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Attaining Financial Efficiency through Funds Utilization: The Bankers' Perspective

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Abstract
In reply to the argument made by the non-believers of Makkah "Sale is similar to riba", Almighty Allah ordered "Sale is permissible while riba is impermissible[1]". The main intent of the study was to clarify the fallacy prevailing among the Muslims that in practical terms the product of Murabaha[2] which is being offered by the Islamic banks is similar to that of conventional interest based business loan[3]. However, specific objective was to ascertain the degree of financial efficiency on the basis of fund/loan utilization for intended purpose of Murabaha financing vis-à-vis conventional interest based business loan. The study employed survey strategy to collect primary data through structured close ended questionnaires from the sample of 98 Murabaha officers and 178 loan officers out of the whole population of 5 Islamic and 10 conventional banks respectively. Quantitative and qualitative techniques were used to analyze the data and the same is tabulated by use of frequency tables. The study found that the financial efficiency of Murabaha financing is more than that of conventional interest based business loan by 28% as Murabaha funds of Islamic banks are utilized for its intended purpose to the extent of 97% on average, compared to 69% of business loan[4] offered by conventional banks.
Keywords: Financial Efficiency, Murabaha Funds, Loan Amount, Utilization.

1.0 Introduction

Every country tries to allocate her resources in an effective and efficient manner for accomplishment of macroeconomic objectives i.e. economic growth, unemployment reduction and price stability. Academia, research institutes, and governmental and non- governmental bodies undertake in-depth research to help policy makers initiate structural programs, and to achieve these objectives. Despite all these measures taken by the economic masters, the world was seen stunned in October, 2008 when financial meltdown took the worlds' biggest economy to a level where a mild push was required to crumble the entire edifice. According to (Chapra, 2008) financial crises seized the money market and created fear regarding the future of the global economy. In today's economic circles, the financial meltdown of October 2008 is considered to be the second largest recession after the great depression of 1929.

Financial agencies, analysts and economic researchers of different schools of thought including Capitalistic, Socialistic and Islamic Schools have once again started to dig out the causes and effects of this severe recession. According to Jickling, (2010) central banks' primary focus of policy became the prevention of a prolonged downturn on the order of the Great Depression.

Islamic finance considered being a utopian idea almost 40 years back in Pakistan, through the grace of Almighty Allah and the rigorous effort of human capital since 1979, Islamic finance has accelerated its momentum in today's market place and making the news on a daily basis. According to Beck & Kunt (2010), The current global financial crisis has not only shed doubts on the proper functioning of conventional "Western" banking, but has also increased the attention on Islamic banking. According to Ahmed (2010) financial institutions should seek help from the principles of Islamic finance that encourage business and trade activities and help to generate fair and legitimate profit which creates a close link between financial flow and productivity.

1.1 Statements of the Problem

Despite the tremendous growth of the Islamic banks in the last decade worldwide together with being more resilient than to its conventional counterpart, Islamic banks still face some impediments that hinder its escalation to the exponential rate. Among these are the masses that misinterpret the true essence of the Islamic banking and finance either due to lack of knowledge or no knowledge about the Islamic jurisprudence for the same.

[1] Chapter no:2, verse no:275- The Holy Book of Glorious Quran
[2] A kind of sale in which seller discloses the cost as well as profit to the buyer.
[3] Almost the similar argument of Non-believers of Makkah
[4] Business loan includes Running finance, OD facility, working capital finance etc.

According to Beck & Kunt (2010), Islamic banks are similar to the conventional bank with a bit difference in business models. Among all the products of the Islamic banks, murabaha financing is widely used and at the same time highly criticized by the academia as well as practitioners. It is usually whispered in the drawing room gossips that product of murabaha which is used by the contemporary Islamic Banks as an alternative to interest based loan is nothing but a replica to it and has the same utilization as well as the financial efficiency as of the conventional banks' loan amount. Shaikh (2013), while disparaging the murabaha financing post the question that where and how the Islamic bank takes the risk? He further writes that by monetizing its funds using asset backed financing provision, Islamic bank all of a sudden becomes seller of every Halal type of asset without bearing any market or price risk and without managing and keeping any sort of an inventory or warehouse.

Baseless and ignorant criticism about the Islamic banking in general and murabaha financing in particular put on suspicions in the mind of the general public that makes them interested to do banking with interest based conventional banks beside knowing the fact that there is a declaration of war from Allah and His Messenger (S.A.W) against those who do not give up riba.*'O those who believe, fear Allah and give up what still remains of the riba if you are believers. But you do not, then listen to the declaration of war from Allah and His Messenger (S.A.W)" (2,278).* Moreover, these ignorant arguments create problems in the way of development of the intellectual sound and morally pious human capital for the Islamic Banks. According to Solé (2007), Practitioners need to understand the principles of Islamic banking & finance in order to be able to provide the services and products demanded by consumers who want to comply with Islamic principles.

The study therefore seeks to investigate the differences between the murabaha financing offered by the Islamic banks and the product of business loan offered by the conventional banks so that the findings can be used not only by the prospective customers and/or clients before they chose to do banking with either of the two financing alternatives but also helps reverse the mindset of the general public influenced by the literature written against the Islamic banking and finance.

1.2 Murabaha Financing

There are several kinds of sale in accordance with Islamic jurisprudence, some of which are as under:

a) Bai Tolia[1]
b) Bai Wazia'[2]
c) Bai Musawwmah[3]
d) Bai Murabaha

According to Usmani (1998), Murabaha is one of the kinds of sale which has nothing to do with financing in its original sense. However, in order to escape from interest and where the Musharaka and Mudarabah cannot be undertaken, one can use the Bai[4] Murabaha on deferred payment basis (Bai- Muajjal)[5] provided that all the rulings of Sharia' pertains to Murabaha and Bai-Muajjal are fully adhered to. Following is the illustration which helps understand the implementation of Murabaha financing in the Islamic banks.

Suppose Mr. A is a Sugar Mill owner and he needs financing for the sugar cane from the Islamic bank. An Islamic bank may undertake the following steps to fulfill customer's need by using Murabaha Financing.

Step 1:- Islamic Bank and Mr. A signs the Master Murabaha Agreement whereby Mr. A promises to purchase the sugar cane from the bank time to time but within his approved limit.

Step 2:- Contract of Wakala (Agency) is signed between the bank and Mr. A whereby the Bank becomes the principal and Mr. A becomes the agent.

Step 3:- Mr. A purchases the sugar cane from the open market on behalf of the bank i.e. as an agent of the bank.

Step 4:- Mr. A informs the bank that I have taken possession of the sugar cane on behalf of the bank and offers to purchase the sugar cane.

Step5:- The bank accepts the offer made by Mr. A and the contract of Murabaha is concluded between the bank and Mr. A.

Step 1 is not an essential step to be undertaken by the Islamic banks in the eye of Sharia' and the banks are advised not to take promise from the customer if the bank perceives that the customer is honest and trustworthy enough to buy the commodity after the banks' purchase from the open market. Similarly, step 2 is also not important in the eye of Sharia' and the banks are advised not to be indulged in the contract of agency when the commodity is highly marketable and/or standardized in nature.

It is immensely important that the bank takes the risk of the sugar cane from Step 3 to Step 5 in order to make the transaction valid in the eye of Sharia'.It is also very important that the bank should take into account

[1] A kind of sale in which things are sold on cost.
[2] A kind of sale in which things are sold below cost.
[3] A kind of sale in which things are sold without disclosing the cost to the buyer.
[4] Sale
[5] Sale on credit

all the Sharia' rulings of sale from Step 3 to Step 5.

1.3 Conventional interest based Business Loan

According to the "Business Credit America" business loan is defined in the following words.
"A business loan is a loan granted by a financial institution to a nonindividual entity. Business loans can be given to sole proprietors, corporations, limited liability companies, partnerships and nonprofits"

The amount of business loan may be used to initiate new business or to sustain existing business in times of financial difficulty. The utilization of a business loan includes but not limited to the following.

- Purchase of inventory
- Purchase of new equipment
- Construction and renovation
- Covering emergency expenses
- To begin work on new projects

Business loan may be unsecured or guaranteed by some collateral or with some personal assets. It may have a definite maturity period or be available for borrowing and repayment again and again.

1.4 Financial Efficiency

Efficient and effective financial system is the back bone of any country without which it is almost impossible to achieve macroeconomic objectives of price stability, reduction in unemployment and economic growth. According to **Marimuthu (2012)** efficiency is the internal process that leads to output. It focuses on the means to achieve the desired end. The study considers financial efficiency as the degree to which murabaha fund vis a' vis conventional loan is transformed into its intended purpose as **Zala (2010)** in his study stated that financial efficiency refers to the efficiency with which resources are correctly allocated among competing uses.

1.5 Purpose of the study

The purpose of the study is to examine the level of financial efficiency through funds utilization by the Islamic as well as the conventional banks.

1.6 Objectives of the study

The study is guided by the following objectives.

a) To determine usage of the loan amount offered by the conventional banks.
b) To find out utilization of the Murabaha funds by Islamic banks.

1.7 Research questions

a) Is loan proceed of the conventional banks entirely utilize for its intended purpose?
b) Do Islamic banks utilize Murabaha funds for the purpose it was initially requested?

1.8 Significance of the study

Financial efficiency of any banking system whether Conventional or Islamic has far more socio-economic implication than one can think of. Therefore, beneficiaries of this research study includes but not limited to the following.

a) The findings of the study will help State Bank of Pakistan before the issuance of license to both the Conventional and Islamic banks on the basis of financial efficiency.
b) The study helps reduce the misconceptions about the Islamic banking among the public in general and prospective customer/clients of both the Conventional and Islamic banks in particular. It also facilitate general public choose to do banking between the two alternative systems.
c) To help fresh graduates decide which system of banking to work for.
d) Since financial efficiency of any banking system is an important determinant to frame Monetary and Fiscal policies, therefore, this study helps Government and policy makers as to which system of banking is effective to accomplish macroeconomic objectives i.e. economic growth, unemployment reduction and price stability.
e) This study provides more literature for the prospective and existing researchers on the subject of socio-economics differences between Conventional and Islamic banking.

1.9 The Scope of the study

a) Geographical Scope

The study covered the following 10 Conventional and 5 Islamic banks in Karachi, Pakistan.

Conventional Banks	Islamic Banks
Habib Bank Limited (HBL)	Meezan Bank Limited
Muslim Commercial Bank (MCB)	Bank Islami
Allied Bank of Pakistan (ABL)	Bank Al-Baraka
Bank Al-Habib Limited	Dubai Islamic Bank
Soneri Bank	Burj Bank
National Bank of Pakistan	-
Askari Bank	-
United Bank Limited	-
JS Bank	-
Summit Bank	-

b) Subject Scope

- The study is focused on those products of conventional banks in which payment to supplier is not made directly by the bank. i.e. the payment is directly credited to the borrowers' account for instance, Business loan, Working Capital Finance, Running Finance, OD facility.
- The study does not include as to where the amount of loan is used by the borrower other than its intended purpose.

2.0 LITERATURE REVIEW

Tim Lohrentz (2013) while presenting the net economic impact of payday loans declare that the main purpose of these loans is to help people in meeting their expenses arising in case of emergency or some other special occasions. On the contrary, study shows that borrower utilizes payday loans for recurring expenses like in paying utility and credit card bills and not for the purpose these loans were initially acquired. The author further discusses the net economic impact of payday loans by pointing out the economic activity generated by the payday lending firms by receiving interest payments is less than the lost economic activity by reduction in purchasing power of the payday loans customers. This is quantified in the following table that each dollar that pays in interest adds $1.70 to the US economy but subtracts $1.9, an estimated 24 cents is lost to the US economy.

Economic Impact of $1.00 and $40.00 in Payday Interest Paid

Scenario	Total impact from Each Dollar of Interest	Impact from $40 Payday Interest Payment
Amount of Interest Payment	$1.00	$40.00
Scenario1: Payday Lending Industry Economic Impact Multiplier	$1.70	$68.00
Scenario2:Private Household Economic Impact Multiplier	($1.94)	($77.60)
Net Impact from the Two Scenarios	**($0.24)**	**($9.60)**

Source: author, based on IMPLAN, an economic modeling application. See http://implan.com/V4/Index MIG, Inc is the sole-source provider of the IMPLAN.

Pervaiz (2011) somewhat supports the viewpoint given by the Tim Lohrentz by using the terminology "chief motivation" for the profits earned by the conventional bank. He writes that the conventional bank has insufficient checks and balances over the usage of money by the customer that leads to economic crises. **Omara (2007)** in his study on the assessment process and repayment of bank loan in Barclays bank Uganda Ltd finds that 37% of the respondents used the loan proceed other than its intended purpose and 74% of the respondent confirmed that the Barclays bank did not monitor the loan proceed given to us. However, **Griffiths (2013)** disagreed with Tim Lohrentz and Pervaiz by stating that lender before lending the money ask the borrower about the usage of the loan amount. He further writes that if the borrower does not use the money for the purpose it was initially acquired, then the lender has all the rights to repudiate the contract of loan and take the money back.

Hanif (2011) supports Tim Lohrentz, Pervaiz and Omara by doing thorough analysis of the nature of financing of both the Islamic and conventional banks writes that the conventional banks take dictation from the capitalistic economic system in which every factor of production including capital has its fixed return except for entrepreneur. In comparison of both the systems of banking, he finds that the difference between conventional loan and financing under Salam, Bai Muajjal, Istisna and Murabaha is that the former gives cash to the customer where as the later is asset backed which alters the nature of risk and reward of the contracting parties. Moreover, conventional banks while dealing in paper currency builds the blocks of wealth and do not participate in the real sector of the economy.

Samdhani (2013) discusses the similar concept presented by Hanif with a bits difference by emphasizing the risk factor. He writes that the conventional banks provide funds to the client through the contract of loan against interest in which the bank does not bear any risk of loss in the business. On the other hand, Islamic bank purchase commodity from the open market and sell it to client on deferred payment basis. Islamic bank bears the risk of the commodity and hence entitled for the return as it is one of the principles of Sharia' that if a person bears the risk is entitled for the return. It should be noted here that the risk refers to the one which is associated with the commodity and not the default risk.

Zaharuddin (2013) viewed the scenario in terms of the relationship exists between the contracting parties by identifying that the only relationship exist between the conventional bank and the client is the relationship of lender and borrower where as different relationships exist between the Islamic bank and the customer depending upon the nature of the contract both are involved in. He further argued that in conventional banking, priority is given to the ability of customer to pay principal amount together with interest rather than identifying as to where these loan proceeds are going to be utilized by the borrower. He further elaborates that Islamic banks do not generate money through loans rather every financing transaction is backed by the underlying real asset. Islamic banks can give the loan only on humanitarian grounds because Sharia' forbids any kind of benefit to the lender in the transaction of loan. Hence, interest cannot be charged by the Islamic banks "yours is your principal, neither you wrong, not be wronged" [2:279]. On the contrary, conventional banks charge interest considering a price of credit reflecting the opportunity cost of money. Conventional banks works only for its interest and makes no effort to ensure growth with equity.

Dakhlallah & Miniaoui (2011) analyses the whole subject by focusing the objectives of financing under both the Islamic and conventional system. He writes that the conventional banking focuses more on security rather than growth prospects where as being a partner in the project, Islamic banks concerns more about the productivity of a project. He further writes that, in an interest based loan, supply of money cannot be matched with the production of goods and services causing inflationary pressure in the economy which is not the case in Islamic way of financing as each and every financing activity is asset based. **Umer & Kabir (2008)** viewpoint is similar to that of Dakhlallah & Miniaoui by stating that under conventional banking system, greater emphasis is given to the creditworthiness of the customer rather than viability of the projects. They further argued that under conventional banking system, the borrower is under pressure because he has no choice but to repay the principal with interest regardless of the losses arising in project for which funds were borrowed. On the other hand, Islam encourages the people to use their money by becoming the business partner and shares the profit as well as the risk of loss. **Arif (2012)** in his work on the difference between Islamic and conventional banking presented the similar findings as of Miniaoui and Kabir but in different perspective. He inscribed that every financing agreement of the Islamic bank is backed by the asset as money is considered medium of exchange and not the commodity according to the Islamic jurisprudence. Contrarily, conventional bank treats the money as tradable entity, meaning thereby that the loan is given on interest without backing of real asset which results in more volatile and vulnerable market prices.

Ahmed & Hassan (2006) reinforce the finding of Arif by relating the concept of interest with the money's time value. They highlighted that under the capitalist economic system money has a time value due to which if the borrower uses the lender's money s/he charges compensation in the form of interest where as Islam viewed the money different from capitalistic viewpoint. According to the Islamic jurisprudence, money is not a commodity and hence it cannot be used to generate more money except when it is backed by some asset. **Dzuljastr & Hanudin (2013)** concluded that Islamic way of financing is different from conventional way because the former does not treat the money as a commodity where as the latter does. They argued that the debt based financing offered by the conventional banks was the primary reason for the U.S recession 2007 and the product of Musharaka Mutaniqisa offered by the Islamic Banks is the solution to the problems being faced by the customer of Sub-Prime mortgage. They suggest bankers to develop products which do not only offer customer value but also flourish equity financing. **Parashar, S., & Venkatesh, J. (2010)** in their study on how did Islamic Finance do in Global financial crises, finds the conventional banks lend huge amount of loan without the backing of real asset that caused economic instability and was the main reason for the financial crises of 2007.

Simpson (2014) in his work on how conventional bank makes money keeps up the findings that the conventional banks are least interested in knowing as to where the loan amount is going to be utilized. He writes that before the collapse of the housing bubble, home equity financing was the fastest growing arena for the conventional bank in which banks lent to consumers for whatever purpose they wished, with the equity in their home. **Kelly (2012)** while discussing about Georgia Bankruptcy presented his experience in the following words.

"A few weeks ago, a potential client informed me that she had received a lump sum of student loan money for her living expenses for the coming year. Instead of using this money for its intended purpose, she used it to pay

off her credit card debt. Her reasoning was that the student loan interest rate was extremely low and the credit card interest rate was extremely high." (Jeff Kelly, Esq. August 17, 2012, Georgia Bankruptcy)

A.L.M Abdul Ghafoor(2012) finds that both the depositor and the conventional bank do not care about where the money is going to be invested by either party to the contract, whether it is used for productive purposes or not, they don't bother, what are they interested in? is the fixed and /or guaranteed return they have contracted to be received. **According to Tuoitrenews,** The director of the Dak Lak branch of a commercial bank in Veitnam said,

"The coffee manufacturers used the bank loan proceed to purchase VND-billion truck fleet, a VND400-billion warehouse, "The businesses failed to use their loans effectively by investing in non-core sectors that have poor chance of recouping investment,"

Shin-ichi Fukuda (2001) in his work on the impact of bank loans on Economic Development pointed out that the East Asian Crisis might not have occurred had capital inflow was in the form of real goods rather than in the form of bank loan. He further inscribed that it is imperative for the banks to monitor borrowed funds to ensure that funds are used appropriately. **Almossawi (2001)** criticized conventional banking on the ground that it causes to increase money supply in the economy with or without the production of goods & services hence creates inflationary pressure. **Joseph (2012)** recommended that the banks in Zimbabwe should reduced loan funds to the agriculture sector as the borrower utilizes the loan amount for the purpose different from it was initially acquired. **Chapra (2000)**, in his work unveiled that the conventional banks are responsible for the unequal distribution of wealth and should be replaced with Islamic banking products of Musharaka and Mudaraba. **Siddiqui, 2001** in his research work writes that unlike conventional banking, the products of Islamic banking have a great potential to remove inequalities from the society and hence leads to economic prosperity. **Ahmad & Khurshid (2000)** discusses that the one of the main characteristic of an Islamic economy is to have equity based transactions. However, some portion of debt based transaction may also be there in the Islamic economy.

Khoutem & Nedra (2012) discusses the intermediation process in both the system of banking by pointing out that unlike conventional banks, Islamic banks has participative intermediation tools available on the basis of Mudaraba and Musharaka on both the liability and asset side of the balance sheet. The author finds out that due to participatory mode of financing, Islamic bank can take part in the prosperity of society more than that of conventional banks. But, according to him, Islamic bankers feels reluctance to move forward towards mudaraba and musharaka on the asset side due to the exogenous variable such as lack of honesty and integrity, wrong disclosure of profits and expenses, and risk averse behavior of the depositors of Islamic banks.**Saadullah(2007)** in his work trade finance in Islam points out that the murabaha is infact not a financing instrument, it is simply a trust sale in which seller discloses the cost to the buyer together with the profit in the transaction and assumes the risk of the goods as this is one of the principles of Islamic Sharia' that if you take the risk, you are entitled for the return. **Asif & Anjum (2012)** in their research paper concluded that the flaws in the conventional banking is one of the major reasons as to why the world in rushing towards Islamic banking & finance. They found the positive correlation between the flaws in the conventional banking and acceptance of Islamic banking in Peshawar (Pakistan) in particular and worldwide in general.

In the year 2003, State Bank of Pakistan after realizing that the cleaned loan amount is used for Initial Public offerings instructed commercial banks to ask undertaking from the customer that the drawing amount from the loan account will not be used for subscription to an IPO. In the year 2006, SBP of Pakistan via its circular (BPD circular letter No. 14 of 2006) ask commercial banks to ensure that the loan amount will not be utilized for the purpose other than it was initially acquired. Dr.Sudin Haron and Norafifah Ahmad present in their working that through empirical research it is found that not all the Muslims deposit their money only for profit motive as in 1984, Kuwait Finance House did not distribute any profit to their depositors, but there was no evidence of massive withdrawal of deposits. On the contrary, the main motive of the depositor of the conventional bank is good returns

3.0 Research Methodology

3.1 Introduction

The study under consideration is descriptive as well as exploratory in its nature. The response to the study's research questions describes the behavior of the customers about the usage of funds in a given point in time and then presents the data in the form of tables, graphs and charts, hence, the study is descriptive as **Glass & Hopkins (1984)** writes about the descriptive research that it involves gathering data that describe events and then organizes in the tabular and graphical form.

Moreover, the study's general intent together with research questions had never been inquired before thus, the study is exploratory also. According to **Robson (2002)**, exploratory study provides important grounds to determine what is happening to seek new insights about which considerable study was not done before.

3.2 Research Design

The study employed survey strategy as it requires collection of huge amount of data which represents the whole population and also entails durability. **Lynn & Eren (2012)** in his work "A Strategy for Survey Methods Research in the UK" inscribe that there are several ways of collecting data but amongst all, data collected through survey strategy is the best representative of the whole population.

3.3 Survey Population

As the study compares utilization of the loan amount of conventional banks with Murabaha funds of Islamic banks thus, survey population includes loan officers of conventional banks and Murabaha officers of Islamic Banks.

3.4 Sample Size

A sample of 178 loan officers of the 10 conventional banks was taken to inquire the general intent of the study. However, a sample of 98 Murabaha officers of Islamic banks was taken who engage in murabaha financing. The reason to take 98 respondents on board is that according to the State Bank of Pakistan's website there are only five full fledge Islamic scheduled banks operating in Karachi compare to 38 scheduled conventional banks as of December 31st, 2013.

3.5 Instrument for Data Collection

Primary Data

To determine the utilization of loan amount by customers of the conventional banks, primary data was collected from 178 respondents through the technique of structured close ended questionnaires[1] comprises of multiple choice questions.

Similarly, to investigate the usage of murabaha funds of Islamic bank, primary data is collected from 98 Murabaha officers of the Islamic Banks with the help of structured questionnaires[2] that includes multiple choice questions and questions that required ranking to answer.

4.0 Data Analysis and Presentation of Results

Analysis of Murabaha Transactions of the Islamic Banks

To find out whether the Murabaha funds of Islamic banks are utilized for its intended purpose and to attain financial efficiency, it was inevitable to determine the percentage of Murabaha funds directly paid to suppliers vis a' vis to customers of Islamic Banks. For this reason, following questions were asked from the officials of Islamic banks who directly or indirectly indulge in Murabaha financing.

1- Does your bank directly make payment to supplier for Murabaha goods?[3]

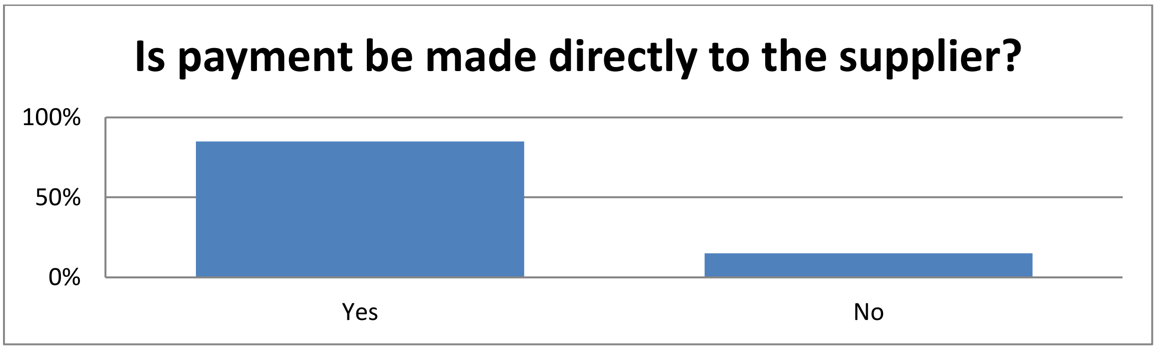
This question was asked due to the fact that Murabaha funds are completely utilized for its intended purpose only in those Murabaha transactions in which the bank makes direct payment to supplier for Murabaha goods hence there is no probability for the customer to utilize murabaha funds other than its intended purpose as funds are not credited to his account. That's why it was worthwhile to determine the exact percentage of Murabaha transactions in which direct payment to supplier was made.

Moreover, this question was significant to determine the percentage of Murabaha transactions in which funds are not directly paid to supplier but credited to the customers' account for which there is every probability that the customer utilized Murabaha funds other than its intended purpose. Table 4.1 unveils the response to the question by Murabaha officers.

Table 4.1

Is payment be made directly to the supplier?	No. of Respondents	Percentage of Respondents
Yes	83	85%
No	15	15%
Total	**98**	**100%**

[1] See Annexure 1
[2] See Annexure 2
[3] Q no:4 in the questionnaire, Annexure 2



The results suggest that 83 out of 98 i.e. 85% of the respondents were at the opinion that the Islamic banks make direct payment to supplier in Murabaha transactions. In other words, 15 out of 98 i.e. almost 15% of the respondents opined that Murabaha funds are credited to the customers' account.

2- Up to what percentage of Murabaha transactions, payment is directly made to the supplier?[1]

This question was asked to those 83 i.e. 85% of the Murabaha officers who responded "Yes" in question no:1 i.e. they were at the opinion that in Murabaha transactions , funds are directly paid to supplier.

The main purpose to ask this question is to determine the exact degree of Murabaha transactions in which payment is made directly to supplier.

Table 4.2

Response of the 83 Murabaha officers regarding the percentage of Murabaha transactions in which Islamic banks make direct payment to supplier.					
Degree of Murabaha transactions in which funds are directly paid to supplier	63%[2]	83%[3]	95%[4]	100%	Total
No. of Murabaha officers	26	20	11	26	**83**

Table 4.2 presents the response showing 26 out of 83 i.e. 31% of the Murabaha officers were at the opinion that Islamic banks make direct payment to supplier in 63% of the Murabaha transactions.

Moreover, 20 out 83 i.e. 24% of the Murabaha officers opined that, payment is directly made to supplier in 83% of the Murabaha transactions.

Similarly, 11 out of 83 i.e. 13% of the murabaha officers responded that the murabaha funds are directly paid to the supplier in 95% of the murabaha transactions and 26 out of 83 i.e. 31 % of the murabaha officers opined that the funds are directly paid to supplier in 100% of the murabaha transactions.

With the help of the Table 4.2, the following table is developed which calculates the weighted average of the Murabaha transactions in which Islamic banks makes direct payment to supplier.

Table 4.3

Weighted Average of the Murabaha Transactions in which payment is made directly to supplier						
% of Murabaha transactions in which payment is made directly to supplier		63%	83%	95%	100**%**	
Number of respondents who opined that Islamic banks make direct payment to supplier in Murabaha transaction to the extent of the percentage mentioned above.	**Qty**	26	20	11	26	83
% of respondents		31%	24%	13%	31%	100%
Weighted Average Percentage of Murabaha Transactions		0.20[5]	0.20[6]	0.13[7]	0.31[8]	84%[9]

[1] Q no: 5 in the questionnaire. See Annexure 2
[2] (51%+75%)/2=63% See Qno:5 in the questionnaire – Annexure 2
[3] (76%+90%)/2=83% See Qno:5 in the questionnaire – Annexure 2
[4] (91%+99%)/2=95% See Qno:5 in the questionnaire – Annexure 2
[5] 0.31*0.63=0.20
[6] 0.24*0.83=0.20
[7] 0.13*0.95=0.13
[8] 0.21*1=0.31
[9] 0.20+0.20+0.13+0.31=0.84=84%

The results suggest that according to the 83 respondents, Islamic banks make direct payment to supplier in 84% of the Murabaha transactions on weighted average basis.

It is noted here that the Murabaha transactions in which Islamic banks make direct payment to supplier have 100% financial efficiency as the Murabaha funds are completely utilized for its intended purpose due to the fact that the prospective customers do not have access to those funds.

Table 4.4 calculates the financial efficiency in response to the opinion of the 83 Murabaha officers.

Table 4.4

S.No	No. of Murabaha Officers	Percentage of Murabaha Officers	Percentage of Murabaha transactions in which the Islamic banks makes direct payment to supplier	Financial Efficiency (%)
1	83[1]	85%	0.84[2]	0.71
2	15[3]	15%	N/A	N/A
Total	**98**	**100%**	N/A	N/A
Financial Efficiency				**71%[4]**

It can be inferred from the Table 4.4 that according to the opinion of 83 respondents the Murabaha funds are credited to the customers' account in the 16% of the Murabaha transactions. Moreover, from the table 4.1 it is inferred that according to the opinion of the 15 Murabaha officers the Islamic banks credit the Murabaha funds into the customers' account in the 100% of the Murabaha Transactions as shown in the Table 4.5

Table 4.5

No. of Respondents	Percentage of Respondents	Percentage of Murabaha transactions in which Islamic banks credit the Murabaha funds into customer's account
83	85%	16%
15	15%	100%

It is note worthy that the Murabaha transactions in which the funds are credited to the prospective customers' account have every probability to be utilized other than its intended purpose by the customer.

Therefore, question no:3 was asked from the 83 Murabaha officers who were at the opinion that the Islamic banks credit the Murabaha funds into the customer's account in 16% of the Murabaha transaction.

Similarly, question no:3 was also asked to those 15 Murabaha officers who opined that the Islamic banks credit the Murabaha funds into the customer's account in 100% of the Murabaha transactions. Table 4.6 presents the response of the Murabaha officers.

3- Do you think that the customer uses murabaha funds for the asset purchase/intended purpose?[5]

Table 4.6

Is the Customer Uses Murabaha Funds for its Intended Purpose?		
Response	**Qty**	**%age of Respondents**
Yes	88	90%
No	10	10%
Total	**98**	**100%**

[1] See Table 4.1
[2] See Table 4.3
[3] See Table 4.1
[4] 0.85*0.84=0.71=71%
[5] Q No: 8 in the questionnaire. See Annexure 2

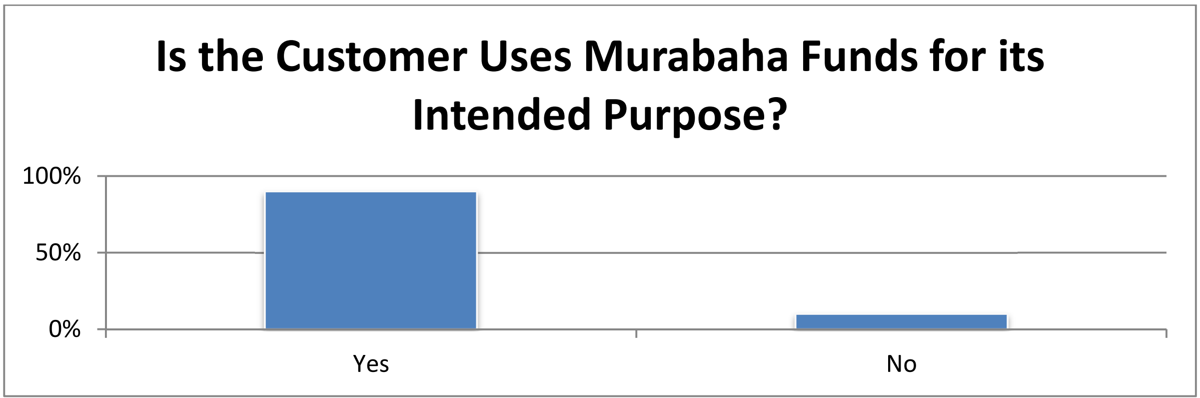


Table 4.6 reveals that 88 out of 98 i.e. 90% of the Murabaha officers responded that the prospective customers use the Murabaha funds for its intended purpose in 90% of the Murabaha transactions. In other words, 10 out of 98 Murabaha officers opined that the prospective customers use the Murabaha funds other than its intended purpose in 10% of the Murabaha transactions.

With the help of table 4.6, the following table is developed which calculates the weighted average of the Murabaha transactions in which the customer uses Murabaha funds for its intended purpose.

It is noted here that it is the response of those 83 and 15 respondents who were at the opinion that the Murabaha funds are credited to the customers' account to extent of 16% and 100% respectively.

Weighted Average of the Murabaha Transactions in which Customers use Murabaha funds for its intended purpose.

Table 4.7

S.No	No. of Respondents	Percentage of Respondents	Percentage of Murabaha transactions in which Islamic banks credit the Murabaha funds into customer's account	Percentage of Respondents who opined that the customer uses Murabaha funds for its intended purpose	Weighted Average of Murabaha Transactions
1	83[1]	85%	16% [2]	90% [3]	12%[4]
2	15 [5]	15%	100% [6]	90% [7]	14%[8]
Total	88	100%	N/A	N/A	**26%**[9]

Table 4.7 shows that weighted average of the Murabaha transactions in which customers use Murabaha funds for its intended purpose is 26%.

In other word, according to the 83 and 15 respondents who were at the opinion that the Murabaha funds are credited to the customers' account to extent of 16% and 100% respectively, the customer uses Murabaha funds for its intended purpose in 26% of the Murabaha transactions on weighted average basis.

Therefore, it can be inferred that according to the aforementioned respondents the financial efficiency of the Murabaha transactions is 26% as the Murabaha funds are utilized for its intended purpose in 26% of the Murabaha transactions.

Finally, with the help of the Table 4.4 and Table 4.7, the following table calculates the total of the financial efficiency of Murabaha transactions

[1] See Table 4.5
[2] See Table 4.5
[3] See Table 4.6
[4] 0.85*0.16*0.90=0.12=12%
[5] See Table 4.5
[6] See Table 4.5
[7] See Table 4.6
[8] 0.15*1*0.90=0.14=14%
[9] 12%+14%=26%

Table 4.8

Total Financial Efficiency of the Murabaha Transactions	
	Financial Efficiency
Table 4.3	71%
Table 4.6	26%
Total	**97%**

Table 4.8 shows that the financial efficiency of the Murabaha transactions is 97% i.e. according to the opinion of the 98 respondents the customers use the funds for its intended purpose in 97% of the Murabaha transactions on weighted average basis.

Analysis of Business Loan Transactions of the Conventional Banks
To find out whether the borrower of business loan amount of the conventional banks utilized the loan for its intended purpose or not, following question was asked from the 178 loan officers the response of which is presented in the Table 4.9

4- In your opinion, how much of the borrowed funds utilized for its intended purpose?
Table 4.9

Weighted Average of Business Loan Amount Utilized for Intended Purpose by Customers of Conventional Banks. (Applicable to 100% of the Business Loan Amount)						
% of loan amount utilizes for intended purpose by customer		25%	50%	75%	100%	
Loan officers' response about utilization of loan amount for its intended purpose by customer	Qty	13	51	82	32	178
% of respondents		7%	29%	46%	18%	100%
Weighted average % of Loan amount utilized for its intended purpose by customers		0.0175[1]	0.145[2]	0.345[3]	0.18[4]	**69%**[5]

The findings suggest that 7% of the loan officers were at the opinion that 25% of the loan amount is utilized for its intended purpose by the borrowers. Moreover, 29% of the loan officers opined that the conventional banks' loan amount is utilized by the borrowers for its intended purpose to the extent of 50%.

The results also suggest that according to 46% and 18% of the loan officers, the customers utilize the loan amount for its intended purpose to the level of 75% and 100% respectively.

Moreover, the Table 4.9 shows that according to the opinion of the 168 loan officers, the weighted average of the loan transactions used for its intended purpose is 69%. In other words, the financial efficiency of the loan transactions is 69%.

Financial Efficiency

Table 4.10

	Murabaha Funds of the Islamic Banks		**Business Loan Amount of the Conventional Banks**	
	Utilized for its intended purpose		Utilized for its intended purpose	
	Yes	**No**	**Yes**	**No**
	97%	3%	69%	31%
Financial Efficiency	**97%**[6]	0%	**69%**[7]	0%

[1] 0.07*0.25=0.0175
[2] 0.29*0.5=0.145
[3] 0.46*0.75=0.345
[4] 0.18*1=0.18
[5] 0.0175+0.145+0.345+0.18=0.69=69%
[6] See Table 4.8
[7] See Table 4.9

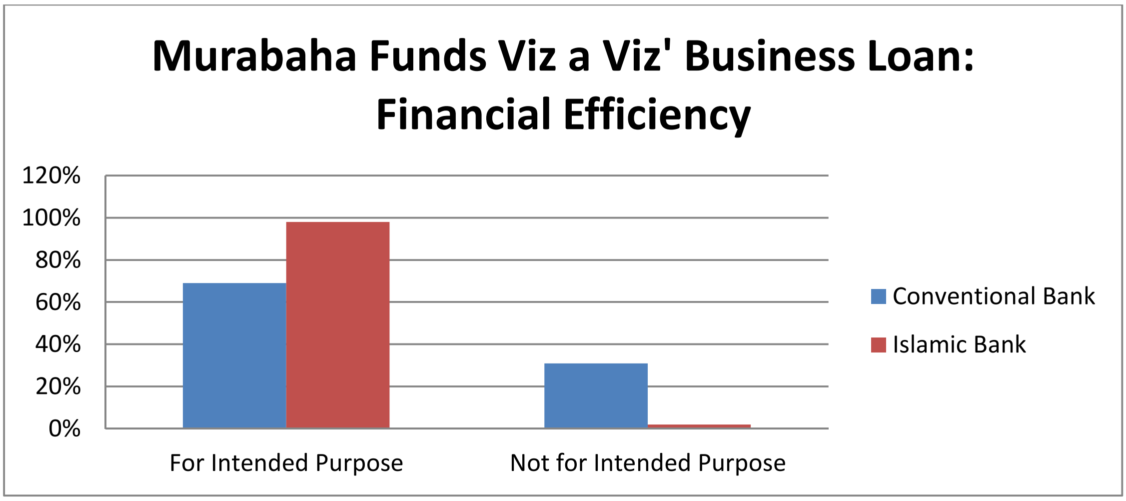


Table 4.10 summarized the finding obtained from the response of 98 Murabaha officers of the Islamic banks and 178 loan officers of the conventional banks which suggests that financial efficiency of Murabaha financing is more than that of conventional interest based business loan by 28% as Murabaha funds of Islamic banks are utilized for its intended purpose to the extent of 97% on weighted average basis, compared to 69% of business loan offered by conventional banks.

5.0 Conclusion and Recommendations

On the basis of research findings it is concluded that the financial efficiency of Murabaha financing is more than that of interest based business loan by 29%. Hence, the researcher recommends the following.

- **Recommendations to the Government of Pakistan**

Since financial efficiency of any banking system is an important determinant to frame Monetary and Fiscal policies and to accomplish macroeconomic objectives i.e. economic growth, unemployment reduction and price stability. Therefore, the Government and policy makers are advised to devote resources towards development of Islamic banking sector in Pakistan.

- **Recommendations to the State Bank of Pakistan**

The decision making authorities of the State Bank of Pakistan pertains to the issuance of licenses to commercial banks are suggested to give an edge to the Islamic banking sector compare to its conventional counterpart.

- **Recommendations to the Muslims**

Muslims are advised to investigate the reality on ground before commenting against Murabaha financing. However, any discrepancies if found may be referred to the Sharia' Advisor of the respective Islamic Bank.

- **Recommendations to the Customers and/or Clients**

Prospective customers and/or clients of the commercial banks are proposed to do banking with the Islamic banks as it is permissible in the eye of Sharia' compare to the interest[1] based conventional bank with is impermissible.

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Annexure 1

QUESTIONNAIRE

Information provided in this questionnaire shall be used solely for research purpose and will not be disclosed to any third party for any reason whatsoever.

1. **Gender**

   Male☐ Female ☐

2. **Age Group**

   20-30 Yrs ☐ 31-40 yrs☐ 41-50 yrs☐
   51-60yrs ☐ 61 and above☐

3. **Educational Background**

   University degree & above ☐ Diploma☐ Certificate☐
   Secondary☐ Other(Specify)☐

4. **Number of years in Credit Department.**

   Less than 2yrs☐ 2-5yrs☐ 5-8yrs☐
   More than 8 yrs☐

5. **Which of the following is the bank more concerned about?**

   Loan repayment capacity of the borrower☐ Security /Collateral☐
   Credit history of the borrower☐ Loan utilization of the borrower☐

6. **Has the bank control over the customer about the utilization of the borrowed funds?**

   Yes☐ NO☐ To certain extent☐ Do not Know☐

7. **In your opinion, how much of the borrowed funds utilized for its intended purpose?**

   100%☐ 75%☐ 50%☐ 25%☐ Others☐

Annexure:2

QUESTIONNAIRE

Information given in this questionnaire shall be used solely for research purpose and will not be disclosed to any third party for any reason whatsoever.

1. **How long have you been working with the Islamic Bank?**

   A- Less than 2 years ☐ B- 2 years to 5 years ☐
   C- 5 years to 10 Years ☐ D- More than 10 Years ☐

2. **How long have you been associated directly or indirectly with Murabaha Financing?**

   A- Less than 2 years ☐ B- 2 years to 5 years ☐
   C- 5 years to 10 Years ☐ D- More than 10 Years ☐

3. **Which of the following factors does your bank consider important while undertaking Murabaha transaction?**

   *Rank 1 to 6 from **most** important to **least** important.*

   A- Loan repayment capacity of the customer ☐
   B- Security/Collateral ☐
   C- Credit History ☐
   D- Utilization/Use of murabaha funds ☐
   E- Customer's Business Cycle ☐
   F- Others*(pls specify)* ☐

4. **Does your bank directly make payment to supplier for the Murabaha goods?**

   A- Yes ☐ B- No ☐

5. **Up to what percentage of Murabaha transactions, payment is directly made to the supplier?**
   A- 51% to 75% ☐ B- 76% to 90% ☐
   C- 91% to 99% ☐ D- 100% ☐

Note:- From QNo:6 onwards, relates to the situation in which bank does not make payment directly to the supplier, rather, Murabaha funds are disbursed in the customer's account.

6. **Do you think that the bank has control on the customer about the utilization of murabaha funds?**
   A- Yes ☐ B- No ☐

7. **What percentage of control does your bank has on the customer about the utilization of murabaha funds?**
   A- 0% to 50% ☐
   B- 51% to 75% ☐
   C- 76% to 90% ☐
   D- 91% to 99% ☐
   E- 100% ☐

8. **Do you think that the customer uses murabaha funds for asset purchase/intended purpose?**
   A. Yes ☐
   B. No ☐

Note: - If your answer to question no: 5 is yes, then, proceed further.

9. **What percentage of Murabaha funds are utilized by the customer for asset purchase?**
   A- 100% ☐
   B- 90% to 99% ☐
   C- 80% to 89% ☐
   D- 0% to 79% ☐

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