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ESTABLISHMENT OF THE FIRST WAQF BANK IN BAHRAIN: EXPLORATORY STUDY

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ABSTRACT

This paper surveys *awqaf* over a historical and geographical trajectory as a backdrop to exploring the lineaments of a new *waqf* bank. The Kingdom of Bahrain is on the cusp of founding a new *waqf* bank but many issues with respect to creation of a *waqf* bank need to be threshed out and limned in detail. To this end, a survey was designed and distributed to key decision-makers in the Islamic Financial Institutions (IFIs) in Bahrain to obtain their feedback about the possibility to establish the first Waqf (Endowment) Bank of Bahrain along three axes; . 1) proposed structure; 2) sources of capital and 3) recommended modes of financial transactions. 67% of IFIs responded and questionnaires filled out by 12 IFIs were analyzed in terms of descriptive statistics. The result of the survey indicate substantial support among IFIs for the creation in Bahrain of a *waqf* bank, organized as a domestic and international investment and development bank, with financings drawn primarily from Muslim sources and public banks (CBB) and secondarily from all corporations (be they Islamic or non-Islamic). Preferred legal status would be as an independent corporation. IFI informants suggest that the new *waqf* bank would be licensed to conduct a wide variety of Islamic transactions, with a strong preference in favor of direct investment with equity participation but, notably, exclusive of engaging in loans with service charges. This study should prove utile to the Central Bank of Bahrain (CBB) in determining how to set up a new *waqf* bank in line with a need to craft new guidelines and regulatory measures covering operations of such new Islamic financial entities. In addition, this study should be particularly relevant to central banking authorities considering in Islamic economies of whether, and how to, go about formation of *waqf* banks in their jurisdictions in Bahrain for strategizing and encouraging the establishment of the Waqf Bank.

JEL Classifications: E5, N25, N50

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INTRODUCTION

Endowment (*waqf*) means a charitable foundation's holding or keeping a designated asset for the sole purpose of helping the poor (Amuda, 2013). In terms of historical antecedents, according to Stibbard et al, 2012, the first religious *waqf*, created during the Prophet's lifetime for religious purposes, was the Mosque of the Quba in Medina. In the course of the first 300 years of Islam, Muslim scholars progressively developed jurisprudence with respect to the creation, management, and administration of *awqaf* (Stibbard et al, 2012). In the course of the ebb and flow of Islamic civilization, *waqf* funds have contributed markedly to the development of Islamic educational institutions spanning from the primary to the tertiary levels (Mahamood and Rahman, 2015). Also dubbed the "third economy," the charity sector is ranked third, after public and private

sectors, in terms of its contribution to the economy. In terms of institutional presence, endowments are active not only throughout Muslim world but also extend into non-Muslim countries. The emergence of endowment institutions reflects demand present both in Muslim and non-Muslim communities worldwide. Indeed, endowment institutions are growing globally at a rapid rate with an impressive record of growth manifesting in a broad swath of countries.

Investment in endowments closely parallels the growth in Islamic Financial Institutions (IFIs) with funds funneled from the latter to the former involving the capitalization of a wide variety of charitable projects run by the former. According to the Global Islamic Finance Report (2017), the global Islamic financial services industry is currently valued at US\$3 trillion. In a related report, the International Association of Islamic Banks (IAIB) reported in 1997 that the total assets managed by Islamic banks equaled US\$ 112.6 billion with a net profit of US\$ 1.2 billion (Khan, 2001). Moreover, the past ten years witnessed high growth in the number of IFIs around the world (Sarea and Hanefah, 2013) with the industry attracting major western institutions such as Citibank, HSBC, BNP-Paribas and Deutsche Bank, which operate Islamic windows inside conventional banks (Maali and Napier, 2010).

LITERATURE REVIEW: NEED FOR THE STUDY

From the time of the prophet (pbuh) to the beginning of the nineteenth century (Mohsin, 2013), *awqaf* have played a significant role throughout Islamic history. Notwithstanding that post-eighteenth-century geopolitical events in the Islamic world, coupled with the administration of Islamic trusts by the state, have served to undercut their utility (Sabit Haji, 2015), the *awqaf* nonetheless possess the potential to contribute positively to the sustainable development of Muslim and non-Muslim societies. Especially pronounced is the potential to contribute to educational, medical, social, financial and environmental spheres of economic activity through global partnerships. Effectively managed *awqaf*, however, need to strike an equitable balance between the needs of current and that of future generations.

A myriad of previous case studies, drawn from Bahrain, Malaysia, Indonesia, Turkey and Bangladesh, have confirmed that the utility of establishing *awqaf* as a mechanism for contributing effectively to economic prosperity. In Bahrain, Islamic banking began in 1979 with the establishment of the Bahrain Islamic bank (Hussein, 2004). In the aftermath of the emergence of Bahrain as the Middle Eastern hub of the Islamic financial sector, the Central Bank of Bahrain (CBB), in partnership with Islamic Financial Institutions (IFIs) in Bahrain, established the Waqf Fund in 2006 under the control of the (CBB Website, 2017). Each of the “22 Member institutions made a one-time contribution to the Waqf Fund’s corpus which is then invested in Islamic money market instruments and the return is used to finance the Fund’s initiatives” (CBB Website, 2017).

In Malaysia, Aziz (2017) observed that *awqaf* in Malaysia is mostly utilized for religious purposes with more than 81% of *waqf* assets being earmarked only for building mosques. In a related study highlighting *waqf* regulation and capitalization, Razak et al., (2016) admonish that in every state in Malaysia, “different rules and strategies (manifest) to collect *waqf* from Muslim society” at large. However, no such regime prevails

tantamount to the alternative model presented by Haji Mohammad (2015) who envisions the operation of the current banking sector in the guise of social Islamic *waqf* banks.

In Indonesia, *waqf* funds, in contrast, have been availed to finance education in such innovative initiatives as the Pondok Modern Gontor Darussalam (PMGD) programme, which evinces sustainability, inasmuch as the alumni, whose tuition having been financed by *waqf* funds, returns capital in the form of labor by contracting to teach in the PMGD programme, in so doing contributing to society in general and the economy in particular (Razak et al., 2016). In Turkey, likewise, *waqf* funds are largely earmarked to support the educational sphere. (Razak et al., 2016).

Finally, in Bangladesh, *awqaf*, absent effective institutional governance tools and mechanisms, exhibit information asymmetries resulting in misallocation of resources (Hasan and Siraj, 2016) speaking for the need for reform of *awqaf* as a platform to contribute, to the maximum extent feasible, to sustainability and economic development in the country (Hasan and Siraj, 2016).

RESEARCH METHODOLOGY

A questionnaire distributed to Islamic Financial Institutions (IFIs) to obtain their perceptions about the establishment of the Waqf Bank in Bahrain has been constructed based on Sabit's instrument (2015) with the questionnaire being divided into three categories with respect to the new waqf bank: 1) proposed structure; 2) sources of capital and 3) recommended modes of financial transactions.

Analysis of these three segments as illustrated in tables (1, 2 & 3) revolves around descriptive statistics. To support the analysis of the research objectives and research questions, however, the questionnaire is specifically oriented with a view to obtain perceptions of decision-makers in Islamic Financial Institutions (IFIs) with respect to the establishment of the Waqf Bank in Bahrain. The sampling size consists of a number of IFIs in Bahrain. However, a total of 18 questionnaires were distributed to the Management of IFIs. Only 12 copies filled out by respondents were obtained to be examined, nearly 67%, which is sufficient for purposes of reliability.

RESEARCH ANALYSIS AND FINDINGS

Based on the previous studies, the researcher divided the establishment of a hypothetical new Waqf Bank items into three sections as discussed above.

The summary of findings is provided in the below Tables:

PART 1: The Proposed Structure of WAQF Bank

TABLE 1: THE STRUCTURE OF THE BANK

No.	Establishment of WAQF (Endowment) Bank	Mean	Std. Deviation
1	Would your organization participate in the establishment of a <i>waqf</i> bank in Bahrain?	3.47	.514

The structure of the bank:

	The <i>waqf</i> bank should be a:		
2	Full bank (doing retail banking, commercial banking)	3.59	.618
3	Investment and development bank	4.24	.562
4	Domestic and international	4.24	.562
	The legal status of the bank should be classified as a:		
5	Independent body	4.41	.795
6	Subsidiary	3.82	.636
7	Corporation	4.24	.846
8	Cooperative financial institution	4.31	.946

A survey method was chosen to measure the possibility for establishing a new waqf bank in Bahrain. Respondents were required to rank their perceptions on the three sections of survey for each item based on the five-point Likert scale with:

- 5 denoting “strongly agree”
- 4 denoting “agree”
- 3 denoting “neutrality” (neither agree nor disagree)
- 2 denoting “disagree”
- 1 denoting “strongly agree.”

Table 1 depicts eight items analyzed in terms of mean and standard deviation (SD). The first statement concerns establishment of a waqf bank in Bahrain and the tested statement was, would your organization participate in the establishment of waqf bank in Bahrain? The mean (3.47) modestly exceeds the level of neutrality (3.00), which approximately equates to -1SD. This implies that, to a degree of nearly 84%, member’s institutions view favorably contribution to and participation in the establishment of a new waqf bank.

For the proposed structure of the bank, the results of the survey, presented in Table 1, reflects that the respondents considered the structure of the waqf Bank to be one (or a combination thereof) of the following: full bank (doing retail banking, commercial banking), investment and development, domestic and international. Results indicate that the stronger preference is a combination: an investment and development bank operating domestically and internationally with a mean of 4.24 and an SD of .562. The mean substantially exceeds the level of neutrality, which approximately equates to -2SD. This implies that, to a degree slightly exceeding 97.5%, member institutions view as highly preferable organizing the *waqf* bank with a license to conduct investment and development at the domestic and international levels. These results nudge out the possibility for organizing the waqf bank as a full service retail/commercial bank with a mean of 3.59 and a SD of .618.

In terms of legal structure, preference appears in the form of an independent corporation given indicative results for an independent body and a corporation, respectively, with a mean and standard deviation of 4.41 and 4.24 and .795 and .846. With respect to the baseline neutral likert score of 3.00, this equates to roughly -1.75 and -1.5 SD in percentage terms, this implies that, to a degree marginally exceeding 96.0%, member institutions view as very highly favorable an independent legal structure, and to a degree marginally falling short of 93.3%, member institutions view as highly preferable a corporate legal structure. These two legal structures are not mutually exclusive and thus

the results suggest an independent legal corporation. A cooperative financial institution lags as an ideal legal structure (equating to -1.33 SD relative to the neutral baseline) though markedly ahead of the clearly inferior legal structure of a subsidiary (equating to -1.25 SD relative to the neutral baseline) – both of which are mutually exclusive with an independent body and corporation – and thus are rejected.

PART 2: Proposed of Sources of Capital

TABLE 2: SOURCES OF CAPITAL

No.	Establishment of WAQF (Endowment) Bank	Mean	Std. Deviation
	Sources of capital		
9	Government	3.53	.514
10	Islamic corporation	3.76	.562
11	All corporations	3.82	.529
12	Muslims	4.71	.588
13	Non-Muslims	2.49	1.439
14	Any one (public) Banks (CBB)	4.24	.664

Regarding the Sources of capital, the results show that the respondents prefer the source of capital from, in descending order, Muslims, public banks (CBB), all corporations and Islamic corporations, and, last though not entirely excludable, government. Measured against a baseline of neutrality (3.00), overwhelming preference is for the sources of capital to be drawn from Muslims as large with mean of 4.71 and a standard deviation of .588 closely trailed by public banks (CBB) with a mean of 4.24 and a standard deviation of .664. In percentage terms, this implies to a respective degree of 99+% and 97.7% that member institutions prefer these sources of funding. However, all corporations and Islamic corporations, as sources of funds also receives substantive [though less support than that attributable to Muslims and public banking authorities (CBB) with means and standard deviations respectively registering at 3.82 and 3.76 and .529 and .562.

In percentage terms, with neutrality associated at marginally less than -1.5SD for Islamic corporations and slightly more than +1.5SD for all corporations, member institutions, to a degree just below and above 91%, would value contributions from the Islamic corporations and all corporations, respectively. Interestingly, all corporations slightly nudge out Islamic corporations in terms of residual preference. Tapping government sources, to which is attributable a mean of 3.53 and a standard deviation of .514, constitutes the least preferable of a -1SD for a degree of certainty on the order of 84%. acceptable sources registering relative to the neutral level of 3.00. Informants, however, reject non-Muslim sources with a mean of 2.49 modestly trailing the neutral level of 3.00. With a standard deviation high relative to the mean at 1.439, results suggest non-normality with informants split along strongly disagree (likert score=1) and strongly agree (likert score=5) with the former in excess of the latter. Antipathy toward tapping into non-Muslim sources of capital may stem from bias in favor of *halal* funding, shariah restrictions/compliance and religious prerogatives.

PART 3: Proposed Modes of Transactions Used By WAQF Bank

TABLE 3: THE MODES OF TRANSACTIONS USED BY WAQF BANK

No.	Establishment of WAQF (Endowment) Bank	Mean	Std. Deviation
	The modes of transactions used by waqf bank		
15	Musyarakah (joint venture)	3.63	1.065
16	Mudarabah (profit-sharing)	3.31	1.249
17	Murabahah (cost plus)	3.47	0.904
18	Ijarah (leasing)	3.46	1.073
19	Direct investment (equity participation)	3.94	1.078
20	Qard hasan (benevolent loan)	3.42	1.017
21	Instalment sale	3.41	1.016
22	Lease purchase	3.315	1.00
23	Ju'alah (transaction based on a commission)	3.47	0.964
24	Muzara'ah (crop sharing)	3.47	1.172
25	Musaqat (gathering)	3.315	1.157
26	Trade bills purchasing	3.526	0.772
27	Rent sharing	3.894	1.100
28	Loan with service charges	2.105	1.523

The above table shows the list items were analysis regarding the modes of transactions used by *waqf* bank. All items were above the neutral level (3.00) except the Loan with service charges. This reflects the contentious discussion among scholars in previous studies with regard to loans with service charges with critics labeling it a form of *ribah*. The strongest preference is for direct investment with equity participation with a mean of 3.94 and a standard deviation of 1.078. This implies that, to a degree slightly trailing 84%, member institutions view as preferable using direct investment as the predominant transactional form. Rent sharing, *musyarakah* and trade bills purchasing stand in the second echelon of preference with a mean and standard deviation of 3.894, 3.63 and 3.526 and 1.100, 1.065 and .772. In reference to the benchmark neutral level (3.00), each register at about $-2/3SD$ for a degree of confidence in the environs of 74.5% with confidence being slightly greater as follows: rent sharing > *musyarakah* > trade bill purchasing. However, the rest of the modes of Islamic business transactions are acceptable, though to a lower degree of confidence, as part of the repertoire of transactions in the proposed of *waqf* Bank in Bahrain with a marginal preference of *murabahah*, *ijarah*, *qard hasan*, *ju'alah* and *muzara'ah* over *mudarabah*, installment sale, lease purchase and *musaqat*.

CONCLUSIONS AND AREA OF FUTURE RESEARCH

Eliciting opinions from practitioners in surveyed Islamic financial institutions (IFIs) serves as a mechanism to gain insight into the degree of institutional support for the creation of -- and how to structure, capitalize and operate -- a new *waqf* (endowment) bank in Bahrain. Questionnaires were distributed to 18 IFIs in Bahrain to obtain perceptions about the establishment of a new *waqf* bank in Bahrain and data was

successfully collected from 12 institutions in Bahrain. This paper contributes to the field of Islamic banking by shedding some light on the nature of *waqf* bank creation, germane but not limited to Bahrain, in countries that have *awqaf* not organized as banks as an aid for decision-making in this sphere; namely, whether and, if so, how to go about creation of a *waqf* bank. In Bahrain, the CBB has taken the initiative to encourage the establishment of *waqf* bank under the guidelines of Islamic banks. This paper also contributes to knowledge in the sphere of Islamic banking by shedding light on how *waqf* funds have been used to meet societal needs, in a variety of spheres, across a cross-section of Muslim countries. as well as to regulatory bodies for encouraging

The main findings of this study indicate that there is substantial support for the establishment of a new *waqf* bank in Bahrain. Strong support manifests for the new *waqf* bank to be structured as an investment and development bank operating, domestically and internationally, as an independent corporation in terms of legal status. Indicated strongly preferred sources of funds are from Muslims and public banks (CBB) closely followed by all corporations and Islamic corporations. However, there is no preference in favor of Islamic corporations as opposed to corporations as a whole. On balance, moreover, opposition inheres to using non-Muslim sources of funds.

As for the modes of proposed transactions of the new *waqf* bank, strongest preference is evinced for direct investment with equity participation. However, support can be found for participation of the new *waqf* bank in a broad array of transactions except for loans with service charges. Future research should combine quantitative and qualitative methods with a view to zeroing in on the most efficient structure, financing and operation of a *waqf* bank with implications for Bahrain and beyond. Interviews and focus groups could provide additional sources of rich data imparting greater confidence in results obtained through survey research. In addition, an investigation of the perceptions of the regulatory bodies in Bahrain, such as Central Bank of Bahrain (CBB) could provide further insights in this sphere.

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