ISLAMIC BANKING AND STAKEHOLDER EXPECTATIONS THE NIGERIAN PERSPECTIVE

S. I. Dugguh and Ahmed Abubakar
Federal University, Kashere, Gombe State, Nigeria

ABSTRACT
Financial options with their attendant stakeholder expectations are many world over. The Islamic banking system is one alternative that lends itself to a zero-interest orientation. The objective of the paper therefore is to advance a theoretical exposition of Islamic banking and stakeholder expectations therein in the Nigerian business environment. The paper reviews literature on various Islamic banking systems, stakeholders and so on. The paper found that Islamic banking is an idea alternative to the western based interest oriented system of banking. It recommends support for the system by providing conducive business environment for its operation and fulfillment of stakeholder expectations.

Keywords: Islamic Banking, Stakeholders, Interest Rate, Financial System, Profit Sharing, CBN, Mudarabah and Musharakah.

INTRODUCTION
At the center of the financial system of a country lies the Apex Bank. Apex banks are known by various names in different countries. It is known as the Central Bank of Nigeria (CBN) as in the case of Nigeria. Its role is to oversee and regulate the activities of the different financial institutions. It has the task of ensuring the stability and efficiency of the financial system and also carrying out the government’s monetary policy. Many different types of institutions make up the financial sector from deposit money banks, capital market, pension funds administrators and insurance companies to mortgage institutions and building societies. They are jointly known as financial intermediaries. They all have the common function of proving a link between those who wish to lend and those who wish to borrow. In other words, they act as the mechanism whereby the supply of funds is matched to the demand for funds. As financial intermediaries these institutions provide four important services. These are: expert advice, expertise in channeling funds, maturity transformation and risk transformation.

The financial system in Nigeria was a prototype of western-type of financial system which was largely driven by interest rate resulting from financial intermediation. Financial intermediation facilitates the savings and investment process through the mobilization of savings from the surplus units to investment by the deficit units. Van Wijnbergen (1990) notes that interest rate, among others, is a major policy instrument with the most influence on savings. According to him, private, portfolio choice/allocation is also a function of interest rate. In Nigeria however, interest has been used over the centuries and still seen as an important monetary policy instrument in monetary management by monetary authorities especially the CBN. Indeed interest is an important but not the only instrument for monetary policy.

It is against this background that Islamic banking lends itself as an alternative to interest-rate system of banking in Nigeria and indeed the world over. Islamic banking therefore is a non-interest banking system which is consistent with Islamic (sharia) law and guided in principles, by Islamic economics. The system (seeks to) prohibits usury (collection and payment of interest: riba) trading in financial risk (securities) which is regarded as “gambling” and investment in unlawful or unethical businesses (haram). With Islamic banking system, it expected that there would be a fair and equitable distribution of income and wealth thus leading to a more efficient and optimal allocation and utilization of resources as compared to the interest-rate western system of banking. It is in line with this that Siddiq (2001) observed that the system will also ensure justice (both distributive and procedural) between the stakeholders involved since the returns to the bank is premised on the operational outcomes of the entrepreneur.

Paper objective
Based on the preceding, the objective of the paper therefore is to give a theoretical exposition on Islamic banking system and stakeholder’s expectations in Nigerian context. It is expected that the objective if accomplish will give credence to the concept of Islamic banking in Nigeria.

E-mail: sdugguh@yahoo.com
Islamic banking system and contracts

Islamic banking involves interest-free banking, in which there is no fixed rate of return. It is the banking system which is operated in accordance with the Islamic laws as guided by Islamic economics and the Sharia a’ board; that guides the financial institutions. This Sharia a’ board authorizes the products that whether these are Sharia a’ compliant or not. In particular, Islamic law prohibits usury (the collection and payment of interest), also commonly called Riba in Islamic discourse. Islamic banking also finds its roots in Islamic finance and all type of transactions are interest-free and of risk sharing. The interest is prohibited in Islamic ways of banking as it is also obvious from Quran. In Quran, in Surah Al-Imran, Allah said that: “O you who believe! Do not devour Riba (usury) multiplying it over and keep your duty to Allah that you may prosper” (3:130). Same kind of prohibition regard fixed interest is also stated in Surah Al-Rum (39), Al-Vasa (160-161) and Al-Baqarah (275-281) of Quran (Muhammad Akram et al., 2011).

Contracts and transactions in Islamic banking are categorized into participatory and non-participatory modes of finances. The former comprises of mudarabah and musharakah and the later comprises of murabaha, musawarah, salam, istisna and ijara (Muhammad, 2008, Issah & Ghulam).

Participatory mode of finances

a. Mudarabah: A form of partnership where one party provides the funds while the other party provides expertise. The people who bring in money are called “Rab-ul-Maal” while the management and work is an exclusive responsibility of the bank (Mudarib). The profit sharing ratio is determined at the time of entering into the Mudarabah agreement whereas in case of loss it is borne by the Rab-ul-Maal only. In case of Islamic banks, the depositors are called Rab-ul-Maal and the bank is called Mudarib. There are two types of Mudarabah: \( i \). Al-Mudarabah Al-Mugayyada: Rab-ul-Maal who, in case of Islamic bank, is a depositor who specifies a particular business or a particular place for the Mudarib (bank), in which case he shall invest the money. This is called Al-Mudarabah Al-Mugayyada (restricted Mudarabah). \( ii \). Al-Mudarabah Al-Muqdah: Is a case where Rab-ul-Maal (depositor) gives full freedom to the Mudarib (bank) to undertake whatever business he deems fit, this is called Al-Mudarabah Al-Muqdah (unrestricted Mudarabah). It is necessary for the validity of Mudarabah that the parties agree on a certain formula of sharing the actual profit right at the beginning of the contract. The Sharia has prescribed no particular proportion of profit sharing rather it has been left to the mutual consent of the parties. For the deposit management, Islamic banks create different pools of investment keeping in view the risk and maturity profile of the depositors. The deposits of the customers are placed in these pools and profit therefrom is distributed between the bank and the depositors as per weightages assigned at the time of agreement (Siddiqi, 1983; Nik et al., 2003).

b. Musharakah: Is a relationship established under a contract by the mutual consent of the parties for sharing of profits and losses in the joint business. Under Islamic banking, it is an agreement under which the Islamic bank provides funds which are mixed with the funds of the business enterprise and others. All providers of capital are entitled to participate in management but not necessarily required to do so. The profit is distributed among the partners in pre-agreed ratios, while the loss is borne by each partner strictly in proportion to respective capital contributions.

Non-participatory modes of finances

a. Murabaha: is one of the most common modes used by Islamic Banks. It refers to a sale where this seller discloses the cost of the commodity and amount of profit charged. Therefore, Murabaha is not a loan given on interest rather it is a sale of a commodity at profit. The mechanism of Murabaha is that the bank purchases the commodity as per requisition of the client and sells him on cost-plus-profit basis. Under this arrangement, the bank is bound to disclose cost and profit margin to the client. Therefore, the bank, rather than advancing money to a borrower, buys the goods from a third party and sell those goods to the customer on profit. A question may be raised that selling goods on profit (under Murabaha) and charging interest on the loan (as per the practice of conventional banks) appears to be one of the same things and also produces the same results. The answer to this query is that there is a clear difference between the mechanism and structure of the product. The
basic difference lies in the contract being used. Murabaha is a sale contract whereas the conventional finance overdraft facility is an interest based lending agreement and transaction. In case of Murabaha, the bank sells an asset and charges profit which is a trade activity declared halal (valid) in the Islamic Sharia. Whereas giving loan and charging interest thereupon is pure interest-based transaction declared haram (prohibited) by Islamic Sharia.

b. Musawamah: this is a general and regular kind of sale in which the price of the commodity to be traded is bargained between the seller and the buyer without any reference to the price paid or cost incurred by the former. Thus, it is different from Murabaha in respect of pricing formula. Unlike Murabaha, the seller in Musawamah is not obliged to reveal his cost. Both the parties negotiate on the price. All other conditions relevant to Murabaha are valid for Musawamah as well. Musawamah can be used where the seller is not in a position to ascertain precisely the costs of commodities that he is offering to sell.

c. Salam: This means a contract in which advance payment is made for goods to be delivered at a future date. The seller undertakes to supply some specific goods to the buyer at a future date in exchange of an advance price fully paid at the time of contract. It is necessary that the quality of the commodity intended to be purchased is fully specified leaving no ambiguity leading to dispute. Salam covers almost everything which is capable of being definitely described as to quantity, quality, and workmanship. For Islamic banks, this product is ideal for agriculture financing, however, this can also be used to finance the working capital needs of the customers (Nasir, et al, 2008).

d. Istisna: It is a specific kind of Bai (sale) where the sale of the commodity is transacted before the commodity comes into existence. The legality of Istisna is accepted by the Sharia scholars because it does not contain any prohibition. As far as this financing mode is concerned, it has been legalized on the basis of the principles of Istisnaan (public interest) Istisna is an agreement culminating in a sale at an agreed price whereby the purchaser places an order to manufacture, assemble or construct (or cause so to do) anything to be delivered at a future date. It becomes an obligation of the manufacturer or the builder (as the case may be) to deliver the asset of agreed specifications at the agreed period of time. As the sale is executed at the time of entering into the Istisna contract, the contracting parties need not renew an exchange of offer and acceptance after the subject matter is prepared. Istisna can be used for providing the facility of financing the manufacture or construction of houses, plants, projects and building of bridges, roads and highways etc. After giving prior notice, either party can cancel the contract before the manufacturing party has begun its work. Once the work starts, the contract cannot be cancelled unilaterally.

e. Ijarah: Refers to transferring the usufruct of an asset but not its ownership. Under Islamic banking, the bank transfers the usufruct to another person for an agreed period at an agreed consideration. The asset under Ijarah should be valuable, non-perishable, non-consumable identified and quantified. All those things which do not maintain their corpus during their use cannot become the subject matter of Ijarah, for instance money. In Ijarah transaction for instance, a customer approaches the bank and expresses his desire for a particular asset/property. The bank acquires the asset as per undertaking of the customer to acquire the said asset on Ijarah basis. The bank leases (transfers the use of the asset) to the customer for an agreed period of time and against an agreed amount of rentals. An Ijarah agreement, signed between the bank and the customer, stipulates all the relevant conditions with regard to the transaction. According to this agreement the bank is the Lessor and the customer is the Lessee. During the Ijarah period, the corpus of the leased property remains in the ownership of the bank and only its usufruct is transferred to the lessee.

Historical development of Islamic banking

Islamic financial system is relatively new, appearing only in the mid-1980s. In fact, all earlier references to commercial or mercantile activities conforming to Islamic principles were designated as either "interest free" or "Islamic" banking. The first modern experiment with Islamic banking was undertaken in Egypt. This pioneering initiative based on the profit-sharing principle was helmed by Ahmad El Najjar. It involved the establishment of a savings bank in the Egyptian town of Mit Ghamr in 1963. By 1966, the number of banks operating on the same principles had grown to nine (Siddiqi, 1988). Thus, they functioned essentially as saving-investment institutions rather than as commercial banks.

Though similar initiatives were being made in Malaysia and Pakistan, the overall growth of Islamic banking was miniscule until the 1970s when the nascent reawakening was propelled forward by the oil boom of 1974. The ensuing prosperity enjoyed by the predominantly Muslim beneficiaries of this boom witnessed the Islamic values in countries with substantial Muslim populations and a
The increased popularity and visibility of the sector was particularly evident in the 1990s when Islamic and non-Islamic financial institutions devised new instruments and both Muddarabah and Musarrat and so on in their daily banking transactions (Zeit, 2006). Furthermore, Islamic innovations consistent with Sharia in order to capitalize on the increased demand for Islamic capital served as a catalyst to draw financing from countries such as Saudi Arabia and Kuwait. Consequently, the Islamic financial institutions using highly innovative banking initiatives.

The phenomenal growth of the Islamic Financial sector is underlined by the fact that there are now about 35 Islamic financial institutions operating in 75 countries, holding assets estimated at more than US$300 billion, and approximately 15 percent per annum and it is projected to grow considerably in the foreseeable future, given developed according to the tenets of the Sharia, the legal and ethical code of Islam and the existence of multinational financial institutions are increasingly becoming actively involved in the sector. According to Islamic banks, Islamic investment companies, Islamic insurance companies, asset management companies, e-commerce, and brokers and dealers to cater for current and future needs. As for principles, insurance products, mutual funds and unit trusts, Islamic bonds, and Sharia compliant stocks.

**Perceived benefits of Islamic banking**

It has been identified despite the license given by the central bank of Nigeria to operate Islamic banking the country does not provide favorable legal climate for Islamic banks to thrive in Nigeria and that dearth of personnel trained in Islamic banking activities and absence of standard Islamic accounting and auditing agreement that some factors might impede the development system of Islamic banking system in Nigeria (Alanamu, 2004). While we identified by Alanamu may not be taken with all seriousness and sincerity, as they are not applicable to for Islamic banks to thrive successfully in Nigeria. Some of them include: the global success of the Islamic banks; the recent global economic meltdown; foreign assistance and Islamic finance courses in Nigerian universities and so on.

Islamic banking is equally important to the Nigerian economy as its acceptance and operation will bring drastic reduction in inflation and also enhance better and efficient income distribution thereby reducing the gap between the rich and the poor (Yahaya 2003).

**The prospect of Islamic banking**

a. The Islamic finance industry is a multi-billion dollar industry developing a global reach and momentum. Following the banking sector consolidation, Nigerian banks have developed a heightened appetite to operate on the global stage which raises the prospect of strategic partnerships and linkages with other global financial institutions offering Islamic financial services.

b. The economic reforms and favorable ratings by global rating institutions have improved Nigeria's profile as a viable investment destination.
c. An interesting fall-out of the global financial crisis is the growing interest and demand for Islamic financial products and services across the world. Amid the crisis, Islamic financial institutions have displayed strong resilience reflecting their conservative approach to business and focus on the basics of financial intermediation as opposed to innovation. This is a positive that could feed into the judgment and preference of Nigerians for Islamic banking as an alternative form of financial intermediation.

d. The on-going financial sector reforms have significantly stabilized and restored confidence in the Nigerian financial system. Islamic banks are expected to benefit from this renewed confidence and stable financial environment.

e. The Zero-interest regime in Islamic banking offers a veritable incentive and attractive option for investors who are strangled by the high lending rates charged by conventional banks.

f. There is a growing preference for ethical investments, products and services by discerning Muslims and Non-Muslims alike. Islamic banking is considered compatible with the ethical orientation and beliefs of this class of people.

g. The licensing of Lotus Capital Plc, the first Islamic capital market operator, by the Securities and Exchange Commission. The successful Initial Public Offer of the company is evidence of the growing popularity and acceptance by Nigerians of Islamic finance as a value proposition.

h. The rapid development and increasing wealth in the Middle East is driving appetite for assets in the region and other parts of the world. Given the positive market environment and latent opportunities in Nigeria, we anticipate that Nigeria will be seen as a safe haven for investors.

i. New techniques in Islamic banking and finance are providing acceptable alternatives to conventional finance, making it possible for investors and corporate to access capital from a growing pool of Islamic liquidity globally and invest in Islamic products.

j. Large number of unbanked Muslim community in Nigeria may be attracted to this type of specialized banking system and get bankable.

k. Implementation of Non-interest Banking would allow people to have different credit choice among different types of banking structures in Nigeria.

l. Development funds. This will allow Nigerian Government and corporate organisations to have access to Islamic development funds available in the international community to finance infrastructural projects.

m. It encourages Muslim communities to invest locally rather than sending their investment to the Middle East.

The Challenges facing Islamic banking in Nigeria

a. Depth of knowledge, skills and technical capacity to regulate, and supervise Islamic banks.

b. Inadequate of Sharia-compliant liquidity management instruments

c. Absence of Islamic insurance (Takaful) to protect investments of Islamic banks against unforeseen hazards and facilitate the growth of the industry respectively.
Absence of deposit insurance scheme for the protection of depositors of Islamic banks.

Inadequate knowledge of accounting and auditing standards pertinent to Islamic financial institutions.

Inadequate of a robust and comprehensive legal framework, especially at the level of adjudication of conflicts involving Islamic finance contracts, products or entities.

In the discharge of its traditional role of lender of last resort, the CBN provides loans to banks at times of liquidity crunch. Islamic banks cannot legitimately benefit from such a facility because such funds are usually provided on the basis of interest. There is therefore, the need to devise and implement an interest-free framework for such assistance.

Dearth of Sharia scholars knowledgeable in conventional economics, law, accounting, banking and finance, which places severe constraints on the regulatory Sharia-compliance mechanism.

Double taxation that would be levied on Islamic banks as a result of stamp duties and capital gains tax those are deductible upon asset transfer.

Another challenge in the area of taxation is that profits generated from the financial instruments offered by Islamic banks are not given the tax relief enjoyed by debt instruments in conventional finance.

There is a lot of misperception about Islamic banking in Nigeria, and with the ethno-religious diversity of Nigeria, it makes it imperative to create mass awareness and acceptance.

Organizational stakeholders expectations

Curtice (2006) defines a stakeholder as an individual or group that can heavily influence the performance of the organization that is, whose support the organization needs if it is to be successful. Organizations do not operate in a vacuum so they say. Every decision that managers make and every action that an organization takes affects those around it. In a similar way, the organization is affected by those who have contact with it. Some of these interactions, according to Fry et al (1998) are exciting troublesome, controllable/uncontrollable, limited in impacts and may have significant long run effects. In other words, a stakeholder is a person or group that has some claim on or expectation of how an organization should operate. The model for a successful organization shows how important stakeholders are.

Classification of stakeholders: There seems to be as many classifications of stakeholders as there are organizations Duggin, (2012). For this paper, Fry et al classification is useful. They classify organizational stakeholders into primary stakeholders and secondary stakeholders.

Primary stakeholders: Are those stakeholders whom an organization affects and interact with most directly. They are:

- The owners of the organization,
- The organization’s customers,
- Employees

They are generally referred to as the “Big Three”. For most business organizations, these three are by far the most important and the scope of the performance measurement is usually focused on them.

Secondary stakeholders: They are those whom the business affects in an indirect or limited way. These include the following:

- Suppliers
- Regulatory authorities
- Former employees
- The community
- Health agencies
- Industry in which the business operates
- Special interest group
- Disabled (physically challenged) people
- Government
- Unions
- Creditors
- Research institutions
- Environment
- Non-governmental organizations
- Other businesses
- Widows (and widowers)
The media
Society in general

Although the organization may not have direct contact with secondary stakeholders on a day-to-day basis, managers must recognize the importance of these stakeholders and their expectations.

Stakeholder expectation/responsibilities: As earlier noted, recognizing the interactions or links between organization and its stakeholders is critical to understanding how the organization (business) and stakeholders interact and affect each other is a unique characteristics of a free market economy. In a command (planned) economy, only one stakeholder group—the government dictates how a business operates. The government further decides production quantity, quality and prices. In a free market economy however, the picture is dramatically different. For example, owners (investors) provide capital; customers influence the volume, quality, models, colours and options that are produced, and competitors influence prices, designs and distribution; government is involved in product, employees and environment safety. Unions affect salaries, wages and working conditions; suppliers affect costs (and prices in turn). All these stakeholders interact to comprise what is known as the free market business system. A defect in the system affects all primary stakeholder and to varying degrees, the secondary stakeholders too.

Stakeholders provide organizations with the capacity to operate. Customers make the purchase that enables the business organization to generate revenue necessary for survival. Employees are the resources necessary to produce products and provide services with quality and efficiency. Communities provide the conducive atmosphere and facilities that help the business attract talented people and keep them happy.

But each of these stakeholders has certain expectations of the business organization. They realize that the organization, to some degree, depends on them to innovate and accomplish goals, so they find it reasonable to place certain expectations (demands or claims) on the organization. For this paper, the expectations of the 'Big Three', for example, are hereby summarized as posited by Curtice (2006) and Fry et al. (1998).

Owner's expectations
- Return on investment
- Organizational stability
- Organizational success
- Liquidity of investment
- Desired attention
- Goal accomplishment

Customer's expectations
- Quality of product
- Choice
- Safety
- Quality of services
- Communication
- Respect

Employee's expectations
- Fair compensation
- Pleasant work environment
- Career development
- Harmonious relationships
- Conducive and safe work conditions
- Procedural justice
- Stability of tenure

Furthermore, suppliers expect good business relations, fair price for raw materials (goods) and on-time payment, while the communities expect business support in form of social responsibility programmes and so on.

Stakeholders should be clearly defined especially if there is any potential question of who is included in each group. Organizational managers must have a balanced approach to these expectations. The implication of the balance approach is that the organization cannot satisfy one stakeholder at the expense of another. For example, customers are very important, but in the long run if an organization's employees are disgruntled, they will not provide the levels of services necessary to satisfy the customers. In the same manner, reducing process to attract more customers may not be sustainable from the owner's viewpoint. There must be a balanced approach to satisfy these expectations.

The organization must recognize its responsibility to address stakeholder expectations. This involves looking at what Fry et al. referred to as "Capacity-stakeholder expectations - business responsibility" framework and trying to determine the best to make it all fit together in order to achieve an effective organizational (corporate) performance.

METHODOLOGY
The paper is descriptive in nature and takes its roots largely from the works of Siddiqi (2001), Nik et al. (2003), Warde (2001), Fry et al. (1998), Basitu (2012) and Chapra & Ahmed (2012) for finding and recommendations.
from the reviews above, the paper found that Islamic banking system has been well accepted worldwide. It has led to improvement in economies of many nations and its introduction in Nigeria would improve the economy socially, politically and culturally.

CONCLUSION

From the Nigerian perspective, stakeholders expect so much from the Islamic banking system. The most important expectation is that of an interest-free banking. Based on sound Islamic principles, the bank advocate among others, and fair distribution of wealth, ethical (lawful) business and stakeholder-participation on viable projects and so on. The various claimers on the other hand place a lot of expectations in form of stability (economic) and goal accomplishment from the system.

RECOMMENDATIONS

In line with the objectives of the paper, it is recommended that:

Islamic banking as an alternative banking system should be encourage and given the necessary stable environment to operate on Islamic principles.

As the bank operates, the various and complex expectations placed on it by stakeholders should be prioritized for a more useful banking operations that would further enhance financial and sustainable economic development in Nigeria.

REFERENCES


Muhammad, T. U. (2008), An Introduction to Islamic Finance, Idara Ishaat ediyat International New Delhi, India.
Nik Norzul et al. (2003), Law and practice of Islamic banking and finance, Malaysia: Sweet and Maxwell Asia.


Yahaya T. (2005), Islamic Banking Interest-free. Aminu schools of Islamic legal studies, Kano.


Portonovacon2012 C. E. Morgan E-mail: octobercon2012@rubna.com