

Financial Analysis Problems in Specialized Islamic Bank

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Abstract

This study is one of very few studies which have investigated financial analysis problems in specialized Islamic Bank to evaluate its financial analysis report. It gives less fair result not correct result to customers, shareholders, suppliers and center bank. Search found that financial report with fair result depend on many factors. It showed financial analysis report problems to meet global rules as Basel rules. Specialized Islamic Banks financial analysis have difference factors than traditional Banks financial analysis as result to Islamic rules also it has some factors affect in the same way as in any bank as result to center bank rules. Islamic bank profitability index shows these differences and similarities which need adjusted in financial ratios and financial analysis problems classification. It can be clarified by discuss financial tables accounting data problems to understand financial analysis tools problems.

Key Words: *Financial Analysis, Islamic bank, Accounting, Problem and Risk.*

Introduction

Islamic bans cause changing in banking sector. It affects now on economic as result to deal with new services. This will affect on customers, companies and government. (Will and Amana, 2011) concentrated on general budget management affected by strategy and structural changing in the public sector and time of needs in long term, short term and medium term. Islamic bank try to cover these needs by give many services with out dealing with interest on loan as other banks. It aims theoretical to build real producing economic.(Thomas, 2011) explained the standard of success tools types is to finance and invest up to suitable time with suitable cost so there must be financing tool, investment tools and saving tools to make money staying. Islamic bank services show resources of returns and show ways to cover needs.

Practically, Success of Islamic banks limit by financial Analysis problems which lead to unfair information to managers, sharers, government, suppliers and customers as individuals or companies. Accounting, strategy and financial analysis tools affect on fair degree. Its data transparency causes problems. Experts financial need data with explain to under stand company accounting and managing. These needs increase when financial analyst and accounting auditor are from out of company as external experts. Different environment may increase this problem or decrease it which depend on the way of factors directing affection. Islamic banks show this case of similar factors impact as traditional bank and show different factors impact as result to Islamic rules. Islamic banks may classified as result to have some branches which give Islamic services or it may be banks which give Islamic services with traditional services up to customer needs. Some center banks rule Islamic banks to give just Islamic services as Specialized Islamic Bank to avoid banks that give loan with interest services to gather with Islamic loan services. It is important for center bank controlling and classified rules managing which affect on financial result and analysis.

The Problem

As any profit organization, Islamic bank financial Analysis problems comes as result to deliberate mistake as result to crime or non-deliberate mistake as result to weak experiences. Problems are repeated even after using computer accounting and financial programs. Ex: Program maker or user can make changes on distributed profits for shareholders as reduce 5% of distributed return and get the 5% by check to placebo person to get these returns. By time many factors show financial analysis problems as result to depending on accounting and managing strategy with limit data. Search problem concentrate on financial analysis problems in specialized Islamic Bank in order to find financial tables accounting data problems and financial analysis tools problems. The other problem comes as result to success Islamic rules applying practically.

The Importance

Define financial analysis problems and classified will affect on financial result to be fair. It show the different financial analysis between traditional banks, Traditional banks which have some Islamic branches and specialized Islamic banks. Explanation will give cases show different in accounting, risks, risks managing and financial tools. It explain the real different needs for specialized Islamic bank financial analysis as different ratios and different standards which help to apply international Basel agreement on these banks also direct financial analysis result to be useful and fair for supplier, shareholders and customers.

The Objectives

This search aims to find financial analysis problems in Specialized Islamic Bank as follow:

- 1- To find difference factors affect on specialized Islamic bank rather than traditional financial analysis.
- 2- To find financial tables accounting data problems as result to show success of entry data in financial analysis.
- 3- To find financial analysis tools problems as result to show financial analysis tools improving to meet different cases.
- 4- To find the effect of success Islamic rules applying on financial analysis.

Literature Review

There is studies show different needs for Islamic banks than traditional banks depending on financial results but these result need prove. (M. Kabir and abdel-hameed, 2002) explained that financial environment affect on performance of Islamic banks and Islamic bank must have big capital to achieve suitable profit as result to different case of real investing which obligate affect on standard of capital/assets ratio. (Suden,2004) found there are facts affect on Islamic bank from internal and external environment which affect on profit. He found that suitable percentage of profit sharing between bank and depositors beside money supply to finance investment at suitable time can increase profit .(Muhammed,2009) showed that partner must accept profit sharing ratio to finance bank equity. (Zubair, 2008) he showed the Islamic bank profit sharing ratio affect on customers and bank and cleared that interest rate lead Traditional Banks to increase profit than Islamic banks as result to get financial leverage. (Essayed, 2013) had tried to show differences between Islamic banks and Traditional banks before, during and after the financial crises in 2008 by financial ratios. There were different in liquidity, credit, risks, profitability and solvency. (Pierre, 2013) showed the important of financial statements which must be done up to suggest model. The model recalculates certain financial statement figures to what it could have been. This can make comparing between current statement and expect statement. (Heinze, Uhlmann and Diermeier, 2014) Explained the important to evaluate companies in crises because there possibility of loss even it has good reputation..

They show that a company which faces crises can reestablish trust with shareholders by announcing an independent investigation by third party.

Difference factors effect on specialized Islamic bank and traditional financial analysis

Profitability index can be divided to three major groups of ratios. As follow:

First: Profitability index in company shows factors effect on gross profit, operating profit and net profit which show in income statement therefore profitability index take care of expenses and costs to reach best amount of profit.

Second: Profitability index shows increased or decreased as result to assets increasing price or growth as animal breeding projects as in Islamic banks or reducing of liabilities which show in balance sheet.

Third: Profitability index shows relationship between income cost with return and mix assets, liabilities with equities. It relates factors that show in income statement with distribution of balance sheet factors.

Traditional profitability index shows those three divisions of rations groups but as result to differences and similar factors between Traditions banks and Islamic Banks there is limits to accept all traditional profitability index divisions as follow:

- 1- It refuses index: as percentage of interest revenue to net profit after taxes.
- 2- It adjusts index: as stores market value to assets market value in case the Islamic bank own stores for selling services.
- 3- It adds index: as result to selling goods with owning store, Add gross profit margin percentage= (sales – cost of goods sold)/ Sales. (Lawrence, 2000)
- 4- It accepts index with limits (Valentine, Calvin and Lilian, 2009), see next table.

Table no (2): Islamic bank Profitability index major division and acceptance as Traditional banks

| Profitability index Major Division | Acceptance |
|---|--|
| Return on Equity = (net profit after taxes/equity) | accept index |
| Return on Assets = (net profit after taxes/assets value) | accept index but assets value must be as in market price not as it cost as result to Islamic rules to apply obligate charity (Zakat) |
| Assets value increasing = Assets cost value – Assets market price value | accept index |
| Du Pont Analysis =(net profit after taxes/assets value)=(net profit after taxes/operation profit) operation profit /assets value)×(| accept index but assets value must be as in market price not as it cost as result to Islamic rules to apply obligate charity (Zakat) |
| Market power = (individual bank loans /country domestic credit) | accept index if Islamic bank gives sales services and lease services by credit |
| Profitability credit risk = Loan /deposit | accept index if Islamic bank gives sales services and lease services by credit |

The difference between Islamic banks and Traditional bank is shown up to liabilities as investment deposit operation and assets mix. It gives idea that Islamic banks is investment company with out interest rate and dealing with direct investment and indirect investment up to Islamic rules see next tables.(as in Bait Tamuil Islamic bank in Kuwait).

Table no (3): Islamic bank balance sheet

| | |
|--|--|
| Current Assets: avoid inters rate 40000 | Liabilities: up to profit sharing 60000 |
| 1- Sharing 10000 | 1-Investment deposits up to 50000 |
| 2- Selling 20000 | Parts of sharing in profit 50000 |
| 3- Leasing 5000 | 2-Current deposit 10000 |
| 4- Services 5000 | (can use limit percentage of deposit as credit with out giving customers profit) |
| 4.1 Transfer services returns 1000 | |
| 4.2 Currency exchange 1000 | |
| 4.3 Commissions 1000 | |
| 4.4 other returns 2000 | |
| Fixed Assets 50000 | Equities: 30000 |
| 1- Building 40000 | avoid lending of shareholders shares and inters rate with out selling preferred shares |
| 2- Stores 10000 | |
| All assets 90000 | Liabilities and Equities 90000 |

Table no (4): Traditional bank balance sheet

| | |
|--|--|
| Current Assets: avoid inters rate 40000 | Liabilities: up to inters rate 60000 |
| 1- Lending up to interest rat 35000 | 1-Investment deposits 50000 |
| 2- Services 5000 | (must give interest rate to customers) |
| 2.1 Transfer services returns 1000 | 2-Current deposit 10000 |
| 2.2 Currency exchange 1000 | (can use limit percentage of deposit as credit with out giving customers profit) |
| 2.3 Commissions 1000 | |
| 2.4 other returns 2000 | |
| Fixed Assets 50000 | Equities: 30000 |
| Buildings with out stores | lending of shareholders shares, deal with inters rate and selling preferred shares |
| All assets 90000 | Liabilities and Equities 90000 |

Specialized Islamic Banks profitability policies

Islamic Banks profitability policies have three major sides. It concentrates on reducing cost, way of calculate profit and way of distribute net profit. Reducing cost is faced by three ways as follow:

- 1- Storing goods but faces storing fire or steal risks.
- 2- To share with commercial companies, agriculture companies, industry companies and services companies which face risk of sharing loosing.
- 3- To sell by credit which faces risk of customer deficit.

As sharing risk and storing risk there are different profitability policies. Cost of storing or sharing must be less than its return to be accepted. Its risk is different from bank to other and from country to other. The three ways affect on investment operations services. More costly will lead to less sales of investment operations. Ex: Morabaha is selling contract with profit. It is one of sales services but if customer find companies price more cheaply he will not deal with Islamic bank until it gives good conditions of selling by credit. Way of calculate profit may increase profitability than competition or it may be done as other competition banks. Ex: Morabaha is selling contract. It equals cost plus expected profit. Expecting profit may be fixed amount of cash as follow:

- 1- Price can be show by added profit on cost as $(1000\$ \text{ cost} + 100 \text{ profit}) = 1100\$$.
- 2- Price can be show by added percentage of profit on cost as $(1000\$ \text{ cost} + 10\% \text{ of cost as profit}) = 1100\$$.

Islamic bank can apply same percentage of interest rate as in traditional banks and up to credit risks to face competition there fore if traditional bank gives credit 2000\$ with interest rate and risk percentage = 15%. Islamic bank will apply profit to equal 15%.

0.15)= 2300\$.×as result to this percentage sales price by credit will = 2000\$ cost + (2000 It keeps customer dealing with Islamic bank. As result to services demand increasing Islamic bank can increase profit to be 0.25. This mean price will= 2500\$. The services have many ways to be calculated which affect on profitability as follow table (Abdullah and Raid, 2009).

Table no (5): Mourabaha calculating profit

| Mourabaha Operation | Ways example | Profitability calculated |
|--|---|---|
| Selling by profit over the cost | Goods cost in <u>market</u> and its risk of damage = 2000\$ + profit = 200 Goods price =2200 | 200\$ Less risk |
| Selling by profit over the cost | Goods cost in bank <u>store</u> and its risk of damage cost beside storing cost = 2000\$ + profit = 200 Goods price =2200 | 200\$ More risk |
| Selling by profit over the cost | Goods cost in bank <u>commercial companies sharers</u> and its risk of damage cost beside storing cost = 2000\$ +profit = 200 Goods price =2200 | 200\$ Sharing risk with sharer and also Sharing profit |

Finally, Islamic bank profitability is affected by profit percentage of sharing returns. Islamic bank considers sharing investment deposit as sharing. Islamic bank profit distributed may manage as following:

(Returns which come by part of bank sharing in investment by capital and effort with investment deposit)

Less (-)

Costs

Less(-)

Reserves

Distributed profit

Customer part of profit

Islamic bank get two types of returns. Bank is one of partner get share return in distribute profit it share by effort and capital to gather + Collecting return from banking services as effort returns

This profitability policy will give bank less profit than the follow profitability policy. (Returns which come by part of bank sharing in investment only by effort with investment deposit)

Less (-)

Costs

Less(-)

Reserves

Distributed profit

Customer part of profit

Islamic bank get three types of returns. Bank get part of distributed profit as return of effort managing investment + Collecting return from banking services returns as effort return + Collecting returns from investment financed by bank capital as sharing in capital return

Percentage of distributed profit between bank and depositors also can increase Islamic bank profitability or reduce up to investment return demand and negotiation with customers.

Specialized Islamic Bank Financial Analysis Problems

Advantage of financial analysis comes from giving better understanding about current financial position of business and helps to planning for success in future. Analysis must cover every unit in company until it covers all company financial analysis (Pierre, 2013). There is two types of financial analysis problems which are type of same problems of financial analysis between any bank as result to center bank rules and company rules but the other type of problems comes as result to difference factors affect on traditional banks and specialized Islamic bank. As result to these factors financial analysis problems can be summarized as in the next figure:

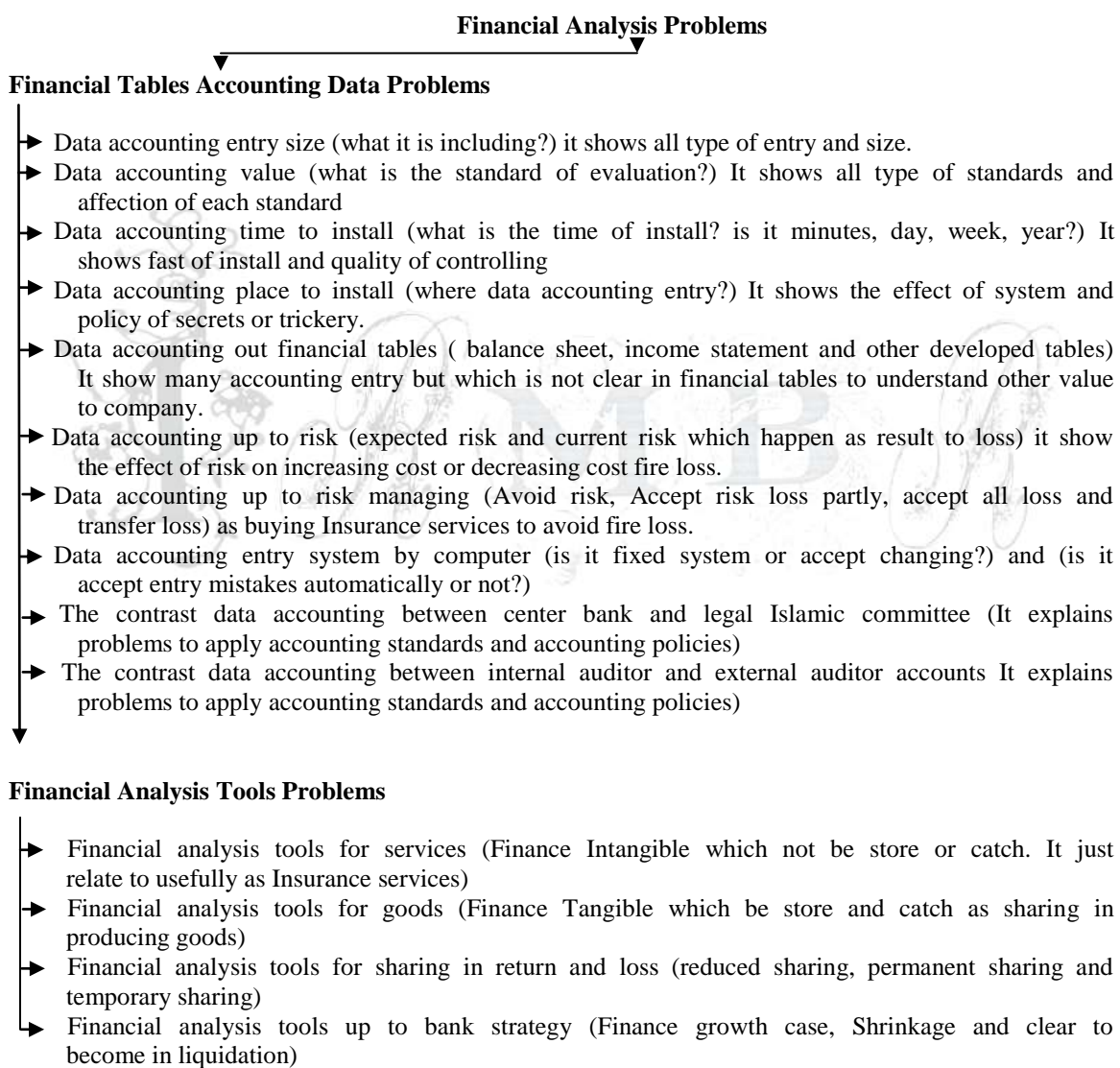


Figure1: Financial Analysis Problems Classification

This figure shows financial analysis problems resources. These resources affected by three rules which are show as follow:

- 1- Center bank rules.
- 2- Islamic rules.
- 3- Bank managing rules.

These rules control financial analysis problems practically. Islamic rules direct accounting entry data as result to Islamic legal committee. It is the major standards of specialized Islamic bank accounting and financial managing while bank managing use flexibility of Islamic rules to work but Center Bank is the real ruler of all banks. Financial analysis problems increase in case there is discrepancy between them. Islamic bank can direct traditional services up to some changes as, Ex: Internet as developed way to give Islamic bank services may get in fraud, viruses and embezzlement. There must be require part of bank capital to face the operation services risk as Basel agreement order. (Mona, Dixie and Elizabeth, 2005). Islamic bank become marketer of internet services as buyer but with commission because this service is managed by traditional organization.

Conclusion

This study is one of very few studies which have investigated financial analysis problems in specialized Islamic Bank to evaluate its financial analysis report. It gives less fair result not correct result to customers, shareholders, suppliers and center bank. Search found that financial report with fair result depend on many factors. It showed financial analysis report problems to meet global rules as Basel rules. Some of these factors are impact as in any traditional bank or organization while other factors come as result to add Islamic standards which obligated practically by Islamic legal committee. This explained that financial analysis problems cause needing new standards to depend accounting data and different financial ratios analysis in order to make financial report more useful practically locally and internationally. Specialized Islamic Banks financial analysis have difference factors than traditional Banks financial analysis as result to Islamic rules also it has some factors affect in the same way as in any bank as result to center bank rules. Islamic bank profitability index shows these differences and similarities which need adjusted in financial ratios and financial analysis problems classification. It can be clarified by discuss financial tables accounting data problems to understand financial analysis tools problems.

Recommendation

It is important to understand financial analysis problems but practically it needs reference for analysts as agenda to work therefore researcher suggest to follow Figure1: Financial Analysis Problems Classification. This figure explains financial analysis problems as factors.

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