



The opportunities and challenges of Islamic banking in the Nigerian economy

Abubakar Muhammad Gidado

Lovely Professional University, Punjab, India

Abstract

Nigeria is the most populous country in Africa, with considerable number of Muslim population. Before the emergence of Islamic banking in Nigeria, the conventional banking system was the only medium of financial transactions, which survives on interest, breeds uncertainty and multiplies speculation, all for profit. Consequent upon economic turmoil and financial crisis in the Western European countries, which had its origin in the United States mortgage crisis in the late 2007, the Islamic system of banking and finance became the only option for the survival of financial system across the globe and Nigeria happened to be among other countries in the world adopting Islamic banking due to its suitability in despising interest and denouncing speculation, with emphasis on resource mobilization for active partnership with entrepreneurs and real sector operators of the economy. This paper therefore investigates the opportunities and challenges of Islamic Banking in Nigeria with a view to offer policy suggestions to the government. The objective of this study is to identify such opportunities and challenges with particular reference to JAIZ International Bank Plc. The study uses secondary data and adopts descriptive method to outline these challenges and determine their causative factors. The major findings of this study are: 1) religion, manpower and moral hazards significantly impaired the operations of Islamic bank: 2) competition with conventional banks is a major setback to Islamic banking in Nigeria. Despite challenges, Islamic banking in Nigeria offers a huge investment opportunities to domestic and foreign investors in Nigeria if all hands should be on deck to re-strengthen the capital base of the Islamic bank in the country. The paper therefore concludes with suggestions on serious measures to be taken to revitalize the Islamic banking in Nigeria.

Keywords: Islamic banking, shariah, opportunities and challenges, central bank of Nigeria, conventional banking

Introduction

Islamic Banking refers to a business of financial intermediation that is in line with the principles of Islamic jurisprudence of mobilizing savings from the general public on the basis of partnership and also advancing capital to entrepreneurship on the same basis within the purview of Islamic economics. The principles which emphasize moral and ethical values in all dealings have wide universal appeal. Shariah (Islamic jurisprudence) prohibits the payment or acceptance of interest charges (riba) for the lending and borrowing of money as well as carrying out trade and other activities that provide goods or services considered contrary to its principles. Islamic banks play a crucial role in the modern economy essentially by performing some important functions in society and significantly influence the distribution of income, the level of economic activity and even the level of cost in a country positively. The function of such financial institutions in economic development cannot be overemphasized considering the evidence from the current empirical studies, which suggest that broader, deeper, and better-functioning financial system can enhance higher economic development which is highly necessary and desirable for Muslim country's economics (INCEIF, 2006). In 2008, the Central Bank of Nigeria (CBN) asserted that the poverty has been a recurring problem in Nigeria since the 1980s. It declared that 70% of Nigeria's population of well over 150 million is not only unbanked, but also lives below the poverty line. In view of this, successive Nigerian

governments over the years have introduced different policies regarding financial inclusion that will facilitate access to finance for all in order to reduce the wide gap between the rich and poor. Unfortunately, the government's efforts in that respect have failed due mainly to low income level or lack of awareness about/or distance from where the services are available. For instance, the CBN long ago have presented microfinance banking in rural and urban settings to cater the needs of non-bankable Nigerians and promote financial inclusion, but still the system ended up being relentless with the problem of low patronage or participation particularly in the northern part of the country. The rejection may be owing to conventional interest based microfinance; its non-compliance with Islamic principles, especially the paying and receipt of interest (Riba), which is strongly prohibited under Islamic sharia law (Aliyu, 2013). The rise of Islamic banking in Nigeria rooted in 1991 with the promulgation of banks and other financial institutions Acts (BOFIA), which replaced the Banking Acts of 1969. In 1992, the central bank granted license for Habib Nigeria Bank Limited (former Bank PHB and now Keystone Bank plc.), to offer non-interest banking services on a "window basis." In addition, under the governorship of Charles Chukuwuma Soludo, the CBN joined the Islamic Development Bank (IDB) as a full member, and also the International Financial Services Board (IFSB) as a full member.

In 2005, the apex bank approved Jaiz Bank's request to establish noninterest banking. Also In 2008, some

conventional banks sought CBN license to run non-interest banking window. It is significant to note that by the time of this research the only full-fledged non-interest bank in Nigeria is Jaiz bank plc which was granted license on 11th November, 2011 to operate as an Islamic bank. On 6th January, 2012, the institution commences business with offices and branches in Kano, Kaduna and Abuja (Jaizbank.com).

Statement of the problem

The launching of Islamic Banking system in Nigeria has generated a lot of issues from some eminent Nigerians, asking the Governor of Central Bank of Nigeria to come and explain the reasons while such policy should be brought into Nigeria where there are different religions. The reason being that Nigeria is a multi-religious nation that is dominated by Muslims, Christians and religious activists. Moreover evidences from Quran and Bible kicked against usury which is the interest charged on borrowed fund. It is in the light of above that this paper focuses on this contemporary issues surrounding the operations of Islamic banking as in prospects and problems.

Purpose of the study

The purpose of the study is to examine the problems and prospects of Islamic Banking in Nigeria due to the recent debates on the issue. The study will equally look at the likely challenges based on the experiences of other nations that have been practising Islamic Banking.

Research Questions

1. Can Islamic banking be a solution to Nigeria economic problem?
2. Can Islamic banking eliminate shortcoming inherent in the conventional banking system?
3. Can Islamic banking accelerate the growth and development of small and medium scale enterprises (SME) in Nigeria?
4. Can the ethical restrictions embedded in Islamic banking increase our values?

Research Methods

The research method employed both primary secondary method of data collection that is the personal interviews from Islamic Scholars, Pastors and University students from various part of the country. The researcher equally made use of the public opinions of Nigerians on the issue.

Literature Review

The origin of the modern Islamic Bank can be traced to the very birth of Islam where the prophet himself acted as an agent for his wife's trading operations. Islamic partnerships (mudarabah) dominated the business world for centuries and the concept of interest found very little application in day-to-day transactions. However in this present life situation many studies have been conducted on challenges of Islamic banking in order to upgrade the establishment and operation of the institution. Mokhtar A. *et al* (2006) opined the idea of allowing conventional banking institutions to offer Islamic banking services by opening a window, separate branch or a subsidiary is expected to be the most effective means for

facilitating the growth and development of Islamic banking in Nigeria, because the policy is capable of increasing the number of institutions offering Islamic banking services at the lowest cost and within the shortest time frame. This model is not novel as it was practiced in many countries, such as Malaysia which adopted the model after a decade of introduction of the Islamic banking towards accelerated growth of the system,

However, most of these studies were focused on identifying the teaming challenges that surrounded the institution. Sanusi (2011) opined that the issues and challenges of Islamic banking in Nigeria and the challenges he outlined among others included lack of Shari'ah education in conventional economics and misconception of the system. Bello (2014) found that the operational challenges that may prevent the successful establishment and management of Islamic banking in Nigeria are religious and cultural differences, sharia related issues, and inadequate awareness. Momoh (2011), Umar (2011) and Ibrahim (2012) found that challenges to awareness, societal belief, socio-political environment, and religious misconception are some of the challenges of Islamic banking in Nigeria. Looking at the studies so far, it's clear that there is a need to find out the dimension in which misconception and religiously related issues can be a challenge to Islamic banking in Nigeria.

Shaikh Ziyaad Mahomed, CEO of Islamic Finance Institution of South Africa (FISA), opined that while conventional or interest-based banking focuses on the money itself to make more money by way of generating interest, non-conventional banking on the other hand focuses on investing the money in the system where people are actually working into to provide infrastructure, amenities and other services. He further contended that conventional banking is focused on the money itself, trying to make more money from the money, but Islamic banking focuses on trade. The major difference is that Islamic banking is based on investment and sharing of risks rather than intermediation or interest.

The perspective of Islamic banking or finance is based upon the productive use of money for growth of the economy and the benefit of the community. It is an asset based system of investment. The thrust of Islamic banking is the prohibition of taking and giving of interest in all form of banking and financial transaction. The Islamic form of financing promotes the profit-loss-sharing module instead of an assured return on loan amount by the interest rate in the conventional banking system. Mohammad, S., *et al* (2015) ^[14] opined that taking a risk is the only provision that entitles one to profit, if there is no risk of loss then there is no assurance of profit to the depositor or the financier. Therefore, profit should be made by means of either trade in tangible assets or on the basis of a profit-and-loss-sharing model.

Islamic Banking Principles

The Shariah prohibits the payment of charges for the renting of money (riba, which in the definition of Islamic scholars covers any excess of financial dealings, usury or interest) for specific terms as well as investing in business that provide goods or services considered contrary to its principles (Haram). While these principles were used as the basis for a flourishing economy in earlier times, it is only in the late 20th

Century that a number of Islamic-Banks were formed to apply these principles to private or semi-private commercial institutions within Muslim Community.

Islamic Banking outlawed riba. The universal nature of these principles is immediately apparent even at a cursory glance can non-Muslim literature. Usury was prohibited in both the old and the new testaments of the Bible (Deut 23¹⁹ and Ezekiel 18¹³)

A popular belief persists that Islamic Banking is simply an interest-free financial structure. Islamic economics is a complete system of social and economic justice. It deals with property rights, the incentive system, the allocation of resources, economic freedom and decision making and the proper role of government.

Religious challenges of Islamic banking in Nigeria

Basically the study has recognized that; religious challenges of Islamic banking can be categorized into two: the external and internal challenges in Nigeria.

The external challenges

This research has identified that the problems confronting Islamic banking in Nigeria are enormous and considerably serious as to look for their solutions. Although the problems on which the study has discussed are purely religious and are all along related to the rejection of the bank. These problems could well be regarded as 'Challenges'. Most of the significant challenges happen to be objections from some non-Muslim individuals and indeed their religious organization that denounce and stay away from the system for many grounds. These set of challenges are what has been termed as 'external challenges' due to its origin from non-Muslim refusal to accept the system as an alternative or at least as an additional mode of banking in Nigeria.

There have been a series of campaign against free-interest banking that are planned and organized by non-Muslim authorities to blackmail the introduction and operations of the Islamic banking system in Nigeria. This overzealous move started since the first license to start non-interest banking was granted. The anti-Islamic banking was tainted with religious sentiment to publicize their view through several news media critically with purpose to call against its survival and patronage. Looking at the benefits of Islamic banking to the economic development on one hand and its prohibition of interest on the other, non-Muslim should also partake in the services of Islamic banking in Nigeria despite the fact that the system was initially established for financial inclusion of mostly Muslims and that Muslims are obliged to abide by Shari'ah (Islamic Law) in all aspect of their life. It has been prescribed in Christian religious scriptures that usury/interest is never acceptable and should, therefore, be banned (Deuteronomy, 23:19 & Leviticus, 25:35-37).

The internal challenges

There are common criticisms of the concepts and practices of Islamic banking and lots of confusion about Islamic theory of finance among public and the intelligentsia. These include ordinary Muslims and indeed the highly recognized economists and experts among them. This is a category of challenges the study termed as internal because they are

emanating from within Islamic boundaries. While some accusations labeled against the Islamic financial institutions originated from few skeptics among scholars of Islamic finance, efforts should be needed to give convincing justifications.

Characteristics/attributes of Islamic banking

1. Islamic Banking is non-inflationary
2. Islamic Banking is entrepreneur driven
3. Islamic ethics transaction and social justice
4. Islamic Banking plays a vital role in economy's vision. That is the vision that moves away from debt based partnership to an equity based and stake taking partnership.
5. Islamic Banking believes in the principle of variable return (Profit and loss sharing) and depends on the actual productivity and performance of the projects.

Islamic prohibition of interest/western justification of interest

The Islamic law of prohibition of interest is not based on economic theory but on Divine Authority, which considered the charging of interest as an act of injustice. Islam recognizes that everything in the world has some usefulness, goodness or utility in them. Interest is therefore not seen as a different thing. Interest has some benefit but the harm it does is more than the benefit. The modern economists have developed many arguments to justify interest. One argument is that interest is the reward for saving, a compensation that the creditor pays the debtor for the latter's temporary loss of the use of capital. Another is that interest is the payment for the loss in value due to inflation. The goods the saving wants will cost more in the future so he is justified in charging a rent for the use of his loan.

Keynes (1883-1946) argued that money is the most liquid of assets that is to say, it is the asset most readily exchangeable for other forms of assets and that interest is the price paid for loss of liquidity. In order to be Islamic, the banking system has to avoid interest. Owing to this, much of the literature on the theory of Islamic Banking has grown out of a concern as to how the monetary and Banking System would function if interest were to be abolished by law.

Notwithstanding Islam not only prohibits dealing in interest and investment in unlawful activities that Islam deems harmful to society, but also transactions involving excessive uncertainty (gharar) and all forms of gambling (maysir).

Conclusion/Recommendation

Islamic banking in many countries of the world has been massively accepted and, therefore, recorded a considerable number of successes. In Nigeria, it is still evolving, and has actualized what can be described as a successful beginning. However, like any other country, Islamic banking is confronted with a number of challenges. These challenges are of various degrees. Asia and Middle East have passed the advocacy stage and deeply engaged in research and innovation. United States and other European government have already been working on promoting its application and developing the indices for accessing the performance of the industry.

However the study revealed that Islamic Banking if adopted in Nigeria will improve the economy of the country, accelerate the growth of SMEs, eliminate exploitation inherent in the conventional banking system, and increased societal values. It equally revealed that Islamic Banking will not islamitise Nigeria. In the words of Professor Akpan Ekpo, Director General, of West African Institute for Financial and Economic Management (WAIFEM) Islamic Banking policy does not prevent non-muslims from participating. It is another Banking technique that should join the existing operations in the industry so that anyone interested could participate.

Like every country, Nigeria has its related issues that directly or indirectly become a challenge to the industry. The religious challenges discussed in this paper are of two categories: Those that emanate from non-Muslim believers on one hand and that which are from within the boundaries of Islam on another hand. When non-Muslims misperceived the institution to be battling against their religious dogmas, some Muslims also misperceived it to be similar to the interest based system i.e. (not in line with the actual teachings of the Shari'ah). The mentioned challenges are regarded religious because of their direct linkage with religious belief. The study found out that factors that originally gave birth to those challenges include: the strong religious affiliation of Nigerians which made them be so emotional in any matters religion; politicization of religious and historic grudges between Islam and Christianity; North vs South politics; Ignorance about the effects of interest and finally lack of awareness. This paper strongly recommends that a sense of patriotism has to be created and put first in the peoples' hearts; looking at things in religious perspectives should also be discarded. It is only then that the sense of unity and everlasting friendship could be implanted in every society that will also give rooms for the needed growth and development. Religious authorities and organizations are to be called to order. Provocative statements and hasty release of comments on social media must be banned. Governments at all levels are urged to create a free relationship with the spiritual leaders and allow interactive sessions to share views and opinions. There should be a friendly collaboration between the stakeholders of Islamic banks and Christian religious clerics in Nigeria. Seminars, sensitizations, and workshops are to be frequently organized to disseminate the fundamental knowledge needed to understand the real meaning of free interest banking.

References

1. Aliyu SUR. Islamic banking and finance in Nigeria: issues, challenges, and opportunities. 2012.
2. The Bible Deut 23-19, Ezekiel, 18-13.
3. The Holy Quran. Q2 vs 275; Q2 Vs 219; Q4 vs 161, Q30 vs 39
4. Daud M, Yussof IM, Abideen A. The establishment and operation of Islamic Banks in Nigeria: Perception study on the role of the Central Bank of Nigeria. Australian Journal of Business and Management Research. 2011; 1(2).
5. Dogarawa AB. An Exploratory Study of the Economic Viability of and Opportunities for Islamic Banking in Nigeria. International Journal of Research in Management, Economics and Commerce. 2011; 2(1):1-16.
6. Clifford Obiyo O. Islamic financing/banking in the Nigerian economy: Is it workable? A review of related issues and prospects. International Journal of Islamic and Middle Eastern Finance and Management. 2008; 1(3): 227-234.
7. Ahmad MM, Pandey D. Are Islamic banks better immunized than Conventional banks in the current economic crisis? In 10th Global Conference on Business & Economics, 2010.
8. Onapajo H. Politics for God: Religion, politics and conflict in democratic Nigeria. The Journal of Pan African Studies. 2012; 4(9):42-66.
9. Ebhomienlen TO, Ukpebor EI. Religion and Politics in Nigeria: A Comparative Study of the Nigeria Supreme Council for Islamic Affairs and the Christian Association of Nigeria. Nienhaus, V. (1983). Profitability of Islamic PLS banks competing with interest banks: problems and prospects. Journal of research in Islamic Economics, 2012; 1(1):37-47.
10. Ebhomienlen TO, Ukpebor EI. Religion and Politics in Nigeria: A Comparative Study of the Nigeria Supreme Council for Islamic Affairs and the Christian Association of Nigeria. Kitause, R. H., & Achunike HC, 2013. Religion in Nigeria from. Research on Humanities and Social Sciences. 1900-2013; 3(18):45-56.
11. Olayemi AAM. The legality of Islamic banking in Nigeria: A critical approach. Available at SSRN 1941010. 2011.
12. Iqbal Z, Mirakhor A. An introduction to Islamic finance: Theory and practice (Vol. 687). John Wiley & Sons. 2011, 687.
13. Moktar SHA, Abdullah N, Al-Habshi SM. Efficiency of Islamic Banking in Malaysia: A Stochastic Frontier Approach, Journal of Economic Cooperation. 2006; 27: 37-70.
14. Mohammad S, *et al.* Enhancing Cross Border Connectivity: Venturing into Islamic Finance as a New Source of Infrastructure Financing, Journal of Emerging Economies and Islamic Research. 2015; 3(3). www.jeeir.com
15. Ojo-Agbody AA, Omah I. Islamic banking in Nigeria: Problems and prospects. International Journals of Marketing and Technology. 2012; 2(7):1-10.