

The Role of Islamic Banking in Jordan in Supporting Industries

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Abstract

This paper aims to point out if Islamic banks in Jordan depend on Islamic Investment "Istisna" in supporting industries? At the beginning there are some definitions of the Islamic investment that the Islamic banks should offer to support industries, "Istisna", the research discussed if Islamic banks in Jordan apply this investment tool, at last the results will show that on average, the Islamic Banks in Jordan do not offer "Istisna". So they do not have any effective role in supporting industries in Jordan.

Keywords: Islamic banking, Islamic investments "Istisna", Industries

1. Introduction

The term "Islamic economics" occurs during the second half of the twentieth century as a natural result of the independence of some Islamic countries from colonialism. The contemporary practice of Islamic banking and finance is now 30 years old, the number of Islamic financial institutions worldwide has risen since the establishment of the monetary system and the Islamic banking does not need to wait to achieve the ideal Islamic society morally conscious, because Islamic financial products may not necessarily require a complete Islamic environment, but can be applied successfully even in non-Islamic countries.

2. The research problem and its importance:

Islamic financial products are aimed at investors who want to comply with the Islamic laws(Sharia) that govern a Muslim's daily life. These laws forbid giving or receiving interest(because earning profit from an exchange of money for money is considered immoral);mandate that all financial transactions be based on real economic activity; and prohibit investment in sectors such as tobacco, alcohol, gambling, and armaments. Islamic financial institutions are providing an increasingly broad range of many financial services, such as fund mobilization, asset allocation, payment and exchange settlement services, and risk transformation and mitigation. But these specialized financial intermediaries perform transactions using financial instruments compliant with Sharia principles.(El Qorchi, 2005)

The obstacle of funding is one of the important obstacles to do small and medium projects, the holders of these projects are usually do not have the savings to enable them to establish their projects, as they have no guarantees that can be provided to banks for which the loans.

So this study came to point out one of the Islamic financing techniques "Istisna" as a realistic solution to finance small and medium industries.

3.Research questions:

This study aims to answer the following questions:

1. what is meant by" Istisna" as one of the Islamic modes of finance?
2. Is there a role of" Istisna" in supporting small and medium industries in Jordan ?

4.Hypotheses:

Istisna is applied (as one of the Islamic modes of finance) effectively in the Islamic Banks in Jordan for the period from 2004 to 2012.

5.Literature Review:

An article titled "Do Islamic banks in Jordan depend on Islamic investments" by (Abdo, 2009), This study aims to point out if Islamic banks in Jordan depend on Islamic Investments? At the beginning there are some definitions of the Islamic investments that the Islamic banks should offer, like Mudaraba, Musharaka, Murabaha, Ijara, Istisna and Build operate transfer, the research discussed if Islamic banks in Jordan apply these investments, at last the results will show that an average of more than 58% of the investments of the Islamic banks in Jordan are non-Islamic such as (cash and deposits in other banks, investing in marketable securities, letters of credits, letters of guarantees, commercial papers, and other assets). These investments forms more than the half of the whole investments, and what remains about 42% of the investments, the Islamic Banks in Jordan offer, are Islamic Investments. On the other hand, the majority of the Islamic investments attributed to Murabaha lel Amer beshera'a and ignores all other Islamic investments.

Another article "Risk in Islamic banks: Evidence from empirical research" by (Ariffin, Archer and Karim, 2009) This study attempted to ascertain the perceptions of Islamic Bankers about the nature of risks, risk measurement and risk management techniques in their banks. It covered 28 Islamic banks in 14 countries using a questionnaire survey. It concluded that the Islamic banks are mostly exposed to similar types of risks to those in conventional banks, but there are differences in the level of the risks. The findings of the study showed both theoretical and policy implications for the issue of transparency, with particular references to risk reporting in Islamic banks.

"Islamic Banking: Size Matters." by (Cihak, M. Hesse, H. 2008). This article discussed the connection between size and stability of Islamic financial institutions worldwide. An International Monetary Fund (IMF) study found that large Islamic banks are less stable than small Islamic banks or large conventional banks, suggesting that a thorough look at credit risk management in large Islamic Banks is needed, the features of Islamic financial contracts, such as profit and loss-sharing financing, and fewer risk-hedging methods, give rise to unique risks.

"Islamic Finance Gears Up" by (El Qorchi, 2005), investigated the importance of Islamic Finance, as well as adopting best practices for supervision and accounting, are critical for future market and industry development. For the foreseeable future, supervisory authorities will continue to face the dual challenges of understanding the industry and striking a balance between providing effective supervision and facilitating the industry's legitimate aspirations for further growth and development.

These challenges can be overcome if the concerned central banks and institutions enhance their multilateral cooperation, and create the appropriate environment and conditions. These conditions would create a level playing field and provide the infrastructure needed for the industry's market-driven development. A sound, well-functioning Islamic financial system can pave the way for the regional financial integration of the countries involved. It can also contribute to their economic and social development, by financing the economic infrastructure and creating job opportunities.

"Islamic Bank in United States" by (Taylor, 2003) investigated the banking practices in compliance with the religion of Islam in the US American regulatory framework affecting the establishment and operation of an Islamic Banking Institutions; Rules and practices in Islamic Banks are derived from religious sources, that's why the Islamic Banking truly is in a developmental stage pertaining to the interaction between: 1) Western financial practices which are based on the role of interest and 2) the dictates of shari'ah law which forbid interest (riba) . The prohibition of riba does not mean that money may not be lent under Islamic law; the prohibition simply forbids unearned profit or any form of gain or profit which was unearned in the sense that they resulted from speculative or risky transactions and could not be precisely calculated in advance by the contraction parties. The author concluded that it was a matter of time until an Islamic banking institution, compliant with shari'ah law will be established in the United States, and it will have great potential for success and profitability.

From (Islamic Development Bank, 2001) "Istisna" is a contract whereby a party undertakes to produce a specific thing which is possible to be made according to certain agreed-upon specifications at a determined price and for a fixed date of delivery. This undertaking of production includes any process of manufacturing, construction, assembling or packaging.

In "Istisna", the work is not conditioned to be accomplished by the undertaking party and this work or part of it can be done by others under his control and responsibility." Istisna", an instrument of pre-shipment financing and it is a contract where the deal can be referred to something not in existence at the time of concluding the contract, while Murabaha is an order to buy goods or commodities which are in existence in hand or possible to be found in the market.

The main objective of the "Istisna" mode of financing is to promote manufacturing capability. This may relate to manufacturing of complete assets in the form of capital goods. These goods may benefit the industrial, agricultural or infrastructure sector.

6. Research Methodology:

The Research will use the descriptive analysis of the data collected and calculated from the annual reports of the two Islamic Banks working in Jordan, the Jordan Islamic Bank for Finance and Investment (JIB) and the Islamic International Arab Bank (IAB).

For the period from 2004 to 2009, since those years are the most recent times of Islamic banks activities and it could be enough periods to test the study hypothesis.

7. Results and discussions:

In order to compare between the results, the research summarized the data. Table no.1 contains the data as it is from the annual reports of Jordan Islamic Bank for Finance and Investment; Table no. 2 contains data of the Islamic International Arab Bank.

By examining tables above, the study concludes that in the Islamic banks working in Jordan Istesna'a percentage are very low, less than 1% for each.

8. Conclusion

Theoretically, Islamic banks should offer "Istisna" to support industries. This research finds that the Islamic Banks in Jordan do not offer "Istisna" services at all. So they do not have any effective role in supporting industries in Jordan. As a result this study recommend Islamic banks in Jordan to increase depending on the Islamic form "Istisna", because this kind of Islamic investment tools plays an important role in supporting small and medium industries, and to find an effective ways to deal with other banks all over the world

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Table (1) Jordan Islamic Bank for Finance and Investment (in J.D)

Year	Istisna
2004	0
2005	0
2006	0
2007	0
2008	0
2009-2011	0

Table (2) Islamic International Arab Bank (in J.D)

Year	Istisna
2004	1361747
2005	2953912
2006	3196225
2007	4999636
2008	7041469
2009	5561435
2010	6726972
2011	7184531

Table (3) the ratio of Istisna per the total of investments for the Jordan Islamic Bank for Investment

Year	Istisna
2004	0%
2005	0%
2006	0%
2007	0%
2008	0%
2009-2011	0%

Table (4) the ratio of Istisna per the total of investments for the Islamic International Arab Bank

Year	Istisna
2004	1%
2005	1%
2006	1%
2007	1%
2008	0%
2009-2011	0%

Table (5) averages of both banks data as a sector of Islamic Banks in Jordan

Bank	Istisna
Average	
Jordan Islamic Bank	0%
Islamic International Arab Bank	1%

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