The Recent Turmoil and Monetary Policy in a Dual Financial System with Islamic Perspective

By
Prof. Dr. Zubair Hasan

Abstract

The financial turmoil that the 2007 subprime debacle of the US set into motion has raised a welter of puzzling questions for the policy makers across the world. The position seems all the more confusing in the Muslim world where the fast expanding Islamic finance operates in competition with the conventional in a dual setting.

The turmoil has led many to blaming the private lure for the colossal failure of financial institutions. In contrast, others counter argue to put public policy in the dock under the exalted banner of 'regime uncertainty'. They blames the aggravation of the trouble on the uncalled for government intervention in financial markets. Interestingly, few draw attention to moral crimes committed on either side of the fence among the causative factors.

This paper seeks to investigate if the monetary policies the Central Banks follow - now including the Basel capital adequacy norms as well - would suit or suffice Islamic banking institutions competing with the conventional in a dual financial framework? In this context, it questions the claim that risk-sharing is or can alone be the basis for Islamic finance.

Self-Adjusting Profit Sharing Ratios for *Mushārakah* Financing

By
Dr. Volker Nienhaus

Abstract

Islamic economists have propagated contractual arrangements for a sharing of profits between capital providers and entrepreneurs and the bearing of losses by the capital providers (mudārabah, mushārakah) as the "true" Islamic alternative to interest-based debt financing. But this ideal is very difficult to implement in a world with distinct information asymmetries, self-interested market players, adverse selection problems, and debt-like Shariah compliant financing techniques with more predictable and less risky financing alternatives. Wrong profit expectations at the beginning of a profit and loss sharing contract can adversely affect the return on the invested capital. The standards of the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) has come up with a number of possible corrections for expectation errors, but they all require a consensus of all contracting parties on a modification of the initial agreement. Since the purpose of re-negotiations is a re-distribution of profit shares from one party to another party, a consensus among self-oriented actors is not very likely. The proposal of a self-adjusting profit sharing ratio obviates the need for discretionary re-negotiations. It uses elements from AAOIFI standards to structure a contractual arrangement that maintains a distribution pattern which was initially agreed upon by the contracting parties. It does so by an automatic adjustment of the profit sharing ratio whenever new information on the expected profit becomes available. This reduces the impact of information asymmetries and reduces the risk of adverse selection, and the formula for the profit sharing ratio can be calibrated such that a risk aversion of the financier is factored in.

Withdrawal Behavior of Malaysian Islamic Bank Customers: Empirical Evidence from Three Major Issues

By
Muhamad Abduh

Abstract

As interest is prohibited, the reliance of Islamic banking towards bank deposits from depositors is higher than conventional banking. Efforts that could help in preventing funds withdrawal by the depositors thus become necessary in order to avoid bank instability. This study is aimed at investigating factors that may influence the withdrawal behavior of Malaysian Islamic banks customers. The withdrawal behavior studied here is in conjunction with three major issues which are (i) issues of non-shariah compliance, (ii) lower returns as compared to other banks, and (iii) rumors about forthcoming financial crisis that may affect the performance of the bank. The research employed a direct survey through a self-administered questionnaire handed out to Islamic banks customers in Malaysia using the multi-stage sampling technique. The intention to avoid interest, type of account, working status, bank status, and bank ownership are the significant factors that could influence withdrawal behavior in model 1. Working status and bank ownership are the factors which influence withdrawal behavior in model 2. Lastly, for model 3, factors that emerged to be significant are type of account, total deposit in bank, awareness on deposit insurance, intention to avoid interest and perception that Islamic banks are less affected by the crisis.

Role of Islamic Banks in Energy Finance in Pakistan

By
Salman Ahmed Shaikh

Abstract

Energy crisis in Pakistan has worsened in recent years leading to loss of output, increased incidence of manufacturing unemployment, cost push inflation, capital flight, low manufacturing capacity utilization and loss of export markets. The contributing factors to the crisis include inefficient energy mix, price distortions and low investment in alternate energy. The short term measure by the government to absorb loss from price distortions created by an inefficient energy mix has resulted in ballooning fiscal deficit. One important piece of solution lies in increased availability of financing for energy infrastructure. In this paper, we analyze the role of Islamic banks in fulfilling this need. Islamic banking in Pakistan has exhibited exceptional success in terms of assets growth. Within 10 years, the niche market now comprises almost 10% of the overall banking sector. However, questions are still raised about its differential economic merit and contribution to the economy. Energy financing presents a vital opportunity for Islamic banks to show their importance and contribution through financing energy infrastructure. We argue in this paper that Islamic banks will themselves benefit from increased financing to energy sector since it will help them i) narrow their banking spreads, ii) increase financing to deposit ratio and iii) reduce operational inefficiencies. Economy wide effects of resolution of energy crisis will help in increasing investment, productivity, fiscal space and export competitiveness. It will also help in reducing crowding out of private sector credit, capital flight and deindustrialization.

Consumer Perceptions of Islamic Banks: The Case of Saudi Arabia

By
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Bukhari M. S. Sillah

Abstract:

There is no clear line and distinction between Islamic and conventional banks in Saudi Arabia. Banks which are perceived as non-Islamic banks do offer various types of Islamic banking products beside their conventional products. Some of the banks are full-fledged Islamic banks. However, the Saudi Arabian banks do not carry the word "Islamic" in their names, as it pertains in U.A.E, Malaysia, Pakistan etc. So, it is hypothesized that the general public might not attach significance to the distinction between Islamic and conventional banks. This paper is conducted to assess the perceptions of Saudi Arabian people of Islamic banking in Saudi Arabia, and to draw conclusions from their views about the degree of the Shariah compliance of the Islamic banking practice. The results of this paper imply that the customers are generally satisfied with the Islamic banking practice, but they want them to do more than current level because they perceive that their banking operations are just marginally Shariah compliant. The customers also generally disapprove of the window Islamic banking by the conventional banks.

Analysis Of The Efficiency Levels Of The Sharia Rural Banks In Indonesia Using The Method Of *Data Envelopment Analysis* (DEA) and ITS Correlation With Camel

By
Muhamad Nadratuzzaman Hosen
& Syafaat Muhari

Abstract:

*The magnitude of the potential micro banking market has to make profits makes this segment important for rural banks (*BPR), *especially Sharia Rural Banks (*SRBs). *Thus,* the *efficiency for SRBs is required to survive amid the competition. This study used* non-*parametric data envelopment analysis (*DEA) *with the operational approach to analyze the efficiency levels of* 73 *SRBs during the periods of 2nd Quarter- June 2011to 1st Quarter- March 2013*. The level of *SRB's efficiency* can be *integrated with the performance of banks* which is adopted from Central Bank (BI/Bank Indonesia) criteria, namely *CAMEL (*Capital, *Asset-Quality*, *Management*, *Earnings and liquidity*). Based on the Spearman correlation, the result of this study indicated that the level of efficiency of SRBs using the DEA method has a real but weak relationship with the CAMEL. *In addition, this study also showed that the SRB is less efficient than Sharia Banks (*BUS).

An Application of Shariah Contract on Islamic Retail Investment Products: An Overview on Malaysia Practice

By
Ahmad Aizuddin Hamzah
Farah Shazwani Ruzaiman
Haneffa Muchlis Gazali

Abstract

The Islamic investment deposit product is one of the tools which increases the capital source of the Islamic financing facilities. As an alternative to the conventional interest-based investment deposit product, the Islamic bank used the profit sharing analysis or also known as mudarabah contract for their investment product. But, despite a few issues with mudarabah investment deposit product and additional rules of the Islamic Financial Service Act 2013 on the Islamic deposit product, many Islamic bank looks at other alternative on their investment deposit facility. Therefore, the introduction of commodity murabahah or tawarruq-based deposit could be the best alternative to take its place. Hence, this paper aims to explore the current Islamic deposit products which are available in Malaysia market. The discussion will include the shariah contract used, the product mechanism and framework and the differences.