CHAPTER – VII

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7.1 Major Findings

7.1.1 Efficiency of Islamic Banking at World Level

There are five Data Envelopment Analysis (DEA) used for measuring the efficiency such as cost, allocative, technical, pure technical and scale efficiency course. They were calculated and correlated with conventional accounting measures of performance and they were also correlated with Return on Asset (ROA) and Return on Equity (ROE) suggesting that these efficiency measures can be usual, concurrently with conventional accounting ratios. The average cost efficiency is 74 per cent whereas profit efficiency is 84 per cent. Although Islamic bank at the world level are less efficient in containing cost, they are relatively efficient in generating profit. The average allocative efficiency is 74 per cent whereas the average technical efficiency is 84 per cent. This means that dominant source of inefficiency is due to allocative inefficiency rather than technical inefficiency. These results are consistent with the fact that the Islamic banks operate in overall regulatory. Average scale efficiency is about 85 per cent and average
pure technical efficiency is 95 per cent. The result shows that there has been good increase in productivity growth over the years, 1997-2006. The results of show that larger bank size and greater profitability are associated with higher efficiency—supporting the economies of scale arguments in Islamic banking industry.

Islamic banking emerged as a response to both religious and economic exigencies. While religious exigency calls for avoiding any transaction based on interest, economic exigencies, on the other hand, provide a new outlook to the role of banking in promoting investment/productive activities, influencing distribution of income and adding stability to the economy. Islamic banking is thus perceived as an improved system in all dimensions. However, in order to sustain in the long-run, the Islamic banking system has to be internally efficient and technologically advanced in order to compete with its conventional counterparts. Even by avoiding interest if Islamic banks can maintain at least the same level of conventional banks indicates the good success of Islamic Banks. If the efficiency results of Islamic Banks are greater than conventional banks it indicates the tremendous success of the Islamic Banks over the conventional banks.

The study also shed some light on the development of Islamic banking globally and this sector has grown not only in the Muslim world, but also has gained significant attention in the Western world as well, with over 250 Islamic banks worldwide and managing assets and client money around, US$ 400 billion. Hence, the growth of these banks is a proof of the success of the idea of Islamic Banks in the world wide and world can escape from the exploitation of interest, the consequent inflation and economic
backwardness and an indication that these banks continue to grow in number and size worldwide.

### 7.1.2 Efficiency of Islamic Banking at Country Level

The empirical findings suggest that pure technical inefficiency outweighs scale inefficiency in the Islamic banking sector implying that the Islamic banks have been managerially inefficient in exploiting their resources to the fullest extent. The empirical findings seem to suggest that the MENA Islamic banks have exhibited higher technical efficiency compared to their Asian Islamic banks counterparts. During the period of study we find that pure technical inefficiency has greater influence in determining the total technical inefficiency of the MENA and the Asian Islamic banking sectors.

### 7.1.3 Efficiency of Islamic Banking in Jordan

Study on Islamic Banking with respect to Jordan found that IIAB and JIBFI showed, the efficiency and ability of both banks have increased and both banks have expanded its instrumental activities playing an important role in financing important projects. Another interesting finding of the study is that these banks have focused on the short term investment rather than long term investment because of the strength of capital structure depends on short term instrument. Islamic Bank for Finance and Investment (IBFI) has a high profitability that encourages other banks to practice
The study evaluates that the growth of these banks is a proof of the successes of the idea of Islamic banking in the world wide and the world can escape from the exploitation of interest and consequent inflation and economic backwardness and an indication that, these banks continue to grow in number and size worldwide. Islamic banking in Jordan has played an important role in financing and contributing to various sectors in the country such as Industry and Mining, Agriculture, construction, trade, and among other.

### 7.1.4 Efficiency of Islamic banking in Algeria

The major finding shows that the existence of Islamic banking in Algeria can be attributed to the process of financial liberalisation. Financial instruments like Murabaha, Ijara, Muntahia were widely used for short term financing which helped the country for the best reallocation of financial resources. However, the sole Islamic bank operating in the national financial market, Banque Al Baraka d'Algerie, offers a limited number of financial products, and most of them are used in short-term financing. During the study period it is found that the bank is relying less on borrowed funds, which reflects an improvement in its financial performance. The Return on Total Asset Ratio (ROA) increased steadily during the period. This indicates that the bank is effective in investing its funds and utilising its savings. The ratio profit/loss per employee is satisfactory indicated that banks labour is highly productive. The calculated financial ratios point to a continuous increase in the bank’s profitability and efficiency.
It is found that the bank performance has improved. Good investment strategies enabled the bank to boost its earnings. Financial ratio analyses also show an improvement in the bank profitability and efficiency. The bank has introduced various methods to enhance the allocation of its financial resources with the framework of Sharia. The result is an increase in the number of bank branches and services. However, there are many constraints facing the bank. This includes: insufficient level of deposits, limited capital, high level of transparency risk and credit risk, and high concentration of banking activities.

7.1.5 Islamic Micro financing

The comparative analysis and statistical study on secular and Islamic Non Governmental Organizations (NGO’s) found that there are several NGO’s currently operating that provide micro financial service based on Islamic principles started since 1993. At the beginning these NGOs were very small in terms of their membership, saving, borrow and disbursement and rate of recovery etc. But later it could outcompete the secular NGO’s in all these respect. Though these NGO’s are relatively more experience and worked more efficiently than Islamic NGO’s during 1999, it became far below the levels of Islamic NGO’s in 2007 period. This may be due to the merit and feasibility of Islamic financial instruments used in Bangladesh for the smooth functioning of micro financial schemes. The significant difference between INGO’s and secular NGO is that while the later charges 15 per cent-20 per cent interest, the former do not provide any interest but apply the concept of bay-muajjal (sale on credit), musharaka of the total increase in employment opportunities 70 per cent of the
increase is through the performance of Islamic NGO’s in micro financing using the “ijara” and “musharaka” as financial instrument.

Islamic NGO’s have basically copied the micro credit mechanism developed by Gramin bank followed by all NGO’s in Bangladesh. However there might be small variations introduced by each NGO’s to suit its on situations.

In Bangladesh, Islamic micro credit created a virtuous cycle to break the viscous circle of poverty by creating self employment for the borrower, increase income leading to increased consumption, saving and additional credit increases further income and so on and the borrowers are expected to come out of poverty. In most cases there is significant improvement in social indicators such as children school enrolment, fertility rates and the use of clear drinking water.

The net saving and its percentage of increase after implementing Islamic micro financial implement particularly in 2005 is very high when compared it with the respective ratios of disbursement of loans and consequent increase in saving. It shows the effectiveness of implementing Islamic mode of micro financing with “ijara” and “mudaraba”. Among the micro financing institutions the performance of the formal sector and government’s organization are not so extensive and price worthy, the out rich, repayment performance and the saving mobilization of all the existing collateral free- interest free programs of NCB, BKB and PAKB are showing remarkable improvements.
In Bangladesh, Islamic micro financing instruments seems to have a larger role than that of formal sector banks in agriculture where people have more employment opportunities to eradicate poverty signs and its role is growing. As of 2005, out of Taka 60013.45 million, Taka 7476.53 million were disbursed as agricultural loans which represents 12.46% of the total cumulative disbursement of loans (CDF 2005) and all these loans are collateral free- interest free and are maintaining good repayment rates.

Following the success of the Islamic micro financing instrument (IMFI) in the field of micro credit, many banks have introduced a number of riba free (interest free) – collateral free programs replicating the models of micro finance in there poverty alleviation programs. Though their overall performance was not as good as formal MFI, still it has been observed that the micro credit programs of the banking sector that are based on the group lending approach with IFIs have been showing comparatively better results. Most of the micro credit programs of MFI are maintaining very good repayment performance.

In comparative analysis of secular and Islamic NGOs found that NGO’s providing micro financial services based on Islamic principles started since 1993 and at the beginning these NGOs were very small in terms of their membership and saving. But it could outcompete the secular NGOs in this respect. For the sake of comparison NGOs of similar size have been selected. Though these NGOs are relatively more experienced and worked more efficiently during 1999 it became far below the levels of Islamic NGOs in 2007. In the aspect of average increase in disbursement of loan and
recovery Islamic NGOs are better than secular NGOs during the period 1999 and 2007. In 2005 borrowers in INGO increased by 48.84 per cent while it was only 10.49 in Secular NGOs. During the period saving increased from Taka 114.157 million to 20552.1 million in Islamic NGOs while it was increased to Taka 15242.6 million from Taka 640.59 million in Secular NGOs.

Existing bias among NGOs is to include mostly women in their programs. Islamic NGOs includes both men and women. Islamic NGOs have basically copied the micro credit mechanism developed by the Grameen Banks. In disbursement INGO showed 55.66 per cent increase while secular NGOs showed 35.3 per cent and in recovery it was 96.28 per cent in INGO and 91.82 per cent in Secular NGOs.

During 2001-2002 to 2007-2008 periods in Bangladesh there were specialized activities for poverty alleviation and employment generation through Islamic micro credit sector. Case study on selected institutions like BRAC, ASA, SWANIRVAN BANGLADESH, PROSHIKA, TMSS, SHAKTI FOUNDATION, SOCIETY FOR SOCIAL SERVICES, and BUREAU BANGLADESH Etc. brought significant result in the increase of employment, beneficiaries, disbursement and recovery of loans etc. Financial instruments like Qirdhasan and Mudaraba took the major role in this respect achieving 70 per cent growth.

Studies on the three specialized institutions, Grameen Bank, PKSF and BRDB in the performance of micro credit programs using IMFI also shows good result in
bringing more employment opportunities and beneficiaries. Main instruments used are Musharaka and Mudaraba. PKSF used Islamic Micro Financial Instruments (IMFI) and achieved 96.8 per cent increase in the number of beneficiaries while it was 68 per cent and 59.59 per cent in Grameen Bank and BRDB respectively which used Non Islamic Micro Financing Institutions. In the disbursement and recovery of loans under the scheme of Mudaraba and Musharaka the commercial banks Ansar-VDP Development Bank, the SIB Ltd., the NB Ltd., the IB Ltd, and the TB Ltd., the BB Ltd., the PB Ltd. and the UB Ltd. shows amazing results. In the aspect of recovery it was 96.65 per cent increase in Islamic sector while it was 87.76 per cent in secular sector. In disbursement of loans it was Taka 1845.6 million in Islamic Sector while it was 1823.98 in Conventional sector. In the case of beneficiaries it was 1298511 persons in Islamic sector while it was only 351114 in Conventional sector.

7.1.6 Islamic Life Insurance or Family Takaful in Malaysia

It is found that Islamic Life Insurance or Family Takaful is a form of saving instrument leading to investment and creation of more income and employment when it is compared to conventional life insurance program in Malaysia. This attested by the effect that the positive employment increment and its profits and fund are invested in Ijara and Mudaraba instrument. Malaysia’s profit performance and its capacity to generate new business by using the premium fund is directly affected by their macro economic variables as measured by Malaysia’s GDP, Consumer Price Index (CPI), TBR and KLCI. Looking at the pattern of relationships a statistical significance exists between the demand for family Takaful and these economic variables. It is assumed that
when variables have a consistent and systematic linkage between them, relationship is present (In this research correlation and regression analysis were used)

The test found the presence of a relationship between new business and economic variables for both companies (TM and TN) as well as when it is combined the relationship was positive for new business and CPI and GDP but negative for TBR and KLI. This is because of the fact that Takaful business in Malaysia is a luxury good and therefore positively related to economic growth (Redzuan and Yaakob (2004)). Here interest rate and stock returns may have a negative effect on the demand for Takaful as they are seen alternative saving instruments. Study finds that there seems to be a negative correlation between family Takaful and inflation rate. This also is due to the fact that in Malaysia Family Takaful being a luxury good, an increase in the general price level leads to a decrease in the demand for Family Takaful. A test on the strength of the association and the size of the correlation coefficient it seemed to indicate that there is a high correlation in the relationship in question. The coefficient of correlation between (+-)0.90 to (+-)1.00 are considered as very strong, (+-)0.71 to 90 is high, (+-)0.41 to (+-)0.70 is moderate and the rest are small to negligible.

7.1.6.1 Employment Creation

Based on the performance of Takaful industry and its effects on the social economy of the country and on employment creation by both Takaful operators in the country a positive trend seemed to appear. This could indicate acceptance of the service
provided to the public and the need for such services in creating an increase in job markets. Both Takaful Malaysia and Takaful National created a job market comprising of 1.5 per cent of the national employment while conventional insurance could only .005 per cent of the national employment. For the same the contribution of the banking sector is .05 per cent, from real estate it is .028 per cent and from other business service sector is 1 per cent. The reason for the high contributive nature of Takaful industry to employment is their efficiency in creating a fund and invest them properly and to bring good income and employment opportunities.

7.2 Suggestions

Islamic Economic instruments like Interest Free Banking, Equity Finance, Micro Financing, and Takaful etc have good impacts in several countries including non Islamic countries. Several countries including Western Europe, America, England and various Asian countries have implemented the Interest Free Banking and Micro Financing successfully. Our Prime Minister Mr. Manmohan Singh is having very favourable attitude towards it. Due to various hindrances in the creation of the required rules and regulations we could not implement any of the systems of Islamic Economics in India .We should make the people aware of the system and its merits etc.; we could bring an economy free from the exploitation of interest. The teaching, training and research are the where-with-all for the development of any discipline. This is more so for the disciplines like Islamic Banking, Islamic Micro Financing and Islamic Insurance (Takaful) which are still nascent but feasible for mitigating economic exploitation and to bring distributive justice.
7.3 Conclusions

By utilising the Islamic Economic Instruments like Interest Free Banking, Profit Loss Sharing, and Collateral Free – Riba Free Micro Financial Systems effectively as study shows we can maintain distributive justice, eradication of poverty by increasing employment opportunities. The model of income determination in the interest free Islamic economy paves the way for framing a new approach in physical and monetary policies for the stabilization of the economy. However such schemes will be somewhat different in nature and deviate in some cases from the traditional ones. Most of the development problems like the ones in which US and Mexico are entangled presently would not rise in such economy. The fact that many Conventional Bank including some major Multinational Western Banks have also started using Islamic Banking Techniques provides an additional support to the viability of Islamic Banking.