

Islamic Banks

Technology and Global Challenges and Opportunities

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ABSTRACT

Islamic banks that are growing quickly have achieved a prominent status in the banking industry today, but still have to accelerate their efforts to meet the technology and global challenges that they are likely to face. It is fitting for Islamic banks to focus their developments not only on retail banking but also on diversifying their banking and financial products. They must search out longer-term investment products such as Islamic equity instruments, bonds, and leases to meet Islamic investors' needs and the long-term financing needs of customers. Conventional banks have recently introduced an increasing number of Islamic products. This reflects growing customer demand for these products and reveals a spirit of cooperation between conventional and Islamic banks. While such cooperation needs to be further cultivated and strengthened, it would at the same time impose competitive pressure on Islamic banks, which would be one of its major challenges.

I. INTRODUCTION

In 15 years, the Islamic banking market has grown to approximately \$100 billion. This market is growing today at between 10% to 15% a year. Our projections suggest that the demand for Islamic financial services will continue to grow in the next 10 years.

During this period major improvement occurred in the business practices of Islamic banks both in the quality of provided service and investment activities. It is evident to economists and bankers that these banks were able to achieve a prominent status among international banks. This achievement should prompt Islamic banks to accelerate their efforts for the development and improvement and the observation standards of quality in response to the dynamic, rapidly evolving investment and finance environment. Islamic banks should thus consider certain approaches to meet the global and technological challenges of the future in order to benefit from the substantial opportunities that exist there for them.

II. ISLAMIC BANKS AND INTERNATIONAL FINANCIAL MARKET TRENDS

In the past, Islamic banking appeared to concentrate on retail banking, to meet the immediate needs of retail customers seeking an alternative to conventional banking. Over time, however, Islamic investors and customers grew more sophisticated and looked for Islamic financial instruments.

It is fitting that Islamic banks develop not only on retail banking but also diversify their banking and financial products into the areas of wholesale and investment. The challenge here is the lack of Islamic instruments in the market. Cooperation and coordination among *shari'ah* authorities and Islamic bankers should thus be strengthened and a common scientific base for collective cooperation (*ijtihad*) established in order to develop Islamic banking products and investment instruments and the Islamization of instruments used in the international financial markets. For instance, Islamic banks will need to acquire and develop the necessary investment banking and fund management skills. They will also need to search out longer term investment projects such as Islamic equity, bonds and leases to achieve the Islamic investors' liquidity needs and the longer-term financing needs of borrowers.

Recently, conventional banks have introduced an increasing number of Islamic products. This is, of course, due to the increasing demand for these products. Some conventional banks find it profitable to deal with Islamic investment funds such as asset-leasing funds and share-dealing funds. This trend supports our view that we will see continuing expansion and growth in the relationship between Islamic and conventional banks.

In addition, some conventional banks are trying to improve the management of these funds so as to compete with the Islamic banks here. Islamic banks should benefit from this by using the experience of these

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conventional banks. This can be achieved through the exchange of expertise between conventional and Islamic banks.

Finally it must be stressed that Islamic and conventional banks should move from competition to cooperation. This will lead to a healthy environment that is in the interest of their customers and shareholders. The Islamic and the conventional banks will expand their Islamic activities and have much to offer to each other in the exchange of skills and knowledge and in identifying joint ventures and shared opportunities for syndication.

III. ISLAMIC BANKS AND GLOBALIZATION

Though globalization ranks high on the list of overused words in the banking business, it is an important trend that requires preparation. Globalization is associated with growing interconnections among financial institutions, facilitated largely by advances in communications and computer technology. Capital moves across national borders primarily as investment flows and secondarily as international trade financing.

The increasing volume of financial transactions and their decreasing costs have put strong competitive pressures on institutions to change the ways in which they operate. Automation of trading includes a number of innovations that have improved the efficiency of financial transactions.

Islamic banks, in order to survive and develop, must cope with these developments. There are many challenges that are imposed by globalization on the banking industry, some of which relate to institutional capacity for self-development in methods and organizations and in providing banking and financial services that can compete and survive. Technology is another challenge. Islamic banks are competing in a highly developed technological market that utilizes a wide range of sophisticated banking products. The problem is not only in the adoption of technology but in the preparation of a suitable environment that will enable them to utilize the technology in order to compete effectively.

Finally, globalization also imposes a challenge on the *shari'ah* authorities in Islamic banks in the issuing of *fatāwā* required in the rapidly evolving international financial markets.

IV. COOPERATION BETWEEN ISLAMIC BANKS AND INTERNATIONAL BANKING AND DEVELOPMENT ORGANIZATIONS

There are great opportunities for Islamic banks to play an important role in financing development projects in the private and public sectors in the developing countries in cooperation with development organizations such as the World Bank, Islamic Development Bank, IMF, and IFC, especially in situations where these organizations need to develop specific Islamic financial instruments for selected development projects. A good example is the IFC's experience with Islamic funds and leasing instruments in project financing through *muḍārabah* for private sector projects in Pakistan and the Middle East. The IFC's successful experience illustrates the fact that there is great potential for the accessibility and employment of Islamic instruments by international organizations to finance private or public projects. The participation of IFC and other international organizations (WB, IDB, and IMF) will also serve to boost confidence in Islamic products.

