

A STUDY ON THE CHALLENGES AND PROSPECTS OF ISLAMIC BANKING IN SULTANATE OF OMAN

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Abstract

The purpose of this study is to investigate the opportunities of development and growth as well as the main challenges to Islamic banking in Oman. Islamic Banks adhere to the concepts of (Sharia'ah) Islamic law. The basic sources of shariah principles are taken from the Holy Book "Al-Quran" which is followed by the consensus of the jurists and interpreters of Islamic law. The shariah prohibits dealing with interest (Riba) in any shape or form which is an essential feature of the Islamic Banking system. The study identified the phenomena related to the future of Islamic Banking, customer's attitudes of Islamic Banking and the effect of Islamic Banking on the economy growth of Oman. This study is also focused on the impact of SWOT Analysis in the recent growth of Islamic Banks in Oman. However, few studies have examined the impact of Islamic banking through SWOT analysis. To fill this gap in the literature, this paper investigates the potential effects of Islamic banking by SWOT analysis. In addition, the Islamic banks in Oman cover larger investors and depositors base and are intended for both Muslims and non-Muslims and also contribute positively towards the country's macroeconomic stability.

Keywords: Riba (interest), Shariah (Islamic law), Islamic Banks; Macroeconomic stability; SWOT Analysis.

1. INTRODUCTION

Islamic banking is currently one of the fastest-growing segments of the financial market industry, operating in over 75 countries through 300 institutions. According to the latest statistics, Islamic banks have a presence in 53 countries on five continents – 65% of which are in the Middle East, 81% in the Arabian Gulf region, 41% in Europe, 7% in the USA, and 3% in Africa. Islamic banks are witnessing steady and continuous growth as they seek to enhance their presence in the different parts of the world, including in non-Muslim countries. Islamic banking 'windows' are now common in many Western countries including the UK and France – where the conventional banking system is based on interest rates (Riba). Transactions in Islamic banks are governed by Islamic Shari'a and jurisprudence, as extracted from the Holy Quran and prophetic traditions. Confirming the past research, Muslim prevalence in a population is found to be the most significant determinant of the diffusion of Islamic banks. Empirical analysis disaffirms the hypothesis that Islamic banks minimize the explanatory power of legal origin on economic growth due to their independent implementation of Shariah law; the results show that accounting for Islamic banks has no effect on the determinative power of legal origin. Islamic Banking is banking based on Islamic law (Shariah). It follows the Islamic rules and practices primarily from the Holy Quran and secondarily from the opinions collectively agreed among shariah scholars. The shariah board is a key element of the structure of an Islamic financial institution, carrying the responsibility of ensuring that all products and services offered by that institutions are fully compliant with the principles of shariah law. Shariah law is derived from Quran and the sunnah. The decision to license the provision of Islamic Banking services in Sultanate of Oman have been announced in 2011. The Islamic banking is expected to experience a rapid growth. The main objectives of this decision were to create a stable Islamic finance industry offering credible banking proposition that complies with international best practices, protects customers, and reflects Shari'ah. All listed Omani banks like Bank Nizwa Islamic bank, Alizz Islamic Bank Islamic bank, (Alhalal) Alahli bank Islamic window, (Muzn) Bank Dohfar Islamic window, (Meethaq) Bank Muscat Islamic window,(Misarah) National Bank of Oman Islamic windows.

2. SIGNIFICANT OF THE STUDY

The Islamic banks have significant roles in the social responsibility. Moreover, the core and guidelines of Islamic economics spontaneously achieve the justice and equality, an example for that, the Zakat payment on annual basis by the Islamic banks which goes to the needy people and zakat channels as outlined in the Holy Quran, as it helps in alleviation of poverty. Zakat is a religious levy deducted from the bank net income and to be paid annually. Furthermore, Social responsibility of Islamic banks refers to all activities carried out by it, to accomplish religious, economic and ethical responsibilities.

The establishment of the local savings bank in Egypt in 1963 marked the beginning of the Islamic banking system. The undertaking was based on Mudaraba (legitimate speculation), through collecting individual savings from people and investing them through Islamic banking systems, and allocating profits as agreed upon with all parties. Similar trials took place at Hyderabad in India, Malaysia, and Pakistan.

In addition, several Islamic governments proposed initiatives to strengthen the concept of Islamic banking. For instance, the establishment of the Islamic Development Bank (IDB) in 1975 in Jeddah, KSA, which provides support for Islamic banking

growth and International Union for Islamic Banks, established in 1977 in Makah, KSA, to promote Islamic values and coordinate Islamic banking activities.

The subsequent international initiatives were a decisive step in contributing to the integration of the Islamic banking system and turning the dream into reality. This has led to the establishment of Islamic banks in the several countries around the world. A few of the examples are:

- Dubai Islamic Bank, which was established in UAE in 1975. The bank is the first integrated model for an Islamic Bank;
- Bahrain Islamic Bank in 1979 and
- Abu Dhabi Islamic Bank in 1997.

Many countries such as Pakistan and Sudan were inspired into transforming their traditional banks into fully-integrated Islamic banks.

The values guiding Islamic finance are the same as those of Islam. These principles are inspired from 'transactional jurisprudence'. The rules and practices of 'transactional jurisprudence' are taken from the Holy Quran; the prophetic traditions; other secondary sources, such as consensus of views of Islamic scholars; analogous incidents; and personal deduction (Ijtihad).

Islamic banking seeks to promote the ideals of a prosperous society and stable economy. It offers a commercially viable alternative to Riba-based finance based on the values of fairness, ethics and compassion.

In fact, Islamic banking was created to benefit, directly and indirectly, all members of the communities that it serves, under Shari'a law.

3. REVIEW OF RELATED LITERATURE

While the initiation of modern Islamic Banking dates back to 1963, the present-day practice debuted in 1975. When banks were established and mandated to operate in adherence to Shari'a rules and principles. Ever since, Islamic Banking has been one of the fastest growing sectors in the global banking industry. As new geographies continue to open up to Islamic Banking, industry forecasts suggest that Islamic Banking assets held by commercial banks globally will continue to grow. The pace of growth has increased dramatically over the past decade driven by awareness and demand, as well as easier access to Islamic Banking services. Across world markets, and particularly in the GCC, South-East and South Asia (which is home to over 50% of the total Islamic Banking industry), the strategy has been to allow a dual banking system, whereby Islamic Banking co-exists with conventional banking.

The growth of the Islamic Banking industry has been fuelled by surging demand for Shari'a-compliant products, not only from financiers in the Middle East and other Islamic countries, but also by investors worldwide, thus making it a global industry. Besides its vast geographical expanse, Islamic Banking is witnessing rapid expansion across the whole spectrum of financial activities including personal banking, insurance and capital market investments. The continued growth in the Islamic banking industry is attributable to three factors: increasing demand from a large number of Muslim communities (including Muslim immigrants to western countries); oil wealth in GCC countries; and the growing attractiveness of Shari'a-compliant financial services to non-Muslim investors seeking 'ethical' investments and banking practices.

Oman's Islamic banking (including Islamic windows) is expected to continue its steady growth over the coming years. Reports and banking experts are also expecting that Oman should witness a growth of sukuk as local and regional players look to raise funds in a Shari'a compliant manner.

Principles of Islamic banks in Oman are as follows

- The absence of interest-based (Riba) transactions.
- The avoidance of economic activities involving oppression (Dhulm)
- The avoidance of economic activities involving speculation and uncertainty (Gharar)
- The avoidance of speculative activities (Qimar)
- The discouragement of the production of goods and services which contradict the injunctions of Islam (Haram).

4. CHALLENGES OF ISLAMIC BANKING IN SULTANATE OF OMAN

Islamic banking in the recent trend is doing well in the Oman economy, but some of the potential opportunities and challenges should be taken up to make Islamic banking more user-friendly in every segment of economy and society. The fear of loss is one of the biggest barriers for fund mobilization for Islamic banks. In some cases, it leads to withdrawal of

funds. The investors should be provided with some kind of protection like supervision of Islamic banks by government regulations. At present, lack of effective prudential regulation is one of the weaknesses of the Islamic banking industry. Some of the challenges faced by Islamic banks in Oman are as follows:

- Islamic banking industries have always suffered from the issue of different opinions of Islamic scholars, suppose a product or practice may be accepted to one scholar, could be considered un-Islamic by another scholar.
- It also faces the difficulties of lack of authentication of decisions because there is no unity in the Muslim community they have the different believes it is possibility that some decisions are not acceptable to one part of the community.
- There is a serious shortage of scholars and qualified managers.
- It is not well regulated at the moment because branch network is limited.
- The lack of skilled and trained professionals to fulfill the requirements of this fast growing industry.
- It also faces business constraints due to the undeveloped money market.
- Lack of public awareness, building trust and market acceptability

5. SWOT ANALYSIS OF ISLAMIC BANKING SYSTEM IN SULTANATE OF OMAN

STRENGTHS	WEAKNESS
<ul style="list-style-type: none"> • Oman citizens are 100% Muslims. • Any form of interest, either paid or collected, is prohibited • Any investment in activities such as alcohol, ham, weapons, immoral businesses or transactions against the tenets of Islam is prohibited. • Any transaction that includes fraud or gambling is prohibited. • Sharing loss, profits and risk as per the agreement of partners is permitted. • A trader should be in possession of the items to be sold so that he can bear any loss or damage. • Islamic banks are responsible and obligated towards the community to carry out a fully Shari'a-compliant banking and services and to obey the rules of Islam in all dealings and businesses, this is in regard to the religious responsibility. • The new Islamic banks are likely to have funding cost advantages as they raise low-cost deposits. 	<ul style="list-style-type: none"> • New Islamic BANKS set up in Oman will struggle initially to compete with established conventional banks offering sharia-compliant services when the country opens up its BANKING market • The microfinance products contribution in the community by financing is focused only on the limited income category. • Absents of a specific Regulatory Authority structure of Islamic Sha'riah Board in Oman. • Shortage of scholars and qualified managers • The absence of Islamic banking laws in Oman.
OPPORTUNITIES	THREATS
<ul style="list-style-type: none"> • This country follows Islamic religion and Sha'riah law. • Islamic banking arm should be launched in Oman and other nations. • Issues related to Islamic banks can be addressed by setting up Sha'riah Board. • It is considered as the Fastest growing economy of Oman • As per the demographic study, the majority of the population are Muslims (including expatriates) • As the Islamic Banking is in the initial stage in the Sultanate; there is ample of opportunities for educating youth to pursue his/ her career in it. • Recently public are aware of Islamic banking and its fortunes, hence there is wide scope for further development. 	<ul style="list-style-type: none"> • Rising economic uncertainties. • Lower growth than expected in the Asian countries that are major importers of Omani Oil. • Most of the customers retain their primary banking relationship, assuming that there are no significant differences in the terms and offer given by the Islamic banks. • Wrong understanding or misconception against Islamic Banking • The decline of crude oil price in the international market. • Lack interest among youth to do professional career in Islamic banking • Lack interest among students for higher level academic achievement.

6. CONCLUSION

The researchers reviewed on the different aspect of Islamic banking mainly about concept and practice of Islamic banking in Oman. Oman is the one of the hub of Islamic financial activity in the Middle East and the researchers also discovered that Oman based conventional Banks with Islamic banking window provides its best services in compliance with Sha'riah law that fulfil the requirements of Muslim community in different sectors especially in Ijarah (leasing), Takaful (insurance) Sukuk (bond) and also provide services in home finance, personal loan, current and saving accounts. Islamic banking is facing great challenges due to lack of deep awareness among the public. In Oman Islamic Banking have great opportunities in terms of growth prospects, because a large number of Muslims from all over the world living in the Oman are playing their role effectively and contributing towards the country's national economic growth.

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