up demanders situation the preferences of respondents or demanders can be described as: Islamic mortgages are considered to be good and conventional mortgages are also good. Islamic mortgages and conventional mortgages are substitutes for each other but consumers' preferences are tilted in favour of Islamic mortgages.

7.4.1.3 Staunch demand

Staunch demanders of Islamic mortgages are expected never to enter into conventional mortgage contracts. This type of respondent may have actually been prevented from using the UK financial systems and not had a chance to get a foot on the property ladder. Those respondents may well be financially and socially excluded. Nonetheless, eight percent of the respondents are staunch demanders of Islamic mortgages, as they are willing to take out an Islamic mortgage no matter what the cost, even if it is much more expensive than the conventional mortgage. In this situation the respondents or the demanders are assumed to be very conservative in their religion; their preferences can be described as Islamic mortgage being good while the conventional mortgage is bad.

This is clear evidence that Islamic finance in the UK is a 'supply–led' phenomenon. Hence, Islamic mortgage providers have to generate demand for their products, as there will not be an automatic demand for their services.

7.4.2 The Ineffective Demand

If a respondent does not believe in the prohibition of an interest-based mortgage system, it is very unlikely that he will take out or switch to an Islamic mortgage. Hence, a non-believer in the prohibition of interest should not be taken as having some effective demand for an Islamic mortgage. Table 7.2 shows that nine percent of the respondents are not willing to take out an Islamic mortgage, they are most likely not practising Muslims and therefore indifferent of the prohibition of interest.

Thus, an estimation of demand for Islamic mortgages in the UK should take into consideration the above different attitudes towards Islamic mortgages. In light of the above findings Islamic mortgage providers have to better understand the needs, preferences and behaviour of their target-group customers in order to stay in the game.

In the future, with an increase in awareness of Islamic mortgages, non-Muslims may also consider Islamic mortgages. This has indeed been a trend in Malaysia where a rising number of Chinese are using Islamic financial services, after an initial unwillingness which lasted over a decade. The demand for Islamic mortgages in Britain is not expected to follow this fashion however, as non-Muslims would be unwilling to pay higher premium for Islamic mortgages.

7.4.3 Factors Affecting the Demand for Islamic Mortgages

It is important to find out what factors might influence the demand for Islamic mortgages in the UK. Hence, this section aims to answer the following research question:

Research question (4) What are the factors for choosing Islamic mortgages?

For this purpose we carry out cross tabulations between the willingness to take out Islamic mortgages and other variable factors as follows:

7.4.3.1 Marital status

From the chi-square test there are significant statistical differences in the distributions of the frequency of the relationship between future demand for Islamic mortgages and marital status of the respondents with chi-square value of 33,50, degree of freedom (df) 15 and significant p-value less than .05 (.004). Hence, these two variables are associated, in other words the willingness to take out Islamic mortgages (the potential demand for Islamic mortgages) depends on the marital status of the Muslim household.

Table 7.3 Chi-Square Test

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	33.504(a)	15	.004
Likelihood Ratio	28.648	15	.018
Linear-by-Linear Association	2.493	1	.114
N of Valid Cases	250		

a 14 cells (58.3%) have expected count less than 5. The minimum expected count is .14.

Table 7.4 Cross Tab Willingness to Take Out Islamic Mortgage and Marital Status

			Martial Status				Total
			Married	Single	Other with children	Other without children	
Willingness of taking Islamic mortgage	Yes, only if the cost are similar or less than conventional	Count	63	30	6	0	99
		% Within Marital Status	45.7%	30.9%	54.5%	.0%	39.6%
	Yes, no matter the cost, even if it is much more expensive	Count	12	7	0	2	21
		% Within Marital Status	8.7%	7.2%	.0%	50.0%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	22	22	1	0	45
		% Within Marital Status	15.9%	22.7%	9.1%	.0%	18.0%
	No, Islamic mortgages are not possible	Count	8	3	1	1	13
		% Within Marital Status	5.8%	3.1%	9.1%	25.0%	5.2%
	No, whatever the difference between Islamic mortgage and con	Count	2	5	2	0	9
		% Within Marital Status	1.4%	5.2%	18.2%	.0%	3.6%
	Not sure	Count	31	30	1	1	63
		% Within Marital Status	22.5%	30.9%	9.1%	25.0%	25.2%
	Total	Count	138	97	11	4	250
		% Within Marital Status	100.0%	100.0%	100.0%	100.0%	100.0%

Table 7.4, above, of the cross tabulation of willingness to take out an Islamic mortgage and marital status shows that 70 percent of those who are married are

willing to take out an Islamic mortgage compared with 61 percent of the single respondents, while of those who are divorced and/or widows with children 64 percent of them are willing to take out an Islamic mortgage compared with 50 percent of those who are widows or divorced without children.

7.4.3.2 Intention to buy a home in the next three years

From the chi-square test there is significant statistical differences in the distributions of the frequency of the relationship between future demand for an Islamic mortgage and the respondents' intention to buy a home in the next three years, with chi-square value of 39.407, degree of freedom (df) 10 and p-value of .000 that is less than .05.Hence, these two variables are associated; in other words the decision to take out an Islamic mortgage (the demand for Islamic mortgages) depends on the Muslim householder's intention to buy in the next three years.

Table 7.5 Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	39.407(a)	10	.000
Likelihood Ratio	42.755	10	.000
Linear-by-Linear Association	14.473	1	.000
N of Valid Cases	190		

a 8 cells (44.4%) have expected count less than 5. The minimum expected count is 1.98.

From the cross tabulation in table 7.6 below we can see that none of those who have the intention of buying a home in the next three years said no to the Islamic mortgage. Conversely, 67 percent of those who are not willing to take out Islamic mortgages because Islamic mortgages are not possible and 63 percent of those who decided never to take out Islamic mortgages whichever of the two prices is cheaper do not intend to buy a home in the next three years. Also the table shows that 49 percent of the pending demanders of Islamic mortgages (those who would be willing to buy if a leading scholar approved it), 45 percent of the conventional demanders (willing to take out an Islamic mortgage if the cost is similar to or less than the conventional mortgage) and 36 percent of the staunch demanders (willing to take out an Islamic mortgage no matter what the cost, even if it is more expensive than the conventional one) have the intention of buying a home in the next three years. Lastly 63 percent of those who are not sure about their willingness to take out an Islamic mortgage are also not sure about their intention to buy in the next three years.

Table 7.6 Cross Tabulation Intention to Buy a Home in the Next Three Years and Willingness to Take Out an Islamic Mortgage

			Willingness to take Islamic mortgage						Total
			Yes, only if the cost is similar to or less than conventional	Yes, no matter the cost, even if it is much more expensive	Yes, if leading Islamic scholars have approved it	No, Islamic mortgages are not possible	No, whatever the difference between Islamic mortgage and con	Not sure	
Intention to buy home in the next 3 years	Yes	Count	32	5	18	0	0	6	61
		% Within willingness to take out Islamic mortgage	45.1%	35.7%	48.6%	.0%	.0%	11.8%	32.1%
	No	Count	11	4	8	6	5	13	47
		% Within willingness to take out Islamic mortgage	15.5%	28.6%	21.6%	66.7%	62.5%	25.5%	24.7%
	Not sure	Count	28	5	11	3	3	32	82
		% Within Willingness to take out Islamic mortgage	39.4%	35.7%	29.7%	33.3%	37.5%	62.7%	43.2%
	Total	Count	71	14	37	9	8	51	190
		% Within Willingness to take out Islamic mortgage	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

7.4.3.3 Preferred Islamic mortgages product

From the chi-square test there are significant statistical differences in the distribution of the frequency of the relationship between the potential demand for Islamic mortgages and the respondents' preferences for Islamic mortgage products since the Pearson chi–square value is 47.427 with 20 degree of freedom (df) and significant p-value of less than .05 *i.e.* 0.001. Hence, these two variables are associated; in other words the willingness to take out an Islamic mortgage (the demand for Islamic mortgages) depends on the respondents preferences for Islamic mortgage products.

Table 7.7 Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	47.427(a)	20	.001
Likelihood Ratio	50.048	20	.000
Linear-by-Linear Association	9.896	1	.002
N of Valid Cases	250		

a 17 cells (56.7%) have expected count less than 5. The minimum expected count is .47.

From the table of cross tabulation between preferred Islamic mortgage products and willingness to take out an Islamic mortgage (table 7.8 below) the *Ijarah* and the Diminishing *Musharakah* mortgage products are preferred by the pending demanders of Islamic mortgages who would be willing to take out an Islamic mortgage if leading scholars approved it. While *Murabahah* mortgage products are preferred by the conventional demander who are willing to take out an Islamic mortgage if the cost is similar to or less than a conventional mortgage.

Interestingly, *Ijarha* attracted no one from the conservative Muslims willing to take an Islamic mortgage no matter the cost even if it is much more expensive. This is different to the assumptions of some researchers who thought *Ijara* was more *Shari'a*-'pure' and would attract more conservative Muslims (Maurer, Bill, 2006).

Table 7.8 Cross Tab Preference for Islamic Mortgage Products and Willingness to take out an Islamic Mortgage

			Willingness to take out Islamic mortgage						Total
			Yes, only if the cost are similar to or less than conventional	Yes, no matter the cost, even if it is much more expensive	Yes, if leading Islamic scholars have approved it	No, Islamic mortgages are not possible	No, whatever the difference between Islamic mortgage and con	Not sure	
Preferred Islamic finance product for mortgage	*Ijarah* (redeemable lease)	Count	5	0	6	0	0	2	13
		% Within Willingness to take Islamic mortgage	5.1%	.0%	13.3%	.0%	.0%	3.2%	5.2%
	Murabahah (instalments credit purchase)	Count	19	7	9	0	1	4	40
		% Within Willingness of taking IM	19.2%	33.3%	20.0%	.0%	11.1%	6.3%	16.0%
	Diminishing *Musharakah* (declining balance partnership)	Count	10	1	9	0	0	2	22
		% Within Willingness to take IM	10.1%	4.8%	20.0%	.0%	.0%	3.2%	8.8%
	Other	Count	5	3	2	0	2	4	16
		% Within Willingness to take IM	5.1%	14.3%	4.4%	.0%	22.2%	6.3%	6.4%
	I do not know.	Count	60	10	19	13	6	51	159
		% Within Willingness to take IM	60.6%	47.6%	42.2%	100.0%	66.7%	81.0%	63.6%
	Total	Count	99	21	45	13	9	63	250
		% Within Willingness IM	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

7.4.3.4 The preferred Islamic mortgage provider

From the chi-square test there are significant statistical differences in the distributions of the frequency of the relationship between the potential demand for Islamic mortgages and the respondents' preferences of Islamic mortgages provider since the Pearson chi –square value is 34.552 with 15 degree of freedom (df) and significant p-value of .003 which is less than .05. Hence, these two variables are associated; in other words the willingness to take out an Islamic mortgage (the potential demand for Islamic mortgages) depends on the respondents' preferences of Islamic mortgages provider.

Table 7.9 Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	34.552(a)	15	.003
Likelihood Ratio	36.585	15	.001
Linear-by-Linear Association	2.231	1	.135
N of Valid Cases	247		

a 10 cells (41.7%) have expected count less than 5. The minimum expected count is .91.

The cross tabulation table 7.10 between the willingness to take out an Islamic mortgage and preferred Islamic mortgage provider shows that the conventional and pent-up demander of Islamic mortgages prefers the stand-alone UK Islamic Bank and then the Islamic windows offered by high street banks and building societies rather than a foreign pure Islamic bank. Conversely, staunch demanders (conservative Muslims) prefer the stand-alone UK Islamic Bank and then a non-UK Islamic bank and the last resort for them is the Islamic window offered by high street banks.

Table 7.10 the Preferred Islamic Mortgages Provider and Willingness to take out an Islamic Mortgage

			Willingness of taking Islamic mortgage						Total
			Yes, only if the cost is similar to or less than conventional	Yes, no matter the cost, even if it is much more expensive	Yes, if leading Islamic scholars have approved it	No, Islamic mortgages are not possible	No, whatever the difference between Islamic mortgage and con	Not sure	
The preferred Islamic mortgage provider	Stand – alone UK Islamic bank	Count	38	9	28	3	3	38	119
		% Within Willingness to take Islamic mortgage	38.4%	45.0%	63.6%	23.1%	33.3%	61.3%	48.2%
	Stand – alone non-UK Islamic bank	Count	12	5	1	2	1	4	25
		% Within Willingness to take IM	12.1%	25.0%	2.3%	15.4%	11.1%	6.5%	10.1%
	Islamic window offer by major high street bank and building	Count	32	4	14	3	2	9	64
		% Within Willingness to take IM	32.3%	20.0%	31.8%	23.1%	22.2%	14.5%	25.9%
	Others	Count	17	2	1	5	3	11	39
		% Within Willingness to take IM	17.2%	10.0%	2.3%	38.5%	33.3%	17.7%	15.8%
	Total	Count	99	20	44	13	9	62	247
		% Within Willingness to take IM	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

7.4.3.5 Awareness

From the chi-square test there are significant statistical differences in the distribution of the frequency of the relationship between the potential demand for Islamic mortgages and the respondents' awareness of Islamic mortgages since the Pearson chi –square value is 55.565 with 10 degree of freedom (df) and significant p-value of .000 which is less than .05. Hence, these two variables are associated; in other words the willingness to take out an Islamic mortgage (the potential demand for Islamic mortgages) depends on the respondents' awareness of the benefits of Islamic mortgages in the UK.

Table 7.11 Chi-Square Tests

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	55.565(a)	10	.000
Likelihood Ratio	53.530	10	.000
Linear-by-Linear Association	18.975	1	.000
N of Valid Cases	250		

a 6 cells (33.3%) have expected count less than 5. The minimum expected count is 2.09.

From the cross tabulation table 7.12 below it is clear that the potential demand for Islamic mortgages lies within Muslim households who are very aware of Islamic mortgages. Awareness of the benefits of Islamic mortgages will push up the demand.

Table 7.12 Willingness to Take out an Islamic Mortgage and Knowledge of differences between Islamic and Conventional Mortgages

			Knowledge of differences between Islamic and conventional mortgages			Total
			Yes	No	Not sure	
Willingness to take out an Islamic mortgage	Yes, only if the cost is similar to or less than conventional	Count	56	24	19	99
		% of Total	22.4%	9.6%	7.6%	39.6%
	Yes, no matter the cost, even if it is much more expensive	Count	10	6	5	21
		% of Total	4.0%	2.4%	2.0%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	35	5	5	45
		% of Total	14.0%	2.0%	2.0%	18.0%
	No, Islamic mortgages are not possible	Count	3	9	1	13
		% of Total	1.2%	3.6%	.4%	5.2%
	No, whatever the difference between Islamic mortgage and con	Count	4	0	5	9
		% of Total	1.6%	.0%	2.0%	3.6%
	Not sure	Count	18	14	31	63
		% of Total	7.2%	5.6%	12.4%	25.2%
	Total	Count	126	58	66	250

7.4.3.6 Income

To take the descriptive analysis further the cross tabulation between willingness to take out an Islamic mortgage and Muslim households' income were run and the results are presented in the table below. The output shows that the highest potential demand for the Islamic mortgages is among the income group of £31k – £40k, as 79.2 percent from this income group are willing to take out an Islamic mortgage. Of those who are in the income group of over £41k, 75 percent of them are willing to take out an Islamic mortgage. It is worth mentioning that 25 percent of those are considered to be staunch future demanders of Islamic mortgages and the remaining 25 percent believe that Islamic mortgages are not possible.

Table 7.13 Cross Tab Willingness to take out an Islamic Mortgage and Income

			Income					Total
			10k and under	11k - 20k	21k - 30k	31k - 40k	Over 41k	
Willingness to take out Islamic mortgage	Yes, only if the cost is similar to or less than conventional	Count	37	25	21	14	2	99
		% Within Income	38.9%	32.1%	42.9%	58.3%	50.0%	39.6%
	Yes, no matter the cost, even if it is much more expensive	Count	8	3	8	1	1	21
		% Within Income	8.4%	3.8%	16.3%	4.2%	25.0%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	16	18	7	4	0	45
		% Within Income	16.8%	23.1%	14.3%	16.7%	.0%	18.0%
	No, Islamic mortgages are not possible	Count	4	5	1	2	1	13
		% Within Income	4.2%	6.4%	2.0%	8.3%	25.0%	5.2%
	No, whatever the difference between Islamic mortgage and conventional	Count	3	3	2	1	0	9
		% Within Income	3.2%	3.8%	4.1%	4.2%	.0%	3.6%
	Not sure	Count	27	24	10	2	0	63
		% Within Income	28.4%	30.8%	20.4%	8.3%	.0%	25.2%
	Total	Count	95	78	49	24	4	250
		% Within Income	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

7.4.3.7 Employment

To take the descriptive analysis further the cross tabulation between willingness to take out an Islamic mortgage and Muslims households' employment status were run; the results are presented in table 7.14 below. The output shows that 39 percent of the working households, 40 percent of the retired households and 41 percent of the unemployed households are conventional demanders of Islamic mortgages (willing to take out an Islamic mortgage only if the cost is similar to or less than the conventional mortgage). Conversely, nine percent of the working respondents, seven percent of the unemployed respondents and none of the retired respondents are staunch demanders of Islamic mortgages in the future (willing to take out an Islamic mortgage no matter the cost even if it is more expensive). On the other hand, 17 percent of the working respondents, 20 percent of the retired respondents and 24 percent of the unemployed respondents are classified as future pending demanders of Islamic mortgages (willing to take out an Islamic mortgage if a leading scholar approves it.).

Table 7.14 Cross Tab Willingness to Take Out an Islamic Mortgage and Employment

			Employment			Total
			Working, for how many years have you been working	Retired, please specify how many years since you retired	Neither	
Willingness to take out an Islamic mortgage	Yes, only if the cost is similar to or less than conventional	Count	78	4	17	99
		% Within Employment	39.4%	40.0%	40.5%	39.6%
	Yes, no matter the cost, even if it is much more expensive	Count	18	0	3	21
		% Within Employment	9.1%	.0%	7.1%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	33	2	10	45
		% Within Employment	16.7%	20.0%	23.8%	18.0%
	No, Islamic mortgages are not possible	Count	9	2	2	13
		% Within Employment	4.5%	20.0%	4.8%	5.2%
	No, whatever the difference between Islamic mortgage and con	Count	8	0	1	9
		% Within Employment	4.0%	.0%	2.4%	3.6%
	Not sure	Count	52	2	9	63
		% Within Employment	26.3%	20.0%	21.4%	25.2%
	Total	Count	198	10	42	250
		% Within Employment	100.0%	100.0%	100.0%	100.0%

7.4.3.8 Qualifications

Table 7.15 below shows that 63 percent of those who have no formal qualifications are willing to take out an Islamic mortgage, 69 percent, 73 percent and 79 percent of those holding GCSE, A level and professional qualifications respectively are willing to take out an Islamic mortgage.

These observations indicate a positive relationship between the willingness to take out an Islamic mortgage (potential demand) up to professional level. On the other hand, those who hold a first degree and Master or PhD degrees make up 62 percent and 54 percent respectively of those willing to take out an Islamic mortgage. In other words those who have no formal qualifications and those who are educated up to professional level are most likely to have a greater demand than those who are educated up to Master and PhD level. One possible reason for this phenomenon is that the former are more aware religiously than the latter.

Table 7.15 Cross Tab Willingness to take out an Islamic Mortgage and Qualifications

			Qualifications						Total
			No formal qualification	GCSE/ O levels	A levels	Professional qualifications (in Accounting,	BA or B.Sc.	MA or PhD	
Willingness to take out Islamic mortgage	Yes, only if the cost is similar to or less than CM	Count	10	13	21	10	24	21	99
		% Within Qualification	52.6%	31.0%	37.5%	41.7%	38.1%	45.7%	39.6%
	Yes, no matter the cost, even if it is much expensive ThanCM	Count	0	4	6	4	5	2	21
		% Within Qualification	.0%	9.5%	10.7%	16.7%	7.9%	4.3%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	2	12	14	5	10	2	45
		% Within Qualification	10.5%	28.6%	25.0%	20.8%	15.9%	4.3%	18.0%
	No, Islamic mortgages are not possible	Count	1	5	3	1	3	0	13
		% Within Qualification	5.3%	11.9%	5.4%	4.2%	4.8%	.0%	5.2%
	No, whatever the difference between IM	Count	1	1	3	0	1	3	9
		% Within Qualification	5.3%	2.4%	5.4%	.0%	1.6%	6.5%	3.6%
	Not sure	Count	5	7	9	4	20	18	63
		% Within Qualification	26.3%	16.7%	16.1%	16.7%	31.7%	39.1%	25.2%
	Total	Count	19	42	56	24	63	46	250
		% Within Qualification	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

7.4.3.9 Age

From the cross tabulation in table 7.16 below we observe that of those who are under 25 years old 61 percent of them are willing to take out an Islamic mortgage, compared to 59 percent, 71 percent, 72 percent and 80 percent of the age groups 26-35years, 36-45 years, 46-55 years and 56-65 years respectively. The older the respondent the more likely he is to be willing to take out an Islamic mortgage. Hence, there may be a positive relationship between the potential demand for Islamic mortgages and the age of the respondents.

Table 7.16 Cross Tabulation between Willingness to Take out an Islamic Mortgage and Age

			Age						Total
			25 and under	26 – 35	36 – 45	46 - 55	56 - 65	66 and +	
Willingness to take out an Islamic mortgage	Yes, only if the cost is similar to or less than conventional	Count	18	26	33	12	9	1	99
		% Within Age	35.3%	32.5%	46.5%	37.5%	60.0%	100.0%	39.6%
	Yes, no matter the cost, even if it is much more expensive	Count	4	7	6	3	1	0	21
		% Within Age	7.8%	8.8%	8.5%	9.4%	6.7%	.0%	8.4%
	Yes, if leading Islamic scholars have approved it	Count	9	14	12	8	2	0	45
		% Within Age	17.6%	17.5%	16.9%	25.0%	13.3%	.0%	18.0%
	No, Islamic mortgages are not possible	Count	4	4	2	2	1	0	13
		% Within Age	7.8%	5.0%	2.8%	6.3%	6.7%	.0%	5.2%
	No, whatever the difference between Islamic mortgage and con	Count	1	4	2	1	1	0	9
		% Within Age	2.0%	5.0%	2.8%	3.1%	6.7%	.0%	3.6%
	Not sure	Count	15	25	16	6	1	0	63
		% Within Age	29.4%	31.3%	22.5%	18.8%	6.7%	.0%	25.2%
	Total	Count	51	80	71	32	15	1	250
		% Within Age	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

The above analysis shows that five factors, namely marital status, the intention to buy a home in three years, preference for Islamic mortgage products, preference for Islamic mortgage providers and the awareness of the benefits of Islamic mortgages are significant determinants of the demand for Islamic mortgages. Other factors like income, employment, qualifications and age are not statistically significant.

There is also evidence that demand for Islamic mortgages is higher in northern cities of the UK than southern as Muslim communities in the north are more close-knit and conservative and more influenced by the religious factor (Dar, 2004). Therefore, regional location is a very important consideration in marketing for Islamic mortgage providers.

7.5 THE PERCEPTION ABOUT ISLAMIC MORTGAGES

This section discusses respondents' perceptions of Islamic mortgages in terms of their attraction to the respondents, role in homeownership for the low income group, services charged, and preferences over conventional mortgages, credibility, and as a solution to avoiding interest. Hence, this section aims to answer the following research question:

Research question (5) What is UK Muslims' perception of Islamic Mortgages?

In order to answer this researches question a couple of survey questions regarding the above mentioned issues have been asked of the respondents, for which the results are presented as follows:

7.5.1 Religious Affiliation

Table 7.17 shows that more than 75 percent of respondents agreed that the religious factor is the most important reason behind the attraction of Islamic mortgages, compared with 8.4 percent who disagreed while 15.7 percent were uncertain about their perception. The table also shows that if the significance of chi square goodness of fit test is lower than 0.05, then the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data.

Table 7.17 the Perception of the IM in Terms of Religious Factor

	VALID	FREQUENCY	PERCENT
The religious factor is the most important reason behind the attraction of Islamic mortgage	Strongly agree	117	46.6
	Agree	73	29.3
	Uncertain	39	15.7
	Disagree	19	7.6
	Strongly disagree	2	.8
	Total	250	100.0

chi-sq 166.080 df 4 Asym.Sig .000

The main concern of the Muslim community is its desire to avoid dealing in *riba*. As far as money is concerned *riba* is loosely translated as interest. Whether this translation is accurate or not, whether the Arabic word *riba* and the English word interest mean the same thing, is the subject of a long-standing debate (Fadel, Mohammad, 2008). To avoid *riba* (interest) in their dealings, a banking system designed to address their concerns has to take into account this main concern as well as other factors. Hence, the religious factor is very important but not the only factor in financial decisions.

7.5.2 The Role of Islamic Mortgages in Home ownership among Low Income Muslim Households:

Considering the role of Islamic housing finance in bridging the gap in homeownership among the Muslim community in the UK, it has no significant role in helping low-income Muslim households get onto the property ladder. As shown in table 7.18 the majority of respondents, with significant chi-square level, agreed that Islamic mortgages are very expensive and do not help the low-income group. It shows that 26 percent and 24 percent of them agreed and strongly agreed with this statement respectively. By contrast, eight percent disagreed and only four percent strongly disagreed with this statement. In addition 38 percent were uncertain about their perceptions. These differences are statistically significant, as the chi-square value is below 0.05.

Table 7.18 the Perception about the Islamic Mortgage in Terms of Role in Home ownership

	VALID	FREQUENCY	PERCENT
The expensiveness of Islamic mortgage does not help the low income group	Strongly agree	61	24.1
	Agree	64	25.7
	Uncertain	95	38.2
	Disagree	19	7.6
	Strongly disagree	11	4.4
	Total	250	100.0

Chi-sq 96.442 df 4 Asymp.Sig .000

7.5.3 The Cost of Islamic Mortgages

In order to meet the ever demanding customer's needs Islamic mortgage providers will need not only to develop a pricing strategy but to develop a strategy around the fundamental components of product pricing, product development, product distribution and delivery channels and last but not least the branding and promotion of Islamic mortgage products. In developing mortgage product pricing and the mortgage products developments there are five key areas that need to be tackled carefully:

1) Getting adequate information on customer and market profile.

2) Developing a better understanding of customers' needs and behaviours.

3) Development of comprehensive and innovative Islamic mortgage products that can be tradable in the capital market, in other words used as capital market instruments so as to link the Islamic mortgage market with the capital market.

4) The provision of sufficient numbers of well-trained and qualified staff and experts.

5) The provision of a broader range of Islamic mortgage products and services need attention.

The majority of Muslim households' respondents perceive the cost of Islamic mortgages to be very expensive requiring high service charges, as clearly shown in table 7.19. It shows that 20.6 percent of them strongly agree and 22.6 percent agree compared with just four percent who strongly disagree and only 10.1 percent who disagree with the same statement. On the other hand 42.7 percent were uncertain in their perception of the cost of the Islamic mortgage. This result is statistically significant as shown in the table the chi-square goodness–fit–test is less than .005.

Table 7.19 the Perception about the Islamic Mortgage in Terms of Cost and Services charged

	VALID	FREQUENCY	PERCENT
Islamic mortgage is very expensive and requires high service charges	Strongly agree	53	20.6
	Agree	56	22.6
	Uncertain	106	42.7
	Disagree	25	10.1
	Strongly disagree	10	4.0

Chi-sq 108.815 df 4 Asymp.Sig .000

Hence, the higher cost of Islamic home finance contributes to the factors hindering the uptake of Islamic mortgages in the UK. For example, the Islamic home mortgage from Lloyds TSB is more expensive than the conventional mortgage from the same bank. Likewise *Amanah's* home financing is more expensive than HSBC's conventional mortgage. Clearly respondents have been put off Islamic mortgages by high costs. This, however, somewhat reflects the limited scale of Islamic mortgages, therefore higher costs per mortgage approved. There are other factors contributing to the high cost of Islamic mortgages, *e.g.* Islamic mortgages are a niche market, which involves high marketing and administration costs. Islamic mortgages require 100 percent capital adequacy by the Financial Services Authority (FSA) which is more than conventional mortgages which require only 50 percent capital adequacy. In addition to this, monitoring Islamic mortgages to be *Shari'a*-compliant involves extra cost, not least to pay the fees and expenses of the scholars of the *Shar'ia* committee.

7.5.4 Premium Pricing

Premium pricing is a deliberate setting of high prices for a product or service to emphasize its quality or exclusiveness (bnet, 2009). Some firms use this strategy which is also known as prestige pricing. This involves setting a high price so that status-conscious consumers will be attracted to the product and buy it, since a high price is an indication of quality and prestige.

Certainly the cost of a mortgage is not the only factor determining the level of business, as the majority of respondents believe that Islamic mortgages should be taken out even if they are more expensive than conventional mortgages. 17 percent strongly agreed and 19 percent of them agreed, in contrast with eight percent and 17 percent who strongly disagreed and disagreed respectively. In addition 39 percent were uncertain whether to pay the premium pricing or not for the Islamic mortgage.

Table 7.20 Perception of the Islamic Mortgage in Terms of Pricing

	VALID	FREQUENCY	PERCENT
Islamic mortgage should be taken even if it is more expensive than conventional mortgage	Strongly agree	44	17.3
	Agree	47	18.9
	Uncertain	96	38.6
	Disagree	43	17.3
	Strongly disagree	20	8.0
	Total	250	100.0

Chi-sq 62.707 df 4 Asymp.Sig .000

The reality is that the potential willingness of Muslim households to pay more for Islamic mortgages found resistance in the experience of the *Al-Ahli* United Bank There is lack of appreciation among many Muslims about the necessity of paying premium pricing for an Islamic mortgage. From the previous discussions of the experience of HSBC *Amanah* the issue seems to be the size of the premium, which greater competition in the market should reduce. If the competition does not bring just and fair prices the *Shari'a* provides moral and ethical norms and rules of behaviour that should be observed by all participants in the market place. Demand in itself does not determine price, price ought to be determined by adherence to all Islamic codes of ethics. Prices must be kept at a reasonable level to make basic goods and services available to the public and governments can intervene when there are distortions.

7.5.5 The Credibility of Islamic Mortgages

The respondents may wonder about the real difference between Islamic mortgages and conventional ones. As has been discussed in Chapter 4 the payments are structured, in the same way and the figures work out pretty much the same, yet the components are called by other names or set by other criteria. This is a key question for the respondents as potential clients. According to the results shown in table 7.21, more than one third of the respondents agreed with the statement that the Islamic mortgage is the same as the conventional mortgage except that it is dressed up as rent; 10 percent of them strongly agree and 24 percent agree. In contrast 17 percent of them disagree and 5 percent strongly disagree. However, 45 percent are uncertain. This result is statistically significant as the table shows the chi-square goodness of fit-test is less than .005.

Table 7.21 the Perception about the Islamic Mortgage in Terms of Credibility

	VALID	FREQUENCY	PERCENT
Islamic mortgage is a similar as interest conventional mortgage but dressed up as a rent	Strongly agree	24	9.6
	Agree	59	23.7
	Uncertain	112	44.6
	Disagree	42	16.9
	Strongly disagree	13	5.2
	Total	250	100.0

Chi-sq 118.691 df 4 Asymp.Sig .000

This is an important question for Islamic banking professionals and they have debated it endlessly. In fact that debate is equally important as the actual Islamic mortgage product itself. One of the main important forums for these discussions is the Islamic Banking and Finance Internet listserv that has operated since 1998 and is well known internationally among Islamic banking professionals. A growing chorus of critics argues that *Shari'a* does not forbid all forms of interest. Furthermore, they argue, that some of the bankers, lawyers and clerics who draft and approve "interest-free" products are profiting from the pious with arrangements that look a lot like conventional ones. Mahmoud Amin El-Gamal, chair of the Islamic economics department at Rice University, argues that such transactions amount to a bait and switch. "The whole is, I want to lend but I don't want to call interest 'interest,' "said El-Gamal. He says such transactions cost more than other conventional financial arrangements and hurt Muslim consumers. According to EL-Gamal "They're trapped because they're told they'll fry in hell if they go to regular banks," Moreover, El-Gamal says obedience to the form of the contract often supersedes the spirit of Islamic economic values, such as serving the poor. He also argues that because conventional mortgages are secured by a physical asset, namely the house that is usually the only asset the lender can repossess if the borrower fails to repay, such loans should not be considered the equivalent of making money by renting money (El-Gamal, 2006).

The Islamic Finance Industry counters that. For example Taha Abdul-Basser, an Islamic law scholar of the Islamic Finance Project at Harvard Law School, US, said that 'Even if some financial transactions serve the same purpose as interest, that doesn't mean they are forbidden by Islam'.

Hussam A. Qutub, a spokesman for Guidance Financial Group, an Islamic bank that offers interest-free mortgages based in Reston, USA cited by (Sacirbey, 2007) said that "It's possible, as it is in many ethical and legal systems, for two different actions to have the same outcome but, because of the way they're done, for one to be wrong or illegal in that ethical or legal system, and for the other to be permissible or lawful," Islam draws a difference between monetary lending agreements and agreements based on commodities. He also said "We're trying to reach the same end result that other financial organizations are trying to reach, which is putting people in homes,". He added "But how are you going to get me there, that's where we differ." The two systems may serve some of the same functions, but there's a legal difference between the two, in terms of inheritance and taxes. Some of the Islamic banker professionals have a ready answer; they think it's the form of the contract, which is different. Their analogy assumed a man and woman are in love and have a child. If they have a certain form of contract (marriage license), their offspring are legitimate. If they don’t, they aren’t. In other words it’s like the difference between a wife and a live-in girlfriend.

With regards to the question about whether a conventional mortgage is *riba*, the Islamic banker professionals counter that, they firmly believe it is *rabawi* and not permissible. This is very clear when the mortgage loan process is closely examined as follows:

1. The client goes to his bank or mortgage broker and applies for a loan.

   a. The loan, at this point, is unspecific and unconnected to a property.

   b. The client qualifies for a loan amount based on how much he or she earns and what his or her credit score is; some ratios may be taken into account.

   c. The loan is "pre-approved" subject to certain conditions including an appraisal of a property that will secure the loan.

2. The client contracts to buy a property.

3. Any loan conditions are met and the property appraised.

4. At closing the lender is required by law to fund the money on the client's behalf to an independent party to prevent fraud and the independent party manages the closing; delivering the client's down payment, the loan proceeds and any other requirements to the seller in exchange for title to the property.

5. At closing, there are many documents, depending upon the state in which the loan is made; three of them are contracts:

   a. The Purchase Contract: This is the contract conveying the property from a buyer to a seller subject to specific conditions and for financial consideration.

   b. The Promissory Note Contract: This is the evidence of a loan or debt and the client promises to pay a set rate of interest for a specific period. The client also promises to pay penalty interest at a specific rate if he is late in making his monthly payments. If he does not pay for three months, the lender will take the note to court in order to seize the property under the terms of the next contract.

c. The Mortgage Contract: this is a specific lien on the house, mandating specific behaviour by the grantor of the security, the client. When the note is presented to a court, the mortgage allows for the note holder to seize the property and take title.

In summary this is pure money lending where the client is contracted to borrow money.

Furthermore, according to the Islamic *Fiqh* Academy(2000) Resolution No.109(3/12) on penalty provision, if a contract contains a prohibited provision, such as a default interest rate or other inappropriate penalty which penalises the client for hardship, then the contract is considered to be prohibited even if the client never incurs the hardship.

Some writers criticize the Islamic mortgage products on offer by high street banks arguing that there are no significant differences between the Islamic mortgage and the conventional mortgage. Both involve *gharar* (ambiguity) of the contract, because the nature of the contract is not very clear, whether it is a lease contract, a purchase contract or a combination of the two. The ambiguity in itself makes the contract of the Islamic mortgage impermissible (*haram*). Furthermore, a combined contract then is prohibited according to the *Hadith* (saying) of the Prophet (peace and blessing of *Allah* be upon him) (Haddad, 2004). However, Hood Bradford of the Islamic University of Medina counters this argument by asserting the provisional nature of *Ijtihad.* In Islamic *Fiqh* (jurisprudence) lease which ends in ownership has been differed over by all the major schools of *Fiqh*, because it is an area of *Ijtihad*, where there are no clear cut-right and wrong answers. It is not logical to criticize the *Ijtihad* of a certain school of thought over that of another when the whole issue is one of *Ijtihad.*

Basically, due to lack of awareness and information respondents may confuse the mark-up in the *Murabaha* mortgage with interest. Also, the immediate purchase and resale of the property by the bank that are unrelated to the payment period looks like a manipulation of the contract. This might explain the criticism of *Murabaha* by wealthy British Muslims (Dar, Hamayoun, 2004).

Ijara and *Ijara wa Iqtina* mortgage models are more appropriate for Islamic housing finance, although, there is concern when the home occupant is not the owner. There will be discrepancies between the rent paid to the bank by the homeowner and the rent paid to the homeowner by the renter as the first will be fixed to the LIBOR (London Inter Bank Offer Rate) and the second will be fixed to the rent market.

7.5.6 Islamic Mortgages as a Solution for Social Exclusion

The issue of social exclusion of British Muslims is addressed in this section. As we saw earlier religion influences decision-making in the choice of the Islamic mortgage, as interest is prohibited in Islam. This may explain the social exclusion of British Muslims, especially before 2003 when there was no Islamic mortgage on offer by the financial system.

Respondents were asked to what extent they agree with the statement that the Islamic mortgage is a solution for Muslims which high street banks could have offered years ago, but at least it is step in the right direction towards avoiding dealing with interest-based products. Table 7.22 shows that more than half of the respondents agree with this statement, 20 percent of them strongly agree and 35 percent agree. In contrast only 10 percent disagree seven percent of them disagree and three percent strongly disagree. On the other hand 35 percent of respondents are uncertain. This result is statistically significant as the table also shows the chi-square goodness of fit-test to be less than .005.

Table 7.22 Perception of the Islamic Mortgage in Terms of Solution to Interest

	VALID	FREQUENCY	PERCENT
Islamic mortgage is a perfect solution for Muslim communities and it is the first step in avoiding paying interest	Strongly agree	48	19.3
	Agree	89	35.3
	Uncertain	87	34.9
	Disagree	18	7.2
	Strongly disagree	8	3.2
	Total	250	100.0

Chi-sq 112.546 df 4 Asymp.Sig .000

7.5.7 Perceptions among Different Ethnics Groups

Are there any differences between the different ethnics groups living in London in terms of their perceptions of Islamic mortgages? The ANOVA test was used to identify these differences, the results of which are presented in table 7.23.

Table 7.23 ANOVA comparison between Ethnic groups in their perceptions about IM

Factors	F	Sig.
The religious factor is the most important reason behind the attraction of Islamic mortgage	1.834	.081
The expensiveness of Islamic mortgage does not help the low-income group	.438	.878
Islamic mortgage is very expensive and requires high service charges	1.139	.339
Islamic mortgage should be taken even if it is more expensive than conventional mortgage	2.160	.038
Islamic mortgage is similar to interest conventional mortgage but dressed up as a rent	1.750	.098
Islamic mortgage is a perfect solution for Muslim communities and it is the first step towards avoiding paying interest	1.112	.356

The results presented in table 7.23 above show that there is no significant difference between any of the different ethnic groups regarding their perception of Islamic mortgages, specifically their perception of the six factors which are listed in table 7.23 above. *E.g.* the role of the religious factor as a main driver behind the attraction of Islamic mortgages, the influence of the expensiveness of Islamic mortgages as a major constraint facing lower income groups and lastly their perceptions of the differences between the Islamic mortgage and conventional mortgage since their significances are greater than 0.05. On the other hand, there are significant differences between the respondent groups in terms of their willingness to take Islamic mortgages even if they are more expensive than conventional mortgages, with a significance value of 0.038. These differences are presented in table 7.23.

Table 7.24 below shows that the white ethnic background are more willing to take Islamic mortgages even if they are more expensive than conventional mortgages compared with Arabs, which indicates their perception about Islamic and conventional mortgages. Likewise The Pakistanis are more willing compared with Arab, Bangladeshi, Black and Indian respondents.

Table 7.24: Post Hoc Tests Multiple Comparisons of Islamic Mortgage should be Taken Even if they are More Expensive than Conventional Mortgages

(I) Ethnic Origin	(J) Ethnic Origin	Mean Difference I-J	Sig
White	Indian	-.84091	.078
	Pakistani	.07353	.864
	Bangladeshi	-.54012	.126
	Black	-.70238	.061
	Arab	-.83621(*)	.021
	Mixed	-.12500	.810
	Other	-.30000	.471
Indian	White	.84091	.078
	Pakistani	.91444(*)	.039
	Bangladeshi	.30079	.412
	Black	.13853	.720
	Arab	.00470	.990
	Mixed	.71591	.177
	Other	.54091	.207
Pakistani	White	-.07353	.864
	Indian	-.91444(*)	.039
	Bangladeshi	-.61365(*)	.044
	Black	-.77591(*)	.019
	Arab	-.90974(*)	.004
	Mixed	-.19853	.685
	Other	-.37353	.321
Bangladeshi	White	.54012	.126
	Indian	-.30079	.412
	Pakistani	.61365(*)	.044
	Black	-.16226	.454
	Arab	-.29608	.132
	Mixed	.41512	.326
	Other	.24012	.399

Continue Table 7.24 Post Hoc Tests Multiple Comparisons of Islamic Mortgages Should be Taken Even if they are More Expensive than Conventional Mortgages

(I) Ethnic Origin	(J) Ethnic Origin	Mean Difference I-J	Sig
Black	White	.70238	.061
	Indian	-.13853	.720
	Pakistani	.77591(*)	.019
	Bangladeshi	.16226	.454
	Arab	-.13383	.562
	Mixed	.57738	.190
	Other	.40238	.195
Arab	White	.83621(*)	.021
	Indian	-.00470	.990
	Pakistani	.90974(*)	.004
	Bangladeshi	.29608	.132
	Black	.13383	.562
	Mixed	.71121	.099
	Other	.53621	.071
Mixed	White	.12500	.810
	Indian	-.71591	.177
	Pakistani	.19853	.685
	Bangladeshi	-.41512	.326
	Black	-.57738	.190
	Arab	-.71121	.099
	Other	-.17500	.714
Other	White	.30000	.471
	Indian	-.54091	.207
	Pakistani	.37353	.321
	Bangladeshi	-.24012	.399
	Black	-.40238	.195
	Arab	-.53621	.071
	Mixed	.17500	.714

* The mean difference is significant at the .05 level.

7.5.8 Perceptions among the Tenures Groups

To study the difference between the perceptions of the two groups of tenures (renters and owners, of the Islamic mortgage, the table shows the T Test output.

The T Test results are demonstrated in Table 7.25. The results presented in the output above suggest that there are no significant differences between renters and owners in their perceptions about the Islamic mortgage. Specifically, there is no difference between their perceptions of the religious factor as a major attraction of the Islamic mortgage, and the expensiveness of Islamic mortgages as a major constraint for the lower income group.

Therefore, the perception of the Islamic mortgage is similar in both groups,, renters and owners, since their significances are above .05. However the table shows a significant difference between the groups studied in their perceptions about the expensiveness of Islamic mortgages as a major constraint for the lower income group, with a significance degree of .022. The owners and the renters present a mean of 2.15 and 2.51 respectively. Hence, the owners group are more of the opinion that the expensiveness of Islamic mortgage does not help the low-income group than the renters.

Table 7.25: T -Test Results for the Differences between Renters and Owners in their Perception about Islamic Mortgages

		Levine's Test for Equality of Variances		t-test for Equality of Means		
		F	Sig.	t	df	Sig. (2-tailed)
The religious factor is the most important reason behind the attraction of Islamic mortgage	Equal variances assumed	1.913	.168	-.603	247	.547
	Equal variances not assumed			-.654	114.561	.514
The expensiveness of Islamic mortgage does not help the low income group	Equal variances assumed	.140	.709	-2.307	247	.022
	Equal variances not assumed			-2.368	103.682	.020
Islamic mortgage is very expensive and requires high service charges	Equal variances assumed	.611	.435	-1.649	246	.100
	Equal variances not assumed			-1.625	97.215	.107
Islamic mortgage should be taken even if it is more expensive than conventional mortgage	Equal variances assumed	1.117	.292	-1.665	247	.097
	Equal variances not assumed			-1.649	97.790	.102
Islamic mortgage is a similar as interest conventional mortgage but dressed up as a rent	Equal variances assumed	.703	.403	-1.139	247	.256
	Equal variances not assumed			-1.226	112.937	.223
Islamic mortgage is a perfect solution for Muslim communities and it is a first step in avoiding paying interest	Equal variances assumed	.532	.466	-1.642	247	.102
	Equal variances not assumed			-1.688	103.935	.094
Preferred Islamic finance product for mortgage	Equal variances assumed	1.032	.311	-.909	248	.364
	Equal variances not assumed			-.889	95.557	.376
The preferred Islamic mortgage provider	Equal variances assumed	2.927	.088	-1.345	245	.180
	Equal variances not assumed			-1.380	104.100	.171

Table 7.26: The Expensiveness of Islamic Mortgage does not help the Low-Income Group

	Renters		Owners	
	Frequency	Percent	Frequency	Percent
Strongly agree	39	20.5	21	35.0
Agree	51	26.8	13	21.7
Uncertain	71	37.4	24	40.0
Disagree	19	10.0	0	0
Strongly disagree	9	4.7	2	3.3
Total	190	100.0	60	100.0
Mean	2.51		2.15	

7.6 INTRODUCING ISLAMIC MORTGAGES INTO THE 'LCHO'

There is a range of public sector home purchase assistance schemes accessible in the UK targeted at those attempting to get on the home ownership ladder; the majority are targeted at tenants in public sector rented accommodation. These include: Right to Buy, Right to Acquire, Rent to Mortgage, Voluntary Purchase Grant Scheme, and Home buy Scheme, Cash Incentive Scheme, and Conventional Shared Ownership.

This section explores how flexible tenure can be achieved within Islamic mortgages. Flexible tenure according to the Council of Mortgage Lenders (CML) is supposed to meet three core objectives: access, sustainability and equity release (Hoyle, 2004).

- **Access**: assisting householders onto the property ladder.
- **Sustainability**: allowing people to remain in home-ownership if there is a recession in the market or if the homeowner faces personal financial hardship.
- **Equity release**: supporting home-owners to access the value of their homes when mostly needed, for example, in later life and when other eventualities

arise that require additional funds being available. Therefore, this section aims to answer the following research question:

Research question (6) Do current structures of Islamic mortgages help low income groups of the Muslim community to achieve homeownership.

Currently, there are a number of schemes, as mentioned earlier, that seek to meet one or more of these core objectives. This section provides an overview of two of these schemes, namely co-ownership and right to buy.

7.6.1 Co-Ownership Scheme

Co-ownership was introduced in the early 1980s to help people in housing need who cannot afford to buy a home outright. Priority will usually be given to key workers, for example National Health Service (NHS) employees, Police Force workers, teachers and those on local authority or housing association waiting lists.

Co-Ownership constitutes the largest form of low-cost home-ownership (LCHO) after the Right to Buy. During co-ownership, the purchaser buys a share of the property, usually from a housing association (HA), and pays rent on the remaining share. Further shares can be bought until the property is owned outright. Although the property is not owned outright initially, the shared owner has the normal rights and responsibilities of a full owner-occupier. The purchaser will generally buy a 25 percent, 50 percent or 75 percent share of the property which is always done by taking out a mortgage.

Respondents were asked their views on integrating Islamic home finance into LCHO schemes, especially the co-ownership scheme. The result is summarised in table 7.27, which shows that 23 percent would not consider co-ownership and 22 percent would consider it as an affordable option of homeownership, while the majority of respondents, 41 percent, said they are not sure about their view and 14 percent said they have never heard of it.

Table 7.27 Introducing the Islamic Mortgage in the LCHO (Co-Ownership)

	VALID	FREQUENCY	PERCENT
Consideration of co-ownership	Yes	55	22.2
	No	57	23.0
	Not sure	104	41.1
	Never heard of it	34	13.7
	Total	250	100.0

Chi-Sq. 39.645 Asymp.Sig: .000

The table also shows that if the chi-square level is lower than 0.05 for this scheme, then the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance.

7.6. 1.1 Factors influencing the co-ownership scheme

It is essential to find out what factors influence consideration of the co-ownership scheme. For this purpose, chi-square and cross tabulation have been run between considerations of co ownership and other variable factors.

7.6.1.1.1 Ethnicity

In order to see whether there is a relationship between preference of co-ownership and ethnicity of respondents the chi square cross tabulation test was run. The result is presented in table 7.28, which shows that there is a significant difference level of .002, Pearson Chi Square value of 44.712.and 21 degree of freedom (our significance level is less than .05). Therefore, we can say that the two variables are associated. Whether respondents would consider the co ownership scheme or not depends on ethnic origin.

Table 7.28 Chi-Square Tests Co-ownership and Ethnicity

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	44.712(a)	21	.002
Likelihood Ratio	50.855	21	.000
Linear-by-Linear Association	12.875	1	.000
N of Valid Cases	248		

a 18 cells (56.3%) have expected count less than 5. The minimum expected count is 1.10.

From cross tabulation between ethnic origin and consideration of co ownership in table 7.29 we see that the majority of those who are considering co ownership are from an Arab background (31percent), also 29 percent of the black community would say yes to the co ownership scheme. Conversely, the majority (37 percent) who would say no to the co ownership scheme are the Bangladeshi community, 53 percent of whom had never heard of the scheme. This is an indication that the awareness of the shared ownership scheme among Muslims is very limited, even though more than 4 percent of Housing Associations (HA) tenants are Muslims (Cheesman, D. 2007).

Table 7.29 Cross tab of Consideration of Co-ownership and Ethnic Origin

			Consideration of co-ownership				Total
			Yes	No	Not sure	Never heard of it	Yes
Ethnic Origin	White	Count	0	3	8	1	12
		% Within Consideration of co-ownership	.0%	5.3%	7.8%	2.9%	4.8%
	Indian	Count	1	2	5	2	10
		% Within Consideration of co-ownership	1.8%	3.5%	4.9%	5.9%	4.0%
	Pakistani	Count	4	6	5	2	17
		% Within Consideration of co-ownership	7.3%	10.5%	4.9%	5.9%	6.9%
	Bangladeshi	Count	4	21	38	18	81
		% Within Consideration of co-ownership	7.3%	36.8%	37.3%	52.9%	32.7%
	Black	Count	16	10	13	3	42
		% Within Consideration of co-ownership	29.1%	17.5%	12.7%	8.8%	16.9%
	Arab	Count	17	12	24	5	58
		% Within Consideration of co-ownership	30.9%	21.1%	23.5%	14.7%	23.4%
	Mixed	Count	4	1	3	0	8
		% Within Consideration of co-ownership	7.3%	1.8%	2.9%	.0%	3.2%
	Other	Count	9	2	6	3	20
		% Within Consideration of co-ownership	16.4%	3.5%	5.9%	8.8%	8.1%
	Total	Count	55	57	102	34	248
		% Within Consideration of co-ownership	100.0%	100.0%	100.0%	100.0%	100.0%

7.6.1.1.2 Awareness of Islamic mortgages

In order to see whether there is any relationship between consideration of co-ownership and awareness of Islamic mortgages among respondents the chi square cross tabulation test was run. The results are presented in table 7.30. The results show that there is a correlation between the consideration of co-ownership and the awareness of Islamic mortgages with significant difference.

Table 7.30 Chi-Square Tests Consideration of Co-Ownership and Awareness of Islamic Mortgages

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	24.862(a)	6	.000
Likelihood Ratio	25.622	6	.000
Linear-by-Linear Association	21.925	1	.000
N of Valid Cases	248		

a 0 cells (.0%) have expected count less than 5. The minimum expected count is 7.81

From table 7.31 of the cross tabulation between the knowledge of differences of Islamic and conventional mortgages and the consideration of the co ownership scheme we see that 69 percent of those who are considering the co ownership scheme know the differences between Islamic and conventional mortgages. While nearly 80 percent of those who are not aware of the co-ownership scheme *i.e.* never heard of it are not aware of Islamic mortgages either.

Table 7.31 Cross Tab Consideration of Co-ownership*Knowledge of the Differences between Islamic and Conventional Mortgage00

			Consideration of co-ownership				Total
			Yes	No	Not sure	Never heard of it	
Knowledge of differences between Islamic and conventional mortgage	Yes	Count	38	33	47	7	125
		% Within Consideration of co-ownership	69.1%	57.9%	46.1%	20.6%	50.4%
	No	Count	9	14	24	10	57
		% Within Consideration of co-ownership	16.4%	24.6%	23.5%	29.4%	23.0%
	Not sure	Count	8	10	31	17	66
		% Within Consideration of co-ownership	14.5%	17.5%	30.4%	50.0%	26.6%
	Total	Count	55	57	102	34	248
		% Within Consideration of co-ownership	100.0%	100.0%	100.0%	100.0%	100.0%

7.6.1.1.3 Spouse employment

In order to see whether there is a relationship between the preference of co-ownership and employment of the respondents' spouses, the chi square cross tabulation test was run. The result is presented in table 7.32, which shows that Pearson Chi-Square value is 19.146, with 6 degree of freedom (df). Our significance is .004. Hence, there is a significant difference (our significance level is less than .05). Therefore, we can say that the two variables are associated. Whether you are considering a co ownership scheme or not depends on the employment status of your spouse.

Table 7.32 Chi-Square Tests Consideration of Co-Ownership and Spouse Employment

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	19.146(a)	6	.004
Likelihood Ratio	19.744	6	.003
Linear-by-Linear Association	7.116	1	.008
N of Valid Cases	136		

From table 7.33 of the cross tabulation between spouse employment and the consideration of a co ownership scheme we see that of those who are considering co-ownership the majority of their spouses are unemployed (75 percent). Nevertheless, of those who have never heard of this scheme, 69 percent of their spouses are working.

Table 7.33 Cross Tab Consideration of Co-ownership and Spouse Employment

			Consideration of co-ownership				Total
			Yes	No	Not sure	Never heard of it	
Spouse Employment	Working:	Count	9	13	20	11	53
		% Within Consideration of co-ownership	25.0%	40.6%	38.5%	68.8%	39.0%
	Retired:	Count	0	5	2	1	8
		% Within Consideration of co-ownership	.0%	15.6%	3.8%	6.3%	5.9%
	Neither:	Count	27	14	30	4	75
		% Within Consideration of co-ownership	75.0%	43.8%	57.7%	25.0%	55.1%
	Total	Count	36	32	52	16	136
		% Within Consideration of co-ownership	100.0%	100.0%	100.0%	100.0%	100.0%

7.6.1.2 Funding co-ownership scheme

There is a substantial demand for home ownership among Muslim HA tenants, and they are ready to pay more than their rent to achieve this (Cheesman, 2007). Given the financial situation of Muslims there is a strong demand among them for low-cost homeownership. Muslims living in social housing were more interested in owning their home than tenants overall and appeared to be slightly less content to be in social housing (Cheesman, 2007).

Clearly Muslims represent a significant market for affordable homeownership through the shared ownership scheme, provided that Islamic mortgages are introduced into this scheme and appropriate Islamic financial products are available.

Funding the co ownership scheme through Islamic finance can be done by long-term saving schemes that lead gradually to homeownership. Building and housing cooperative societies commonly use this practice; the Canadian Islamic Housing Cooperative Society stands out as an earlier Islamic example.

Islamic mortgage providers have to realize the potential of the market in this sector and in order to safely fund the co ownership scheme and put its products in the market, they have to lobby the Government to accelerate the process of resolving the technical, legal and regulatory issues which may be very complex and long overdue.

7.6.1.3 Financing Muslim Housing Associations

There are nine Muslim Housing Associations in the UK most of which are very small housing companies. However, there are relatively bigger Housing Associations in London, for example The North London Housing Association, Bangla Housing Association and Ash-Shahada Housing Association (*Tijara* Pages, 2008).

The North London Housing Association is the largest Muslim-led housing association in the UK. It was founded in 1986 and was registered with the Housing Corporation in1989. By the late 90's the organisation had established its roots in three North London Boroughs, which had a substantial Muslim presence (NLMH, 2008).

The Bangla Housing Association was established in 1991. Its members are mainly of Bangladeshi origin. The Association manages more than 200 properties in four Boroughs in East London (Bangla, 2008).

Ash-Shahada Housing Association operates in South London, mainly in the Borough of Lambeth. Most of its members are Black African Muslims. Like the others Ash-Shahada is a Registered Social Landlord (RSL), which receives financial support from the Government or its agencies. All of them are among Black and Minority Ethnic (BME) housing associations listed in the UK and are registered with charitable status under the Industrial and Provident Societies Act 1965.

These Muslim Housing Associations can be financed through Private Islamic Finance; the Conservative Government first launched the concept of the Private Finance Initiative in 1992. Private finance is funds raised from private sources for investment in social housing (Joseph & Terry, 1997). These funds are not spent directly by the Government and hence are not public finance. Private Islamic Finance can be raised to extend and promote homeownership among low-income Muslim households and social tenants. The closer the match between the requirements of the two parties, the investors or funding bodies and the Muslim Housing Associations, the more likely a good funding deal can be arranged. The required funding can be raised through the structuring of banking syndications involving all the Islamic mortgages providers.

This will allow the financial risk to be spread, as well as providing a wider sharing of returns. The Muslim Housing Association Companies can perform a significant agency role between banking syndications and the end beneficiaries of the LCHO schemes. Financing can then be negotiated and arranged through *Istisnaa* in the case of New Build Home Buy or through lease or *Ijarah* for Social Home Buy.

From the point of view of the banking syndications the investment in the LCHO schemes has to fit with their investment policy. There are three key issues to be evaluated: possible risks, likely returns and marketability - in other words the ease of selling the investment to a different bank for a reasonable price. This type of investment could grow significantly if there was a lasting political consensus between the political parties about the key issues of the Government subsidy to the Housing sector, for example the future of the assured tenancies, housing benefit, Social

Housing Grant, Housing Association Grants and Grants for Rent and Ownership etc. This will be enormously helpful to the decision-making process of Islamic mortgage providers, banking syndications or any other potential investors and financers.

Private finance has been used successfully in England and Wales for funding affordable rented housing. There are at least four factors which enable it to develop effectively. These are:

Subordination of Social Housing Grant and Housing Association Grant, gives the lenders confidence knowing that their loan ranks ahead of Social Housing Grant. The regulations of the Housing Corporation and other Government regulators give confidence to lenders through their regulatory power. The Government subsidy system as discussed earlier and the Housing Associations' in-time payments and having acted responsibly and there have been no significant defaults in the sector (Joseph & Terry, 1997).

The potential of Private Islamic Finance to improve the housing conditions of the Muslims social tenants can be explored further. Nationally Muslims suffer disproportionate housing disadvantage; 30 percent of Bangladeshi and Pakistani homes are deemed unfit and 12 percent of Muslim households have no central heating. Furthermore, 42 percent of Muslim children are living in overcrowded households (Sellick, Patricia, 2004).

To identify whether the Islamic mortgage provider will influence the degree of consideration of co ownership the chi square test was run. The results are presented in table 7.33 which shows that the Pearson Chi Square value is 9.699, with 6 degree of freedom and p-value of .375.

Table 7.34 Chi-sq Test Consideration of Co-Ownership and Preferences of Islamic Mortgage Provider:

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	9.699(a)	9	.375
Likelihood Ratio	10.105	9	.342
Linear-by-Linear Association	.314	1	.575
N of Valid Cases	210		

There is no significant difference (our significance level is more than .05). Therefore, we can say that the two variables are independent. Therefore, the Islamic mortgage provider does not influence consideration of the right of co-ownership scheme.

7.6.2 Right to Buy

The right to buy means that qualifying tenants can buy their homes by paying the full purchase price at once. They receive a discount of between 32 percent and 60 percent for a house and between 44 percent and 70 percent for a flat. Any secure tenant of a District Council, London Borough Council, County Council or other similar body, non-charitable housing association or other registered social landlord or a housing action trust has a right to buy. Tenants may qualify to buy their own home if they have spent a total of at least two years as a tenant of their present landlord, with another right to buy landlord, with a qualifying public body or in accommodation provided by the armed forces.

Respondents were asked their views on integrating Islamic home finance into the LCHO schemes, especially the right to buy. The results are summarised in table 7.35. Since the chi-square level is lower than 0.05 for the scheme, then the null hypothesis will be rejected. Therefore the differences between the options given to the respondents are not attributed to chance. The table also shows that 69.1 percent are of the view that the right to buy is the only away of buying without breaking *Shari'a* law and overstretching their finances, while 25 percent believe that it is the only way for them to become a homeowner. On the other hand, only six percent believe that they will never be a homeowner without the introduction of this scheme.

Table 7.35 Introducing Islamic Mortgages into the LCHO (Right-to-Buy)

	VALID	FREQUENCY	PERCENT
How the right to buy scheme can facilitate home ownership	It is only way for you to become a homeowner	61	24.5
	It is a way of buying without breaking *Shari'a* law and overstretching your finance.	173	69.1
	You will never be a homeowner without the introduction of this scheme	16	6.4

Chi-Sq. Goodness of fit: 155.349. Df: 2 Asymp.Sig:000

Islamic mortgage models cannot be used to purchase properties under the range of low-cost home-ownership schemes currently available. This is because Islamic mortgages involve the bank in the sale and disposal process. For example, in the case of *Murabahah* the bank briefly becomes the property "owner", and becoming the owner for a longer term in the case of *Ijarah*. However, the LCHO initiatives invariably do not allow third party involvement in the acquisition process and there are requirements on disposal within a pre-set time frame according to the Housing Act 1985, as amended by the Housing Act 1996. This negates the discount benefits for potential customers of Islamic mortgages.

The Bank of England Working Party on Islamic mortgages took the view that the current legislation does enable local authorities to allow tenants to buy their homes with Islamic finance (Thomas, 2006). The Office of the Deputy Prime Minister (ODPM) issued a consultation document on 'Non-standard mortgages for purchasing social dwellings' (ODPM 2005d), and consideration will be given to the Government's proposal to enable local authorities to make 'voluntary disposals' to 'tenants who have the Right to Buy but feel they are unable to exercise that right in a way that is compatible with their religious beliefs' (ODPM 2005d: 5). Nonetheless, there are still two reservations. The first concern is about the 'insurance weighting' applied to these LCHO schemes; and the second one is whether these schemes, such as the First Time Buyers' Initiative, Home Buy or other Low Cost Home Ownership programmes, are compatible with *Shari'a*-compliant financing. Research should be commissioned in connection with these schemes regarding house purchase, improvements and repairs to satisfy the *Shari'a* requirements especially in low demand areas, which are populated with Muslim households (ODPM 2004b).

7.7 CONCLUSION

The Muslim population in the UK constitutes the second largest religious population in the country after Christians. It is a very diverse population from different ethnic and cultural backgrounds. Second and third generation Muslims from these ethnic groups are British nationals by birth. They have shown success in educational and professional achievements. There is a natural preference among them to conduct their financial affairs in line with religious convictions and Islamic lifestyles.

There is an effective demand for Islamic mortgages in the UK; three kinds of behaviour can be distinguished towards this demand. The first is conventional demanders who see Islamic mortgages as good and conventional mortgages as also good. The Islamic mortgage and the conventional mortgage are perfect substitutes for each other, only price matters. The second is the pent-up demander who considers religious and other factors when choosing a mortgage product and would be expected to switch to an Islamic mortgage if it was sufficiently competitive *vis-à-vis* a conventional mortgage. And the third is the staunch demander of the Islamic mortgage who is expected never to enter into conventional mortgage contracts. Furthermore, there are five factors, namely marital status, the intention to buy a home in three years, preference for Islamic mortgage products, preference for an Islamic mortgage provider and the awareness of the Islamic mortgages benefits, which are significant determinants of the demand for Islamic mortgages. Other factors like income, employment, qualifications and age are not statistically significant.

The perception of Islamic mortgages is similar between different ethnic and tenure groups. However, some Muslim ethnic backgrounds are more willing than others to take out an Islamic mortgage even if it is more expensive than a conventional mortgage.

The current structure of Islamic mortgages in the open market does not help low-income Muslim households. Private Islamic Finance can be raised to extend and promote homeownership among low-income Muslim households and social tenants.

Chapter 8

MARKETING STRATEGIES OF ISLAMIC HOUSING FINANCE PRODUCTS IN THE UK

8.1 INTRODUCTION

Marketing strategy is one of the most important areas that need to be carefully looked at by the policy-makers of Islamic mortgage providers. A sound marketing strategy becomes very important as Islamic mortgage providers operate in an environment where quality of service is perceived as an essential criterion from the customer's point of view and also compete with conventional mortgage products to attract the general public. Therefore, this chapter aims to respond to the following research question:

Research question (7) What are the best marketing strategies for financial institutions wishing to promote Islamic mortgages among the Muslims Community?

To answer this question respondent were asked a couple of questions to determine the best possible strategies for marketing Islamic mortgages in UK.

Section 8.3 discusses the access issues of the Islamic home loan and how to effectively raise awareness of it among the Muslim Community.

Section 8.4 discuss the integration of the Islamic mortgage and investigates the language preferences of the respondents when dealing with Islamic mortgages.

Section 8.5 covers the importance of staff confidence and checks the acceptability of promoting the Islamic mortgage by a non–Muslim sales person.

Section 8.6 discusses in detail the role of religion as an important factor in encouraging Muslim customers to take out an Islamic mortgage.

Section 8.7 discusses the Muslim households' consumer preferences in terms of Islamic mortgage products and Islamic mortgage providers and also discusses the prospect of Islamic mortgage providers' cross-selling Islamic mortgage products to Muslim customers.

In the final section, 8.8, the main choice criteria which encourage people to choose Islamic mortgages are considered. Four factors are discussed in detail: the deposit required the choice of mortgage available, the finance amount allowed and the reputation of the bank as a mortgage provider.

However, before presenting and analysing these questions it would be useful to know the level of awareness of the Islamic mortgage among the Muslim Community.

8.2 AWARENESS OF ISLAMIC MORTGAGES

This section responds to the following research question:

Research question (8) What is the level of knowledge about Islamic mortgages among the Muslim Community?

To answer this question the respondents were asked to indicate their knowledge and understanding of Islamic finance principles, the differences between Islamic and conventional mortgages and the existence of the Islamic mortgage in the UK. The approach was a straightforward method, which asked the respondent to either answer yes or no. The results are shown in Table 8.1.

From Table 8.1 it is clear that if the significance of chi square goodness of fit test is lower than 0.05 the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data. The table also shows that the majority of respondents (72 percent) knew the principles of Islamic finance .The findings also highlighted the fact that a substantial number of respondents (64 percent) knew of the existences of Islamic mortgages in the UK. However, only about half of them (50.4 percent) knew the differences between Islamic and conventional mortgages. One of the reasons for this lack of awareness among British Muslims is the lack of understanding of Islamic banking and finance in general and Islamic mortgages in particular.

Table 8.1 Awareness of Islamic Mortgages

	VALID	FREQUENCY	PERCENT
Knowledge of Islamic Finance principles *Chi-sq 175.975 df 2 Asymt.Sig 0.000*	Yes	180	72.0
	No	17	6.8
	Not sure	53	21.2
	Total	250	100.0
Knowledge of differences between Islamic and conventional mortgages *Chi-sq 33.152 df. 2 Asymp.Sig 0.000*	Yes	126	50.4
	No	58	23.2
	Not sure	66	26.4
	Total	250	100.0
Knowledge of the existence of Islamic mortgages in UK *Chi-sq 105.896 df 2 Asymp.Sig .000*	Yes	160	64.0
	No	47	18.8
	Not sure	43	17.2
	Total	250	100.0

A study conducted in Malaysia in 1994, regarding knowledge about Islamic banking showed that almost 100 percent of the Muslim population were aware of the existence of the Islamic bank. Nonetheless, out of these just 27.3 percent completely understood the differences between Islamic banks and conventional banks; a similar result was achieved in another study in Singapore (Gerrard and Cunningham, 1997).

With this new finding, it is hoped that the providers of Islamic mortgages, with the collaboration of Muslim Community leaders, will put some effort into educating the public on adopting Islamic principles in their financial affairs. Furthermore, the banks should focus on explaining the nature of *Shari'a*-compliant mortgage products, as clients will be interested in this, because at the end of the day it is this that attracted them to the bank.

Table (8.2) presents the result of cross tabulation between the levels of awareness of the Islamic mortgage and ethnic origin, which shows that there is a relationship between these factors since the significance of Chi-Square is equal to 0.001.

Table 8.2 Cross Tabulation and Chi-Sq Test of Knowledge of Differences between Islamic and Conventional Mortgages and Ethnic Origin

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	35.364(a)	14	.001
Likelihood Ratio	40.446	14	.000
Linear-by-Linear Association	3.326	1	.068
N of Valid Cases	250		

a 10 cells (41.7%) have expected count less than 5. The minimum expected count is 1.86.

We see that our Pearson Chi Square value is 35.364. There are 14 degrees of freedom. Our significance is .001.There is a significant difference (our significance level is less than .05). Therefore, we can say that the two variables are associated. Whether or not respondents are aware of the differences between Islamic and conventional mortgages depends on their ethnic origin. This is probably because the more rich or high-income and the more religiously-educated and aware the ethnic group, the better placed the members of this group will be to know the difference between Islamic and conventional mortgages. For more in-depth analysis we ran cross tabulation between the knowledge of Islamic mortgages and ethnic origin. The results are presented in the table below which shows that those of Pakistani ethnic origin are more aware about Islamic mortgages as 76.5 percent of them know the difference between conventional and Islamic mortgages. On the other hand, only 11.8 percent do not know the differences between the two mortgages and the same percentages are not sure about their knowledge.

Those of White ethnic origin are very aware about the Islamic mortgage as 67 percent of them know the difference between conventional and Islamic mortgages and 33 percent of them are not sure about their knowledge.

Arabs come third regarding awareness of the Islamic mortgage with the cross-tabulation table below showing that they have a high level of awareness of the Islamic mortgage after those of Pakistani and White ethnic origin. 66.1 percent of them know the difference between the Islamic and conventional mortgage, while only 16.9 percent are not sure about their knowledge and the same percentage do not know the difference at all between the two products.

Table 8.3 Cross Tab of Knowledge of Difference between Islamic Mortgages and Conventional Mortgages and Ethnic Origin

			Ethnic Origin								Total
			White	Indian	Pakistani	Bangladeshi	Black	Arab	Mixed	Other	
Knowledge of differences between Islamic and conventional mortgages	Yes	Count	8	4	13	24	22	39	5	11	126
		% Within Ethnic Origin	66.7%	36.4%	76.5%	29.6%	52.4%	66.1%	62.5%	55.0%	50.4%
	No	Count	0	4	2	23	12	10	3	4	58
		% Within Ethnic Origin	.0%	36.4%	11.8%	28.4%	28.6%	16.9%	37.5%	20.0%	23.2%
	Not sure	Count	4	3	2	34	8	10	0	5	66
		% Within Ethnic Origin	33.3%	27.3%	11.8%	42.0%	19.0%	16.9%	.0%	25.0%	26.4%
	Total	Count	12	11	17	81	42	59	8	20	250
		% Within Ethnic Origin	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

The Mixed Race and Other ethnic origins also show a high level of awareness about the Islamic mortgage, as 62.5 percent and 55 percent of them respectively know the difference between the Islamic mortgage and the conventional mortgage.

On the other hand those of Bangladeshi ethnic origin show the lowest level of awareness among the whole ethnicity, as only 29.6 percent know the difference between the Islamic and the conventional mortgage. Conversely, 28.4 percent do not know the difference between Islamic and conventional mortgages and the majority of them (42 percent) are not sure about their knowledge. Those of Indian ethnic origin also show a low level of awareness about the Islamic mortgage as 36.4 percent know the difference between Islamic and conventional mortgages; the same percentage do not know the difference at all and 27.3 percent are not sure about their knowledge.
Those of Black ethnic origin show an average level of awareness of the Islamic mortgage, as 52.4 percent of them know the difference between Islamic and conventional mortgages. In contrast 28.6 percent do not know the difference at all and only 19 percent are not sure about their knowledge.

These significant differences in the levels of awareness among these communities are attributed to the level of income and the level of religious education among these communities.

In summary, the Pakistani, the White and the Arab ethnic groups show a very high level of awareness about the Islamic mortgage. Conversely, the Bangladeshi and the Indian groups show a very low level of awareness about the Islamic mortgage and those of Black ethnic origin show an average level of awareness about the Islamic mortgage.

8.3 ACCESSING ISLAMIC MORTGAGES

This section will discuss the access issues of Islamic home finance. The results of chi-square goodness-of-fit test, in table 8.4 show that there is a very reasonable likelihood that the differences in the means of knowledge of the Islamic mortgage choices in the sample data can be attributed to chance. When respondents were asked how they found out about Islamic mortgages, 40 percent said from relatives and friends. Only 20 percent of the respondents found out about the Islamic mortgage through bank publications and just 15 percent obtained information about Islamic mortgages from local mosques. Lastly six percent found out about Islamic mortgages from national and/or local newspapers.

Hence, the most effective means of raising the awareness of the Islamic home finance is through relatives and friends and then banks' publications.

Table 8.4 Means of Knowledge about Islamic Mortgages

	VALID	FREQUENCY	PERCENT
Means of knowledge about Islamic mortgages	Bank publications	40	19.7
	Local Mosque	31	15.3
	Relatives /Friend	81	39.9
	Internet	18	8.9
	Newspaper/local newspaper	13	6.4
	Others	20	9.9
	Not applicable	47	
	Total	250	100.0

Chi-sq 93.010 df 5Asymp.Sig, 000

When respondents were asked how they found out about Islamic mortgages, 40 percent said from relatives and friends. This is efficient and cost-free advertising for the Islamic mortgage and could be a powerful marketing tool for influencing respondents to take out an Islamic mortgage. That means, if relatives take out an Islamic mortgage and recommend it to the respondents, then the respondents feel socially pressurized to take out Islamic mortgages, otherwise they may be seen as not good Muslims (Elena, 2007). This may explain the phenomenon of Islamic finance always being a bottom-up rather than top-down movement; in other words the main support for Islamic finance comes from ordinary people rather than governments. This is why the retail market became the dominant activity for the big Islamic banks (Wilson, 2005).

Islamic mortgage providers are not making enough effort to increase the awareness of the existence of the Islamic mortgage as only 20 percent of respondents found out about the Islamic mortgage through bank publications. Such publications should provide relevant information which is clear and concise. They should convey a positive message stressing, for example, that their ethical value is better rather than only stressing prohibitions. Most people are aware of the prohibition of *riba,* but may be less aware of the ethical merits of the Islamic products (Wilson, 2005).

Ironically only 6 percent found out about Islamic mortgages from national and/or local newspapers, despite the fact that their existence received extensive coverage from the national papers. This may be due to the fact that most Muslims have some reservations towards the national media because it portrays them negatively and is by no means fair towards them (The Guardian,2007 November14).

Local mosques have a potential role to play in educating Muslims in all Islamic affairs, but contribute little to the awareness of the existence of Islamic mortgages, with only 15 percent of respondents getting information about Islamic mortgages from them. This may be due to the fact that many *imams* in these local mosques do not know English and never talk about life in Britain today, but rather dust down old sermons written in Arabic or Urdu. Local mosques could collaborate with the banks to educate the public on adopting Islamic principles in their financial affairs.

8.4 ASSIMILATION

This section investigates language preferences of customers when dealing with Islamic mortgages. The Muslim community in the UK is a diverse population, as although the majority is very long-established communities some are newly arrived. The respondents were asked about their preferred language in dealing with Islamic mortgages and the result has been summarized in table 8.5. The table also shows the result of the chi-square goodness-of-fit test which is .000 (less than .005) which indicates that the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance. The table also shows that the majority of them (76 percent) preferred the English language in dealing with Islamic mortgages. Conversely, only 20 percent preferred their own mother tongue and just four percent other languages.

Table 8.5 Language Preferred in Islamic Mortgages

	VALID	FREQUENCY	PERCENT
Language preferred in dealing with Islamic mortgages	English	190	76.0
	Own mother tong language	49	19.6
	Others	11	4.4
	Total	250	100.0

Chi-sq goodness of fit: 213.464. Df: 2. Asym.Sig: .000

The interpretations of this result show that those long-established communities, particularly the Asian Muslims, have developed a good social infrastructure and, as they are second or third generation in UK, English is of course their first language. Nonetheless, those who arrived more recently, for example Somalis, Iraqis and East African Muslims, lack this social infrastructure and English seems to be the main barrier to them accessing the information about Islamic mortgage services.

Islamic mortgage providers should ensure greater awareness among those minorities about the services provided by them and publish more information in relevant community languages for promotion and marketing as well as to encourage greater take–up of Islamic mortgages.

It has been shown earlier that word of mouth has proven to be very effective among the Muslim Community in their decision to take out an Islamic mortgage. Hence, if the access to the information and decision has been mediated through a third party there may be a worrying issue of potential customers being misinformed.

The majority of the older generation speaks Urdu or other languages from the Indian subcontinent, but most also speak at least some English and can read with varying degrees of proficiency. The younger generations have English as their first language, and more learn other European languages at school, such as French, rather than Asian languages. The minority of the older generation who came from East Africa speaks

English as their first language. Young and old mostly have some knowledge of Arabic, and can recite *Quranic* verses.

However, Islamic mortgage providers have to bear in mind that the names of the contracts and products have to be in Arabic (*e.g.* the term *Ijarah* should be used as a substitute for the English term lease) to add further credibility to the products (El-Gamal, 1997). As the Quran, which was revealed in Arabic, is the main source of Islamic finance and great importance is placed on its recitation, all Muslims treat it with respect and admiration. Hence, Arabic terminologies give Islamic finance products a sentimental dimension among Muslims customers.

8.5 STAFF COMPETENCE

Good selection and appropriate training of sales persons who have contact with customers to promote the Islamic mortgage products is important. Islamic mortgage providers need to ensure that they have competent staff, in other words people who have the skills, experience and knowledge to do their job properly and safely under all working conditions (HSE, 2002).

To check the acceptability of promoting the Islamic mortgage by non-Muslim sales persons, the respondents were asked whether they mind non-Muslim sales persons from the banks approaching them to inform them of and provide them with Islamic mortgage products. The result of this question has been summarized in table 8.6. The table also shows the chi-square goodness of-fit- test level is lower than 0.05 therefore the null hypothesis will be rejected. Thus, the differences between the options given to the respondents are not attributed to chance.

Table 8.6 Acceptability of Non-Muslims promoting Islamic Mortgages

	VALID	FREQUENCY	PERCENT
Acceptability of promoting Islamic mortgages by non-Muslims sale persons	No	45	18.0
	Yes	143	57.2
	Not sure	62	24.8
	Total	250	100.0

Chi-Sq. goodness of fit: 65.816, df: 2, Asymp.Sig.: .000

From this table it is clear that 57 percent of the respondents do not mind being approached and informed about Islamic mortgages by a non-Muslim sales person; in other words they accept the promotion of the Islamic mortgage by a non Muslim. Conversely, 18 percent do not accept a non-Muslim promoting the Islamic mortgage; and 25 percent are not sure about their position.

To check the acceptability of promoting and marketing the Islamic mortgage products by non-Muslim sales persons within the respondent's ethnic origin, the SPSS Chi-Square test has been run. The result of the test has been presented in table 8.7. We see that our Pearson Chi Square value is 36.998; there are 14 degrees of freedom, the significance is .001.

Table 8.7 Chi-Square Tests for Acceptability of Promoting Islamic Mortgages by Non-Muslims and Ethnic Origin

	Value	df	Asymp. Sig. (2-sided)
Pearson Chi-Square	36.998(a)	14	.001
Likelihood Ratio	37.700	14	.001
Linear-by-Linear Association	2.311	1	.128
N of Valid Cases	250		

an 11 cells (45.8%) have expected count less than 5. The minimum expected count is 1.44.

There is a significant difference (our significance level is less than .05). Therefore, we can say that the two variables are associated. Whether respondents mind a bank's non-Muslim clerk/sales person approaching them to inform them of and provide them with Islamic mortgage products or not depends on their ethnic origins.

Table 8.8 Cross Tab Acceptability of Promoting Islamic Mortgages by Non-Muslims and Ethnic Origin

			Ethnic Origin								Total
			White	Indian	Pakistani	Bangladeshi	Black	Arab	Mixed	Other	
Do you mind if a bank's non-Muslim clerk /sales person approach you to inform you and provide you with Islamic mortgage products?	Yes	Count	5	0	2	12	14	11	0	1	45
		% Within Ethnic Origin	41.7%	.0%	11.8%	14.8%	33.3%	18.6%	.0%	5.0%	18.0%
	No	Count	4	5	13	57	18	30	3	13	143
		% Within Ethnic Origin	33.3%	45.5%	76.5%	70.4%	42.9%	50.8%	37.5%	65.0%	57.2%
	Not sure	Count	3	6	2	12	10	18	5	6	62
		% Within Ethnic Origin	25.0%	54.5%	11.8%	14.8%	23.8%	30.5%	62.5%	30.0%	24.8%
	Total	Count	12	11	17	81	42	59	8	20	250
		% Within Ethnic Origin	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

The cross tabulation above shows that the majority of the Pakistani community (76.5 percent) accept non-Muslim sales persons promoting and marketing Islamic mortgages. Conversely, only 11.8 percent do not accept non-Muslim sales person marketing Islamic mortgages and the same percentage are not sure. The table also shows that the majority of the Bangladeshi community (70 percent) accepts the non-Muslim sales person promoting Islamic mortgages. Conversely, 14.8 percent do not accept non-Muslim sales persons promoting Islamic mortgages, and the same percentage is not sure. The table also shows 65 percent of other ethnicities do not mind non-Muslim sales persons promoting Islamic mortgages. Conversely, just five percent do not accept the idea of non-Muslims promoting the Islamic mortgage and 30 percent are not sure. Finally the table shows that the majority of those of Arab ethnic origin accept non-Muslim sales persons but not a large majority like the previously-mentioned ethnic origins, as just 50.8 percent accept. Conversely, 18.6 percent of them do not accept and 30.5 percent are not sure.

Nonetheless, the majority of those of White ethnic origin (41.7 percent) do not accept non-Muslim sales persons promoting the Islamic mortgage. Conversely, 33.3 percent of them accept the non-Muslim sales person, while 25 percent are not sure.

In summary, the majority of those from the White community (42 percent) and more than one third of the Black community (33 percent) do not accept non-Muslim sales persons promoting Islamic mortgages. Conversely, the majority of the Pakistani community (77 percent), the Bangladeshi community (70 percent), and the Arab community (51 percent) accept non-Muslim sales persons promoting Islamic mortgages, while the majority of the Indian Muslim community (54.5 percent) and Muslims of mixed ethnic origin (62.5 percent) are not sure.

There is no prohibition in Islam regarding Muslim-non-Muslim business transactions and the history of Islam is full of examples. Hence it is not surprising that the majority of respondents do not mind a non-Muslim sales person promoting and informing them about the Islamic mortgage.

As far as Muslims of White ethnic origin are concerned this rule does not seem applicable to them because of their particular circumstances. White Muslims consist of White British converts and East European Muslims including Bosnian and Turkish Muslims. The sample data was over-represented by converts and Bosnians and both are expected to behave differently towards non-Muslims than other main-stream Muslims. The converts are perceived as better Muslims because as converts they are very committed. Most of them they feel uncomfortable being a White British Muslim in Britain. There seems to be a barrier in the West to White people being Muslims. According to the experiences of most converts, when they first embraced Islam their families and friends were shocked and horrified and were very keen to express their negative views. Also the Bosnians have been put off accepting non-Muslims in general because of their experience of genocide by their non Muslim fellow citizens. According to the Islamic Human Rights Commission (IHRC, 2004) White British Muslims report more discrimination than any other ethnic group.

The most important thing for Muslim customers is trust, which is not an easy thing to build, especially when a lack of professionalism gives valid reasons for mistrust. A study conducted on Malaysian Muslim customers by Haron et al. (1994) found that the friendliness of the bank's personnel and their knowledge of customers' needs, in other words their professionalism, were important factors for customers selecting a bank. If the sales person focuses on offering the best possible service and the most competitive prices in the market, he will achieve the trust of the members of the community.

8.6 RELIGIOUS AFFILIATION

The British Muslim communities consist of a majority of *Sunni* Muslims and a small minority of *Shi'a* Muslims. They both consider religion to be an important factor when taking out an Islamic mortgage. Table 8.9 shows with significant chi-square of goodness-fit-test, i.e. less than 0.005 that more than 75 percent of the respondents agree that the religious factor is the most important reason for the attraction of Islamic mortgages, compared with 8.4 percent who disagree, while 15.7 are uncertain.

Table 8.9 Importance of the Religious Factor

	VALID	FREQUENCY	PERCENT
The religious factor is the most important reason for the attraction of Islamic mortgages	Strongly agree	117	46.6
	Agree	73	29.3
	Uncertain	39	15.7
	Disagree	19	7.6
	Strongly disagree	2	.8
	Total	250	100.0

chi-sq 166.080 df 4 Asym.Sig .000

The main concern of the Muslim community is its desire to avoid dealing in *riba*, because *riba* is strictly prohibited in Islam. As far as money is concerned, *riba* is loosely translated as interest. Whether this translation is accurate or not, whether the Arabic word *riba* and the English word interest mean the same thing is a subject of a long-standing debate. To avoid *riba* (interest) in their dealings, a banking system designed to address their concerns has to take into account this main concern as well as other factors. Hence, the religious factor is very important but not the only factor in financial decisions.

8.7 CONSUMER PREFERENCES

In this section we discuss the Muslim households' consumption preferences in terms of Islamic mortgage products and Islamic mortgage providers. Consumer preference is used mainly to indicate an option that has the greatest predictable value among a number of other options. Preference and acceptance can, in certain circumstances, mean the same thing but it is useful to keep the distinction in mind with preference tending to indicate choices among neutral or more valued options with acceptance indicating a willingness to tolerate the less desirable option.

Section 8.7.1 will discuss the choices of Muslim households regarding Islamic mortgage products; it will also examine the financial capability of Muslim customers.

Section 8.7.2 discusses the Islamic mortgage providers preferred by the respondents; Islamic windows in the high street banks, the wholly Islamic British bank and wholly Islamic foreign banks are discussed in detail with appropriate examples. Section 8.7.3 discusses the scope of the future of Islamic mortgage products in the British financial market.

8.7.1 The Preferred Islamic Mortgage Products

Islamic home-financing modes are classified into fixed-return such as *Murabahah* mortgages and variable return such as *Ijarah* and Diminishing *Musharakah* mortgages.

This section discusses Muslim households' choices of Islamic mortgage products. It aims to answer the following research question:

Research question (9) What is the preferred mode of finance for Islamic mortgages among Muslims in UK?

To answer this question respondent were asked what type of Islamic mortgage products they preferred. The result of this question has been presented in table 8.10. As can be seen in the table the result of the chi-square goodness-of-fit test indicates that there is very low likelihood that the differences in preference of Islamic finance methods in the sample data can be attributed to chance. As can be seen from the results of table 8.9 around 16 percent and eight percent of the respondents prefer to use *Murabahah* and *Musharakah* respectively. In contrast with only five percent who prefer *Ijarah* and six percent who prefer other modes. On the other hand, the majority (64 percent) are not sure about their preferred instruments. This indicates that the majority of respondents are unaware and uneducated about Islamic mortgage models. For their own benefit the Islamic mortgage providers need to raise the awareness of the public and educate them about Islamic finance in general and Islamic mortgages in particular. Education to familiarise Muslims and other consumers with new products and new forms of finance will be crucial. From this perspective the FSA together with the Islamic finance industry, Muslim voluntary organisations, the media, and other concerned government agencies should find ways to improve Muslim households' financial capability.

Table 8.10 Preferred Islamic Mortgage Products

	VALID	FREQUENCY	PERCENT
Preferred Islamic finance product for mortgage	*Ijarah* (redeemable lease)	13	5.2
	Murabahah (instalment credit purchase)	40	16.0
	Diminishing *Musharakah* (declining balance partnership)	22	8.8
	Other	16	6.4
	I do not know.	159	63.6

Chi-sq 305.800 df 4 Asymp.sig.0.00

The most-used Islamic mortgage model in the UK is Diminishing *Musharakah;* it is presented by means of an incentive to the customer that the ownership of the property transfers gradually to the customer without sharing the capital gains that may occur due to the appreciation of the property's value (Dar, 2007). *Musharaka* transactions should involve a loss-sharing arrangement between the bank and the client, based on their respective equity shares. This may increase the bank's risk in case of negative equity (decreasing home values) above the level of risk faced by a conventional lender. Nonetheless, with a long-term Diminishing *Musharakah* it is most likely that property prices will increase over time rather than decreasing if there is a loss to be borne, it is more likely to be in the earlier life of the contract and therefore assumed in large part by the bank rather than the client (Loudy, 2007).

Ijarah and *Ijarah wa Iqtina* (leasing and higher purchase contracts) are more appropriate for housing finance. If they are done with a fixed rental rate for the length of the transaction, then they fit into the same risk category as a *Murabahah* mortgage model. However, if the *Ijarah* is done with an adjustable rental rate fixed to an index, or an adjustable *Musharakah*, then it is subject to the risk of re-pricing, as in a conventional average rate of mortgage (ARM) (Loudy, 2007). Nonetheless, there is concern about the *Ijarah* model when the property is not occupied by the actual owner. There may be discrepancies between the rent paid to the bank by the homeowner and the rent paid to the homeowner by the renter. This is due to the former being tied to LIBOR and the latter being tied to the market rent.

There are prudent requirements for these products; for example under Basel 1, *Murabahah*-based home finance products were considered to have the same risk as conventional mortgages, risk weighted at 50 percent. *Ijarah*-based products, however, were risk-weighted at 100 percent, making them slightly more expensive for providers than conventional mortgages. Under the EU Capital Requirements Directive, the risk weights of all three products are the same in the UK, set at 35 percent, under the standardised approach (Ainley & Mashayekhi, 2007).

It is clear from table 8.9 that the most popular model chosen by the respondents is the *Murabahah* mortgage. Residential *Murabahah* transactions are available from a couple of providers in durations ranging from seven years to 25 years. By its nature as a fixed pool of debt, a *Murabahah* has no re-pricing risk as does a conventional ARM (Adjustable Rate Mortgage) or its variants. If a client qualifies for a *Murabahah* at its inception, unless the client's circumstances change, the client will be qualified at its conclusion.

A significant weakness of *Murabahah* is that the practice has a poor perception among many Muslims, relating either to abuse in some cases by the bank, or an inability of the client to distinguish it from a conventional loan secured by a note and a mortgage, due to the lack of awareness and/or misinformation (Dar, 2002). As far as the *Murabahah* is concerned, customers are guided by a pecking order when choosing between financing opportunities. The most popular reason for this behaviour, as mentioned by Read (1998) is control, which is the desire to avoid external interference and maintain independence. The amount of debt or equity sought is determined, to a large extent, by the enterprises owners' and managers' goals of protecting the control of enterprise. Nasr (2005) argues that if the pecking order hypothesis holds, then owners should be reluctant to use the *Musharakah* mode of finance mainly due to the absence of a control factor from the demand side and high risk embedded in the instrument from the supply side. According to Nasr (2005) owners prefer to be financed using *Murabahah* then *Ijarah wa Iqtinaa*, followed by *Mudarabah* and lastly *Musharakah*. However, the *Ijarah* model is thought to be more *Shari'a* compliant than *Murabahah* as it is based on risk sharing and firmly tied to rent not the interest rate. *Ijarah* and Diminishing *Musharakah* are the most commonly used methods in the UK; these contracts are called Home Purchase Plans (HPPs) for regulatory purposes. The Financial Services Authority (FSA) regulates these products under the Finance Act 2007 to create a level playing field, as customers of Islamic mortgages have not enjoyed the same levels of protection as customers of conventional mortgages. Hence, Muslim customers were potentially vulnerable to unfair treatment, with no means of redress (Ainley & Mashayekhi, , 2007).

In general, there are two factors that make households choose one mortgage product over another: the cost and the perceived level of *Shari'a* compliance. As discussed earlier 40 percent of the respondents are willing to take out Islamic mortgage products if the cost is similar to or less than the conventional mortgage and 18 percent stated that they would take one out if a leading *Shari'a* scholar approved it (Tameme & Ahmed, 2008).

There is a lesson to be learned by the Islamic finance industry from the meltdown in the US mortgage market and global credit crunch. Fraud, greed, poor underwriting, reduced diligence and selling complex products to the wrong people for whom the products were not designed are maps leading to a world of hurt. Nonetheless, religious and cultural differences may help to reduce the risk of the Islamic market falling into some of the same traps. The Islamic market might develop with appropriate safeguards in place to prevent many of the threats from ever being incorporated into the system (Loundy, 2007).

8.7.2 The Preferred Islamic Mortgage Provider

The size of the Islamic mortgage market in the UK is estimated at only £500m compared with over £1.1 trillion for the general mortgage market. There are nine or ten regulated financial institutions, including major high street banks, providing Islamic retail products. However, the FSA has received a few applications by existing providers and more than 50 by intermediaries to offer Islamic mortgage products (Treasury News, 30.01.07).

Although the now defunct Al-Baraka International Bank initiated Islamic housing finance in Britain (Wilson, 1999), HSBC became the first large British-based banking chain to offer a range of Islamic mortgage products as part of its global growth strategy, having gained the approval of its *Shari'a* Board and United Kingdom banking regulators.

ABC International Bank (Arab Banking Cooperation) and Bristol & West plc an English subsidiary of the Bank of Ireland introduced Alburaq Islamic Home Finance, distributed through Lloyds TSB bank chains and Islamic Bank of Britain (IBB) (Smith, 2004). The Ahali United Bank (the successor of United Bank of Kuwait) offers the Manzil home purchase plan, distributed through the network of the West Bromwich Building Society. Also United National Bank (UNB) which is a UK registered bank that is authorised and regulated by the Financial Services Authority (FSA) offers Islamic Mortgages.

This section intends to answer the following research question:

Research question (10) Do Muslims prefer to be financed by a branded high street bank rather than other small bank?

To answer this question the respondents were asked about their preferred Islamic mortgage provider; their answers are summarised in table 8.11 with statistical significant degree of chi-square goodness-of-fit test. This indicates that there is a low likelihood that the differences in preferences of Islamic mortgage provider in the sample data can be attributed to chance. However, the majority of respondents (48.2 percent) prefer a stand-alone UK Islamic bank as their home financer. In contrast 25.9 percent prefer Islamic windows offered by high street banks while only 10.1 percent prefer stand-alone non-UK Islamic banks and 15.8 percent prefer others which could include non-bank financial firms, cooperatives etc.

Table 8.11 Preferred Islamic Mortgage Providers

	VALID	FREQUENCY	PERCENT
The preferred Islamic mortgage provider	Stand – alone UK Islamic bank	122	48.2
	Stand – alone non-UK Islamic bank	25	10.1
	Islamic window offer by major high street bank and building	64	25.9
	Others	39	15.8
	Total	250	100.0

chi-sq 83.413 df 3Asymp.sig.0.00

8.7.2.1 Stand-alone UK Islamic banks

So far in the UK five wholly Islamic banks have been authorised by the FSA and initiated by a group of Gulf businessmen and financial institutions. The Islamic Bank of Britain began operations as an authorised retail bank in 2004 with start up capital of £50 million and by June 2007 had a balance sheet of around £140m (IBB report, 2007). The European Islamic Investment Bank, which was authorised as a wholesale bank in 2006, had a balance sheet of £302m and the Bank of London and the Middle East was also authorised as a wholesale bank in July 2007, with a start up capital of £175m (Ainely, *et al*. 2007).

The FSA's staffs were knowledgeable about Islamic banking, indeed they were charged with regulating the London operations of banks from different parts of the Muslim World. The opening of the first branch of the Islamic Bank of Britain (IBB) attracted much media attention and was well received by Muslims as it extended the choice of financial products available to them, tailored to their needs and complying with their faith.

The main issue that arose was the definition of a 'deposit'. In the United Kingdom according to the Banking Act, 1987 a deposit is defined as a 'sum of money paid according to terms under which it will be repaid either on demand or in circumstances agreed by parties' (Statutory instrument, 1990). The deposit-takers are regulated and the customer is legally assured of full repayment as long as the bank remains solvent. This is consistent with *Shari'a* for the current account which is based on *qard* (loan to the bank). As far as the investment *Mudarabah* account is concerned, this is not consistent with *Shari'a* law, which requires the customer to accept the risk of loss of original capital in case the 'deposit' is a profit–and-loss sharing account. To comply with FSA requirements IBB say that its depositors are legally entitled to full repayment. Nonetheless, the customers had the right to turn down deposit protection on religious grounds and opt for repayment under a *Shari'a*-compliant risk sharing and loss bearing formula.

The FSA cannot and will not provide assurance of *Shari'a* compliance; that is up to the IBB management and its *Shari'a* board. However, the FSA requires that customers have to be fully informed about the product's characteristics and the risk associated with it for the sake of customers' protection.

The IBB now offers a range of Islamic mortgage products and other retail and business banking facilities. It has eight branches across the country in cities with large Muslim populations. According to a recent report, the IBB had over 50,000 accounts and some 42,000 customers (IBB annual report, 2006).

8.7.2.2 Islamic windows of high street banks

A number of Multinational Banks such as Citi, Deutsche, and HSBC have been in the Middle East and South East Asia for quite a lot of years. Consequently, they have developed significant knowledge and experience of local markets, as well as Islamic ones. To tap into the growing demand for Islamic products, they have established business lines known as 'Islamic windows', some of which are based in the UK and others in the Middle East and South East Asia. It is, however, not required for conventional banks to have separate authorization from the FSA to carry out the business of Islamic finance unless such banks were to establish a subsidiary or separate entity to carry out this business. These windows have contributed considerably to the development of Islamic finance because of the banks' global experience in product development and their access to far greater resources than those accessible to local banks in the Middle East and South East Asia.

The major conventional banks offering Islamic mortgage products are HSBC and Lloyds TSB banks. HSBC bank through its dedicated Amanah Islamic finance division entered the market in 2004 encouraged by the abolition of the double stamp duty. Lloyds TSB entered the market in March 2005 in a major way, with 17 branches including Luton, Slough, Birmingham, Basingstoke, Southampton, as well as four in London and four in West Yorkshire - three in Bradford alone.

These banks have trained staff to cater for local demand for *Shari'a*-compliant financial products. Both banks offer Islamic deposit and current accounts linked to Islamic home finance, as customers make their mortgage repayments through these accounts. These accounts offer normal transaction facilities such as chequebooks, standing orders and direct debit facilities, monthly statements and multifunctional cards that serve as cheque guarantee and debit cards. And of course there is no payment or charge of interest in these accounts. Amanah requires a minimum balance of £1000 to maintain the account while for Lloyds TSB there is no minimum balance.

8.7.2.3 Stand alone non-UK Islamic bank

There are a few banks in London from the Middle East and South East Asia offering Islamic products such as home finance. Nonetheless, these products are generally uncompetitive in terms of pricing and most were not regulated by the FSA. Hence, their consumers did not have the same protection as other consumers, such as the availability of the Financial Ombudsman Service and the possibility of redress from the Financial Services Compensation Scheme.

The Al-Baraka International Bank was the best example of this kind of bank. It was established in the 1980's after the Saudi investment company, Al-Baraka, bought Hargrave Securities, a licensed deposit taker, and converted it into an Islamic bank (Wilson, 2006). It caters for Arab holidaymakers in London of high net worth. By 1991 its business had expanded; the deposits rose from £23 million in 1983 to £154 million and they had three branches, two in London and one in Birmingham, as by then the bank had in the region of 12,000 customers. In addition to the current account the bank offered investment deposits on a *Mudarabah* (profit sharing) basis for sums exceeding £5,000, with 75 percent of the annually-declared rate of profit paid to those deposits subject to three months notice, and 90 per cent paid for time deposits of over one year. Al-Baraka did not have the staff or resources to adequately monitor client funding. Hence, much of its assets were placed with other banks on Islamic basis.

Al Baraka started to offer long term Islamic mortgages to its clients in 1988 in an *Ijarah*-based model for a period ranging between 10 and 20 years. Al-Baraka Bank lacked the economy of scale to achieve a competitive cost base in an industry dominated by large institutions. Moreover, the Bank of England tightened its regulations after the demise of the Bank of Credit and Commerce International (BCCI). Hence, Al-Baraka surrendered its banking licence and closed its branches in June 1993, but continued operating as an investment company (Wilson, 2006).

8.7.3 Cross Selling Islamic Mortgage Products

The foundations for the future development of Islamic mortgages in the UK have been firmly laid. Although the likely growth cannot be predicted accurately, there is scope for expansion in retail markets in general.

So far the industry has concentrated on providing mortgages and savings products for retail consumers, and growth has been modest. The tax and regulatory developments benefit the market some firms are expanding their product ranges by offering new savings and investment accounts.

Banks can attract Muslim clients through Islamic mortgage products and then cross-sell other products such as interest-free student overdrafts. For example, HSBC Amanah launched an Islamic pension fund in May 2004, where the assets held in the fund are screened for *Shari'a* compliance. The product is marketed to individuals and small Muslim family businesses.

Looking further ahead, there is scope to expand the market for Islamic products and services to non-Muslims as well as Muslims. It may be difficult to market Islamic mortgages which address the relative minority who are prepared to make financial sacrifices in following their faith to non-Muslims. Nevertheless, Islamic mortgage providers can explore the equity release market, as in the UK this market is estimated to be in excess of £1 trillion worth of property owned free of mortgage by individuals aged over 65. If a sound Islamic investment product gave a better result than the conventional one this market segment could attract customers to release some of their equity via Islamic products (Cook, 2005). If Islamic mortgage providers can position their products to appeal more to the much larger non-Muslim population, then it could benefit from economies of scale, which would help its sustainability in the long term.

It seems there is demand for new retail products for personal finance and the small and medium-size enterprise (SME) markets. Some regional stockbrokers and financial advisers are offering tailored advice to Muslims customer.

8.8 MAIN CHOICE CRITERIA ENCOURAGING CHOOSING ISLAMIC MORTGAGES

This section investigates the choice criteria for the Islamic mortgage; the question of which factors motivate choice in the Islamic home loan market is an important one, the answer to which will be of interest to academics and bankers alike. Hence, this section intends to answer the following research question:

Research question (11) What are the main choice criteria by which Muslims choose between Islamic mortgage providers?

To answer this question the respondents were asked about the main criteria that encouraged them to choose their Islamic home loan from different Islamic mortgage providers.

The respondents were given the following four factors; the deposit required, the choice of mortgage available, the lend amount allowed and the reputation of the bank as a mortgage provider. The respondents were asked to place their choice in rank from one to five using five to indicate the most important choice and one the least important.

The results have been presented and discussed as follows:

Section 8.8.1 analyses and discusses why the majority of respondents (31 percent) considered the affordability of the deposit required by the bank to be the most important choice criteria in encouraging them to choose between the different Islamic mortgages providers.

Section 8.8.2 discusses the importance of the choice of mortgages available to respondents as the main choice criteria encouraging them to choose between the different Islamic mortgages providers.

Section 8.8.3 discusses the real difficulties faced by the respondents in securing a mortgage and how important it is for them that the bank is prepared to lend them the required amount of money needed to buy a home.

Section 8.8.4 covers the issue of the reputation and the service quality of the bank as the main choice criteria in selecting Islamic mortgage products between different Islamic mortgage providers.

Section 8.8.5 extends the analysis to focus on potential differences in the importance of choice criteria in the Islamic mortgage market with respect to ethnicity and kind of tenures factors.

8.8.1 Deposits Required

The table shows that the significance of chi square goodness of-fit test is lower than 0.05 therefore the null hypothesis will be rejected. Thus, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data. Also the table shows that 31percent of the respondents rank the deposit required by the bank as the most important factor in their choice of Islamic home loan and 12 percent ranked it as the second most important factor. Nonetheless, 21 percent ranked it as unimportant factor for their choice.

Table 8.12 Main Criteria Encouraging Choosing Islamic Mortgages

	IMPORTANCE	FREQUENCY	PERCENT
Deposits required	**1.least important**	**52**	**20.8**
	2.less important	40	16.0
	3.important	51	20.4
	4.very important	30	12.0
	5. Most important	77	30.8
	Total	250	100.0

Chi-sq. 24.680 df.4 Asymp.Sig. .000

When raising Islamic housing loans, retail clients are required to make a deposit of 10-20 percent of the total property value. Recently, it has been possible to raise a deposit-free housing loan in the general mortgage market under partially changed loan terms, as banks may require a life insurance policy of the borrower, a larger number of guarantors and/or larger mortgage amount. This kind of mortgage is called a 100 percent mortgage where 100 percent of the value of the property to be purchased is borrowed. Generally, the higher the deposit that is placed on a property, the better the mortgage terms; for example, a deposit of 10 percent or more facilitates access to lower interest loan, flexible lower repayments and even a shorter mortgage term. Conversely, the 100 percent mortgage is very costly due to higher interest being charged, the borrower possibly being tied into a mortgage deal with heavy early redemption penalties and possibly getting into negative equity if the property value falls rather than rising.

For many first time borrowers a 100 percent mortgage is the only option, but due to the “credit crunch” 100 percent mortgages are very few. Borrowers will be charged a “higher lending charge” (HLC) premium than if they put some of their own money towards the purchase price.

8.8.2 Choice of Mortgages Available

The significance of chi square goodness-of-fit test is lower than 0.05 therefore the null hypothesis will be rejected. Thus, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data. The table also shows that the majority of respondents (almost 26 percent) rank the choice of mortgages available as not important at all, while only 16 percent of them rank it as most important and 13 percent as very important.

Table 8.13 Main Criteria Encouraging the Choice of Islamic Mortgages

	IMPORTANCE	FREQUENCY	PERCENT
Choice of mortgage available	1.least important	64	25.6
	2.less important	48	19.2
	3.important	64	25.6
	4.very important	33	13.2
	5. most important	41	16.4
	Total	250	100.0

Chi-sq. 15.320 df: 4 Asymp.Sig .004

As discussed earlier there are three types of mortgage models and a range of mortgage deals on offer by Islamic mortgage providers. These include buying a first home, moving home and remortgaging from conventional mortgage to Islamic mortgage and are on offer by nearly all the Islamic mortgage providers. There are also a number of Islamic mortgages available for those interested in investment properties and buy–to-lets offered by all major Islamic mortgage providers expect HSBC Amanah. Alburaq offer a unique deal among Islamic mortgage providers called Portfolio Builder which allows the client who owns a number of properties to switch them all to an Islamic mortgage based portfolio. There has been a huge drop in the range of mortgage deals that were on offer in the UK mortgage market according to a recent report, which suggests that due to the credit crunch the number of different mortgage deals has dropped from 15,599 mortgage deals to just 5725 (cited by JST Financial News on 31 March 2008). Over recent months more and more conventional mortgage lenders have been taking various deals off the shelves, such as 100 percent mortgages and other special mortgage types.

8.8.3 The Finance Amount Allowed

Choosing a mortgage from an Islamic mortgage provider that was prepared to finance the required amount also featured highly on the list of choice criteria. This is perhaps indicative of the real or expected difficulties that customers may face in securing a mortgage.

The significance of chi square goodness-of-fit test is lower than 0.05 therefore the null hypothesis will be rejected. Thus, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data. The table shows that almost 21 percent of respondents rank the most important reason for choosing the mortgage provider is finding an Islamic mortgage provider that is prepared to lend the required amount. On the other hand 13 percent rank that as very important and only 10 percent rank this criterion as not important.

Table 8.14 Main Criteria Encouraging the Choice of Islamic Mortgages

	IMPORTANCE	FREQUENCY	PERCENT
The financing amount allowed	1.least important	24	9.6
	2.less important	61	24.4
	3.important	80	32.0
	4.very important	33	13.2
	5. most important	52	20.8
	Total	250	100.0

Chi-sq: 39.800 df:4 Asymp.Sig: .000

Without further information or data regarding the comparison of shopping carried out by customers between the different Islamic mortgage providers, interpretation of such findings is somewhat problematic. It may be that this is indicative of a significant percentage of the market struggling to get finance and being in danger of suffering financial exclusion. Otherwise, it may well be the case that clients choose the first provider that accepts them as a customer and give the matter little further thought.

8.8.4 The Reputation of the Bank as a Mortgage Provider

It is interesting to discover that the least important choice criterion is the reputation of the bank as a mortgage provider. As presented in table 8.15 below 18 percent of respondents rank the reputation of the bank as a mortgage provider as the least important choice criterion in contrast with 17.6 percent who rate it as most important and 14 percent who rate it as very important. The significance of chi square goodness–of-fit test is lower than 0.05 so the null hypothesis will be rejected. Therefore, the differences between the options given to the respondents are not attributed to chance. Hence, the observations fit well and reflect the data.

Table 8.15 Main Criteria Encouraging Choosing Islamic Mortgages

	IMPORTANCE	FREQUENCY	PERCENT
The reputation of the Bank as a mortgage provider	1.least important	45	18.0
	2.less important	52	20.8
	3.important	74	29.6
	4.very important	35	14.0
	5. most important	44	17.6
	Total	250	100.0

Chi-sq: 17.320 df: 4 Asymp.Sig: .002

Given the emphasis that many banks and financial services organizations put on service quality and the huge cost that is incurred in advertising, it is surprising to find out how relatively unimportant such criteria are to the Muslim households in general.

Earlier studies which focused on banking in general found that reputation and service quality factors were important choice criteria. Furthermore, a previous study by Skinner and Ford (2000) found that the reputation of the bank was potentially important in motivating choice in the mortgage market. Hence, such findings may indicate that the mortgage market is different from banking and financial services in general. The interpretation of this finding may be that the reputation of the bank will dominate as a choice criterion when there is a lack of information about specific product criteria that can be searched for to understand and evaluate it before purchasing. Conversely, in the mortgage market this is not the case where such factors such as minimum deposit, payment terms and lending limits to the customers are searchable.

8.8.5 Factors Influencing the Main Choice Criteria Encouraging the Choice of an Islamic Mortgage:

This section extends the analysis to focus on potential differences in the importance of choice criteria in the Islamic mortgage market with respect to ethnicity and kind of tenures factors. Hence, it intends to answer the following research question:

Research question (12) Does importance of the choice criteria vary with respect to the ethnicity and kind of tenures factors and if so, what are the main marketing implications?

In order to investigate whether there are any differences between the ethnic groups in the degree of importance of the main criteria encouraging them to choose their Islamic home loan, the analysis of variance (ANOVA) test was used for this investigation and the result is presented in table (8.16).

Table 8.16 ANOVA Comparison between Ethnic groups in their Differences in the Main Criteria Encouraging them to Choose their Islamic Home Loan

		Mean Square	F	Sig.
Deposits required	Between Groups	4.378	1.930	.066
	Within Groups	2.268		
Choice of mortgage available	Between Groups	3.452	1.809	.086
	Within Groups	1.909		
The lend amount	Between Groups	1.834	1.162	.326
	Within Groups	1.579		
The reputation of the Bank as a mortgage provider	Between Groups	6.054	3.670	.001
	Within Groups	1.650		

The above result shows that there are no significant differences between the ethnic groups in the degree of importance of the main three criteria encouraging them to take out an Islamic home loan. These three criteria: are the deposit required, the choice of mortgage available and the lend amount, since their significances are greater than 0.05. In contrast, there are significant differences between the respondent groups in terms of their assessments of the degree of the importance of the reputation of the bank as a mortgage provider with a significance value of 0.001. Hence, the respondents, regardless of their ethnic background and kind of tenure, have assessed the main criteria that encourage them to take out an Islamic mortgage without differences, while the result shows that there are differences between the respondents groups in their ranking of the importance of the reputation of the bank as a mortgage provider. Table 8.17 below presents these main differences.

Table 8.17 the Main Differences of the Reputation of the Bank

(I) Ethnic Origin	(J) Ethnic Origin	Mean Difference (I-J)	Sig.
White	Indian	-.94697	.079
	Pakistani	-.17157	.723
	Bangladeshi	-.20062	.614
	Black	-1.01190(*)	.017
	Arab	-.82062(*)	.045
	Mixed	.66667	.257
	Other	-.58333	.215
Indian	White	.94697	.079
	Pakistani	.77540	.120
	Bangladeshi	.74635	.072
	Black	-.06494	.881
	Arab	.12635	.765
	Mixed	1.61364(*)	.007
	Other	.36364	.451
Pakistani	White	.17157	.723
	Indian	-.77540	.120
	Bangladeshi	-.02905	.933
	Black	-.84034(*)	.024
	Arab	-.64905	.068
	Mixed	.83824	.129
	Other	-.41176	.332
Bangladeshi	White	.20062	.614
	Indian	-.74635	.072
	Pakistani	.02905	.933
	Black	-.81129(*)	.001
	Arab	-.62000(*)	.005
	Mixed	.86728	.070
	Other	-.38272	.234

Continue Table 8.17 the Main Differences of the Reputation of the Bank

I) Ethnic Origin	(J) Ethnic Origin	Mean Difference (I-J)	Sig.
Black	White	1.01190(*)	.017
	Indian	.06494	.881
	Pakistani	.84034(*)	.024
	Bangladeshi	.81129(*)	.001
	Arab	.19128	.461
	Mixed	1.67857(*)	.001
	Other	.42857	.221
Arab	White	.82062(*)	.045
	Indian	-.12635	.765
	Pakistani	.64905	.068
	Bangladeshi	.62000(*)	.005
	Black	-.19128	.461
	Mixed	1.48729(*)	.002
	Other	.23729	.476
Mixed	White	-.66667	.257
	Indian	-1.61364(*)	.007
	Pakistani	-.83824	.129
	Bangladeshi	-.86728	.070
	Black	-1.67857(*)	.001
	Arab	-1.48729(*)	.002
	Other	-1.25000(*)	.021
Other	White	.58333	.215
	Indian	-.36364	.451
	Pakistani	.41176	.332
	Bangladeshi	.38272	.234
	Black	-.42857	.221
	Arab	-.23729	.476
	Mixed	1.25000(*)	.021

As indicated by the main differences in table 8.17 the reputation of the bank as a mortgage provider encourages more customers within the Black community to choose their Islamic home loan provider than in the White, Pakistani, Bangladeshi, and mixed communities. Likewise the respondents from the Arab community are more encouraged by this factor than the White, Bangladeshi, and Mixed communities to choose their Islamic mortgage provider according to the reputation of the bank as a mortgage provider. Lastly the Indian ethnic groups are more encouraged by this factor to select their Islamic home loan provider than the Mixed groups.

Such a finding will potentially have important implications for the marketing of Islamic mortgages, although an explanation not immediately apparent. It is an area where further, more tailored research is required to produce a more complete understanding.

To study the difference of the main criteria encouraging selecting Islamic mortgage between the two tenure groups (homeowners and renters), the SPSS T-test has been run and the results are presented in table 8.18 below. The results show that there are no significant differences between the renters and homeowners in terms of the effects of the main criteria encouraging them to choose their Islamic home loan from different Islamic mortgage providers available in the market. Specifically the effects of the following factors: the amount of the deposit required, the choice of the mortgage available, the lend amount permitted to the client and the reputation of the bank as a mortgage provider. Hence, the effects of the main criteria encourage the Muslim household to choose his Islamic home loan from a range of providers available in the market with different banks are similar in both groups, renters and homeowners, since their significances are above .05.

Table 8.18 T-Test Main Criteria Encouraging Selection of Islamic Mortgages by Homeowners and Renters, Independent Sample Test

		Levene's Test for Equality of Variances		t-test for Equality of Means			
		F	Sig.	t	df	Sig. (2-tailed)	Mean Difference
Deposits required	Equal variances assumed	.236	.627	.620	248	.536	.14035
	Equal variances not assumed			.633	102.403	.528	.14035
Choice of mortgage available	Equal variances assumed	.265	.607	.068	248	.946	.01404
	Equal variances not assumed			.069	101.483	.945	.01404
The lend amount	Equal variances assumed	.089	.765	1.210	248	.227	.22544
	Equal variances not assumed			1.263	106.499	.209	.22544
The reputation of the Bank as a mortgage provider	Equal variances assumed	.170	.681	.729	248	.467	.14386
	Equal variances not assumed			.736	100.609	.464	.14386

A new study in the US conducted by Experian Consumer Direct found that homeowners have higher credit scores and lower late payment rates than renters. Although the study did not give any explanation for this finding it is worth noting that homeowners generally have greater financial resources, higher levels of financial sophistication, and are more confident in handling debts than renters (Harney, K. R. 2006). This theory may in turn have implications for marketing Islamic mortgage products to homeowners.

8.9 CONCLUSION

As the discussion so far indicates the majority of the respondents knew the principles of Islamic finance and a substantial number of them knew of the existence of Islamic mortgages in the UK. However, only about half knew the differences between Islamic and conventional mortgages. The Pakistanis, Whites and the Arabs showed a very high level of awareness about Islamic mortgages.

An effective means of raising the awareness of Islamic home financing among the Muslim community in the UK is through relatives and friends. This is an efficient and cost-free advertisement for the Islamic mortgage and could be a powerful tool for marketing, influencing the respondents to take out an Islamic mortgage. Local community institutions such as mosques can play a vital role in providing information about Islamic mortgages.

The Islamic mortgage is well integrated in the British financial system and the vast majority of respondents preferred the English language when dealing with it. However, Islamic mortgage providers should consider the small minorities who do not speak good English and ensure greater awareness among those minorities of the services provided by them and should publish more information in relevant community languages for promotion and marketing as well as to encourage greater take–up of Islamic mortgages.

There is no prohibition in Islam regarding Muslim-non-Muslim business transactions and the tradition and the history of Islam is full of examples. Hence, it is not surprising that the majority of respondents do not mind a non-Muslim sales person promoting and informing them about Islamic mortgages. The exception to this is the majority of white Muslims and one third of the black Muslims who would not accept a non–Muslim sales person promoting Islamic mortgages to them. On the other hand the religious factor is the most important reason behind the attraction of Islamic mortgages.

Murabahah is the most preferred mortgage product among the Muslim community even though the majority is not sure about their preferred mortgage products. This indicates that the majority of respondents are unaware and uneducated about the Islamic mortgage models. For their own benefit Islamic mortgage providers need to raise the public's awareness and educate them about Islamic finance in general and Islamic mortgages in particular.

The British Muslims preferred a wholly British Islamic bank to finance their homes. Alternatively they accept the Islamic windows offered by the high street banks, but they are very suspicious about foreign Islamic banks. Looking further ahead, there is scope to expand the market for Islamic products and services to non-Muslims as well as Muslims.

The most important main choice criteria by which Muslims choose between different Islamic mortgage providers is the deposit required by the bank. While the least important main choice criteria by which Muslims choose between different Islamic mortgage providers is the reputation of the bank. The respondents, regardless of their ethnic background and kind of tenure, have assessed the main criteria that encourage them to take out Islamic mortgages without differences, while the result shows that there are differences between the respondent groups in how they rank the importance of the reputation of the bank as a mortgage provider. The reputation of the bank as a mortgage provider encourages more customers within the Black and Arab community to choose their Islamic home loan provider than in the White, Pakistani, Bangladeshi, and Mixed communities. Such a finding will potentially have important implications for the marketing of Islamic mortgages, although an explanation is not immediately apparent. This is an area where further, more tailored research is required to produce a more complete understanding. Nonetheless, there are no significant differences between renters and homeowners regarding the effects of the main criteria encouraging them to choose their Islamic home loan from different Islamic mortgage providers available in the market.

Chapter 9

CONCLUSION

9.1 INTRODUCTION

The objective of this research was to investigate the demand for Islamic housing finance in the United Kingdom and to examine the current structure of Islamic mortgages and its role in achieving homeownership for low-income Muslim households. In addition, this study examined the obstacles and factors influencing decision-making. Furthermore, it evaluated the perception of the Islamic mortgage among British Muslims and also evaluated the Islamic finance products offered by the high street banks. These issues are discussed in the last chapters and hopefully this discussion will open new horizons in the area of Islamic housing finance.

At the start of this thesis, 12 research questions were set out and have been addressed in subsequent chapters. I now return to these and summarize the findings; for convenience they are repeated here:

1) What are the challenges and prospects of homeownership for the Muslim community in the UK?

2) What factor/s might encourage/discourage home buying in the Muslim community?

3) Is there any effective demand for Islamic Mortgages in the UK?

4) What are the factors for choosing Islamic mortgages?

5) What is the perception of Islamic Mortgages among UK Muslims?

6) Do current structures of Islamic mortgages help low income groups in the Muslim community to achieve homeownership?

7) What are the best marketing strategies for financial institutions to promote Islamic mortgages among the Muslim Community?

8) What is the level of knowledge about Islamic mortgages in the Muslim Community?
9) What is the preferred mode of finance for Islamic mortgages of Muslims in the UK?
10) Do Muslims prefer to be financed by a branded high street bank rather than other small banks?
11) What are the main choice criteria by which Muslims choose between Islamic mortgage providers?
12) Does importance of the choice criteria vary with respect to the ethnicity and type of tenure factors and if so, what are the main marketing implications?

The following sections of this conclusion will present a summary of the findings which deals with these questions. The findings are discussed and recommended policies have been derived on the supply side, demand side and general recommendations for the policy makers on theoretical, institutional and practical levels. Furthermore, the reflection of these findings has been discussed in details and questions arising from this study are used to propose an agenda for future research.

9.2 FINDINGS OF THE STUDY

This section aims to summarise the important findings of this research which deals with the research questions in the following sections.

9.2.1 Homeownership

9.2.1.1 Tenures

The majority of the respondents (76 percent) are renting the home in which they live compared to only 24 percent who own their home. Also 83 percent of the Muslim homeowners have mortgages on their homes and 17 percent of them are outright owners. Nearly 20 percent of the respondents have conventional mortgages whereas, in contrast, less than two percent have Islamic mortgages. Within the Muslim households' owner-occupations 75 percent have conventional home mortgages and only 8.3 percent have Islamic home mortgages. The provision of Islamic mortgages and stable house prices are the most important factors in encouraging Muslim householders to buy a home in the near future. It is a fact that there is a gap in homeownership among the Muslim community compared to the general public. Only about half of Muslim householders (51percent) are homeowners, compared with 71 percent of the general population. Muslims are more dependent on social housing than the general population (Sellick, 2004).

The issue of taking out a conventional mortgage concerns Muslims today in a way that it did not concern their parents. For the first generation of Muslims the common solution to the housing problems was to buy a house outright. The mechanism by which first generation Muslims achieved homeownership through outright purchase was to form a club or a cooperative. A number of people would club together to save a certain amount per week, thus within a certain time a total pool of a house price was available and would be used to purchase a house for the first member of the club. All the members would then continue to save until another house could be bought, and so on.

9.2.1.2 Obstacles

There is a gap in homeownership in the Muslim community compared to the general public. This gap is identified as follows: First the affordability gap, with the greatest affordability concern for British Muslims being the ability to raise a deposit, as 58 percent of the surveyed respondents have no funds available for a deposit on a house. This is due to the limited opportunities to accumulate liquid wealth and the earning of relatively low wages. In addition to this mortgage repayment is quite difficult for most of the respondents as many of them (nearly 39 percent) can allocate only less than 10 percent from their income to repaying a mortgage.

The second gap in homeownership in the British Muslim community is financial exclusion. Many British Muslims were unable to get their foot onto the property ladder as a result of interest-bearing mortgages being forbidden. Almost 36 percent of the respondents could not take out an interest-bearing mortgage. The religious conviction of Islam embraces all aspects of a Muslim's life, including the way finance and business transactions are conducted.

The third main gap identified in this survey is the problems of accessing the information about housing and the home-buying process, as 14 percent of the respondents perceive the home buying process as too complicated.

9.2.1.3 Aspiration

Aspiration for homeownership among British Muslims does not appear strong enough, as just over a third (32 percent) of the respondents aspired to own their own home. However it is in fact very high. There is a correlation between the aspiration for homeownership and age, as aspiration for homeownership is very high among the middle age groups (36–55) and low among younger Muslims who are under 25 years, who are over represented in the Muslims population and very low among the elderly. Also there is a positive relationship between aspiration for homeownership and respondents' income.

9.2.1.4 Confidence

British Muslims are very confident about housing and homeownership, as the majority of them (63 percent) perceived it as a good long term investment. They also perceived paying rent as not a good investment. In fact, for some Muslim households the intangible satisfaction of homeownership is even more important than the monetary investment benefits. Analysis of individuals' local activities confirms that homeowners invest considerably more in their local communities than do rental tenants.

9.2.2 The Demand Side

9.2.2.1 The Potential Demand

There is a great demand for Islamic mortgages as 66 percent of the respondents said they are willing to take on an Islamic mortgage. Willingness to take out or switch to an Islamic mortgage provides a good indicator of demand for the Islamic mortgage. There is an effective demand for Islamic mortgages in the UK and three kinds of behaviour can be distinguished regarding this demand. First the conventional demander who sees Islamic mortgages as good and conventional mortgages as also good. If the Islamic mortgage and the conventional mortgage are perfect substitutes for each other, then only price matters. Secondly the pent-up demander considers religious and other factors in choosing a mortgage product and is expected to switch to an Islamic mortgage if it is sufficiently competitive *vis-à-vis* the conventional mortgage. The third is the staunch demander, who is motivated by a strong belief system for the Islamic mortgage, and is expected never to enter into a conventional mortgage contract.

The study confirms that Islamic mortgages are a supply-led phenomenon in the United Kingdom, as it implies that the Islamic mortgage provider has to create a demand as there may not be an automatic demand. This is clearly evident from this study as only 8.4 percent are staunch demanders of Islamic mortgages in UK.

9.2.2.2 Factors Influencing the Demand

This study has established that there are five significant determinants of the demand for Islamic mortgages, namely marital status, the intention to buy a home in three years, preferred Islamic mortgage products, preferred Islamic mortgage providers and the awareness of the benefits of Islamic mortgages. Other factors such as income, employment, qualifications and age are not statistically significant. There is also evidence that demand for Islamic mortgages are influenced by location.

9.2.2.3 The British Muslims' Perceptions

9.2.2.3.1 Attraction

More than 75 percent of the respondents agreed that the religious factor is the most important reason for the attraction of Islamic mortgages. The main concern of the Muslim community is its desire to avoid dealing in *riba*, because *riba* is strictly prohibited in Islam. The general consensus among Islamic scholars is that *riba* covers not only usury but also the charging of "interest" as widely practiced.

9.2.2.3.2 Role in Homeownership for the Average Muslim

The majority of respondents within the given categories (50 percent) agreed that the Islamic mortgage is very expensive and does not help the low-income group. Islamic mortgages have been marketed mainly to wealthy members of the British Muslim community, for example professionals and business people, but the majority of Muslims earn a modest income and can only afford much cheaper housing, and many rent public or private accommodation. Islamic mortgages could appeal to many

Muslim households and encourage them to take their first step on the homeownership ladder, thus becoming greater stakeholders in British society.

9.2.2.3.3 Service Charges

A large proportion of Muslim households (43 percent) perceive the cost of Islamic mortgages as very expensive and requiring a high service charge. A number of factors contribute to the expensiveness of Islamic mortgages, for example high cost of marketing and administration, lack of economies of scale and requiring additional monitoring to be *Shari'a* compliant which involve extra cost, not least the fees and expenses of the scholars of the *Shari'a* committee. Hence, the higher cost of Islamic home finance contributes to the factors that hinder the uptake of Islamic mortgages in the UK.

9.2.2.3.4 Preferences over the Conventional Mortgage

The cost of a mortgage is certainly not the only factor determining the level of business, as the majority of respondents within the given categories (36 percent) believe that an Islamic mortgage should be taken even if it is more expensive than a conventional mortgage. From the market experiences the issue seems to be the size of the premium which should be reduced by greater competition in the market. If the competition does not bring just and fair prices the *Shari'a* provides moral and ethical norms and rules of behaviour that should be observed by all the participants in the market place.

9.2.2.3.5 Credibility

More than one third of the respondents (34 percent) questioned the *Shari'a* compliance of Islamic mortgages; they believed them to be the same as conventional mortgages but dressed up as rent. Basically, due to the lack of awareness and information, the respondents may confuse the mark-up on the *Murabahah* mortgage with interest. Also, the immediate purchase and resale of the property by the bank that is unrelated to the payment period looks like a manipulation of the contract. *Ijara* and *Ijara wa Iqtina* mortgage models are more appropriate for Islamic housing finance, although there is concern when the occupant is not the owner. Nevertheless, this is an important issue bearing significant relevance to the demand for Islamic mortgages.

9.2.2.3.6 Social Inclusion

Most of the respondents (55 percent) believed the Islamic mortgage to be a perfect solution for Muslims which the high street banks could have offered years ago, but at least it is step in the right direction towards avoiding dealing with an interest-based product. The issue of the social exclusion of British Muslims is very relevant, especially before 2003 when there was no Islamic mortgage on offer by the financial system.

9.2.2.3.7 Perceptions among Different Ethnic Groups and Tenures

The perception of Islamic mortgages is similar between different ethnic groups, and tenure groups. However, Muslims of some ethnic backgrounds are more willing than others to take on an Islamic mortgage even if it is more expensive than a conventional mortgage. For example, Muslims from the White ethnic background are more willing to take on an Islamic mortgage even if it is more expensive than a conventional mortgage compared with Arabs. Likewise The Pakistanis are more willing compared with those of Arab, Bangladeshi, Black and Indian ethnic backgrounds.

The 'owners' group believe more than the renters that the expensiveness of Islamic mortgage does not help the low-income group.

9.2.2.4 Islamic Housing Finance as Part of Social Housing

The current structure of Islamic mortgages on the open market does not help low-income Muslim households.

9.2.2.4.1 Co-Ownership scheme

The majority of respondents are not aware of the LCHO schemes especially co-ownership. 55 percent of them were not aware of the scheme as an affordable homeownership option available to them. Furthermore, three factors, namely ethnicity, the benefit of the awareness of Islamic mortgages and spouse employment significantly influence the consideration of the co-ownership scheme.

Muslims represent a significant market for affordable homeownership through the shared ownership scheme, provided that the Islamic mortgages introduced in this scheme and appropriate Islamic financial products are available.

- Funding the co ownership scheme through Islamic finance can be done by the long-term saving schemes that lead gradually towards homeownership.

- Private Islamic finance can be raised to extend and promote homeownership among low-income Muslim households and social tenants. The closer the match between the requirements of the two parties, the investors or funding bodies and the Muslim Housing Associations, the more likely a good funding deal can be arranged. The required funding can be raised through the structuring of banking syndications involving all the Islamic mortgage providers. This type of investment could grow significantly if there is a lasting political consensus between the political parties regarding the key issues of Government subsidy to the Housing sector.

9.2.2.4.2 Right to Buy

Regarding the right to buy, 69.1 percent are of the view that it is the only way of buying without breaking the *Shari'a* law and overstretching their finances. At present, Islamic mortgage models cannot be used to purchase properties under the range of low-cost home-ownership schemes currently available. Nonetheless, there are still two reservations. The first concern is about the 'insurance weighting' applied to these LCHO schemes; and the second is whether schemes such as the First Time Buyers Initiative, Home Buy or other Low Cost Home Ownership programmes, are compatible with *Shari'a*-compliant financing.

9.2.3 Marketing Issues

9.2.3.1 The Level of Awareness

The majority of the respondents are very aware about the Islamic finance in general, as 72 percent of them knew the principles of Islamic finance. The findings also highlighted the fact that a substantial number of respondents (64 percent) knew of the existence of Islamic mortgages in the United Kingdom. Nonetheless, only about half of the respondents (50.4 percent) knew what the differences were between Islamic and conventional mortgages.

One of the causes of this lack of awareness among British Muslims is the lack of understanding they have about Islamic mortgages.

The Pakistani, White and Arab ethnic groups show a very high level of awareness about Islamic mortgages.

9.2.3.2 Access issues

An effective means of raising the awareness of Islamic home finance among the Muslim community in the UK is through relatives and friends as 40 percent of the respondents had learned about Islamic mortgages from relatives and friends. This is an efficient and cost-free advertisement for Islamic mortgages and could be a powerful marketing tool for influencing respondents to take out Islamic mortgages. Local community institutions such as mosques could play a vital role in providing information about Islamic mortgages.

Islamic mortgage providers are not making enough effort concerning the awareness of the existence of the Islamic mortgage as only 20 percent of respondents found out about Islamic mortgages through the banks' publications.

9.2.3.3 Integration

The Islamic mortgage is well integrated into the British financial system and the vast majority of respondents (76 percent) preferred the English language when dealing with it. However, Islamic mortgage providers should consider the minority who do not know good English and ensure greater awareness among them about the services they provide and publish more information in relevant community languages for promotion and marketing as well as to encourage greater take–up of Islamic mortgages.

The interpretations of this result may be that those long-established communities mainly the Asian Muslims have developed good social infrastructures and as they are a second or third generation in UK, English is of course their first language.

9.2.3.4 Employees' Competence

The majority of the respondents (57 percent) do not mind being approached and informed about Islamic mortgages by a non-Muslim sales person, in other words they accept the promotion of Islamic mortgages by a non–Muslim.

This is not surprising as there is no prohibition in Islam regarding Muslim-non-Muslim business transactions, the tradition and the history of Islam is full of examples. What is more important for Muslim customers, in addition to the professionalism of the sales person, is the trust in that person and his institution. The exception to this is the majority of White Muslims (42 percent) and one third of Black Muslims (33 percent) who do not accept a non–Muslim sales person promoting Islamic mortgages to them. This is most likely due to reasons based on their own experience and backgrounds rather than Islamic-based reasons.

9.2.3.5 Religious Affiliation

The religious factor is very important but not the only factor in financial decisions, as 75 percent of the respondents agreed that the religious factor is the most important reason behind the attraction of Islamic mortgages.

9.2.3.6 Muslim Householders' Preferences

Murabahah is the most preferred mortgage product for the Muslim community with 16 percent preferring this mode of financing. Nonetheless, the majority of the respondents (64 percent) were not sure about their preferred mortgage products. This indicates that the majority of respondents are unaware and uneducated about the Islamic mortgage models.

The majority of respondents (48.2 percent) preferred a wholly British Islamic bank to finance their homes. Alternatively 25.9 percent of them accept the Islamic windows offered by the high street banks but are very suspicious about foreign Islamic banks. Looking further ahead, there is scope to expand the market for Islamic products and services to non-Muslims as well as Muslims.

9.2.3.7 Choice Criteria

The most important choice criteria by which Muslims choose between different Islamic mortgage providers is the deposit required by banks, with 31percent of the respondents ranking the deposit required by the bank as the most important criteria in their choice of Islamic home finance, while the least important criteria by which they choose between different Islamic mortgage providers is the reputation of the bank. The respondents, regardless of their ethnic background and kind of tenure, assessed the main criteria that encouraged them to take out Islamic mortgages without differences, while the result shows that there are differences between the respondent groups in their ranking of the importance of the reputation of the bank as a mortgage provider. The reputation of the bank as a mortgage provider encourages more customers within the Black and Arab communities to choose their Islamic home loan provider than in the White, Pakistani, Bangladeshi, and Mixed communities. Such a finding will potentially have important implications for the marketing of Islamic mortgages, although an explanation is not immediately apparent. It is an area where further, more tailored research is required to produce a more complete understanding. There are no significant differences between renters and homeowners regarding the effects of the main criteria in choosing between different Islamic mortgage providers available in the market for their Islamic home loan.

9.3 REFLECTING ON THE FINDINGS

The present relevance of housing finance should not be underestimated as it has significant micro- and macro-economic implications. Housing forms an important part of any government's strategy for the alleviation of poverty and employment generation. Despite similar homeownership rates, the structure of the mortgage markets, the public policy objectives and the rates, terms and products of mortgage instruments all substantially differ across the developed countries. These disparities do not appear to result from differences in the demographics affecting housing demand across these countries. Neither do they appear to result from any significant variations in the volatility in housing markets and in the share of housing relative to GDP. It has been concluded that many of the differences come from the public policy objectives of these countries. The way to analyse this is through the examination of outcomes - whether people can obtain housing finance on similar terms where similar risks are involved - rather than looking at whether or not they do this through similar instruments and organisations.

The formalisation of Islamic home finance is one of the most important developments in retail Islamic finance. In most of the Muslim world limited work was initially done concerning Islamic housing finance; however in the last decade there has been significant progress. A secondary market in *Sukuk* is emerging slowly with a potential role in securitization for the Islamic home finance products. Also standardization is emerging as a crucial but highly challenging issue for the Islamic housing finance market. The industry spread from Pakistan, Malaysia and the Middle East to become a fast growing sector in the West.

There is a growing Muslim population across western countries, which is younger than average, highly educated -especially in Canada - and earning an above-average income in the US and below average in the UK. The common factor among these minorities in the United States, Canada, Australia and the United Kingdom is that there is substantial demand for Islamic housing finance which remains unmet. With exception to the UK, and to some extent the US, the handful of financial institutions catering for this demand is characterized by its local ownership, small size, and limited capacity. These attributes explain their inability to meet this demand.

Islamic mortgage products are very expensive compared to conventional products in Australia and Canada, however, the spread is narrow in the US which reflects the maturity of the Islamic financial market in the US. This is due to the private and public sector securitizations of Islamic home finance instruments that present a wonderful opportunity to expand the market rapidly and has led to many entrants in the market, for example Guidance, Devon Bank, University Bank etc. However there is a gap in this success story. The Islamic financial market in the US is lagging behind other markets. For example, while London has been in a marketing mode as a world hub of Islamic finance the US regulators have been in exploratory mode. So far there have been five purely Islamic banks in the United Kingdom and none in the US. Financial institutions offering Islamic home finance products have found slim pickings in the US and many have withdrawn. The rewards are likely to be insufficient to tempt them. The uptake has been so weak in the US because the Muslim community is widely dispersed and well integrated, unlike the tight concentrations of culturally homogeneous groups found in UK cities. The implications of this dispersed community are that: First it will be hard for the Islamic mortgage providers to focus marketing campaign. Secondly, seeking regulatory approval in multiple states can be time consuming and expensive.

When looking into product offerings related to home financing, *Ijarah*-based contracts - *Ijara* and Diminishing *Musharakah* - are commonly used methods in the United Kingdom. In Canada and Australia *Ijarah wa Iqtina*-based contracts dominate. In the US *Ijara wa Iqtina* and *Murabahah* dominate. The average term of contracts is 25 years, the finance-to-value range between 80 percent-95 percent.

In the United Kingdom a level playing field has been established for these products. There is also the potential to take advantage of a cross-border services passport, which enables it to be offered across all European states without the need to open branches (Anile *et.al* 2007). On the other hand Islamic mortgage products in other Western countries are still facing legal and regulatory challenges.

Maladministration, deception and ethical behaviour lie at the root of the current financial problems. The Islamic principles of *riba* and *gharar* are concerned with issues of fairness and justice and also aim to make the financial system healthier and more stable rather than narrowly defined by efficiency. So, discussion of Islamic finance in connection with the international financial system introduces a welcome ethical dimension.

This study reveals that there is good indication for potential and effective demand for Islamic mortgages in the UK. Muslim households take both religious as well as financial implications into consideration regarding Islamic mortgages. This implies that demand for Islamic mortgages may not be a purely religious phenomenon. Hence suppliers of Islamic mortgages cannot put a significantly large premium on the *Sharia* compliance of mortgages that in itself is questioned by more than one third of the respondents (34 percent). Basically, this negative perception about the *Sharia* compliance of mortgages' credibility is due to the lack of awareness and information amongst Muslims. The perception about the Islamic mortgage is similar between different ethnics, and tenure groups. However, some Muslim ethnic groups are more willing than others to take on an Islamic mortgage even if it is more expensive than a conventional mortgage. These include the White and Pakistani Muslims, possibly because new Muslims tend adhere more strictly to their re-affirmed new religion than those who were born Muslim and Pakistani Muslims are more religiously educated and aware than other ethnic groups.

The results indicate that *Murabahah* was the most preferred mode of Islamic mortgage. However the majority were not sure about their knowledge of Islamic finance modes. This indicates that the majority of respondents are unaware and uneducated about Islamic mortgages models. The study also suggested the need for new products besides *Murabahah* and *Ijarah* to be subjected to more scrutiny and refining so as to make them more tolerable and attractive to the bank as well as the customers within the frame work of *Shari'a*.

Based on the perception analysis presented in the previous chapters, this study has established that there are five significant determinants of the demand for Islamic mortgages, namely marital status, the intention to buy a home in three years, preferred Islamic mortgage products, preferred Islamic mortgage providers and the awareness of the benefits of Islamic mortgages. These are crucial factors that drive the Muslim households' demand for Islamic mortgages (the positive relationship of household characteristics with Islamic mortgages demand have been presented in chapter 8). This result differs from previous empirical studies (*e.g.* Dar, 2004) on estimation of Islamic financial services demand, taking income and demographic parameters in a log-linear regression. However, these differences may very well be due to the fact that this study only focuses on the perceptions of Muslim households who are seeking Islamic mortgages. Also, it may very well be due to heterogeneity in questionnaire design and methodology. Other factors such as income, employment, qualifications and age are not statistically significant from the Muslim household point of view. These factors relate to the Muslim household's ability to repay, hence they are efficient determinants of the default risk from the Islamic mortgage providers' point of view.

The findings of this study demonstrate that many British Muslims preferred a full-fledged British Islamic bank to finance their homes. In other words, purely British Islamic bank will enjoy greater customer acceptance and will tend to develop a natural affinity with customers by offering an 'untainted' truly *Shari'a*-compliant product offering which is regulated by the FSA. Also this type of bank ensures that all supporting services, operations and processes are *Shari'a*-compliant. Alternatively 25.9 percent of the respondents accept the Islamic windows offered by the high street banks, or so called Hybrid Islamic institutions. This can be classified into two types: Islamic subsidiaries and Islamic windows. Islamic subsidiaries of conventional banks are separate entities with all supporting operations and processes ensuring *Shari'a* compliance. Islamic windows of conventional banks offer Islamic products alongside the conventional financial products and are admittedly the less *Shari'a* compliant of the two hybrid models. Nonetheless, the hybrid providers enjoy distinctive advantages in terms of leverage from their existing customer base and market infrastructure, established brand awareness, product development expertise, more competitive pricing and wider distribution channels.

The respondents are suspicious about foreign and small Islamic banks. This may be due to the fact that their products are generally uncompetitive in terms of pricing and that most were not regulated by the FSA. Hence, their consumers did not have the same protection as other consumers, such as the availability of the Financial Ombudsman Service and the possibility of redress from the Financial Services Compensation Scheme.

For Islamic mortgages to take off in the United Kingdom they need to be offered by major high street bank. Muslim communities identify strongly with their local area, hence banks with a strong regional presence in these areas of the country are well placed to serve this market. So far the industry has concentrated on providing mortgages and savings products for retail consumers, and growth has been modest. The tax and regulatory developments benefit the market and some firms are expanding their product ranges by offering new savings and investment accounts. Looking further ahead, there is scope to expand the market for Islamic products and services to non-Muslims as well as Muslims. It may be difficult to market Islamic mortgages, which address the relative minority who are prepared to make financial sacrifices in following their faith to non-Muslims. Nevertheless, Islamic mortgage providers can explore the equity release market, as in the UK this market is estimated to be in excess of £1 trillion worth of property owned free of mortgage by individuals aged over 65. If a sound Islamic investment product gave a better result than the conventional one this market segment could attract customers to release some of their equity via Islamic products (Cook, 2005).

The study also confirms that Islamic mortgages are a supply-led phenomenon in the United Kingdom, as it implies that the Islamic mortgages provider has to create a demand as there may not be an automatic demand. This is clearly evident from this study as only 8.4 percent are staunch demanders of Islamic mortgages in UK. Furthermore, 40 percent of the respondents stated that they would be willing to take out an Islamic mortgage only if the cost was similar to or less than a conventional mortgage. The respondents would demand an Islamic mortgage if it was sufficiently competitive *vis-à-vis* a conventional mortgage. The respondents considered religious as well as economic factors in choosing an Islamic mortgage. This finding is in conformity with previous studies that established the religious factor is not enough to encourage Muslims to use Islamic banking facilities e.g. (Rosly and Abu Bakar, 2003).

One of the important finding of this study is that relatives and friends are a powerful tool for marketing and influencing the respondents to take out Islamic mortgages. Islamic mortgage providers should consider the small minorities who do not speak good English and ensure greater awareness among those minorities of the services provided by them and should publish more information in relevant community languages for promotion and marketing as well as to encourage greater take–up of Islamic mortgages.

The most important main choice criteria identified by this study by which Muslims choose between different Islamic mortgage providers is the deposit required by the bank. While the least important main choice criteria by which Muslims choose between different Islamic mortgage providers is the reputation of the bank. The respondents, regardless of their ethnic background and kind of tenure, have assessed the main criteria that encourage them to take out Islamic mortgages without differences, while the result shows that there are differences between the respondent groups in how they rank the importance of the reputation of the bank as a mortgage provider. The reputation of the bank as a mortgage provider encourages more customers within the Black and Arab communities to choose their Islamic home loan provider than in the White, Pakistani, Bangladeshi, and Mixed communities. Such a finding will potentially have important implications for the marketing of Islamic mortgages, although an explanation is not immediately apparent. This is an area where further, more tailored research is required to produce a more complete understanding. Nonetheless, there are no significant differences between renters and homeowners regarding the effects of the main criteria encouraging them to choose their Islamic home loan from different Islamic mortgage providers available in the market. Although the study did not have an obvious explanation for this finding it is worth noting that homeowners generally have greater financial resources, higher levels of financial sophistication, and are more confident in handling debts than renters (Harney, 2006). This theory may in turn have implications for marketing Islamic mortgage products to homeowners. As such, Islamic mortgage providers can learn and plan to offer attractive schemes for the Islamic home finance market that meet British Muslims' needs.

The current structure of Islamic mortgages in the open market does not help low-income Muslim households. Islamic mortgages to date have been marketed to the wealthy members of the Muslim communities, but most Muslims in the UK can only afford much cheaper housing. As this study suggest the majority of the Muslim households are able to allocate only less than 10% of their income to meet mortgage installments. Similarly, almost half of the respondents believe that the expensiveness of Islamic mortgage does not help the low-income group to take their first step on the homeownership ladder. Hence, there is a need for the extension of Islamic home financing facilities for the "right to buy" and social housing sectors. This will enable many Muslims to avail themselves of the opportunities while staying within the ambit of their faith. Muslims represent a significant market for affordable homeownership through the shared ownership scheme, provided that the Islamic mortgages introduced in this scheme and appropriate Islamic financial products are available. Funding the co ownership scheme through Islamic finance can be done by the long-term saving schemes that lead gradually towards homeownership. Private Islamic finance can be raised to extend and promote homeownership among low-income Muslim households and social tenants. The closer the match between the requirements of the two parties, the investors or funding bodies and the Muslim Housing Associations, the more likely a good funding deal can be arranged. The required funding can be raised through the structuring of banking syndications involving all the Islamic mortgage providers. This type of investment could grow significantly if there is a lasting political consensus between the political parties regarding the key issues of Government subsidy to the Housing sector.

The prospects for Islamic housing finance in the United Kingdom is very promising as this study suggest that there is a great demand for Islamic mortgages, as 66 percent of the respondents said they are willing to take out an Islamic mortgage. Willingness to take out or switch to an Islamic mortgage provides a good indicator of demand for Islamic mortgages. The study classifies the demand for Islamic mortgages in the UK into three types. First, the conventional demand which sees Islamic mortgages as good and conventional mortgages also as good. The Islamic mortgage and the conventional mortgage are perfect substitutes for each other, only price matters. Secondly, the pent-up demand which considers religious and other factors in choosing a mortgage product and one is expected to switch to an Islamic mortgage if it is sufficiently competitive *vis-à-vis* the conventional mortgage. The third is the staunch demand, in which customers are motivated by a strong belief system for the Islamic mortgage and are expected never to enter into a conventional mortgage contract. This classification is important, as it allows the providers of Islamic mortgages to target the right population groups for different market campaigns. This is the best and only way to realise this demand by implementing the correct marketing strategies.

There is much that other Western countries can learn from the quarter of a century of experience in the UK. While now many in the Muslim community believe that Islamic mortgages are really taking off in the United Kingdom, some banks like HSBC admit that business in the US simply never took off (Bush, 2006).

The issue of taking out a conventional mortgage raises issues for Muslims today in a way that was not faced by their parents. For the first generation of Muslims the common solution of the housing problems was to buy a house outright without much concern for religious issue due to necessity. In the early 1960s this was fairly common practice even for indigenous British citizen. The mechanism by which the first generation Muslims achieved homeownership through outright purchase referred to in several studies such as Halliday (1992) in his studies of Yemenis. He says that a group of people would club together to save a certain amount per week, thus in a certain time a total pool of a house price was available and would be used to purchase a house for the first member of the club. All the members would then continue to save until some time later another house could be bought, and so on.

The study found that one of the barriers for homeownership in the British Muslim community is interest, as many British Muslims (36 percent of the respondents) were unable to get their foot onto the property ladder as a result of the interest-bearing mortgages being forbidden. This means that the issue of Muslims' financial exclusion is very relevant especially before 2003 when there was no alternative as the conventional mortgage products were inappropriate for Muslims. Thus, Islamic finance solutions serve to overcome financial exclusion, which works in line with current government's policies of social capital development and micro economy-based economic development strategies. It is, however, important that financial exclusion requires people with earnings. As this study indicates, Muslim are excluded not only because faith-based finance is not available, but also because they have not been able to integrate with the larger economy to have a stake through which they could have finances available for them to be included in the financial system, including in the Islamic finance sector, through various products.

It should also be noted that, as this study also indicates, the younger generation of the Muslim population is more inclined towards requiring Islamic finance solutions compared to the first and second generation. This is very much to do with identity politics, as the first and second generations attempted to make a home, while the third generation, who are educated, have informed choices about their lives including financial issues.

Unlike conventional banks' mortgages, those I have examined have not been financed by borrowing from wholesale markets, but rather from Islamic deposits. Islamic housing finance has proved sustainable, and has not been subject to the problems associated with sub-prime defaults. On the other hand the careful risk appraisal undertaken by Islamic institutions providing housing finance has made it more difficult for low-income Muslims or those with less secure employment to obtain *Shari'a* compliant mortgages.

9.4 RECOMMENDATIONS OF THE STUDY

The analysis presented in this study provides ample opportunity to reflect on the results in order to develop some recommendations to overcome the highlighted shortcomings, obstacles and difficulties facing the supply and demand of Islamic housing finance in the United Kingdom.

9.4.1 Supply Recommendations

1. Muslims in the United Kingdom identify strongly with their local areas and hence building societies with a strong regional presence in one or a number of areas of the country are well placed to serve this market.

2. The careful selection and good training of sale persons who promote the Islamic mortgage products face-to-face is important. Islamic mortgage providers need to ensure that they have competent staff who have the skills, experience and knowledge to do their job properly and safely under all working conditions.

3. Banks' publications should provide relevant information which is clear and concise. A positive message, such as stressing their ethical value, is better than just stressing prohibitions. Most people are aware of the prohibition of *riba*, but may be less aware of the ethical merits of Islamic products.

4. If Islamic mortgage providers can position their products to appeal more to the much larger non-Muslim population, then they can benefit from economies of scale, which would help their sustainability in the long term.

5. Banks can attract Muslim clients through Islamic mortgage products and then cross-sell other products such as interest-free student overdrafts, Islamic pension funds, child trust funds *etc.*

6. Islamic mortgage providers can explore the equity release market, as it is estimated that in the UK in excess of £1 trillion worth of property is owned free of mortgage by individuals aged over 65.

7. There is a need for new systems to mitigate the credit risk of Islamic housing finance. One possible solution is Islamic home insurance (home *Takaful*), which is based on the concept of mutual cooperation in the sharing of risk, to protect the Islamic mortgages provider against losses due to foreclosures. For Islamic mortgages to be sustainable the state may implement the Government guarantee system, or *Shari'a*-compliant system equivalent to the income support for mortgage interest scheme.

8. The required funding for *Shari'a-compliant* LCHO schemes can be raised through the structuring of banking syndications involving all the Islamic mortgage providers. This will allow spreading the financial risk as well as wider sharing of returns. The Muslim Housing Associations Companies can perform a significant agency role between banking syndications and the end beneficiaries of the LCHO schemes. Then financing can be negotiated and arranged through *Istisnaa* in the case of New Build Home Buying or through lease or *Ijarah* for Social Home Buying. Also, Muslim beneficiaries from these schemes should be involved in the process of designing their houses in line with the requirements of *Shari'a* and the prevailing social traditions.

9. Islamic mortgage providers have to realize the potential of the market in the LCHO schemes sector and, in order to safely fund the co ownership scheme and put its products on the market, they have to lobby the Government to accelerate the process of resolving the technical, legal and regulatory issues which may be very complex and long overdue.

10. Funding the co ownership scheme through Islamic finance can be done by the long-term saving schemes that lead gradually towards homeownership. Building and housing cooperative societies commonly use this practice.

11. Training opportunities in the field of Islamic financing techniques should be made available for personnel working in the field of housing in councils and boroughs that are populated by Muslims.

9.4.2 Demand Recommendations

1. Education to familiarise Muslims and other consumers with new products and new forms of finance are crucial. In this perspective the FSA, together with the Islamic finance industry, Muslims voluntary organisations, the media, and other concerned government agencies, should find ways to improve Muslim householders' financial capability.

2. Islamic mortgage providers, with the collaboration of Muslim Community leaders, need to put some effort into educating the public on adopting Islamic principles in their financial affairs. Furthermore, the banks should focus on explaining the nature of *Shari'a*-compliant mortgage products, as clients will be interested in these, because at the end of the day it is these that attracted them to the bank.

3. In order to meet ever-demanding customer needs, Islamic mortgage providers will need to develop not only pricing strategy but strategy surrounding the fundamental components of product pricing, product development, product distribution and delivery channels and lastly the branding and promotion of Islamic mortgage products.

4. There is a positive relationship between the potential demand for Islamic mortgages and the age of the respondents. Also the aspiration for home ownership is higher for the middle age groups. From this, it can be inferred that the middle age group are usually the ones with stable incomes and mostly have their own family and want to have a property to settle down in, thus, most buyers are in this age group. Hence, it can be stated that this particular age group has the enthusiasm and mortgage providers should realise this and maximise their promotion and utilise information among this particular group.

5. Demand in itself does not determine price, price ought to be determined by adherence to all Islamic codes of ethics. Prices must be kept at a reasonable level to make basic goods and services available to the public. Governments can intervene when there are distortions.

6. Islamic mortgage providers should consider those minorities who do not know good English and ensure greater awareness among them about the services provided by them. They should publish more information in relevant community languages for promotion and marketing as well as to encourage greater take–up of Islamic mortgages.

7. The issue of housing affordability has demanded the attention of lenders, financial advisers, and policy-makers.

8. Individual savings and deposits within the framework of housing schemes should be enhanced and encouraged to help solve the problem of affordability among the Muslim community.

9.4.3 General Recommendations

1. The provision of decent housing facilities for all citizens falls within the domain of State responsibility. Therefore, Islamic *Shari'a* has given much consideration to this subject.

2. There is a need for further development policies to help Muslims in the housing market and increase the rate of homeownership among the Muslim community.

3. Given the fact that Muslims are proportionately the biggest segment of society using social housing, there is a need to speed up the efforts in process to adopt the required adaptation of regulations in local authority and housing associations to enable Islamic housing finance in social housing.

4. Policy makers and relevant organizations have to ensure that greater awareness about services is provided by statutory and voluntary sector organizations as well as more information in relevant community languages, to encourage greater take-up of services.

5. The construction sector should be supported and the Government's plan to boost housing supply should be achieved with a view to making homeownership more affordable.

6. The potential of private Islamic finance can be explored further to improve the housing conditions of Muslim social tenants as bad housing conditions have economic and social costs that affect the whole community.

7. There is a need to establish an umbrella organization for Islamic housing finance such as the Council of Mortgage Lenders (CML) in the UK, European Mortgage Federation (EMF) and International Union for Housing Finance (IUHF) to organize workshops, seminars and conferences for financial institutions and housing corporations working in the field of Islamic housing finance at local, regional and international levels, to share their experiences, with a view to legal regulatory and product development.

9.5 LIMITATION OF THE STUDY

The issues identified under future research could have added more to the contribution of the study. When this study commenced there was not much research on Islamic housing finance in the United Kingdom. Nonetheless, the research adopted a general perception-oriented approach. However, focusing on a certain topic in the study of Islamic housing finance *e.g.* the attitudes held by non-Muslims towards Islamic housing finance, the role of the *Sukuk* in securitizing Islamic home finance products and linking the Islamic mortgage market to the international Islamic capital market and the actual effects of Islamic housing finance on Muslim homeownership patterns and political participation in the United Kingdom, as suggested in section 9.6, would have contributed more to the literature.

9.6 AREAS FOR FURTHER RESEARCH

In the course of this thesis, some specific areas worthy of further research have become apparent. Focusing on a certain topic in the study of Islamic housing finance would be very important and vital for the development of the sector.

1. Further research should be conducted to examine the attitudes held by non-Muslims towards Islamic housing finance.

2. Also further research is needed for the role of the *Sukuk* in securitizing Islamic home finance products and linking the Islamic mortgage market to the international Islamic capital market.

3. Future research is needed on the actual effects of Islamic housing finance on Muslim homeownership patterns and political participation in the United Kingdom. This could be approached through an analysis of quantitative data that might become available in future from Islamic mortgage providers and/or council of mortgage lenders.

4. Further tailored research is required to investigate the choice criteria of Islamic home financing for marketing Islamic mortgages among the different ethnic groups in the Muslim community to produce a more complete understanding.

5. Further research should be commissioned in connection with the LCHO schemes regarding house purchase, improvement and repairs to satisfy *Shari'a* requirements, especially in low demand areas which are populated by Muslim households.

6. Further research is required to survey the Islamic housing mode used by financial institutions in different countries and the similarities and differences of these financing techniques in various banks and countries should be noted.

7. Further research is needed to establish the credibility of Islamic mortgages, as many Muslims questioned the *Shari'a* compliance of Islamic mortgages. This could be due to the lack of information but nevertheless, it is an important issue bearing significant relevance to the demand for Islamic mortgages. Islamic mortgage models need to be carefully reviewed from the point of view of the *Shari'a*. One has to first determine what exactly is being practised and how. This can be done by reviewing the contract forms used by the banks for various Islamic mortgage models. Once the practice is established beyond any reasonable doubt, it may be submitted to independent *Shari'a* scholars for review.

8. Standardization is essential in order to promote honest competition and permit comparability of financial performance of different banks. A review of the Islamic mortgage models used by various banks and the determination of the exact nature of these models would also lead to their standardization as the banks themselves would know what other banks were doing and would be able to eliminate illegal and inefficient practices. Gradually standardization may

evolve over time through experience. Nonetheless, imaginative and innovative research may accelerate this process without trying the impossible unification of *fatwas*.

9. Research could also be undertaken on the various economic aspects of the Islamic housing finance techniques. Comparisons between these models and other questions on efficiency and stability, finance mobilization, promotion of economic justice, etc. need to be addressed in future empirical research.

Appendixes

School of Government and International Affairs
Institute of Middle East and Islamic Studies
Al-Qasimi Building
Elvet Hill Road
DURHAM AH1 3TU
UK
Tel: +44 (0)7866365770
Fax: +44 (0)191 334 5661
E-mail: m.e.k.mamoun-tameme@durham.ac.uk

Questionnaire for Muslim's households seeking Islamic mortgage in East London

The following questions relate to research conducted in Islamic housing finance at Durham University. I recognize that some of the information in this survey may be personal, but I assure you that the data will only be used in the aggregate to statistically compare different types of services provided. Your responses will be kept confidential.

Please answer the questions below by ticking the most appropriate answer or by filling in information.

Mohammed Tameme

Section One: Personal Details

Q.1. How old are you?
☐ 25 and under ☐ 26 – 35 ☐ 36 – 45 ☐ 46 - 55 ☐ 56 - 65 ☐ 66 and +

Q.2. What is your gender?
☐ Male ☐ Female

Q.3. What is your ethnic origin?
☐ White ☐ Indian ☐ Pakistani ☐ Bangladeshi
☐ Black ☐ Arab ☐ Mixed ☐ Others

Q.4. What educational qualification do you have?
☐ No formal qualification ☐ GCSE/ O levels
☐ A levels ☐ Professional qualifications (in Accounting, banking.. etc)
☐ BA or B.Sc. ☐ MA or PhD

Q5. Are you……….
☐ Working, for how many years have you been working?...................
☐ Retired, please specify how many years since you retired? (Then go to Q. 7)
☐ Neither, please specify--(Then go to Q. 7)

Q.6. Which industry are you working for?
☐ Public sector ☐ Finance ☐ Self employed ☐ Management and IT
☐ Health ☐ Education ☐ Others please specify…………………

Q.7. How much is your income?
☐ 10k and under ☐ 11k - 20k ☐ 21k - 30k ☐ 31k - 40k ☐ Over 41k

Q.8. How many dependents do you have in your household apart from your spouse (if you have one)?
☐ Less than 2 ☐ 2 - 4 ☐ 5 - 7 ☐ Over 7

Q.9.Are you
☐ Married ☐ Single (Go to Q. 16)
☐ Other with children (Go to Q. 13) ☐ Other without children (Go to Q. 16)
Q.10. Is your spouse:
☐ Working: Please specify how many years he/she works? --------- Years
☐ Retired: Please specify how many years since he/she retired? ----Years (Go to Q. 12)
☐ Neither: Please specify ---------------------- (Go to Q. 12)

Q.11. Which industry is your spouse working for?
☐ Public sector ☐ Finance ☐ Self employed ☐ Management and IT
☐ Health ☐ Education ☐ Not working ☐ Others please specify……

Q.12. How much is your spouse income?
☐ No income at all ☐ 10k and under ☐ 11k - 20k
☐ 21k - 30k ☐ 31k - 40k ☐ Over 41k

Q.13. How many children have you?

1	2	3	4	5	More than 5
☐	☐	☐	☐	☐	☐

Q.14. Does any of your son/s or daughter/s contribute to the finances of the household?
☐ Yes ☐ No (Go to Q16)

Q15. If yes, how much is her/his total earnings? (If you have more than son or daughter add their earning together)
☐ 10k and under ☐ 11k - 20k ☐ 21k - 30k
☐ 31k - 40k ☐ Over 41k

Q16. If you have another contributor to your finances how much is her/his total earnings? (If you have more than one contributor add their earning together)
☐ No other contributor ☐ 10k and under ☐ 11k - 20k
☐ 21k - 30k ☐ 31k - 40k ☐ Over 41k

Section Two: Financial Situation

Q.17. Do you have a bank account?
☐ Yes ☐ No (then go to Q20)

Q.18. If yes, is it with (you can tick more than one):
☐ A conventional bank: Please specify the name of the bank/branch……………
☐ An Islamic bank: Please specify the name of the bank/branch………………....

Q.19. What banking services are you availing? (You can tick more than one)
☐ Current account ☐ Saving account ☐ Investment account
☐ Overdraft account/Personal loan ☐ Debit card
☐ Credit card ☐ Home mortgage ☐ Islamic Home mortgage

Q.20. How far does your money stretch? (tick one answer only)
☐ We can mostly afford what we want, and often have money left over
☐ We can mostly afford what we need, but there is not much left over
☐ We struggle to make ends meet. (Please estimate how much the deficit per month £............)

Section Three: Home Ownership and Affordability

Q.21. Do you
☐ Own the house/flat you are living in: **are you.**
☐ Paying a mortgage (Go to Q29)
☐ An outright owner (Go to Q29)
☐ Rent house/flat you are living in

Q.22. If you are tenant what is the major reason why you have not bought a home? (You can tick more than one)
☐ Cannot afford a deposit for mortgage
☐ Cannot afford the repayments for mortgage
☐ Do not have a good enough credit for mortgage
☐ The home-buying process seems too complicated
☐ Cannot find Islamic mortgage provider
☐ Due to religious reasons, I can not take interest bearing mortgages

Q.23. What factors might encourage you to buy a home in the next 3 years?
☐ More affordable house prices ☐ Income rise ☐ New job
☐ House prices stable ☐ Stamp duty reduced ☐ Moving cost
☐ Need to get foot on ladder ☐ If get help with the deposit
☐ Provision of Islamic mortgages (interest free)

Q.24. If you rent your house/flat do you intend to buy a home in 3 years time?
☐ Yes ☐ No ☐ Not sure

Q.25. What factors might discourage you to buy a home in the next 3 years?
☐ High house prices ☐ Can not save deposit ☐ Income too low
☐ Job insecurity ☐ Expect house prices to fall
☐ Stamp duty ☐ Moving cost
☐ Non-provision of Islamic mortgages
☐ None

Q.26. Have you the funds for a deposit on a house?
☐ Yes ☐ No ☐ Not sure

Q.27. What proportion of your monthly salary would you be able to allocate to mortgage repayment?
☐ Less than 10% ☐ 10%- 19% ☐ 20%- 29% ☐ 30%- 39% ☐ 40% and more

Q.28. Would you be prepared to buy a leasehold property rather than freehold property?
☐ Yes ☐ No ☐ Not sure

Q.29. What are the major reasons to buy a home? (You can tick more than one reason)
☐ It is good long term investment ☐ Paying rent is not good investment
☐ To live in a neighborhood that you like ☐ Getting married and expecting children
☐ It provides the feeling of owning something of your own
☐ It is something you always dream of doing
☐ Encouraging by the discount in the “right to buy” scheme

Section Four: Islamic Mortgage

Q.30. Do you know that Islam as a religion has certain prescribed rules of financial matters?
☐ Yes ☐ No ☐ Not sure

Q.31. Do you know what is the difference/s between Islamic mortgages and conventional mortgages?
☐ Yes ☐ No ☐ Not sure

Q.32. Have you heard of the existence of the Islamic mortgage in UK?
☐ Yes ☐ No ☐ Not sure

Q.33. If yes, how did you find out about Islamic mortgage?
☐ Bank publications. ☐ Local Mosque ☐ Relatives /Friend
☐ Internet ☐ Newspaper/local newspaper ☐ Others

Q.34. Since Islamic Mortgages are now available, are you willing to take out the Islamic mortgage?
☐ Yes, only if the cost are similar or less than conventional mortgage
☐ Yes, no matter the cost, even if it is much more expensive
☐ Yes, if leading Islamic scholars have approved it
☐ No, Islamic mortgages are not possible
☐ No, whatever the difference between Islamic mortgage and conventional mortgage
☐ Not sure

Q.35. To what extent you agree with the statement that “the most important reasons, which attract you to the Islamic mortgage, are religious reasons”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.36. To what extent you agree with the statement that “Islamic mortgages are very expensive and requires a high deposit; this does not help people on low income or give them the same opportunity as others”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.37. To what extent you agree with the statement that “Islamic mortgage is very expensive and required high servicing charges”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.38. To what extent you agree with the statement that “you should take Islamic mortgage even the costs were higher than the conventional mortgage”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.39. To what extent you agree with the statement that “the Islamic mortgage is the same as the conventional mortgage pay interest except it’s dressed up as rent”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.40. To what extent you agree with the statement that “Islamic mortgage is perfect solution to Muslims, the high streets banks could have offered years ago, but at least it is step in the right direction at avoiding in dealing with interest based products”?
☐ Strongly agree ☐ Agree ☐ Uncertain ☐ Disagree ☐ Strongly disagree

Q.41. If you are aware of Islamic finance products, what type of Islamic mortgage products you prefer?
☐ *Ijara* (redeemable lease)
☐ *Murabhah* (installment credit purchase)
☐ Diminishing *musharkah* (declining balance partnership)
☐ Other
☐ I do not know.

Why did you choose this method? ---------------

Q.42. Which provider of Islamic mortgage you prefer?
☐ Stand – alone UK Islamic bank
☐ Stand – alone non-UK Islamic bank
☐ Islamic window offer by major high street bank and building society
☐ Others (please specify)………..

Q.43. How the scheme of introducing Islamic mortgage in buying social housing “right to buy” can facilitate ownership to you as Muslim renter?
☐ It is only way for you to become a homeowner
☐ It is away of buying without breaking the *Shariah* law and overstretching your finance
☐ You will never be a homeowner without introducing this scheme

Q.44. If Co-ownership scheme is available, would you consider it? (Co-ownership allows you to part-buy and part- rent your home)
☐ Yes ☐ No ☐ Not sure ☐ Never heard about it

Q.45. If you are to apply for an Islamic mortgage and there is a range of providers available in the market with different banks. What would be the main criteria to encourage you to choose your Islamic home loan?
Please place your choice in rank order from 1 – 5 using 5 to indicate the most important choice and 1 the not important choice

	1	2	3	4	5
The deposit amount required	☐	☐	☐	☐	☐
Choice of mortgages available	☐	☐	☐	☐	☐
The lend amount allowed	☐	☐	☐	☐	☐
The image and reputation of the bank	☐	☐	☐	☐	☐

Q.46. what language do you prefer when dealing with Islamic mortgage matters?
☐ English ☐ Your own mother tong language ☐ Others please specify…….

Q.47. Do you mind if non-Muslim clerk /sales person from banks to approach you for informing you and providing you with Islamic mortgage products?
☐ Yes ☐ No ☐ Not sure

If you have any further comments, please add them here:

Thank you for your co-operations
The identity of respondents will be treated in strict confidence and not revealed in the theses or any other publications. So if you want your copy of my findings, please provide me with your details and address:
Name………………………………
Address……………………………………………………………………………….
………………………………………………………………………………………..
Tel………………………………...
Fax………………………………..
E-mail…………………………….

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