

FACTORS OF INFLUENCE IN THE ESTABLISHMENT OF ISLAMIC BANKING AND FINANCE IN ALGERIA

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ABSTRACT

The present study is conducted in Algeria for the establishment of Islamic banking and finance. The study tries to examine those factors that become a hindrance to the establishment and development of the sharia compliance for Islamic banking and finance in Algeria. Survey data based on a set of questionnaires were distributed to employee and customers of nine selected banks in the city of Boumerdes, Algeria. Results of the study show the existence of the technical, social and legal obstacles as the main factors that hamper the success of the establishment of the Islamic banking in Algeria. This study is helpful for the policy makers, bankers and investors for formulating the future policy. Besides, this paper is the first attempt to establish the factors which affect the development and establishment of Islamic banking and finance in Algeria.

Keywords: Islamic banking, Finance, Establish, Factors, Obstacles, SPSS, Algeria.

INTRODUCTION

In the economy of any country, financial system plays an important role, which consists of credit facilities and provision of loans for the production process. Most of the banks which are operating in many countries of the world rely on the system of interest. In Islam, interest is called Riba which drives against the principle of Sharia (Maqsaid al-shariah) and a termed as a haram (forbidden) as explained by (Abidin, Bakar & Haseeb, 2014 & 2015; Kameel & Larbani, 2009).

In many Muslim countries, the Islamic banking system has been established to serve the needs of the Muslim communities where the practice of usury or Riba' is prohibited. This Sharia compliance Islamic banking system operates in parallel with the conventional banking which was in existence before the establishment of Islamic banks. Despite many challenges, Islamic banking system is proven to be viable and able to withstand the impacts of the economic and financial crisis. In addition, Islamic banking system is also very well accepted by the conventional banking system with the introduction of sharia compliance banking products and services by the significant conventional banks in the non-Islamic countries (Abidin & Haseeb, 2015; Bittman, Davies, Russell & Goussakova, 2017).

Today, Islamic banking has become a substantial segment of the global financial market in Islamic and non-Islamic countries that offers a wide range of financial products and services (Dusuki, 2008). The establishment of this Sharia compliance Islamic banking and finance is concentrated mainly in the Middle East and Southeast Asia countries. Besides these regions also serve as a Centre for promoting the sharia base Islamic banking and finance to western businesses and financial markets (Tarman, 2010).

In Algeria, despite being a Muslim country, the share of Islamic bank and finance is small which accounts for not more than 1% of banking activity (Abidin, Haseeb, Azam & Islam, 2015; Elhachemi, 2012). In 1991, Banque Al Baraka d'Alge'rie - a private bank, became the first

Islamic bank to operate in Algeria which offers a limited financial product to its customers (Benamraoui, 2008). However, there are no Islamic banking products in all public banks in Algeria. The introduction of the Islamic banking system in Algeria will undoubtedly help in elevating the level of technical performance of the Islamic banking system.

The motivation of this paper is to identify the obstacles that become a hindrance to the success of promotion and the establishment of the Islamic banking in Algeria as an alternative to the conventional banks. Besides, this paper focuses on social, technical and legal issues about the establishment of Islamic banking in Algeria. The study includes the Islamic banking and financial products in all public-sector commercial banks operate in Algeria. However, due to the large size of the community in Algeria, the study includes only all the branches of commercial public banks in the selected city of Boumerdes.

OVERVIEW OF ISLAMIC BANKING AND FINANCE

The foundation of Islamic banking and finance is the prohibition of interest or Riba in its practices which distinguishes it from its counterpart; the conventional bank (Iqbal, 1997). According to Muslim scholars Riba' is like interest or usury and therefore always be condemned (Haron & Shanmugam, 1997). The practices of Islamic banking and finance require the application of the provisions of Islamic law in all transactions and investments. Accordingly, all profit and loss transactions must be done according to the Islamic banking operations which include the method of financial intermediation. In general, the Islamic banking business must adhere to the Islamic values and ethics in the banking business (Abidin, Haseeb & Islam, 2016; Abidina, Haseeb & Jantan, 2016).

In addition, financing is a primary function of Islamic banking like conventional banks. In the Islamic banking 50 and 80 percent resources are used for the financing activities (Haron & Shanmugam, 1997). Approximately, the financing activities have three areas categorization, like investment, trade and lending. Moreover, different financing activities are based on PLS scheme, benevolent loans and other on the mark-up. Broadly saying, these are the areas in which Islamic banks are most active in trade and commodity finance, leasing and property.

ALGERIA'S BANKING SECTOR

Algeria's banking sector controlled by the government banks and suffered from a higher level of non-performing loans towards state-owned enterprises (SOEs). In 2007, the government banks controlled the 95 percent of total bank assets. There are 22 banks in Algeria today, with eight related to public-sector and fourteen private sectors (Elhachemi, 2012). Despite Algeria is a Muslim country and the second article of the Constitution provides that Islam is the state religion, Algerian market share of Islamic banks still marginal which not exceed by 1 percent (Suryanto, 2016; Suryanto & Ridwansyah, 2016).

In 1991, first Islamic bank opened its doors in Algeria is the Banque al Baraka Algeria and operations are limited in the scope and scale. However, with the passage of time, the number of borrowers and savers of the banks are steadily increased. It is stated by (Benamraoui, 2008) that the banks across Algeria increased their branches. The law on credit and money permits Islamic banking products and transactions, including mortgages because these products do not establish any break of the Algerian law. Approximately, 99% loans of the real estates disbursed by banks based on interest rates. Additionally, there is a growing realisation among the Muslims population regarding the need for Islamic banking as an alternative banking system in Algeria.

The increasing demand for Riba' free financial products due to the religious conviction are on the rise in Algeria. Also, the Islamic banking system provides a platform for resolving the issue concerning the problem of the investment tax and Riba-based practice.

METHODOLOGY AND RESEARCH DESIGN

This study aims to investigate the factors that become a hindrance to the success in establishing Islamic banking and finance in Algeria. The study embarked on quantitative research which is considered as an appropriate method for investigating business related notions in useful concept (Alex, 2010; Tarman, 2010). Besides, this approach also has several advantages like possessing a high rate of reliability to the collected data, indicate a positive relationship between the subjects under study and its suitability in investigating individual opinions behind their motive of action, behaviour and attitude as well (Matveev, 2002). In applying the quantitative research design, we will examine the relationship between dependent variable (the success of Islamic banking in Algeria) and independent variables (social, legal (legislative) with banking (technical) constraints).

Data Sampling

Due to the large size of the community, we select a sample of banks which includes all commercial public banks operating in the city of Boumerdes. These banks are named as: Banque Nationale' Algeria (BNA), Banque Extérieure Algérie (BEA), Banque Agriculture Developpement Rural (BADR), Banque de Développement Local (BDL), Credit Populaire d'Algérie (CPA), Caisse Nationale Epargne et de Prévoyance (CNEP), Caisse Nationale de Mutualité Agricole (CNMA) and Algérie Poste (La Poste). The research survey questionnaires were distributed to the selected respondent. The validity ensures the ability or scale to measure the content or dimensions. For the reliability and validity, various statistical tests are applied. In relation, reliability defined the degree in which the results are free from errors and inconsistent. On the other hand, measurements, experiments and tests provide the same results in all repeated trials (Carmines & Zeller, 1979). Reliability is also conducted to check the internal consistency of dependent and independent variable. In general, for the better and closer reliability, the value of the alpha coefficient should be closer to 1.0. According to Sekaran (2000), below 0.60 is considered poor reliability and the acceptable range is 0.70 and over 0.80 is considered excellent reliability. So in this study according to the recommendation of Nunnally (1978), minimum reliability set is 0.60.

However, reliability operationalised that it is the internal consistency of scale, which describe the degree in which all items are homogeneous. It is proposed by (Werts, Linn & Jöreskog, 1974), the composite reliability measurement which is an alternative conceptualisation of reliability shows proportion for the measurement of variance attribute for the underlined trait. So for this study, the composite reliability is used to assess the reliability of scales. Also, stated by Bagozzi & Yi (1988) that a scale should be considered a reliable if each instrument value is more than the benchmark of 0.60.

HYPOTHESES

Rogers (2004) proposes that each adopted category has different characteristics. Based on the relationship between the variables described in the theoretical framework, we develop the

following hypotheses that will be tested in this study:

Hypothesis 1: Technical issue complicate the establishment of the Islamic banking and finance in Algeria.

Hypothesis2: Social issues complicate the establishment of the Islamic banking and finance in Algeria face no social obstacles.

Hypothesis3: Legal policy and law complicate the establishment of the Islamic banking in Algeria.

EMPIRICAL RESULTS

A degree in which all the measurements are free from errors and produced consistent results is called reliability. In addition, it is the internal consistency of a scale that evaluates the degree in which the measurements of all items are homogenous. In this study, Cronbach 'alpha is used to validate the reliability of each variable from the collected data (Table 1).

Variables	No. of Items	Cronbach's Alpha
Legal obstacles	05	0.769
Social constraints	08	0.865
Technical banking constraints	09	0.832
Islamic banking adoption	05	0.716

The Cronbach's alpha for the variables Legal Obstacles, Social Constraints, Technical Banking Constraints and Islamic Banking Adoption: 0.769, 0.865, 0.832 and 0.716 are respectively. So, from this result, it is concluded that Cronbach alpha is more than 0.7. So, it shows that all the measurement is internally consistent and reliable.

Table 2 shows the means and standard deviations of each variable that are used in this study which is measured in SPSS.

	N		Maximum	Mean	Std. Deviation
Legal obstacles	250	3.40	5.00	4.2592	0.44992
Technical obstacles	250	2.56	4.33	3.5751	0.58964
Social obstacles	250	2.12	4.62	3.4225	0.73414
Adoption	250	2.00	4.60	3.6440	0.62259
Valid N (listwise)	250				

The level of association between the variables is measured through correlation analysis which considers strength and direction of the relationship. It differs from the no relationship (0) to the perfect relationship (1) or the perfect negative relationship (-1) as well. In addition, the value of R² explains the variation in the dependent variable by all the explanatory variables of the study.

In relation, Pearson correlation matrix indicates the directions, strengths and significance of the bivariate association between the variables in the study. Table 3 shows the correlations between adoption and three effect factors. In Algeria, the technical and social obstacles are significantly and positively correlated with the adoption of Islamic bank and finance, but the legal obstacles have a negative correlation. Also, the Pearson correlation for the technical, Social

and legal obstacles are presented. The Pearson correlation for technical, social and legal obstacles in Algeria are 0.16, 0.468 and 0.476 respectively which represent the relationship between technical obstacles, legal obstacle and social obstacle with the adoption of Islamic banking and finance.

		Legal Constraint	Adoption	Technical Obstacles	Social obstacles
Leg lob	Pearson Correlation	1	-0.169**	0.171**	0.124
	Sig. (2-tailed)		0.007	0.007	0.051
	N	250	250	250	250
Adoption	Pearson Correlation	-0.169**	1	0.468**	0.476**
	Sig. (2-tailed)	0.007		0.000	0.000
	N	250	250	250	250
Tbc	Pearson Correlation	0.171**	0.468**	1	0.938**
	Sig. (2-tailed)	0.007	0.000		0.000
	N	250	250	250	250
Soc	Pearson Correlation	0.124	0.476**	0.938**	1
	Sig. (2-tailed)	0.051	0.000	0.000	
	N	250	250	250	250
** Correlation at the 0.01 level (2-tailed is significant)					

From the above table, it is concluded that for our hypothesis testing all our hypotheses are accepted and are summarised in the following Table 4.

Number	Hypothesis	Conclusion	Sig
H1	Technical issues complicate the establishment of the Islamic banking and finance in Algeria	reject	0.000
H2	Social issues complicate the establishment of the Islamic banking and finance in Algeria face no social obstacles.	reject	0.000
H3	Legal policy and law complicate the establishment of the Islamic banking in Algeria.	reject	0.007

Table 4 depicts that all the significant Values are less than 0.05 which concludes that all hypotheses in this study are accepted.

CONCLUSION

The primary objective of this study is to propose the Islamic bank as the alternative to the conventional bank especially in Muslims countries like Algeria. Our contributions in this study are to identify the obstacles that hamper the implementation and for the establishment of the Islamic Banking practices in Algeria. This study divides the obstacles into three types; social, banking (technical) and legal obstacles. The results indicate that more than 70 percent of

respondents agree that legislation is a most critical factor in determining the success or failure of the establishment of Islamic banking in Algeria. Also, the lack of legislation laws about the Islamic banking in Algeria forms the primary barrier to the establishment of the Islamic banking system in Algeria. Additionally, about 80 percent of respondents agree of the non-existence of the Islamic technical and development plans as well as the mechanisms in promoting the Islamic banking and finance system. There is a shortage of qualified individuals in the field Islamic banking and finance is determined as the primary factor that hinders the development of the Islamic banking in Algeria. The failure of media in playing their roles in educating the public on Islamic banking system and finance in Algeria also recognised as one of the factors contributing to the delay in implementing the Islamic banking in Algeria. It is clear from the study that there is an existence of the social, technical and legal obstacle towards the implementation of the Islamic banking and finance in Algeria. We conclude that by overcoming the above-identified obstacles, there will be a successful implementation of Islamic banking and finance in Algeria as an alternative to the conventional system. On the other hand, the central bank of Algeria would provide new set policies and regulations about the establishment of Islamic banking and finance. Moreover, the central bank must provide the mechanisms and facilities for the development of Islamic banking and finance similar to commercial banks.

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