Banking control laws in saudi arabia

Countries

Introduction

The Kingdom of Saudi Arabia is one of the most economically sound nations of the Middle Eastern region. It is oil rich and has relatively robust banking system. Its laws have been rather progressive over the past few years. However excessive government interference, Islamic laws and too many amendments may have prevented the banking system form achieving its full potential.

Laws in the Saudi Arabian banking sector

The official religion in Saudi Arabia is Islam and all the citizens within this country are required to prescribe to this faith. Additionally, the latter religion also forms the basis of the legal code within this country thus implying that most of foreign investors may have a difficult time trying to carry out business within such a country. (Library of Congress, 2008)

The banking sector industry is highly stable. This is partly because it is often regulated by the Saudi Arabia Monetary Fund abbreviated as SAMA. Those banks that conform to Islamic law are not expected to pay their respective depositors for holding theirmoneyfor them because they prohibit interest rates.

Additionally, a number of banks benefit from high amounts of oil revenues, consequently, they are in a position to take up a lot of profits. As of the financial year 2006, Saudi Banks boasted of revenue amounting to one hundred and thirty eight billion US dollars. In Saudi Arabia, no bank has ever been passed of as being a failed one. Also, the latter country only has about nine percent worth of non performing loans as of 2007.

Given all the latter facts and figures, one can therefore imagine that Saudi Bank laws are quite favorable for business. However, compared to other developed nations, there are a number of issues that make this sector lag behind. First of all, the country only allowed foreign banks to operate in their nation after 2000. Consequently, the regulatory framework for their operation is not well laid out. The Gulf International Ban, Emirates bank International and National Bank of Kuwait are just some of the few foreign banks within this banking sector.

The latter country passed the Capital market law in 2003 that was designed to eliminate barriers faced by foreign financial institutions. However, many foreign banks are yet to be satisfied by the bankingenvironment. More effective legislation is still needed in this regard.

Besides the latter matter, the Saudi government is yet to look into development of its investment and intermediary banks. This is largely because their laws do not consider any of the latter institutions seriously and this has therefore prevented growth in the latter sector. In other developed nations such as the United States, the investment banking sector has been one of the drivers of the economy. Consequently, if Saudi Arabian laws were to acknowledge this fact, then they would enact laws top boost that sector and thus make the issue more feasible. (Al Hamidy, 2009)

In Saudi Arabia, there is also minimal legislature on the issue of entrepreneur financial sectors and also in the venture capital segment. This means that most local investors tend to look towards their ownfamilyand friends for capital; a method that always hinders economic growth. In close relation to this is the fact that the government has yet to develop the insurance industry.

Through the Cooperative Insurance Companies Control law, the government has a real monopoly in this industry. Again, such a law has caused Saudi Arabian economic institutions to lag behind certain countries in the developed world. On top of the latter, there is also a need to acknowledge the fact that these laws are rather traditional and they are affecting the perceptions of this country in the eyes of other potential investors.

However, besides having the latter negatives, there are certain developments that have gone on in the banking sector over the past few years; these signify some moves towards the right directions. First of all, SAMA has tried growing some of the following sectors

- Mutual funds
- Bonds
- Stocks
- Initial Public offerings
- etc

In the year 1997, the latter country opted to open these investments to people from other countries and therefore experienced a time of economic boom. It should be noted that most investments prior to that year were restricted to the Gulf Cooperation Council. This means that now citizens are financially aware and this could have explained why the country reported close to six hundred and fifty billion dollars worth of capitalization there. (Al Sayari, 2008)

Some seven years ago, the country decided to pass the Tadawul law that was designed to make some of these securities more accessible to the country's citizens and thus encourage them or make more investments in the sector. The latter law was passed in order to facilitate online trading – an aspect that is common among most developed nations. This was also in line with the official trading floor that had been established within the latter country.

Despite the latter developments, there are still a number of flaws that have been reported within this system. First of all the biggest problem facing them is secrecy in which citizens may take part in an IPO but fail to realize the benefits that they had expected. The country's laws have also failed to recognize some of these trading hurdles that have been going on in the last few years thus disappointing investors and making the latter sector weaker than it actually is. The lack of transparency in this trading has prevented further growth and development there.

In line with the latter matter is the challenge of government interference in their banking sector. In certain circumstances, government intervention can be a welcome issue when done in an open manner and when it involves a series of stakeholders. However, because of the legacy of powerful families (linked to the Dynasty) within this country, it is often common to find that the latter party is given precedence when purchasing securities compared to other ordinary citizens.

Most of the time, this government interference has been kept under check. However, in 2006, the stock market recorded an unexpected decline after positive gains for three years. This served as warning sign to investors that their system was not as safe as expected. (IMF, 2007)

It should be noted that a number of portfolios within the Saudi Arabian banking sector are rather conservative. This is largely because in the past, the latter sector has been resistant to a series if shock. Consequently, most banks feel as though they have the ability to resist these external factors by maintaining conservative product offerings and also by having large cushions of capital. In line with the latter, most banks tend to augment government securities through the utilization of derivative products.

The latter methods are not sufficient because there is no incentive for purchasing interbank trades through the process of reviewing pricing. Consequently, one can assert that there are a number of issues that are yet to receive some improvement and they include:

- Liquidity
- Credit
- Interest rates

If the government were to review their repurchasing law through deregulation of pricing offered by the Saudi Arabian Monetary Agency (SAMA) then this would go a long way in improving the performance of this respective system.

The issue of Asset concentration in most Saudi banks needs to be addressed. The country needs to look into the implications and asset concentration more seriously. This can be done through the use of certain mechanisms. First of all, they can work on their level of household indebtednesses which statistics have shown to be increasing. Besides this, the government needs to work on certain price risk that may be associated with Sharia complaint offerings.

This country‘ s banking sector is yet to include the private sector in its industry offerings. This is largely because there are very limited banking intermediaries within this country. In fact, it has been shown that twenty nine percent of the private sector has not been claimed by this arena. Consequently, diversification is urgently needed in this sector. Besides the latter matter, these diversification efforts need to be done though the support of institutional efforts.

It should be noted that the equity market in Saudis Arabia is one of the most stable within the Arabian stock market. However, there is still a need to improve this framework through improvement of the Companies Law that had been passed in 1965. An amendment is urgently needed in this line of work. Also, there is a need to re-examine most of the liquidity arrangements, debt markets and even deficit financial arrangements. (IMF, 2007)

Lastly, the Saudi Arabian Monetary Agency has been solving problems through temporary decisions making mechanisms and this may affect the overall credibility of the sector

Conclusion

There is no doubt that the Saudi Arabian banking sector has undergone numerous changes over the past decade. They have managed to open up their markets to foreign investors. However, the system is still marred with secrecy and government interference. Their systems are still traditional compared to their counterparts in other regions of the work and all these can be fixed through legislative amendments but most importantly a change in attitude.

References

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