Islamic Banking and Economic Growth in Libya

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Abstract

The main aim of this article is to critically examine the interactions between Islamic banking and economic growth in Libya, also to find whether it influences economic growth and transforms the operation of the financial system and trade activities to enhance the Libyan economic sector in the long-run. The author discovered that in the short-run only fixed investment that cause Islamic banking to develop, where as in the long-run, there is evidence of a relationship between Islamic banking and fixed investment with a promising chance to strategically support gross domestic product (GDP) in Libya. Both qualitative and quantitative data collection methods were used while undertaken this research and the primarily results indicated that Islamic banking is the way forward to increase the turnover and profit margin in the short run. Meanwhile, the final results have revealed the significant relationship between Islamic banking and economic in the long run. However, more studies are needed to discover the unknown about the impact of Islamic banking on the Libyan economy.

K**eywords:** Islamic Banking, Libyan Economic Growth, Islamic Financial System, Fixed Investment, Trade Activities.

2. Introduction

Customary banking system that can be accepted by Muslim clients has been questioned by Islamic scholars to suit Islamic business principles, values and religious obligations. Conventional banks which deal with interest-based transactions are not really accepted by Libyan customers for the generation of assets and liabilities, therefore many banks in Libya now are avoiding dealing with interest-based activities, indulging speculative business activities, or other specific unlawful investments and financing (Warde, I, 2000). Islam clearly prohibits the use of the tradition of interest, and it is clearly specified in the Holy Quran, in the chapter of Al-Nissa and the chapter of Al-Rahman (Bangake, 2011). As from that prospective, Islamic banking in return provides banking products and services which are based on the Islamic financial concepts and principles that are primarily based on non-interest and trade-based modes (Ali, Salman Syed, 2004).

To be more precise, since its commencement more than four decades ago in southern eastern Muslim countries in Asia, the Islamic banking system has been also growing in different parts of the world and the assets of Global Islamic Banking reached US$1.00 trillion in 2015 providing an option for millions of existing and new customers to benefit from the financial products and services according to their faith commitment. Also, Islamic banking accounts for major share of Islamic finance industry reached 79% share in overall Islamic finance industry in the world (Shu-Chin, Lin, 2009). This portray the importance of Islamic banking financial operations and transactions in the entire Islamic finance architecture (Siddiqui, S.H, 2006). Another thing to be mentioned, that in the Muslim world choosing financial products and services are selected according to customer's religious values are important consideration before an actual purchase. For example, interest is strictly prohibited according to the Islamic faith, hence the convenient banking system is questioned on religious grounds. And Islamic banking products and services are available from decades and acceptability still raising among Arab and Muslim consumers after improving their products and services in an effective and efficient manner and that will consequently lead to a stable economic growth. Furthermore, previous studies about Islamic Banking have indicated that financial development is generally defined as an increase in the volume of financial services of banks and other financial intermediaries.

Eventually, to meet their customers' needs, different Islamic banks have developed Ijaar, Murabaha, Mudarbaha and Musharakah agreements that will be explained later because Islamic banking system is based on Islamic values and principles and is chosen by many users due to their faith commitments. However, there are other elements which are considered by individual obligations while choosing Islamic banking. These can be categorized into individual, social, cultural and religious factors (Deutsche Bank, 2011) as well as institutional factors such as facilities, convenience, professional staff quality, availability of cash, speed, fees, family and friends influence, service variety, and so on (Al-Jarrah, 2005). Moreover, financial transactions on capital markets and economic growth have always been a major subject in the field of economic improvement. And financial sectors in most developing countries like Libya play a growth promoting role if they are able to direct financial resources (FR) towards public sectors that need those FR the most. Furthermore, once the Libyan financial sector is more developed, more financial resources can be allocated into productive and rational use, and more physical capital will be formed which can contribute positively to Libya's economic growth. Out of the extensive research carried out in this field, there are no sufficient previous studies conducted by other Libyan authors within the Islamic financial framework. The other objective of this paper, therefore, is to narrow the gap in literature by examining the relationship between Islamic banking development and potential Libyan economic growth, particularly in the context of Libya in comparison with other successful Muslim countries around the globe focusing on other Muslim nations which are considered to be good examples in Islamic Banking and finance.

3. Study Research Hypotheses / Problems

As previously mentioned this study manly concerns with examining the dynamic interactions between Islamic banking/ finance and economic growth in Libya and the author realized the importance of Islamic finance and how it might develop and improve the Libyan economy after the positive experiences of public and private Islamic banks that influenced some giant global banks like HSBC, Natwets and Lloyds TSB, beside the great examples of some countries like Malaysia which has evolved as viable and competitive component on the overall financial systems as a driver of sustainable economic growth and strategic development in which the financial system in the state of Libya desperately needs to overcome financial problems, increase profit, reduce loss and costs, meet all clients' needs and sustain competitive advantages in very competing local and regional markets.

On the other hand, the Islamic financial system would guarantee the required level economic growth and improvement by justifying and closing the gap between performance and achievement focusing on the importance of financial development for this developing country and to find if the economic growth causes Islamic banking institutions to change and develop on regular bases. Conversely, this academic study is guided by the author aiming to respond to the following research questions:

RQ1: How important is the Islamic banking system for economic growth and development initiatives in Libya?
RQ2: What is the nature of the possible relationship between Islamic financial development and economic growth in Libya?
RQ3: Will the new Islamic banking system be risk free and help for sustaining and controlling economic growth in Libya?

The author has also worked hard enough on external literature sources review with focusing on work-field and the experimental part results in order to get the best outcomes for examining the convenience and effectiveness of the Islamic banking on economic growth in Libya.

4. Study Aims and Objectives

The main aim of this study concerns with investigating the effectiveness of Islamic Banking towards the Libyan economy improvement comparing to other Islamic and Arab countries by knowledge sharing and practices with examining the differences in performance, knowledge, experience, and how to sustain our economic growth by using Islamic financial system. In particular this study is aiming to:

1- To examine the nature of the possible relationship between Islamic banking development and economic growth in the case of Libya?

2- To find whether Islamic financial system would transform the operation of the financial system and trade activities to enhance the Libyan economic sector.

3- To open a new channel and more creative source of income for economic growth and development in Libya.

5. Study Methodology

During this academic work the author has applied quantitative and qualitative approaches that were used in this research design to collect, critically analyze, discuss, evaluate and interpret the required data. The qualitative research approach was the dominant in this academic study to find out whether Islamic Banking improvement has a direct impact on the Libyan economic growth and achievement. Meanwhile, the quantitative approach was adopted in the final phases of this research by asking 100 university lecturers, researchers, graduates, bankers and professionals in the treatment of group samples crucial open questions about the impact of Islamic Banking Development towards gross domestic product (GDP) enhancement and economic growth in Libya. Therefore, the author believes that this research is significant for the following reasons:
1- This research is the first attempt to examine the impact of Islamic banking on economic growth in Libya.
2- To fill the prior gap in literature, this research investigates the potential effects of Islamic banking on the Libyan economic growth.
3- To find if the final results of this article supports the hypothesis that Islamic banking is a real channel of economic growth in Libya?
4- To examine any obstacles in the light of establishing the Islamic financial systems in Libya?

6. Study Motivation and Literature Review

Many previous studies have paid enough attention to the impact of finance on economic growth. However, fewer studies have examined the impact of Islamic banking on economic growth, especially in Arab world which represent a good market of Islamic Finance for having a religious societies that fully support Islamic Banking system and finance as one of the best channels of economic growth in them countries while aiming for financial improvement and economic stability taking advantage of the benefits of the Islamic banking system over conventional banks taking into accounts the key instruments of Islamic banks with illustrating the relationship nature between Islamic financing, in general, and Islamic banking in particular, and economic development. This will also reviews the comparative performance between Islamic and conventional banking systems, especially in the last economic and financial crisis because of the political instability in Libya.

6.1 The First Movement of Islamic Banking

The notion of Interest-free banking transactions was first introduced in the late 1940s by Anwar Qureshi (1946), Naiem Siddiqi (1948) and Mahmud Ahmad (1952). Moreover, the first modern experiment with Islamic banking in the Arab world was established in a small town in Egypt, called Mit Ghamr, in 1963 by Dr. Ahmed El Najjar and the bank had adopted the form of a saving-investment bank based on profit sharing and loss principals, compering to other conventional banks. (Siddiqi, 2006). Other previous studies especially from South East Asian Muslim countries, proved different levels at which Islamic banking has been operating for decades. However, there are full- fledge of Islamic banks which are providing only Islamic banking products and services but in Libya there are banks which only provide conventional banking products, services and transactions, also there is a dual banking system in Libya which is providing both Islamic and conventional products and services and finally they opened Islamic Departments in some Libyan banks that only provides products and services according to Islamic Shariaa Law. Moreover, the Islamic financial system in different parts of the world like Brunei, Indonesia and Malaysia have evolved as viable and competitive component on the overall financial systems as a driver of sustainable economic growth and strategic development. In particular, Malaysia has tremendously set up a strategic comprehensive Islamic financial infrastructures such as Islamic banking in 1983, Islamic insurance in 1984, Islamic capital market in 1993, Islamic inter-bank money market 1994, Kuala Lumpur Stock Exchange (KLSE) Shariah Index (1999) and in March 2001, Central Bank of Malaysia launched the financial sector master plan which incorporated 10- years master plan for Islamic banking and TAKAFUL (exchange) that is aiming to create an efficient, progressive and comprehensive Islamic Financial System (IFS) and to promote Malaysia as regional financial center/ market leader for Islamic banking and finance in which Libya can take as a good example in response to the domestic huge Islamic banking demand (Furqani, H. & Mulyany, R, 2009).

6.2 The Second Movement of Islamic Banking

In regard to the second Islamic Banking real movement around the globe, previous studies indicated that in the 1970s, the Islamic banking movement re-emerged with the foundation of the Islamic Development Bank (IDB) in 1974 by the Organization of Islamic Countries (OIC), which has been considered as the stepping-stone for the movement's second phase (Abdel-Haq, 1989).. As an example, Dubai Islamic Bank (l975), Faisal Islamic Bank of Egypt (l977), Faisal Islamic Bank of Sudan (l977), and Bahrain Islamic Bank (l979) were amongst the earliest commercial banks in the Arab countries (Shu-Chin, Lin, 2009). However, recent Islamic banks, both with Offline and E-Banking services were established not only in the

Muslim countries, but have also gained footing in non-Muslim countries. And in Europe the Islamic Finance House in Luxembourg was established in 1978 to represent the first attempt at Islamic banking in the Western world (Ariff, 1988), followed by the first Shariah-compliant insurance company (takaful) in 1983 in Luxembourg as well. Many traditional Western banks have established Islamic windows and branches such the HSBC Bank, ANZ Grindlays, Standard Chartered Bank, Barclays, Lloyds Bank, Citibank, ABN AMBRO, Klienwort Benson, Merrill Lynch, Midland Montagu, and Goldman Sachs (Hassan, K, 2011).

Later on, some Islamic countries such as Iran and Sudan have fully Islamized their banking systems (Sundararajan and Errico, 2002). Islamic financial institutions have taken the form of commercial banks, investment banks, investment and finance companies, insurance companies, and financial service companies. The banking sector, in particular, follows different banking models, such as private banks in a conventional economy (as in most Arab countries and the western world) Islamic banking in Libyan banks started operating gradually less than ten years ago and established a legal commission for the transformation from conventional financial system to promote Halal (legal) - based financing and transactions, also new departments of Islamic financing were developed in most Libyan banks. Since then, measures have been taken to increase the improvement and growth of Islamic banking in Libya and as a result, there has been a considerable shift in the Libyan financial landscape that enables fresh channels and prospects in the Islamic banking sector and hence shows that a huge untapped market still exists.

Also, like in any other Islamic state, the Libyan financial market has a huge market potential for Islamic banking. Masses of Islamic Banking customers in the rural areas and big cities of Libya representing different income-level groups are being exposed to Islamic banking products, services and financing to make informed purchasing decisions according to their needs and expectations (Ali, Salman Syed, 2011). In this regard, Libyan banks offering Islamic financing are exhibiting better options comparing to conventional banks. Furthermore, Islamic financial system in Libya is not only competing with full-fledged conventional banks but also with a dual banking system, which means banks with Islamic departments in Libya now are offering products and services, such as saving accounts, current accounts, business accounts, Visa cards, home financing, other products and services within the same segment. Hence the increasing banking competition in Libya is pushing banks with Islamic finance orientation to develop unique marketing strategies to develop and maintain relationships with their existing and new customers for long-term corporate sustainability mutually beneficial for all parties.

6.3 The Importance of Financial Development

In accordance to the importance of banking/ financial development for a developing country such as Libya, study on causal relationship between the development of financial intermediaries' activities and economic growth must be carried extensively. Moreover, scholars like King and Levine (1993) for instance, studied this issue using data from 80 countries over the 1960-1989 periods. They constructed four indicators of the level of financial sector developments which is regressed with the real gross domestic product (GDP) per capital and its sources. First of all is "financial depth" which equals the ratio of liquid liabilities of the financial system to GDP. The second thing is the ratio of deposit money bank domestic assets to deposit money bank, deposit assets plus central bank domestic assets to measure the relative importance of specific financial institutions. Other previous studies have clearly indicated that the third and fourth financial development indicators are designed to measure domestic asset distribution. The proportion of credit allocated to private enterprises by the financial system and the ratio of claims on the non-financial private sector, respectively and their conclusion is consistent with Schumpeter's view that the financial development promotes economic growth. And this important conclusion is primarily supported by the works of Agha Oliver (2012).

6.4 Financial Development and Economic Growth

Some previous authors proved that countries with high income and rich experiences in relation to both economic and financial development displayed some evidence of reverse causation so that the relationship between financial development and growth appears to be bi-directional. Furthermore, Rioja and Valev (2002) posit that there is no significant relationship between financial depth and economic growth in countries with low income per capital. However, However, the significant relationship between financial development and economic growth only appears in the high income countries like the US, Japan, China, and Germany, also some other studies have taken a more microeconomic approach and some used stock markets as the proxy for financial improvement. As an example, Fisman and Love (2003) revisited an earlier paper was undertaken by Rajan and Zingales (1998) and re-examined their assumptions, and the robustness of their final results to alternative theories and interpretations. The result has supported the idea that financial development helps industries with good economic growth opportunities. It also reinforces their argument that the role of financial development is to reallocate resources to industries that have well economic growth opportunities but not to other industries with "technological dependence" on external finance (Bangake, C. & Eggoh, J, 2011). On the one hand, presuming that the relationship between Islamic banking and financial development and economic growth in Libya is following the view of "demand-following" which means that economic growth causes Islamic banking institutions to change and develop gradually. Furthermore, financial development and economic growth could be achieved in developing countries including Libya by injecting the banking system with more investment for better productivity and guaranteed strategic economic growth as shown below:

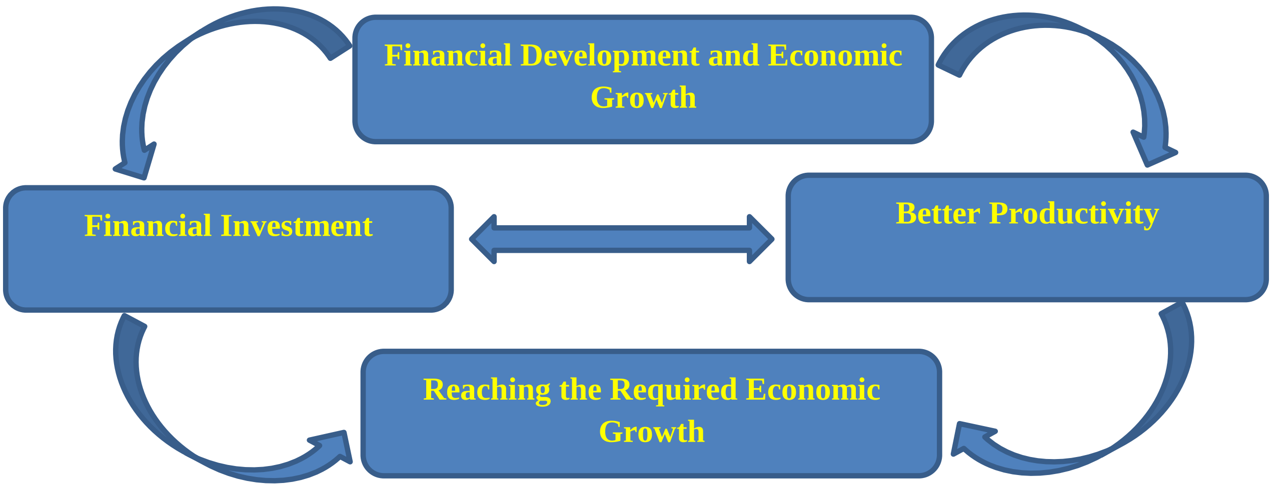

Figure 1. Financial Development and Economic Growth

(Model Source: Young, 2016, p. 164)

6.5 Key Investments in Islamic Banking

In Islamic finance there is a fact that money itself has no substantial value. As a matter of faith, an ordinary Muslim in any part of the world cannot lend money to, or receive money from someone and expect to benefit. This means that interest (which is Riba in Islam) is not allowed and making money out of lending money is forbidden in the Islamic Teaching. Furthermore, money must be used in a productive way, by which wealth can only be made through legitimate trade, transactions and investments in assets. Thus, the financial principal means of Islamic banking are based on trading under an extreme condition that any gains relating to the trading must be shared between the party providing the capital and the party providing the expertise. As a result, the Islamic banks have developed four main Islamic financing techniques and those who are involved in the trading or the business process in many way such as: Musharaka, Murabaha, Ijaara and Mudaraba. (AAOIFI, 2010).

6.5.1 Musharaka (Joint Venture or Profit and Loss Sharing “PLS”):

In the Islamic Fiqh (Teaching) Musharaka means a clear profit and loss sharing joint venture. And it is intended to combine the talents of two or more partners in a business enterprise, where each business partner contributes capital, managerial expertise, solution providing efforts and other essential services in equal level or varying degrees. Accordingly, business partners in Islamic finance share in both risks and financial results on the basis of their share in capital and efforts. And because most banks do not wish to be actively involved with the management of a venture, this form of partnership is not commonly preferred nor applied in Islamic banks in many Muslim countries worldwide (Alam, 2003).

6.5.2 Mudaraba (Trust Financing)

Mudaraba in Islamic finance is a business partnership of a financing partner and a managing partner. The financing business partner which is the financier, entrusts his capital to the managing partner regarded as entrepreneur, who in turn contributes his knowledge, experience and entrepreneurial financial skills to the agreed project. The financing partner is not involved in the actual management side of the partnership. And this makes trust financing the preferred form of partnership for most Islamic banks. Moreover, profits are shared in a pre-determined ratio and in the event of a loss, the financing business partner bears the loss, while the managing business partner loses their time and efforts, unless this loss was caused by the irresponsible behavior/ performance by the managing partner. Also in that sense, Islamic banks around the globe are regarded in the Islamic Teaching as Mudaraba companies, where the depositors are regarded as the financier and the shareholders in general and regarded as the entrepreneur (Olson, D. and Zoubi, T.A, 2007).

6.5.3 Ijaara (Leasing)

Ijaara is simply an Islamic lease agreement. It is defined by as: “Ownership of the right to the benefit of using an asset in return for consideration” (AAOIFI, 2010). In this kind of financing, the bank purchases a piece of product or property selected by a certain customer, and then leases it back to him/her for a specified rental over a specific period of time. The time duration of the lease, as well as the basis for rental, are set and agreed in advance and in many cases, the bank may lease a tangible asset from a third party and subleases that product/ property to its client (Ali, 2004). Moreover, Islamic banks are currently practicing this financial technique in circumstances, under which customers at the end chooses to buy the product(s). Thus, in such circumstances, Ijaara is mainly practiced either in the form of “lease and ownership” or “lease with diminishing sharing". And in case of signing a contract of "lease and ownership" extends the concept of Ijaara to a hire and purchase agreement including a promise from the client to buy the product/ equipment at the end of the lease period, at a pre-agreed price. Rentals paid during the period of the lease constitute part of the purchase price.

In simple words, the monthly payment will consist of two components, i.e., rental for the use of the equipment and an installment payment towards the purchase price. Usually, as a result, the final sale will be for an agreed sum. However, the second contract of "lease with diminishing sharing" is commonly used by home-buying customers. Diminishing sharing means that the bank reduces its equity in a property with any additional capital payment the end user makes, over and above his/her normal rental payments. The tenant's ownership in the property increases and the bank's ownership decreases by a similar amount each time the client makes another capital payment. Ultimately, the bank transfers ownership of the property entirely over to the client. The liquidity risk in both types of Ijaara contract will therefore be limited because the sale price is built up into the rental installments (Suleiman, 2000).

6.5.4 Murabaha (Cost-plus financing or Mark-up financing)

Murabaha is known in the Islamic teaching as the sale of goods at cost plus an agreed profit mark-up (Ali, Salman Syed, 2011). It is an obligation in this type of Islamic financing that the seller truthfully informs the buyer of the price at which he/she purchased the product and stipulates an amount of profit in addition to the original cost (see for instance: Ibn-Qudama, Vol. 4). Therefore, Murabaha is, in theory, a shape of trade financing. It is then a sales contract that fixes the price of certain products or items, plus a specified percentage mark-up/ profit. However, it is currently practiced as an agreement between a final purchaser (the end user) and a middleman (the Islamic bank), by which the Islamic bank takes the role of financer. Hence, in this case, a customer requests the bank to purchase the selected items according to certain specifications. Once the bank purchases the goods, it resells them to that client at the cost plus a certain profit and the Murabaha contract in such a case is called "Murabaha to the Purchase Deal" (Suleiman, 2000).

6.6 Benefits of Islamic Banking

Over the years, Islamic banking has shown many positive indicators of its strategic benefits. As well as, driven from and based on the previous discussion especially in the above important key investments factors, the Islamic banking and financial system has the following advantages over the conventional interest based banking system (Goaied and Sassi, 2010):

6.6.1 Reduction of Moral Risk

Islamic banks have a superior advantage over all different conventional banks to benefit from the different types of key investments mentioned before, especially the productivity factor and the freedom from the typical unethical investments to reduce the moral hazard and adverse selection problems. In addition, the willingness to increase deposits and attract more depositors drives Islamic banks to launch " Inter Cultural Programs" to instruct their new and existing employees on the religious dimensions of their activity. The knowledge of Islamic teaching known as (Sharia) combined with a high level of inter cultural aptitude reinforcing the credibility of Islamic banks and generate sustaining their competitive advantage comparing to conventional banks (Goaied and Sassi, 2010).

6.6.2 Extra Financial Stability

The Islamic banking system in Libya can lead to a more financial stability as it's based on “zero interest” with profit sharing and loss principles (Ibrahim, A, 2012). And this proves that Islamic financial system is financially stronger and less risky than conventional banks. Having said that, it is argued that shareholders of investment accounts in Islamic banking system don't have fixed value securities, which means that investment depositors automatically share profits and losses in the case of asset reduction due to macroeconomic or bank-specific crises.

6.6.3 More Efficiency

Many authors stated that zero nominal interest rate is a necessary condition for an optimal allowance of resources. In addition, zero interest rate is both necessary and sufficient for efficiency allocation in general balanced models. The reason is when fixing a zero interest rate, traders tend to have no reason to change real resources for money, which means that more resources will be conducted to beneficial investments. Goaied and Sassi supported this approach explaining that by ignoring interest principle from its mechanism, Islamic banks exclude all speculative financial activities related to interest rate expectations, and, hence, change in money flow will directly reflect on real sphere by a change in demands and supplies of products and services (Riahi-Belkaoui, Ahmed, 2000). On the other hand, some other studies, have used cost and profit functions to compare the efficiency of Islamic and conventional banks, and concluded that Islamic banks are more efficient than conventional banks (Al-Jarrah and Molyneux, 2005). Moreover, the previously discussed key investment principles of “profit sharing”, play important role to increase the competition among Islamic banks to drive the profitability to its maximum in level both the short and long run, which make all of them more aware and attached to the real financial market.

6.6.4 Less Poverty and ore More Equality

Since the main standard for financing projects in the conventional banking system is the ability to repay loans, mortgages and guarantees, only rich people then will have most access to financial products and services. In the opposite, Islamic Banking and financial services provide funds on the basis of profit sharing and loss principle, paying good attention to profitability and rate to return making it not only possible for rich clients to have access to financial product and services but poor customers as well could benefit from the same products and services with taking into account risk assessment and feasibility study results but at the end they would have a better chance to acquire finance from Islamic Banks. Furthermore, this proves that Islamic financial institutions do not only focus on maximizing profit, but they also play a vital role in addressing socio-economic issues such as poverty reduction and improvements in important aspects of equality and human welfare by effectively channeling financial resources towards productive opportunities, hence enhancing productivity, financial investment and trade activities (Naqvi, S.N.H, 2003).

Relatively, it’s important to notice the experience of Islamic banks in reducing poverty through the use of Zakah funds and interest-free loans to improve the socio-economic development in all societies. And this can be achieved by either making the poor people more productive, which in turn contribute to the local economy development, financing human welfare activities, or better both. Thus, there are two examples to considered here: The first one is Jordan Islamic Bank that has established a special fund for interest-free loans to the needy people for the period from 2001 through 2003 and the fund provided $22 million to more than 40 thousand beneficiaries, an amount that is approximately 230% of the total net profits realized by the bank during these three years. And, the second example is the Islamic Development Bank in Jeddah, which has $100 million in its "Waqf" account, to be spent on research, training, development studies, technical assistance program. Furthermore, the previously mentioned four advantages are of Islamic Banking are:

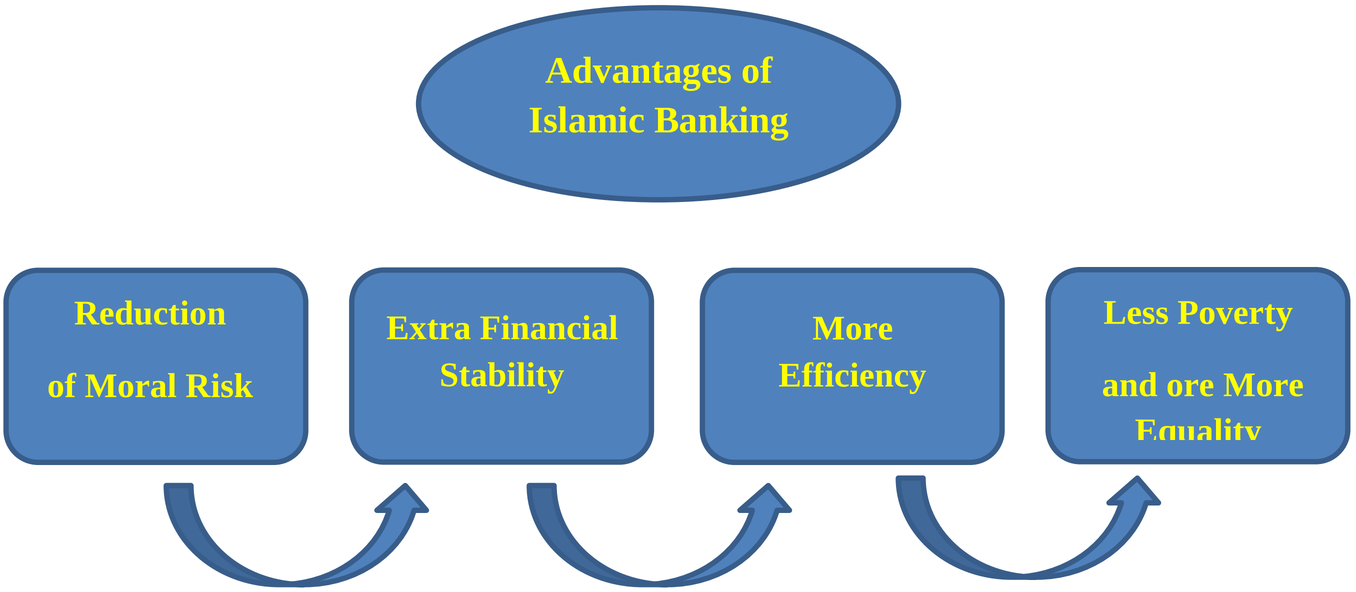

Figure 2. Logical model for advantages of Islamic Banking

(Model Source, Goaied and Sassi, 2010, p. 79)

6.7 Financial Ratios and Competitive Performance Between Conventional and Islamic Banks

Previous studies investigated if financial ratios will differentiate significantly between the two categories of banks; Conventional banks via Islamic banks. Thus, some scholars examined 16 financial ratios commonly used in the banking industry and used regular neural networks, and k-means nearest neighbors to find out whether bankers, researchers and regulators could use these ratios to make a distinction between different types of banks. Moreover, the two categories of banks have nearly the same financial ratios, the best nonlinear classification technique (k-means nearest neighbors) that's able to correctly distinguish Islamic from conventional banks in out-of-sample tests at about 87% success rate. The results have clearly indicated that characteristics such as efficiency ratios, profitability ratios, key performance indicators, assets quality indicators, and cash/liability ratios are good distinguisher between Islamic and conventional banks in the Islamic world. Such outcomes are symmetrical with the literature on corporate success, failure, credit rating, and risk assessment that also show that accounting numbers are useful for classifying firms within the same kind of industry into two or more categories based on their financial orientations (Huang, H. & Shu-Chin, Lin, 2009).

Janbota & Anju Kishore got different results when they examined the performance of Islamic banks in the Arabian Gulf, where the Islamic funds are highly concentrated and they found out that the UAE Islamic banks are relatively more profitable, less liquid, less risky, and more efficient compared to the UAE conventional banks. Thus, authors associated this performance to productive characteristic of Islamic products and services on the basis of profit-loss sharing principle. To go more in depth, Karim and Ali (1989) have investigated the effect of the interaction between the financial strategies adopted by banks on the capital structure of two Islamic banks, Faisal Islamic bank and Kuwait Finance House and the results indicated that the composition of the capital structure of the two banks that were examined was depending on the management strategic choice. It suggested that Islamic banks may prefer to obtain funds from depositors/ account holders rather than from shareholders during expansionary periods in an economy when combined with the requirement for risk sharing, return on equity should be higher for Islamic than for conventional banks.

Ahmed and Khababa (1999) studied the consequences of business risk, market concentration, and profitability size of 11 commercial banks in the Kingdom of Saudi Arabia for the period of 1992-1997. And they employed a regression model putting into use 3 measures of profitability: return on assets, return on equity, and earnings per share and the final results showed that business risk and size explain bank profitability in Saudi Arabia. As well as, Murjan and Ruza (2002) examined the competitiveness of the commercial banks in 9 different Arab countries (Bahrain, Egypt, Jordan, Kuwait, Oman, Qatar, Saudi Arabia, Tunisia, and United Arab Emirates). Using a Ross-Ponzar test for the period of 1993-1999, and their study suggested that the banking and financial industry in those countries operate under conditions of monopolistic competition. Moreover, Essayyad and Madani (2003) examined the concentration, efficiency, and profitability of 10 commercial banks in Saudi Arabia for the period 1989-2001. Their results indicated that the Saudi Arabian banking industry is highly concentrated and has a four-firm concentration ratio ranging between 69% and 87%. They also found that profitability rises with increases in bank efficiency and that bank profits are positively related to oil revenues. And to be more precise, Al-Tamimi and Al-Amiri (2003) examined the service quality of two Islamic banks in UAE (Abu Dhabi Islamic Bank and Dubai Islamic Bank) by distributing questionnaires to 700 customers. About 350 feedback responses were received revealing that clients are very satisfied with the quality of services received from their Islamic banks (Abdul-Majid, 2005). In another study, Rosly and Abu Baker (2003) examined six financial ratios for Islamic and mainstream banks in Malaysia from 1996 to1999 discovering that Islamic banks' return on assets, profit margin, and net operating margin are statistically larger than for mainstream banks, however operating efficiency and asset utilization ratios are statistically smaller than for conventional banks. Nevertheless, they suggested that Islamic banks have chosen to behave more like mainstream banks than required by Shariah principles. Their unique study leaves unresolved question of whether both kinds of banks behave similarly in other countries and whether financial ratios can be used to truly differentiating between Islamic and conventional banks. Another line of research has focused on the profitability of the banking sector in general, without comparison between Islamic and conventional banking system in different countries in the Islamic world. Furthermore, Islam in (2003) has investigated the development and performance of commercial banks in Bahrain, Oman, Dubai and Abu Dhabi for the period of 1998-2000. And he used several financial ratios to measure bank performance and show that GCC banks perform well relative to western banks. He also indicated that competition among GCC banks increased over the period examined (Alshammari, SH, 2003). Moin (2008) has examined the performance of the first Islamic bank in Pakistan, Meezan Bank Limited (MBL) comparing it with 5 Pakistani conventional banks, in terms of profitability achievement, liquidity, risk levels, and efficiency for the period of 2003-2007. And he put into action 12 different Financial ratios, such as; Return on Asset (ROA), Return on Equity (ROE), Loan to Deposit ratio (LDR), Loan to Assets ratio (LAR), Debt to Equity ratio (DER), Asset Utilization (AU), and Income to Expense ratio

(IER), in order to evaluate banking performances. T-test and F-test were used in determining the importance of the differential performance of the two kinds of banks. The study found that MBL is less profitable, more solvent (less risky) comparing to the conventional banks. However, MBL is improving rapidly over time proving affinity with the performance of the conventional banks. And in terms of liquidity, the results indicated that there was no significant difference between the two sets of banks.

7- Study Experimental Part/ Field Study

This research field study was conducted in Cyrenaica province which is located in far north east of Libya and counted on the participation of different groups that were of lecturers, researchers, graduates, bankers, bank managers, regulators and customers who were participating in focused groups, meetings, round tables, interviews and questionnaire to critically examine the direct and indirect impact of Islamic banking on the Libyan micro and macro-economy growth and development (Furqani, H. & Mulyany, R, 2009). The selection of this group sample was based on the fact that they were representing both service providers and the end users and they worked hard with the author as they were highly interested in changing the current conventional banking system which is only based on interest towards Islamic Banking that's based on profit sharing practice and loss principles. All groups of participants described that Libyan clients and depositors are more interested in using Islamic Banks and finance as they are committing to their Islamic faith obligations. Libyan customers showed an outstanding trust in Islamic Banking making them inject more cash, purchasing more products and using more services representing an important opportunity for supporting the Libyan economy by opining a new liquidity channel and not to rely only on the oil and gas industry (Scott and Marshal, 2005). Furthermore, the majority of participants in the experimental part of this academic study have strongly agreed that providing Online Banking, using new information and communication technology in Libyan Islamic Banks will rapidly improve all products and services with increasing and sustaining different advantages such as long term investment, annual revenue, profit margin and eventually gross domestic product (GDP). The following are several data collection procedures used to collect the required information:

7.1 Using Economic analysis

Islamic departments in Libyan banks need to use econometric analysis, annually time-series data of economic growth. And despite of not finding an accurate record, an analysis was conducted to gain a general idea of the effective Islamic financing system through deposits, shares, products, services, equities and charity/ Zakah funds through modes of financing as a proxy for the development of gross domestic product, gross fixed capita formation as proxies for an effective economic growth in Libya. Also this promotes the notion that a well-functioning Islamic banking system strengthen the Libyan economic growth. Moreover, the results show that Islamic banking and has contributed to more investments proving significant relationship between economic growth and Islamic bank’s financing in the short and long run.

7.2 Diaries

The collected data proved that Islamic Banking is one of the best ways forward for economic growth in Libya. Furthermore. These different data were then triangulated and analyzed. The data collection method was the difficult stage during this research to examine the advantages of Islamic banking and the benefits it can add to the Libyan gross domestic product (GDP). However, it was very interesting to see how the participants offered the best of themselves to this study. At the end of this experimental part the author resulted that for Libyan economic development, it is better if Libyan financial regulators to take an example of Qatari Islamic banks successful experience from the period of 2002 to 2008 as shown in Figure (3) and the numbers are in Billions:

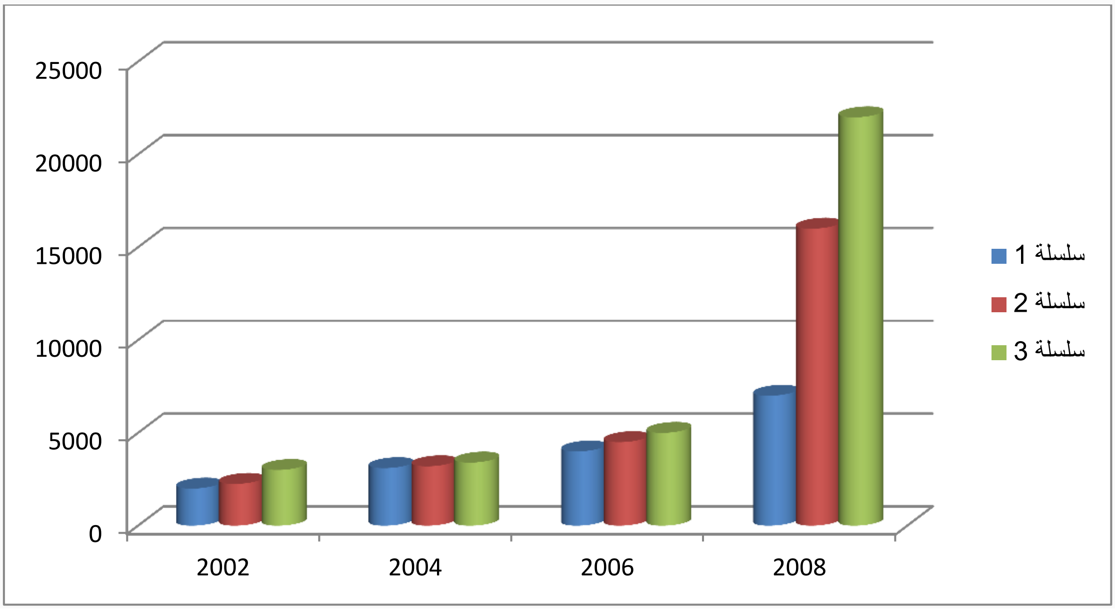

Figure 3. Islamic banks financing growth in Qatar, 2002-2008

(Model Source, Blominvest report, 2011, p. 162)

8- Findings and Conclusions

At the end of this academic study the author eventually discovered that strategically applying the Islamic Banking and Financial System in Libya will certainly lead to an increase in GDP and economic growth, with concluding the following:

1- This research is the first attempt to examine the impact of Islamic banking on economic growth in Libya..

2- The author discovered that in the short-run only fixed investment that cause Islamic banking to develop, where it's more promising in the long run.

3- This study is important to the Libyan regulators and policy makers for strategic planning and financial development.

4- This article is a direct response to the expansion of Islamic Banking in Libya to improve different products and services which are demanded by Libyan clients.

5- This study will help Libyan conventional banks to try interest-free based system to meet their clients' needs in different products and services.

6- This study have successfully contributed to the body of knowledge sharing practices and minimized the gap between Islamic banking and economic growth in Libya.

9- Study Recommendations

Based on the above findings, the author highly recommends all interested writers for further studies about Islamic Banking and economic growth in Libya and the Arab world, especially in the increased dimensions of this important article taking into account other additional variables. This study also managed to identify the strong relationship that exists between Islamic Banking and sustainable economic growth in Libya with recommending:

1- Islamic banking will positively contribute o Libya's economic growth.
2- Libya must take good examples of other successful Islamic Banks worldwide.
3- All Islamic financial institutions must equip their staff members with the needed professional skills to properly manage these institutions.
4- Islamic Finance will support GDP in Libya with guaranteeing cash-flow stability.
5- Islamic banking may not be good enough for the Libyan economic growth if there is low expansion in Islamic banking financial sector.
6- Adapting an Islamic banking and financial system will weaken financial risk because of the productivity factor and the freedom from the typical unethical investments which at the end reduces moral hazard and adverse selection problems.

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