

# FINANCIAL PERSPECTIVES OF ISLAMIC BANK'S IN OMAN

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## Abstract

This paper discusses about the inauguration of banking system in Oman. It studies the financial position of Islamic banks working in the Sultanate. This paper is studying the profitability of Islamic Banks in Oman. This study was a pilot test for the questionnaire in which 50 respondents filled the questionnaire. It was concluded that the respondents had high awareness of Islamic banking products in Oman. Secondly, Majority of the people are Muslim, therefore they like to use Islamic Banking. Thirdly, majority of the Muslims are high at their religiosity, therefore they also like to use the Islamic Banking. But with all these results of study one cannot understand why the Islamic banks are not able to have high profits. These findings suggest also suggest that Islamic Banking is rapidly increasing its assets in Oman.

**Keywords:** Islamic Banking Regulatory Framework (IBRF), Islamic Banks, Financial Performance

**JEL Classification:** C39, E58, G21,

## 1. Introduction

The economic development depends of one of the sectors which is banking sector. In Oman we have developed banking system which consists of conventional banks and Islamic Banks The most common banks in Oman is Bank Muscat, Bank Dhofar, Bank NBO Etc., it includes certain foreign banks as HSBC, Standard Chartered bank.

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On the other side we have Islamic banks which is divided into full-fledged Islamic banks as well as windows of commercial banks.

The History of Banking sector is back from the year 1974 in which banking law established the Central Bank of Oman (CBO), with started its working in April 1975. In the year 2016 the conventional banks were 16 in number. Out of these 7 banks were locally registered and 9 banks were foreign banks which were operating in Oman.

By the end of 2016 two full Islamic banks were incorporated. There were 70 branches of Islamic windows of commercial banks at the end of 2016 which had 72 ATMS and 17 cash deposit machines. There were 6 finance and leasing companies which were registered and licensed by CBO. There were 3 specialized development banks which are related to housing and agriculture and fisheries, namely: The Oman Development Bank; The Oman Housing Bank; and the Oman Bank for Agriculture and Fisheries(Annual Report, CBO 2016).

## **2. Organization system of Islamic banking**

Oman has the great potential in Islamic Banking. In recent decades, the Islamic Banking and Finance has grown up with the implementation of Islamic Banking Regulatory Framework. These industry nascent players are two independent Islamic Banks (IIB) and five Islamic Banking windows. The shariah compliant format announced by the Royal Decree which inspired the banking systems to be more competitive to its banks.

There is great written on both hosts with lots of assets generally optimistic analysis of the development of the car industry in terms of market share along with prospects in the Gulf Cooperation Council countries, capacity and commitment to Islamic banking. Oman, status dwindling oil resources is classified as an oil-rich economy, which has relied heavily on 2012. Almost 80 per cent of their income in this way, the economy of our regional partners and external Oman stood in front of the position associated with commodity prices. However, the government has been all kinds of measures to diversify into higher public and non-oil economy by means higher investment supported by private consumption (tourism and mining mainly) structures. There were two full-fledged Islamic banks i.e. Bank Nizwa and Al Izz Bank in Oman. The conventional banks have opened Islamic windows which are as follows:

- Meetaq is the window for Islamic bank,
- Muzn is the Islamic window of National Bank of Oman
- Sohar is the Islamic window of Sohar Bank
- Maisarah is the Islamic window of Bank Dhofar
- Al Hilal is the Islamic window of Ahli Bank

A lot has been speculated about hunger and perhaps Islamic banking and markets based on regional market growth stories in different countries. These estimates are broadly, cognitive reveries, heuristics and optimism without extensive general and driven development based on stories from the past - the local banking industry, regulatory parameters and the reference balance sheet structure dynamics. A quote, Moody's reports for Islamic banking in Oman are confident in the ability to get a ballpark projection of six to eight percent of the system's assets within the next three to five years. The amount of this decision by Moody's, Islamic banking assets, 10% YOY growth of total banking assets in the period of 5 years, assuming 8% penetration of Islamic banking, should reach around OMR 3 Bn mark. I find with a conservative stance by Ernst & Young, and in a matter of a few years see surmounting USD 6.00 Bn (OMR 2.3 Bn). Dubai-based Arqaam Capital Research Organization predicts that, by 2017, declaring that IBI (2017. OMR 745 Mn to largely dominate around Meethaq per cent of all loans by Islamic assets 15 with the IBW will be created, with all turns out much hope that Bank Muscat) 40% share. But the bank may not come as a surprise. Muscat with total banking assets equally dominant part is to claim (38%). As of December 2014, retail deposits in the form of private sector credit mobilization or more can be seen on core banking activities. With nevertheless, get-set-go stage is set for human resources in all kinds of products, branches working, infrastructure and space, emphasized. The analysis is performed in the next section following table, equity, deposits and financing breakup and physical outreach initiative as a micro view of the branches of the data presented in the financial statements, bank-wise core activities.

Islamic banks were introduced in the year 2011. Among all the GCC countries Oman is the last country to start Islamic Banking. Islamic banking system works on the principles of interest free banking which is considered haram according to the Islamic laws.

**Table 1**  
**Combined Balance Sheet of Islamic Banks/Windows (Rial Omani Million)**

Indicators	Balance Sheet ending for the Year					Change from 2013 to 2016 (%)
	Dec-2013	Dec-2014	Dec-2015	Dec-2016	Dec-2016-Dec-2013	
<b>Cash on hand and deposits with CBO</b>	72.8	131.5	149.4	237.2	164.40	225.82
<b>Due from Head Office, affiliates and other banks abroad</b>	77.7	56.1	24	48.6	(29.10)	(37.45)
<b>Total financing</b>	434.3	1049.5	1781.3	2425.9	1991.60	458.58
<b>Total investments</b>	104.2	44.9	145.3	159.9	55.70	53.45
<b>Net fixed assets</b>	32.8	34.2	35	34	1.20	3.66
<b>Other assets</b>	5.7	54.8	118.7	174	168.30	2952.63
<b>Total assets /liabilities</b>	815.2	1371	2253.8	3079.6	2264.40	277.77
<b>Total deposits</b>	171.9	688.9	1539.4	2169.8	1997.90	1162.25
<b>Due to Head Office, affiliates and other banks abroad</b>	23.2	157.6	154.1	259.8	236.60	1019.83
<b>Core capital and reserves</b>	328.1	350.6	391.3	433	104.90	31.97
<b>Other liabilities</b>	204.6	173.9	169	217	12.40	6.06

Source: Compiled by authors from Central Bank of Oman Annual reports 2013 to 2016

By the end of 2016 the financing provided by Islamic banks amounted to 2425.9 million Omani Rial which is 458.8% rise from the year 2013. The total deposit during the same period was 2169.8 million which increased from 171.9 million in the year 2013.

**Table 2****Profit and loss figures of Islamic Banks**

loss for the period	2011-2012	2012-2013	2013-2014	2014-2015	2015-2016
Alizz Islamic Bank SAOG	-168,432	-3,232,132	-5,499,477	-5,356,384	-4,724,906
BANK NIZWA SAOG	-4,811,927	-12,304,780	-7,708,761	-5,260,242	109,722

*Source: Compiled by authors from Annual Reports of Alizz Islamic Bank & Bank Nizwa 2013 to 2016*

It can be seen that the Islamic banking came into existence in 2011. It was under a gestation period in the both the banks were facing huge losses. Alizz bank was having a loss of nearly OMR 1684320 in the year 2011-2012 which is increasing throughout the years and in the year 2015-16 we can see it raised to OMR 4724906 whereas Bank Nizwa started with losses but was able to get profits in the year 2015-2016 which amounted to 109722 OMR

**3. Literature review**

According to De la Harpe (2017) Morocco is the country which started Islamic banking. The central bank approved 5 banks to start sharia compliant services under Islamic banking. In Morocco they are not using the terminology Islamic banking but instead they are using 'participatory' banking.

Riyas et al. (2015) have studied Islamic banking by SWOT analysis, and they concluded that Islamic banking is contributing positively in the economic development of countries.

Mohammed et al. (2017) discussed about the factors which influence the customers' preferences for the Islamic banking. In this study they extracted 4 factors which explained 79.14% of variance. These factors were better returns, clear and transparent, profit sharing ratios, Sharia complied business, technological considerations.

Naureen and Sahiwal (2013) studied 200 customers from different banks of Pakistan and they tried to find out the relationship between customer's satisfaction, demographics and customers loyalty. They concluded that on customer's loyalty there was a positive impact of demographical characteristics and customer satisfaction.

Sain et al. (2016) explained the necessity of Islamic Finance as an alternative financial system. They study different aspects of Islamic finance with the various advantages of the same for the different

economies. It also talks about current issues of Islamic Finance in Australia.

Ali & Zhou (2013) approach with interest the service quality of the banks which included Islamic banks as well as conventional banks. They conclude that the assurance dimension was relatively highest in case of Islamic banks, whereas perception about technology use was less in case of Islamic banks. They concluded that the service quality related to internet and online banking services should be improved. On the other hand, elaborate training should be given to conventional bankers.

Muhammad (2013) analyzed the development of Islamic Banking in Pakistan, taking into account the six full-fledged Islamic banks which are operating, and 12 conventional banks are operating with Islamic window in Pakistan. He concluded that the most important aspect in developing the Islamic banking system is transparency of Shariah compliance products.

#### **4. Research Problem**

The Islamic banking is getting a good momentum as it is being preferred by not only Muslims but also the non-Muslims. Around the world the Muslim community is scattered therefore the choice of Islamic banking is increasing all over the world. In Oman Islamic banking entities provided financing amounting to RO 2.42 billion at the end of December 2016, a rise of 36.2 percent over the previous year's outstanding of RO 1.78 billion.

##### **4.1. Objectives of study**

1. To study the financial position of Islamic banks in Oman.
2. To study the profitability position of Islamic banks in Oman.
3. To identify the customer awareness about Islamic Banking.
4. To determine the customer preference toward Islamic Banking as compare to traditional banking.
5. To explore the challenges for Islamic Banking in Oman
6. To provide the recommendations for Islamic Banking in Oman

## **4.2. Hypothesis**

H1: There is positive effect of customer awareness about Islamic Banking on customer intention to use Islamic Banking.

H2: Muslims prefer to use Islamic Banking as compare to conventional Banking.

H3: Religiosity of the Customers has positive effect on the customer intention to use Islamic Banking.

## **4.3. Research Methodology**

This study will adopt the quantitative Research Methodology. The data will be collected from the customers of Islamic Banking in Oman. Current study will determine the customer behavior; therefore, it will use quantitative research methodology. For this purpose, a survey will be conducted, and that data will be numerical form. Therefore, quantitative methodology will be employed.

## **5. Data Analysis and Results**

This paper will highlight that how the Muslim prefers the Islamic Banking as compare to traditional banking. On the basis of these, we evaluated the customer's perception and their preferences toward Islamic Banking. One an important factor can be religiosity which may have effect on the customer's perceptions and their intentions toward the Islamic Banking. This study adopted the quantitative Research Methodology. The data is collected from the customers of Islamic Banking in Oman. We used a survey method and collected data from 50 customers of Islamic Banks.

### **5.1. Questionnaire analysis**

The demographics of the respondents were analyzed by the frequency of the respondents. There are total 50 customers among of them the male members are only 35 (70) that is the majority of the sample. In age of the respondents, majority of the respondents were related to the more than 29 years. In qualification, the 20% respondents are undergraduates, 40% are the graduate and similarly, the 40% have done their Masters. In experience of Islamic banking, the majority of the respondents have less than 1-year experience.

**Table 3**

**Demographics of the respondent**

		<b>Respondents</b>	<b>Percentage of responses</b>
<b>Gender</b>	Male	35	70%
	Females	15	30%
<b>Age</b>	18 to 28 years	15	30%
	29 to 40 years	15	30%
	41 to 55 years	20	40%
<b>Qualification</b>	Under-Graduation	10	20%
	Graduation	20	40%
	Masters	20	40%
<b>Experience of Islamic Banking Using</b>	Less than 1 year	35	70%
	More than 2 years	15	30%

*Source: Data compiled by author (based on questionnaire)*

**Table 4**

**Descriptive of Questionnaire**

	<b>Questions Awareness about Islamic Banking</b>	<b>Not aware of it</b>	<b>Aware but do not use it</b>	<b>Aware and use it</b>
1	Are aware about current account in Islamic Banking?	10	12	28
2	Are aware about Time deposit A/C in Islamic Banking?	5	7	38
3	Are aware about Mudarabah in Islamic Banking?	4	10	36
4	Are aware about Musharakahin Islamic Banking?	14	14	22
5	Are aware about Ijara financing in Islamic Banking?	8	8	34
6	Are aware about Traveler's cheques in Islamic Banking?	4	10	36
7	Are aware about Overdraft in Islamic Banking?	14	14	22



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8	Are aware about Letter of credit in Islamic Banking?	12	14		14
9	Are aware about Murabaha financing in Islamic Banking?	6	12		32
<b>Questions Satisfaction</b>					
		<b>Strongly Satisfied</b>	<b>Satisfied</b>	<b>Neutral</b>	<b>Dissatisfied</b>
10	Are you satisfied regarding Management proficiency in Islamic Banking in Oman?	32	6	3	9
11	Are you satisfied regarding Bank's personal knowledge in Islamic Banking in Oman?	33	7	5	5
12	Are you satisfied regarding Cost of services in Islamic Banking in Oman?	25	12	3	10
13	Are you satisfied regarding Efficiency of transactions in Islamic Banking in Oman?	34	7	5	4
14	Are you satisfied regarding Facilities of parking in Islamic Banking in Oman?	28	15	3	4
15	Are you satisfied regarding Advertising campaign in Islamic Banking in Oman?	33	7	5	5
16	Are you satisfied regarding Working hours in Islamic Banking in Oman?	24	6	3	17
17	Are you satisfied regarding Financial counseling in Islamic Banking in Oman?	32	12	3	3
<b>Religiosity</b>					
		<b>Not at All</b>	<b>Not</b>	<b>Yes</b>	<b>Very Much</b>
18	How much you are religious in your routine life?	13	2	4	31

19	I prefer my religious obligation in my routine life.	12	4	3	21
20	Due to Islamization, I love to use Islamic Banking.	13	12	3	22
21	As compare to traditional banking, I always prefer to use Islamic Banking	25	6	7	12

*Source: Data compiled by author (based on questionnaire)*

Descriptive of the questionnaire showed that all the respondents answered the all questions included in the questionnaire. The majority of the respondents are aware about the products of Islamic Banking in Oman. All the respondents are Muslim in this dataset. Majority of the respondents are high at their religiosity due to living in a pure Islamic Society.

### 5.2. Reliability Analysis

In the above questionnaire, we measured the concepts of customers awareness, religiosity and intention to use Islamic Banking by using the 21 question items. To check the internal consistency and reliability of the data, we calculated the Cronbach Alpha value of all three variables. The Cronbach Alpha value of all the variables were found more than 0.70 (See the Table 5).

**Table 5**

#### Reliability Analysis

Variable	Cronbach Alpha
Customer Awareness	0.78
Religiosity	0.83
Intention to Use Islamic Banking	0.85

*Data compiled by author (based on questionnaire)*

### 5.3. Hypotheses Testing by Regression Analysis

To test the following hypotheses, we performed multiple regression analysis by using SPSS 21 version. We tested the following hypotheses:

H1: There is positive effect of customer awareness about Islamic Banking on customer intention to use Islamic Banking.

H2: Muslims prefer to use Islamic Banking as compare to Traditional Banking.

H3: Religiosity of the Customers have positive effect on the customer intention to use Islamic Banking.

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.560 <sup>a</sup>	.31	.010	4.39977

a. Predictors: (Constant), Customer Awareness, Islam, and Religiosity

**ANOVA<sup>a</sup>**

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	104.896	3	34.965	3.806	.03 <sup>b</sup>
Residual	4568.491	236	19.358		
Total	4673.387	239			

a. Dependent Variable: Intention to use Islamic Banking

b. Predictors: (Constant), marketopenness\_1, marketdynamics\_1, Commerical\_Infra\_1

**Coefficients<sup>a</sup>**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	6.287	1.302		4.830	.000
Customer Awareness	.516	.20	.32	3.614	.003
Islam	.922	.431	.28	2.138	.034
Religiosity	.95	.343	.20	2.299	.02

a. Dependent Variable: Intention to use Islamic Banking

In our hypothesis 1, we proposed that “There is positive effect of customer awareness about Islamic Banking on customer intention to use Islamic Banking” that is accepted by our results (estimate= 0.32, p<0.05).

In our hypothesis 2, we proposed that “Muslims prefer to use Islamic Banking as compare to Traditional Banking.” that is accepted by our results (estimate= 0.28, p<0.05).

In our hypothesis 3, we proposed that “Religiosity of the Customers have positive effect on the customer intention to use Islamic Banking.” that is accepted by our results (estimate= 0.20, p<0.05).

**Summary of Hypotheses**

<b>Serial #</b>	<b>Hypothesis</b>	<b>Status</b>
H1	There is positive effect of customer awareness about Islamic Banking on customer intention to use Islamic Banking.	Accepted
H2	Muslims prefer to use Islamic Banking as compare to Traditional Banking.	Accepted
H3	H3: Religiosity of the Customers have positive effect on the customer intention to use Islamic Banking.	Accepted

Results of our study explained that due to high awareness of Islamic banking products in Oman, the people have higher tendency toward Islamic Banking. Secondly, Majority of the people are Muslim, therefore they like to use Islamic Banking. Thirdly, majority of the Muslims are high at their religiosity, therefore they also like to use the Islamic Banking. These findings suggest, Islamic Banking is promoting very rapidly in Oman.

**6. Conclusions and recommendations**

This study adopted the quantitative Research Methodology. The data is collected from the customers of Islamic Banking in Oman as well as financial data from the annual reports of the respective Islamic banks and websites of Central bank of Oman.

Results of our study explained that due to high awareness of Islamic banking products in Oman, the people have higher tendency toward Islamic Banking. Secondly, Majority of the people are Muslim, therefore they like to use Islamic Banking. Thirdly, majority of the Muslims are high at their religiosity, therefore they also like to use the Islamic Banking. These findings suggest, Islamic Banking is promoting very rapidly in Oman. However, the financial results of both the Islamic banks working from 2011 is not good. Some more measures should be adopted to increase the financial conditions of the Islamic banks.

In recent years Islamic banking has been nourished enormously and gained enough popularity around the globe. It aims at growing rapidly in coming years as well. Despite of its enormously growing rate it is facing some challenges as well. These challenges must need to be addressed by Islamic banks if they want to sustain

and grow in years to come where competition is very dynamic. Regulatory framework is necessary to address the upcoming issues and challenges in Islamic banking sector. All the obstacles such as in terms of the capital adequacy, supervisory issues and market discipline and corporate governance should be tackled with expertise so that it aids to the expansion of the system. In recent global economic crises, conventional banking faced huge threats and issues, but Islamic banking maintained its growth due to its unique principles and solid foundation on the basis of Shariah.

Global banking crises had a least effect on Islamic banking as compared to conventional banking sector. However, there are some future challenges and threats that must need to be addressed properly. For instance, lack of standard practices can lead to serious issues in coming future. Similarly, market and disciplinary issues also need in time handling. On other hand corporate governance problems may arise to hurdles. In order to address and resolve such type of issues here we have some recommendations for the challenges that are being faced by Islamic banks. It could assist and aid management authorities of Islamic financial institutions to design the policies by taking them into consideration. These are as follows:

- 1) Uniformity and standardization of Sharia'ah rules in a crucial aspect. For this Islamic bank may have one standard to follow strictly across the board. It will assist the banks to enhance their credibility and goodwill.
- 2) It is important for financial banks, especially Islamic banks that they must consider the safety and strength of their system. This can be done with the capital adequacy measures. Secondly, they must need to have a cushion against losses of capital.
- 3) Elimination of moral hazard issues which may arise due to the attempt of raising the return rates must be addressed positively. It will build the confidence of customers in Islamic banking sector.
- 4) The management of the liquidity issues is also important. So authorities must establish a sound system where these issues can be managed appropriately.
- 5) Timely and effective information must be circulated to IAH so that standards of effective corporate governance can be fulfilled. It will also generate the support for effective market transparency and discipline.

- 6) Developing needs and latest trends are necessary to compete with conventional banking. For the future growth and development, it is equally important to focus on the infrastructure needs of the banks. Reasonable investment should be made in this area, it should be also observed that experts in the field of Islamic banking must be generated and skills must be passed to new learners to strengthen the Islamic banking regulations and laws.
- 7) The need of Ijtihad has been increasingly felt to nourish Islamic economy and Islamic financial institutions. All issues and problems must be addressed in the light of Quran and Sunnah and this should be the benchmark in Islamic banking sector as well. This will aid Muslims and non-Muslims as well to understand the Islamic teachings in day to day life matters.
- 8) Challenges which are faced by government and authorities must be addressed significantly. For instance, legal infrastructure and framework is necessary to strengthen Islamic financial institution.
- 9) The refinement of the Islamic commercial law will also be helpful to Islamic banking sector. Islamic commercial law is in its initial stages, so it is not mature enough yet to face the challenges. So, in the light of Quran and Sunnah it can be groomed effectively.
- 10) Supervisors and regulators in Islamic banking must be given enough power so that they regulate and supervise effectively. In order to make them perform their duties more effectively, they can be trained as per Islamic laws and regulations under the light of Shari'ah.

This study was based on the general Islamic banking system operating in Oman, we can study on the financial analysis of all the Islamic banks as well as Islamic windows working in Oman with the customer's perspective with a model based on regression analysis.

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