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**THE EXPERIENCE OF BANK ISLAM MALAYSIA BERHAD  
IN STIMULATING SAVINGS AND CHANNELLING  
THEM INTO EQUITY INVESTMENT**

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This is certify that Bro./Sis Siti Khaidah Ab. Mannan  
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under my supervision. The relevant comments made on the paper during its presentation have been incorporated in the present version of the paper to my full satisfaction.

I have pleasure in recommending that the graduate committee may approve the paper in partial fulfilment of the requirements for the degree of Master of Economics.

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## 1. INTRODUCTION.

The Bank Islam Malaysia Berhad, like most Islamic banks in the world, is operating in capitalistic economy where the use of interest predominates. Being in such an environment, in addition to the existence of already matured conventional financial system, it is argued as to whether the Islamic bank can be viable and competent.

In so far, viability and competency of any banking institution are measured by looking at its liquidity, profitability and solvency. While those criteria are not neglected, under certain circumstances, the coverage of its customers and the efficiency in the use of its funds should also be considered.

Experience has shown that, as the only bank which operates strictly on the basis of shariah principles, BIMB can co-exist with conventional banks. However, as far as its performance is concerned, the track record of BIMB's savings and investments isn't very impressive.

Hence, an attempt is made to review the experience of BIMB in stimulating savings. In addition, the study is intended to see how BIMB operates in mobilizing savings of the ummah for investment purpose. A special attention is given to the equity investment of the bank.

For the purpose of the study, information is obtained mainly from the Bank Islam Malaysia Berhad. Additional information is taken from several related articles, magazines as well as newspapers.

The paper is divided into five different sections. Section one is the introduction. Section two describe briefly the background of the bank and its performance. Section three discuss the role of the bank in stimulating saving and investment. The problems and challenges of the bank are discussed in section four. The recommendations and conclusion are drawn in section five.

## 2. BIMB : BACKGROUND AND PERFORMANCE.

The establishment of the Pilgrim Management Fund Board (PMFB) in August 1969 marked the beginning of an interest-free financial institution in the country. The successful implementation of of PMFB then prompted a pressure on the government to establish full-fledged Islamic bank. Resulting from the continuous pressure from the Muslim, the Islamic bank namely BIMB, was finally established.

The BIMB was incorporated on 1st March 1983 under the Company Act 1965. The operation of its banking business then commenced on the first of July 1983. The bank formulated its corporate objective as follows:(1)

The corporate objective of the bank is to provide banking facilities and services in accordance with Shariah principles, rules and practices to all Muslims and the population of this country. The bank's effort to provide these banking facilities and services is to be undertaken within the framework of its viability and capacity to continuously grow and expand.

At the time of establishment, the paid-up capital of the bank, subscribed by the shareholders, was RM80 million with the Federal Government, through a company called Minister of Finance Incorporation, owned RM30 million. The

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1 See Dr. Abdul Halim Ismail, "Bank Islam Malaysia: Structure and Functions", Paper presented at the Seminar on Current Trends and Development of the Banking Industry in Malaysia 6-7 June, 1983.

Pilgrim Management Fund Board (PMFB) held RM10 million and Muslim Welfare Organisation of Malaysia held RM5 Million. The State Religious Council and States Religious Agencies owned RM20 million and RM3 million respectively and a final RM 12 million was held by Federal Agencies.

The implementation of Employees' Share Option Scheme on April 6, 1990 raised the share capital of the bank. As at November 1991, together with the issuance of "special share" (2), the capital of the bank amounted to RM83.55 million. Through the acquisition of an additional 36.15 percent equity interest in Syarikat Takaful Malaysia Sdn. Bhd. (STMSB), an equivalent of RM3.62 million shares. The bank's total issued and paid-up capital was RM87.169 million. With the right issue of RM27.89million new ordinary shares and a public issue of RM18.23 million new shares, the BIMB's capital base was expanded to RM133.41 million shares.

During the first financial year, the bank had four branches. Through heavy emphasis on staff recruitment and training, the bank has been able to expand its branch network. At present, the bank has a total of 30 branches covered all the states throughout Malaysia. Over the next 10 years, the bank expect to increase its branch network to 60 branches.

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2 "Special Share" is One Special Right Redeemable Preference Share with a RM1 per value.



The bank has established three subsidiary companies with the purpose of streamlining its operations and expanding the coverage of its facilities and services. Two wholly-owned subsidiaries are Al-Wakalah Nominees Sdn. Bhd. which specialises in investment activities, and Syarikat Al-Ijarah Sdn. Bhd., a leasing company which acquire assets for lease to BIMB. The Syarikat Takaful Malaysia Sdn. Bhd., a star performer of the Group which operates an Islamic insurance business, formerly had 51 percent of its equity held by the bank. After the acquisition of another 36.15 percent equity, the bank now held 87.15 percent of its equity. The rest was held by various state religious council and agencies.

Since its establishment some nine years ago, the bank has managed to show its viability and remain competitive against the numerous other financial institutions in the country. Its assets had increased more than triple, rising from RM325.5 million in 1984 to RM1357.2 million in 1991 (Refer Table 1).

The customers' deposits increased quite tremendously especially during the first few years of its operation. From the amount of RM241.4 million in 1984, the bank was able to collect RM1.175 billion by the end of June 1991. The rise in the overall deposits stems mainly from the growth in incomes as well as the expansion of branch networks.

Table 1.

BIMB: PERFORMANCE SINCE 1984-1991. (RM Million)						
Year	Share Capital	Total Assets	Total Deposits	Profits before Zakat & Tax	Branches	
1984	79.9	325.5	241.4	-1.3	4	
1985	79.9	514.2	410.2	4.4	8	
1986	79.9	677.5	566.9	2.36	14	
1987	79.9	923.9	809.1	3.98	18	
1988	79.9	1149.6	1022	6.5	21	
1989	79.9	1388.7	1229	9.9	24	
1990	80.1	1396.3	1220	13.4	27	
1991	82.3	1357.2	1175	14.9	29	

Sources: BIMB Annual Reports.

As at Nov. 1991, after the acquisition of equity from STMSB and the issuance of shares, the share capital of BIMB amounted to RM133.4 million.

# At present, BIMB branches is 30.

The latest figure however, seems quite disappointing as the bank's customers' deposits remain stagnant for the past two years. This trend is particularly due to less attractiveness of the bank's rate of profit on its investment account vis-a-vis the conventional banks' rate of interest on their fixed deposits (3). This is so because the restrictive monetary policy had resulted in the relative scarcity of liquidity, thus exerting pressure on the bank's cost of fund. In ten years time, the bank expects to increase its current level of deposits to about RM3 billion, "providing the economy does grow" (4).

3 BIMB Annual Report, 1991.

4 See Malaysian Business, June 1-15, 1991.

Due to the stagnancy of the bank's deposits, its financing in 1991 was marginally lower than the previous year. From the total amount of RM807.8 million in 1990, the bank's financing extended to its customers in 1991 was only at RM789.3 million.

In order to boost its profit return, the bank has introduced several new facilities. Among them are trade financing under the concept of Bai ad-Dayn (debt-trading) and share financing facilities under the principle of Bai bi-thaman Ajil.

The financing facilities offered by the BIMB are well received by the business community. It is proved as the bank has created several landmarks involving big companies : (5)

1. In 1990, SHELL MDS had sought RM125 million financing syndication through corporate bonds, raised by the bank.

2. The bank also had a RM560 million joint participating financing with SHELL.

Al-Musharakah participating bearer certificates were issued, entitling the holders to a distribution of annual returns.

3. Al-Ijarah financing was given to an oil refining company to finance the installation of a catalytic reformer unit in Terengganu.

Though the overall performance of the bank seems respectable, the recent performance of its saving and investment is quite disheartening. The next section will analyse the detail of the bank's saving and equity investment. The role of the bank in stimulating saving and equity investment shall also be discussed.

### 3. AN EVALUATION OF BIMB'S ROLE IN STIMULATING SAVINGS AND CHANELLING THEM INTO EQUITY INVESTMENT.

The BIMB is an Islamic commercial bank which operates on the basis of shariah principles. Like other commercial banks, it acted as a financial intermediary in managing two different entities, the provider and the user of funds. In view of these, this section will discuss the experience of BIMB in stimulating savings and how it channel them to equity investment.

#### 3.1. The Sources of Funds.

The bank receive funds from its customers through three different types of accounts namely current account, saving account and investment account. For the purpose of the study, we shall have to take a closer look at its saving and investment account.

##### 3.1.1. Current Account.

The current account of BIMB is accepted under the principle of al-Wadiah (safe keeping). Under this principle, the bank request permission from customers to use the funds for generating profits. In return, the bank provides the customers with cheque books and other usual curent account services.

The deposits of the bank's current account are growing though not regularly. (Refer Table 2 and Figure 1).

Table 2.

BIMB: SCHEDULE OF CUSTOMERS' DEPOSITS. (RM Million)				
Year	Current	Savings	Gen Inv.	Specific Inv.
1984	39.98	26.104	101.223	71.000
1985	43.17	46.482	276.183	49.397
1986	56.6	78.205	404.232	36.750
1987	122.98	113.766	572.105	16.809
1988	142.25	152.797	724.584	23.347
1989	140.62	181.511	943.935	5.452
1990	197.4	212.671	725.072	123.500
1991	225.21	249.523	647.900	95.573

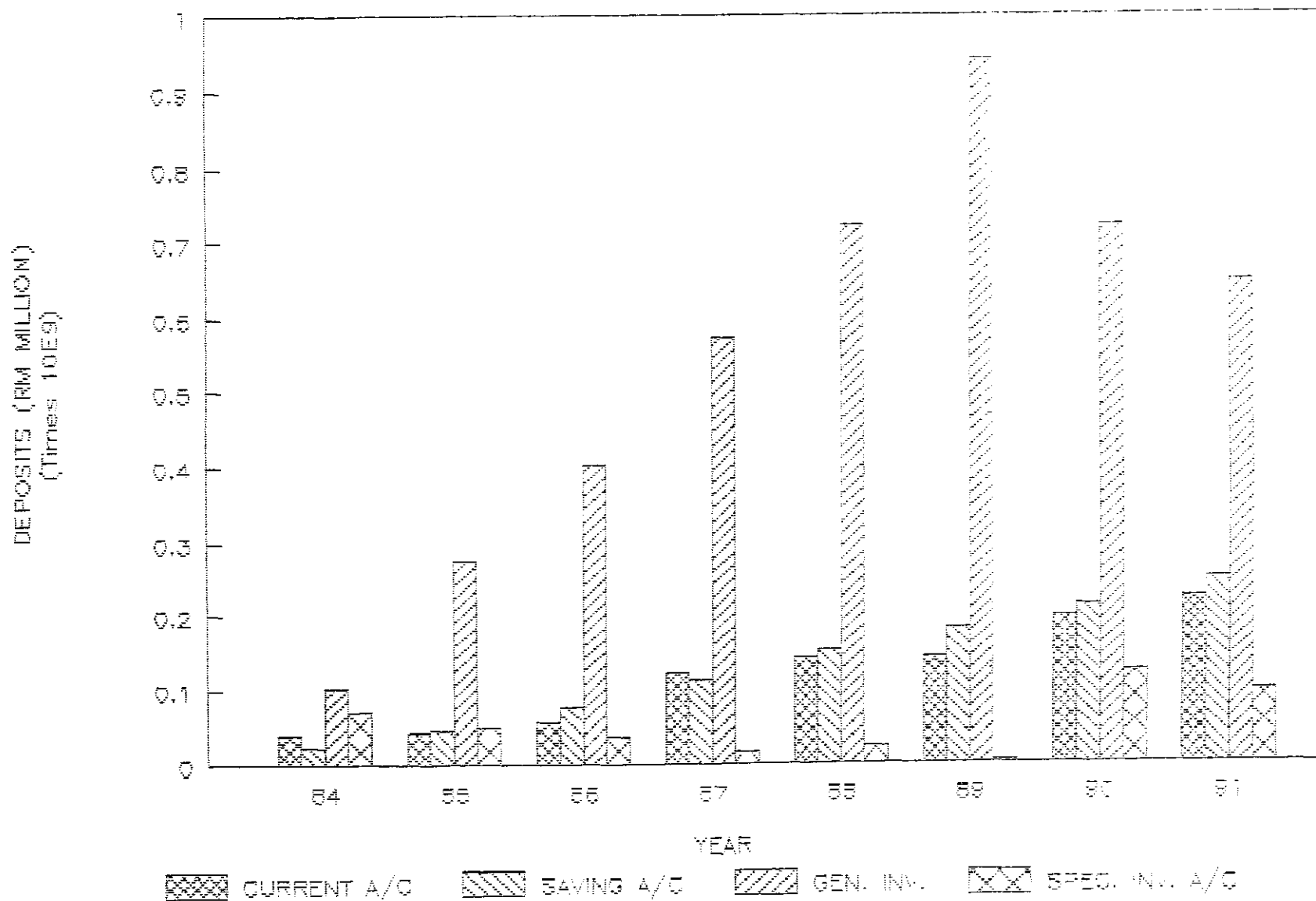
Source: Bank Islam Malaysia Berhad.

Table 3.

BIMB: ANNUAL GROWTH RATE OF DEPOSITS. ( % )				
Year	Current	Savings	Gen. Inv.	Specific Inv.
1985	7.98	78.1	172.8	-30.4
1986	29.1	68.2	46.4	-25.6
1987	117.3	45.5	41.5	-54.3
1988	15.7	34.3	26.7	38.9
1989	-1.14	18.8	30.3	-76.6
1990	40.4	17.2	-23.2	2165.2
1991	14.1	17.3	-10.6	-22.6

Source: Bank Islam Malaysia Berhad.

FIG.1a BIMB:DEPOSIT POSITION 1984-1991



### 3.1.2. Saving Account.

The saving account is accepted from its customers looking for custody of their funds and convenience in their use on the principle of al-Wadiah (safe keeping under trusteeship). The customers may withdraw part or whole of their balance on demand. For the purpose of generating profit, the bank request permission to use these funds.

Although saving account holders are not entitled to a share of the bank's profit but the bank may, at its absolute discretion, reward the customers part of the generated profits as an appreciation for the deposit of money with the bank. The return to the saving account deposits is generally lower than the return to investment account deposits. The reason being that the deposits at saving account are repayable on demand.

In order to attract more savers, the bank has introduced several schemes. They are Children Saving Schemes, Coin Box, and Khairat Kematian. While the first two are specially meant for young depositors, the Khairat Kematian is a form of added advantage for Saving account holders. Under this scheme, some portion of the individual saving deposits is transferred to Takaful as an insurance redeemable by the heritance in time of death of the depositors.

The annual growth rate of the bank's saving deposits in so far, took a continued downward trend although the total



amount of saving deposits increased steadily up (Refer Table 2 and 3). During the first few years of its operation, the growth of the bank's saving deposits was respectable. From the amount of RM26.1 million in 1984, the deposits grew to RM46.5 million in 1985, an increase of about 78.1 percent. This tremendous growth of deposits might be partly due to the zealotness of the Muslim to deposits in the newly emerged Islamic bank. The commitment of the Muslim who have been long waiting for the emergence of Islamic bank contributes to the steady growth of the bank's saving deposits. This category constitutes about one third of the total Muslim depositors in the country (6).

Another factor which is no less important is the fact that during the first few years of its operation, there was a shake-out in the banking sector following the 1985-86 recession. The failure of some banks led the customers to have less confidence in the other banking institutions thereby boosted the image of BIMB as an alternative bank.

The annual growth rates of saving deposits however, seemed gradually declining with the latest growth rate at only 17.3 percent. The intense competition lately in terms of services, facilities and special attractive schemes offered by the conventional banks might be the reason for the decline.

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6 Based on unstructured interview with En. Mustafa Hamat, Account manager of BIMB.

While the over all performance of the bank's saving deposits seemed increasing, judging from its absolute term, the relative performance of each branch didn't show much progress. With 29 branches in 1991, the average collection of each branch is about RM7 million compared to RM6 million per branch in 1984. This indicates that the over all increase in saving deposits stems mainly from the expansion of branch network.

### 3.1.3. Investment Accounts.

The investment account, encompassing both general and specific account, are accepted on the basis of Mudharabah principle. This principle allows the bank to use the deposits with the profits being shared with depositors. The bank paid this obligatory profits to these depositors according to the maturity of their deposits and the prevalent rate of return.

The bank's depositors consisted of individuals, government departments and statutory bodies and various entities from the corporate sectors. The special investment account is normally meant for deposits from government and corporate sectors. The bank accepts deposits for general investment account on a specified maturity period, ranging from one month to a maximum of five years. This deposits are invested in any projects deemed fit by the bank. Unlike the general account, the customers in specific investment account

specify the manner in which the funds are to be invested. Generally, the funds are invested in Bai ad-Dayn, security papers, shares and stocks and special projects /financing.

Generally, the annual growth of both general and specific investment deposits is rather unfavourable (Refer Table 3). For the general investment deposits, the annual growth rate increased steadily up to 1989, but then decreasing drastically to negative 23.2 in 1990 and negative 10.6 in 1991. While the special investment account, its annual growth rate seems fluctuating with the highest rate being at 2146 percent in 1990, a tremendous jump from the previous negative rate. The growth rate then fall substantially to negative 22.6 percent in 1991.

The positive growth rates for the investment deposits during the first few years of its operation were basically due to the competitiveness of the bank's rate of return vis-a-vis the conventional interest rates. Hence, the investors, who are mainly concern with the return on their investment, seemed indifference in their choice between BIMB and other banks.

However, the Central Bank's announcement to free the Base Lending Rate (BLR), effective on Feb. 1, 1990, had caused a switch in BIMB's investment deposits. With this deregulation which allow tha banks to fix their own BLR,

competition becoming more intense and the deposit rate of the banks becoming more and more attractive when compared to the return on BIMB's investment account. The difference between BIMB's rate of return and conventional banks' rate of interest is shown in Table 4 and 5.

Table 4.

BIMB: RATES OF PROFITS TO DEPOSITORS AS AT JUNE.								
( % )								
	1984	1985	1986	1987	1988	1989	1990	1991
Savings	4.96	5.46	4.71	4.20	3.25	3.31	3.37	3.35
Inv. A/c								
1 month		6.11	5.28	4.70	3.64	3.71	3.78	4.29
3 months		6.49	5.61	4.99	3.87	3.94	4.01	4.55
6 "	6.25	6.88	5.94	5.29	4.09	4.17	4.25	4.82
12 "	6.95	7.64	6.60	5.88	4.54	4.64	4.72	5.36
15 "		8.02	6.92	6.17	4.77	4.87	4.96	5.36
18 "		8.40	7.25	6.46	5.00	5.10	5.19	5.89
24 "		8.79	7.58	6.76	5.23	5.34	5.43	6.16
36 "		9.17	7.91	7.05	5.45	5.57	5.67	6.43
48 "		9.55	8.24	7.34	5.68	5.80	5.90	6.70
60 & above		9.93	8.57	7.64	5.91	6.03	6.14	6.97

Source: Bank Islam Malaysia Berhad.

Table 5.

COMMERCIAL BANKS: RATES OF INTEREST* AS AT JUNE.								
( % )								
	1984	1985	1986	1987	1988	1989	1990	1991
Savings	6.5	6.5	6.0	4.0	3.5	3.5	3.5	3.5
Fixed Deposits								
1 month	9.0	8.0	7.25	2.5	3.0	4.0	5.25	6.5
3 months	9.25	8.5	7.25	2.75	3.50	4.5	6.0	7.0
6 "	9.25	9.0	7.25	3.75	3.75	5.0	6.0	7.1
12 "	9.5	9.0	7.5	4.50	4.25	5.5	6.5	7.0

Source: Bank Negara Malaysia, Quarterly Bulletin 1984-1991.

Note: Interest rates for fixed deposits with maturities exceeding 12 months are negotiable.

\* Only the modes are taken.

### 3.2. Application of Funds.

All the funds received by the bank are collected in pool of depositors funds. These deposits are then mobilised into statutory reserve, liquid assets, trade financing, financing the acquisition of assets, project financing, investment (equity participation) and others. We shall limit our discussion to only project financing and investment (equity participation) of the bank.

#### 3.2.1. Project Financing.

The bank's financing for its customers' projects are governed by the principles of Mudharabah and Musharakah. Under the principle of Mudharabah, the bank (provider of capitals) will provide 100 percent financing for the relevant projects while the customer (entrepreneur) will manage the projects. The bank cannot interfere in the management of the projects but has the right to undertake the follow-up and supervision tasks. Any generated profit is distributed to both parties upon agreement. In the event of loss however, the bank has to bear all losses.

For project financing under the principle of Musharakah (joint-venture project financing), the bank, together with its customer (entrepreneur) will provide the financing in an agreed proportion. The bank, unlike under Mudharabah, has

the right to participate in the management of the projects. The distribution of profits generated from the projects is agreed through negotiation. While in the event of of loss, both parties bear the loss in proportion to their shares of financing.

Prior to the approval of the projects, there are certain factors which determine the eligibility of the projects.

They are :(8)

- i) The projects must not transgress any shariah prescriptions.
- ii) Viability of the projects.
- iii) The availability of the bank's funds.
- iv) The bank's financing and investment policy.

In order to ensure a good profit return from the project financing, the bank has laid down several other conditional factors :(9)

- i) Capacity of borrowing.

Before making any approval, the bank has to look at the organizational aspects of the firm. For example, if the company is a limited company, then the Memorandum and Articles of Association will determine whether or not the company can get the financing.

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8 See Ahmad Tajuddin A. Rahman, "Peranan Bank Islam Terhadap Usahawan Muslimin", Paper presented at Seminar Usahawan Muslimin, ITM, 1987.

9 Ibid.

ii) Credibility and Integrity.

This refer to the commitment and performance of the customers in their previous projects' record.

iii) Purpose of borrowing; must be in line with the bank's financing policy.

iv) Ability to repay.

The ability of a certain project to repay the borrowing is evaluated from such aspects as its management, marketing, technicality, liquidity and profitability.

In giving its financing, the bank, like many of its counterparts, do require collateral as a security for the financing. However, it is not the main criteria of its financing decision. What is more important is the viability and profitability of the projects.

There has been quite a number of criticism made against BIMB. Among others is that, its equity-financing modes of Mudharabah and Musharakah represent a very small proportion of its investment portfolio. The available data on its financing revealed that the criticism is legitimate (refer Table 6). Since its establishment, the use of Mudharabah and Musharakah financing remain around one percent of the total financing. Therefore, it was alleged that the bank, as the only Islamic bank in the country, concern itself

Table 6.

BIMB: MODES OF FINANCING (IN %)								
Year	1984	1985	1986	1987	1988	1989	1990	1991
BBA	49.1	68.4	77.0	78.7	76.0	75.8	70.8	73.7
M*	37.2	22.8	15.5	15.0	18.9	20.9	17.8	13.2
Ijrh	9.3	5.9	4.9	3.4	2.9	3.1	11.2	13.0
M**	3.1	0.9	0.3	0.3	0.1	0.06	0.04	0.04
M***	1.2	2.0	2.2	2.1	1.8	0.01	0.01	0.01
Q-H	0.1	0.0	0.1	0.5	0.5	0.06	0.07	0.07
Total	100	100	100	100	100	100	100	100

Source: BIMB Annual Reports 1984-1991.

- M\* Murabahah.
- M\*\* Mudharabah.
- M\*\*\* Musharakah.
- Q-H Qard-Hasan.

only with doing business which assures a profit rather than undertaking projects based on PLS which involves risk in its returns but yield more social benefits such as development of entrepreneurial talent in the community.

While the apprehension is undeniable, the fact that the bank could not resort to mostly Mudharabah and Musharakah has its own explanation. The concept of Mudharabah and Musharakah is still very new to many. Not all of the Malaysian Muslim, not to mention the non-Muslim, are aware of the existing concepts.

Eventhough some already knew the underlying principles, they are less willing to participate in the financing through