

TABLE OF CONTENTS

ACKNOWLEDGMENTS	III
LIST OF TABLES	IV
LIST OF ABBRIVATION.....	V
<i>Abstract</i>	VII
CHAPTER ONE: INTRODUCTION	1
1.1. BACKGROUND OF THE STUDY	1
1.1.1. HISTORICAL DEVELOPMENT OF IFB.....	2
1.1.2. BANKS PROVIDING IFB SERVICES IN ETHIOPIA.....	5
1.2. STATEMENT OF THE PROBLEM	7
1.3. RESEARCH QUESTIONS.....	8
1.4. OBJECTIVE OF THE STUDY	9
1.4.1. GENERAL OBJECTIVE	9
1.4.2. SPECIFIC OBJECTIVE.....	9
1.5. SIGNIFICANCE OF THE STUDY	9
1.6. DELIMITATION/SCOPE OF THE STUDY	9
1.7. LIMITATION OF THE STUDY	10
1.8. OPERATIONAL DEFINATION OF KEY TERMS	10
1.9. ORGANIZATION OF THE STUDY	10
CHAPTER TWO: LITERATURE REVIEW	11
2.1. INTRODUCTION.....	11
2.2. AN OVERVIEW OF IFB WINDOW	11
2.3. BASIC PRINCIPLES AND MODES OF OPERATION OF ISLAMIC BANKING	12
2.3.1. BASIC PRINCIPLES (FEATURES) OF ISLAMIC BANKING	13
2.3.2. MODES OF OPERATION IN ISLAMIC BANKING	14
2.4. ISLAMIC BANKING MARKET OVERVIEW AND PROMISING POTENTIAL OF ISLAMIC FINANCE	16
2.4.1. ISLAMIC BANKING MARKET OVERVIEW	16

2.4.2. PROMISING POTENTIAL OF ISLAMIC FINANCE	19
2.4.3. ISSUES IN ISLAMIC FINANCE.....	21
2.4.4. THE EXPERIENCE OF INTEREST FREE ISLAMIC BANKS	27
2.5. REVIEW OF COUNTRY-SPECIFIC STUDIES ON THE CHALLENGES OF INTEREST FREE BANKING SYSTEM.....	32
CHAPTER THREE: RESEARCH METHODOLOGY	35
3.1. RESEARCH DESIGN AND APPROACH	35
3.2. POPULATION, SAMPLE SIZE AND SAMPLING TECHNIQUE	35
3.3. SOURCES OF DATA AND METHOD OF DATA COLLECTION	37
3.4. DATA VALIDITY AND RELIABILITY	37
3.5. DATA ANALYSIS TECHNIQUES.....	38
3.6. ETHICAL CONSIDERATION	38
CHAPTER FOUR: DATA ANALYSIS AND PRESENTATION.....	39
4.1. CHARACTERISTICS OF RESPONDENTS.....	39
4.2. EXPECTED OPERATIONAL CHALLENGES OF IFB SERVICES IN ETHIOPIA	41
4.3. BANKS' CAPACITY/KNOW HOW TO PROVIDE IFB PRODUCTS.....	44
4.4. LEVEL OF DEMAND FOR INTEREST FREE BANKING PRODUCTS.....	47
4.5. EMPLOYEE AWARENESS LEVEL FOR INTEREST FREE BANKING PRODUCTS.....	49
4.6. RELIGIOUS AND CULTURAL DIFFERENCE IN ETHIOPIA.....	53
CHAPTER FIVE: SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION	58
5.1. SUMMARY OF FINDINGS.....	58
5.2. CONCLUSION.....	60
5.4. RECOMMENDATIONS	61
REFERENCES.....	63
APPENDICES.....	67

ACKNOWLEDGMENTS

It is to the Almighty God that I am most grateful for granting me the wisdom and the strength to come this far.

My deepest and heartfelt gratitude goes to my advisor Ass.Prof. Maru Shate for his constructive criticisms, insightful comments and unreluctant follow-up of the progress of the study. My very special thanks go to the employees and managements of Commercial Bank of Ethiopia, United Bank, Wegagen Bank, Oromia International Bank, Cooperative Bank of Oromia and Nib International Bank for their valuable and considerable support and cooperation during data collection.

I would like to say thank you for my beloved wife Helina Dessie for support in the course study and in this thesis study in financially and material support also deepest and heartfelt gratitude to my relatives.

Finally, I must express my very profound gratitude to colleagues and friends for providing me with unfailing support and continuous encouragement throughout my years of study and through the process of researching and writing this thesis. This accomplishment would not have been possible without them. Thank you.

LIST OF TABLE

	Page No
Table 1; Total number of permanent interest free banking employee	36
For sampled size	
Table 2; Table for determining sample size of a known population	37
Table 3; Characteristics of the Respondents	39
Table 4; Expected operational challenges of IFB services in Ethiopia	42
Table 5; Banks capacity/knowhow to provide IFB products	45
Table 6; Level of demand for IFB products	48
Table 7; Employee awareness level for IFB Products	50
Table 8; Religious and cultural difference in Ethiopia	54

LIST OF ABBRIVATION

AAOIFI—Accounting and Auditing Organization for Islamic Financial Institution

ABN—Algemene Bank Netherland

AMRO—Amsterdam Rotterdam Bank

ARCIFI—International Arbitration and Reconciliation Center for Islamic Financial Institution

CBD—Commercial Bank Deposit

CBE—Commercial Bank of Ethiopia

CBO—Cooperative Bank of Oromia

DB—Deutsche Bank

FSA—Financial Service Authority

GCC—Gulf Co-operation Council

GCIBAFI—The General Council for Islamic Banks and Financial Institutions

HNWIs—Middle Eastern High Net-Worth Individuals

HSBC—Hong Kong and Shanghai Banking Cooperation

IAH—Investment Account Holder

IDB—Islamic Development Bank

IES—Islamic Economic System

IFB—Interest Free Banking

IFIs—Islamic Financial Institutions

IFSB—Islamic Financial Service Board

IFSF—Islamic Financial Stability Forum

IIFM—International Islamic Financial Market

IIFS—Institution offering Islamic Financial Service

IIRA—International Islamic Rating Agency

IMFIs—Islamic Micro Finance Institutions

LCM—Liquidation Management Center

NBE—National Bank of Ethiopia

NBFIs—Non Bank Financial Institutions

NIB—Nib International Bank

OIB—Oromia International Bank

OIC—Organization for Islamic Cooperation

PLS—Profit and Loss Sharing

SSB—Sharia Supervisory Board

UBS—Union Bank of Switzerland

UB—United Bank

UK—United Kingdom, V/P CATS—Vice president Customer and Accounts

WB—Wegagen Bank

WFS—Western Financial System

Abstract

Islamic banking system is a fairly new player in the Ethiopian financial industry, and thus, is faced with inadequate legal and regulatory environment; banks provide conventional banking service on IFB window, problem of providing dedicated window and banks use IFB related services for conventional banking challenges. The main purpose of this study is to assess and describe operational challenges and prospects of Islamic banking systems in selected banks in Addis Ababa.

The study tries to address the basic questions. In order to address the basic questions and objective, descriptive survey research design was employed which comprises quantitative methods of data gathering. Data was gathered through questionnaire that was made to triangulate and increase the validity of the data obtained. The study selected Commercial banks of Ethiopia that deliver IFB Service. Among 442 population of the research used there were a total target populations for this research were 320(55%) employees using non-probabilistic expert sampling technique. To collect representative data, 175 questionnaire copies were distributed. The data collected from target respondents through questionnaire was compiled and summarized by using SPSS statistical package for social science software version 21. The variables were analyzed by using frequency counts and percentages.

The significance of the study clearly shows Islamic banking is mostly large amounts that were given great concern by the bank in relation to the country's growth and transformation plan. However, interest free banking has different challenges that can be observed from employees and the banks perspectives.

Finally, the results indicate the increased growth of the banking sectors have to faces some challenges and these must be overcome. Interest free banking is playing vital role in the growth of economy with special reference to corporate social responsibility.

Keywords; *Islamic banking, operational challenges, Commercial banks*