



## Emerging Islamic Banks in the KSA: The Case Study of Alinma Bank

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**Abstract:** *The main purpose of this case study is to specify the key factors that assist Alinma Bank in achieving its objectives and to ensure continuous business operations carried out by the bank in the event of a disaster. In addition, it discusses the fintech employed by the bank and the lessons learned from its experiences. Moreover, the case study highlights the role of the Shariah board in monitoring and supervising the banking products and services in accordance to Islamic principles*

Keywords: Fintech, Alinma Bank, Islamic Banking, KSA

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### INTRODUCTION

Islam is the second largest religion in the world. Its adherents or Muslims constitute approximately 1.8 billion among the world's population. They are largely distributed in 57 countries of the world including Saudi Arabia. Islam is the state religion of the Kingdom of Saudi Arabia (KSA). The relationship between Islam and the Kingdom is unique due to the presence of the two Muslim holy cities i.e. Makkah and Medina. Islam plays a pivotal role in shaping the Saudi society. It is more than just a religion rather it is a way of life and a primary source of reference for all political, socio-cultural, educational and legal provisions and procedures, especially commercial transactions. Operations of the majority of Saudi Arabian companies, their corporate governance, activities and business dealings are predominantly based on the teachings of the Islamic faith.

Indeed, the fundamental Islamic teaching is the prohibition of *Riba* (interest). In the past, it succeeded in safeguarding the exploitation of poor borrowers who used to be charged exorbitant interest rates by wealthy lenders. In the modern day banking system *Riba* is still prevalent because the capitalistic system operates in a regulated setup and charges market-based interest rates. This subtle rationale regarding exploitation of the poor seems less compelling though. However, Islamic banking and finance relies on the cardinal principle of Profit and Loss Sharing (PLS) between parties that are taking part

in a risky economic activity. Alinma Bank is reputed to be one of the successful examples of companies based on the provisions and controls of *Shariah* principles in its banking and finance services in Saudi Arabia. The bank adopts a rule whereby bank depositors could choose either not to be remunerated at all (at the expense of suffering even a loss), or place their savings in the “investment accounts”. Moreover, this incurs not a fixed rate but a variable Rate of Returns (ROI), depending on the bank’s profitability margin. Thus the Alinma bank has to share its “profits” at the end of the accounting period with the depositors who are willing to accept the investment risk in the first place.

In fact, generally Islamic banks do not normally share all their “profits” but partially retain them for future investment needs. These are shared wealth transferred to shareholders called “Income Before Cost of Funding” (IBCF). Meanwhile, Alinma Bank provides assistance to its clients to do their businesses by providing an array of *Shariah*-compliant corporate financing products such as:

1. LC *Murabahah*
2. *Bai al-Ajel*
3. Forward *Ijarah Murabahah*
4. Forward *Ijarah Musharakah*
5. *Al-Ijarah*

Remarkably, these products succeeded in sustaining the profitability of Alinma Bank as evidenced from their lucrative Return on Equity (ROE). Hence, the purpose of this case study highlights three main concerns as follows:

1. In theory, an Islamic bank is effectively in a position to make its profitability less volatile over the cycle, thanks to the provision of profit-sharing.
2. In addition, empirical evidence tends to show that Islamic banks are certainly more profitable than their conventional peers as they enjoy the same balance sheet structure. The main reason for such a difference is that Islamic banks benefit from the market imperfection i.e. the availability of large amounts of non-remunerated deposits in their books, which considerably decreased the cost of funding.
3. Finally, Islamic banking, in spite of its advantage on the grounds of profitability, is not a panacea for bankers in the Islamic world, because they are constrained by several recurrent weaknesses in terms of liquidity, concentration risks and operational efficiency.

## **BACKGROUND**

Alinma Bank was established as a Saudi public shareholding company according to the Royal Decree dated 28/2/1427 AH corresponding to 3/28/2006, and the Commercial Register No. (10102-250808) dated 21 Jumada al Awwal 1429 AH corresponding to May 26, 2008 AD, to provide banking and investment services that are in compliance with *Shariah* rules and regulations.

The main activity of the bank is to provide a comprehensive range of *Shariah*-compliant banking services. Alinma Bank works to meet the needs of partners and

strives to provide the best services available to its institutional and individual partners through its 170 locations (95 branches for men, 71 branches for women and 4 sales centres) as at the end of 2019. Alinma Bank is equipped with the latest technologies and trained human competencies. Also it provides the latest facilities of contemporary electronic products such as the bank's website, the bank's phone, the bank's application for smartphones, and widespread ATM network throughout the Kingdom which numbered 1,523 teller machines at the end of 2019.

The capital of the bank, reached fifteen thousand million Riyals (15,000,000,000) divided into one thousand five hundred million (1,500,000,000) nominal shares and ordinary shares of equal value i.e. ten (10) Riyals each.

The ownership structure and the founders of the bank comprise of the Public Investment Fund, the Public Pension Agency, and the General Organization for Social Insurance, where each of them was allocated 10% of the bank's shares upon incorporation, and 70% was offered for shareholders of Saudi citizens during Rabi` al Thani 1429 AH corresponding to April 2008.

Table 1: Financial Results (2015-2019) in (millions)

<i>Years</i>	2015	2016	2017	2018	2019
Net financing	57,006	70,312	79,063	83,889	94,801
Investments	23,565	23,799	25,108	18,399	23,478
Total assets	88,725	104,730	115,005	121,538	131,839
Customer deposits	65,695	80,612	89,065	90,128	102,063
Total liabilities	70,372	85,551	94,408	100,240	109,395
Shareholders' equity	18,352	19,178	20,344	21,298	22,445

**Source:** Annual Reports of Alinma Bank

The financial performance of the bank gave an impression that strategic direction of the bank is proved to be the right type i.e. producing healthy financial results as shown in Table 1 and supported by the last five years annual operational outcomes as elaborated in Table 2.

Table 2: Operational Efficiency

<i>Operational results</i>	2015	2016	2017	2018	2019
Net income from investment and financing	2,279	2,652	3,493	3,798	4,394
Income from fees and banking services, currency exchange and other income	784	676	880	1,047	1,216
Total operating income	3,063	3,328	4,373	4,845	5,610
Total operating expenses	(1,285)	(1,513)	(1,751)	(1,861)	(2,087)
Net income before deduction of provisions	1,778	1,815	2,622	2,984	3,523
Provisions for impairment of financing other assets	(308)	(313)	(611)	(467)	(706)
Net income before <i>zakat</i>	1,470	1,502	2,011	2,517	2,817
<i>Zakat</i>	271	(42)	104	340	(282)
Net income after <i>Zakat</i>	1,199	1,502	1,907	2,857	2,535

**Source:** Annual Reports of Alinma Bank

Nonetheless, there needs to be a synergy in the strategic and structure since structure follows the strategy for a successful organizational management. Figure 1 below is the High Level organizational structure of Alinma Bank. This strong management team is said to be one of the reasons behind the bank’s success.

The bank is managed by a board of directors comprised of nine people appointed by the shareholders in the ordinary general assembly for a period of three years. They are Dr. Abdul-Malik bin Abdullah Al-Hogail (Chairman of the Board) and Dr. Hamad bin Sulaiman Al-Bazei (Vice-Chairman of the Board) and the rest of the members of the board are Mr. Abdul Mohsen Al-Faris and Prof. Muhammad Dayel, Professor Abdul Mohsen Al-Hussein, Eng. Mutlaq Al-Murished, Professor Abdul Rahman Addas, Dr. Saud Al-Nimr, and Professor Haitham Mubarak.

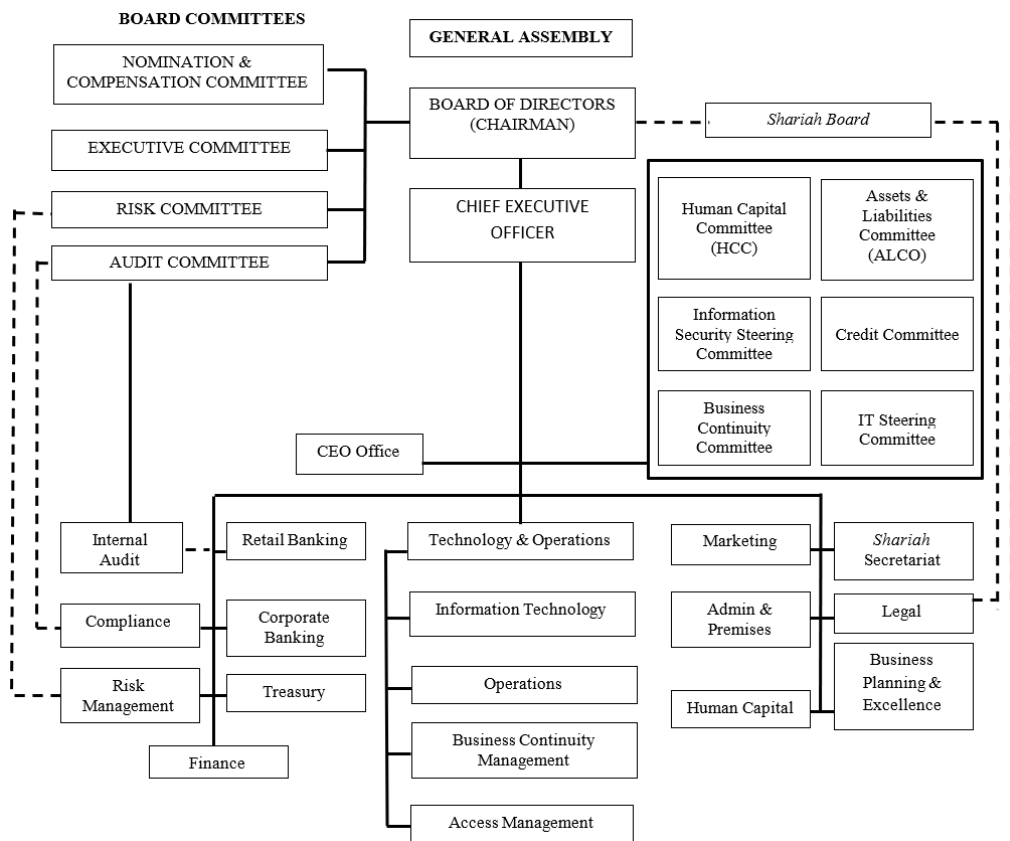


Figure 1: Alinma Bank - The High-Level Organization Structure

The Board of Directors has formed committees to help them perform their duties and responsibilities more effectively. These committees include the Executive Committee, the Nomination and Remuneration Committee, the Audit Committee and the Risk Management Committee. Also, the bank consists of 14 functional departments.

## COMPETITIVENESS OF SAUDI BANKS

Saudi banks are among the most important pillars of the Saudi economy since the establishment of the Kingdom, as the strength and durability of the banking sector increases the strength of competition for the Saudi economy globally. The Saudi banking institutions play a prominent role in the growth and economic development in the Kingdom. They have contributed to the recruitment of national cadres, the increase and rotation of capital, and the support of government and private sector institutions with loans that have contributed to the expansion of their projects. The banking sector has considerably contributed funds to the training needs of Saudis who have joined to work in its banks. A large number of the trained personnel occupy high leadership positions that contributed to making strategic decisions that we see today. Also, increasing competition in the banking sector actually increases the efficiency and effectiveness of banks in terms of performance and dealing with employees and customers and providing various products and developed services that suit customers' needs. Also, competitiveness increases the eagerness of banks such as Alinma Bank to contribute to community service in order to reach a strong competitive position against other banks in Saudi Arabia.

Therefore, in order to maintain its competitiveness and maintain its market share locally and globally, the Alinma bank continuously develop its services and offer various options for its clients in terms of loans and investments, meet the requirements of the business sector, expand and diversify its investment portfolio, and enter foreign markets through various joint-venture projects to reduce risks and increase opportunities for success.

## MANAGEMENT OF ALINMA BANK ACCORDING TO ISLAMIC TEACHINGS

As mentioned earlier, the majority of companies in the Kingdom of Saudi Arabia practice their corporate governance and administrative procedures based on the provisions of *shariah*. Alinma Bank is no exception as it seeks to promote Islamic principles especially observing strictly the five pillars of Islam in its management practices and provisions.

### **The *Shariah* Board: Objectives and Tasks**

The Banks has its own *Shariah* board that ensures all banking services and products are implemented in accordance to Islamic principles. Below are the major objectives and tasks performed by the *Shariah* Board at Alinma Bank:

#### ***Objectives***

Statement of *Shariah* provisions in all bank transactions including:

- Verifying *Shariah* compliance in all bank transactions.
- Contributing to the development of the bank's performance in terms of *Shariah* and preserving its Islamic identity in policies, standards, procedures, and the like.

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- Enhancing the bank's participation in introducing Islamic banking and contributing to its development.

### ***Specialties and tasks***

The committee shall have the authority to consider *Shariah* law in all the bank's transactions and activities, and to monitor *Shariah*'s performance, whether inside or outside the Kingdom of Saudi Arabia. Among the most prominent of these are the following:

- Reviewing all bank transactions, contracts, agreements, forms, documents etc. and issuing what is necessary in their regard.
- Contributing towards product innovation and development in the light of the provisions of Islamic law.
- Monitoring the bank's compliance with the provisions of Islamic law in all its activities and transactions, and ensuring that the committee's decisions are properly implemented.

Approval of *Shariah* supervisory standards:

- Study *Shariah* performance reports and control notes and issue the necessary actions in this regard.
- Set legal controls to get rid of sums excluded as a result of a *Shariah* violation, and supervising their disbursement.
- Review of the financial statements of the bank before approval by the Board of Directors, and this includes ensuring that *Zakat* is calculated in a *Shariah* manner.
- Issue the periodic report on the bank's performance from the *Shariah* point of view, announce it to the shareholders, and answer any shareholders' queries about it.
- Evaluate the Secretariat's technical performance.

### **Islamic Concepts as the Source of Business Policy for Alinma Bank**

Alinma Bank relies on a set of Islamic concepts in its management practices and its internal and external environment. The following are the main concepts:

**Mastering** -One of the goals of Alinma Bank is to strive for and encourage mastery and excellence in work. To this end, the Bank has organized a series of continuing education and development activities, including:

-Implementing a 7140 training days for the bank employees, and the training include cognitive, skill and behavioural courses in the banking, financial, legal and administrative fields. These are provided by a number of specialized expertise houses in the fields of training. In addition, courses of automated systems, products and services are also provided by the bank.

- Development of e-learning materials targeting all bank employees in the field of banking products, business continuity, information security and compliance.

- Completion of the personal mentoring program(Coaching Program) with a total of 113 participants from managers in Alinma Bank, with the aim of providing them with the most important leadership skills, such as listening and directing useful

questions between the manager and his subordinates. It also aims to enhance communication between bank employees.

**Encouragement of good deeds** - Since its establishment, Alinma Bank has been building a work environment committed to the highest ethical standards stemming from *shariah* rulings, regulations, and instructions issued by the Kingdom's regulatory and supervisory authorities. The bank is constantly working to familiarize its employees with work ethics to improve customer service. The bank also encourages its employees through training and awareness programs to adhere to transparency, sensing responsibility, creativity at work, good dealing with clients and colleagues at work, and avoiding anything that contradicts with Islamic values or conflicts with the values of the bank or Supervisory systems or controls, and working to establish those values with all bank employees.

**Adl (Justice)** - Alinma Bank has fair procedures and regulations with regards to the appointment of employees and the distribution of tasks, salaries and penalties. Appropriate compensation policies are followed in accordance with the instructions issued by the Saudi Arabian Monetary Agency and the principles and standards adopted by the Financial Stability Board. This system is in line with the overall performance of the bank and the performance related to each job as per the performance appraisal. In addition to that the bank regularly reviews its compensation policies and makes adjustments to it when necessary.

**Falah (gain)** - One of the important obligations and basic principles of the bank is social responsibility and community service. It always encourages the bank's management and engages its employees in its social initiatives. Examples of the bank's activities in the field of social responsibility are:

- Alinma Bank donates 1000 Ramadan baskets distributed to needy families in several regions of the Kingdom as part of the bank's activities in the field of social responsibility. Its employees participate in preserving food from waste in cooperation with the Food Charity Association (Ata'am). They also contribute to a voluntary campaign with the association to distribute surplus food to needy families in the city of Riyadh.
- Blood donation campaigns

In order to raise awareness among its employees of the importance of blood donation, in 2019 Alinma Bank implemented a number of blood donation campaigns in cooperation with the King Faisal Specialist Hospital and Research Centre. This inculcates health culture among its employees as this initiative serves the noble purpose that contributes to saving the lives of others.

**Ikhlas (sincerity):** The bank has basic values and principles that guide it in setting its goals, preparing plans and building strategies, and employees are obligated to work on the values to achieve sincerity and effectiveness in their work and services to partners. They are encouraged to strive to lead, practice honesty, strengthen relationships, serve their partners, innovate, respect, take initiatives and serve the community at large.

## Leadership by Example

The leaders of Alinma Bank are distinguished by the characteristics of the servant and guardian leadership style, as the bank managers are keen on sharing power and serving the needs of workers, training and assisting them in developing their performance and reaching their goals. In addition, the bank applies the concept of *shura* in decision-making as it organizes periodic meetings involving all departments and various levels to discuss current issues, suggestions and decision-making.

### **Major leadership concepts practiced are as follows**

*Listening:* The leaders of Alinma Bank encourage employees in various departments to express their opinions, suggestions, and complaints through periodic meetings or through direct contact with senior management.

*Awareness:* Each department manager at Alinma Bank has sufficient awareness about the workers in its department, what are their strengths, what are the weaknesses and what are their needs.

*Commitment to the Growth of People:* The leaders of Alinma Bank are committed to develop and support employees by providing knowledge, skills and behavioural training courses in the banking, financial, legal and administrative fields and constantly evaluating employee performance to ensure the success of the development process.

*Foresight:* During some of the bank's crises, the bank's leaders have proven that they have the ability to make courageous and decisive decisions through perception and their ability to imagine the possibilities and consequences and make the right decisions.

### **Implementation of Islamic Management System by Alinma Bank**

Alinma Bank has an Islamic management system, which is the bank's commitment in all its transactions to the provisions and controls of Islamic *shariah* as the articles of association of the bank stipulated in Article 50 that all the company's activities are subject to the provisions and controls of the Islamic *Shariah*. In 2007, the Bank appointed a *shariah* Board that outlined *shariah* provisions in all of the bank's transactions. And to verify the legal commitment in all the bank's transactions, and the board includes in its membership a number of distinguished scholars who specialize in the jurisprudence of financial transactions and economics, and supports the *Shariah* committee in achieving its goals and performance of its business. The secretariat of the *Shariah* Board is an administrative group within the bank's organizational structure.

Here are some of the functions of the *Shariah* Board in the bank:

- Contribute towards product innovation and development in the light of the provisions of Islamic *Shariah*.
- Monitor the bank's compliance with the provisions of Islamic *Shariah* in all its activities and transactions, and ensure that the decisions of the Authority are implemented properly.
- *Shariah* review of the bank's financial statements before they are approved by the Board of Directors and this includes verifying the *Zakat* account in a legitimate manner.
- Evaluate the technical performance of the secretariat.



Islam urges virtuous acts and ethics that enhance the quality of life in various aspects, especially in work. God requires from His servants while performing their work honesty and sensing God's observation on them. They are also urged to work and complete their tasks to the fullest extent. In addition Islam also preaches employees to cooperate and provide assistance while dealing with colleagues at work or with clients while sensing the reward of God to them. Moreover, Islam teaches people to start with greetings, smile and give good treatment to others. This contributes to creating a comfortable and positive work environment, therefore if the Muslim employee adheres to Islamic principles while working inevitably this will increase the effectiveness and efficiency of his performance.

Alinma Bank provides special facilities for Muslims such as places designated for prayer (Mosque or Musalla) in all its branches. Also it allows workers to take a break to perform the daily prayers. During the month of Ramadan the bank introduces working time changes and even reduces working hours to accommodate Muslim employees. Finally, the bank provides official holidays such as Eid al-Fitr and Eid al-Adha. Finally, the bank grants paid expenses for Muslim employees wishing to perform the Hajj.

### **The Digital Services**

In addition, Alinma Bank consistently develops and offers a wide range of digital banking services to suit the needs of clients throughout the day. The available digital services include:

- Immediate issuance of a bank cheque in Saudi riyals.
- Immediate issuance of a cheque book.
- Immediate printing of a bank balance certificate.
- Immediate printing of the account statement.
- Immediate printing of proof of deposit.
- Interactive teller services for "large withdrawals and deposits".
- Small denominations exchange services such as "five and ten riyals."
- Opening a current account for "new partners" through the self-service machine and printing the Alinma Mada Card.
- Update the personal data of the client account.
- Authentication of the personal signature of the digital account.

### **CONCLUSION**

From the beginning, Alinma Bank has persistently endeavoured to achieve its vision to be the preferred financial partner for all of its partners, whether individuals or companies, by providing distinctive and innovative products and services in a manner and approach consistent with the provisions and jurisdictions of the Islamic *Shariah*. The bank has shown its keenness and influence to be present in all parts of the Kingdom of Saudi Arabia through a network of bank branches and ATMs. In fact, the bank has achieved this amazing vision by achieving several awards in 2019 namely the Excellence Award in Islamic Banking, the Best Bank Award in Corporate Banking and the Global Standard for Business Continuity Quality. Furthermore, to the bank had succeeded in creating attractive and suitable working environments for its Muslim

employees and also attracted the largest number of clients and partners by providing various and distinctive services that are compatible with the rules and provisions of Islamic law and with the culture of the Saudi society. The bank's exemplary contributions in community service and Corporate Social Responsibility (CSR) programs via its *Zakat* payment has benefitted the poor, the needy and other *asnafs*.

### QUESTIONS

1. Do you think that the Islamic concepts applied by the Alinma bank contributed to its success and why?
2. Despite the increases in assets value there seems to be a dip in investment during the year 2016. Also the bank did not show any increased income from fees and banking besides not paying attention to net income after Zakat. What could be the justification?
3. Can Alinma Bank expand globally by complying principles of Shariah rules and regulations? What is the best country for expansion?
4. What capabilities does Alinma Bank need to develop in order to maximize its chance of success in even non-Muslim majority countries?
5. Briefly discuss the role of the Shariah Board in the Alinma Bank?
6. How far does the Alinma Bank cope with the digital transformation in providing its services? Give examples.

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