

The Performance of Islamic Banking : A Maqasid Approach

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ABSTRACT

It has been taken for granted that Islamic banking (IB) is only about avoiding riba. The failure to address the objectives of IB has left some scholars with no choice but to adopt the conventional yardsticks to measure the performance of Islamic banks. Whether these are the right criteria to measure the performance of Islamic banks is subject to empirical test. But apparently, evidences in most studies using conventional yardsticks to measure the results of Islamic banks show Islamic banks trailing behind conventional banks. Hence, there is a mismatch between the objectives of IB and its outcome. The mismatch could be attributed partly to the fact that the objectives of IB have not been questioned, and partly due to the performance yardsticks used, which apparently do not conform to the ideal objectives of IB. This paper therefore aims to identify the ideal objectives of IB from the theory of Maqasid al-Shari'ah and, proposes a model of IB performance measures based on these objectives. Operationalization method of Sekaran (2000) will be used to quantify the Maqasid into measurable IB performance indicators.

Introduction

Why has IB come into existence? The obvious answer, apparently, would be that banking as a financial institution has become so vital to almost all modern economies that governments, firms and individuals cannot afford to do without it. Governments use banks - especially the central banks, among others, to regulate and supervise the health of their economies. Firms and individuals rely on banks for savings, investments and the purchase of goods and services. Modern banks through financial intermediaries are central to the activities of the product and factor markets. The rapid changes in government regulations, technologies and financial innovations due to globalization have resulted in more banking facilities. Such facilities include the provision of banking services through electronic channels, namely Automated Teller Machines (ATMs), PC banking, phone banking, banking kiosks, credit cards, debit cards and prepaid cards to mention but a few. These changes have revolutionized the way people raise and use their money.

The first experiment of the modern IB is the Mit Ghamr bank in Egypt, established in 1963. The bank lasted for only 4 years until 1967 (Ready, 1981) as cited by Ariff (1988). Compared to the conventional banking, which has been around for over 900 years, modern IB is only 32 years old since the establishment of the first bank, the Dubai Islamic Bank in 1975. However, the expansion and performance of IB within this period has been remarkable in spite of operating in a competitive environment along side its conventional counter-part. A few statistics may be necessary here to substantiate the claim.

Up to May 1997, twenty two years after the inception of the first Islamic bank, there were already about 150 Islamic banks and financial institutions managing investments estimated at about USD 75.5 billion in Asia, Africa, Europe and the U.S., covering more than 27 countries (Kamel, 1997). Just less than ten years later, i.e., as of May 2006, there were more than 250 Islamic financial institutions in about 100 countries globally, the majority being in Asia. The IB industry is growing at 15% annually, much higher than the conventional banking growth rate¹. Total assets now managed by Islamic financial institutions are close to USD300 billion, while Islamic equity funds and off-balance-sheet investment accounts are conservatively estimated between USD15 billion and USD30 billion. Taken together, that's roughly the equivalent of Russia's gross domestic product.²

Therefore, apparently IB seems to be expanding rapidly. However, the real question still stands. What are the objectives of IB? Unfortunately, no serious effort has been made to address this question. It has never been discussed formally. What can be seen in many literatures are scanty and disjointed discussions about the objectives of IB. It has been taken for granted that IB is only about avoiding riba (Siddiqi, 2000). Even the concept of riba itself has been confined only to interest.

¹ Beng, P.K. (2004, August 20). The Global March of Islamic Banking. *Asia Times*. Downloaded on 30th May 2006 from: http://www.atimes.com/atimes/Global_Economy/FH20Dj02.html

² Time Europe Magazine 16 Dec 2002).

Since no serious effort has been made by scholars to theoretically study these objectives, most Islamic banks shy away from specifying clearly the objectives of their establishment. The failure to address the objectives of Islamic banks has left some scholars with no choice but to adopt the conventional yardsticks to measure the performance of Islamic banks. Whether these are the right criteria to measure the performance of Islamic banks is subject to empirical test. But apparently, evidences in most studies using conventional yardsticks to measure the results of Islamic banks show Islamic banks trailing behind conventional banks.

Naqvi (2000) citing (IRTI, 1998) related to a survey of expert opinion on 30 major Islamic banks reveals dismal performance of Islamic banks. Based on the results of the study, it was found that the rate of returns offered by Islamic banks had been generally lower than that of the interest-based banks. The study also concluded that cases of loan default had risen dramatically among Islamic banks, which appeared less able to deal with such cases effectively than the interest-based banks. Mokhtar, et al. (2006) in their comparative study of full-fledged Islamic banks, Islamic windows and conventional banks in Malaysia for the period 1997-2003 conclude that full fledged Islamic banks were less efficient than the conventional banks. Abdus Samad (1999) conducted a study comparing between the efficiency of Islamic Bank (BIMB) and conventional banks in Malaysia. His result using ANOVA test showed that conventional banks had higher managerial efficiency than Islamic Bank of Malaysia. A study by Abd el Rahman, et al. (2003) to investigate the X-efficiency of Islamic banks in Sudan reveals that these banks suffered from technical inefficiency.

1.1. Problem of the Research

Absence of a careful study on the objectives of IB has resulted into misinformation and misgivings about the primary reasons for the existence of Islamic banks. As a result, most Islamic banks shy away from specifying the objectives of their establishment. Inadvertently, many of the Stakeholders cannot clearly see the difference between the Islamic and conventional banking. Further more, by using the same conventional yardstick to measure Islamic banking there is a mismatch between these conventional performance indicators and the objectives of IB. Whether these are the right criteria to measure the performance of Islamic banking is subject to empirical test. Given all these shortcomings, no careful study – to the best knowledge of the author – has been conducted to review the objectives of IB.

1.2. Objectives of the Research

- a. To identify the ideal objectives of IB from the theory of Maqasid al-Shari'ah
- b. To propose an idea of developing a model of IB performance measures based on the objectives identified in (a) above.

The introductory section begins with the background of the study. It then provides a problem statement after a thorough review of literature, and the research objectives. Section two deals with the literature review, which also includes discussion on the theory

of Maqasid al-Shari'ah and identifies what could be the ideal broad objectives of Islamic banking. The third section proposes an idea of developing a model of IB performance measures based on the broad objectives identified in section three. The final section concludes the study and makes suggestions for future research.

2. Literature Review

Objectives are specific commitment consistent with the mission of the organization over a specified time period. They may be quantified, and may be inappropriate in some circumstances (Lynch, 1997, p.425). Objectives are measurable, defined, operational, simple steps, and specific. They contribute to the fulfillment of specified goals, complete with a beginning and an end³.

Most of the discussions by modern Muslim scholars on the objectives of Islamic banking, however, have not dwelled in depth into the theoretical framework underlying the objectives of Islamic economics, banking and finance. For example, Kamel (1997) opines that unless the impact of the implementation of IB is reflected in economic development, creation of value added factor, increased exports, less imports, job creation, rehabilitation of the incapacitated and training of capable elements, the gap between the Islamic and conventional banks would be narrower. It is also eluded that IB would strive for a just, fair and balanced society; it is community oriented and entrepreneur friendly emphasizing productivity and expansion in real economy; and it will promote brotherhood and cooperation (Dusuki, 2005) citing (Chapra, 1985, 1992; Ahmad 2000; Chapra 2000a, 2000b; Siddiqui 2001; and Naqvi 2003). Chapra (1985) has outlined the following distinctive features of Islamic banks, among others: abolition of interest, adherence to public interest, catalyst for development, promotion of economic well-being, establishment of social and economic justice, and equitable distribution of income.

2.1 The Theory of Maqasid al-Shari'ah

As mentioned earlier, the IB objectives have not been formally reviewed. Hence, the author will try to derive the objectives of IB from the theory of the objectives of al-Shari'ah (Maqasid al-Shari'ah), which Muslim scholars have developed as far as the third century after Hirah, 9th Century A.D. (al-Raysuni, 1992).

Almost all the scholars of maqasid are unanimous about the general objectives of al-Shari'ah, which are to promote virtues and avoid vices (Ibn 'Ashur, 1998, p.190). However, some of them differ in their classification of the specific objectives inspite of some similarities. For example, Ibn 'Ashur mentions that the specific objectives of the Shari'ah should include the preservation of order, promotion of human welfare, prevention of corruption, establishment of justice and, maintaining stability and harmony (al-Risuni, 1992). Meanwhile 'Ilal al-Fasi includes in his classification objectives such as reforming the human mind, developing the earth, managing benefits for all, preserving order and system of livelihood, establishing justice and, utilizing natural resources (Ibid). A more refined form of the specific objectives of al-Shari'ah is provided by Abu Zaharah

³ Available at: <http://www.msu.edu/course/aec/806/snapshot.afs/syllabus/notes7.htm>

(1997). His classification summarizes to some extent all the other classifications into three broad areas, namely:

- Educating the individual (Tahdhib al-Fard)
- Establishing justice (Iqamah al-`Adl)
- Promoting Welfare (al-Maslahah)

This study shall adopt Ibn 'Ashur's definition of the general objectives of al-Shari'ah and Abu Zaharah's classification of specific objectives. Accordingly, the study will make use of Sekaran's method (2000, pp.176-195) to operationally define these three broad objectives of Islamic banking into measurable items. This is done by looking at the behavioral dimensions denoted by the concept. These are then translated into observable and measurable elements so as to form an index of measurement of the concept. Various components of the dimensions and elements of the objectives are organized in the form of tables, which are presented towards the end of the paper.

3. Developing Islamic banking Performance Measures from Al-Maqasid

This section will explain step by step the process of operationalizing the 3 identified broad objectives of Islamic banking into behavioral dimensions and measurable elements in the following phases:

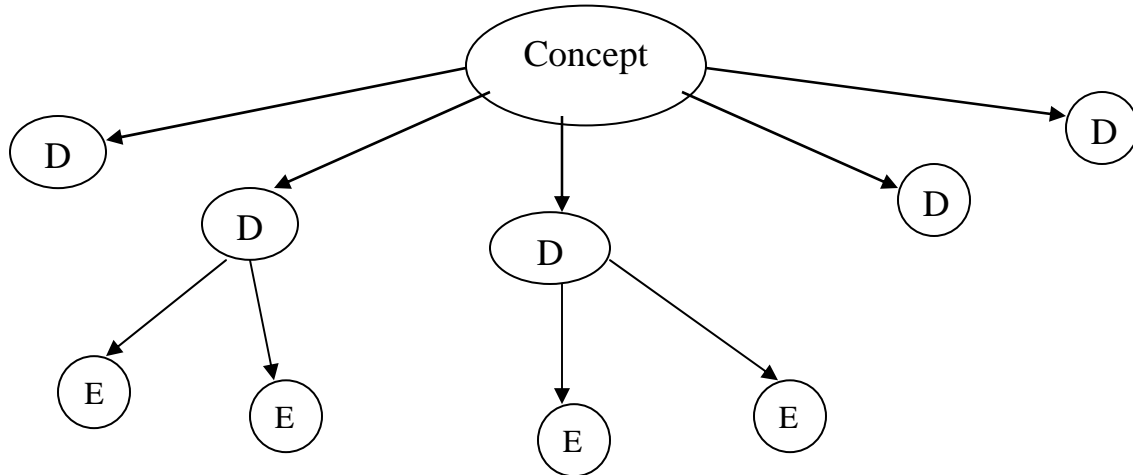
Phase 1: Overview of Sekaran's (2000) concepts of Operationalization Method

Phase 2: Identifying the relevant dimensions and elements associated with the ideal objectives of Islamic banking. The aim here is to come up with performance measures. This is achieved by going through Shari'ah sources (Qur'an and Sunnah) and other secondary sources of information.

3.1 Overview of Sekaran's concepts of Operationalization Method

As stated earlier, this section will try to translate the objectives of Islamic banking into dimensions and measurable elements. This will be done using the operationalization method provided by Uma Sekaran (2000), with some modification though. Sekaran's method breaks down abstract notions or concepts (C) into observable characteristic behaviors, which she termed as dimensions (D). The dimensions are then further broken down into measurable behaviors that she referred to as elements (E). She cited the example of thirst as a concept. The behavior of thirsty people is to drink a lot of fluid (Dimension). The degree of thirst can be measured by the number of glasses drunk by each thirsty individual (Element).

Sekaran's model can be illustrated as follows:



Where D denotes Dimensions and E, Elements

Section two has identified 3 broad ideal objectives of IB, namely educating individuals, establishing justice and public interest. Each of these concepts (c) would thereafter be broken down into broad characteristics or dimensions (D) and finally into measurable behaviors or elements (E) as follows:

Table 1
Operationalizing the Objectives of Islamic Banking (Phase 2)

Concepts	Dimensions	Elements	Performance Indicators	Source of Data
Educating Individual	D1	E1	PI1	Annual Report/Interview
		E2	PI2	Annual Report/Interview
	D2	E3	PI3	Annual Report/Interview
	D3	E4	PI4	Annual Report/Interview
Establishing Justice	D4	E5	PI5	Annual Report/Interview
	D5	E6	PI6	Annual Report/Interview
	D6	E7	PI7	Annual Report/Interview
Public Interest	D7	E8	PI8	Annual Report/Interview
	D8	E9	PI9	Annual Report/Interview
	D9	E10	PI10	Annual Report/Interview

3.2 Phase 2: Identifying the Dimensions and Elements of IB Ideal Objectives

This section will discuss the process of identifying the relevant dimensions and elements associated with the ideal objectives of Islamic banking. The aim here is to come up with IB performance measures. This will be achieved by going through Shari'ah sources (Qur'an and Sunnah) and other secondary sources of information, which include academic journals, books and working papers.

3.2.1. Phase 2(a): Identifying the Dimensions of IB Ideal Objectives

The dimensions will be identified from the following ideal IB objectives:

Educating Individual

In the new economy of the millennium, knowledge has emerged as an asset to be valued, developed and managed (Bogdanowicz et al., 2002). This paradigm shift comes at a time when Islam had made the pursuit of knowledge obligatory over 1400 years ago⁴. One of the avenues to acquire knowledge is through education, which also includes training and disciplining the self.

In the Islamic scripture and literature there are a lot of inspiration not only towards the advancement of knowledge and skill training but also towards providing information to the public and the market. The Qur'an relates the story of how man is given superiority over the angels and other creations due to his knowledge⁵. The most knowledgeable individual is ranked higher than the one who has less knowledge⁶. This is because the former can give an expert opinion in their respective fields and the Qur'an confirms that none can inform you better than the experts themselves⁷. Therefore, the implication is that every individual must continue to advance his frontier of knowledge to achieve the highest rank of becoming an expert at a given time. Moreover, Islam considers knowledge as a lost treasure of the believer⁸. He has to strive for its pursuit even if he has to go to China⁹.

Besides advancing knowledge in one's field, Islam also encourages the acquisition of skills. The Shari'ah has all the praise for a skillful¹⁰ and efficient¹¹ worker.

⁴“Pursuit of knowledge is an obligation to a Muslim man and Muslim woman”, a hadith narrated by al-Tabrani (Hasan'), available at: www.offok.com

⁵ Al-Baqarah, 2: 31-34

⁶ Al-Mujadilah, 58:11

⁷ Fatir, 35:14

⁸ “Wisdom is the lost treasure of a believer and wherever he finds it he is more deserving to acquire it”, hadith narrated by Abu Hurayrah (Dha'if), available at: www.offok.com

⁹ “Seek knowledge even though unto China”, hadith narrated by Anas Ibn Malik (Dha'if), available at: www.offok.com

¹⁰ “Allah loves a believer who is skillful”, hadith narrated by Tirmithi and al-Bayhaqi in al-Shu'ab, and by al-Tabrani in al-Kabir (Hasan), available at: www.offok.com.

¹¹ “Allah loves one who if he does work he does it efficiently”, hadith by Al-Tabrani (Hasan), available at: www.offok.com

On the other hand, beneficial knowledge should be disseminated to others. The Shari'ah provides several incentives to those who contribute directly or indirectly to the advancement of knowledge¹². Muslims during the medieval era used to donate libraries and books as endowments (waqf), and scholars would forego their intellectual property rights as waqf (Kahf, 1999). Al-Maghribi (2004, pp.435-442) in his book, 'Strategic Management in Islamic Banking (Arabic)', concludes that the social responsibility of Islamic banks includes education. Islamic banks should provide scholarships, research grants, finance Da'wa activities, Quranic memorization programs, educational conferences and workshops, and publications, among others. Al-Omar and Iqbal (2000) suggested in their study that Islamic banks need to do more in the areas of teaching, training and research development.

Apart from the specialized form of knowledge discussed above, there is the general knowledge especially one which is related to providing full information to the market. Islam abhors, rather condemns it if the market is left in a state of ignorance (Jahalah) about its products and business activities (al-Zuhayli, 1985). It is the responsibility of the seller to fully disclose all the relevant information related to activities of the business entity. This is to safeguard the interest of all the stakeholders to the business. Ali (1994) says that Islamic society expects Muslim firms to record and report, besides profitability, liquidity, solvency and efficiency, matters such as the firm's contribution towards socio-economic development, the extent to which it abides by Islamic Ethics, etc.

It then follows from the discussion above that Islamic banking is dutiful not only to educate and train its workers but also to contribute towards the advancement of knowledge and to keep the public well informed about its objectives and activities.

Accordingly, the following three dimensions can be derived, among others:

1. Dimension 1: Advancement of knowledge or encouragement of knowledge
2. Dimension 2: Instilling new skills and improvements
3. Dimension 3: Creating awareness of Islamic banking (educating the public)

Establishing Justice

Justice is a comprehensive term in Islam and covers all spheres of human life. The focus here would be on economic justice, though it is also inter-related with social and political justice. The Qur'an has laid down several premises for economic justice. For example, people are not allowed to devour their wealth unjustly except through mutual consent¹³. All forms of elements that would create economic injustices such as bribery (al-Rashwa)¹⁴, fraud or deception (al-Ghish)¹⁵, gambling (al-Maysir)¹⁶, dubious contracts

¹² "The best among you are those who learn Quran and teaches it to others", available at: www.offok.com. Although the hadith mentions about disseminating the knowledge of Qur'an, it can also imply all branches of knowledge related to alShar'ah.

¹³ Al-Nisaa, 4:29

¹⁴ "The Prophet s.a.w cursed the briber, the bribed and the intermediary between the two", hadith narrated by al-Tirmithi, in "Commentry by Ibn 'Arabi".

¹⁵ "The Prophet s.a.w said, whoever deceives is not among us" hadith narrated by Ibn Majah.

(al-Gharar)¹⁷ and riba¹⁸ are condemned in the highest term. Interest is considered as a major destabilizing factor that contributes to cyclical fluctuations in the economy (Minsky, 1982) as cited by Akkas (1996). Interest has numerous moral ills (Afzal-ur-Rahman, 1975). It transfers resources from the poor to the rich and breeds envy.

Conversely, the Shari'ah encourages all forms of activities that would ensure economic justice such as wealth circulation (al-Tadawul or al-Riwaj)¹⁹ that should not only be confined to the rich, fair share of returns (al-Shirkah)²⁰ among the contracting parties and fair pricing (Tas'ir)²¹ while avoiding profiteering²² that burdens the public. Hassan (2003) observes that the Islamic banking system must seek to realize economic justice through wealth circulation, elimination of absolute poverty and efficiency in the utilization of resources available. Iqbal (2001) sees the profit and loss sharing arrangements on the pattern of equity contracts as closest to the Islamic ethos than the predetermined fixed interest debt which is unjust and a taboo. Islamic banking must seek to realize economic justice that would result in permanent contribution to economic efficiency, productivity, growth and stability (Hassan, 2003). To ensure social justice as enjoined in the Qur'an, Islamic banks must strike effective balance between profitability and social justice (Pramanik, 2006)

In the light of the discussion above, the following dimensions are identified, among others:

Dimension 4: Fair returns to the bank and its customers

Dimension 5: Offer products and services that are less financially burdensome to bank customers

Dimension 6: Elimination of negative elements that breed economic injustices such as interest

Public Interest

Al-Shatibi (d.790H/1390A.D) considers public interest as the overriding objectives of al-Shari'ah. In case of a conflict between the private and societal goals, the latter prevails (Al-'Ubaidi 1992, pp.139-147). The Shari'ah encourages the individuals to align their interest to the public interest. Wealth from individuals, firms and governments are trust from Allah and must therefore be directed towards achieving the common social goals²³. Redistributing wealth is not a favor by the rich to the poor but the right of the latter. "In

¹⁶ Al-Maidah, 5:90

¹⁷ "The Prophet s.a.w has made dubious contracts unlawful" hadith narrated by Muslim.

¹⁸ Al-Baqarah, 2:275

¹⁹ Al-Hash, 59:7

²⁰ Sad, 38:24

²¹ "A man came to the Prophet s.a.w and said, 'fix price for us (because it was high due to shortage of supply as a result of famine). The Prophet s.a.w replied, 'Allah is the One who fixes price, He is the Possessor, the Giver and the Sustainer. I want to meet Allah while none of you have claimants upon me injustices for to (one's) blood or wealth.'" hadith narrated by Abu Hurayrah.

²²

²³ Al-An'am, 6: 165

their (rich's) wealth, there is a due right for the poor and the deprived"²⁴. According to Zubair (1986) all excessive wealth held beyond one's legitimate needs should be held as a trust (Amanah) and surrendered to the members of the society. The Shari'ah has provided several measures for spending this wealth on the society. These include Zakah²⁵, endowment (Waqf)²⁶, voluntary charity (Sadaqat)²⁷, inheritance (Faraid)²⁸, Will (Wasiyyah)²⁹, donations and grants ('Itiyyah), and social security (al-Takaful al-Ijtima'i)³⁰.

Besides these measures, al-Shaybani (1986) recommends that investments be carried out in real sectors that have large spheres of public goods. This implies that such investments can be carried out by individuals, firms and governments. In Islamic banks, deposits are public money and thus must be directed towards the public interest (Khaleefa, 1993, p.38). According to Khaleefa, Islamic banks in Sudan are required by law to contribute to community development projects.

Needless to say, in the Islamic economic system, the state plays a much bigger and wider role towards public interest. Such roles include provision of basic needs, arrange social security and foster equitable distribution of income and wealth, fulfillment of social obligations (Fardh Kifayah) and provision of public services and amenities (Iqbal and Khan, 2004). However, Islamic banking can also contribute through the government towards realizing this social goal. It can be in the form of direct corporate tax³¹ and Zakah. It can also be in the form of purchase of sukuk bonds and financing development projects to allow the government to save some of its budget for other programs (Iqbal and Khan, 2004). In this regard, the Islamic Development Bank (IDB) has played a very big role in financing government projects and community projects in member countries. The IDB projects include mobilize waqf funds and spend them on the needy, finance research and training programs, finance government projects, finance trade, assist in enhancing trade among Muslim countries, invest in vital real sectors of the economy and poverty alleviation (IDB Report, June 2005).

The discussion above leads us to identify the following dimensions, among others:

Dimension 7: Transfer measures that would redistribute income and wealth to the poor and less privileged section of the society

Dimension 8: Financing government budget to increase development projects and provision of public goods

Dimension 9: Investment in real sectors that have large spheres of public welfare

The nine dimensions that have been identified above are shown in table 2 below.

²⁴ Al-Ma'arij, 70:24-25.

²⁵ Al-Tawbah, 9:60

²⁶ Ali 'Imran, 3:92; Al-Baqarah, 2:267

²⁷ Al-Baqarah, 2:3

²⁸ Al-Baqarah, 2:180

²⁹ Al-Nisaa, 4: 11-12

³⁰ Al-Tawbah, 9:103

³¹ Ibid. Also a hadith narrated by al-Tirmithi, "In wealth there are rights other than Zakah".

Table 2
Operationalizing the Objectives of Islamic Banking (Phase 2 (a))

Concepts	Dimensions	Elements	Performance Indicators	Sources of Data
1. Educating Individual	D1. Advancement Of Knowledge	E1	PI1	Annual Report/Interview
		E2	PI2	Annual Report/Interview
	D2. Instilling new skills and improvements	E3	PI3	Annual Report/Interview
	D3. Creating Awareness of Islamic banking	E4	PI4	Annual Report/Interview
2. Establishing Justice	D4. Fair returns	E5	PI5	Annual Report/Interview
	D5. Cheap product and services	E6	PI6	Annual Report/Interview
	D6. Elimination of injustices	E7	PI7	Annual Report/Interview
3. Public Interest	D7. Redistribution of income & wealth	E8	PI8	Annual Report/Interview
	D8. Financing gov. budget	E9	PI9	Annual Report/Interview
	D9. Investment in vital real sector	E10	PI10	Annual Report/Interview

3.2.2. Phase 2(b): Identifying the Elements of IB Ideal Objectives

After reducing the abstract level of the three concepts into nine dimensions, each of these nine dimensions will now be broken further into its elements, thus delineating the actual patterns of behavior that would be exhibited. These should somehow be quantitatively measurable. The elements have been identified based on the discussion in phases 2 and 2 (a) above.

Elements of Dimension 1

Advancement of knowledge or encouragement of knowledge can be measured through (1) scholarship and (2) research

Elements of Dimension 2

Instilling new skills and improvements can be measured through (1) training

Elements of Dimension 3

Creating awareness of Islamic banking (educating the public) can be achieved through (1) Publicity

Elements of Dimension 4

Fair returns to the bank and its customers can be realized through (1) fair profit and loss sharing (PLS) ratio

Elements of Dimension 5

Offering products and services that are less financially burdensome to bank customers can be measured by (1) fair pricing

Elements of Dimension 6

Elimination of negative elements that breed economic injustices such as interest can be achieved by (1) offering interest free product and services

Elements of Dimension 7

Transfer measures that would redistribute income and wealth to the poor and less privileged section of the society can be measured by (1) transfers to personal income

Elements of Dimension 8

Financing government budget to increase development projects and provision of public goods can be done through (1) government revenue

Elements of Dimension 9

Investment in real sectors that have large spheres of public welfare can be measured (1) identifying the major real sectors

Ten elements have been identified from the 9 dimensions above. These 10 elements are shown in Table 3 below:

Table 3
Operationalizing the Objectives of Islamic Banking (Phase 2 (b))

Concepts	Dimensions	Elements	Performance Indicators	Sources of Data
1. Educatin	D1.Advancement Of Knowledge	E1.Scholarship	PI1	Annual Report/Interview
		E2.Research	PI2	Annual Report/Interview
	D2. Instilling new skills and improvements	E3.training	PI3	Annual Report/Interview

g Individual 1	D3. Creating Awareness of Islamic banking	E4.Publicity	PI4	Annual Report/Interview
2. Establishing Justice	D4. Fair returns	E5. Fair PLS Ratio	PI5	Annual Report/Interview
	D5.Cheap product and services	E6. Fair pricing	PI6	Annual Report/Interview
	D6. Elimination of injustices	E7. Interest free product	PI7	Annual Report/Interview
3. Public Interest	D7. Redistribution of income & wealth	E8. Personal Income	PI8	Annual Report/Interview
	D8. Financing gov. budget	E9. Government revenue	PI9	Annual Report/Interview
	D9. Investment in vital real sector	E10. Interest free product	PI10	Annual Report/Interview

3.2.3. Phase 2(c): Specification of performance Indicators (PI)

From the 10 elements identified in Phase 2 (b) above, 11 performance indicators are specified to be used in this study. These indicators were chosen based on the following criteria:

- Discussion on the objectives of Islamic banking and on the dimensions and elements identified from these objectives.
- Past similar research using the same indicators for measuring performance of Islamic and conventional banks (Mahmood al-Osaymy et al., 2004, Shahul Hameed et al., 2006, Ali Khass, 1996).
- Statistical conveniences in relation to the source of data (Annual reports) and the research method (Multi Attribute Decision Making)
- Accurate possible representation of the conceptual level of Maqasid al-Shari'ah, though not necessarily exhaustible. The benefits derived from al-Maqasid should accrue to both the bank and its stakeholders.

Four indicators, namely scholarship income ratio; research income ratio; training expenses ratio and percentage of publicity expense ratio are assigned as measures to the first objective of Educating Individual. Hence, the higher the budget that the bank allocates for these three indicators, the more the bank is concerned about achieving

educating individuals in its program. This is also good for the bank to enhance the quality of its human resource and at the same time work towards creating informed customers about its objectives and product.

Four indicators (Profit Income Ratio or Interest Income Ratio (Ali Khass, 1996), Bad Debt Total Investment Ratio, Interest free Investment/ Total Investment Ratio and, Interest free Income/Total Income Ratio (Shahul Hameed et al., 2006)) are identified for measuring the second objective of Establishing Justice.

Khass used Profit Income Ratio or Interest Income Ratio to measure the relative distributive efficiency between Islamic and conventional banks, which are relevant to this study. Whereas Hameed et al. utilized Interest free Investment/ Total Investment Ratio and, Interest free Income/Total Income Ratio for the purpose of disclosure index for two Islamic banks, namely Bank Islam Malaysia Berhad and Bahrain Islamic Bank.

Profit Income Ratio or Interest Income Ratio is related to returns to the bank and the depositors. The higher these rates of returns are the higher is the realization of public interest and the interest of the bank. Hassoune (2002) is of the opinion that Islamic banks do not share the “profits” with depositors because profit is defined as the final amount of wealth attributable to the shareholders. He said Islamic banking get a ‘free lunch’ by relying for their funding on high amounts of non-profit bearing deposits. Here Hassoune may be referring to returns on Wadi’ah and general Mudharabah accounts that are at the discretion of the bank.

High rate of the ratio of bad debt to total investment indicates widening gap in income distribution due to indebtedness. Usually the banks will end up imposing penalties or repossessing the assets or projects. A penalty due to customer’s negligence is justified (Saleh, 2002). However, high rate of none performing loans due to the mode of financing or nature of the product (Siddiqi, 2004) may undermine public interest. Likewise, high ratio of Interest free investment to total investment contributes positively towards minimizing the income and wealth disparity, since interest basically transfers wealth from the poor to the rich³². Hence the bank must ensure the kind of product they offer do not create high probabilities of default.

Lastly, three PI are selected for the third objective – Public Interest. They are Zakah Net Asset Ratio, Corporate tax Profit Ratio and, Sectorial Investment Ratio. High Zakah Net Asset Ratio shows transfer of income and wealth to the poor and the needy, thereby helping to bridge the inequality gap. Similarly, higher corporate tax contributes to the government budget for more developmental projects and social services, which in turn increases the welfare of the public. Sectorial investment ratio refers to the number of vital sectors in which the banks invest in. Here, the importance is given to those real economic sectors that have direct implications to the wider population, especially those in the rural areas. Such sectors include agriculture, mining, fisheries, construction, manufacturing and small and medium scale businesses. Therefore, higher sectorial investment ratio implies wider sphere of public interest. Shahul Hameed et al., 2006, confined his sectorial investment ratio to only two banking products, namely Mudharabah and Musharakah.

³² Al-Rum, 30:39

In conclusion, table 4 below shows the indicators or measures related to each objectives of the Islamic banking. These measures however are not exhaustible.

Table 4
Operationalizing the Objectives of Islamic Banking (Phase 3 (c))

Concepts	Dimensions	Elements	Performance Indicators	Sources of Data
1. Educating Individual	D1. Advancement Of Knowledge	E1. Scholarship	PI1. Scholarship Income Ratio	Annual Report
		E2. Research	PI2. Research Income Ratio	Annual Report
	D2. Instilling new skills and improvements	E3. training	PI3. Training Expenses Ratio	Annual Report
	D3. Creating Awareness of Islamic banking	E4. Publicity	PI4. Percentage of Publicity expense	Interview
2. Establishing Justice	D4. Fair returns	E5. Fair PLS Ratio	PI5. profit Income Ratio or Interest Income Ratio	Annual Report
	D5. Cheap product and services	E6. Fair pricing	PI6. Bad Debt Total Investment Ratio	Annual Report
	D6. Elimination of injustices	E7. Interest free product	PI7. Interest free Investment/ Total Investment Ratio	Annual Report
PI8. Interest free Income/ Total Income Ratio			Annual Report	
3. Public Interest	D7. Redistribution of income & wealth	E8. Personal Income	PI9. Zakah Net Asset Ratio	Annual Report
	D8. Financing gov. budget	E9. Government revenue	PI10. Corporate tax Profit Ratio	Annual Report
	D9. Investment in vital real sector	E10. Interest free product	PI11. Sectorial Investment Ratio	Annual Report

4. Conclusion

The greatest significance of this study is that it tries to identify the objectives of IB from Maqasid al-Shari'ah perspective. It has also suggested a methodology that should develop IB performance measures from a Shari'ah framework. This will attempt to resolve a pertinent issue of whether the poor performance of Islamic banks is the reflection of their true performance or a mismatch between their objectives and conventional performance measures. This study has come at an opportune time for Islamic banks to revisit their objectives after three decades in operation. Since this is an exploratory study, hopefully future research will take it as a point of departure for developing further the objectives and performance measures of IB from a Shari'ah framework

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