Islamic Banks in Jordan: Performance and Efficiency Analysis

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Abstract: Islamic banking commenced in Jordan approximately two decades ago. Ever since it has played an important role in financing and contributing to different economic and social sectors in the country. However, there are limited studies on the financial performance of Islamic banks. This paper, therefore, examines and analyzes the Jordanian experience of Islamic banking, focusing on the two largest Islamic banks in the country: the Jordan Islamic Bank for Finance and Investment (JIBFI) and the Islamic International Arab Bank (IIAB), and evaluates these Islamic banks' performance. The paper also sheds some light on the domestic and global challenges that this sector faces. We used a performance evaluation methodology, and conducted profit maximization, capital structure and liquidity tests, and found that both banks' efficiency and ability has increased, both have expanded their investment and activities and played an important role in financing projects in Jordan. Another interesting finding is that these banks focused on short-term investments, which is often found in most Islamic banking practices. Our research also found that Islamic banks have a high growth in credit facilities and in profitability; and postulates whether this might encourage other banks to adopt the Islamic financial system.

I. Introduction

An Islamic bank is a financial and social institution whose aims, principles and practices comply with the *Sharīʿah* rules, and which must avoid charging interest in any of its practices (Ahmed, 2004). The desirability of abolishing

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fixed interest rates and the Islamization of financial systems were major issues of discussion at the first meeting of the Islamic Organization Conference (IOC) in Jeddah in 1973 (Haqiqi and Pomeranz, 2005). Many Islamic banks were subsequently founded under the profit and loss sharing system (PLS). According to Haqiqi and Pomeranz (2005) Islamic banking in its modern form went through three phases of development:

1972–1975 period: During this period, running from 1972-1975, Islamic banking was associated with a surge in oil revenues and great liquidity, many important events occurred, notably the establishment of IOC and the launch of Dubai Islamic bank in mid 1970s.

In the second phase from 1976 to the early 1980s, Islamic banking spread from the Gulf countries to Malaysia and westward to the UK. Many international and intercontinental institutions were established, such as Islamic banking associations, and consultant bodies to expand their operations.

In the last phase from 1983-to the present, Islamic banking has come of age. The Arab countries were confronted by economic setbacks, for example slowdowns in oil revenue during the early 1980s, the relative strength of the US dollar, high interest rates in the US, and capital outflow from OPEC countries. Many Arab banks opened branches in the US, Europe, Asia, and other parts of the world. In some countries - Iran, Bahrain, and Sudan, for example - the operations of the entire banking system were converted to the Islamic mode of finance.

Islamic banking practices are spreading all over the globe. According to some estimates it has grown at an annual rate of 15% over the past five years. Currently there are over 250 institutions managing assets and client money valued at around US$400 billion (AME Info, 2005). The growth of Islamic banks is proof of at least their viability. We should always bear in mind that Islamic banks are part of the banking system in the countries in which they operate and subject to the same rules and regulations.

With the continual growth of Islamic banking in the Arab and Middle East world, the concept was certain to take hold in Jordan. Jordan has a relatively open society, and an experienced and active banking and finance sector that was strengthened by a number of reforms initiated during the 1980s. The most important factor encouraging Islamic banking in Jordan is undoubtedly the fact that 92% of its people (around 6 million) are Muslims, most of whom are keen to obtain competitive financial services that conform to their beliefs. The country was thus well-placed and ready to adopt the Islamic banking concept and develop it further.

Islamic banking in Jordan started approximately two decades ago, with the foundation of its first Islamic bank, the Jordan Islamic Bank for Finance and Investment in 1978. Since then, Islamic banks in the country have grown in number and size, with the establishment of more branches and more Islamic banks such as the Islamic International Arab Bank, and the establishment of other Islamic financial institutions, such as Jordan Islamic Insurance, Islamic Investment House and Jordan Finance House.

Because there have been limited studies of Islamic banking performance in Jordan, this paper aims to examine and analyze the Jordanian experience of Islamic banking by evaluating the performance of Islamic banks in the country which have been operating over the last two decades. The paper also sheds some light on the role of Islamic banking in Jordan in terms of financing and contributing to various economic and social sectors in the country. We also review some of the changes (domestic and global), which are facing this sector.

This paper is organized as follows. Section II provides an overview of the development of the banking industry and Islamic banking in Jordan. Section III, after explaining the methodology and tools for measuring bank performance, reports the results and analysis. Section IV highlights the challenges ahead and prospects for Islamic banking in Jordan. Section V presents a summary and the paper's conclusions.

II. Banking and Islamic Finance in Jordan

The banking system in Jordan has traditionally been dominated by the Central Bank and Amman Financial Market. The Central Bank was established in 1964, and its major role was for note issue, exchange reserves management, and regulation of credit. The bank acted as the fiscal agent for the government, regulated the commercial banking sector, and sponsored the creation of new financial institutions. The banking sector during the 1970s and early 1980s saw loans and deposits more than double. Over the same period the number of financial institutions tripled as the government encouraged the expansion of banking services as a key driver of its economic development policy. Deposits were attracted from other Arab countries, as well as savings and remittances, which served to supply loans to growing companies in need of capital.

During the 1980s Jordan was a unique case among the Arab World when the value of its bank assets surpassed its GDP. Commercial bank assets rose from JD1.1 million in 1980 to JD2.3 billion in 1985. Total deposits also increased from about JD800 million to JD1.7 billion. Strict Central Bank consumer credit controls and government success in encouraging savings resulted in annual growth of 7% from 1980 to 1987. The liquid money supply reached about JD900 million during this period, with no significant inflation. But during the mid-1980s, the government became concerned that the banking sector in the country was expanding too rapidly. It was worried that the banks might get into risky lending activity and that excessive competition for assets might drive them to lend to foreign companies instead of local ones. The Central Bank of Jordan therefore imposed a moratorium on the establishment of new commercial banks. In 1985 more than 27% of commercial bank credit financed trade, and less than 10% financed corporate investment (JIR, 2005).

The 1980s also saw the government exercise greater regulation of bank activity to counterbalance fluctuating stock values and the rapid expansion of banking. Among the regulations was that banks were required to invest 8% of their deposits in government bills and bonds, and invest at least 15% of their capital in public and mixed-sector corporate equity. The minimum capital requirement was increased to JD5 million. Binding interest rate ceilings were set on both loans and deposits, and dinar exchange rates were fixed by the Central Bank.

During the late 1980s, 30 major banks and financial institutions operated in the country, among them eight major locally based conventional commercial banks, six foreign banks, two Islamic banks, and a host of smaller or more specialized foreign and domestic financial institutions. The Arab Bank was by far the largest locally based commercial bank, a Palestinian institution that moved to Amman from Jerusalem in 1948. In terms of total assets the Jordan National Bank, the Cairo-Amman Bank, the Jordan-Kuwait bank, and the Petra Bank were the most important local institutions. Foreign banks included Citibank, Grindlays Bank, the Hong Kong-based British Bank of the Middle East, as well as the Iraq's Rafidayn Bank and Egypt's Arab Land Bank. Chase Manhattan left Jordan following the 1984 government-imposed financial regulations (JIR, 2005).

Since 1989 the Central Bank of Jordan (CBJ) has undertaken a number of reforms to make the banking system more secure and competitive, including:

(i) Paid-up capital of Jordanian banks increased to JD 20 million;
(ii) Paid-up capital of foreign banks increased to JD 10 million;
(iii) Banks are required to hold 80% of required reserves at the CBJ;
(iv) Restrictions on the inter-bank foreign exchange market were lifted during 1996;
(v) Restrictions on the flow of trade in foreign currency were removed during 1997;
(vi) Main restrictions on foreign capital were removed during 1997 (JIB, 2005);
(vii) During 1999-2002, more reforms were undertaken to enhance the sector such as the new banking law, new securities law, new auditing profession law, among others (Khamis, 2003).

The number of banks operating in Jordan rose to 24 at the end of 2004, of which 14 were commercial, eight foreign banks and two Islamic banks (Central Bank of Jordan, 2004). In addition to that, there are four specialized credit institutions in Jordan (such as Industrial Development Bank etc). These banks carry out business throughout the Kingdom through a network of 447 branches and 154 representative offices. Thus, the population branch index of operating banks, at the end of 2004, was nearly 11.9 thousand citizens per branch. On the other hand, the number of branches of Jordanian banks operating abroad reached 124, of which 52 branches were operating in Palestine in addition to ten representative offices (Central Bank of Jordan, 2004). It is also worth noting here that the Amman Stock Exchange (ASE) was established in 1976, and is considered to be the most efficient stock exchange in the Arab World, as well as the largest and fastest growing market in the region open to investors. The ASE is one of the few Middle East and North African countries (MENA) markets which take part in the International Finance Corporation Emerging Markets Index. Its market capitalization to GDP ratio of 73.1% is one of the highest in the region, exceeding that of many countries such as Israel, Saudi Arabia, Egypt, among others (JIB, 2005).

III. The Structure of Islamic Banking in Jordan

Currently there are two Islamic banks listed in the Amman Stock Exchange (ASE): namely Jordan Islamic Bank for Finance and Investment and Islamic International Arab Bank PLC.

3.1. The Jordan Islamic Bank for Finance and Investment (JIBFI)

The Jordan Islamic Bank for Finance and Investment was established as a public shareholding company in 1978, and was licensed with the objective to practice financing, banking and investment activities in compliance with the provisions of *Sharīʿah* law. It has succeeded in achieving substantial growth (Table 1) and, by providing all kinds of investment activities, has established itself as one of the leading banks in Jordan.

Table 1: Jordan Islamic Bank for Finance and Investment (JIBFI) Aggregates during 1998-2003

	1998	1999	2000	2001	2002	2003
Total Assets	706.763	657.562	658.892	703.843	797.012	975.490
Direct Credit Facilities, Net	391.594	277.572	250.958	252.571	281.369	321.983
Customers Deposits	534.821	547.794	564.577	621.509	710.520	876.956
Total Shareholders Equity	50.910	52.588	54.529	53.578	55.592	56.983
Growth (%)						
Total Assets		-6.9614	0.2022	6.8223	13.2371	22.3935
Direct Credit Facilities, Net		-29.1176	-9.5880	0.6427	11.4020	14.4343
Customers Deposits		2.4257	3.0638	10.0839	14.3218	23.4245
Total Shareholders Equity		3.2965	3.6899	-1.7430	3.7575	2.5022

Source: Central Bank of Jordan and Amman Stock Exchange

JIBFI plays an effective role in developing economic and social activities, as evidenced by the growing number of people who deposit their savings with the bank. The bank channels these deposits into investment and job-creation. The number of people who benefited from interest free loans reached about 144,000, and the total value of such loans amounted to JD 51.1 million. Given the objective of the bank to increase its presence in the country so as to reach all citizens interested in using Islamic banking products (such as *Muḍāraba, Mushārka, Murābaḥa, etc.*), it spread its network, which comprised 52 branches and 12 cash offices. By 2004, the number of accounts opened with the bank through its network reached 997,000; the number of its employees reached 1418 in 2004. Also, it has been successful in establishing correspondent relations with more than 300 international banks (JIBFI, Annual Report, 2004).

3.2. The Islamic International Arab Bank (IIAB)

The Islamic International Arab Bank (IIAB) is the second bank in Jordan to operate according to Islamic *Sharīʿah*. It began its operations in February 1998 with four branches in Jordan. It is offering a complete set of Islamic banking, financing and correspondence services to meet economic and social needs within the banking sector in accordance with the *Sharīʿah*. IIAB is now ranked as the fourth bank in Jordan with a paid-up capital of 40 JD million (1 JD = US $1.429). At the end of 2002 it had eleven branches around he country, and 217 employees. Table 2 summarizes the banks aggregates during the period 1998-2003 (IIAB, 2002).

Table 2: Islamic International Arab Bank Aggregates during 1998-2003

	1998	1999	2000	2001	2002	2003
Total Assets	137.294	216.321	197.036	253.246	314.741	385.529
Direct Credit Facilities, Net	85.982	145.747	55.174	97.063	105.927	122.670
Customers Deposits	94.408	169.233	77.361	112.436	152.328	197.594
Total Shareholders Equity	40.610	42.025	45.177	45.559	47.085	48.917
Growth (%)						
Total Assets		57.561	-8.915	28.528	24.282	22.491
Direct Credit Facilities, Net		69.509	-62.144	75.922	9.133	15.806
Customers Deposits		79.257	-54.287	45.339	35.480	29.716
Total Shareholders Equity		3.484	7.500	0.846	3.349	3.892

Source: Central Bank of Jordan and Amman Stock Exchange

IV. Methodology and Performance Analysis of Islamic Banks in Jordan

According to financial management theory, banks' performance can be evaluated using various financial ratios, for example, profitability ratios and liquidity ratios, among others. Sabi (1996) and Samad (1999), among others, have used such financial ratios to evaluate or analyze bank performance. In this study, 'Banking Efficiency Model' will be used to measure the performance of Islamic banking in Jordan. Due to unavailability of long-period time-series data for IIAB, the study is limited only to four years time-series data. Even so, since there have been no studies on the development of Islamic banks in Jordan, the evaluation done here should be of some use.

Performance evaluation is an important step to measure the growth and development of any bank. It is customary in commercial banks to evaluate their objectives and goals. The core objective of banks, as of most commercial institutions, is to maximize profits. Without making profits firms are unable to continue working and develop services. On the other hand, Islamic banks also have other objectives besides making or maximizing profits, namely to foster economic and social well-being and to ensure that there is no exploitation of the customers.

4.1 Profit Maximization Test

Eight indicators of profitability and performance are taken to evaluate the bank performance as depicted in Table 3 and Table 4.

Table 3: Profitability and Performance for JIBFI

Profitability and Performance	2000	2001	2002	2003
Return on Assets (ROA) (%)	0.33	0.14	0.26	0.33
Return on Equity (ROE) (%)	3.95	1.88	3.68	5.62
Net Profit and Commissions Income/Operational Income (%)	88.41	86.31	90.37	87.44
Credit Profit / Credit Facilities, Net (%)	11.89	10.75	10.15	10.09
Net Income / Total Revenues (%)	6.38	3.18	5.89	7.95
Total Revenues / Total Assets (%)	5.12	4.50	4.37	4.13
(Provision for Credit Facilities + Profit in Suspense) / Credit Facilities (%)	9.95	10.65	11.01	6.86
Net Income / Total Liabilities	0.36	0.16	0.28	0.35

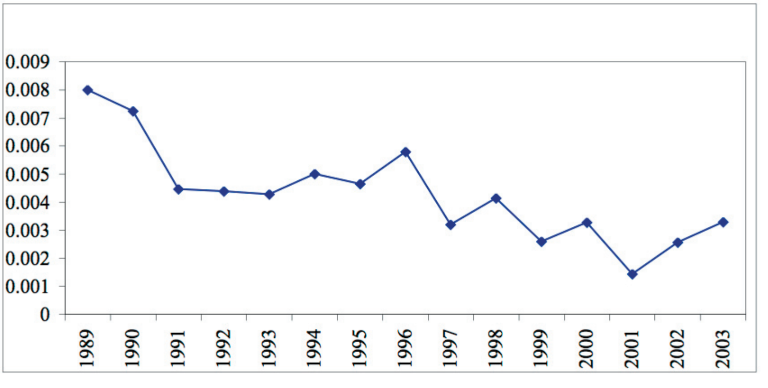
These analyses in tables 3 and 4 demonstrate that both measures of performance (ROA and ROE) are positive for both banks. Both measures of performance are higher in IIAB in all years, compared with JIBFI. The ROA in 2000 was 0.33% JIBFI compared with 1.59% for IIAB. The ROE in 2000 was 3.95% for JIBFI, compared with 6.94% for IIAB.

Table 4: Profitability and Performance for IIAB

Profitability and Performance	2000	2001	2002	2003
Return on Assets (ROA) (%)	1.59	1.14	0.58	0.52
Return on Equity (ROE) (%)	6.94	6.33	3.88	4.08
Net Profit and Commissions Income/Operational Income (%)	33.43	44.21	62.50	60.20
Credit Profit / Credit Facilities, Net (%)	8.95	6.68	6.39	5.66
Net Income / Total Revenues (%)	32.03	26.75	18.66	19.30
Total Revenues / Total Assets (%)	4.97	4.25	3.11	2.68
(Provision for Credit Facilities + Profit in Suspense) / Credit Facilities (%)	1.43	1.48	1.40	1.51
Net Income / Total Liabilities	2.06	1.39	0.68	0.59

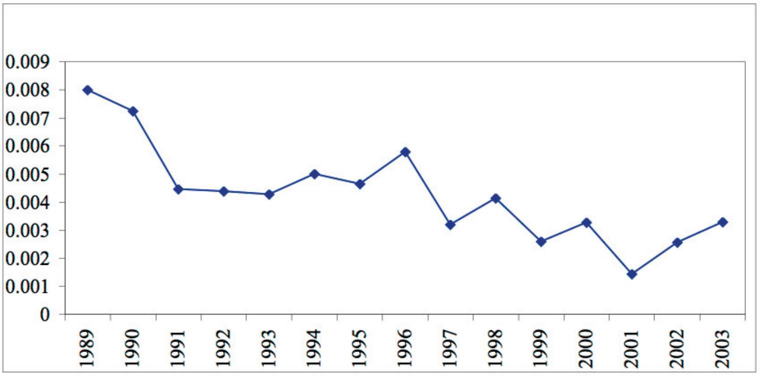
Figures 1 and 2 show the ROI and ROE for JIBFI from 1989 to 2003. The bank's ROI decreased during 1991, 1997, 1999, 2001, and 2002. The decrease during the years 1999, 2001 and 2002 might be due to competition between the two Islamic banks, while the decrease during 1991 could be because of the First Gulf War.

Figure 1: Return on Investment (ROI) for JIBFI



Source: Amman Stock Exchange and JIBFI

Figure 2: Return on Equity (ROE) for JIBFI

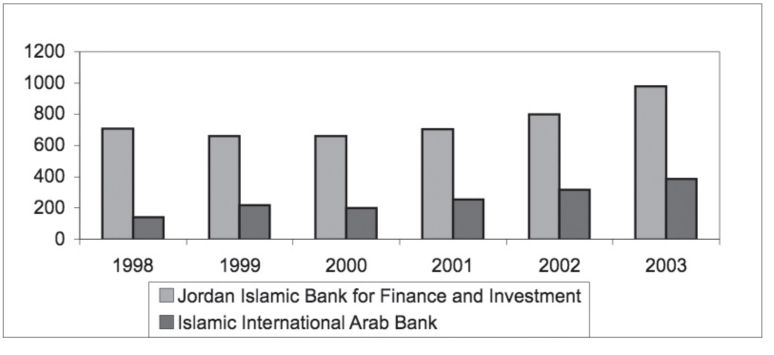


Source: Amman Stock Exchange and JIBFI

The bank performance measure ROA declined for both banks in 2001. While it increased for JIBFI in 2002 and 2003, it continued to decrease for IIAB. However, ROA was still higher for the IIAB than for JIBFI.

Figure 3 shows that the total assets held by JIBFI were more than the total assets held by IIAB in the years studied: approximately 461.856 million in 2000 and 589,961 million in 2003. Also, the total shareholder equity in JIBFI is greater than the total shareholder equity in IIAB: approximately 9.352 million, compared with 8.065 million in 2003.

Figure 3: Total Assets in Islamic Banks in Jordan, 1998-2003



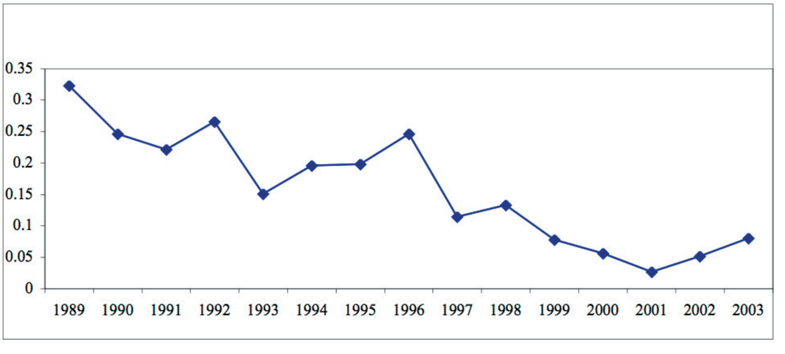
Source: Amman Stock Exchange

Other performance measures calculate facilities and liabilities. Net profit and commissions income/operational income in 2000 was 88.41% for JIBFI, compared with 33.43% for IIAB. This ratio increased for both banks in 2002 and was still very high for JIBFI, at 87.44% in 2003, compared with 60.20 % for IIAB. This ratio shows that the IIAB increased its profit and commissions income, which indicates that the bank expanded its activities at a higher rate.

'Credit profit/credit facilities, net', 'net income/total revenues' and 'total revenues/total assets' are also calculated for both banks. Both 'credit profit/credit facilities' and 'total revenues/total assets' are higher for JIBFI, compared with IIAB (see Table 3 and Table 4). For example, the ratio of 'Credit Profit/Credit Facilities' for JIBFI was 11.89% in 2000 compared with 8.95% for IIAB.

The Net Income/Total Revenues ratio for JIBFI was 6.38% in 2000 compared with 32.03% for IIAB. This ratio increased in 2003 to 7.95% for JIBFI and decreased for IIAB to 19.30%, which could be due to increased administration expenses resulting from expansion and opening of new branches.

Figure 4: Earning per Share (EPS) for JIBFI



Source: Amman Stock Exchange

Another ratio, the provision for credit facilities + profits in suspense/credit facilities ratio, was very high for the JIBFI, compared with the same period for IIAB. For example, this ratio was 6.86 % in 2003 for JIBFI, compared with 1.51 % for IIAB. Net income/total liabilities was lower for JIBFI compared with IIAB.

Another measure used to evaluate bank performance is bank earning per share (EPS). Figure 4 shows that this ratio for JIBFI decreased during the last six years measured.

Overall, the above performance measures show the ability and the efficiency of both Islamic banks to increase their income and reduce expenses.

4.2 Capital structure

The importance of capital structure analysis is that it reflects bank risk, and also shows the structure of bank loans and deposits, as well as to what degree the bank is able to face an emergency such as a demand deposit. Furthermore, it determines what types of investment the banks concentrate on, and whether the bank prefers to invest in long-term or short-term investments.

Table 5: Capital Structure for JIBFI

Capital Structure	2000	2001	2002	2003
Equity Ratio (%)	8.28	7.61	6.98	5.84
Shareholders Equity / Total Deposits (%)	9.59	8.56	7.78	6.46
Debt Ratio (%)	91.72	92.39	93.02	94.16
Total Deposits / Total Assets (%)	86.30	88.95	89.69	90.36
Net Credit Facilities to Total Assets (%)	38.09	35.88	35.30	33.01
Net Credit Facilities to Total Deposits (%)	44.13	40.34	39.36	36.53
Shareholders Equity to Credit Facilities, Net (%)	21.73	21.21	19.76	17.70
Current Assets / Total Assets	39.467	41.121	40.328	51.041
Total Debt / Total Equity	1,108.33	1,213.67	1,333.69	1,611.91

Tables 5 and 6 show ten ratios to measure the capital structure of the Islamic banks. The equity ratio reflects the total equity/total assets. For JIBFI the equity ratio decreased to 5.84% in 2003 compared to 8.28% in 2000; for IIAB, it declined to 12.69% in 2003 compared to 22.93% in 2000. The lower equity ratio for JIBFI reflects the expansion of this bank in total assets. The higher equity ratio for IIAB indicates that the bank was expanding its investments.

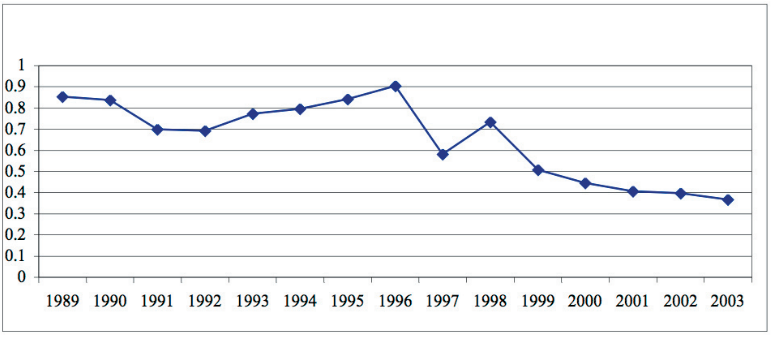
The shareholder equity/total deposit measure reflects the percentage of total equity to total deposit. This decreased from 9.59 % in 2000 to 6.46 % in 2003 for JIBFI, which also decreased from 31.47 % to 15.29 % for IIAB during the same period. This decrease reflects the increase in customers' deposits. As seen from the tables, JIBFI increased its deposits from 2000 until 2003 at a higher rate.

Table 6: Capital structure for IIAB

Capital structure	2000	2001	2002	2003
Equity Ratio (%)	22.93	17.99	14.96	12.69
Shareholders Equity / Total Deposits (%)	31.47	23.48	18.64	15.29
Debt Ratio (%)	77.07	82.01	85.04	87.31
Total Deposits / Total Assets (%)	72.87	76.61	80.24	82.97
Net Credit Facilities to Total Assets (%)	28.00	38.33	33.66	31.82
Net Credit Facilities to Total Deposits (%)	38.43	50.03	41.95	38.35
Shareholders Equity to Credit Facilities, Net (%)	81.88	46.94	44.45	39.88
Current Assets / Total Assets	48.12	51.07	49.40	50.14
Total Debt / Total Equity	336.14	455.87	568.46	688.12

The debt ratio for both banks is very high because of a high percentage of customer deposits, and because each bank depends on customer deposits to lend money. The debt ratio increased from 91.72 % in 2000 to 94.16 % in 2003 for JIBFI, and also increased from 77.07 per cent in 2000 to 87.31 % in 2003 for IIAB. Tables 5 and 6 show that both banks increased their debt ratio over the years analyzed. The results in the previous ratio are explained by the ratio of total deposits/total assets ratio. This ratio shows the growth of deposits in both banks. Both ratios (net credit facilities to total assets and net credit facilities to total deposits) for JIBFI decreased in 2003 in comparison with 2000, 2001 and 2002. Both ratios increased for IIAB in 2003 (see Tables 5 and 6).

Figure 5: Credit to Deposit Ratio for Jordan Islamic For Finance and Investment

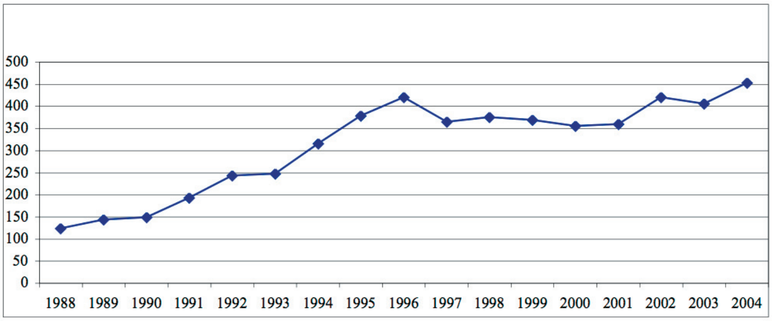


Source: Amman Stock Exchange, Annual Reports

Another measure that shows that JIBFI increased their lending activities more than IIAB is the Shareholders Equity to Credit Facilities ratio. The ratio was 17.70% and 21.73% in 2003 and 2000 respectively for JIBFI, and 39.88% and 81.88% in 2003 and 2000 respectively for IIAB. The results also tell us that IIAB facilities were growing at a higher rate. Figure 5 indicates that the credit to deposits ratio decreased in the last five years for JIBFI. This could be as a result of a higher increase in deposits compared with low increase in credit. Figure 6 shows that the yearly credit issued by JIBFI increased from 1989 to 2004. The credit facilities increased during the last 15 years, which reflects the bank's growth in credit in the Jordanian market.

The current assets/total assets ratio reflects the structure of assets, as a measure of liquidity. This ratio increased in both banks: from 39.467 % in 2000 to 51.041% in 2003 for JIBFI, for example. This increase is due to the increase in the bank's deposits as well as other assets in which the bank expanded its investment in facilities. This suggests that JIBFI focuses on short-term rather than long-term investment.

Figure 6: Yearly Islamic Bank Credit for JIBFI



Source: Central Bank of Jordan

Another measure of capital structure is the total debt/total equity ratio. Tables 5 and 6 show that this ratio increased for both banks. The main reason is the high percentage increases in customer deposits. The total debt/total equity rose to 1,611.91% for JIBFI in 2003 compared with a rise to 688.12% for IIAB in the same year. This indicates that both banks increased their activities and were growing in the market. The ratio more than doubled for IIAB, meaning that it expanded its activities and enjoyed growth in deposits.

4.3 Liquidity Measures

Liquidity management ensures the bank's ability to meet its short-term and long-term funding commitments while achieving optimal return on investment. The liquidity position of the bank and appropriate policy strategies and adjustments are an important element of its position and ability to expand and issue loans, and expand its investment activities. Liquidity analysis at different levels including a maturities analysis of assets and liabilities is important for banks to be confident about their liquidity. Such analysis also covers the source and use of funds.

As discussed earlier, the capital structure of both Islamic banks became stronger and more dependent on short-term rather than long term investment. The structure of its capital affects the liquidity risk. To measure that risk and the bank's ability to meet its obligations, three measures of liquidity are taken. Tables 7 and 8 summarize these ratios in both banks. JIBFI increased its quick ratio in 2003 to 0.56% from 0.46% in 2000. The quick ratio in IIAB was higher, going to 0.60% in 2003 from 0.66% in 2000.

The ratio of cash and investments to total deposits was close to 65% in both banks in 2003. The increase indicates that there was a growing rate of lending. It also reflects the banks' ability to cover loans from assets as well as to face instant demand for deposits. Both banks have the ability to meet instant demand for money.

Another measure of liquidity is the Cash + Trading Investments/ Total Deposits ratio. This ratio for IIAB was higher than for JIBFI.

Table 7: Bank Liquidity, JIBFI

Liquidity ratios	2000	2001	2002	2003
Quick Ratio (Times)	0.46	0.46	0.45	0.56
Cash + Investments / Total Deposits (%)	61.94	64.31	56.78	65.13
Cash + Trading Investments / Total Deposits(Times)	0.46	0.47	0.45	0.56

Table 8: Bank Liquidity IIAB

Liquidity ratios	2000	2001	2002	2003
Quick Ratio (Times)	0.66	0.67	0.62	0.60
Cash + Investments / Total Deposits (%)	66.04	66.67	64.23	64.75
Cash + Trading Investments / Total Deposits (Times)	0.66	0.67	0.62	0.60

V. Challenges and Prospects of Islamic Banking in Jordan

The Islamic banking industry has grown rapidly worldwide since the 1970s, and has become an important issue for bankers, researchers and policy makers. It has grown rapidly in the Middle East and in Jordan in particular, because the country has an open and active society and is one of the most experienced banking sectors in the Arabic region. The country's majority Muslim population, most of whom are professionals and businessmen, are keen to obtain competitive financial services that meet their beliefs. These factors have created a conducive environment and opportunities for the country to be engaged in Islamic banking concepts for the last two decades.

Islamic banks in Jordan have great potential to grow further in the coming years, because they are focusing on many strategies to attract more customers from Muslim as well as non-Muslim areas, and are enhancing their marketing activities by increasing the awareness of their type of banking services and strengthening the relationship with customers. Islamic banks in Jordan are trying to build a solid, long-term relationship between Islamic banking providers and customers. Islamic banks in Jordan have great potential to attract foreign capital investment from other Muslim and neighbouring Arab and Middle Eastern countries, especially after September 11. This will naturally assist the development of the county's economy.

Islamic banks in Jordan have played an important role in financing and developing various sectors in the Jordanian economy by using elements of the Islamic approach to banking (see Table 9), such as *Mushārakah, Muḍārabah, Murābaḥah Istiṣnāʿ*, among many others. Table 10 shows how the Islamic International Arab Bank has contributed to various sectors in the economy, such as industry and mining, agriculture, construction, trade and others. Where most of these sectors are in urgent need for finance, Islamic banks have played an important role in financing business operations, improving their business performance and creating jobs in the labour market. This is of course true for other Islamic banks in the country, but especially so for the Jordan Islamic Bank, as shown in Table 11, where its contribution to various sectors and thus its commitment to its social role are evidenced. For example, the Jordan Islamic Bank has continued its programme for financing small-scale industries. Since the start of this programme, the bank has financed nearly 40 projects, with a cumulative cost of approximately JD 700,500 (JIBFI, 2003). Table 11 shows the bank's contribution to different sectors of the Jordanian economy. This covers a wide range of social activities and utilities, including hospitals, medical clinics, education, transport and many others.

Table 9: Elements of the Financing and Investment Portfolio for IIAB

	1999	2000	2001	2002
Murābahah	16,711,772	29,314,743	49,087,017	46,274,243
Muḍārabah	279,366	1,311,785	1,052,426	2,905,134
Mushārakah	---	325,284	626,993	605,132
*Istiṣnā*ʿ	755,928	1,390,300	1,151,330	936,531
Specified Commodities Investments	69,502,530	121,216,710	163,260,477	137,105,390
Customers' Liabilities-Letters of Credit	4,404,745	8,368,316	5,878,097	6,231,320
Customers' Liabilities- Letters of Guarantee	1,173,921	1,856,350	2,443,216	3,736,371
Acceptances	682,084	1,898,128	2,546,015	4,061,085

Source: IIAB (2002)

Table 10: Contribution of Islamic Banking in the following Sectors: IIAB

Sector	1999	2000	2001	2002
Industry and Mining	1,618,631	2,165,131	2,070,024	2,527,679
Agriculture	205,732	525,747	590,980	711,323
Construction	795,328	1,034,227	4,158,566	4,946,451
General Trade	9,068,609	7,592,845	12,993,493	9,613,811
Transportation Services	674,874	504,756	289,578	108,346
Properties, Real Estate Financing	2,048,528	5,074,269	7,959,681	8,881,677
Automobile Financing	1,341,555	3,151,534	7,421,749	7,980,575
Consumer Goods Financing	1,924,993	9,545,582	9,871,763	9,355,737
Others	370,536	3,081,791	6,561,932	6,595,441

Source: IIAB (2002)

Table 11: Contribution of JIBFI in various Economic Sectors 2002-2003

Sectors	2002 (JD 000)	2003 (JD 000)
Agriculture	1,070	1,261
Industry and Mining	31,496	33,420
General Trade	55,205	95,072
Construction	113,832	116,770
Transport	45,645	57,137
Miscellaneous	233,143	168,638
Total	480,391	472,298

Source: JIBFI (2003)

Islamic banks in Jordan have the potential to increase their customer base to cover most of the country by opening new branches and offices in order to be near to current as well as potential customers. The banks are working hard to achieve these goals, despite the strong local challanges and the difficult circumstances facing this sector. The banks nevertheless have the potential to grow further and to enhance development in production sectors, as evidenced by the bank's record of performance and its strategies. Among these are: maintaining the strength of the banks' financial position, increasing the Islamic banks' market share, optimizing the profits of shareholders and depositors, increasing adherence to ethical values and improving performance standards.

Islamic banks in Jordan are trying to adopt all the necessary tools and other means to achieve their goals by increasing their customer base, increasing the awareness of Islamic banking products, adopting new financial and investment tools, adopting IT to provide the best services for its customers, providing training for its employees and many other means important for their development and performance. Islamic banks in Jordan have good support from both the public as well as private sectors. These banks have the potential to succeed by providing distinguished banking and investment services that satisfy government and private institutions as well as individuals, and will play an important role in strengthening the Jordanian banking sector as well as the economy as a whole.

Even though the Islamic banks in Jordan are performing well and have solid plans for the future, they also face some key challenges domestically as well as globally that reduce their growth potential. Among these are the conflict situations in the region (for example, the political turmoil in Palestine and other parts of the Middle East), the economic slowdown that has plagued the country for the past few years, globalization (for example, abolition of tax barriers, liberalization of commodities and services and so on), increased cash surpluses with limited finance and investment opportunities (IIAB, 2002), public awareness and acceptance, lack of institutions that conduct research and development in this area, lack of skilled professional people, and local competition from large numbers of commercial banks operating in the country.

Islamic banking globally also faces many challenges. Saleh and Zeitun (2005) identify many for Lebanon, such as public awareness and acceptance, high competition from many conventional banks, lack of talented labour, among others. Islamic banking also faces financial globalization, speculation, the flow of savings abroad, competition from international banks (AME, 2005), lack of an inter-bank Islamic money market and Islamic money brokers, investors who are unwilling to hold to maturity Islamic paper with a long-term nature, different interpretation by Islamic scholars in different countries (AME, 2005) and so on. Banks also face problems regarding their readiness to meet global competition (due to their limited capital and asset base) and shortage of skilled and trained labour in the Islamic banking industry, the defaulting culture of borrowers, a lack of harmonization of Islamic financial practices, confusion about what is acceptable practice in the Islamic banking industry and many other challenges (Sarker, 1999; Saleh and Zeitun, 2005). Further, Islamic banking must concentrate on risk management and product innovation. The issue of human capital also needs greater attention, and development is required to meet the needs of more diversified business activities.

VI. Conclusion

While Islamic banks in Jordan have been operating for the last two decades, there have been limited studies on their financial performance. To fill this gap, this paper has analyzed and evaluated the Jordanian experience with Islamic banking in order to determine the Islamic banks' performance as well as their activities. The paper also reviewed the domestic and global challenges that are facing this relatively new concept.

By using performance evaluation procedures, which are important to measure the growth and development of any bank, we found that both the IIAB and JIBFI banks showed that their efficiency and the profitability increased. Both banks expanded their investments and activities and have played significant roles in financing important projects in the market. These Islamic banks had a high growth in credit facilities and profitability.

Additional interesting findings were that these Islamic banks have focused on short- rather than long-term investments. This seems to be the case for most Islamic banking practices, where the capital structure becomes stronger and depends on short-term investment. In comparing the two banks, the Jordan Islamic Bank for Finance and Investment has increased its lending activities more than the Islamic International Arab Bank, and the facilities of the latter also grew at a higher rate. The results also show that the Jordan Islamic Bank for Finance and Investment has a high profitability, which should encourage other banks to employ financial Islamic products.

Islamic banking in Jordan has played an important role in financing and contributing to various sectors in the country, such as industry and mining, agriculture, construction, trade and others. Most of these sectors are in urgent need of finance, so Islamic banks' investments here show their commitment to their social role. They have played an important role in financing business operations, improved their own business performance and created jobs in the labour market.

The paper also sheds some light on the development of Islamic banking globally. This sector has not only grown in the Muslim world, but has also gained significant attention in the Western world, with over 250 Islamic banks worldwide controlling approximately US$400 billion in assets and client money. The growth of these banks is proof of their success, and an indication that these banks continue to grow in number and size worldwide.

Islamic banks in Jordan are facing many challenges, among them, conflicts in the region, the economic slowdown, globalization, increased cash surpluses with limited finance and investment opportunities, public awareness and acceptance, lack of institutions that conduct research and development in this area, lack of skilled and professional people, and local competition from large numbers of commercial banks that are operating in the country.

Since the majority of the population in Jordan are Muslims, and given the promising and positive factors in the Islamic banking system, the future of Islamic banks in the country seems promising, and they could emerge as major financial institutions in the region. However, in order to ensure continuous success, Islamic banks need to have good corporate governance, and invest in IT and innovation, in order to increase their competitiveness. They should adopt more strategies to promote their products and establish long-term relationships with customers. Public awareness needs to be increased, and customers need to understand the Islamic financial concepts much better in order to trust and utilize these banks' products. Therefore, Islamic banks have to work harder to brand their products and to build a good relationship with customers.

The management of Islamic banks must also ensure that staff has the necessary skills and knowledge about Islamic banking products and principles. There is a need for more collaboration between Islamic banks in Jordan, as well as with other Islamic banks in the Arab and Muslim world, to increase and open up more Islamic banking training centres and develop institutions that conduct research and development to improve the work of Islamic banks.

Jordan needs to lead collaboration with other countries that are embracing this concept, such as Dubai, Bahrain, Malaysia and others, in order to exchange ideas and knowledge and work on issues such as the application of universal banking, crisis management and developing an Islamic financial market (especially for medium- and long-term products). In order to eliminate confusion and develop a more comprehensive Islamic banking system, the development of the securitization process, *Sharīʿah* harmonization, product standardization and the application of *Sharīʿah*-compliant products are also needed.

These banks should always be ready to adopt new, and enhance their existing, IT and other skills to maintain efficiency and productivity, in order to be customer oriented, and innovative in terms of products to meet the requirements of more diversified business activities.

This paper used performance evaluation methodology to examine the Jordanian experience in Islamic banking, and found that the efficiency and ability of Islamic banks in Jordan have expanded, and that they have played an important role in financing many investment projects in the country. Islamic banks in Jordan have achieved high growth levels in terms of profitability and credit expansion, which should encourage other banks to operate under and practice Islamic banking principles based on *Sharīʿah* rules.

Because there are very limited studies in the area of Islamic banking in Jordan, this study is an important first step towards understanding the development of Islamic banking in the Middle East, and in Jordan in particular. This study can also be extended to compare the performance of Jordanian Islamic banks with conventional ones by using more sophisticated techniques such as panel data regression models or Data Envelopment Analysis (DEA).

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