Chapter 2

Islamic Banking in Libya: Emergence, Growth, and Prospects

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ABSTRACT

This chapter identifies the internal and external challenges for Islamic banking in Libya. It is a conceptual work using secondary data where relevant concepts in terms of challenges of the conversion process in Libya were demonstrated. Conversion process is surrounded and faced by many challenges. Internal challenges are not less significant than external ones. Trained human resource, lack of awareness in Islamic banking, and resistance to change to Islamic banks are considered as internal challenges which represent the stage of readiness to convert the sector. On the other hand, the economic structure, the political situation, and the regulatory framework hinder the process externally. This implies that stakeholders should come up with comprehensive strategies and plans about the conversion process which will improve the readiness level of the banks, raise the awareness and willingness of their employees, and increase the skills of banks’ staff.

INTRODUCTION

Islamic finance has grown to the extent that it has become a standard norm in the global financial system. At an average growth rate of more than 15% (GIFF, 2016), Islamic financial assets have reached US$ 2.1 trillion as at the end of 2017, even though a bit slower than expected (Damak, 2018). Interestingly, the demand for Islamic financial products is still very high especially with the opening of new markets.

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in unexpected Asian countries such as Japan, South Korea, Hong Kong and China. In Africa, Islamic finance is fast becoming an area of interest in many countries like South Africa, Nigeria, Libya, Senegal, Morocco and many others (MIFC, 2016).

Islamic banking is a significant branch of Islamic finance and therefore the major proportion of the Islamic finance assets operate under the management of full-fledged Islamic banks which was estimated at USD1.286 billion in 2015 (Global Islamic Finance Forum, 2016). In most Muslim countries, the government takes the initiative to introduce and expand Islamic banking (Rafay & Sadiq, 2015). Some Muslim countries like Sudan, Iran, Pakistan and recently Libya imposed Islamic methods of finance to be exclusively the banking system in the country and simultaneously outlawing regular banking practices. To conform with the Islamic principles of banking, the conventional banks were mandated to change their operational system in terms of technology, structure, culture, strategy, processes and infrastructure to operate in accordance to the Shari’ah methods of finance and banking (mu’amalat). Even though the adoption of Islamic finance in most of the new markets are restricted to Sukuk, there are still moves to convert the whole financial system to Islamic especially in the rich oil countries like Libya.

Libya is a developing Arab country located in North Africa. It has an area of 1.8 million square kilometres and a population of 6,411,776; most of them are Muslims (Libyan General Information Authority, 2013). Libya has an attractive geographical location which is surrounded by African countries such as Egypt from the east and Sudan from the south-east, Chad and Niger from the south and Tunisia and Algieri from the west side. Among these countries, only Egypt, Sudan and recently Tunisia are already practising Islamic methods of finance.

This geographical location makes the country commercially and economically viable given the trade link between these countries. Libya is now seeking to adopt a free market system to encourage investment, especially after the Arab revolution in 2011. This means opening the door for Islamic banks worldwide, especially from neighbouring countries to establish new branches in Libya (Gait, 2009). As a populated Muslim country, Libyan people, in general, expect that the government should adopt the Islamic philosophy of economics which is based upon justice, equity and the prohibition of usurious transactions that involve gambling and excessive speculation (Gath, 2009). This expectation was emphasised by earlier studies that report most Libyans willing to deal with Islamic ways and religion as the significant reason of that (Humaira & Iswusi, 2010; Kumati, 2008).

The Libyan government is indeed one of the few countries that has taken the stance to transform all its bank into Islamic banks following the Libyan law no. 1 of 2013 which postulated that all conventional banks must stop interest-based transactions by the end of 2015. As mentioned, Libya is a 100% Muslim country, which is a factor that significantly proved to facilitate the smooth conversion process to Islamic finance (Gait, 2009). Unfortunately, the process of conversion is deteriorating; in fact, no single bank has yet converted to Islamic banking.

At the beginning of 2015, when Law No. 1/2013 was enforced, the financial system of Libya froze and went into a severe liquidity crisis. Consequently, the government had to extend the enforcement of Law 1/2013 until 2020 by issuing another Law (Law No 7 - 2015, 2015). Of course, there are many challenges at both the bank level and beyond that hinder the successful conversion, which we examine in this chapter. The challenges were classified into internal and external challenges to proffer solutions on the way forward to some of the challenges.
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