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MUDARABA FINANCIAL PRODUCT AND PERFORMANCE OF COMMERCIAL BANKS IN GARISSA COUNTY.

* Abdirahman Ali Dahir, [1]Dr. Peter Butali & [2] Dr. Robert Odunga

** Master Student*, School of Business and Economics, *Garissa University, Kenya*

[1]*Lecturer*, School of Business and Economics, *Garissa University, Kenya*

[2]*Lecturer*, School of Business and Economics, *Garissa University, Kenya,*

Corresponding Author Email: abdirahmandahir258@gau.ac.ke

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ABSTRACT

Financing is the engine of any business irrespective of its nature and therefore should be a top priority to any firm's management. A lot of debate on the subject of Islamic finance which is highly inclined on the Islamic religion has therefore been a contemporary issue in the field of finance. This research aimed to investigate the influence of Mudaraba Islamic Financial Product on the Performance of Commercial Banks in Kenya. The study was guided by One Tier Mudaraba Model. Descriptive research design was employed. The study population was 138 employees from 6 Commercial Banks in Garissa, Kenya offering Islamic finance products namely, Absa bank, Commercial Bank, Equity Bank, National Bank of Kenya, Gulf African bank and Premier Bank. The study used primary and also secondary data with questionnaires being used in collection of primary data and data collection sheet utilized in the collection of secondary data. After collection, the data was coded and edited before being analyzed through SPSS tool. Descriptive statistics alongside inferential statistics were generated. Mudaraba financing was found as having positive significant relationship with commercial banks performance and as explaining 55.6% variations in commercial banks performance. Recommendations of the study is for the banks to enhance this Islamic product especially in terms of information to customers and public. Data was presented via tables and graphs and the study will be useful to management of Commercial Banks, key policy makers' scholars and other researchers.

Keywords: Mudaraba Financial Product, Performance of Commercial Banks, Garissa County

BACKGROUND OF THE STUDY

Islamic finance stems from the jurisprudential body of knowledge known as Shariah, whereas its principles are derived from Qur'an (the Holy book) and from Sunnah that governs the economic activities, social activities all muslims' undertakings. Among the chief goals of Islam religion is maintaining justice in society (Chapra, 2008). According to economic framework of Islam, it is not possible to attain viable development in absence of justice as injustice eventually results to destruction (Qur'an 57:25). Islamic economic system stimulates justice mainly in two ways, that is, by financier sharing the risk of the entrepreneur and having an equitable resource sharing to enable the poor eradicate poverty, to expand employment opportunities and also to reduce income inequalities (Ahmed, 2015). Thus, Islamic finance aims at establishing an equitable economic and financial order whereas also achieving a transaction-friendly order (Rethel, 2011). Ultimately, there should be spreading of socio-economic justice to everyone irrespective of their social status (Kayed & Hassan, 2011). Globally, in 1963 the first contemporary Islamic Bank was established in Cairo, Egypt and it aimed at offering the ordinary deposit and loan facilities to local businessmen through sharing profit-and-loss as opposed to interest charging (Rundell, 2018). Subsequently, the Islamic banking system has developed to a vital component of global banking generally driven by financial products from Muslim populations in Middle East and Asia (Odongo & Muchelule, 2019). In Africa, Islamic banking has developed into a masterpiece with numerous market regulatory and development efforts being taken by several countries, recently so as to enable Islamic Finance products be offered in those countries (Negara Malaysia, 2017). In Kenya, the financial regulators have allowed Islamic finance to thrive and Kenya may become a hub of Islamic banking in Eastern region (Dahir, 2017). The country already has an Insurance company by name Takaful, which is sharia compliant mutual fund as well as two SACCOs (Odongo & Muchelule, 2019). Additionally, Kenya has joined the IFSB, a body which promotes and regulates sound Islamic banking products globally (Dahir, 2017).

STATEMENT OF THE PROBLEM

Financing is the engine of any business irrespective of its nature and therefore should be a top priority to any firm's management (Nagaoka, 2007). The banking industry is one of the key pillars in achieving vision 2030 through enhanced savings, FDI encouragement, economy safeguard from internal and external shocks and driving Kenya to a prominent financial epicenter in East and Southern Africa. Since the introduction of Islamic banking, there are few enterprises that have accessed and benefited from the financing products in Kenya (Ahmed, 2015).The deterred growth in the Islamic financing in Kenya are related to the lack of information on emerging issues in Islamic financing that are in line with the Sharia laws (Ahmed 2015). According to Ahmed (2015) most businesses never accessed banking services and financing from the Islamic banks in Kenya due to illiteracy and lack of information on the contemporary Islamic financing issues.

A lot of debate on the subject of Islamic finance which is highly inclined on the Islamic religion has therefore been a contemporary issue in the field of finance. To date, research on Islamic finance is disjointed and ad-hoc (Aklin, 2009). Nasir (2012) in his study observed that the Islamic enterprises in Kenya had realized considerable growth in the last decade as a result of support of Islamic Financing from the religious leadership. However, most Islamic businesses have very limited options on banking services, investment services, insurance services and other financial services. The above research studies have however not addressed the effect of Islamic financing products on the profitability of Commercial Banks in Kenya which is the hub of Islamic businesses in East Africa. By studying the effect of Mudaraba finances on performance of Commercial Banks in Kenya, this study will seek to address the subject and suggest probable solutions that will open up the economy.

OBJECTIVE OF THE STUDY

To explore the effect of Mudaraba (Equity sharing) financing on performance of commercial banks in Garissa County, Kenya.

THEORETICAL LITERATURE REVIEW

The study was supported by One Tier Model. One tier model is an adaptation of the Islamic banking early works that were based on conventional modes of finance specifically Mudaraba. In practice Islamic banks experienced several difficulties while using these traditional modes. Subsequently, there have been evolvement of practices in Islamic banking that have made significant contributions to new modes of Islamic banking alongside the theoretical development of instruments in Islamic finances. These traditional modes were founded on either Musharaka (partnerships) or Mudaraba, that is, equity sharing (Mirakhor, 2007). Currently, Islamic banking practice has evolved to include various types of temporary, permanent and also declining partnerships built on Musharaka and Mudaraba principles but which have adaptable arrangements in respect of managerial responsibilities. With respect to this study, this theory aligns with objective as concerns the effects of adapted Islamic traditional methods of finance namely Mudaraba on the performance of the commercial banks in Kenya.

CONCEPTUAL FRAMEWORK

Finance Product

Mudaraba (Equity Sharing)

- Amount of short term projects funded
- Amount of medium-term

Independent Variable

Performance

Commercial Banks Performance

- Profitability

Dependent Variable

EMPIRICAL LITERATURE REVIEW

The writings of previous researchers were reviewed including Habiba and Yusoff (2019) surveyed impact that Mudarabah financing had on performance of Tanzanian commercial banks. The study established that Mudarabah financing positively and significantly affected performance of those commercial banks. Odongo and Muchelule (2019) study was on Mudarabah loans effect on financial performance of Kenyan commercial banks and was conducted in Nairobi County involving ten commercial banks. The study conclusion was that Mudarabah loans negatively and insignificantly influenced commercial banks financial performance in Nairobi. Mohammad (2019) conducted a study on Mudaraba contracts influence on financial performance of United Kingdom commercial banks. This study findings were that there existed a negative influence of these Mudaraba contracts on the commercial banks performance. Idries, et al., (2018) investigated the impact that Mudarabah loans had on profitability of Jordan Islamic based banks. The study findings indicated the existence of a grave challenge with the Mudarabah loans for those Islamic banks operating in countries with a hybrid structure in form of Islamic and conventional banks. The problem emanated from borrowers preferring conventional banks when they anticipated high ROI but running to Islamic banks in cases of anticipated low returns.

RESEARCH METHODOLOGY

Descriptive research design was employed in the study, analyzing Mudaraba Islamic financial product alongside the performance of commercial banks. This design involved with data collection from a population so as help conclude on the current position of the target population in respect of some variables (Kothari, 2008). By use of this descriptive survey, the researcher answered questions regarding the topic under study. Data were collected from the six commercial banks offering Islamic financial products in Garissa County, Kenya namely Absa bank, Equity Bank, National Bank of Kenya, Gulf African bank and Premier Bank. The target population was 138 employees in the six commercial banks currently operating within Garissa County. The employees include those in Top management, middle management and lower cadre. The study's sampling frame was derived from listed licensed commercial banks offering Islamic financial products and operating in Garissa County as obtained from Central Bank of Kenya website database, December, 2021. The sample size was determined based on Nassiuma's (2008) formula and the researcher used simple stratified sampling technique in coming up with the study's sample. Descriptive statistics conducted generated measure of spread in form of standard deviation and central tendency measures which included means and standard deviations. Inferential analysis was through multiple regression models and was used in establishing the nature and degree of relationship between the response and the predictor variables. The regression model was in form of Performance Y (Performance) = $\alpha + \beta 1X1 + \mu i$ Where: X1= Mudaraba, α =Constant, βn=Coefficient of Mudaraka predictor variable and μi the error term. Findings were presented in charts and tables.

RESEARCH FINDINGS AND DISCUSSION

Of the 65 questionnaires distributed, 53 were filled and returned. This was a response rate of 81.54% which was considered good as a response rate of at least 70% according to Mugenda & Mugenda (2003) is very good. Influence of Mudaraba financing with regard to commercial banks performance was evaluated using Likert scale in obtaining the respondent's views.

COMMERCIAL BANKS PERFORMANCE

The research sought to determine the extent of performance of commercial banks in Garissa County, Kenya with data being collected by use of a questionnaire and on average, the indicators of commercial banks performance in totality were either high or modest as shown in table 1.

Table 1: Commercial Banks Performance

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Profit Increase	6%	36%	39%	17%	2%
Asset Increase	6%	30%	49%	13%	2%
Deposit Increase	10%	30%	43%	15%	2%
Income Increase	2%	26%	55%	15%	2%
Customer Increase	6%	32%	43%	19%	0%
ROI Increase	4%	39%	42%	15%	0%

MUDARABA FINANCING

On whether mudaraba financing influenced performance of commercial banks, massive number (87%) were in agreement. Thus the findings show that bank employees were aware that mudaraba financing was central to the banks performance.

Table 2: Mudaraba Financing influence on Commercial Banks Performance

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	46	86.8	86.8	86.8
	No	7	13.2	13.2	100.0
	Total	53	100.0	100.0	

The study further established that each mudaraba financing component was rated modestly with amount of short-term projects funded under mudaraba getting the maximum rating of 3.28 on average.

Table 3: Components of Mudaraba Financing

	N	Minimum	Maximum	Mean	Std. Deviation
INFORMATION REGARDING MUDARABA	53	2.00	5.00	3.1132	.75091
SHORT TERM PROJECTS WITH MUDARABA	53	2.00	5.00	3.2830	.76905

MEDIUM TERM PROJECTS WITH MUDARABA	53	2.00	5.00	3.1509	.74411
Valid N (listwise)	53				

REGRESSION ANALYSIS

Commercial banks performance was regressed on mudaraba financing yielding a p-value = 0.000. Since the generated p-value, was below 0.05, the researcher drew the conclusion that there existed a substantial influence of mudaraba financing on performance of commercial banks in Garissa County.

Table 4: ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	18.459	1	18.459	66.195	.000[b]
	Residual	14.222	51	.279		
	Total	32.681	52			

a. Dependent Variable: commercial banks performance

b. Predictors: (Constant), mudaraba financing

The regression coefficient between mudaraba financing and performance of commercial banks shows that the model intercept was 0.157 and the slope was 0.997 with p-value being .000. This was an indicator of a significant positive influence of mudaraba financing on performance of commercial banks.

a) Coefficients

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.
1	(Constant)	.157	.397		.396	.694
	MUDARABA FINANCING	.997	.123	.752	8.136	.000

a. Dependent Variable: commercial banks performance

CORRELATION ANALYSIS

The researcher sought to determine the strength of relationship between the variables used in the study using Pearson Correlation. Pearson correlation (r) shows the extent of linear relationship between variables, and how the change of one will affect the other. Pearson Correlation (r) ranges from -1 to +1, where a negative value depicts a negative relationship, zero depicts no relationship and a positive value depicts a positive relationship, Turney (2022). The table 4 shows that mudaraba financing was highly correlated with banks performance with correlation coefficient of 0.752. Coefficient of determination, R^2, was found to be 0.556 showing that 55.6% of variation in banks performance was explained by Mudaraba independent variable.

Table 5: Correlations

		Commercial banks performance	MUDARABA FINANCING
Commercial banks performance	Pearson Correlation	1	.752**
	Sig. (2-tailed)		.000
	N	53	53

MUDARABAFINANCING	Pearson Correlation	.752**	1
	Sig. (2-tailed)	.000	
	N	53	53

**. Correlation is significant at the 0.01 level (2-tailed).

The study assessed what influence Mudaraba financing had on commercial banks performance in Garissa County, and again the overall level of mudaraba indicators ratings was modest with a mean score of between 3.11 and 3.28. Mudaraba financing was also found as having a positive and significant influence on commercial banks performance in Garissa County. ANOVA test revealed a p-value statistic was 0.000.These results are in agreement with Habiba and Yusoff (2019) who surveyed the impact that Mudarabah financing had on performance of Tanzanian commercial banks. The study established that Mudarabah financing positively and significantly affected performance of those commercial banks.

CONCLUSION

The study concluded that mudaraba financing highly influenced commercial banks performance in Garissa County, Kenya. This was evidenced by a p-value statistic of $0.000<0.05$ and correlation coefficient, $R=0.752$ generated by regressing performance of commercial banks in Garissa County on mudaraba financing.

RECOMMENDATIONS

The findings established that mudaraba financing had a strong positive influence on commercial banks' performance in Garissa County, Kenya. Thus, the study offers the recommendation that the banks ought to improve on mudaraba financing especially in terms of informing customers and public about mudaraba financing as it was modestly ranked.

AUTHOR'S CONTRIBUTIONS.

Abdirahman Ali Dahir wrote the proposal and this article. Under the guidance and supervision of Dr. John Gitau Kagumu and Dr. Samuel Nyambega, he sought permission from relevant institutions, collected the data, analyzed it, and finally published this article.

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CONFLICT OF INTEREST DECLARATION.

The author declares that there exists no conflict of interest concerning this publication. High ethical standards were observed in the course of the whole research.

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