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**Islamic Banking Performance in the Middle East:
A Case Study of Jordan**

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Abstract

Islamic banking in Jordan started around two decades ago. Since then it has played an important role in financing and contributing to different economics and social sectors in the country in compliance with the principles of Shariah rules in Islamic banking practices. Since there have been limited studies on the financial performance of Islamic banks in the country. The aim of this paper is to examine and analyse the Jordanian experience with Islamic banking, and in particular the experience for the first and second Islamic bank in the country, Jordan Islamic Bank for Finance and Investment (JIBFI), and Islamic International Arab Bank (IIAB) in order to evaluate the Islamic banks' performance in the county. The paper goes further to shed some light on the domestic as well as global challenges, which are facing this sector. However, this paper used the performance evaluation methodology by conducting the profit maximization, capital structure, and liquidity tests. This paper found that the efficiency and ability of both banks has increased and both have expanded their investment and activities and had played an important role in financing projects in Jordan. Another interesting finding of the paper that these banks have focused on the short-term investment, perhaps this seems to be the case in most Islamic banking practices. Another finding is that the Bank for Finance and Investment (JIBFI) has a high profitability that encourages other banks to practice the Islamic financial system. The paper also found that Islamic banks have a high growth in the credit facilities and in profitability.

Keywords: Islamic banking, Performance, Efficiency, Challenges, Jordan

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1. Introduction

Islamic bank is a financial and social institution whose aims, principles as well as practices must comply with the Islamic Shariah rules and which must avoid the interest in any of its practices (Ahmed, 2004). However, it is worth noting here that the desirability of abolishing fixed interest rates and the Islamization of financial systems was a main discussions at the first meeting of the Islamic Organization Conference (IOC) in Jeddah in 1973 (Haqiqi and Pomeranz, 2005), many Islamic banks were founded under the profit and loss sharing system (PLS). It is worth noting here that Modern Islamic banking has undergone through three phases of development:

1. The period of 1972-1975. This period was associated with a surge in oil revenues and great liquidity. During that time many important events have occurred including the establishment of IOC and launched of Dubai Islamic bank in mid 1970s.
2. The period of 1976 to the early 1980s: the Islamic banking during to this period spread from the Gulf countries to Malaysia and westward to England. During this period many international and intercontinental institutions were established. For example Islamic banking associations, and consultant bodies to expand their operations.
3. The period of 1983- to the present or maturity period of Islamic banks. The Arab countries were confronted by economic setbacks, for example slowdowns in oil revenue (oil shocks during the early 1980s), the relative strength of the U.S. dollar, high interest rates in the U.S., and capital outflow from OPEC countries. It is worth noting here that during this period many Arab banks have been opened branches in the U.S., Europe, Asia, and other part of the world. In courtiers like Iran, Bahrain, and Sudan, the operations of the entire banking system have been converted to the Islamic mode of finance.

Hence, Islamic banking is growing in number and size all over the globe. According to some estimates Islamic banking has grown at an annual rate of 15% over the past five years. Currently there are over 250 institutions managing assets and client money around US\$400 billion (AME Info, 2005). The growth of these banks is proof of their success. It is worth noting here that we should never forget that Islamic banks are part of the banking system in the countries in which they operate and are subject to the same rules and regulations.

However, with the continual growth of Islamic banking in the Arab and Middle East world, the concept has also engaged Jordan because it has open society, experience and active banking and finance sector, number of reforms has initiated to the banking sector during 1980s to strengthen the sector. But the most important factor, which assists Jordan to engage in Islamic banking, is that the majority of the population (around 6 million) are

Muslim (92%), most of whom are keen and interest to obtain competitive financial services that meet their beliefs. Hence, the country was in a good position and ready to adopt Islamic banking concept and develop it further to its full potential.

The Islamic banking in Jordan started around two decades ago with the foundation of its first Islamic bank that is Jordan Islamic bank for finance investment in 1978, since then the Islamic banks in the country have grown in number and size with the establishment of more branches and more Islamic banks such as Islamic International Arab bank and the establishment of other Islamic institutions such as Jordan Islamic Insurance, Islamic Investment House and Jordan Finance House.

Hence, since there have been limited studies in the case of Islamic banking performance in Jordan, the objective of this paper is to examine and analyse the Jordanian experience in Islamic banking by evaluating the performance of Islamic banks in the country which have been operating since the last two decades. Nevertheless, the paper shed 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. The paper also reviews some of the changes (domestic and global), which are facing this sector. However, this paper is organized as follows. Section 2 provides an overview as well as the development of banking industry and Islamic banking in Jordan. Section 3 reports the methodology and the tools for measuring bank performance; results and analysis are also reported in this section. Section 4 highlights the challenges as well as the prospects of Islamic banking in Jordan. Summary and conclusion are discussed in section 5.

2. Banking and Islamic Finance in Jordan

The banking system in Jordan was dominated by the Central Bank and Amman Financial Market. The central Bank established in 1964, was responsible 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 1970s and the early 1980s has seen more than doubles loans and deposits. During this period the number of financial institutions tripled as the government encouraged the expansion of banking services as a key driver to its economic development policy. Deposits were attracted from other Arab countries, and the savings and remittances were also captured. These deposits were used as loans to growing companies that needed capital.

Furthermore, during the 1980s Jordan was the only Arab country in which the value of bank assets exceeded GDP. Commercial bank assets have risen from JD1.1 million in 1980 to JD2.3 billion in 1985. Total deposits as well increased from about JD800 million to JD1.7 billion. Strict Central bank consumer credit controls and government success in encouraging savings was resulted in a growth of 7% per year 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 cautious that the banking sector in the country was expanding rapidly. Because the greater concern of the

government was during that time that the banks could involve in risky lending activity and excessive competition for assets and could lend to foreign companies instead of locale one. As a result the Central bank of Jordan 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).

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

It is worth noting here that in the late 1980s, thirty 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 specialised 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 including 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 Bank left Jordan following the 1984 government imposed financial regulations (JIR, 2005).

Moreover, it is worth noting here that the Central Bank of Jordan since 1989 has initiated a number of reforms to make the banking system more secure and complete as follows:

1. Paid up capital of Jordanian banks increased paid up to JD 20 million
2. Paid up capital of foreign banks increased to JD 10 million
3. Banks are required to hold 80% of required reserves at the CBJ
4. Restrictions on the inter-bank foreign exchange market were lifted during 1996.
5. Restrictions on the flow of trade in foreign currency were removed during 1997.
6. Main restrictions on foreing caopital were removed during 1997 (JIB, 2005).
7. Recently during 1999-2002 more reforms have been undertaken to enhance the sector such as the new banking law, new securities law, new auditing profession law, among others (Khamis, 2003).

However, recently the numbers of banks operating in Jordan rose to twenty four banks at the end of 2004, of whom fourteen are 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) branches, of which 52

branches are operating in Palestine in addition to ten representative offices (Central Bank of Jordan, 2004). In addition to that, it is worth noting here that Amman Stock Exchange (ASE) was established in 1976, considered to be the most efficient stock exchanges in the Arab World, as well as the largest and fastest growing markets in the region opens to investors. The ASE is one of the few Middle East and North African countries (MENA) markets, which engaged 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, and among others (JIB, 2005).

2.1 Islamic Banking in Jordan

As indicated earlier that Islamic banking in Jordan has been operating for around 2 decades. As indicated earlier that Islamic banks paid no interest on deposits, and collected no interest on loans. Instead, they made equity investments in companies and then shared in the venture's profit or loss, some of which would then passed on the depositors. Currently there are two Islamic banks listed in the Amman Stock Exchange (ASE) (Jordan Islamic Bank for Finance and Investment and Islamic international Arab bank PLC).

2.1.1 Jordan Islamic Bank for Finance and Investment

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 Islamic Shariah law. Since its establishments the bank succeeded in achieving growth (Table 1) and in establishing itself as one of the leading banks in Jordan by providing all kinds and investment activities.

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

The Bank plays an effective role in developing the economic and social activities as evidence by the growing number of people to deposit their savings with the bank, and channelling these deposits towards investment and creating jobs. The number of people who benefited from interest free loans reached about 144,000, and the total loans granted to them amounted to JD 51.1 million. Furthermore, with the objective of the bank to

increase its presence in the country to reach all citizens who is interested to use Islamic banking products (such as Mudaraba, Musharka, Murabaha etc), the bank has increased its network, which comprised of 52 branches and 12 cash offices. It is worth noting here that the number of accounts opened with the bank through its network, has reached 997,000 accounts, the number of the bank's employees has reached 1418 in 2004. Furthermore, the Bank has been successful in establishing correspondent relations with more than 300 international banks (JIBFI, Annual Report, 2004).

2.1.2 Islamic International Arab Bank

The Islamic International Arab Bank (IIAB) is the second bank in Jordan to operate according to Islamic Shariah. It began its operations in February 1998 with four branches in Jordan. The bank is offering a complete set of Islamic banking, financing and correspondence services. The Islamic international Arab Bank aims to cover economical and social needs within the banking sector, in accordance with the Islamic banking Shariah rules. The Islamic International Arab Bank is now ranked as the fourth bank in Jordan with a paid-up capital, which amounts to 40,000,000 Jordanian Dinars². The total number of Islamic International Arab Bank employees by the end of 2002 reached 217, compared with 207 by the end of 2001. The numbers of branches are 11 around the kingdom. Table 2 summarizes the banks aggregate during the period 1998-2003 (IIAB, 2002).

Table 2: Islamic International Arab Bank plc 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

3. Methodology and Performance Analysis of Islamic Banks in Jordan

According to the financial management theory banks' performance can be evaluated by using many financial ratios, for example profitability ratios, liquidity ratios, among other ratios. For example Patnam (1983), Sabi (1996) and Samad (1999), among others have used many financial ratios to evaluate or analyze the bank's performance. However, in the context of this study, and in order to examine the performance of Islamic banking in

² Every 1 JD equal \$1.429 US dollar.

Jordan, “Banking Efficiency Model” will be taken into consideration to measure the bank’s performance. Due to an unavailability of long period time series data for Islamic International Arab Bank (IIAB), this study is limited only to four years time series data. But nevertheless this study is important since there have been no studies on the development of Islamic banks in Jordan.

Hence, 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 main objective of Banks and any institutions is to maximize profits. Without making profits firms are unable to continue work and develop services. On the other hand, Islamic banks have also other objectives besides making or maximizing profits; their aim is to achieve economic and social welfare and to ensure that there is no exploitation of the customers.

3.1 Profit Maximization Test

Eight indicators of profitability and performance are taken to evaluate the bank performance (see Table 3 and Table 4).

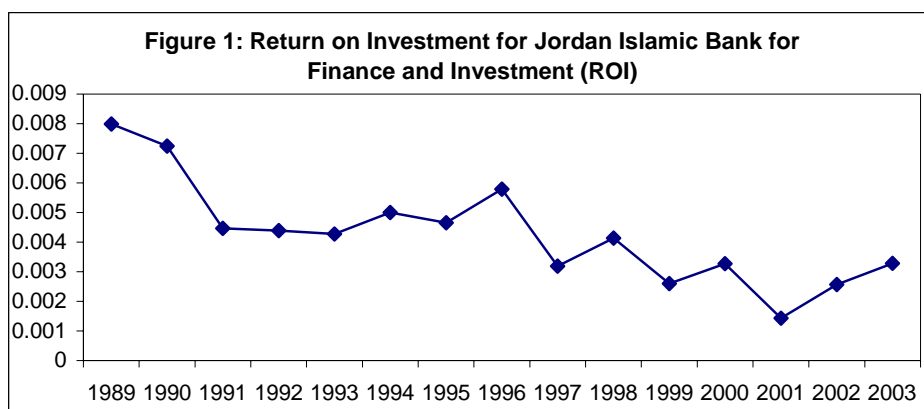
Table 3: Profitability and Performance for Jordan Islamic Bank for Finance and Investment

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 Interest and Commissions Income/Operational Income%	88.41	86.31	90.37	87.44
Credit Interest / 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 + Interest in Suspense) / Credit Facilities%	9.95	10.65	11.01	6.86
Net income/total liabilities	0.36	0.16	0.28	0.35

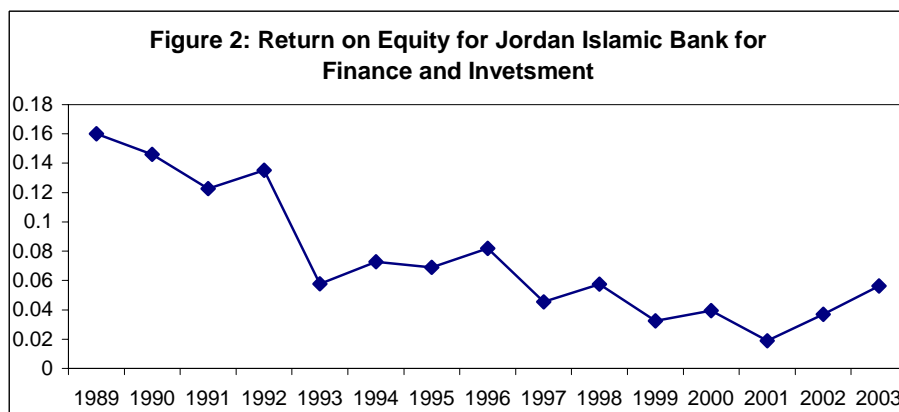
Table 4: Profitability and Performance for Islamic international Arab bank PLC

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 Interest and Commissions Income/Operational Income%	33.43	44.21	62.50	60.20
Credit Interest / 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 + Interest in Suspense) / Credit Facilities%	1.43	1.48	1.40	1.51
Net Income/Total Liabilities	2.06	1.39	0.68	0.59

Table 3 and Table 4 show that both measures of performance ROA and ROE have a positive sign in both banks. Both measures of performance are higher in Islamic International Arab Bank in all years compared with the Islamic Bank for Finance and investment. The ROA in 2000 is 0.33% in Jordan Islamic Bank for Finance and Investment compared with 1.59% in Islamic International Arab Bank. Figure 1 and 2 show the ROI and ROE for Jordan Islamic Bank for Finance and Investment from 1989-2003. It seems that the bank ROI is decreased during 1991, 1997, 1999, 2001, and 2002. The decrease during the years 1999, 2001 and 2002 could be as a result of competition between the two Islamic banks while the decreasing during 1991 could be as a result of Gulf War one.

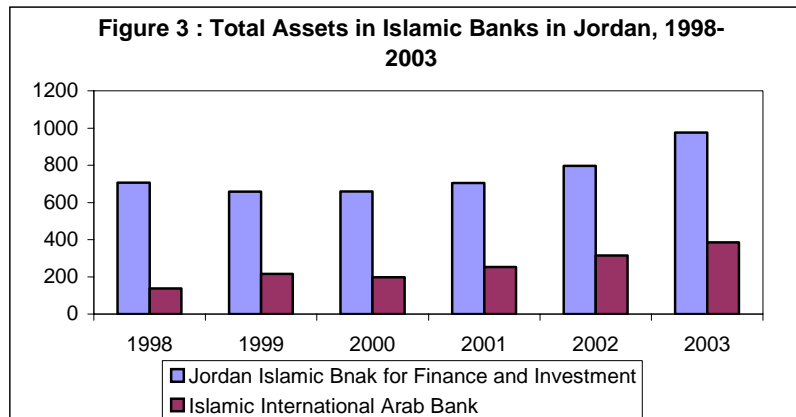


Source: Amman stock Exchange and JIBFI



Source: Amman stock Exchange and JIBFI

The bank performance measure ROA is decreased in both banks in 2001 and increased in both banks in 2002 and 2003, but ROA is still higher in Islamic International Arab Bank than in Islamic Bank for Finance and Banking.



Source: Amman Stock Exchange

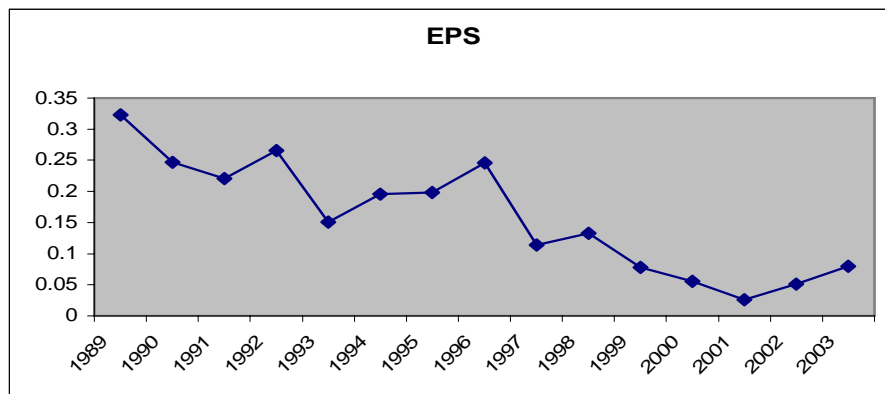
Figure 3 shows that the total assets in the Islamic bank for finance and investment is more than the total assets in the Islamic international Arab bank in about 461.856 millions in 2000 and 589,961 millions in 2003. Also, the total shareholders equity in Islamic Bank for finance and investment is greater than the total shareholders equity in Islamic international Arab bank in about 9.352 million compared with 8.065 millions in 2003 (See Figure 3).

Furthermore, other measures of performance are calculated to measure the performance taking into account the facilities and liabilities. Net Interest and Commissions Income/Operational Income in 2000 is 88.41% in Jordan Islamic bank for finance compared with 33.43% in the Islamic International Arab Bank. This ratio increased in both banks in 2002 and is still very high in Jordan Islamic bank for finance 87.44% in 2003 compared with 60.20 % for the Islamic international Arab bank. This ratio shows that the Islamic International bank increased its interest and commissions income, which indicates that the bank expanded its activities in at a higher rate. Credit Interest / Credit Facilities, Net, Net Income / Total Revenues, and Total Revenues / Total Assets are also calculated for both banks. Both ratios Credit Interest / Credit Facilities, and Total Revenues / Total Assets are higher in Jordan Islamic Bank for finance and investment compared with the Islamic international Arab bank ratios (see Table3 and Table 4). For example, the ratio of credit interest / credit facilities in Jordan Islamic bank for finance and investment is 11.89% in 2000 compared with 8.95% for the Islamic international Arab bank.

The Net Income / Total Revenues ratio is 6.38% in 2000 in Jordan Islamic Bank for finance and investment compared with 32.03% in Islamic international Arab bank. While, this ratio increased in 2003 reaching 7.95% in Jordan Islamic Bank for finance and investment it decreased in Islamic International Arab bank to reach 19.30% and this could

be as a result of increasing the administration expense resulting from expansion and opening of new branches.

Another ratio is calculated the (Provision for Credit Facilities + Interest in Suspense) / Credit Facilities ratio is very high in Jordan Islamic Bank for Finance and investment compared with the same ratio in Islamic international Arab bank. For example, the (Provision for Credit Facilities + Interest in Suspense) / Credit Facilities ratio is 6.86% in 2003 for Jordan Islamic bank compared with 1.51% for Islamic international Arab bank. Furthermore, Net Income/Total Liabilities is lower for Jordan Islamic bank compared with Islamic international Arab bank. Another measure of performance that used to evaluate the bank performance is the bank earning per share (EPS). Figure 4 shows that this ratio for the Jordan Islamic Bank for finance and Investment decreased during the last 6 years. The performance measures show the ability and the efficiency of both the Islamic banks to increase its income and decrease its expenses.



Source: Amman stock Exchange

3.2 Capital Structure

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

Table 5: Jordan Islamic Bank for Finance and Investment Capital Structure

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

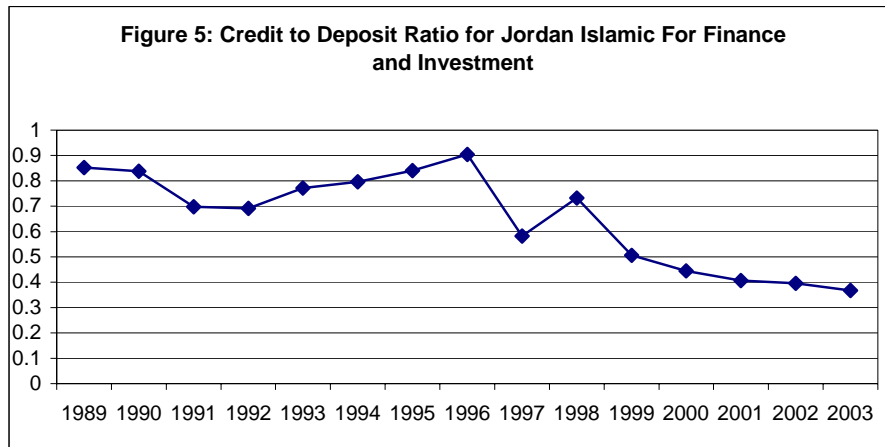
Table 6: Capital structure for Islamic international Arab Bank

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

Table 5 and Table 6 show ten ratios to measure the capital structure of the Islamic banks. The equity ratio reflects the total equity/ total assets. The equity ratio decreased to 5.84% in 2003 compared with 8.28% in 2000 for the Jordan Islamic Bank for Finance and Investment. The equity ratio also declined to 12.69% in 2003 compared with 22.93% in 2000. The lower amount of equity ratio for Jordan Islamic Bank for Finance and Investment reflects the expansion of this bank in total assets. On the other hand, the higher equity ratio in Islamic international Arab bank indicates that the bank is expanding its investments. The shareholders equity/total deposits reflect the percentage of total equity to total deposit. The Shareholders Equity / Total Deposits decreased from 9.59% in 2000 to 6.46 % for the Jordan Islamic Bank for Finance and Investment. Also this ratio is decreased from 31.47% in 2000 to 15.29% in 2003 for Islamic international Arab bank. The decrease in this ratio reflects the increase in customers' deposits. As we can see from the table the Islamic international Arab bank increased the deposits from the years 2000 until 2003 at a higher rate.

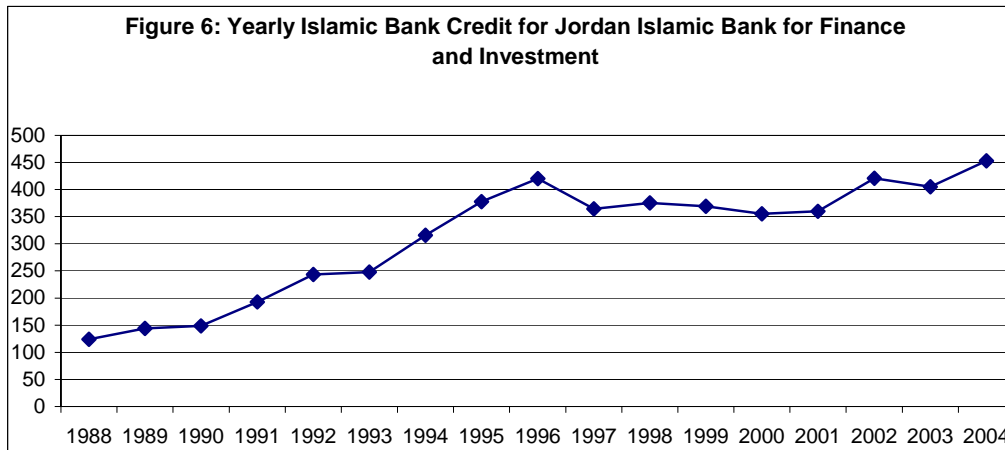
The debt ratio in both banks is very high as a result of high percentage of customer deposits and because the bank depends on customer deposits to lend money. For example, the debt ratio is increased from 91.72 % in 2000 to 94.16% in 2003 for the Jordan Islamic Bank for Finance and Investment, and also increased from 77.07% in 2000 to 87.31% in

2003 for the Islamic international Arab bank. As shown in Tables 5 and 6 show that both banks increased their debt ratio. The results in the previous ratio are explained by the ratio of Total Deposits / Total Assets ratio. This ratio shows the growth of the banks deposits in both banks. Both ratios, Net Credit Facilities to Total Assets and Net Credit Facilities to Total Deposits for the Jordan Islamic Bank for Finance and Investment are decreased in 2003 in comparison with 2000, 2001, and 2002. Both ratios increased in the case of the Islamic international Arab bank in 2003 (see Tables 5 and 6).



Source: Amman stock Exchange, Annual Reports

Another ratio that shows that Jordan Islamic Bank for Finance and Investment increase their lending activities more than the Islamic international Arab bank is the Shareholders Equity to Credit Facilities. For example, shareholders Equity to Credit Facilities are 17.70% and 21.73% in 2003 and 2000 respectively for Jordan Islamic Bank for Finance and Investment, while it is 39.88% and 81.88% in 2003 and 2000 respectively. The results also reflect that the Islamic international Arab bank facilities growing at a higher rate. Figure 5 indicates that the credit to deposits ratio decreased in the last five years for the Jordan Islamic Bank for Finance and Investment. The decrease in this ratio could be as a result of a higher increase in the deposits compared with low increase in credit. Figure 6 show the yearly credit issued by Jordan Islamic Bank for Finance and Investment increased from 1989 to 2004. The credit facilities are in an increasing function during the last 15 years. The increase in the credit facilities reflects the bank growth in credit in the Jordanian market.



Source: Central Bank of Jordan

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

Another measure of capital structure is the total debt/total equity. Table 5 and Table 6 show that total liabilities/total assets ratio increased for both banks. The main reason for this increase in this ratio resulted from the increases of the customer deposits in a high percentage. The total debt/ total equity is 1,611.91% for Jordan Islamic bank for finance and investment in 2003 compared with 688.12% in 2003 for the Islamic international Arab Bank. This indicates that the bank increased its activities and is growing in the market. This ratio increased more than 100% in the Islamic international Arab Bank, meaning that the bank expand its activities and growth in deposit.

3.3 Liquidity Measures

Liquidity management ensures the Bank's ability to meet its short-term and long -term funding commitments while achieving the optimal return on investment. The liquidity position of the Bank, as well as strategies and adjustment of policies are an important aspect that affect the bank position and ability to expand and issued loan, and expand in investment activities. Liquidity analysis at different levels includes a maturities analysis of assets and liabilities are important for banks to be sure about the liquidity of the bank. It also includes an analysis of the source and use of funds.

As discussed earlier, the capital structure of Islamic banks become stronger and more dependent on short term investment rather than long term investment in both banks. The structure of its capital affects the liquidity risk. To evaluate the bank liquidity risk and its

ability to pay its obligations three measures of liquidity are taken. Table 7 and Table 8 summarize these ratios in both banks. Jordan Islamic Bank for Finance and Investment increased its quick ratio in 2003 to 0.56% compared with 0.46% in 2000. The quick ratio in the Islamic international Arab bank is higher, which is 0.60% in 2003 and 0.66% in 2000. The other ratio is the cash and investments to total deposits; this ratio is nearly close to 65% in both banks in 2003. The increase indicates that there is a growing rate of lending facilities. Furthermore, this ratio reflects the banks' ability to cover loans from assets as well as to face the instant demand for deposits. Both banks have the ability to meet the instant demand for money. Another ratio that measures the liquidity is (Cash + Trading Investments)/ Total Deposits. This ratio in Islamic international Arab bank is higher than in Jordan Islamic Bank for Finance and Investment.

Table 7: Table bank liquidity Jordan Islamic Bank for Finance and Investment

Liquidity ratios	2000	2001	2002	2003
Quick Ratio (Times)	0.46	0.46	0.45	0.56
Cash & Investments to 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: Islamic international Arab bank PLC

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

4. Challenges and Prospects of Islamic Banking

As indicated earlier, that the Islamic banking industry is growing in number and size as the country has an open society, active and one of the most experienced banking sectors in the Arabic region. The country's majority muslim population, most of whom are professionals and businessmen, whom are keen to obtain competitive financial services that meet their beliefs. All these factors have created a good environment for the country to be engaged in Islamic banking concepts for the last two decades.

Islamic banks in Jordan have a great potential to grow positively in the coming years as they are focusing on many strategies to attract more customers from Muslim as well as non Muslim through enhancing their market activities to increase the awareness of the banking services, strengthening the relationship with the customers. In other words, Islamic banks in Jordan are trying to build a good and long relationship between the Islamic banking products 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 the September 11 event. As indicated before, for example this will naturally induce 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 many elements of the Islamic products (see

Table 9) such as Musharaka, Mudaraba, Murabaha Istisn'a, or Mudaraba, among many others. For example, Table 10 indicates the case of Islamic International Arab Bank and its contribution to various sectors in the economy such as Industry and Mining, Agriculture, construction, trade, and among others. Where most of these sectors are in an urgent needs for finance, thus Islamic banks play an important role in financing of business operation and improve their business performance and create jobs in the labour market. Furthermore, this is as well the case of other Islamic banks in the country, as shown in Table 11 that Jordan Islamic Bank plays as well an important role and committed to its social role. For example continue its program for financing small-scale industries. And since the start of this program, the bank has financed close to 40 projects with a cumulative cost of about JD 700,500 (JIBFI, 2003). Moreover, Table 11 shows the bank's contribution to different sectors of the Jordanian economy and covers a wide range of social activities and utilities including hospitals, medical clinics, education sectors, transports and many others. According to classification of the Central banks, the contribution of the bank in these activities reported as shown in Table 11.

Table 9 The Elements of the Financing and Investment Portfolio (Case of Islamic International Bank)

	1999	2000	2001	2002
Murabaha	16,711,772	29,314,743	49,087,017	46,274,243
Mudaraba	279,366	1,311,785	1,052,426	2,905,134
Musharka	---	325,284	626,993	605,132
Istisn'a	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 (Case of Islamic International Bank)

	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 Jordan Islamic Bank in various economic sectors 2002-2003, (in thousand JD)

Sectors	2002	2003
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)

Moreover, Islamic banks in Jordan has the potential to increase its customer base to cover most geographical parts in Jordan by opening new branches and offices in order to be nearby the current as well as the potential customers. They are working hard to achieve their goals despite the strong local and the difficult circumstances facing this sector. Even though, the bank has the potential to grow further and to enhance development among the production sectors in the country as evidenced by the bank's performance and its strategies. Among the strategies which the Islamic banks are looking for in Jordan, maintaining the strength of the Banks' financial position; increasing the Islamic banks market share, optimising the profits of shareholders and depositors, increasing the ethical values and performance standards, among other strategies. Hence, the Islamic banks in Jordan are trying to adopt all the necessary needs and other means to achieve their goals by increasing their customer base, increasing the awareness of the Islamic banking products, adopting all the new financial and investment tools, adopting IT to provide the best for its customers, training for its employees and all other means which are important for the bank's development and performance. Hence, Islamic banks in Jordan have good support from both the public as well as the private sectors. Therefore, these banks have good potential to succeed by providing distinguished banking and investment services that satisfy government and private institutions as well as individuals. This 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 good plan for the future, nevertheless these banks are also facing some key challenges domestically as well as globally that reduce their growth potential. Among the challenges are the conflicting situation in the region (e.g. political status in Palestine and other part of Middle East), the economic slowdown which has plagued the country for the past few years, globalisation (e.g. abolition of tax barriers, liberalisation of commodity and services etc), increased cash surpluses with limited finance and investment opportunities (IIAB, 2002), public awareness and acceptance, lack of institutions which conduct research and development to in this area, lack of skilled and professional people, and local competition from large numbers of commercial banks that are operating in the country.

Islamic banking globally faces also many challenges. Saleh and Zeitun (2005) have identified many challenges that are facing Islamic banking industry in the case of Lebanon such as public awareness and acceptance; high competition from many conventional

banks; lack of talented man power and among others. Globally Islamic banking faces as well ,many challenges such as financial globalisation, speculation, the flow of savings abroad, competition from international banks (AME, 2005), lack of inter-bank Islamic money market and Islamic money brokers, investors are unwilling to hold to maturity Islamic paper with a long term nature, different interpretation by Islamic scholars in different countries (AME, 2005), banks faced problems when their readiness to meet global competition (due to their limited capital and asset base) and shortage of skilled and training Manpower in Islamic banking industry, Defaulting culture of the borrowers, lack of Harmonization of Islamic financial practices, confusion about what is acceptable practice in Islamic banking industry and many other challenges (Sarker, 1999; Saleh and Zeitun, 2005). Further, Islamic banking has to concentrate on risk management and product innovation; the issue of human capital needs greater attention, and development to meet the requirements of more diversified business activities.

5. Conclusion

While Islamic banks in Jordan have been in existence for the last two decades, there have been limited studies on the financial performance of Islamic banks in the country. Thus, to fill this gap, the paper has analysed and evaluated the Jordanian experience with Islamic banking in order to determine the Islamic banks' performance as well as its activities. The paper went further than that to review the domestic as well as global challenges which 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 the performance measures of both banks (IIAB and JIBFI) showed that the efficiency and the ability of both banks has increased and both banks have expanded its investment and activities and playing an important role in financing important projects in the market. Among other findings, these Islamic banks have a high growth in the credit facilities and in the profitability. Another interesting finding of the paper that these Islamic banks have focused on the sort-term investment rather than the long run investment, perhaps this seems to be the case in most Islamic banking practices where the capital structure become stronger and depend on short term investment. In comparison with the two banks, the results showed that Jordan Islamic Bank for Finance and Investment has increased their lending activities more that the Islamic International Arab bank and the facilities of the latter is growing as well at a higher rate. The results show also that the Islamic bank for Finance and Investment has a high profitability that encourages other banks to practice the financial Islamic products.

The review in this paper also indicates that 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 among other. Most of these sectors are in an urgent needs for finance, thus Islamic banks committed to its social role and play an important role in financing of business operation and improve their business performance and create jobs in the labour market. Furthermore, the paper also shed some light on the development of Islamic banking globally and this sector has grown not only in the Muslim world, but also has gained significant attention in the Western world as well,

with over 250 Islamic banks worldwide and managing assets and client money around US\$ 400 billion. Hence, the growth of these banks is proof of their success and an indication that these banks continue to grow in number and size worldwide.

The review of the issue of challenges which are facing Islamic banks in Jordan suggest that these banks are facing many challenges among them the conflicting situation in the region, the economic slowdown which has plagued the country for the past few years, globalisation, increased cash surpluses with limited finance and investment opportunities, public awareness and acceptance, lack of institutions which conduct research and development to 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 could emerge as a major financial institutions in the region. However, in order to ensure continuous success, Islamic banks needs to have good corporate governance, invest in IT and innovation in order to increase their competitiveness. They should adopt more strategies to promote their products and establishing long-term relationship 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 those products. Therefore, Islamic banks have to work more to brand their products and to build a good relationship between the customers and Islamic banks.

The management of the Islamic banks also has to 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 centers, institutions which conduct research and development to improve the work of Islamic banks.

More importantly, Jordan should collaborate with other countries which are leading in this concept such as Dubai, Bahrain, Malaysia and among others in order to exchange ideas, knowledge and work on issues such as application of universal banking, crisis management, developing an Islamic financial market (especially for medium and long term products) as well as developing the securitisation process, Shariah harmonization, products standardization and application of Shariah compliant products in order to eliminate confusion and develop a more comprehensive Islamic banking system. Nevertheless these banks should always be ready to adopt and enhance IT and skills to maintain efficiency and productivity, to be customer oriented, innovative in terms of products to meet the requirements of more diversified business activities.

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