FUTURE TRENDS AND FINANCE APPROACHES IN ISLAMIC BANKING

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Abstract **Briefly, Islamic banking refers to financial activities that are governed by the teachings of the Islamic law (Quran, Sharia) and essentially prevent payments and receive interests. Islamic banking today attracts Muslim and non-Muslim market player. While the global financial tension has created new weaknesses in the international financial system around the world, Islamic banking demonstrate symptoms of relative resistance to these shocks. It is even argued that if Islamic principles were implemented, it would prevent a financial crisis. Despite the fact that the growth of Islamic banking in recent years has promising a bright future in this area, it is imperative that Islamic financial institutions and Islamic banks do many things. Islamic banks, which are now focusing on strategic options and basic operations and infrastructure, will be in a more powerful position in order to achieve the intact market excellent opportunities and manipulate the changing dynamics of their industry.**

Keywords Islamic Banking, Conventional Banking, Market Strategy, Operational Efficiency, Finance approaches

I. INTRODUCTION

In brief, the existence of Islamic banks in the second half of the 20th century came as an offshoot of the newly rediscovered Islamic economics [1]. The purpose of Islamic banking is to finance activities that are governed by the doctrine of the Islamic principle of Islam and essentially prevent payments and receive interests [2]. Islamic banking today attracts Muslim and non-Muslim market players. The global market for sharia-compliant financial products is estimated at $ 800 billion to $ 1 trillion. According to International Financial Services London, by the end of 2008, Sharia (religious l-owned assets have risen to $ 951 billion that increase of 25 per cent from $ 758 billion in 2016 and 75 per cent from $ 549 billion in 2018 (The Islamic finance industry has grown at an annual rate of 15-20%, much larger than the growth of the traditional financial industry (conventional). Islamic financing mechanisms have different alternative forms and transactions from the conventional financial institutions in which they do not deal with interest [1]. While the global financial crisis has created new weaknesses in the international financial system around the world, Islamic financial showed an indication of relative resistance to shocks. It is even argued that if the Islamic principles were implemented, it would prevent a financial crisis [2]. These Sharia principles have a fundamental concept that God is the owner of the whole world as well as the whole wealth. Muslims have the right to enjoy their wealth providing that it is realized or invested in a way that is adhering to Sharia principles [1]. Islamic financial instruments should all follow the Sharia dictates.[3]

However, some of the effects of the crisis were felt in the industry and exposed vulnerabilities that need to be quickly identified in order to sustain the growth of Islamic banking [3]. In spite of the fact that there is no consensus about the causes of the global financial crisis, there are a number of different authors who have made a lot of guesses. Some argue that the complex and excessive use of structured finance products, derivatives and other unreliable assets in the wake of the financial crisis is to blame. Others argue that monetary policy, financial supervision and easy regulation combined with surplus leverage and credit growth are fundamental factors that triggered the crisis.

All of the above items require prudential regulation and supervision. The lack of supervision and regulation in the financial sector played an important role in the financial crisis, which led to poor liquidity management. Islamic banking, as a solid industry, faces many challenges. For example, the lack of effective regulatory frameworks, standards and guidelines, decent manpower, effective government support, regulations and prudential supervision, risk management and external auditing for Islamic banks are challenges facing the industry for future growth.

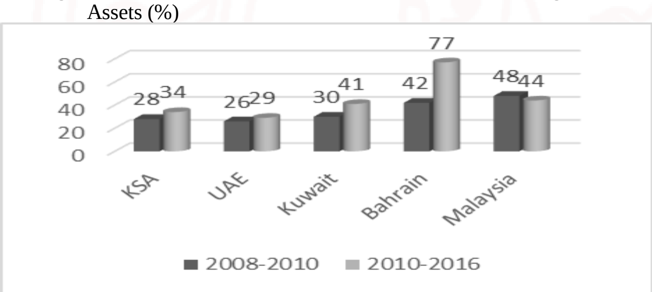
The methodology of this study is documenting analysis with a comparative approach. Secondary data has been collected through manuals, Religious texts, Islamic finance related websites, guidelines issued by various regulatory bodies, guidance note suggested by various institutes, legal provisions in the legislation of several countries and various research papers were reviewed and their findings were used as a secondary data to expand this paper [4].

This paper is organized as follow: we conduct in section II, according to the mentioned comprehension, the growth trend of Islamic banks has been investigated from the profitability factor. In section III, scrutiny the challenges faced by Islamic banks. In section IV, proposed the most important markets that operate are in accordance with Islamic law; In Section V, competition between these banks and conventional banks is examined in terms of customer-centric approach; In Section VI, presented derivatives Islamic Instruments and its Challenges have been raised and some examples of Islamic banks have been mentioned. In Section VII, presents prospects and opportunities for better efficiency and solutions to improve the performance of executive management, create opportunities, and achieve effective efficiency. At the end of the paper in section VIII, we have collected and concluded the discussed issues. The strategy of this paper focuses on finding a position and attaining sustainable growth through more efficient use of opportunities and opportunities.

II. ISLAMIC BANKING DYNAMICS

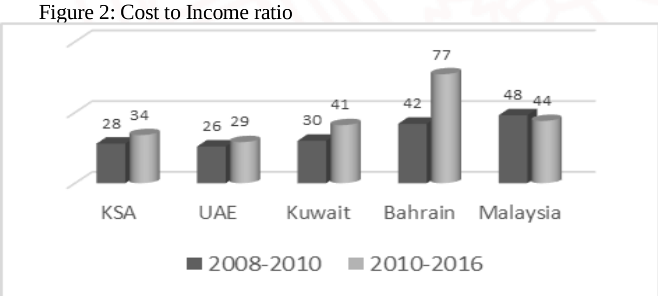
A closer look reveals that dynamics and market forces are changing, and two key indicators in the Islamic banking industry indicate the need to review strategies in this industry:

Figure 1: The Difference between Growth in Islamic Banking and Banking Assets (%)



Source: Bank Negara Malaysia (2018)

Figure 2: Cost to Income ratio



Source: Bank Negara Malaysia (2018)

Islamic assets of conventional banks are considered in the level of conventional banks because they are considered to be the yield of the conventional bank[4].

1. Slow growth current

After several years of rapid growth in which Islamic banking surpassed many of the conventional banks, the growth of asset differentials in key geographic districts, including Saudi Arabia and the United Arab Emirates, was stopped. Soon, growth in Islamic banking can be reduced due to the full market, and Islamic banks will lose their "normal" share[5]. Although current data are non-deterministic, they can be considered as a primary indication.

2. Reduced profitability

Although Islamic banks have surpassed conventional banks in terms of growth in recent decades, they are not higher to profitability. For example, many small Islamic banks in the GCC have been struggling to profitably for many years; some have also suffered from a regional economic crisis that is mentioned in the "Islamic Banking Challenges" section [6]. Most importantly, some important Islamic banks, especially GCC, have seen a drop-in margin in the last five years. In order to maintain profitability, the ability to increase the capacity of Islamic banking, especially those that have not yet been exploited, is essential. From a strategic point of view, this means that Islamic banks, which so far only imitated conventional banks, need to rethink their position [7]. From an operational point of view, Islamic banks need more efficiency over their value chain.

III. THE CHALLENGES OF ISL1AMIC BANKING

Considering the slow growth and the reduction in the profitability of Islamic Banking, we will address some of the major challenges facing this industry.

1. The size

It has been observed that many Islamic banks are smaller than their usual rivals in their domestic markets. So that even the major’s Islamic banks are usually compared to conventional international competitors. [8]. In fact, there is no Islamic advance bank in the world that has a particular Islamic or broad-based business model [9].

2. Competition

Although the growth of the market is declining, the number of Islamic banks and financial institutions is on the rise. For example, the only new banking licenses issued in the United Arab Emirates in recent years have been for Islamic banks, while conventional banks are opening up and providing Islamic instruments. Consequently, it is not a significant distinction only in accordance with the Sharia[10].

3. Standardization and Legislation

Standardization and legislation are the constant challenges of Islamic banks. Different perceptions of accepting various products from the Sharia perspective make standardization difficult. For example, an Islamic financial instrument can be accepted by a group of angels and rejected by another group, because the Sharia and jurisprudence decrees issued by these jurists are based on their personal perception and jurisprudential rules[2]. Moreover, there is a difference in the admission of products and services between Southeast Asia and the Middle East and now, an approach has emerged. As the Bank of Nigeria (the Central Bank of Malaysia) avoids selling GCC-denominated banking products to increase standardization in the industry; Legal issues could also arise from the absence of specific Islamic banking laws in some countries[11].

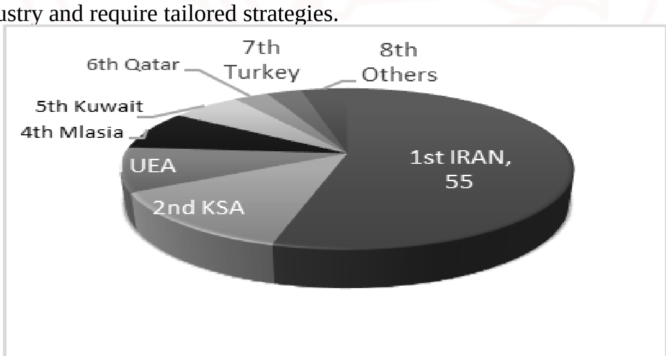
4. Cost structure

Most Islamic banks, despite the dramatic growth, have not been continuously profitable, especially after the global banking crisis. Part of this defect is the structural factors. Because Islamic instruments are usually more complex than conventional tools, which increases the cost of providing and producing these services[12]. Banks' specific weaknesses, for example, risk management and operational efficiency, also contribute to this issue.

IV. OVERVIEW OF THE MARKET

Islamic Banking - Financial activities in accordance with Sharia and jurisprudence and Islamic law have become part of the global financial services industry, which has seen rapid growth both in size and in terms of structure[2]. The total Islamic assets in 2016 are estimated at around $ 1200 billion. Islamic bank assets account for about 90 per cent of this figure, while Islamic capital accounts for 10 per cent of the remainder.
The main geographic markets are Iran, Saudi Arabia, United Arab Emirates, Malaysia, Kuwait, Qatar and Turkey (figure 3).

Figure 3: The eight core markets are the growth engine for global industry and require tailored strategies.



Sources: central banks, EY analysis (2018)

In recent years, Islamic banking has had a significant growth rate. For example, the combination of the annual rate of growth (CAGR) in Saudi Arabia was 21% between 2006 and 2010, and in Malaysia, it was 24%.
Markets in the form of the influence of Islamic banking (the number of Islamic banks' assets as a percentage of total bank assets) can be divided into three main categories: fixed, emerging and intact (Table 1).

The consolidated category of Islamic banking in the Middle East and Southeast Asia comes with some of the most active global markets like Kuwait, Saudi Arabia, the United Arab Emirates and Malaysia. Emerging markets such as Pakistan and Indonesia have a large Muslim population and with this in mind, it is expected to have a good perspective in the future. Similarly, large and untapped markets like India are considered to be a tremendous asset for courageous investors.

Table 1. Islamic financial markets

	Musilm population	GDP	Islamic assest , billion $	% of Islamic assets of total assets
Kuwait	3	40517	62	40%
KSA	27	23201	142	38%
UEA	6	59533	94	22%
Malasia	17	15022	86	17%
Pakistan	175	2516	6	7%
Turkey	73	13150	25	5%
Indonesia	209	4250	10	3%
India	162	3408	-	-
China	22	7544	-	-

Sources: Company financial reports, EY universe, EY analysis (2018)

At present, there has been no effective step in promoting the expansion of Islamic banking. From a strategic point of view, markets like India are a great opportunity to develop. The three main types of actors in the Islamic banking industry are noteworthy: Islamic Banks and Islamic Financial Companies. All Islamic banks or institutions are entirely independent or are under the umbrella of conventional banks, with Islamic instruments, are abandoned and isolated in Islamic banking, which are placed within conventional banks.[13]
Islamic financial institutions focus on providing financial instruments based on jurisprudence and religious law, such as housing and automobile financing, and are not allowed to receive interests.

1. Is there a market or Niche market?

Basically, Islamic banks have two strategic options ahead:
The exploitation of the Islamic banking Niche market in full contrast with conventional banks before moving on any of these paths, by adopting a mixture of both strategies, we present concepts from each of them[8].

2. Exploitation of the Niche market

The full exploitation of the Niche market is intended to target segments of customers who are heavily involved in financial transactions in compliance with religious law. As well as the provision of products and services that not only address public financing but also the specific needs of Muslim customers. While Islamic banking services are plentiful in banking (for example, auto loans and credit cards), while there are vacancies in some more complex and advanced areas (for example, asset management and wealth management), Such products that are appropriate to the specific needs of Muslim customers, provide a ground for actual distinction [14].

In microfinance, target customers can consist religious conservatives, clerics, endowment organs, or members of the Islamic Ministries of Justice. An example case of a microfinance product that is specific to Muslims is the financing of pilgrimage to Hajj pilgrimages. This service is also suitable for clients who commonly consider less importance in their finances to comply with religious law. Such products are now existing in some Muslim countries; for instance, the Tabung banking in Malaysia and Brunei[15]. In personal banking, the objective sectors may comprise the holders of Halal industries.

Providing expert consultation to people with great particular worthwhile sketching for the endowment can be a various and specific service in this section. In corporate banking, the target sectors could include Islamic philanthropy foundations and the Halal industry[16]. Asset Management for Endowments, funded by Western organizations, purchased by private companies based on religious law, can be considered as an essential service in the field of Islamic banking. In institutional banking, other financial institutions can serve the purpose of providing specialized banking services to support the development of Islamic financial activities. On the other hand, the full exploitation of Islamic banking requires attention to pricing. Since target customers are less willing to accept conventional banking products, Islamic banking products can be priced at a higher price than conventional products, provided they remain competitive among Islamic products.[15, p. 04]

Maintaining a personal relationship in gaining "loyalties to Islamic banking is important, and this means providing bricks and cement (physical) branches where the line staff can face-to-face meetings with customers[17]. At the same time, non-Traditional methods to reach customers through alternative ways, like the phone bank, should also be taken into consideration[18]. In addition, the social responsibility of the organization, for example, to support local community associations and the establishment of Islamic philanthropy foundations, can be strongly requested by Islamic banking customers.

Some international banks have Islamic effects in many countries, for example, HSBC Annual in Malaysia and some Islamic banking communities that are resident in the GCC have significant geographical envelopment[19]. Although some banks focus on the same country, geographic extension is considered an opportunity for growth for centralized banks on Niche market. There are good markets outside Malaysia and the GCC, including emerging markets with a majority of Muslim populations, like Indonesia and Iraq, and rich and developed markets with Muslim minorities like Germany and France. In these two countries, venture cooperatives can be the best entry strategy [18].

Market vacuums are very diverse so that opportunities to meet the specific needs of Muslim customers with special banking outcomes consistent with fundamental Islamic values are still not developed and provide adsorbent areas for development and profit for those who are keen on exploiting Niche market [20].

3. Face-to-face competition with conventional banks

It is the obvious that many Islamic banks challenge versus their competitors. At the same time, everybody does not notice that the face-to-face strategy is essentially different to the strategy of exploiting the Niche market Islamic banking. Competition against conventional banks means attracting customers who are less important in their financial activities to comply with religious rules and pay more attention to competitive products and effective services in the banking market[21].

There are three key principles in targeting the customer segments. First, identifying the segments of the customers who have the least openness to Islamic banking (to prevent). Second, identifying sectors that are not fully compliant with religious law (To understand the shortcomings) and third, identify the sectors open to ethical banking (to reach Muslim and non-Muslim audiences [17].

V. INCREASING COMPETITION AND THE NEED FOR CUSTOMER-CENTRIC APPROACHES IN ISLAMIC BANKS

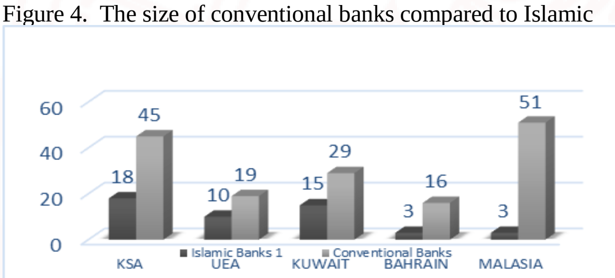
The attraction of these customers' needs to satisfy a wider range of customer needs and, therefore, due to the ease of use and reasonable prices compared to conventional banks. To achieve this goal, product innovation in the form of expanding services using existing Islamic structures and the design of new Islamic structures has a special priority [22]. Financial services and products for small and medium-sized enterprises appear in emerging Islamic banking and moral banking products, investment in sustainable energy, are an opportunity to expand the range of services provided. The structures of new Islamic banking products do not easily fit with religious rules. These include covert funds (a speciality of alternative assets for individuals with a net asset value and derivative instruments for corporate and institutional customers. Although some Islamic banks provide Islamic derivative instruments, such tools, in general, they are not accepted as products based on religious law [12].

Islamic banks are usually at a disadvantage in competing with their conventional counterparts because they usually have smaller sizes (figure 4). For example, in microfinance, the extent and scope of the network are more dramatic [20]. To compete successful, focusing on two areas is essential. First, Islamic banks should pay attention to using alternative ways likewise, Internet banking and mobile banking to attainment market contribution.

Applying these as a sales channel is superior to focusing on services that are already customary. Second, the use of different branch patterns should be investigated according to the needs of target customers. These patterns include a range of service delivery, focusing on a wider range of customers, to complete branches that cover all customer segments. Alternative subsurface patterns have other advantages, which include reducing investment costs, operating costs, and deployment times and, if combined with alternatives, will be very powerful. A new and customer-focused illustration that emphasizes ethical and social values or environmental efforts will reach the largest collection of Muslim and non-Muslim audiences [23].

Therefore, training programs on Islamic banking products and structures are also needed. When facing with the conventional banks, the first step before the international expansion is to build a strong domestic foundation. Integration and ownership provide intriguing opportunities for achieving synergies related to scale from wider operations. [24] Strategic integration and ownership of Islamic banks allows the expansion of their branch networks, the exploitation of synergies Operational and financial penetration is more effective than conventional banks[10].

Figure 4. The size of conventional banks compared to Islamic



Sources: Central banks, EY analysis (2018)

VI. DERIVATIVES ISLAMIC INSTRUMENTS

Combination tools are very common in Islamic banking. Some experts in the Islamic banking industry condemn these tools because they consider these tools to be incompatible with religious principles [25]. They believe that a delay in bilateral commitments to future time is implied in the debt swap ruling without the transfer of an initial asset, which is considered to be the probability of a transaction speculated. This is the most important reason for the rejection of Derivatives instruments in the Muslim world, especially the Gulf States.

At the same time, some of the leaders of the Islamic financial functions industry need to understand the need to manage the potential risks and potential benefits of their tools to cover. For example, the Central Bank of Malaysia (Negara), which has always been the defendant of mentioning and providing derivative instruments in Islamic banking, assigns that with the juridical, regulatory and corporate governance framework, the Islamic Finance system can be reclaim and expanded[26]. The bank presented the first Islamic International Instrument settlement to document Islamic Transactions in 2007. The Malaysian bank also introduced the first Islamic-derived yield in 2005 (the exchange rate for Islamic interest). Another milestone is for Tahawwat's Islamic derivative instruments, which were presented by the Islamic International Financial Market in 2010 (a Bahraini Standardization Standard for Islamic Money and Capital Markets and the International Association of Swaps and Derivatives Instruments) [25]. Contracts, including Modaraba, Mosavama, indicate which of the parties can obtain into risk management adjustments for covert funds, standard anatomies and documentation[2]. These new standards, if broadly accepted, could strengthen the market for Islamic derivative.

Presently, Malaysian banks and main international banks present Islamic derivatives. The most comprehensive of these instruments is the swap of the Islamic interest, exchange swaps, exchange rate swaps, futures contracts and structured products of shares of Islamic instruments, unlike traditional instruments, cannot be traded because their goal is only to cover and not speculative tools.

Reducing development and profitability shows that the time has come to exploit the potential of Islamic banking. In this regard, Islamic banks should inspection their tactical position and increment their functioning efficiency[27].

Over the years, multitude of Islamic banks have experienced a two-digit growth rate that surpassed their rivals in conventional banking. at first sight, everything looks good for banking. There is abundance of circumstances for growth and advancement, as Islamic banking, even at the Gulf Cooperation Council (GCC) and Malaysia, seldom soars a third of the universal market quota. Many potential markets that are full of Muslim populations (such as India and the Commonwealth of Independent States (CIS) from the former Soviet Union remain intact[22]. In addition, the general influence of banking on multitude grand industry markets are still slight. For example, the GCC countries have not yet attained the level of banking in countries such as France and Britain. meanwhile, several emerging markets have been opened up to Islamic banking [22].

VII. OPPORTUNITIES FOR IMPROVING EFFICIENCY

An Islamic bank pursues any strategic position, requires more efficiency for processor activities to adding value. Like other GCC banks, crucial areas include sales advantage, operational efficiency, and efficiency management.

1. Focus on the customer

The number of banking products and income per client in the GCC remains comparatively low compared to developed markets. Customer euphoria is a vital element in expanding the market share of banks, while studies have shown that GCC banks do not care about customer satisfaction as a priority. The three main areas for improving customer focus can be:

- Workers: Line staff (Sales staff have a very limited knowledge of the services and products they provide), which is more common in Islamic banking, while that Islamic banking customers need additional explanations for Sharia-based structures and products. There is also a need to improve responsiveness, for example, customer contact at the right time.[2]
- Information**:** When customers have important information about a product before Do not buy, usually leads to serious and lasting damage to brand loyalty (For example, awareness of additional costs after purchase)
- Contact facilities: Customers usually have a limited number of calls centres or services and often go from part to another. There are only a few Islamic banks that have a many-sided client relationship perspective.

Improving client service begins with a framework in which consistent with all features of the institution (people, culture, performance metrics, processes, and infrastructure). When the rivalry escalates, a more intelligent, complicated and customer-centred approach to Islamic banks is needed. Redesigning sales staff and shifting the focus from product to customer segments, improving skills and sales techniques, and deploying multi-channel delivery through organizational co-ordination will maintain costs down and increase customer satisfaction. Preserving a viewpoint towards the customer in all Aspects has a specific advantage.

2. Operational efficiency

Most of banking processes in the GCC are still handy, with numerous paper documents and layers of decision making. This issue is very difficult in Islamic banking because there is always a transfer of an asset in Islamic banking[28]. Re-designing processes can bring significant improvements and, even in some cases, reduce resource requirements by up to 50%. in spite of the fact that automation is very significant, it is not consistently obligatory, especially considering the low cost of working in the Gulf Cooperation Council. Targeted IT investments are significant because they align the all organization with respect to the strategy and recapitulation of the structures and can dramatically improve performance. Outsourcing offer options for focusing on business processes, developing service surfaces, and raising controls. Despite the fact that is a relatively new concept in the GCC, many regional banks have successfully outsourced their relatively simple processes to India and Egypt.

A structured approach to product design and offering (cost analysis and cost savings identification for strategic and functioning costs can decrease costs in some cases by up to 30 %.)

3. Performance Management

Supervising and rewarding the most successful people are the clue to improving performance surfaces. Remunerations can be financially, career progression, or introduction of people in an organization[23]. An appropriate and structured motivational system can be a powerful tool for maintaining employees, especially in Islamic banking, which has a deficiency of experienced human resources. The key factor here is the direct linking of rewards to implement actions that have already been defined at employee level (so that improvements can be made at a high cost).

VIII. SUMMARY AND CONCLUSION

This study, however, focused on the Islamic banking segment only; and noted that there are also new instruments for financing and capital market products, Islamic banks were among the first categories of financial institutions that emerged in Islamic financial services industry. As this industry expanded, and as the conventional financial sector in MENA countries diversified into capital markets and other segments, many Islamic non-bank financial institutions and services also emerged in Islamic finance. Now the Islamic financial services industry is not only composed of Islamic banks but also includes investment and mutual funds, project finance companies and takaful institutions.[26]

The growth of Islamic banking in recent years has promising a bright future in this area. But along with increasing competition and some recent signs of this growth has declined, so it is necessary for the financial institutions and Islamic banks to do many things. In Islamic banking, with any strategy that a strategy focuses on locating in the context of, or competing with, conventional banks either face-to-face or a combination of both, sustaining growth requires more efficiency along the supply chain. The Islamic finance industry is in the midst of a phenomenal expansionary phase, exhibiting average annual grown rates of about 15 per cent in recent years. This rapid growth has been fueled not only by surging demand for Sharia-compliant products from financiers from the Middle East and other Muslim countries but also by investors around the world, thus rendering the expansion of Islamic finance a global phenomenon[8]. New product innovation is also driven by domestic banks' interest in risk diversification. With a large number of new Islamic banks across the Middle East and Asia especially, diversification of products enables banks to offer the right product mix to more sophisticated clients. A few banks are already active across different jurisdictions, and this trend is certainly going to continue in the near future with possibly some consolidation. Infrastructure plays an important role in supporting a nation's economic growth [29-31]. Islamic banks, which are already focusing on strategic and basic operations and infrastructure, will be in a more formidable circumstances in regards to achieve pristine market opportunities and manage dynamic variables in their industry.

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