ISLAMIC BANKING IN PAKISTAN:

QUANTITATIVE ANALYSIS (SERIES-II)

Prof. Dr. Khawaja Amjad Saeed*

PRELUDE

This piece presents quantitative analysis of the growth of Islamic Banking Institutions (IBIs) in Pakistan. The focus of quantitative analysis has been reviewed covering: Branch Network, Financing Pattern of IBIs, their Investments, Financing and selected performance indicators as compared to total banking industry of the country. Information in respect of above was extracted from two issues of Islamic Banking Bulletin (December 2009 & March 2010) released by Islamic Banking Department of State Bank of Pakistan, Karachi.

IBIs BRANCH NETWORK

Total number of IBIs Branches in the year 2003 was 17. This number rose to 854 in March 2010. This shows 38 times increase in the growth of IBIs Branch Network in Pakistan. Future, accordingly, augurs well for their growth.

This total number based on data available till December 2009 of full fledged Islamic Banks, was six having 400 branches. Islamic branches of Conventional Banks, generally termed as stand-alone branches, were 168. Total numbers of sub-branches was fifty-one (51). IBIs Network covered all Pakistan with a break up of: Punjab 45%, Sindh 34%, KP 10%, Balochistan 5%, Federal Capital 5%, Azad Kashmir 1% and with a presence of one branch in Northern Areas. Amongst the full fledged IBIs, the break up consisted of Meezan Bank Limited, 41%, BankIslamic Pakistan 18%, Emirates Global Islamic Bank Limited 15%, Dawood Islamic Bank Limited 9% and Albaraka Islamic Bank 7%.

There is a current trend of growing network of the above banks throughout Pakistan. Stand-alone Islamic branches of Conventional banks represented: Bank Alfalah Limited 36, Askari Bank Limited, 17, the Bank of Khyber 10, MCB Bank Limited 6, Standard Chartered Bank 6, National Bank of Pakistan 5, Bank Al-Habib Limited 4, Faisal Bank Limited 4, Soneri Bank Limited 4, United Bank Limited 3, Habib Metropolitan Limited 2, Royal Bank of Scotland 2 and Habib Bank Limited 1.

The State Bank of Pakistan is urged to monitor the growth of stand-alone branches which is extremely low. These banks do not appear to be serious of converting their Conventional banks into Islamic Banks. The time target may be announced to address the above aspects. The sooner, this is done the better. It is interesting to know that there is a wide spread city-wise presence of branches of IBIs throughout all the four Provinces of Pakistan including Azad Kashmir, Federal Capital and Northern Areas. Similar comments are applicable to IBIs sub-branches.

In respect of location of branch network of IBIs, the minimum was one branch (Northern Areas/Gilgit) and the maximum was in Sind / Karachi spread over five cities with 180 branches. Punjab ranked No. 2 (109 branches), Federal Capital / Islamabad (31 branches), Khyber Pakhtoonkhwa (28 branches in eight cities) and 21 branches in Balochistan in eight cities.

The above analysis guides us to conclude that branch network of IBIs is expanding. However, Conventional Banks which are currently enjoying the facility of setting up stand-alone branches need to be motivated and encouraged to follow the above trend.

IBIS FINANCING

It is interesting to note that IBIs financing as of March 31, 2010 was Rs.162 billion. This was concentrated only in three major products namely, Murabaha (38%), Diminishing Musharqa (38%) and Ijara (14%) – aggregating to a total of 84%. The remaining 16% was in three Istisna, Salam, Musharqa etc. (16%). There is an urgent need of IBIs to employ ideological inspired and professionally qualified people with innovative mind to undertake the challenging work of innovating new products and offer to the stakeholders new products, failing which the progress will be slow. R&D should be carried out and institutionalized arrangements and be undertaken in this respect. This is a critical area screaming for attention of IBIs and SBPO.

Sectoral composition of IBIs financing was undertaken by us which showed pattern such as: Textile (20%), Individuals (20%), Chemical and Pharma (10%), Sugar (6%), Energy Products and Transmission (4%), Cement (3%), and other sectors (including 31% others). All these aggregate to a total of 100%.

An analytical analysis was undertaken in respect of all IBIs' Non-Performing Loans. This represented growing trend: March 2009: 4.5%, December 2009: 6.3% and March 2010: 7.3%.

It is high time that IBIs attend to this negative growth and try to arrest and reverse the trend. However, their trend is lower as compared to Conventional Banks.

IBIs Investments

Unfortunately, not much innovative work has been undertaken by IBIs in respect of their investment strategy. To our dismay, capital market in Pakistan is not a well developed one. However, the pattern of IBIs investment upto March 31, 2010 was: Federal Government Securities 37%, TFCs, Debentures, Bonds and PTCs 34%, fully paid up ordinary shares 3% aggregating to 74% and others represented 26%. One wonders, why they are investing in debentures which generally carries fixed rate of interest and is UnIslamic. The matter of investing in Federal Government Securities which also carries fixed rate of return also does not appear to fall, in our opinion, in accordance with Shariah. However, IBIs total investment (Rs. 73 billion) represented: available for sale 81%, held to maturity 16% and others 3%.

Inter-Bank Comparison

Total assets of IBIs in 2003 were 1% of the banking sector. This rose to 4% in 2007 and till March 2010 it was 6%. A comparison of deposits held also followed the same pattern. Net financing investment was also on the same pattern. All in all, our analysis of the data till March 2010 revealed that total assets were 6%, deposits were 5% and net-financing investment was 5% of the total banking industry of Pakistan

Performance Indicators of IBIs with total banking industry of Pakistan requires a very comprehensive and independent treatment. However, some analysis was undertaken and results have been included in this piece. IBIs showed better capital adequacy ratio as compared to banking industry and lower NPLs. However, room for improvement exists in earnings and profitability as compared to total banking industry in the areas of net income to total assets, return on equity, trading and exchange gain, operating expenses to gross income and spread between financing and deposits rates. These critical areas require careful attention of IBIs.

Conclusion

Future of IBIs augurs well in Pakistan. However, they have to go a long way. State Bank of Pakistan is requested to undertake a serious monitoring work and give a deadline to all Conventional Banks to switch to Islamic Banking so that the Constitutional obligation for eliminating **Riba** from the economy of the country is achieved.

Business Schools in Pakistan are urged to offer MBA in Islamic Banking. To begin with specialization in Islamic Banking may be offered and Human Resource side which is, at present is deficient, is properly addressed. An institutionalized system of producing Shariah Scholars to set up so that they can effectively play their role as Shariah Advisors. Innovation should attract investments through R&D so that new products are developed and Islamic Banking is popularized on for widespread basis throughout the country. We owe a lot to institutionalize Islamic Economic System in a broad framework with Islamic Banking as sub-set. Time is on our side and every is urged to demonstrate commitment to this mission. Allah, with His infinite wisdom will bless us with His favours.

*The writer is **Professor Emeritus and Principal**, Hailey College of Banking & Finance, University of the Punjab, Allama Iqbal Campus, Lahore. Contact Email: kamjadsaeed@yahoo.com