

# Islamic Principles as a Predictor of Investment Behaviour of Muslim Investors in Delhi/NCR

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## Abstract

Investment by Muslim investors should be based upon 'shariah' (Islamic Principles). Religious beliefs and practices have an impact on the personal lives of Muslims around the world. This is a little researched area in behavioural finance particularly in India. A research gap was found that whether religious beliefs drive investment decisions of Muslims and to know the extent to which Indian Muslims stick to the Islamic laws of investment. Results of this study state that there is impact of Islamic religious principles on investment behaviour of Indian Muslims but strength of this relationship depends on level of religiosity of individual Muslim investor and influence of other Indian religion prevalent in society on lifestyle of Muslims.

**Key words:** Investment Behaviour, Religiosity, Shariah, Islamic laws, Muslim investors, interest income, risk.

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## Introduction

A change has been observed in the pattern of investment behavior across the world since last twenty years. Religion is deep rooted force while involving social or investment behavior. Just as man is social by nature, he is also religious. Religious beliefs and practices have a large impact on ethical, social, demographic, economic, saving and consumer behavior of people and influence their life on a routine basis. This study investigates the influence of religiosity on the investment behavior of the Indian Muslim investors in Delhi/ NCR. In particular, the study explores adherence of Indian Muslim investors to Islamic laws while investing and their attitude about interest income, ethical investment, conventional banking and risk aversion, investment in equity shares, mutual funds and life insurance schemes.

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## Culture and Religion

“Culture is defined as those traditional beliefs and values that cultural, religious and social groups spread as it is from generation to generation”. We all feel that we have a culture that we belong to and that makes us who we are (example, French, Spanish, Indian, Italian etc.). Culture is influenced by the dominant religion of a society. Human beings differ from each other in terms of personality and culture. One’s personality is bound with one’s culture. The cultural difference is crucial to understand religion (Nye, 2003).

The two key aspects with which religion can be associated are religious affiliation and religiosity. Religious affiliation refers to the specific religious group to which an individual belongs (Lehrer & Chiswick, 1993). On the other hand, religiosity is defined by (Worthington, Hight, McCullough, Berry, & Ripley, 2003) as “the degree to which a person adheres to his or her religious values, beliefs, and practices and uses them in daily living. The supposition is that a highly religious person will evaluate the world through religious schemas and thus will integrate his or her religion into much of his or her life.”

Religion gives meaning to life. It shapes the life. Furthermore, it is suggested that those who are strongly committed to religion are both attitudinally and behaviorally capable of making decisions consistent with moral conscience (Delener, 1994). A positive relationship exists between religiosity and ethical behavior and between religiosity and risk aversion (Hess, 2012). These relationships provided a hypothetical foundation for the focus of this study. Christian bible and Muslim Quran also supports the above relationships.

The most followed non-Indian religion is Islam. They are about 14% of India's population. Islam is the world's second largest religion with 46 countries having majority Muslim populations and many more having significant Muslim minorities.

### **Islamic laws 'Shariah'**

Wealth must be earned through "good", "productive" and "beneficial" work. This type of work is specified by the *Shariah* which defines the methods of earning wealth lawfully and also the types of economic activity which are prohibited are outlined. The *Shariah* specifies non-permissible professions and trade and economic activity which may lead to unlawfully acquired wealth. Even within each profession, the *Shariah* specifies proper and improper practices. Unlawfully acquired or accumulated wealth for its own sake is condemned as "corruption" and retrogression to the basis of all human negative qualities, i.e., greed (Wani, 2006). Investment permissibility for Muslims is decided by Islamic laws (shairah).

### **Interest & Islamic Banking**

Interest is defined in the Oxford English Dictionary as, "Money paid for the use of money lent (the principal), or for forbearance of a debt, according to a fixed ratio." In Islam, interest is forbidden (haram) in all its form. Muslims must engage in trade and commerce in accordance with the Islamic Shariah. No other issue has been condemned so strongly in the Quran as has usury. Usury is act of lending money at an exorbitant rate of interest. Quran speak against interest income.

Interest has become so completely institutionalized and accepted in modern economies that it is almost

impossible to conceive that there are some who completely oppose it. But there are devout Muslims who refuse to deal in interest.

Reason behind opposition to interest is that if an individual wishes to use his money to make more money, then he must be willing to put his money at risk. In other words, he cannot guarantee for himself a fixed return (whose amount keeps growing over time) regardless of the result of the investment that his money is used for. If he puts his money at risk, he is deserving of some share of the profits. However, this also means that he must accept losses if losses occur. This is a system that is based on justice.

The concept of Islamic banks brought in India in 2010 by Kerala government in Kochi. Islamic banks have the same purpose as the conventional banks except the fact that Islamic banks works as per the Islamic principles 'shariah'. Islamic banks are not operated under guidelines of RBI and cannot issue cheques. These banks do not have the status of conventional banks as do not provide interest and can be specifically called as financial institutions.

### **Equity and Debt Financing in Islam**

Quran speak against carrying debt (Hess, 2012). According to Usmani (1999), Muslims can invest in equity shares pursuant to three states of affairs. First, a Muslim can only invest in companies whose main businesses are compliant with Islamic Shariah (A few examples of businesses that are not Shariah compliant include companies that provide interest-based loans, insurance companies, companies that manufacture or sell intoxicants, pork, companies involved in gambling, nightclubbing nightclubbing, pornography, etc.). This prohibition extends to all facets of such activities and is not restricted to the supplier/manufacturers, but all involved in the supply chain. Hence, Muslims are forbidden to engage in certain activities in any manner what so ever and therefore investing in such companies involves a direct involvement with the forbidden activity.

### **Insurance in Islam**

Under common interpretations of Islamic law, conventional insurance is forbidden in Islam. Islam points out that paying money for something, with no

guarantee of benefit, involves high ambiguity and risk. One pays into the program, but may or may not need to receive compensation from the program, which could be considered a form of gambling.

### **Risk Taking in Islam**

Muslims are risk averse and thereby their investment behavior can be said to have some similarities with the Markowitz model and Islamic laws. In respect of “religious” Muslims, their investment behavior is more associated with Islamic culture than the assumptions underlying the Markowitz (1952, 1959) portfolio theory.

### **Literature Review**

Little empirical evidence related to impact of religiosity on financial/ investment decisions were established. Religion affects the way in which people behave (Sadler, 1970), and it is perceived that it may affect an individual’s perception (Eum, 2011). Religion helps the way to do things and serve a platform for social behaviour (Delener, 1994). Religion affects investment behaviour indirectly by shaping demographic behaviours (Choi J. S., 2001). Religion influences the way and attitude of people evaluating characteristics of the products (Choi, 2010; Delener, 1990, 1994). It is claimed that religion would affect individual behaviour directly through development of code of conduct (Sood and Nasu 1995). Culture affects the judgment or decision made by individual (Choi J. S., 2001). Inferring the social implications of religion by the social scientists started with the Karl Marx and Max Weber (1950).

Dan W. Hass found that there is a positive relationship exists between religiosity and ethical behaviour (Hess, 2012).

Farhana carried out a study in Bangladesh and said that Islamic capital market products, Islamic deposits and credit products have become increasingly popular in Muslims. Also Shariah does not allow Muslims to purchase insurance products, particularly life insurance. It is further advocated that Muslim consumers’ buying attitudes are positively influenced by their religiosity. That is, devout Muslims place greater importance on Shariah -compliant financial products than less religious consumers (Farhana, 2016).

Haron and Wan Azmi found Islamic banking abides by the principles of ‘shariah’. Contrary to the results, Islamic banking customers place profit motive above their religious motive when making economic decision (Haron and Wan Azmi, 2008).

Kaur & Vohra identified various factors affecting individual investment behaviour from available literature on it (refer table i). Personal values affecting individual investment behaviour include socially and religiously expressive characteristics that determine attitude of investors towards controversial stocks (Kaur & Vohra, December 2012). It is supported by observation that personal values such as socially and religiously expressive characteristics affect stocks owned by individual investor (Hood, Nofsinger, & Varma, 2011).

Lakshmeshwar found that investment in stocks of alcohol, pork or tobacco is not permissible in Islam (Lakshmeshwar, 2010).

Muhamad and S. Susela Devi observed that there is influence of religiosity on the investment behaviour of Malay Muslims. Speculative gains are mainly avoided by Malay Muslims. They ensure ‘shariah’ compliance in their investment decisions (Rusnah Muhamad, 2005). They concluded that the Islam religion had an impact on investment behaviour of Malay Muslims in Malaysia. Highly religious Muslim investors do not invest for speculative gains and ensure ‘shariah’ compliance before investment (Rusnah Muhamad, 2005).

Shakeel M. observed that religion strongly influences an individual’s emotional experience, thinking, behaviour, and psychological well-being (Shakeel, 2015 ). Relationship between Islamic religion and Muslim’s investment behavior were examined outside India, particularly in a Islamic and Gulf countries but not in India except the study done by Shakeel, M. (2015).

Tahir & Brimble concluded that Islam does influence investment behaviour. It is found Muslim investors in west comply less with Islamic laws, more with common law prevalent in west. However, the extent to which the Muslim adheres to the Islamic investment principles depends on their level of religiosity. Muslim culture does play an influential role in the investment behaviour in some of its religious adherents, it must be stressed that not each and every Muslim, abides by

Islamic law as some Muslims did choose, for example, to invest in banks, which is not permissible under Islamic law. In respect of 'religious' Muslims, their investment behaviour is more associated with Islamic culture than the assumptions underlying the Markowitz (1952, 1959) portfolio theory. Conversely, Muslims who are not religious behave like non-Muslims; therefore, their investment behaviour appears to be more aligned with the Markowitz model. It is evidenced that Islamic investors consider factors other than the risk, return, and religious concerns when making financial decisions (Tahir Imran, 2011). If main business of the company is in 'shariah' compliance but company earns some interest on its accounts, the Muslim investor doesn't retain the proportion of interest income included in the dividend received. This is called dividend purifying process. If Muslim shareholder sells the stock of such company, then also he give away the proportion of interest income from the stock price, he receives. Companies in Muslim countries mostly rely upon equity financing as debt financing is debarred in Islam. Speculative gains are prohibited in Islam (Tahir & Brimble, 2011).

Tao, Eric, & Johan found that geographical heterogeneity in religious beliefs is an important force shaping up financial decisions in modern finance world (Tao, Eric, & Johan, December, 2009).

It is concluded from above literature that religiosity influences individual's investment behaviour (Rusnah Muhamad, 2005) (Tahir Imran, 2011), demographic and economic behaviour (Lehrer, 2004), social behaviour (Delener, 1994), ethical behaviour and risk aversion (Hess, 2012).

Further, religion affects individual behaviour (Sood and Nasu, 1995), consumer behaviour (Choi Y. , 2010) and saving behaviour (Haron & Wan Azmi, 2008). Socially and religiously expressive characteristics of investors influence their decisions of investment in stocks (Kaur & Vohra, December 2012). But how far religious affiliation affects investment decision of individual in particular constituted the major concern of this study. To fulfil this research gap, the present research is an attempt to study influence of Islamic principles and beliefs on investment behaviour of Muslim investors in India with reference to Delhi/ NCR.

Little empirical evidence related to impact of religiosity on financial/ investment decisions were established. This provides an opportunity for the present study to explore the effect of Islamic principles on the individual investment behavior in India with geographical restriction to Delhi/ NCR. To fulfill this gap, the present research is an attempt to study religious influences in Islamic investment behavior in Delhi/ NCR.

## **Research Methodology**

### **Objectives of Study**

- To determine impact of Islamic beliefs and practices on investment behavior of Muslim investors.
- To find out factors influencing decision making of investment among Muslim investors.

### **Research Design**

This study used both qualitative and quantitative research design.

### **Data Collection**

Data collection for qualitative study is done through focus group discussions and in depth interviews with Muslim investors in Delhi/ NCR. Muslim investors, learned academicians and researchers from department of comparative religion studies, Islamic studies, and Muslim professors from Commerce, and Economics and Management departments at different reputed universities of Delhi & NCR were the respondent of in-depth interviews and focus group as they were considered to have comprehensive and thoughtful awareness on Islam as well understanding of individual investment behavior.

For quantitative study, data was collected through field survey based on the structured questionnaire filled by individual investors in Delhi/ NCR.

### **Tools for Data Analysis**

Qualitative study was analyzed using ethnography study and content analysis.

Data collected for quantitative study was tested for normality, validity and reliability. Independent variable

religious affiliation was on nominal scale (categorical). Dependent variables were on nominal and ordinal scale. To check the normality of data, Shapiro-Wilk's test was applied and to check whether the sample is true representation of population or not, Kolmogorov-Smirnov (K-S) one sample test was applied. Concurrent validity was checked based on literature review. Value of Cronbach Alpha coefficient was calculated to test reliability of instrument. Data is not found to be normally distributed. Therefore, non-parametric tests were used for data analysis in the study (Coopers & Schindler, 2013, 12th Edition).

To check whether individual investment behavior is independent of Islamic Laws, test of independence two-way chi square test was used. Descriptive statistics, histograms, frequencies and Cross tabulation, percentage, pie chart, plots and bar chart were used to describe respondent's characteristics, frequency of responses of each variable and comparing the responses religion wise.

### **Sampling Design**

Judgmental sampling method was used to get structured questionnaires filled as people hesitate to share their religious emotions and often reluctant to divulge their investment details. Sample size for survey with structured questionnaire was 315 individual investors out of which 117 were Muslim investors. Sampling area was Delhi/ NCR.

### **Data Analysis**

The data analysis is performed in two steps; qualitative and quantitative. Both studies are complimentary to each other. Qualitative study is based upon analysis of personal interviews and focus group while quantitative study based upon analysis of survey of structured questionnaire. Quantitative data analysis is further divided into data coding, demographic profile of respondents, cross tabulation and its graphical representation, construct validity and reliability, tests of normality and hypothesis testing. Hypothesis testing was done using Chi Square test. Analysis is preceded with interpretation of all sections. Test of normality includes Kolmogorov-Smirnov test and Shapiro-Wilk test. Qualitative study by way of one to one interview and focus group discussion were considered to be

enriched source for obtaining the information on investment behavior so as to bring facts and reality in results (See table 1 to 4).

### **Findings**

1. Muslims in Delhi/ NCR have less practice of investment as compared to investors of other religious affiliation do.
2. Muslims are forbidden to have income from interest, as a result of it, they do not invest in conventional banks, insurance, recurring and fixed deposit, mutual funds, shares of companies whose main business is not as per 'shariah'. They can invest in gold and real estate but as compared to other religions, Muslims rarely invest. But few Muslims keep their money in bank which is not permissible under 'shariah' which is also supported by Tahir & Brimble, 2011.
3. Few Muslims keep their money in bank which is not permissible under 'shariah' (Tahir & Brimble, 2011). This study contradicts the results.
4. Muslims are risk averse and their investments are found less in accordance with Markowitz model and more with Islamic laws. Muslims do not invest in shares of companies engaged in businesses are said to be not in compliant with 'shairah'.
5. Impact of culture, society and lifestyle priorities can be seen in modern Muslims which decrease the adherence of Islamic laws on Muslim's investment behaviour. Indian Muslims are found to behave differently than those in Gulf countries as religious commitment differs from one culture to another. Results are supported by study of Tahir & Brimble that Most Muslims in the west do not adhere with the Islamic laws rather they follow common law prevalent in the west. Muslim culture plays a considerable role in influencing investment behaviour but not all Muslims abide by Islamic laws.
6. Speculative gains, gambling and profit from taking risk is debarred in Islam. Debt is prohibited under Islamic principles. This finding is also evidenced in Muslim Quran speaking against carrying debt (Hess, 2012). The Muslims in the

west take home loan (Tahir & Brimble, 2011) which is in contradiction of the finding. This is understandable from above conclusions that Islam does influence the investment behaviour, and however, the degree to which it does depends upon religiosity of investor and influence of Indian culture.

### **Contribution/ Implications of the Study**

Behavioural finance theories are extended that not only the market information structure but the religious affiliations of the Muslim individual investor also influence the investment decisions/ patterns. As interest is prohibited, money lending and interest based investments are not encouraged in Islam whereby flow of money in Indian economy may hinder and it may result in negative effect on development of India. This study facilitates the fund managers to design investment products according to the need of the Muslim investors. Muslim investors should be provided with the investment solutions in adherence to the aforesaid laws.

An important implication of the study is to motivate the Muslim community who invest less in comparison to other communities. Islamic banking should be promoted in India. Such products are available in financial markets of Muslim countries.

This study can be proved as an opportunity for Indian banks and financial institutions to design 'shariah' compliance investment products. From a private client portfolio management perspective, once prepared with Shariah -permissible products, an investment committee at an Islamic private wealth firm would face the same issues as any other, namely, how to develop, implement and monitor an investment policy consistent with a client's objectives. They may explore the market of shariah- compliant instruments exist in Islamic countries which may be proved helpful for designing Islamic products.

Managing assets in accordance with Islamic precepts will be unique in that the practice is socially accountable investing with the unique specification of avoiding interest bearing investments of any kind.

Because borrowing and setting aside excess funds in short-term, low-risk, interest-bearing instruments are

integral to corporate finance, the application of Islamic law to corporate finance poses some challenge for fund managers.

Portfolio constructors need to be aware of the degree of variance in religious adherence of Muslim investors. Additional challenges exist, namely the lack of secondary market for these products and the lack of uniform standards in the selection process across the Muslim world.

### **Limitations of the Study**

The time and the resource constraints of present study have imposed the following restrictions:

- 1 The study has geographical restrictions to Delhi/ NCR.
- 2 Reluctance of the respondents to provide the complete information being a sensitive issue can affect the reliability of the responses.
- 3 The sample size of quantitative study was limited to 315 respondents only, even though 450 were served.
- 4 Possibility of external validity issue may be a limitation.
- 5 Impact of demographic variable and Cultural and societal influence was not controllable and could affect results.

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## APPENDIX

**Table 1: Data Coding Scheme for Dependent Variables**

Constructs	Variables	Response	Coded Value
Preferred investment Avenues	Saving bank account	Never	1
	Recurring deposit	Rarely	2
	Fixed deposit	Sometimes	3
	PPF/ NSC	Often	4
	Insurance	Frequently	5
	Shares		
	Mutual funds		
	Precious metals/ gold		
	Corporate bonds		
	Real estate		
Other factors influencing investment decisions	Attitude towards savings	No	1
	Attitude towards debt	Neutral	2
	Attitude towards interest.	Yes	3
	Attitude towards donations to poor or needy.		
	Attitude towards insurance.		
	Attitude towards risk tolerance.		
Objectives of Investment	Safety of principal money	Strongly Disagree	1
	Return/ Interest	Disagree	2
	Save income tax	Neutral	3
	Future Security	Agree	4
		Strongly Agree	5
Financial obligations	Education of children	Strongly Disagree	1
	Marriage of children	Disagree	2
	Buying house	Neutral	3
	Health security	Agree	4
	Retirement planning	Strongly Agree	5
Mode of fulfilling financial obligations	Prefer to fulfill financial obligations through savings	No	1
	Prefer to fulfill financial obligations through loan	Neutral	2
	Prefer to fulfill financial obligations through savings and loan both	Yes	3

**Table 2: Reliability Statistics**

Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	Number of Items
.756	.759	315



**Table 3: Tests of Normality**

Variable	Kolmogorov-Smirnov <sup>a</sup>			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
Saving Bank Account	.238	315	.000	.825	315	.000
Recurring Deposit	.211	315	.000	.838	315	.000
Fixed Deposit	.190	315	.000	.884	315	.000
PPF/ NSC	.242	315	.000	.840	315	.000
Insurance	.248	315	.000	.891	315	.000
Shares	.289	315	.000	.795	315	.000
Mutual Funds	.282	315	.000	.809	315	.000
Precious metals/ gold	.173	315	.000	.910	315	.000
Corporate Bonds	.374	315	.000	.675	315	.000
Real Estate	.154	315	.000	.889	315	.000
Attitude towards savings	.244	315	.000	.787	315	.000
Attitude towards debt	.356	315	.000	.714	315	.000
Attitude towards interest	.341	315	.000	.727	315	.000
Attitude towards donations to poor or needy	.392	315	.000	.664	315	.000

**Table 4: Results of Chi-Square Tests for Influence of Religious Affiliation on Individual Investment Behavior**

Variable	Value of Test			Result
	$\chi^2$ Value	Degree of Freedom	p value	
Saving Bank Account	173.444	12	.000	Significant
Recurring Deposit	77.193	12	.000	Significant
Fixed Deposit	117.243	12	.000	Significant
PPF/ NSC	71.619	12	.000	Significant
Insurance	95.650	12	.000	Significant
Shares	102.538	12	.000	Significant
Mutual Funds	175.847	12	.000	Significant
Precious metals/ gold	146.951	12	.000	Significant
Corporate Bonds	56.594	9	.000	Significant
Real Estate	104.897	12	.000	Significant
Attitude towards savings	42.158	6	.000	Significant
Attitude towards debt	77.189	6	.000	Significant
Attitude towards interest	89.167	6	.000	Significant
Attitude towards donations to poor or needy	51.031	6	.000	Significant
Attitude towards insurance	52.856	6	.000	Significant
Attitude towards risk tolerance level	48.019	6	.000	Significant
Safety of principal money	65.916	9	.000	Significant
Return/ Interest	104.821	12	.000	Significant
Save Income Tax	85.340	12	.000	Significant
Future Security	24.748	6	.000	Significant
Education of Children	50.554	6	.000	Significant
Marriage of Children	46.359	6	.000	Significant
Buying House	126.956	9	.000	Significant
Health Security	100.045	9	.000	Significant
Retirement Planning	71.044	6	.000	Significant
Prefer to fulfill financial obligations through savings	31.731	3	.000	Significant
Prefer to fulfill financial obligations through loan	150.733	6	.000	Significant
Prefer to fulfill financial obligations through savings and loan both	34.377	6	.000	Significant