CHALLENGES AND GROWTH PROSPECTS OF ISLAMIC BANKING IN THE KINGDOM OF BAHRAIN

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Abstract- Islamic banking system has emerged as a competitive and a viable substitute for the conventional banking system during the last four decades. However, Islamic banks are also finding it challenging to cope with the evolving global banking environment and making appropriate rules and regulations to cope with these changes while still remaining competitive with their conventional counterparts. Accordingly, this study attempts to evaluate the growth of Islamic Banking in the Kingdom of Bahrain and to examine and focus on the challenges faced by the growth of Islamic Banking. The findings of the study have shown that Islamic banking growth over years in the Kingdom of Bahrain is a result of many factors. One of its main factors is the Government support by having reputed regulations and legislations through the Central Bank of Bahrain and other regulatory bodies. This study is therefore expected to further contribute towards investigating opportunities to strengthen the Islamic banking industry in the Kingdom of Bahrain, which will support its banking sector as one of the main financial centres in the GCC region.

Key Words- Islamic banking and finance, conventional finance, Kingdom of Bahrain, growth of Islamic banking, challenges.

I. INTRODUCTION

Islamic banking system has emerged as a competitive and a viable substitute for the conventional banking system during the last four decades. Islamic banking is a banking activity that is in accordance with the laws of Islam (Islamic jurisprudence) and its practical application is in the development of Islamic economics. The rapid growth of Islamic finance during the last decade has drawn the increasing attention of national policy makers as well as of international institutions (Abdelsalam et al., 2016; Islamic Financial Services Board, 2016).

Furthermore, the Islamic financial system has witnessed considerable developments in the past four decades and is now regarded as one of the fastest growing segments of the global financial system. According to Gheeraert (2014), Islamic finance assets grew at double-digit rates during the past decade, from about US$200 billion in 2003 to an estimated US$1.8 trillion at the end of 2013. The report also state that total Islamic finance assets are projected to reach $3.25 trillion by 2020 and Islamic commercial banking assets are projected to reach $2,610 billion by 2020.

However, Islamic banks are also finding it challenging to cope with the evolving global banking enviro nment and making appropriate rules and regulations to cope with these changes while still remaining competitive with their conventional counterparts. Additionally, the Islamic Banking sector lacks consistency in product structures and investment practices that adversely affects its credibility, reputation, perception and regulation capabilities. Accordingly, this study attempts to:

- evaluate the growth of Islamic Banking in the Kingdom of Bahrain;
- examine and focus on the challenges faced by the growth of Islamic Banking; and
- recommend opportunities in the market which can sustain the growth of Islamic Banks.

The 2008 global financial crisis sparked renewed interest in the field as scholars investigated the geographic distribution of alternative financial systems, including Islamic finance (Wyman, 2009). In order to form a more complete picture of the world city network, researchers have investigated networks of corporations that reside outside the confines of the traditional world city complex, representing what Pollard and Samers (2007) term “postcolonial political economies.” The case of Manama, Kingdom of Bahrain, provides unique insights into the practical requirements of creating and sustaining a global hub of Islamic Banking Finance (IBF), as well as the deeply geographic processes of rise and decline in International Financial Centres (IFCs). A pearling and fishing economy before the discovery of oil in 1932, Bahrain has capitalized on its roots as a trading hub and proximity to larger, wealthier markets to become a center of offshore banking and the “undisputed Mecca” of Islamic finance (Bassens et al., 2011).

After a long period of success over the past five years, Bahrain has also faced an uphill battle to maintain its status. One challenge concerns the increasingly competitive global landscape of IBF as new centers emerge in the oil-producing Arab Gulf, Southeast Asia, and even the West (Abedifar, et al., 2013). But equally significant, fostering domestic political tensions and Bahrain’s geographic position between regional rivals in Saudi Arabia and Iran have raised questions about the Kingdom’s short-term stability and, ultimately, viability as a global hub of IBF. Surprisingly, however, despite the serious economic and political challenges afflicting Bahrain since 2011, Manama has not witnessed a mass exodus of the IBF industry. In fact, although its market share has been reduced by greater competition from nearby capitals such as Dubai and Doha, it still appears on track to retain its dominant position within Islamic finance (Hassan & Lewis, 2014). This observation serves to draw attention to the matter of what it is exactly – if not political stability, economic resources, or modern infrastructure, that gives Bahrain its edge. More broadly, what is it that accounts for why certain hubs of IBF, such as Manama, Bahrain, emerge and under what conditions might they be subject to decline (Zeitun, 2012).

Though handicapped in other respects compared to its neighbors, Bahrain remains home to a majority of the Islamic scholars and organizations that act as "gatekeepers" of the industry by certifying products as religiously compliant (Bassens et al., 2011). To be sure, the entire impetus behind IBF is the concern among Muslims that their money is managed in a way permissible under Islamic law (the shari'a), rather than in a way that guarantees the highest returns. Thus, Bahrain's relative monopoly on those who literally bless financial instruments is a key intangible growth factor of IBF. This study is expected to further contribute towards investigating opportunities to strengthen the Islamic banking industry in the Kingdom of Bahrain, which will support its banking sector as one of the main financial centres in the GCC region.

Islamic finance has achieved considerable growth and considered to be the fastest growing segment of the financial system. The main jurisdictions in the GCC and Malaysia have experienced notable growth. There however remain various challenges such as lack of human capital, Shari'ah standardization and harmonization, public awareness, regulation and supervision, access to finance, liquidity management and others.

The Islamic financial industry has risen out of Muslim discomfort with the practices of conventional finance – interest-based trading, speculation, inequitable transactions, and investment in products that violate the religion – and posits itself as an alternative, morally grounded economic system. Today, the Islamic banking and finance (IBF) industry is increasingly successful in convincing consumers in the Muslim world that its products are the "'appropriate' way of banking, financing projects, and getting insurance" (Bassens et al., 2011). More than merely a reaction to Western practices, the growth of Islamic finance in Muslim countries and regions is also a function of the financialization of the global economy and the culturally specific growth of local banking demand. Together, these forces have led to the emergence of Manama, Bahrain, and other Middle East and Asian cities as centers of IBF, and it is from these non-Western hubs that Islamic financial products are being created and issued for retail markets.

Most recently, sovereign wealth funds, such as those of Gulf Cooperation Council (GCC) member states have changed the map of IFCs. Their presence in places like Dubai, Doha, Manama, and Riyadh – far beyond the hinterlands of traditional financial centers – has stimulated the growth of burgeoning agglomeration economies in these places. This development could present a window of opportunity for challenging the existing order and hegemony of investment capital in global financial centers (Dixon, 2011).

II. RESEARCH METHODOLOGY

The study was based on a quantitative approach where the researchers designed a five-point scale questionnaire to be able to collect primary data. The questionnaire included three parts according to the research objectives mentioned above. Targeted respondents were 30 selected using stratified random sampling from Islamic banks in the Kingdom of Bahrain. The population of the research included general managers, assistant general managers, senior departmental managers, sharia scholars, and financial controllers.

Mean	Interpretation
1 to 1.49	Strongly Disagree
1.5 to 2.49	Disagree
2.5 to 3.49	Neither Agree Nor Disagree
3.5 to 4.49	Agree
4.5 to 5.0	Strongly agree

The researchers collected secondary data on Islamic banking from books, journals, newspaper articles, documents and the Internet. It has been employed by the researchers as background information to formulate the questionnaires sent out to the respondents. The statistical tools that were used by the researchers for the analysis of the questionnaires included the mean, standard deviation, and relative weight. Thus, ranking and the interpretations were also added. The analysis was done on SPSS. Frequency tabulations and cross tabulations were used to bring out the findings of the study. The data is interpreted based on the declared criteria, where the table below shows how the mean scores are interpreted.

III. RESULTS AND DISCUSSION

3.1. Profile of respondents

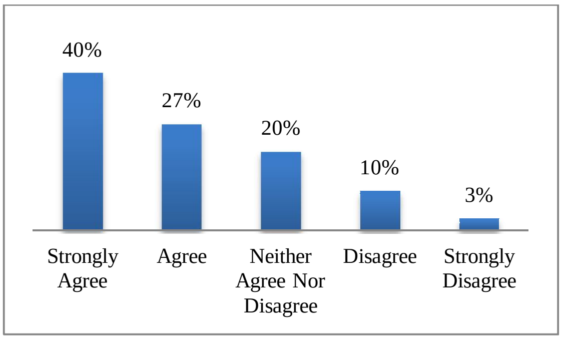
The profile of respondents could be recapitulated as 63% working for Islamic institutions, while 37%

working for conventional banks. They represent 67% males and 33%) females; with average age of 36 years and their educational qualifications are 23% with Diploma and 77% Bachelor degree.

3.2. Growth of Islamic banking

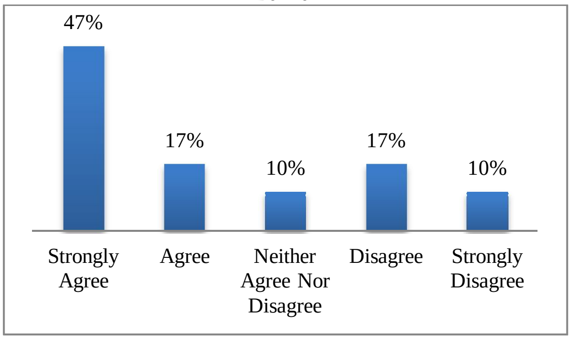
The average total shows that the respondents agreed on the growth of the Islamic banking in the Kingdom of Bahrain where the relative weight is 69.25% and the mean is 3.5. These totals illustrate an agreement on the growth of the Islamic banking.

Figure 1: The growth of Islamic banking in the Kingdom of Bahrain:



The figure above shows that the majority of the respondents strongly agree that Islamic banking in the Kingdom of Bahrain is facing a huge growth. More than 60% of the respondents agreed that the Islamic banking awareness is increasing. The respondents have also mentioned that increased awareness and recognition of Islamic instruments with existence of religious scholars in the sharia'a boards of Islamic banks has no doubt affected this growth.

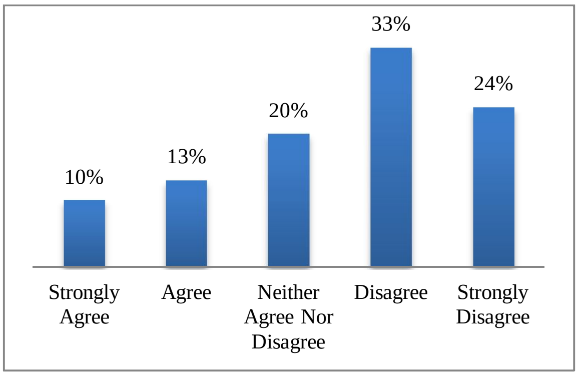
Figure 2: The Islamic banking awareness in the Kingdom of Bahrain



The Islamic banking awareness in the Kingdom of Bahrain showed standard deviation of 1.46, relative weight of 75% and mean of 3.73. As illustrated in figure 2 above, the majority of respondents agreed that there has been an increased awareness of the Islamic banking in the Kingdom of Bahrain over years.

3.3. Challenges facing Islamic banking

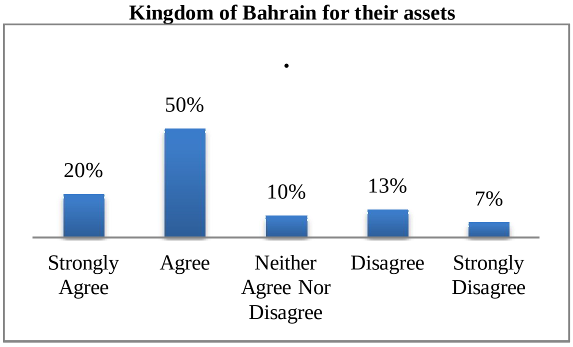
Figure 3: The Efficiency of Islamic banks in the Kingdom of Bahrain with regard to human resources and customer services



As shown in figure 3, 57% of the respondents have considered the human resources issues as an obstacle which limits Islamic banking growth due to the insufficient training of Islamic banks' personnel to understand Islamic banking. Hence, requirement of competent sharia'a human resources such as scholars, internal auditors and good training courses are needed for Islamic banks.

The findings showed that a major challenge facing Islamic banking in Bahrain, which has been identified by more than 80% of the respondents, relates to risk management and corporate governance. Accordingly, it is recommended that necessary actions are required to implement proper risk measures, control and corporate governance by Islamic banks.

Figure 4: Lack secondary markets Islamic banks in the Kingdom of Bahrain for their assets

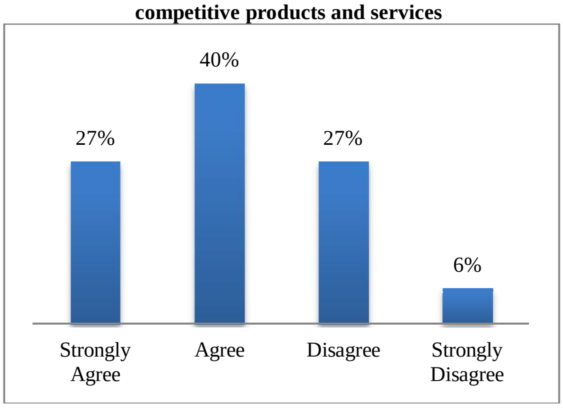


Lack of secondary markets is one of the issues challenging the growth of Islamic banking in the Kingdom of Bahrain. 70% of the respondents agreed that Islamic banks in Bahrain lack secondary markets for their assets. It is therefore important for Islamic banks to develop products to reduce liquidity risks and better employment of assets.

3.4. Advantages of Islamic Banking in the Kingdom of Bahrain

The standard deviation of 1.44, relative weight of 74% and mean of 3.7 shows that Islamic banking is that it plays an important role in the economy of Bahrain.The findings have shown that more than 60% of the respondents have agreed that the economic growth can lead to Islamic banking growth and vice versa.

Figure 5: Islamic banks in the Kingdom of Bahrain offer competitive products and services



The figure above shows that the majority (67%) of the respondents agree that Islamic banks compete with conventional banks to provide better services and products to customers,

Moreover, Islamic banks should still continue innovating products to compete and remain in the market by having their Research & Development departments gather information from the market and develop new products. In addition, these departments will support customer services enhancement and provide necessary data to enhance further customer services.

CONCLUSIONS

Although Islamic banks in the Kingdom of Bahrain have grown substantially, they are still considered small and can't compete with regional and international banks. Internally, they compete with conventional banks to provide better services and products to customers. Further, difficulty of attracting and recruiting quality staff is another challenge. They are also still behind conventional banks and they depend on them to structure secondary markets due to their limited size.

Islamic banking growth over years in the Kingdom of Bahrain is a result of many factors. One of its main factors is the Government support by having reputed regulations and legislations through the Central Bank of Bahrain and other regulatory bodies. This was the gateway, which encouraged international and regional banks to have branches and Islamic windows as well as supporting organizations for Islamic banking; in Bahrain.

The other main factor for this growth is the economic development in Bahrain due to the increased income from oil exports and stability of the country's economy. Meanwhile, recent innovation and products development by Islamic banks; especially restricted investment products that yield higher returns to customers provided them added value, which contributed to this growth.
Besides, increased awareness among the public due to higher demand for religious products, phenomenal success of Islamic banks lately and availability of human resources as well as the increased effect of media and communications (The Internet) are other factors of growth.

In order for Islamic banking in the Kingdom if Bahrain to continue its growth; the following challenges should be addressed:

a.Shortage of human resources: It is believed that Islamic banking is growing faster than training and qualifying human resources in this field which ascertain the shortage of qualified employees for the sector. There are many Sharia'a scholars available who can provide enough support to banks and to train their employees.
b. Risk management and corporate governance: Islamic banks face similar risk management issues as conventional banks, yet they need to develop financial risk management strategies and plans to better compete in the market. Some sharia'a principles such as initially buying the asset and then selling it to the customer need to be addressed properly, as well as the issue of financing defaulters.

It is evident from the above conclusions that some growth factors and challenges of Islamic banking are internal while others are external where Islamic banks should focus on and develop further in order to sustain growth over years.

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