

# The Role of Islamic Banks in the Development of the Jordanian Economy

## "Exploratory Study on Arab Islamic Bank"

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Received: May 25, 2016

Accepted: Sep 23, 2016

Published: October 1, 2016

doi:10.5296/jmr.v8i4.9513

URL: <http://dx.doi.org/10.5296/jmr.v8i4.9513>

### **Abstract**

This study aimed to identify the role of Islamic banks in the development of the Jordanian economy. The study population consisted of public administration and branches of the Arab Islamic Bank. The study sample consisted of (85) customer relationship officers and (30) corporate service officers with a total (115) questionnaires distributed on all respondents. Descriptive approach of means and standard deviation was used; also Simple Regression was used to measure the impact of the role of Islamic banks in the development of the Jordanian economy.

Among the most important findings of the study that Islamic banks have a medium level role in the development of the Jordanian economy and the development of the industrial sector, and it was clear that at Islamic banks have low level role with negative impact on the development of agricultural sector. The findings have also revealed that Islamic banks develop the construction sector at a high level.

The study recommended the need to overcome the problems faced by agricultural and industrial entrepreneurs by Islamic banks in order to get farmers and manufacturers to get the funds necessary for them as this raises the level of development of the Jordanian economy.

**Keywords:** Economic development, Islamic banks.

## 1. Introduction

The current era is witnessing many developments in various economic fields; this development has led to the expansion of the activities, orders and growth and development of facilities, whether this development is internal or external as well as the increasing demand for funds, which led to the growing importance of Islamic banks.

Considering that Islamic banks play a key role in supporting and developing the economy, which are also a safe place for investors in terms of deposit funds and reinvest them, the Islamic banks evaluate the performance by financial indicators to demonstrate their financial position it, and to demonstrate their ability to settle their obligations and to determine their profitability and liquidity (Zayoud & Al-Ameen & Al-Mohandis, 2005).

Finance and investments processes practiced by Islamic banks are considered the real employments of funds which then add actual productivity energy, which gives them an important and positive role in the development of economic activity in the community (Hindi, 2000).

Therefore, this study will shed light on the role of Islamic banks in the development of the Jordanian economy through the decision-makers in the Arab Islamic Bank, as well as to identify the most important indicators for the Jordanian Islamic banks.

## 2. Theoretical Framework

### 2.1 Defining Islamic Bank

Financial institution aimed at pooling funds and savings from all those who do not want to deal with Reba (interest) and then work to employ them in different fields of economic activity, as well as providing various banking services for customers in accordance with Islamic Sharia and support the objectives of achieving economic and social development in the community (Mubarak & Younis, 1996).

### 2.2 Defining Economic Development

It is the process used by the state of incomplete growth in real economic exploitation of their resources in order to increase the real national income and thus increase the per capita average (Erekat, 1992).

Islam is deeply interested in the problem of economic development, but Islam deals with it as a part of the problem of humanitarian development, and therefore the focus in the economic sector was on human development, so that economic development remains as an integral component (Yousri, 2010).

2.3 Jordanian Economy: Is the knowledge economy which follows the path of the development of education, privatization, continuous economic liberalization, with the economic restructuring to gain access to a knowledge-based economy (Piro, 1998).

#### *2.4 The participation of Islamic banks in economic development*

Any Islamic bank is inherently a development institution that mobilize savings and fight against compactness and channeling savings into investment to serve the community in a manner consistent with Islamic law; it is an economic, social, financial and banking organization that seek to put money in its main function in society, and Islamic banks seek to create Islamic alternatives for all banking transactions that meet the needs of individual investors, companies and institutions, and thus encouraging investment in the commercial, industrial, agricultural and construction sectors, and then push the economic and social development(Ali,1995)

### **3. Previous studies**

**Huneiti**, This study aimed to identify the role of Islamic Sukuk in achieving the economic development. The study depends on financial reports that published on the official site of Dubai Islamic Bank. The study reveals that: the mobilization of resources through these Sukuk is weak and limited compared with what it was expected from the point-view of Dubai Islamic Bank. In addition, the results show that there is a decline in the ratio of financing through Sukuk/ GDP. Moreover (Huneiti,2015).

**Al-Oqool & Okab & Bashayreh**, In this paper, an attempt has been conducted to explore the relation between financial Islamic banking development (FIBD) and economic growth (EG) of Jordan. FINC and DEPT are used as a measure of FIBD, while RGDP used as an indicator of EG. The results show that there is bi-directional long-run Granger causality between RGDP and FINC reflecting a positive contribution of Jordanian Islamic banks in financing the process of Jordanian social and economic development. With regarding to short-run causality there isn't any significant relations between FIBD and EG. Taken together, these empirical findings involve valuable information for Jordanian policy makers (Al-Oqool & Okab & Bashayreh, 2014).

**AL-Tamimi**, The study aims to identify the role of Islamic banks in Jordan in economic development. the results indicate that The statistical analysis shows that there is a statistically significant relationship, despite the achievement of Islamic banks operating in Jordan high rates of growth in the size of their assets and deposits by employing them, but their contribution in economic development in Jordan is still marginal compared with the contribution of the Jordanian banking system. (AL-Tamimi, 2013).

**Abu Shihab & Soufan & Abdul-Khaliq**, This paper aims to point out if Islamic banks in Jordan depend on Islamic Investment "Istisna" in supporting industries? At the beginning there are some definitions of the Islamic investment that the Islamic banks should offer to support industries, "Istisna", the research discussed if Islamic banks in Jordan apply this investment tool, at last the results will show that on average, the Islamic Banks in Jordan do not offer "Istisna". So they do not have any effective role in supporting industries in Jordan (Abu Shihab & Soufan & Abdul-Khaliq,2013).

**Mkdad & Halas**, This study is discussing the role of Islamic Banks in financing economic development in Palestine. The researchers depend on the published as well as the primary

data, collected from Islamic Banks and its branches that work in Gaza Strip, through a self-designed questionnaire prepared for this reason. But results show that they failed support direct or indirect investment and facilitate loans especially in Palestine, and this will reduce the role of Islamic Banks in compliance the economic development in Palestine (Mkdad & Halas,2005).

#### **4. Methodology**

The decisions to grant funds to all sectors are subject to the rules adopted in Islamic banks including ensuring the debtor's ability to settle the debt at maturity, and to minimize the risk of funding decisions through studying the credit track for the client , his reputation and the feasibility study for the project, which guarantees the right of the Islamic bank in refunding its funds and therefore the aim of this study is to answer the following question: what is the role of the Jordanian Islamic banks in the development of Jordanian economy?. From this main question the following sub-questions arise:

- 1- What is the role of the Jordanian Islamic banks in the development of Commercial sector?
- 2- What is the role of the Jordanian Islamic banks in the development of Industrial sector?
- 3- What is the role of the Jordanian Islamic banks in the development of agricultural sector?
- 4- What is the role of the Jordanian Islamic banks in the development of Construction sector?

Based on this context, the following hypotheses are proposed:

$H_{0.1}$ : There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the development of the Jordanian economy.

Base on this hypothesis, the following sub-hypotheses emerge :

1.  $H_{0.1-1}$ : There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian sector commercial development.
2.  $H_{0.1-2}$ : There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian industrial sector development.
3.  $H_{0.1-3}$ : There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian agricultural sector development.
4.  $H_{0.1-3}$ : There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian construction sector development.

##### *4.1 Scope of the study*

The study focused on customer relationship officers (cro) and corporate service officers (coso) in public administration and branches of the Arab Islamic Bank (finance officials) using purposive stratified sampling to study the role of Islamic banks in the development of the economy where 100 questionnaires were distributed on customer relationship officers and (40)

questionnaires were distributed on corporate service officers. After retrieving questionnaires the final sample was (115) questionnaires for all the study sample which represents (82%) of the main sample, and data were collected during the months March, April 2016..

#### 4.2 Multivariate analysis – probit model

Simple regression of five variables model, of which a variable independent consists of the role of Islamic banks. The dependent variables are four variables which are sector commercial development, the industrial sector development, the development of the agricultural sector, and construction sector development.

### 5. Analysis

Descriptive statistics were used to answer study questions by calculating frequencies and percentages to describe the study sample, the use of Cronbach's alpha test to verify the reliability of the study tool, means and standard deviations were calculated. Simple regression test was used to identify the impact of the role of the Jordanian Islamic banks in the development of the Jordanian economy.

#### 5.1 Demographic distribution of study sample

Table 1. Sample's Distribution According to Demographic Information

Category	Frequency	Percentage%
Gender		
Male	82	71.3
Female	33	28.7
Total	115	100.0
Job title		
Customer Relationship Officer	85	73.9
Corporate service officer	30	26.1
Total	115	100.0
Experience		
Less than 10 years	18	15.7
10-20 years	64	55.7
More than 20 years	33	28.7
Total	115	100.0

Source: Author

#### 5.2 Study tool

The tool for the measurement of the role of Islamic banks in the development of the Jordanian economy was developed through referring to theoretical literature and previous studies such as (Al-Oqool & Okab & Bashayreh (2014)) and (AL-Tamimi (2013)). The study tool consisted of two parts:

Part (I): It includes demographic information, consisting of: sex, occupation and experience.

Part (II): It includes study questions consisting of (30) items, all of which relate to the role of the Jordanian Islamic banks in the development of the Jordanian economy, and the study tool has been designed like Likert five point scale where the role of Islamic banks were addressed in the following dimensions:

Dimension (1): relates to the development of Jordanian economy, which includes (6) items.

Dimension (2): relates to the development of Commercial sector, which includes (6) items.

Dimension (3): relates to the development of Industrial sector, which includes (6) items.

Dimension (4): relates to the development of agricultural sector, which includes (6) items.

Dimension (5): relates to the development of Construction sector, which includes (6) items.

### 5.3 Cronbach's alpha test

To identify the consistency of each item of the scale with the dimension it belongs to, the study has used the correlation coefficients between each item account to measure the reliability of study tool by using (Cronbach's alpha) coefficient , and Table (2) shows test results.

Table 2. Stability of the tool study using Cronbach's alpha testing coefficient

Variable	Consistency using Cronbach's alpha coefficient
The role of Islamic banks	0.87
The development of commercial sector	0.87
The development of industrial sector	0.88
The development of agricultural sector	0.88
The development of construction sector	0.82
The tool as a whole	0.93

Source: Author

Table (2) shows that Cronbach's alpha coefficient values for sub-dimensions of the scale ranged between (0.82- 0.88) and also the value of consistency coefficient using Cronbach's alpha for the total score of the scale was (0.93).

Likert scale used in the study was graded according to the rules and characteristics of the scales as follows:

The level of the role				
Strongly Agree	agree	neutral	Disagree	Strongly Disagree
5	4	3	2	1

Source: Author

Based on the above, the values of the means of the study were dealt as follows:

Higher value - the minimum value of alternatives of the answers divided by the number of levels: 1.33 and this value is the category length

Low level is  $\leq 2.333$

Medium level equals: (2.34 - 3.666)

High level equals: (3.67 – 5.00).

### 5.3 Means and standard deviations

Means and standard deviations were calculated to identify the responses of the study sample about:

1- The role of Islamic banks in the development of the Jordanian economy from the point of view of customer relationship officers and corporate service officers in Arab Islamic Bank. (See table 3).

Table 3. Means and standard Deviations of for sample's responses toward the role of Islamic banks in the development of the Jordanian economy, "in descending order"

No	Transaction	Mean	S.Deviation	order	Level
4	Islamic banks seek to apply the development plan by employing the resources of Islamic banks	4.09	1.00	1	High
2	Islamic banks provide concrete facilities to assess vital development projects	3.70	1.13	2	High
6	Islamic banks handle the coordination and integration of work between banks to serve the financing of economic development	3.51	1.19	3	medium
5	Islamic banks offer private banking legislations regulating Islamic banking business what help them to finance economic development.	3.45	1.24	4	medium
3	Islamic banks are required to finance major economic sectors	3.30	1.10	5	medium
1	Islamic banks provide a plan for financing economic sectors	3.15	1.44	6	medium
	Grand mean	3.53	0.79		medium

Source: Author

Table 3 shows that means of (The role of Islamic banks in the development of the Jordanian economy) ranged between (3.15 – 4.09) where the role had a mean of (3.53) which is a medium level. Item (4) had scored the highest mean (4.09) and a standard deviation of (1.00) which is high level where the item states (Islamic banks seek to apply the development plan by employing the resources of Islamic banks).

Item (1) ranked last with a mean of (3.15) and a standard deviation of (1.44) which is a medium level , where the item stated ( Islamic banks provide a plan for financing economic sectors).

This explains that Islamic banks have a medium level role in the development of the Jordanian economy from the standpoint of the study sample.

1- The role of Islamic banks in the development of commercial sector from the point of view of customer relationship officers and corporate service officers in Arab Islamic Bank. (See table 4).

Table 4. Means and standard Deviations of for sample's responses toward the role of Islamic banks in the Jordanian sector commercial development members, "in descending order".

No	Transactions	Mean	S.Deviation	order	Level
2	Islamic banks reduce commission and profit ratios for importers.	3.93	0.98	1	High
6	Islamic banks offer checkbook quickly to allow traders to operate within batches.	3.86	0.95	2	High
5	Islamic banks provide commercial financing for long periods of time	3.70	0.93	3	High
1	Islamic banks offer special services to capital owners working in the trade.	3.56	1.04	4	medium
4	Islamic banks reduce commission and profit ratios for exporters	3.53	1.02	5	medium
3	Islamic banks grant funds extensively for traders	3.49	1.07	6	medium
	Grand mean	3.68	0.76		High

Source: Author

Table 4 shows that means of (The role of Islamic banks in the development of commercial sector) ranged between (3.49 – 3.93) where the role had a mean of (3.68) which is high level. Item (2) had scored the highest mean (3.93) and a standard deviation of (0.98) which is high level where the item states (Islamic banks reduce commission and profit ratios for importers).

Item (3) ranked last with a mean of (3.49) and a standard deviation of (1.07) which is a medium level, where the item stated (Islamic banks grant funds extensively for traders).

This explains that Islamic banks have a medium level role in the development of commercial sector from the standpoint of the study sample.

3- The role of Islamic banks in the development of industrial sector from the point of view of customer relationship officers and corporate service officers in Arab Islamic Bank. (See table 5).



Table 5. Means and standard Deviations of for sample's responses toward the role of Islamic banks in the in the Jordanian industrial sector development of individuals, "in descending order"

No	Transaction	Mean	S.Deviation	order	Level
1	Islamic banks encourage industrial sector through the provision of special services to them	3.96	0.79	1	High
5	Islamic banks provide funds for long periods of time for manufacturers	3.86	0.84	2	High
2	Islamic banks reduce commission and profit ratios to the owners of light and heavy industries	3.58	0.92	3	medium
4	Islamic banks extensively grant funds to the owners of industrial companies	3.55	0.99	4	medium
6	Islamic banks offer checkbook quickly to allow owners of plants to operate within batches	3.41	0.98	5	medium
3	Islamic banks reduce commission and profit ratios to manufacturers	3.39	0.93	6	medium
	Grand mean	3.62	0.64		medium

Source: Author

Table 5 shows that means of (The role of Islamic banks in the development of industrial sector) ranged between (3.39 – 3.96) where the role had a mean of (3.62) which is medium level. Item (1) had scored the highest mean (3.96) and a standard deviation of (0.79) which is high level where the item states (Islamic banks encourage industrial sector through the provision of special services to them).

Item (3) ranked last with a mean of (3.39) and a standard deviation of (0.93) which is a medium level , where the item stated(Islamic banks reduce commission and profit ratios to manufacturers).

This explains that Islamic banks have a medium level role in the development of industrial sector from the standpoint of the study sample.

4-The role of Islamic banks in the development of agricultural sector from the point of view of customer relationship officers and corporate service officers in Arab Islamic Bank (see table 6).

Table 6. Means and standard Deviations of for sample's responses toward the role of Islamic banks in the in Jordan's agricultural sector development, "in descending order".

No	Transactions	Mean	S.Deviation	order	Level
4	Islamic banks extensively grant funds to the owners farms and owners of the vast territory	2.41	1.05	1	medium
5	Islamic banks provide funds for long periods of time for farmers	2.36	0.94	2	medium
6	Islamic banks offer checkbook quickly to allow farms owners to operate within batches	2.35	1.00	3	medium
3	Islamic banks reduce commission and profit ratios for exporter farmers	2.11	0.81	4	Low
2	Islamic banks reduce commission and profit ratios to the farmers	2.08	0.93	5	Low
1	Islamic banks encourage agricultural sector through the provision of special services to them	1.90	0.68	6	Low
	Grand mean	2.20	0.65		Low

Source: Author

Table 6 shows that means of (The role of Islamic banks in the development of agricultural sector) ranged between (1.90 – 2.41) where the role had a mean of (2.20) which is low level. Item (4) had scored the highest mean (2.41) and a standard deviation of (1.05) which is medium level where the item states (Islamic banks extensively grant funds to the owners farms and owners of the vast territory).

Item (1) ranked last with a mean of (1.90) and a standard deviation of (0.68) which is a low level , where the item stated(Islamic banks encourage agricultural sector through the provision of special services to them).

This explains that Islamic banks have a low level role in the development of agricultural sector from the standpoint of the study sample.

1- The role of Islamic banks in the development of construction sector from the point of view of customer relationship officers and corporate service officers in Arab Islamic Bank. (See table 7).

Table 7. Means and standard Deviations of for sample's responses toward the role of Islamic banks in Jordan's construction sector development, "in descending order".

No	Transactions	Mean	S.Deviation	order	Level
2	Islamic banks reduce commission and profit ratios for construction sector.	3.98	1.11	1	High
6	Islamic banks offer checkbook quickly to allow construction sector and companies to operate within batches	3.80	0.97	2	High
3	Islamic banks work on granting of funds to the owners of construction companies to build and sell through such banks with low commissions and long-term repayment periods.	3.77	1.06	3	High
5	Islamic banks provide funds for long periods of time for construction sector	3.76	1.08	4	High
4	Islamic banks extensively grant funds to the owners of construction companies	3.70	1.09	5	High
1	Islamic banks encourage construction sector through the provision of special services to them	3.68	1.08	6	High
	Grand mean	3.78	0.89		High

Source: Author

Table 7 shows that means of (The role of Islamic banks in the development of construction sector) ranged between (3.68 – 3.98) where the role had a mean of (3.78) which is high level. Item (2) had scored the highest mean (3.98) and a standard deviation of (1.11) which is medium level where the item states (Islamic banks reduce commission and profit ratios for construction sector).

Item (1) ranked last with a mean of (3.68) and a standard deviation of (1.08) which is a high level , where the item stated (Islamic banks encourage construction sector through the provision of special services to them).

This explains that Islamic banks have a low level role in the development of construction sector from the standpoint of the study sample.

#### 5.4 Testing Study's hypotheses

Hypotheses of the study were tested by multiple linear regression analysis, and the results were as follows:

(H<sub>0.1</sub>): There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the development of the Jordanian economy.

Base on this hypothesis, the following sub-hypotheses emerge :

(H<sub>0.1-1</sub>): There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian sector commercial development.

(H<sub>0.1-2</sub>): There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the

role of Islamic banks on the Jordanian industrial sector development.

(H<sub>0.1-3</sub>): There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian agricultural sector development.

(H<sub>0.1-4</sub>): There is no statistically significant impact at the level of significance ( $\alpha \leq 0.05$ ) for the role of Islamic banks on the Jordanian construction sector development.

In order to examine the first main hypothesis, multiple regression analysis was used, and the results were as follows:

Table 8. The results of examining the effect for the role of Islamic banks on the development of the Jordanian economy as measured by sector commercial development, industrial sector development, agricultural sector development ,and construction sector development

<b>Indep Variable</b>	<b>Dep Variable</b>	<b><math>\beta</math></b>	<b>R correlation coefficient</b>	<b>R<sup>2</sup> coefficient of determination</b>	<b>calculated F</b>	<b>Sig F*</b>
Role of Islamic banks	Sector Commercial Development	0.677	0.707	0.499	112.680	0.000*
	Industrial Sector Development	0.434	0.532	0.283	44.683	0.000*
	Agricultural Sector Development	-0.491	0.619	0.383	70.009	0.000*
	Construction Sector Development	0.517	0.787	0.619	145.878	0.000*

(\*) The effect is statistically significant at ( $\alpha \leq 0.05$ )

Source: Author

The results from table (8) are that the effect is statistically significant, where calculated F value is (112.680), and the level of significance (Sig F = 0.000) which is less than 0.05, while the correlation coefficient (R = 0.707) refers to the relationship between the variables ,in addition to the value of the coefficient of determination was (R<sup>2</sup> = 0.499), pointing out that (49.9%) of the variation in the role of Islamic banks can be explained by the variation in sector commercial development.

The results from table (8) are that the effect is statistically significant, where calculated F value is (44.683), and the level of significance (Sig F = 0.000) which is less than 0.05, while the correlation coefficient (R = 0.532) refers to the relationship between the variables ,in addition to the value of the coefficient of determination was (R<sup>2</sup> = 0.283), pointing out that (49.9%) of the variation in the role of Islamic banks can be explained by the variation in industrial sector development.

The results from table (8) are that the effect is statistically significant, where calculated F value is (70.009), and the level of significance (Sig F = 0.000) which is less than 0.05, while the correlation coefficient (R = 0.619) refers to the relationship between the variables ,in addition

to the value of the coefficient of determination was ( $R^2 = 0.383$ ), pointing out that (49.9%) of the variation in the role of Islamic banks can be explained by the variation in agricultural sector development.

The results from table (8) are that the effect is statistically significant, where calculated F value is (145.878), and the level of significance (Sig F = 0.000) which is less than 0.05, while the correlation coefficient ( $R = 0.787$ ) refers to the relationship between the variables, in addition to the value of the coefficient of determination was ( $R^2 = 0.619$ ), pointing out that (49.9%) of the variation in the role of Islamic banks can be explained by the variation in construction sector development.

## **6. Conclusions and Recommendations**

### *6.1 Conclusions*

The current study found the following results:

- The results showed that the role of Islamic banks in the development of the Jordanian economy was of average level, and this result is attributed to the investment method in Islam which is based on sharing in profit and loss and restricted by controls and standards of investment in Islamic legislation.
- The results showed that Islamic banks have a high-level role in the commercial sector development and the construction sector. This is attributed to the decrease in the level of risk, and the high level of the guarantee of recovery of the bank's money, especially in the construction sector through the bank's right to seizure the property. This pushes the economic and social development.
- The results showed that the Islamic banks has an average and near to the high level role in the Jordanian industrial sector development, and this result is attributed to that Islamic banks in Jordan have a desire to expand in financing the industrial sector, but lack of the necessary guarantees by manufacturers reduces financing operations .
- The results showed that Islamic banks have a weak role of negative impact in the agricultural sector development. This result was attributed to the reluctance of banks for financing this sector due to high risk level due to weather factors and inability to predict the quantity of production and prices.

### *6.2 Recommendations*

- Businessmen and owners of industrial projects need to provide guarantees accepted by Islamic banks.
- Overcome the problems faced by industrial entrepreneurs by Islamic banks in order to get finance necessary for them, as this raises the level of the Jordanian economy.
- The state must encourage Islamic banks in financing the agricultural sector by guaranteeing debts to reduce financing risks of this sector.
- Islamic banks must support the construction sector because it attracts capitals to invest

due to lack of risk factor in this sector.

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