



Islamic Banking's Decades-Long Institutionalisation Struggle: The Case of Pakistan

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Abstract

Islamic Banking (IB) still struggles to institutionalise its practices at the wider societal level. The literature, despite having covered the sector from several angles, has overlooked an objective evaluation of the root causes of its restricted institutionalisation so far. This empirical investigation into Pakistan's IB sector fills this void and investigates the sector's apparent limited success in institutionalising its practices despite having been formally accorded legitimate legal status around the world. The paper, bringing the sector's governance to the spotlight, concludes that the social practice's 'site' of development – the Islamic Shari'ah jurisprudence, has too strong a coupling of internal elements to accommodate the sector's current loose adherence to its principles and laws, and thus the sector, rather than its 'site' of its development, needs to adapt and reorient to accomplish unrestricted institutionalisation. The paper also extends Foucault's theoretical constructs in the sector's peculiar context, which stems from a unique cultural, economic, and regulatory environment. The paper aims to add a new dimension to the IB governance literature and help steer future research focus to areas with the highest marginal utility for the sector and its stakeholders.²

Keywords: Islamic banking; institutionalization; institutionalisation, compliance with Shari'ah; site of the social, Pakistan

JEL: F33; G15; L1; L2; P51

SDG: SDG8, Target 8.A

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1. Introduction

The magnitude of effectiveness for social practices' institutionalisation varies immensely across different social settings, and a business sector's corporate governance determines the extent of its sustainability and survival in the long run. Some practices get socially accepted and institutionalised relatively quickly, while others struggle for decades to achieve legitimate societal acceptance. A similar situation has Islamic banking (IB) been facing over the last few decades. IB is a specialised form of financial services that amalgamates traditional interest-based banking practices with the applicable laws from the Islamic jurisprudence – the *Shari'ah*.³, which calls for leniency towards the borrowers if they cannot pay their debt on time, avoiding a third party guarantee (Vinnicombe 2012), the conduct of all financial transactions by banks, both loaning as well as public deposit taking, without the involvement of *riba* (interest)⁴, *gharar* (uncertainty) and gambling (Akhtar, Akhter and Shahbaz 2017; Miah and Uddin 2017), and ensuring the sharing of risk, profit and loss by the bank and the borrower in proportion to the principal contribution in the form of a joint venture⁵ (Iqbal and Molyneux 2016; Azmat, Skully and Brown 2015; Miah and Uddin 2017). Hence, the IB sector offers alternative products, such as *Qard Hasana* (interest-free loans), *Musharakah/Mudarabah* (Islamic joint ventures), and *Murabaha/Ijarah/Salam/Istisna* (lease or trade-based financing) (Azmat et al. 2015; Chong and Liu, 2009). However, Islamic *Shari'ah* law basic requirements are not being meticulously observed by the present day IB when executing these products⁶ (Mahmood and Rahman, 2017; Azmat et al., 2015; Hashmi, 2012; Kettell, 2011, pp. 31; Khan, 2010; Ahmad et al., 2013; also (see Siddiqi 2006; Iqbal and Molyneux 2016). The IB's *modus operandi* is derived from the economic philosophy of *Shari'ah* and the monetary theory of Islamic economics (Shah, Raza and Khurshid 2012). Islamic Banking (IB) claims to overcome traditional banking's several shortcomings from the perspective of morality, justice and ethics (see Hassan and Lewis 2007; Porzio 2010; Zarrokh 2010; Ahmad and Hassan 2007; Ariff and Iqbal 2011; Ariff 2011; Clarke 2009; Venardos 2005; Khan 2010).

IB is more profitable than its conventional counterpart. However, its compliance with its founding principles that stem from the Islamic *Shari'ah* law is still questionable (Iqbal and Molyneux 2016). The sector is worth an estimated 2 Trillion dollars, growing annually at 15% (Garifullin, Daryakin and Galeeva, 2018). While the sector's claims to be fully compliant with the applicable Islamic principles are endorsed mostly at a formal institutional level, they are yet to be fully endorsed at a wider societal level. Most practitioners struggle to convince the general public of the sector's complete compliance with the Islamic *Shari'ah* jurisprudence, often presenting the sector as the 'best available option' to people chasing pure Islamic banking alternatives (see Majeed and Zainab 2017). This study provides empirical evidence that while the bankers themselves are convinced about the IB's *Shari'ah* compliance (also endorsed by Shah, Niazi and Majid 2016), they struggle on a daily basis to convince the

³ *Shari'ah* "is the Islamic law of human conduct, which regulates all matters of the lives of Muslims. It is based on God's [H]oly word in the Qur'an, the deeds and sayings of the Prophet Mohammed [peace be upon him] (*Sunnah*), and the consensus of Islamic religious scholars" (Venardos 2005; Maali, Casson and Napier 2006, pp. 267; see also Kettell 2011; Shah et al. 2012).

⁴ Islam terms 'interest' *riba* and categorically prohibits its involvement in any form, charging as well as payment, in financial transactions (Kazmi 2012; Ahmad and Hassan 2007; Kettell 2011; Hashmi 2012; Ahrenfeld and Abadi 2008; Malik et al. 2011; Venardos 2005; Doraisami et al. 2011; Zarrokh 2010).

⁵ Appendix A provides some quotes from the Holy Quran and *Sunnah* prohibiting *riba* (interest), *gharar* (uncertainty) and gambling.

⁶ Though understandably, there could be tens of illustrations of Islamic *Shari'ah* law-compliant banking transactions, one typical transaction is illustrated in Appendix B for readers to make sense of the real essence of IB.

general masses on this. The sector's strong stance on risk-aversion and social justice keeps it strong and resilient in the face of the world financial crises when its conventional counterparts struggle (see Mahmood and Rahman, 2017; Chapra, 2011; Rosman Wahab and Zainol, 2014; Miah and Uddin 2017; Sheikh and Qureshi 2017). The sector is distinct from conventional banking in many aspects (Mollah, Hassan, Alfarooque and Mubarek 2016), and it needs to present itself as unique and independent of its conventional counterparts (Narayan and Phan 2017). The literature also calls for more research on the outreach aspects of the 'niche' banking sector (Beck, Demirgüç-Kunt and Merrouche 2013).

The sector runs the risk of involvement in unethical business practices as meticulous compliance to Islamic *Shari'ah* law is still questioned in the literature (see Narayan and Phan 2017; Iqbal and Molyneux 2016; Ali and Raza 2017; Khan 2010; Siddiqi 2006; Chong and Liu, 2009; Ahmad et al. 2013; Siddiqi 2006). This paper aims to understand the reasons behind the sector's restricted institutionalisation and help reposition the sector by apprising the practitioners and policymakers of some 'informed' inputs into future policies to help it accomplish long-term sustainability and unrestricted growth. The study resorts to the constructionist thematic analysis wing of the epistemological research (see Braun and Clarke 2006) to pursue the study objectives. The sector's institutionalisation struggle has already been empirically investigated from the clients' end (see Asif, Shah, Afeef and Ahmed 2017), and this study aims to complete the picture by investigating the phenomenon from the bankers' perspective. Clients are more satisfied with the service quality dimension of the sector. However, managers need to do more regarding the sector's compliance with *Shari'ah* law and product innovation (Ali and Raza 2017). The literature calls for more research into how the sector's governing bodies can play a more important role in the sector's development (see Mollah et al. 2016).

The rest of the paper is structured in four main sections: Section 2 reviews the relevant literature, followed by a section on the study's research design. Section 4 presents the analysis of the qualitative data, amalgamating the empirical data findings with the pertinent themes emerging in the literature. The last section provides a discussion of the study's main findings and concludes the paper.

2. Review of the Literature

Participants in the process of construction of social practices freely interact, subject to their peculiar social position and norms, to create new or amend existing social practices (Kilfoyle and Richardson 2011). A business sector's social practices evolve over time, responding to various internal and external triggers for change, and eventually operate at a 'balanced state' before being hit by another wave of such triggers (see Laughlin 1991). The sector's management and governance dynamics play a major role in shaping its social practices and routines and 'promoting' them to be 'legitimised' and 'valid' in the context of the sector's *modus operandi*. The author asserts that since these players interact with several internal and external variables, including their inherent pursuit of self-interest, the sector always has to brace 'subjective' outcomes of its management and governance initiatives. The extent of 'objectivity' of the outcome of such interactions for the sector's beneficiaries is determined by the magnitude and thrust of each player's 'power' and 'authority'. Islamic Banking has been endeavouring a similar 'power play' in its struggle for institutionalisation ever since it was inception.

Muslims' need for Islamic-compliant financial services around the world gave rise to Islamic financial systems. The establishment of the first formal Islamic commercial bank can be traced back to Egypt in the 1960s (Rammal and Zurbruegg 2007; Malik, Malik and Mustafa 2011; Karim 2012). However, it gained high momentum with a commercial emphasis in the 1970s (Ahrenfeld and Abadi 2008; Rammal and Zurbruegg 2007; Hassan and Lewis 2007). Since then, many Muslim countries, including Pakistan, Iran, United Arab Emirates, Saudi Arabia and Sudan, have tried to align their banking system with *Shari'ah* jurisprudence (Aftab 1986; The Economist 1992; Hashmi 2012).

Islamic Banking (IB) claims to overcome traditional banking's several shortcomings from the perspective of morality, justice and ethics (see Hassan and Lewis 2007; Porzio 2010; Zarrokh 2010; Ahmad and Hassan 2007; Ariff and Iqbal 2011; Ariff 2011; Clarke 2009; Venardos 2005; Khan 2010). The primary distinguishing characteristic of all IB products is the elimination of interest (*riba*). Some modernists try to justify modern interest and usury by differentiating it from the Islamic *Shari'ah* law, which prohibited *riba* and created classifications of individual and institutional *riba* with the aim of defending the latter. However, there is no substance in these claims, and Islam admonishes *riba* in all forms and manifestations (Kazmi 2012; Ahmad and Hassan 2007; Zarrokh 2010; also see Saeed 2011; Khan, 2010; and Akhtar et al. 2017). The sector is more profitable than its conventional counterpart (Ramlan and Adnan 2016; Mollah et al. 2016). A strong focus on risk aversion and social justice has helped the sector outperform its conventional counterparts in times of crisis (see Mahmood and Rahman, 2017; Chapra, 2011). Table 2 below highlights the positives the IB sector enjoys over the conventional banks:

IB's Positives over its Conventional Counterparts	The Reporting Literature	Sample/sub-sample
<ul style="list-style-type: none"> IB's development has a positive impact on the banking sector development as a whole. 	Gheeraert 2014;	Islamic commercial banks from around the world over a period of 2000-2005, from the IFIRST database
<ul style="list-style-type: none"> IB sector growth encourages healthy competition that leads conventional banks to be more cost-efficient. Though less cost effective, Islamic banks are better capitalised, less likely to disintermediate and have a better asset quality with a better 	Becket al. 2013	2956 banks, including 99 Islamic banks, from 141 countries, period covered: 1995–2007
<ul style="list-style-type: none"> Listed Islamic banks in Indonesia, Malaysia, Turkey, and Yemen demonstrated better share performance on the stock exchange and a higher loan-deposit ratio than conventional banks during the late 2000s global financial crises During local financial crises, Islamic banks demonstrated even higher capitalisation and loan-deposit ratios than conventional banks. 	Becket al. 2013	(Sub-sample) 380 total banks, including 65 Islamic banks

<ul style="list-style-type: none"> • Though conventional banks were better cost managers, Islamic banks demonstrated better short-term solvency. • Islamic banks are more stable than conventional banks. However, the credit comes at the cost of efficiency. 	Miah and Uddin, 2017	48 conventional banks plus 28 Islamic banks in the GCC (Gulf Cooperative Council) countries, period covered: 2005 to
<ul style="list-style-type: none"> • Islamic banks demonstrated higher returns on shares for investors during the financial crises compared to their conventional counterparts. Figure 1 below shows the comparison graph. 	Becket al. 2013	(Sub-sample) 207 Stock Exchange-listed banks in 21 countries; period covered: 2005-
<ul style="list-style-type: none"> • Assets growth rate in IB is almost double (38%) than the conventional banks (20%) • Islamic banks operate with more fixed operating assets (3.85%) than conventional banks (2.94%) • Islamic banks’ earnings are more volatile than conventional banks • Capital structure choice also varies between IB (driven by profitability, size and tangibility) and conventional banks (with growth and earnings volatility as additional driving factors). 	Sheikh and Qureshi, 2017	20 conventional banks (177 bank-year observations) and 5 Islamic banks (39 bank-year observations), the period covered: 2004-2014.
<ul style="list-style-type: none"> • Islamic banks demonstrated high profitability, more liquidity, better capitalisation, and lower credit risk compared to their conventional counterparts. 	1.Khediri, Charfeddine, and Youssef 2015 2.Rosman Wahab and Zainol 2014	1. 62 banks comprising of 18 Islamic and 44 conventional banks in the GCC countries. A total of 466 bank-year observations 2. 79 Islamic banks from the Middle East

Table 2: IB sector’s Positives over the conventional banking model.

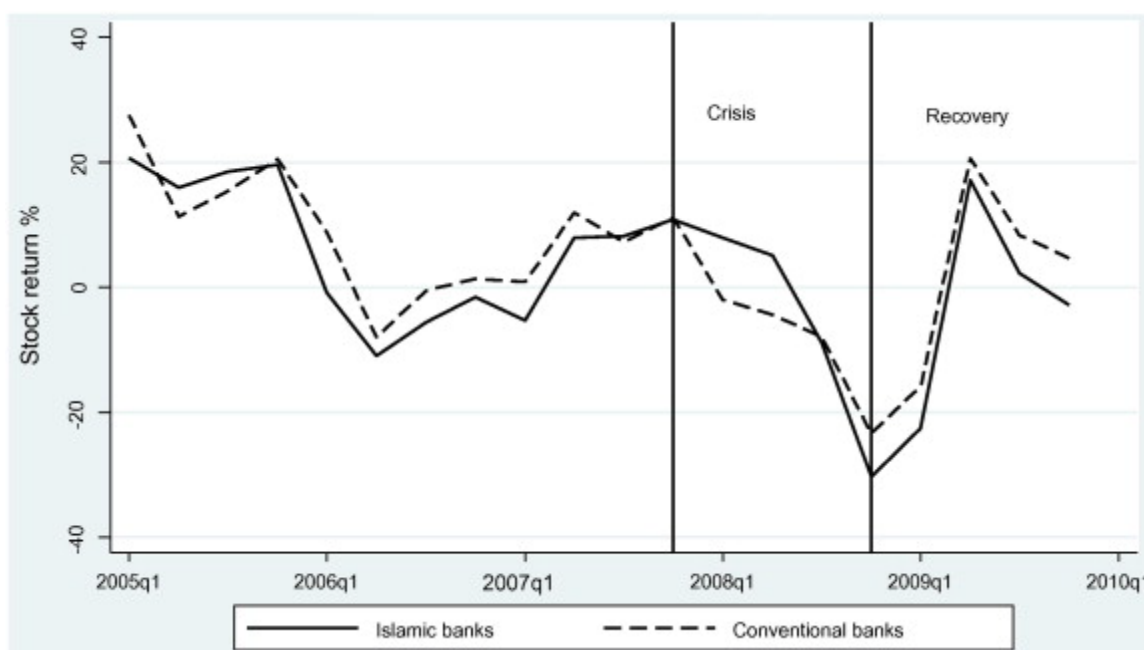


Figure 1: Average bank stock return by bank type, 2005–2009.

Source: Beck et al. (2013) compiled from Datastream.

The existing literature contains a detailed disquisition of all operational aspects of the innovative financial system in the light of the Qur'an.⁷ and *Sunnah*⁸ (see Yusoff and Wilson 2009; Ahmad and Hassan 2007; Venardos 2005; Maali et al. 2006; Kettell 2011; Hashmi 2012; Ahrenfeld and Abadi 2008; Malik et al. 2011; Rammal and Zurbruegg 2007). Hence, shedding more light on these aspects would belabour the reader and hence is out of the scope of this research. The major concern that forms a basis for this paper is that all these products claim to exclude *riba* (interest) and operate on a profit and loss sharing basis. However, when analysed objectively, these products, as operationalised at the current IB' sites', disguise 'interest' and encapsulate only semantic changes from those offered by their mainstream counterparts (see Sheikh and Qureshi 2017; Azmat et al. 2015; Mahmood and Rahman 2017; Zaman and Zaman 2001; Hashmi 2012; Kettell 2011; Shaharuddin 2010; Ahmad et al. 2013; Siddiqi 2006). At a formal level, the Accounting and Audit Organization for Islamic Financial Institutions (AAOIFI), a registered nonprofit corporate body with 200 member financial institutions from 45 countries in different parts of the world, bestows a legitimate and in-compliance status to Islamic financial institutions around the world (see Garifullin, Daryakin and Galeeva, 2018). In the case of Pakistan, the AAOIFI standards have been adapted to suit the country's peculiar regulatory and legal framework, and the *Shari'ah* Board of the State Bank of Pakistan (SBP), the country's Central bank, has been in the process of ensuring Islamic banks' compliance to the standards⁹.

This empirical paper makes a first objective probe into the sector's long struggle to fully institutionalise at the wider societal level, equal in magnitude to traditional mainstream commercial banking. The paper furthers the current literature by probing into the root causes of the sector's limited success in institutionalising its practices and securing a legitimate status in the sight of the Muslim communities whom it is primarily targeting. The objective is to draw academics' and practitioners' attention to the empirically informed reasons for this 'isolation'. Demand for the sector's service is continuously rising (Sheikh and Qureshi, 2017). Despite the phenomenal growth the sector has enjoyed, all is still not good for the sector's future, with many challenges to confront (Gheeraert 2014; Shah et al. 2012). A general perception among Muslims prevails that IB products, when operationalised, in real essence, are little different to the products offered under mainstream banking (see Hashmi 2012; Ahmad et al. 2013; Shaharuddin 2010; Siddiqi 2006; Khan 2010). This general societal perception is a great impediment confronting the sector's institutionalisation efforts. Questions raised during the interviews primarily hovered around these main themes – for instance, why IB, despite its phenomenal spread across the globe, still remains a 'niche' sector with only limited acceptance among its target audience, both in the Muslim as well as the non-Muslim world? What is it that the sector's governance disparately needs to do that it is avoiding to ensure the sector's unrestricted acceptance at a wider societal level? What role can the religious scholar's community – the *muftis* and the *imams*- play in this connection? What are the fundamental shortcomings that the sector in its current form has in its products, services, and procedures, and how can it overcome these? What sort of difficulties do Islamic bankers face when inviting members of the public to bank with them?

⁷ The religion Islam's Holy Book, the Word of God, was revealed to the Prophet Mohammad (see Vinnicombe 2012).

⁸ A written record of the sayings and actions of the Prophet of Islam – Muhammad (peace be upon him), and actions and sayings of his companions that he, explicitly or implicitly, ratified (see Kettell 2011; Vinnicombe 2012).

⁹ From March 2008 to December 2011, only 4 out of 41 standards were implemented (see Global Islamic Finance Report 2012) at: http://www.gifr.net/gifr2012/ch_13.pdf.

Generally, any subjective manipulation of a system and/or accounting data to compromise an organisation's performance with an aim to enhance individual performance results in a qualitative or quantitative cost to the organisation (Dillard et al. 2011; Hopwood 1972). This also happens where inter-organisational politics is 'in action' and a 'politicised' group within the organisation, creating 'power zones', works subjectively (see Baxter and Chua 2003, pp. 104; Dillard et al. 2011) to manipulate the system for personal gains at the cost of the organisation or the sector as a whole. Islamic banking, given its basic stance on adhering to Islamic *Shari'ah* principles, will remain vulnerable to external manipulation and thus never realise its full potential unless it objectively purpose-tailors its products and services and overall business strategy to be fully Islamic compliant, even at the cost of profitability. As venturing into purely Islamic-compliant banking is costly, requiring a dedicated shift in the infrastructure, it is being avoided at the sectoral level, intentionally or unintentionally.

3. Research Design

This study used the case study methodology to investigate the Islamic banking sector in Pakistan's peculiar context for pursuing the study's objectives. The country has a predominantly Muslim population, and the sector has been consistently struggling to get itself institutionalised at the wider societal level since its inception decades ago. Primary qualitative empirical data was collected from Pakistan during December 2016 and January 2017.

A total of 14¹⁰ Semi-structured interviews were conducted to glean the empirical data (see Table 1). The researcher tailored and expanded the interview questions to interviewees' varying responses and moods to help glean the most relevant and pertinent information related to the study objectives. The objective was to keep the momentum of the discussion intact and glean the most relevant information for the research project. Participants' written consent was secured before tape-recording all interviews. All tap-recorded interviews were transcribed (non-verbatim) and then analysed using Thematic Analysis (see Braun and Clarke 2006) in pursuit of prominent themes most pertinent to the study objectives and related and referenced to the relevant literature, a process that facilitates replication of the study results to other settings. Strauss & Corbin's (1998) 'open coding' technique, under the Grounded Theory approach (see Blair, 2015), was resorted to identifying pertinent themes in the data. The interview transcripts were analysed for different themes that were then compared and contrasted with the relevant literature to identify similarities and uniqueness of themes in the relevant scholarly literature. A theoretical version of the study, putting forth propositions for empirical investigation, was presented at the APIRA conference in New Zealand in July 2019.

Table 1: List of Interview Participants (Semi-structured interviews)

Participants	Location	Bank Name
P1	Lahore	Allied Bank Limited
P2	Lahore	Muslim Commercial Bank
P3	Lahore	Muslim Commercial Bank
P4	Lahore	Dubai Islamic Bank
P5	Lahore	Faysal Bank
P6	Lahore	Faysal Bank

¹⁰ Qualitative data from fourteen interviews sufficed for making informed conclusions for this research. Kuzel (1992) and Fossey et al. (2002) posit that there cannot be a specific limit, minimum or maximum, on the number of interviews under qualitative research. Interviews should continue until emerging themes start repeating in subsequent interviews (Kuzel 1992; Fossey et al. 2002).

P7	Lahore	Allied Bank Limited
P8	Lahore	Habib Bank Limited
P9	Lahore	National Bank of Pakistan (<i>Eitemad Bank</i>)
P10	Lahore	Dubai Islamic Bank
P11	Lahore	Bank Al-Habib Limited
P12	Lahore	Bank Al-Habib Limited
P13	Islamabad	Bank Islami
P14	Islamabad	Meezan Bank

4. The Empirical Data Analysis and the Literature

IB in Pakistan was instigated in 1979 with a governmental push for the Islamization of the country's banking sector through the elimination of interest from all financial transactions (Iqbal and Molyneux 2016). The sector witnessed real growth in the early 2000s, with Meezan Bank pioneering the phenomenon (P2, P6). The sector has grown phenomenally over the past decade or so in terms of the number of bank branches dealing in Islamic banking products. It has become a necessity for even conventional banks' survival that they step into this area and grab a share in the ever-increasing market (P7). However, "...there are still gaps [and] questions...which need to be...addressed properly, at the proper level, so that the customer understand[s] what it is and how it's different the conventional way of things" (P2). State Bank of Pakistan (SBP) aims to fully transform Pakistan's banking system to make it Islamic *Shari'ah* compliant (P1). The general public wants and is in dire need of a *Shari'ah*-compliant banking system (P11), and they would listen to religious scholars more than any other entity in this respect (P12). Thus, there is a dire need for all the stakeholders, government, IB sector representatives and religious scholars from all Schools of thought to meet together, discuss and reconcile their differences (P12). Given Muslims' growing numbers and attraction to the Islamic form of banking in the country, most of the country's conventional banks and several of its multinational banks have entered the market, opening an IB wing to tap into this growing market and fetch a share. Participant 3 did not agree that all these banks' products are 100% Islamic compliant even though they are emphasising their compliance with the Islamic *Shari'ah* jurisprudence. P7 expressed similar remarks about his own bank.

IB is a distinctive banking model (Mollah et al. 2016). It aims at establishing itself as an alternate form of banking that abolishes interest in financial transactions. It boasts equality through ensuring equal share in risk and profit and loss for both the lender and the borrower, and, despite having registered some encouraging growth since its inception, is still not without challenges (Miah and Uddin 2017; Azmat et al. 2015; Hashmi 2012; Shah et al. 2012; Malik et al. 2011; Gheeraert 2014). Though the sector is growing in terms of the number of banks, its widespread acceptance at the wider societal level as a legitimate Islamic-compliant banking system remains a challenge. Currently, the peculiar banking system is promoted by bank managers as the 'best available alternative' that is a good first step towards a pure Islamic compliant banking system (P1 and P13). To help the situation, better client awareness about the IB products and how these differ from those offered by the mainstream banking system is required (see Doraisami et al. 2011; Zarrokh 2010), a fact this study's empirical data endorsed in the context of Pakistan (P1, P3, P4 and P5). Given the proliferation of Islamic banks in the majority of the financially dominant countries of the world, both Islamic and non-Islamic,

mainstream local and foreign banks have opened Islamic principles compliant 'windows' (Rammal and Zurbruegg 2007). P3 endorsed this. Banks primarily aim to fetch a share in the growing financial sector (Khan, 2010); however, in practice, they are not fully observant of the Islamic *Shari'ah* law requirements (Chong and Liu, 2009; Khan, 2010).

Banks' attempts at ensuring compliance with Islamic law lacks objectivity as most of their products are only a semantic modification from conventional products aiming primarily at fetching a market share while keeping the *modus operandi* of transactions the same (see Sheikh and Qureshi 2017; Shaharuddin 2010; Ahmad et al. 2013; Siddiqi 2006; Khan 2010; Zaman and Zaman 2001; Azmat, Skully and Brown 2015). P7 concurred with this, asserting that IB has become a necessity for survival and even conventional banks are opening 'Islamic compliant' wings/branches. We distinguish our products by using the word 'profit' rather than 'interest', which is used by conventional banks, P4 remarked. We base our products' rate of profit on the Karachi Inter-Bank Offer Rate (KIBOR), which drives our rates up or down (P4). In the case of Pakistan, the State Bank has made it mandatory for all conventional banks to open Islamic banking windows to run parallel to their conventional banking system. The country's central bank has plans to transform all banking in the country to be Islamic compliant (P1). The empirical evidence revealed that securing a share in the fast-growing lucrative business with a high rate of return on investment has so far been driving the sector's growth (P1 and P3).

Riba is strictly prohibited by Islamic *Shari'ah* law in all financial transactions and covers any amount charged by the lender over and above the principal lent. In literal terms, most Islamic banks' products involve charging amounts over and above the principal, usually at a predetermined rate. A similar practice, contradicting the applicable Islamic *riba*-specific principles, is observed in the case of return on deposits kept with Islamic banks (Hashmi 2012). Describing this principal shortcoming in most IB products, Kettell (2011, pp. 31) asserts:

"... they [Islamic banks] can't charge interest, but they use something else which is [in essence] the same thing..."

Islamic banking is more profitable than its conventional counterpart (Ramlan and Adnan 2016; Khediri, Charfeddine, and Youssef 2015). However, the current IB practices operate under a disguise with a primary motive to earn a profit. The very basic requirements of *Shari'ah* compliance are not met by these institutions (Khan 2010; Ahmad et al. 2013) (see Siddiqi 2006). Profit and loss sharing in proportion to the respective capital contribution by the borrower and the banker in all loan transactions, as laid down as a requirement by the SBP, is not being observed, and no formal mechanism has been put in place for the scrutiny of IB operating procedures for ensuring their Islamic *Shari'ah* compliance (Iqbal and Molyneux 2016).

3.2. The Notion of Accountability – The Role of Good Governance

Public Accountability literature encompasses and demands objective behaviour on the part of an organisation or a business sector's management, particularly where the community's well-being is at stake. The public, in addition to the formal form of accountability, can exercise power informally by choosing not to legitimise a social practice and hold a business sector accountable if it is disguising its core objectives. Accountability is a relative term and refers to a situation where people must "...take responsibility for their actions" (Sinclair 1995, pp. 221) and provide an "account or reckoning of those actions for which one is responsible" (Gray et al. 1996, pp. 39), or where "the giving and demanding of reasons for conduct" (Roberts and Scapens 1985, pp. 447) is required. In the realm of modern capitalism, which apparently has a profound impact on the IB's choice of disguised operations in the pursuit of profitability, the "class status" notion from Weber (2012, p. 424) highlights the contextual significance of

accountability.

The literature has raised doubts about the sector's compliance with the Islamic *Shari'ah* law (see Narayan and Phan 2017; Khan 2010; Ahmad et al. 2013; Siddiqi 2006; Chong and Liu, 2009). IB as a sector has been evading accountability by not objectively tailoring its practices and products to demonstrate meticulous compliance to its founding principles, the Islamic *Shari'ah* jurisprudence, and disguising them with different names. "...If it's not purely Islamic banking, then I personally believe that it's a better step towards Islamic banking", P1 remarked about the state of Islamic banking's *Shari'ah* compliance in Pakistan. P9, quoting the country's most prominent *mufti*¹¹ A recognised Islamic scholar acknowledged to him that the system was not 100% Islamic compliant and that it was a first step towards IB in the country. P11 concurred with this stance, acknowledging that they go by the prevailing market conditions and adapt their products accordingly. El-Halaby and Hussainey (2016) endorsed this for forty-three Islamic banks across eight countries in terms of their level of compliance with AAOIFI *Shari'ah* compliance standards.

IB is the future of banking in Pakistan. Hence, we should adopt it and refine it along the way as we go, P13 suggested. P15 expressed similar views. Islamic banks must understand their target audience's perception of their products, emphasise innovation, and differentiate their products from those offered by their conventional counterparts, and authorities have not been paying attention to address this concern (P1 and P13). Recent literature also recommends the same (see Ali and Raza 2017). The general public's decades-old mindset about 'banking' to be illegitimate and un-Islamic will need a serious effort to change. How could the conventional banks' legacy of 55 years make a change to Islamic banking all of a sudden? P7 reiterated. P13, P14 and P15 expressed similar concerns about the dominance of the country's conventional banking sector. P1 asserted that the general public had a peculiar "frame of mind" and that for them, it is usually "difficult to accept the change", particularly when it comes to their religious beliefs. P6, P7, P11 and P12 concurred with this stance. P7 even complained that the term 'bank(ing)' in the context of IB needs to be replaced with another suitable title as the public perceives it to be a non-Islamic activity to start with.

P1 further added that a few *muftis* in the country had endorsed the legitimacy of Islamic banking practices. However, there is a necessity for a large number of public awareness workshops by the State Bank of Pakistan and the sector's governing bodies and open fora to help spread the word and convince the general masses about the Islamicity of the sector's practices (P1, P2, P4). Currently, even the professionals who teach Islamic economics in universities express doubts about the Islamic compliance of the IB products, let alone the layman (P10). Asif et al. (2017) found that even the government's support does not help influence the public's acceptance of the peculiar banking system. Local mosques' *imams*¹² *Fatwas* by *muftis* have a significant role to play if the sector aims to accomplish unrestricted institutionalisation at the wider societal level (P1, P2). State Bank of Pakistan needs to take on more responsibility in facilitating a closer interaction between religious scholars, bankers and the government to reconcile their differences and agree on what's required to help shape a positive public perception of the innovative banking sector (P12). If the sector is able to convince society's religious scholars from all/most Schools of thought, it will help it entice the majority of its target population. This segment is willing to adopt *Shari'ah* law-compliant banking products if reassured, to their satisfaction, of their meticulous compliance with the

¹¹ A religious scholar with recognised expertise in *Shari'ah* matters. Such persons often issue religiously binding opinions, referred to as *fatwas*, on different religious matters (Riaz, Burton and Monk, 2017).

¹² Highly respected religious people lead the five daily congregational prayers at their local mosques, and usually, people request them to officiate at wedding ceremonies (Riaz, Burton and Monk, 2017).

relevant Islamic principles. This is evident from the fact that the majority of practising Muslims opt out of the sector's products and services despite having little knowledge about *Shari'ah*-compliant banking products (see Rammal and Zurbruegg 2007).

The literature endorses the fact that IB currently differs in theory and practice (Sheikh and Qureshi 2017). The paper argues that, given the sector's peculiar stance on its products' specifications, a purpose-built operational structure, both collectively within the sector as well as severally inside the sector's constituents, is needed to be promulgated to ensure *Shari'ah* compliant operationalisation of the sector's currently theoretically *Shari'ah* compliant products and practices. As P1 and P11 commented, a complete transformation of the country's banking system to Islamic banking, eliminating conventional banking altogether, seems to be the one concrete step to help institutionalise it at the wider societal level. Even the country's constitution requires it to eliminate interest from the entire banking system (P15). P14 agreed with the suggestion, pointing to the cases of Malaysia and Indonesia, where he claimed the policy had proved effective. As conventional banks have extensive branch networks, both domestic and international, the State Bank of Pakistan should facilitate Islamic banks' expansion and spread of branches to combat their conventional rivals, P11 added. Furthermore, conventional banks have to meet regulations only from the country's Central bank, the SBP, while IB is subjected to several sets of regulations from various ends – SBP, Islamic *Shari'ah* law and the banks' own standard operating procedures and policies. Thus, once the country's entire banking gets transformed into IB, competition among banks will be on more equitable grounds (P11).

There are several challenges that the Islamic financial system has to counter before it can, on the one hand, claim a legitimate status with a parallel standing to its conventional counterparts in the formal regulatory circles and, on the other hand, achieve a legitimate IB status in the sight of the general public, in informal community circles. On account of the formal challenges facing the industry, the sector is in dire need of a purpose-built regulatory framework as well as accounting standards to govern the sector and ensure its objective compliance with the *Shari'ah* law requirements. Stiff competition among the conventional and the Islamic banks in this milieu is another challenge (see Akhtar et al. 2017). P13 cited innovation and variety as requisites for the IB sector to confront this competition. Furthermore, Islamic banks' navigation under regulatory environments heavily dominated by Western influences is yet another challenge that tends to raise agency costs as well in the case of IB (Vinnicombe, 2012). Conventional banks in the country still outperform IB in terms of their business development, though the latter group is more profitable (Majeed and Zainab 2017; Khediri, Charfeddine, and Youssef 2015). Again, this signals to the sector's struggle to capture a higher market share despite the higher profitability of its operations.

3.2.1. The Future Outlook

“I do agree” that we are not 100% Islamic compliant, but we still are the best alternative to conventional banking (P4, P7). P9 remarked in this connection that he met the most prominent *mufti*, advocate and supporter of IB in Pakistan at a conference, and he confirmed that IB in Pakistan, as it stands now, is not 100% Islamic *Shari'ah* compliant. However, we have taken the first step; the *mufti* was quoted as concluding by P9. Meezan Bank, the pioneer of IB in Pakistan and the largest market shareholder in Pakistan, underwent eight years of struggle to secure some legitimacy in the sight of the general public. The bank still ‘refines’ its products, in collaboration with its own dedicated *Shari'ah* Board, on a daily basis to bring them in line with *Shari'ah* jurisprudence (P7, P8). The struggle is gradually on the decline with the expansion of the industry; P10 and P14 expressed hope. P9 also seemed hopeful that he would be able to convince the public about their products in around 80% of situations.

There is a widespread misconception among the community members that wherever a rate of return is fixed, it will render the transaction un-Islamic, P14, a sitting *Shari'ah* advisor in one of the participating banks, remarked. The religious community is not studying the phenomenon or doing any research and just throwing *fatwas*, while criticism on an issue is required to be based on thorough background knowledge (P14). Another significant obstacle for IB in its way of accomplishing a widespread institutionalisation for banks involved in both Islamic and conventional banking is the combined Treasury operations for both Islamic banking and conventional banking sources of funds. *Sukook* (Islamic bonds) are government-endorsed *halal*¹³ Sources of generating funds that are not left idle sitting in a bank to earn interest, but rather invested in *halal* business ventures to earn a profit for the bondholders. The sector needs to develop more such products (P13). "IB treasury should be different" to the conventional banking treasury, P1 remarked. P7 and P8 asserted that Islamic bankers are convinced about the Islamic compliance of their products (see also Shah, Niazi and Majid 2016). However, customers always doubt it, usually pointing to the similarity between the two systems and ignoring the differences between the procedures both banking systems follow.

On account of the informal challenges facing the sector, in both the Islamic and the non-Islamic world, it needs to convince the target market - the Muslim population, of its legitimate existence as a distinct entity that comprehensively addresses all *Shari'ah* compliance requirements. The empirical data gleaned for this study clearly signalled this as a "daily struggle" (P1, P2, P3). "We do more struggle than the conventional banks", even though our products comparatively work out better for the customer, remarked P7. P11 had comments along the same lines. P8 concurred with these bankers; however, they attributed this to the lack of proper training/knowledge of the Islamic bank managers for not being able to convincingly explain the real essence of IB to clients. Most, if not all, staff in IB have joined the sector from the conventional banking sector, P8 argued. P13 commented along the same line. People keep adherence to Islamic *Shari'ah* jurisprudence so dear that they find it hard to trust bank managers who try to convince them of the new banking phenomenon, P3 asserted.

IB is a distinct form of banking (Mollah et al. 2016). Given the scale of its operations, it ought to be 'independent' of its conventional counterparts in handling its operations (Narayan and Phan 2017). Islamic banks set their daily 'return' rate based on the mainstream banks' KIBOR, and this is used as one of the main reference points by the public when objecting to the IB's non-Islamic-compliant nature (P1, P4, P5, P6). With no other reference point to resort to in our financing products, "KIBOR is the only conflict in the market we are facing", P7 remarked. KIBOR is negatively affecting customers' perception of IB (P8). Creating a distinct overall approach is the key for IB. Having the same staff attire, same in-branch environment, same transaction style, and same or similar products are all impediments to the IB's success (P4, P5). What the public does not appreciate is the way these products are operationalised (P10). The procedure behind the products is what makes a product Islamic or non-Islamic compliant, P10 further remarked. P14 concurred with this stance. The loan or the deposit agreement that governs the procedures and policies behind a financial transaction is signed by the parties. However, due attention is not paid to it by the customer, P14 noted. Though Islamic banks are in the process of eliminating any kind of reference to KIBOR from their operations and instead developing their own Islamic Inter-bank Offer Rate (IBOR), this is still not a reality. The State Bank of Pakistan is working towards it, which will resolve much of the public concerns (P8, P14).

People object to Islamic banks investing their funds in the same ventures as conventional banks. Hence, there is no difference between the two. Even though our products and bank

¹³ Permitted under the Islamic *Shari'ah* jurisprudence.

procedures are fully Islamic *Shari'ah* compliant, making people understand this and agree to it is very difficult (P3). The State Bank of Pakistan has become stricter on this, taking steps to ensure that IB's sources of deposits as well as investments are Islamic compliant, aiming to curb general public sentiments about the perceived non-Islamic compliance of the current IB. It is aiming to implement IBOR and has instructed IBs to keep their IB structure separate and distinct from that of their conventional banking operations, even keeping a separate organisational hierarchy with a separate President looking after the IB portfolio of products (P4, P8). The country's central bank has a dedicated team of IB auditors entrusted with the responsibility of auditing all IBs' operations to ensure Islamic compliance, even enforcing the use of IB-specific terminologies (*Mudaraba*, *Musharaka*, *Murahaba*, '*Rabbul Maal*', '*mudarib*', and so on) when dealing with clients (P5). P7 argued for the word 'bank/banking' to be replaced by another word in the case of IB. "I feel and face more problems...even in my relatives and social [gatherings]"; people say that I bluff with people in the name of Islamic banking, P7 continued. Most Islamic bankers face such remarks in the marketplace, he further added. "How can you prove" that IB is really Islamic? P12 said this is a question he often faces in social gatherings.

Western cultural influences have penetrated into most Islamic countries through the spread of social media and the Internet (Maali et al. 2006). However, the tight coupling of the *Shari'ah* principles with the core societal values, norms and beliefs has still prevented these principles from cracking and accommodating the 'foreign' influences. Some community groups do not even hesitate to reject a *fatwa* (religious ruling by a prominent religious scholar) endorsing IB and the person issuing it if it contradicts their core beliefs on *riba* (interest) (P6). Even the government's support would not help in this connection (Asif et al. 2017). A wide belief among Muslims, in both the Islamic and the non-Islamic world, still prevalent, is that most current IB practices and products and services are no different, in their real essence, from conventional mainstream banking (see Ahmad et al. 2013; Siddiqi 2006; Khan 2010). Several of the interview participants clearly endorsed this. The situation is exacerbated through the interaction of those with insufficient knowledge of Islamic law-compliant banking systems with those who oppose the current IB model (P1). The latter group can conveniently convince the former to distance themselves from this alternate banking paradigm (Rammal and Zurbruegg 2007; Shah et al. 2012; Hashmi 2012; Malik et al. 2011). Another prominent issue the empirical data revealed is that people associate themselves with one of the four Schools of thought, all approved and legitimate under the main umbrella of Islam, which have slightly different views of the phenomenon and the extent of its compliance with Islamic law (P6). If leaders of a particular School reject IB as non-*Shari'ah* compliant, then followers will hold on to this position until the leaders change their stance, no matter what (P11).

3.2.2. The Peculiar IB Social Practice and the Stakeholders

Social practices and routines become industry' norms' and 'institutions' only if found compliant with the expectations of the industry's 'ratifying authority', which in the case of IB is vested in the Muslim community, which in turn is derived from the *Shari'ah* law.¹⁴ In turn, the spread of institutionalised social practices occurs through what the literature terms 'mimic' and 'isomorphism'.¹⁵ Such practices may or may not have yet been conferred a 'legitimate' status by the applicable 'ratifying authority'. Hassan and Lewis (2007, pp. 2) in their book point to this foundational value of IB: "An Islamic banking and financial system exists to provide a variety of religiously acceptable financial services to the Muslim communities". However, these practices can still spread as predicted under the 'mimic' and 'isomorphism'

¹⁴ See Foucault's (2002) theoretical constructs of 'power' and 'governmentality'.

¹⁵ See DiMaggio and Powell (1983) and Scott (1995) for more details on these notions.

theoretical constructs. In the case of IB, the practices spread among all banks, whether primarily Islamic or conventional, with an Islamic wing, despite not having accomplished the 'legitimate' badge from its applicable 'ratifying authority' – the general public.

Meticulous compliance with Islamic Sharia jurisprudence is missing in the sector's products and procedures (Iqbal and Molyneux 2016). Hence, objective efforts are needed to address this. "It is a struggle every day" for Islamic bankers to convince the general masses about their Islamic compliance (P2). P1, P3 and P6 had similar views on their day-to-day efforts to convince the general public to join in. Some people even do not trust branch managers who try hard to convince them and think they are tricking them into non-Islamic compliant banking and using them to their personal benefit (P3). People trust their local mosque *imams* and *muftis* more than bank managers when it comes to IB's validity (P6). From banks' upper management to lower level employees, in addition to the *muftis*, are trying hard in this connection (P4). The struggles are worth the effort for the industry's long-term sustainability as a strong banking sector with a comparable standing to its mainstream counterpart and, therefore, deserves thorough academic input.

Clients' acceptance of IB is directly correlated to their extent of religiousness (P2). The rest of the empirical data, contrary to this notion, revealed that highly religious people are more cautious and susceptible to rejecting IB. However, P2 justified his stance, indicating that these people try to shift their responsibility to the *fatwas*-issuing scholars. Most prospective clients may well be convinced. However, they want surety from the community's recognised scholars, *muftis*, and local mosque *imams* (P6).

The particular religious School of thought people associate with also has a bearing on the level of their inclination to accept IB as legitimate, as does their geographical location in the country (P2). These Schools need to reconcile their differences as well for the sake of the betterment of the sector (P13). 'Reference' also works in the context of Pakistan. If a customer who is already convinced explains to a new audience, they are more inclined to accept his/her stance. IB customers who sign the documents usually do not read through or understand them. They mostly go by what is told to them and the extent to which someone has convinced them; advertisements through different media outlets would not help (P2). P6 and P7 opined contrary to this, saying intensive campaigns on social media and TV commercials could help create awareness among community members about IB practices and their legitimacy and should be actively employed for the purpose. P14 recommended that bank staff also need to have a good knowledge of IB as only then will they be able to present a convincing picture to the public. P7 advocated for a sitting, fully-equipped Islamic scholar in each branch. Empirical data revealed mutually conflicting demands from the public. On the one hand, they want fully compliant Islamic banking products that prohibit predetermination of profit rates on customers' deposits, and on the other hand, they want an assurance that their bank deposit would earn them a competitive profit.¹⁶

Convincing the general public of the sector's Islamic compliance has been a daily struggle for Islamic bank branch managers. "It is a struggle every day that this is really Islamic" due to "the perception in the market created by conventional banks and by public in general, which have hooked" the entire system to *riba* (P2) on the one hand and lack of awareness and education on the part of the general public on the other (P1, P2, P3, P7). P2 claimed that conventional banks were also partly to blame for the limited success of Islamic banks as they fed their prospective customers with wrong information about Islamic banks. The sector's

¹⁶ In the case of Indonesia, depositors were found to switch to conventional banks in pursuit of high returns on their deposits (see Azmat et al. 2015).

current regulatory body – the Islamic Financial Services Board¹⁷ (IFSB), does provide this platform; however, so far, it has not been able to overcome the informal challenges the sector has been facing, and since these challenges are put forth by the sector's primary audience – the Muslim population, both in Islamic and non-Islamic countries, the Board remains challenged in its attempt to reach a fully legitimate status in the sight of its target population. It is evident that the reason is not having enough input and formal representation from the religion's established scholars, which is essential to convince its target population of its endeavours as genuinely Islamic and in complete conformity with the Islamic *Shari'ah* jurisprudence.

There is also a case in favour of deducing an effective communication strategy for the sector, in addition to selling and marketing campaigns, to ensure the dissemination of a thorough knowledge of the IB products to the sector's target audiences (see Rammal and Zurbruegg 2007). Thus, a business structure has been established in the country without ensuring a sufficient supply of properly trained and educated people to run it effectively (Sheikh and Qureshi 2017). Empirical data for this study concurred with this. P2 asserted that people with a predisposition to believing that IB is not purely Islamic and those who lack appropriate knowledge in the area would argue that both banking systems are one and the same. P4, P12 and P13 expressed similar views. IB sector staff knowledge also needs to be enhanced through proper and dedicated training initiatives (P8, P12). P3 noted that people with a predisposition to IB as a non-compliant, tricky venture do not even bother to visit Islamic banks or ask questions. The sector attracts only the educated class of society with some knowledge and interest in exploring the unique banking sector, P3 remarked. Hence, the sector needs trained and dedicated staff to deal with such clientele, as is the case of Meezan Bank and Dubai Islamic Bank, where managers are formally trained in IB before they are posted to a branch (P8). A better trained/educated staff will convey a more convincing message to the public (P12), and our education system needs to incorporate courses on Islamic economics and finance, P15 suggested. We hire a large number of university graduates every year, and we always face the challenge of not having graduates with a formal education in Islamic economics and finance. We have started working with the country's prominent business schools to address this issue (P15).

On the formal challenges front, too, a need for more regulating and governing agencies is felt (Karim 2012) to help boost informal societal confidence in the sector's genuine Islamic stance. Despite the sheer size and around five decades in operations of the IB industry's profitable products and services, it took the Bank of England until 2002 to liberalise its regulative framework to accommodate IB as a legitimate niche banking system. Neoclassical theories' basic assumptions of a highly developed perfect market with unrestricted flow of communication across the Board to all market players, rational decision-making on the part of all individuals and organisations, and high turnover of transactions do not hold true in all situations and circumstances. Understandably, different countries have varying levels of market perfection, economic development, and regulatory frameworks' strength and effectiveness. Marxist notion advocates that any abnormal production cycles and market disturbances would render the notion of capitalism questionable (see Mihret et al. 2010). Thus, the neoclassical economic theories cannot explain or predict the functioning of the IB that operates under unique circumstances, varied regulatory frameworks across the Islamic and non-Islamic world, and imperfect market conditions with little organised flow of information across the market, and, thus, requires a distinct theoretical framework to explain and predict

¹⁷ The Board has 150 members that include 37 regularity and supervisory authorities, some from the mainstream financial sector, such as the World Bank, IMF, Asian Development Bank, and Islamic Development Bank (Clarke 2009).

its general functioning, social disclosure practices, and attempts to penetrate familiar and non-familiar (Muslim and non-Muslim world respectively) markets with its unique products and services.

5. Discussion and Conclusion

Organisations are socially constructed and are susceptible to people's aspirations as well as the 'power mix' of the members of their management teams, and therefore amenable to pressure modifications through certain practices that are suited to the management members' individual interests more than the sector's objective requirements (see Benson 1977). 'Power' and 'governmentality' (through knowledge, authority) that confer legitimacy to and institutionalise new social practices and their role in the construction of social reality and the institutionalisation of social practices have been highlighted in the context of the development of societies (see Foucault 2002). The IB social practice has been experiencing this since its inception. From a management accounting perspective, the sector seems to be handicapped by both the 'design quality failure' and 'conformance quality failure' (see Salimian, Rashidirad and Soltani 2017; Narayan and Phan 2017). To overcome both these shortcomings, product and service re-design, re-engineering, and innovation are the keys to success. The sector's current governing authorities and its leading constituents, resorting to the 'power' vested in them, endorse policies and practices for the sector that are not thoroughly *Shari'ah*-compliant. Given its peculiar stance and social construction 'site' put forth by the sector's 'constitution of existence' – Islamic *Shari'ah* principles, IB must remain immune to external interventions and pressure for inclusion of social practices into its portfolio that are not endorsed by its target audiences, if it is to sustain and prosper in the long run.

The sector overall is progressing well in terms of gaining wider societal recognition and endorsement. P4 and P7 expressed their contentment that the sector, though not fully compliant in its present form with the Islamic *Shari'ah* law, was a reliable first step towards establishing Islamic Banking in the country. P9 expressed similar remarks, quoting a country's prominent mufti on his stance. Meezan Bank, the country's highly recognised Islamic bank, struggled for eight years to reach its current state of societal recognition and is still refining its products (P7, P8). P10 and P14 were also content with the progress the sector was making towards its institutionalisation goal. P9 also expressed satisfaction, quoting his more positive experiences in recent times with members of the general public. To fully institutionalise, the sector must fully, rather than partially, comply with the *Shari'ah* law. Regulatory agencies are putting in an effort to convince the general public of the legitimacy of IB, and people are slowly accepting the new banking phenomenon. However, it's a daily struggle for managers to fully convince them, and it is going to be a slow process before the system gets widespread societal endorsement (P2, P14). Objective assurance and confirmation from the religious scholars, *muftis*, and local mosque *imams* will contribute greatly to this connection. However, the problem is that "they are not convinced themselves", and they hardly speak positively about it (P6, P8). P8 raised questions on these *imams*' own knowledge of the IB as well as the Islamic *Shari'ah* law. Local mosque *imams* usually are not Islamic scholars and lack appropriate knowledge about Islamic banking, P12 remarked. Hence, IB is expanding in non-Islamic countries at a much higher rate than in Islamic countries, much due to the fact that the general public there is more informed, P8 further remarked. Pakistan has a lesson to learn from IB's encouraging experience in the Middle East (P12).

The sector's constituents attempt to be seen as representing a legitimate Islamic-compliant sector. During the data collection process, the researcher observed that in most of the participating banks, the overall appearance of the bank managers and the person(s) whose part

of the job was to interact with the general public on a daily basis conformed with that of a practising Muslim (i.e. with a beard or the lady wearing the Islamic scarf/hijab), which signalled a subtle attempt at earning public's trust and convincing them of the bank's Islamic compliance. Similarly, the National Bank of Pakistan uses a distinct name for its Islamic banking branches, *Aitemaad* (a word from the Urdu language that translates to 'trust' in English). Meezan Bank's dedicated Islamic scholar, who remains mobile and visits different branches to respond to customers' queries, depicted a complete adherence to the general Islamic code of conduct from his overall attire/appearance – clothing, beard and a men-head-scarf.

The sector ought to establish its own sector-specific standing entirely independent of its traditional counterparts' *modus operandi*. Public awareness workshops, seminars and local gatherings arranged by the State Bank of Pakistan and the local mosques *Imams* and *muftis* from all four Islamic Schools of thought are crucial if the sector is destined to achieve institutionalisation at the wider societal level (P1, P2, P3, P7). People listen to religious scholars in this connection more than the government agencies, P12 noted. This group's input is significant as community members interact with them on a day-to-day basis and, in most situations, listen to and accept their advice as their immediate, convenient and reliable contact point on religious matters (P6). P4 recommended a closer interaction between the IB management and the prospective clients to understand and resolve each party's concerns. The government can help by providing appropriate infrastructure and policy framework; for instance, creating 'comfort zones' with tax reforms would help the sector gain momentum and be better established in the long run, P14 remarked. From the researcher's discussions with managers, executives and a sitting *mufti* in one of the participating banks, IB's products may be Islamic *Shari'ah* compliant; however, decades-long community perception may be hindering the sector's progress, so much so that some community groups even doubt the validity of the *fatwas* from supportive religious scholars (P6). "Give every reason to them", but their mind and heart are set on the belief that IB is not *halal* and they will never accept it (P12). P14 agreed with the statement. P7 remarked in this connection that the word 'bank' is always on the head of people, treating it as synonymous with conventional 'non-Islamic' banking. Given this, a replacement term for IB would help clients get out of their predisposition to the word 'bank' as something 'non-Islamic'.

A few prominent factors that came forth needing special attention from policymakers and regulators are lack of public awareness and psychological and societal pressure on community members. "Banking", in general, has been condemned for a long time in Pakistan by religious-minded people as non-Islamic, and the general public is still stuck hard into those feelings, avoiding the risk of violating the *Shari'ah* ruling, which is highly strict in the case of *riba*. Lack of general public awareness and objective input from the religious scholars (local mosques *imams* and *muftis*) from all four Schools of Thought; lack of appropriate training/knowledge of IB staff; and the sector's dependence on the KIBOR in its financial transactions all require objective input from the sector's governance. A stern commitment to four main responsibilities on the part of the sector's governance, which relate to the three main hurdles for IB, operational difficulties, moral hazard and government policies, Mahmood and Rahman (2017) reported in their empirical study, would help a great deal in this connection: Eliminate fixed rate of return/profit on deposits and loan products; meticulous compliance to the risk and profit and loss sharing requirement in all financial transactions; investment of funds only in *halal* business ventures; structural organisational adaptation to suit IB requirements even at the cost of profitability (trained and dedicated staff, active involvement in clients' business ventures as 'equity partners', separate treasury operations, and funding all operations from *halal* sources); transformation of the country's entire banking system into IB

leaving no other options with the public; and, including IB education in the Higher Secondary School, college and university curricula. Banks' meticulous adherence to Islamic *Shari'ah* principles must be ensured as a priority over ensuring bank profitability. P6 asserted that government intervention at the Parliament level, through promulgating laws, is crucial for the sector's long-term sustainability as a distinct Islamic-compliant banking system.

The paper aims to apprise practitioners and policymakers of the peculiar requirements the sector is missing out on in its pursuit of institutionalisation. The study's findings will bridge the gap in the literature by providing a platform for concentrated research in the area and, thus, help the sector overcome impediments to its decades-long institutionalisation struggle. Longitudinal studies in the future under varying social, economic and religious circumstances would greatly contribute to this connection.

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Appendix A (see footnote 3)

Quotes from the Holy Quran (translation of the meanings):

Chapter Al' Imran, verses 130-132(prohibiting interest/*riba*): “O you believe, do not eat up the amounts acquired through *Riba* (interest), doubled and multiplied. Fear Allah, so that you may be successful, [130] and fear the fire that has been prepared for the disbelievers. [131] Obey Allah and the Messenger, so that you may be blessed.” [132]

Chapter 2 Al-baqarah, verse 275 (prohibiting interest/*riba*): “Those who devour usury will not stand except as stand one whom the Evil one by his touch Hath driven to madness. That is because they say: "Trade is like usury," but Allah hath permitted trade and forbidden usury. Those who after receiving direction from their Lord, desist, shall be pardoned for the past; their case is for Allah (to judge); but those who repeat (The offence) are companions of the Fire: They will abide therein (for ever).”

Chapter 5 Al-māidah, verse 91 (prohibiting gambling and toxicants): Satan's plan is (but) to excite enmity and hatred between you, with intoxicants and gambling, and hinder you from the remembrance of Allah, and from prayer: will ye not then abstain?

Quotes from Sunnah:

Prohibition of interest/*riba*: “The Prophet of Allah (Peace and Blessings be upon him) cursed the receiver and the payer of *riba*, the one who records it and the two witnesses to the transaction and said: they are alike (in guilt)”

Prohibition of uncertainty/*Gharar*: The Prophet (s.a.w) has forbidden the purchase of the unborn animal in the mother’s womb, the sale of the milk in the udder without measurement, the purchase of spoils of war prior to distribution, the purchase of charities prior to their receipt, and the purchase of the catch of a diver.

Appendix B (see footnote 4)

Illustrations of a typical Islamic compliant loaning/banking transaction:

1. Mr A, an experienced small business owner (bring in *riba*, pls, *gharar*, risk, halal business), started his loan application for US\$50,000 to Bank Ethics (an Islamic bank) on January 1, 2018. His loan application got finally approved by the bank on July 1, 2018 after a few revisions of his application in the light of the bank’s requirements. Mr A wanted the loan for establishing a small retail store for selling alcohol. However, he intended to do this after the sale of his home which he had put up for sale recently to arrange a \$30000 capital into the proposed small business, and after his uncle agrees to join him in the business as a partner. The concerned bank officer agreed in principle to sanction him the loan at an interest rate of 10% per annum irrespective of whether Mr A’s proposed business turns a profit or loss. The loan application was reviewed by the bank’s sitting Shari’ah advisor and asked for the following amendments to the proposed loan agreement to render it eligible for an Islamic compliant loan: 1. Mr. A must invest the money into a halal (permitted under the Shari’ah law) business venture; 2. The loan agreement must be in the form of a ‘joint venture’ between the bank and Mr. A where both parties must share in the profit/loss of the business in the ratio of their respective capital contribution to the ‘joint venture’ with no prior specification of interest rate; 3. Mr. A must remove the *gharar* (uncertainty) of selling his home and his uncle joining him as his business partner. After these conditions are met, this would be a typical Islamic compliant business transaction, called *Musharakah* or *mudarabah*.

2. A *murabahah* transaction involves buying of a good that the borrower wants to buy (a car or a home, for instance) by the Islamic bank on behalf of the borrower and then selling it to the borrower at an increased priced, duly agreed to by the borrower in the light of the agreed upon specifications of the good, where the borrower agrees to repay to the bank the 'resale price' in instalments over an agreed time period. is: Mr. X wants to buy a Proton Waja car but he does not have cash money. He approaches to the Islamic bank to buy the car. The Islamic bank will ask the customer (Mr. X) to provide with detailed specifications of the car, year, colour, automatic or manual, maximum price etc. The Islamic bank will make a contract with the customer that it will buy the car and sell to the customer with a mark-up profit and the customer will be given an opportunity to pay by installments for a fixed period say five or ten years. When this contract is signed by the customer, the Islamic bank will buy the car in accordance with the specifications provided and sell it to the customer with installment facilities.