

Chapter 4

Financial Performance of IBS during 1996-2000

4.1 Introduction

We may now analyse the performance of foreign banks' SPI operations in detail. As mentioned earlier, the data available for our investigation is that from 1996 onwards, as the financial statements of the Islamic banking operations in conventional banks are only reported beginning from that year. As such, we will study the performance of foreign banks' SPI operations from 1996 to 2000, a period that is significant to a banking study. During this period, most banks in Asia – including foreign banks in Malaysia, experienced such a great instability, largely due to regional crisis. The crisis, famously known as Asian Crisis, that struck throughout 1997-98 hit most Asian countries with the more severe ones are Thailand, South Korea, Indonesia, Philippines and, to a lesser degree, Malaysia.

Given this unfortunate event, the financial sector suffered the most where bank failure was a common phenomenon. It is, therefore, interesting to investigate whether Islamic banking suffered a similar fate during this crisis; or in the case of SPI, whether the crisis had adversely affected the operations of Islamic banking at foreign banks under study. There are two methods used in this study, one is trend analysis and the other is ratio analysis.

These two methods are used following a similar study done by another researcher (Iqbal, 2001), covering 12 Islamic banks in ten Muslim countries. Although the scope and magnitude of this study are smaller than Iqbal's, the analysis of both studies would significantly contribute to the empirical-study literature on Islamic banking. While Iqbal focuses on performance of several Islamic banks versus

conventional ones, this study would compare the performance of Islamic banking operations at foreign banks versus conventional operations of the same banks.

Likewise, despite the similarity of the methods used, trend and ratio analysis, but the scope of analysis is different. Iqbal's is broader, since, for instance, it includes profitability (including return on equity) ratios, capital asset ratio (CAR), liquidity Ratio, deployment ratio and few others in his analysis; while this study is not as extensive. Nevertheless, this would not hinder the good analysis to come out from the present study, since all of the above analysis/ratios might not be relevant when we study a division of a firm (i.e., Islamic banking division).

4.2 Trend Analysis

Here we will look into some indicators or trends from the operations of Islamic banking at foreign banks. Trend analysis looks at performance of the bank over a number of years to examine long-term performance (Hirt & Block, 1999). The indicators that we will use are growth rate of deposits, financing, and assets. It is perhaps the most convenient way to track down the banks' record and performance during the stated period, given the availability of data and ease of analysis. However, this analysis might not reflect the true state of affairs of the banks under study, i.e., profitability. Thereby, trend analysis is complimented by the ratio analysis later.

4.2.1 Deposits growth in Islamic banking

During 1996-2000, the Islamic banking sector enjoyed a robust and sustainable growth, particularly in deposits mobilisations. Over the period, as we will

see in Table 2, deposits mobilised by Islamic banking sector grew more than 46% annually.⁶³

In fact, during and post the Asian Crisis or during 1998 and 1999, deposit mobilisation grew even faster compared to any other period. It may suggest that Islamic banking remained resilient even during the hard time, where other banks are suffering from insolvency and lost of credibility. This is evident from the higher growth rate recorded by most foreign banks under study and, apparently, by the two Islamic banks (BIMB and Bank Muamalat). As such, Islamic banking as a whole grew at 53% during 1998 and 62% during 1999.

Table 2
Deposits growth in percentage

Banks/SPI	1997	1998	1999	2000	Yearly Average
Islamic banking	36%	53%	62%	34%	46%
Islamic banks+	-2%	25%	138%	16%	44%
SPI	68%	67%	35%	45%	54%
HSBC	63%	10%	34%	21%	32%
OCBC	80%	88%	545%	16%	182%
SCBMB	106%	68%	87%	-32%	57%

Notes: + Consist of Bank Islam and Bank Muamalat (starting 1999).
- Base year for this table is 1996.

Source: - BNM Annual Reports.
- Banks' Annual Report/Financial Statements.

Table 2 also shows that total deposits of the overall Islamic banking sector have been growing strongly over the period of 1996-2000. On average, SPI's growth rate is higher than that of Islamic banks annually. While Bank Islam & Bank Muamalat combined grew at an average of 44% per annum, SPI recorded an impressive 54% growth rate in deposits mobilization during the same period. In fact, SPI also grew faster than the overall Islamic banking sector (46%) in deposit mobilisations.

⁶³ Based on BNM Annual Reports.

However, the most remarkable rate is recorded by OCBC, as can be seen in the same table. On average, OCBC's deposits collection grew at more than 180% per annum during 1997-2000. The highest growth rate was recorded in 1998-99, the year of the Asian crisis. It can be concluded from the event that there was a huge migration of funds into Islamic banking division of OCBC during the crisis. And this influx is from external customers, not from OCBC's conventional counters.⁶⁴ This indicates that, one; OCBC is a solid bank and remained resilient even during the crisis, although its total deposits slightly decreased during the period of 1998-99; OCBC's Islamic banking new depositors are mostly Chinese who have found that during the crisis, it is more profitable to bank with Islamic banking.⁶⁵

It should also be noted, though, that in 2000 most banks' deposits were growing rather slowly than other periods. In fact, in the case of SCBMB, the growth rate was negative.

In nominal terms, we also found that Islamic banking has been able to absorb more than RM 32 billion as at the end of 2000. On average, Islamic banking mobilised almost RM 18 billion annually during the period of 1996-2000. Table 3 also reveals that the share of deposits absorbed by Islamic banks to the total deposits has been decreasing over the years. At the peak of the crisis, which is 1998, Islamic banks only mobilised some 27% of the total deposits collected by the Islamic banking sector. However, with the opening of Bank Muamalat as the second Islamic bank in 1999, the Islamic banks' share increased to 39% in 1999.

⁶⁴ Interview. OCBC's total deposits collection during the period are: 1997 RM12,706 million, 1998 RM11,228 million, 1999 RM12,672 million, and 2000 RM13,515 million.

⁶⁵ *Ibid.*

Table 3

Deposits mobilisation by Islamic banking

Banks/SPI	1996 (RM'000)	1997 (RM'000)	1998 (RM'000)	1999 (RM'000)	2000 (RM'000)
Islamic Banking	7,264,146	9,895,393	15,172,080	24,637,548	32,966,810
Islamic Banks	3,283,289	3,223,440	4,039,747	9,611,697	11,108,348
- Overall share (%)	45.2	32.58	26.63	39.01	33.70
SPI	3,980,857	6,671,953	11,132,333	15,025,851	21,858,462
- Overall Share (%)	54.8	67.42	73.37	60.99	66.30

Source: - Bank Negara Malaysia. *Annual Reports*

- Annual Reports of each banks.

- Bank Negara's web site: www.bnm.gov.my/IslamicBanking/statistics

As Table 3 indicates, it was during this period that SPI overtook the Islamic banks in mobilising funds from the public. In 1995, SPI (or SPTF, as it was known then) only absorbed some RM 2.18 billion while the Islamic bank (at the time, only BIMB) mobilised more than RM 2.7 billion. The figure was even more in favour of the Islamic Bank when SPTF was introduced in 1993. SPTF mobilised only RM 246 million, while the Islamic bank collected more than RM 2 billion. However, starting from 1996, SPI has been able to absorb more funds from the public than the Islamic banks.⁶⁶

This is interesting, and explains a lot why SPI is an important factor for the development of Islamic banking in Malaysia. The rise of SPI, in terms of deposits mobilisation, also indicates that the increasing majority of Islamic banking patrons are those not explained by, among others, Kader (1993, 1995). Namely the strict and pious Muslims who totally avoid the *riba* banks; the less strict Muslims who hold accounts both at BIMB and interest-based banks; and the least strict Muslims who only patronize conventional banks (products).⁶⁷ It may suggest that, the latter category might have now adopted Islamic banking instead of conventional. The other

⁶⁶ BNM, *Annual Reports*.

⁶⁷ See, for instance, Radiah (1995) in *Leading Issues in Islamic Banking and Finance*. Pp 103-5.

possibility is the increasing numbers of non-Muslims adopting Islamic banking system.

Aside from that, the number of SPI participants also explains this phenomenon. In 1993, only a handful of commercial banks and finance companies participated in SPI/SPTF. But two years later, in November 1995, the figure had soared to more than 40, which included commercial banks, merchant banks and finance companies. Among these institutions, all three foreign banks under study were already in the SPTF by 1995, whereby SCBMB was the first foreign bank to join the scheme in 1993.⁶⁸

4.2.2 Deposits growth at foreign banks

Total Deposits

One obvious fact about deposit mobilisation by Islamic banking is that it has been steadily increasing over the period of study. In the case of Islamic banks, the amount of deposits mobilised from their customers has been relatively lower than that of SPI, since 1996. In fact, the difference between SPI deposits and Islamic banks has widened over the period.

In Table 4, we will look into the proportion of foreign banks SPI deposits to the overall Islamic banking and SPI deposits. This comparison is aimed at evaluating the significance of SPI operations at the foreign banks relative to the Islamic banking sector performance at large.

⁶⁸ See Yakcop (1996). Pp. 65-57.

Table 4

Deposits growth of Islamic banking at foreign banks

Assets/SPI	1996 (RM'000)	1997 (RM'000)	1998 (RM'000)	1999 (RM'000)	2000 (RM'000)
Islamic Banking	7,264,146	9,895,393	15,172,080	24,637,548	32,966,810
Foreign Banks	3,283,289	3,223,440	4,039,747	9,611,697	11,108,348
	3,980,857	6,671,953	11,132,333	15,025,851	21,858,462
	15,110	24,601	27,138	36,231	44,003
Share of Islamic Banking to SPI^	0.21%	0.25%	0.18%	0.15%	0.13%
Share of Foreign Banks to SPI*	0.38%	0.37%	0.24%	0.24%	0.20%
	14,494	26,074	49,074	316,517	366,114
Share of Islamic Banking to SPI^	0.20%	0.26%	0.32%	1.28%	1.11%
Share of Foreign Banks to SPI*	0.36%	0.39%	0.44%	2.11%	1.67%
B	13,352	27,554	46,220	86,279	58,913
Share of Islamic Banking to SPI^	0.18%	0.28%	0.30%	0.35%	0.18%
Share of Foreign Banks to SPI*	0.33%	0.41%	0.41%	0.57%	0.27%
Number of banks#	42,956	78,229	122,432	439,027	469,030
Share of Islamic Banking to SPI^	0.59%	0.79%	0.81%	1.78%	1.42%
Share of Foreign Banks to SPI*	1.08%	1.17%	1.10%	2.92%	2.14%

Source: - Bank Negara Malaysia. *Annual Reports*

- Annual Reports of each banks.

- Bank Negara's web site: www.bnm.gov.my/IslamicBanking/statistics

Notes: ^ Share of foreign banks SPI to overall Islamic banking deposit.

* Share of foreign banks SPI to overall SPI deposits.

All the three foreign banks combined.

In general, we found that the contribution of foreign banks' SPI to the Islamic banking sector is still negligible. Their combined deposits were still about 2% of the total deposits absorbed by the Islamic banking sector as a whole. It means that foreign banks' participation, generally, is still insignificant in terms of deposits absorption. The individual foreign bank's share of deposit mobilisation is also extremely low, ranging only from 0.13% to 1.67%. However, over the period, percentage share of deposits among the foreign banks has been increasing, notably at OCBC. OCBC's share of deposits has been growing by about 500% from 1996 to 2000, or from a modest RM 14 million (share of total Islamic banking deposits) in 1996 to almost RM 370 million (1.11%) in 2000. However, the other two foreign banks' share of total deposits have been declining, resulting in a lower share of total deposits in 2000 compared to previous years.

years. In the case of SCBMB, the decrease is significant. In 2000, its share of total deposits was only 0.18%, which is a far cry from 0.35% share it recorded in 1999.

Further, as shown in Table 2 earlier, the growth rate of deposits at foreign banks are relatively higher than the Islamic banking sector in general, except for HSBC. In fact, it is higher than that of Islamic banks and SPI banks. It shows, among others, that foreign banks also enjoyed buoyant market sentiments onto Islamic banking.

However, it is imperative to examine this growth in greater details, particularly whether this healthy growth also reflects the significance of Islamic banking to the banks concerned. This examination is also in line with the target set by BNM to the achievement of Islamic banking operations at SPI institutions, in this case foreign banks.

Table 5

SPI deposits at foreign banks

Bank/Deposit	1996 (RM'000)	1997 (RM'000)	1998 (RM'000)	1999 (RM'000)	2000 (RM'000)
1. HSBC					
a. Overall	12,818,574	17,010,219	16,889,769	18,236,841	19,020,684
b. SPI	15,110	24,601	27,138	36,231	44,003
c. SPI percentage	0.118%	0.145%	0.161%	0.199%	0.231%
2. OCBC					
a. Overall	9,078,698	12,706,119	11,227,975	12,672,393	13,514,938
b. SPI	14,494	26,074	49,095	316,517	366,114
c. SPI percentage	0.160%	0.205%	0.437%	2.50%	2.71%
3. SCBMB					
a. Overall	8,327,975	12,058,493	11,530,755	13,041,569	13,476,562
b. SPI	13,352	27,554	46,220	86,279	58,913
c. SPI percentage	0.160%	0.229%	0.401%	0.662%	0.437%

Source: Annual Reports/Financial Statements.

In Table 5, we found that, only OCBC managed to significantly increase the portion of SPI deposits to its total deposits, year after year. The other two banks, despite enjoying a rather sustainable growth, have not been able to increase the proportion of SPI beyond 1% of their overall deposits. This is somewhat discouraging since BNM has set the target of 5% of SPI contribution to overall banking operations, at the end of 2000. It is now a necessity for these banks, including OCBC, to multiple their efforts in meeting BNM's targets. What more, BNM would like to see this target to be reviewed periodically, in line with the target of 20% by 2010 set in the Financial Sector Master Plan 2001.

Savings & Investment Deposits

With regard to type of deposits, as evident in Table 6, savings is still the largest chunk of the banks portfolio. All the three foreign banks have had a large portion of savings account in their liabilities, although in the case of HSBC and OCBC, the trend has been more in favour of investment deposits, since 1998 and 1999. Nevertheless, savings accounts will continue to absorb more funds in the future, although investment deposits will be tailing behind closely.

It is also interesting to note the surge of investment deposits in 1997 through 1999, or during the Asian crisis. This is so in the case of OCBC, whereby its investment deposits jumped from a modest RM 3 million in 1997 to more than RM 200 million in 1999. In 2000, investment deposits at OCBC has increased further to more than RM 216 million.

Likewise, SCBMB also recorded a similar surge, although to a much lesser degree. In 1997, its investment deposits only constituted about half of the total deposits, but in 1999 rose to almost 75% of all deposits mobilised by its SPI. This is an indication of increasing popularity of Islamic mode of investments among patrons

are longer than five years constitute only a fraction of total deposits, while those with maturity period less than a year are the majority. This is what the foreign banks under study should look into, rather more carefully.

Table 7

Maturity Structure of Investment Deposits

Bank/Maturity	1996 (%)	1997 (%)	1998 (%)	1999 (%)	2000 (%)
HSBC	N/A	N/A	N/A	N/A	N/A
OCBC					
- Within six months	84.56	76.59	53.03	79.29	84.96
- Six months – one year	14.96	20.81	31.26	11.93	13.59
- One – three years	0.43	2.28	14.98	7.57	1.00
- Three – five years	0.05	0.33	0.73	1.21	0.45
SCBMB					
- Within six months		94.22	8.15	98.03	97.25
- Six months – one year		5.40	81.38	1.97	2.62
- One – three years		0.38	10.47	0.00	0.13
- Three – five years		0.00	0.00	0.00	0.00

Source: Annual Reports/Financial Statements

Table 7 above also shows that over the period, most of the investment deposits have been deposited at the banks for less than a year. About 90% of investment deposits are held within one-year period, while those deposits maturing more than three years are extremely small. In fact, for SCBMB, it holds no investment deposits due more than three years. However, interestingly, customers did hold the deposits for a longer period during the crisis years (1998 and 1999). Both OCBC and SCBMB recorded this phenomenon, whereby, the amount of deposits with more than one-year maturity period was higher than the previous period. This is due, among others, to depositors having more confidence to SPI during this period, compared to deposits at other counters, i.e. conventional deposits.⁷⁰

⁷⁰ This is inline with earlier finding on migration of funds from conventional counters to SPI.

Depositors

Lastly, we will look into the proportion of depositors at foreign banks. Although, we cannot ascertain to what ethnic groups these customers belong to, which would actually make this study very interesting, we still can determine whether the majority of customers are individuals or firms/companies. In Table 8, we found that all of the banks have more individual customers/depositors than that of enterprises. However, one interesting finding emerged from the table, which is OCBC's corporate customers have been increasing over the period of 1996-2000, while that of SCBMB have been steadily declining. This may suggest that the two banks have different policy and approach in reaching out for customers; one is trying to tap more of business depositors while the other is trying to get away with them. The reason, however, is not clear, since both banks have never made such deliberate policy on its marketing efforts.

Table 8
Deposits by Type of Customers

<i>Bank/Customers</i>	<i>1996</i>	<i>1997</i>	<i>1998</i>	<i>1999</i>	<i>2000</i>
	<i>(%)</i>	<i>(%)</i>	<i>(%)</i>	<i>(%)</i>	<i>(%)</i>
HSBC					
- Business enterprises	2.17	2.52	1.50	1.63	1.88
- Individuals	80.62	94.77	91.81	90.72	89.97
- Others	17.21	2.71	6.69	7.65	8.15
OBCB					
- Business enterprises	4.48	5.29	7.16	18.01	32.17
- Individuals	90.90	93.23	89.01	79.34	61.04
- Others	4.62	1.48	3.83	2.65	6.79
SCBMB					
- Business enterprises	23.33	16.11	8.15	3.27	2.85
- Individuals	65.35	83.05	81.38	81.63	91.75
- Others	11.32	0.84	10.47	15.10	5.40

Source: Annual Reports/Financial Statements

4.2.3 Financing growth of Islamic banking

Unlike deposit mobilisation, financing by Islamic banking is not as promising, especially among the foreign banks. Whilst there was a jump in the amount of loans extended from 1996 to 1997, the Islamic banking sector's financing suffered a negative growth by 3% in the following year. Among the foreign banks, though, it was only HSBC that had a negative financing growth in 1998, by almost 100%. The rest were enjoying a lofty growth in their investment, despite the crisis and unfavourable general market sentiments.

Table 9

Islamic Financing Growth

Banks/Financing	1997 %	1998 %	1999 %	2000 %	Yearly Average
Islamic Banking	79	-3	27	50	38.25
- Islamic Banks	48	4	38	26	29.00
- SPI	98	-6	22	62	44.00
HSBC	-	-98	100	786850	196713.00
OCBC	69	178	171	52	117.50
SCBMB	-	593	18	-23	147.00

Source: Stream of data.

Nevertheless, the growth of financing of the Islamic banking sector is substantially solid. Overall, the sector enjoyed more than 38% growth in loans and financing disbursement over the period under study. The highest average growth was recorded by HSBC, primarily due to a sudden increase in financing during 2000. However, this does not reflect HSBC's strength since its financing has been extremely low prior to 2000. In fact, it utilised most of SPI deposits on investment securities such as Government investment certificates and Islamic debt securities over this period. Only in 2000 that the proportion of investment securities has been reduced

considerably, but still it constitutes about 71% of its total assets. Compare that with SPI loans and financing which is only 27%.⁷¹

Thus, in general, OCBC fares better in financing performance. Not only that it has grown steadily, but it also has been able to maintain its financing growth at 117% annually⁷². Likewise, SCBCMB is also relatively stable and consistent in its loans and financing disbursement, although, as we will find out later, they are extremely eschewed towards BBA property financing.

In sum, financing growth of Islamic banking has been relatively solid and steady. With the introduction of more financing products and more innovation on the part of participating banks, we hope to see improvements in financing extended by Islamic banking in the near future. The trend showed by the tables below surely supports such optimism.

Table 10

Financing extended by Islamic banking

Banks/Financing	1996 (RM'000)	1997 (RM'000)	1998 (RM'000)	1999 (RM'000)	2000 (RM'000)
Islamic Banking	6,001,731	10,749,351	10,461,223	13,333,299	19,935,424
- Islamic Banks	2,259,069	3,350,689	3,471,438	4,779,379	6,044,102
- SPI	3,742,662	7,398,662	6,989,785	8,553,920	13,891,322
HSBC	-	48	1	2	15,739
OCBC	5,376	9,081	25,223	68,469	104,375
SCBMB	-	5,330	36,915	43,578	33,441

Source: Stream of data.

Table 10 above shows that Islamic banking sector finances and advances have been growing rather progressively. From a mere RM 6 billion in 1996, the financing extended by Islamic banking has increased to almost RM 20 billion in 2000, or a 230% increase. In the case of foreign banks, however, the nominal amount of loans and finances made has been rather modest, compared to the Islamic banking at large.

⁷¹ HSBC, Annual Reports/Financial Statements.

⁷² OCBC, Annual Reports/Financial Statements.

Nevertheless, the increase recorded by all the three banks has been encouraging, if not impressive. OCBC, for instance, its loans and finances have been increasing steadily. From RM 5 million amounts of loans made in 1996, the bank was able to extend more than RM 100 million of financing in 2000. Similarly, the other two banks also recorded an encouraging improvement in their loans and financing over the period, albeit more are expected to come out from them.

4.2.4 Direction of Financing at foreign banks

Another important aspect of Islamic financing is the direction of financing made by foreign banks. In this regard, we first look into this aspect at large. According to BNM Reports, as summarised in Table 11, the property sector has been receiving more than 40% of total lending and financing made by SPI for the period of 1996-2000. It is similarly so for the Islamic banks.⁷³ In total, we find that Islamic banking is heavily eschewed to property financing, particularly such products developed with BBA concept, as has been shown in Chapter 3 (Graph 1).

Table 11

Direction of Financing by Islamic banking

Sector	1996 %	1997 %	1998 %	1999 %	2000 %
1. Broad Property sector	40.3	48.1	41.7	44.9	35.9
2. Consumption credit	12.8	2.7	8.6	15.0	19.4
3. Manufacturing	6.3	7.8	11.8	8.9	9.8
4. Agriculture related	4.3	0.9	1.6	3.6	7.6
5. Electricity, gas & water	0.1	0.2	0.3	1.6	4.1
6. Wholesale, retails, restaurant	5.7	4.2	5.7	5.4	4.1
7. Transport, storage, comm.	7.0	10.0	6.6	5.5	3.8
8. Purchase of securities	-3.8	13.6	7.8	5.4	3.4
9. Finance, insurance & business services	9.3	-5.0	4.2	4.6	2.9
10. Others	18	17.5	11.7	5.1	9
Total	100	100	100	100	100

Source: BNM, *Annual Reports*.

⁷³ BNM, *Annual Reports*.

Thereby it is reasonable to investigate whether this trend is also relevant to the foreign banks, although we might be tempted to assume so. In Table 12, we found that our assumption is not necessarily correct. In the case of HSBC, we found that, surprisingly, no loans have been extended to the property sector thus far. Most of its financing goes to the manufacturing sector, followed by mining and quarrying, general commerce and business services such as insurance and finance. Prior to 2000, HSBC lent exclusively to consumption credits based on the Qardhul Hasan concept, although the amount was negligible.

In contrast, SCBMB seems to find property financing as most profitable. All of its financing went to BBA residential property financing, over this period. It is interesting to note that SCBMB's financing was very high during the crisis, whereby it jumped by more than 500% from the previous period. Sadly, however, the trend is on the decline afterwards. During 2000, SCBMB's financing had gone down by more than 20% from the previous year.

On the other hand, OCBC is quite proportionate in its loans and financing disbursement. Although, property financing is still the favourite, OCBC has found many avenues and projects to invest its monies. Among the sectors that is beginning to embrace Islamic financing are manufacturing, general commerce, business services and agriculture related (including hunting, forestry and fishing).

Table 12

Direction of Financing at foreign banks⁷⁴

Bank/Financing	1996 (RM'000)	1997 (RM'000)	1998 (RM'000)	1999 (RM'000)	2000 (RM'000)
1. HSBC					
- Broad property financing	-	0	0	0	0
- Consumption	-	49	2	3	0
- Manufacturing	-	0	0	0	6,551
- Agriculture related	-	0	0	0	608
- Transport, storage & communication	-	0	0	0	0
- Wholesale, retailers	-	0	0	0	1,704
- Finance, insurance, etc	-	0	0	0	1,300
- Others (including mining & quarrying)	-	0	0	0	5,843
Total	--	49	2	3	16,006
2. OCBC					
- Broad property financing	5,415	9,114	23,666	61,189	87,516
- Consumption	0	0	331	366	367
- Manufacturing	0	0	0	344	8,871
- Agriculture related	0	0	625	1,268	1,160
- Transport, storage & communication	0	0	122	122	378
- Wholesale, retailers	0	0	803	5,986	5,708
- Finance, insurance, etc	0	0	294	281	1,995
- Others	25	146	21	566	1,145
Total	5,440	9,260	25,862	70,122	107,140
3. SCBMB					
- Property financing (housing)	-	5,330	36,915	44,242	34,382
- Others	-	0	0	0	0
Total	-	5,330	36,915	44,242	34,382

Thus we can safely say that broad property financing is still the *primadona* of Islamic banking at large. In the case of foreign banks, this is generally true with an exception of HSBC. This exception, however, is somehow 'compensated' by the 100% property-financing portfolio of SCBMB. In sum, BBA financing and, specifically, property financing will continue to lead in Islamic banking financing for many years ahead.

⁷⁴ The financing figures in this part are before deduction of provisions for bad and doubtful debts & financing.

Financing by Concepts

In terms of concepts, financing by foreign banks is dissimilar. Although BBA is still the favourite, following the application of the concept on broad property financing, other type of products have been increasing, particularly Ijarah/leasing. Table 13 summarises the above statement. As expected, BBA financing consists of more than 90% of foreign banks financing, with exception of HSBC, which does not extend any loans to property sector during 1996-2000. In fact, in the case of SCBMB, all of its financings are for property sector, hence based on BBA.

As mentioned earlier, this trend is widespread among all SPI participants and Islamic banks. This occurrence has been dealt with in details earlier in Chapter 3. However, it should be noted that this trend is not entirely satisfying to some Islamic banking analysts, among others Rosly (1996). He noted that "... (it) is my fear that Islamic financing is not moving towards its goal, namely establishing economic justice. People are still apprehensive about bay' bithaman-ajil (BBA) and murabahah, bay' innah and bay' al-dayn which today are dominant products in interest-free investments. The point is, although these products are said to be permissible (*halal*), it does not necessarily mean that the contracts upon which they are developed are the same too."⁷⁵

Nonetheless, the bank managers argued that it is rather difficult for foreign banks to offer other Islamic products to their customers. Not only that the economic conditions are not favourable, but also, to their customers, BBA financing is the only product that seems to be profitable to them.⁷⁶

⁷⁵ Rosly, Saiful Azhar. *Ijtihad, taqlid and Islamic financing*, in *Business & Islam*, in *The Sun*, May 3, 1996.

⁷⁶ Interviews.

Table 13

Percentage of Financing by Concepts

Bank/Concept	1996	1997	1998	1999	2000
HSBC					
- Al-Ijarah	-	0	0	0	85.62
- Al-Ijarah Thumma Al-Bai	-	0	0	0	8.13
- Al-Qardhul Hasan	-	100	100	100	6.25
OCBC					
- Al-Ijarah	0	0.01	0	0	5.07
- Al-Bai' Bithaman Ajil/BBA	100	99.99	99.95	99.98	94.92
- Al-Qardhul Hasan	0	0	0.05	0.02	0.01
SCBMB					
- Al-Bai' Bithaman Ajil/BBA	-	100	100	100	100

Source: Annual Reports/Financial Statements.

Maturity Structure of Financing

Whilst Table 7 earlier shows the maturity structure of investment deposits, we may now compare it with the maturity structure of financing, which will provide us with necessary information on the banks' liquidity. Table 14 summarizes our findings on the matter. We find that, with the exception HSBC, most of foreign banks financing and loans are long-term, particularly in the property sector. Whilst the percentage has been decreasing for both banks, but the proportion is still extremely high, covering more than 90% of the total financing. In the case of HSBC, the lesser degree of long-term financing reflects its concentration on consumption financing and not that of property financing.

This thrust on long-term financing is somewhat disturbing, since most of these loans and advances are financed by mostly short-term deposits (savings and short-term investment deposits). Although, the banks have been able to meet all their liabilities thus far, this situation might pose the banks with some serious problems in the long run. Thus, it is imperative for these foreign banks to strategize on how to

attract more long-term investments to finance the ever increasing/popular Islamic property financing (i.e., BBA).

Table 14
Maturity structure of financing

Bank/Maturity	1996 (%)	1997 (%)	1998 (%)	1999 (%)	2000 (%)
HSBC					
- Within one year	-	100	100	100	6.25
- One – three years	-	0	0	0	68.84
- Three – five years	-	0	0	0	24.90
- Over five years	-	0	0	0	0
OCBC					
- Within one year	0	0.01	0.45	0.24	0.05
- One – three years	0	0	0	0.43	7.65
- Three – five years	7.76	0	0.46	7.95	8.00
- Over five years	92.24	99.99	99.09	91.40	84.30
SCBMB					
- Within one year	-	0	0	0	0
- One – three years	-	0	0	0.02	1.01
- Three – five years	-	0	0	0.93	1.09
- Over five years	-	100	100	99.05	97.90

Source: Annual Report/Financial Statements.

4.3 Ratio Analysis

Ratio analysis brings together balance sheet and income statement data to permit a better understanding of the bank's past and current health. It is used to weigh and evaluate the operating performance and capital structure of the bank, and any firms for that matter (Hirt & Block, 1999). It is also used to appraise the position of the bank, to identify trouble spots that need attention, and to provide a basis for making projections and forecasts about the course of future operations (Shim & Siegel, 1994).

To Hirt & Block (2000, pp. 216-26), there are about 20 significant financial ratios available to analyse a firm, of which can be classified into six broader categories. They are profitability, asset-utilization, liquidity, debt-utilization, price

and other ratios. In the first instance, profitability ratios, includes operating margin, return on equity, return on assets and profit margin. However, only the last two of profitability ratios that are relevant to this study, apart from constrained by the availability of data.

4.3.1 Return on Assets (ROA)

ROA measures the profitability of the SPI operations at the foreign banks, whereby the banks' own overall operations, i.e. overall ROA, will be used as a benchmark in this analysis. In other words, it is measuring the foreign banks' SPI profitability relative to their overall profitability. However, this analysis will be complimented by the comparison across the Islamic banking sector at large. This is to put this study in a broader and meaningful perspective.

ROA is measured as a ratio of net income over total assets at a given period;

$$\text{Return on Assets} = \frac{\text{Net income}}{\text{Total Assets}}$$

Table 9 reveals that SPI's return on assets is slightly better than the overall ROAs of the foreign banks. The highest ROA for SPI was recorded by HSBC, average of 2.52% during 1996-2000, followed by OCBC 1.395% and SCBMB by 0.834% during the same period. It should be noted that, during this period, all foreign banks' SPI enjoyed a positive ROA throughout, while its overall ROAs were not so. In the case of HSBC, it suffered a negative ROA during the 1998 and 1999, which is the peak of, and post, Asian crisis.

Interestingly, the banks SPI's ROAs are relatively high during the Asian crisis or 1998, compared to the previous year. The highest was recorded by HSBC by more than 3 percent, followed by OCBC and SCBMB. In fact, the ROA of SPI operations have been high during the period of 1996-2000. Thus, we can conclude that SPI

operations of the foreign banks have been profitable from the beginning and throughout the period of this study

Table 14

Return on Assets

Bank	1996	1997	1998	1999	2000
HSBC					
- SPI	1.217	1.733	3.610	3.362	2.686
- Overall	1.898	0.890	-1.160	-2.116	1.809
OCBC					
- SPI	2.214	1.082	2.032	0.435	1.214
- Overall	1.380	1.081	0.503	1.760	1.287
SCBMB					
- SPI	0.035	0.320	1.315	0.952	1.546
- Overall	1.738	2.047	1.025	1.883	1.607
Banking system at large	2.000	1.300	-0.300	0.700	1.500

Source: Stream of data

Meanwhile, the performance of the banking system in general was rather modest during the period of 1996-2000. On average, excluding Islamic banks, the banking system's ROAs was only about 0.8%, while that of foreign banks SPI combined was more than 1.58% over the same period. Individually, HSBC recorded the highest ROA for its SPI operations averaging at 2.52%, followed by OCBC 1.39% and SCBMB at only 0.8% over the period of 1996-2000.

This figure suggested that over the period of study, Islamic banking at foreign banks has been performing considerably better than the banking system in general. Although, ROA alone would not be able to portray an exact picture of Islamic banking operations at the banks, it should be sufficient to conclude so. What more, the trend analysis earlier has been comprehensive, and it has suggested similar results and conclusion.

4.4 Conclusion

As mentioned earlier, the SPI operations of the foreign banks have been profitable throughout the period of this study. This is, perhaps, one good reason for foreign banks to continue and expand their Islamic banking operations. It is also one element that should attract more foreign banks to embrace and offer Islamic banking in the country. This is important, since by the end of 2000 only four foreign owned banks offering Islamic banking (the other one is Citibank).⁷⁷ All these four are, fortunately, the top largest foreign banks in terms of total assets⁷⁸, thus signify the importance of Islamic banking among the foreign banks in the country. Yet, it would be more desirable to bring in more foreign banks into the stable, not only to enhance the image of the sector, but also to expand the wings of Islamic banking further.

⁷⁷ BNM (2001), *Financial Sector Master Plan*. Pg.77.

⁷⁸ BNM (1999), *The Central Bank and the Financial System in Malaysia*. Pg. 390.