

# The Role of the Jordanian Banking Sector in Economic Development

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## Abstract

The aim of this study is to investigate the impact of the Jordanian banking sector on economic development that was measured by the Gross Domestic Product (GDP). It aims to identify the role of the Jordanian banking sector in the support of economic development through the study of the size of the credit facilities offered by banks.

The study relied on descriptive and analytic method, as well as on field study. The population of this study represents the working banks in Jordan, which offers various banking services to the customers. The tool of the study include data of credit facilities, banking deposits for Jordanian banking sector, and gross domestic product that were collected from the annual financial status of Jordanian Central Bank for the period (2000- 2015).

The study found that there is a significant statistical impact of the factors (the deposits of the banking sector, Credit facilities) on Gross Domestic Product (GDP). The study rejected the null hypothesis and accepted the alternative hypothesis for the two hypotheses. Also, the study recommended that the Jordanian banking sector should expand in the granting of credit facilities to all economic sectors.

**JEL Classification:** G21, G29, E51, A10, E58

**Keywords:** Jordanian banking sector, banking deposits, credit facilities, economic development, central bank

## 1. Introduction

Subsequently, the banking sector play important role in the economic resource allocation of countries. The banking system is a major factor that affects the organization of social and economic life cycle in the economies of the world. It is considered as an indicator of economic and social development .Also, developed economic system should be characterized by the existence of a modern and sophisticated banking system which contributes to achieving economic balance. It also encourages domestic and foreign investment through the banking system's ability to states. The aim of the banking system is to attract savings locally and abroad, and direct those savings into Productive investment. As a result, this contributes to the achievement of economic and social development process, and also facilitates investment activity.

Basically, banks have an important role in advancing development in the economy. They perform the role of collecting savings (units of surplus) and directing those savings into units of the deficit. This can be accomplished through its role in financing the different economic sectors and the development of economic activity.

The banks' role in the financing of small and medium projects has a major effect in supporting the poor and the middle layer. Banks perform a function of reducing the rate of unemployment. Thus, they provide medium and long-term financing for projects production and services. Infrastructure construction has a big role in attracting domestic and foreign investments, export promotion, geographic expansion of banks, opening new bank branches, and staff training in banks. Consequently, this helps to stimulate the economy and reduce the size of unemployment and the support of new projects.

## 2. Research Problem and Research Questions

Banks play a significant role in the economy and they are considered to be the heart of the economy of any country. The problem of the study shows that Jordan is suffering from an increase in public debt, where public debt amounted to 25 850 million in 1st of October, 2016. Also, there was a decline in the rate of economic growth, as well as a permanent deficit in the trade balance.

The banks are the main player in any economy by being able to mediate between the units of the deficit and the surplus units. Thus, this leads to the provision of credit facilities that contribute to economic development in terms of attracting new investment, reducing the rate of unemployment, and increasing the volume of exports and the Gross Domestic Product (GDP). The problem of the study is in studying the effect of the Jordanian banking sector on economic development that was measured by the Gross Domestic Product (GDP). Therefore, the research questions of this study are as follows:

1. What is the size of financing the productive projects by banks in Jordan?
2. Is there any significant statistical impact of the credit facilities granted by the banking sector on the different sectors of the economy's Gross Domestic Product (GDP)?
3. Is there any significant statistical impact of the deposits of the banking sector on Gross Domestic Product (GDP)?

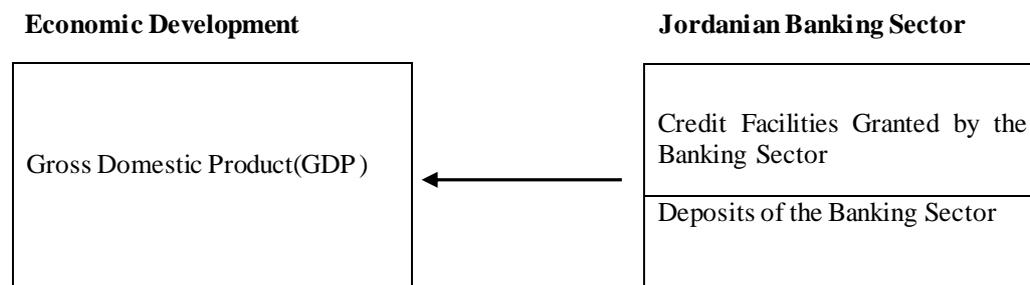
**3. Study Objectives**

Therefore, the objectives of the study are as follows:

1. Identify the role of the Jordanian banking sector in support of Economic Development through the study of the size of the credit facilities offered by banks.
2. Identify the development of the banking system in Jordan.
3. Identify the impact of the credit facilities granted by the banking sector to the different sectors of the economy's Gross Domestic Product (GDP).
4. Identify the impact of the deposits of the banking sector on Gross Domestic Product (GDP).
5. Making the appropriate recommendations

**4. Study Framework and Hypotheses**

To study the role of the Jordanian Banking Sector in economic development, the following model was constructed as follows:



Furthermore, to study the role of the Jordanian Banking Sector in economic development, the following hypotheses were built. These hypotheses, however, are directly related to the research questions:

Ho1 - There is no significant statistical impact of the Credit facilities Granted by the banking sector in the Gross Domestic Product (GDP) at  $p \leq 0.05$ .

Ho2 - There is no significant statistical impact of the Deposits of the banking sector in the Gross Domestic Product (GDP) at  $p \leq 0.05$ .

**5. The Theoretical Framework**

*5.1 Concept*

The emergence of banks in Jordan began back in 1925 when a branch of the Bank in Ottoman was opened. In 1934, the Arab Bank in Amman was opened. However, in 1960, the number of banks amounted to eight banks. In 1980, there was a large spread of the banks and their branches have now become 26 commercial and Islamic banks. The Central Bank of Jordan was established in 1964. It considers the fiscal authority in Jordan and performs the functions of central banks such as supporting monetary stability and fostering economic and social development (Alruihat, 2014).

The number of banks in Jordan is twenty-six, and they are distributed as follows: 13 Jordanian commercial banks (9 foreign commercial banks and three Jordanian Islamic banks which are Islamic International Arab Bank, Jordanian Dubai Islamic Bank, Jordanian Islamic bank) and a foreign Islamic bank known as AL-Rajhi Bank (Annual Report of the Association of Banks in Jordan in 2015).

The commercial banks provide the customer with various services (modern and traditional services) such as accepting deposits and granting credit to various economic sectors and facilities. Other functions are credit card provision, the provision of economic and financial consulting and bill collection, and contributing to development and economic plans.

Subsequently, the deposits are the most important sources of funds for banks and facilities. Investments are considered to be the most important and most profitable for the banks. Also, the difference between the debt interest and credit interest is the spread, and it considers the profit of the bank in achieving profit (Ramadan & Goda, 2013).

**Credit Facilities:** The bank provide a sum of money to the customer with the right of repayment with interest and with any other penalties, guarantees, or commitments issued by the Bank.

Additionally, there are different types of direct credit whereby the Bank provides money to the client. Examples include loans and debt current and credit card .On the other hand, the second type of credit facilities does not include provision of money. However, the bank offers Bail and Commitment to the customer. Examples include letters of credit which guarantees Banking (Al-abadallat, 2016) Table 1 below shows the size of the credit facilities granted by the Jordanian banks.

Table 1. Granted credit facilities

Credit Facilities	Year
4546.5	2000
4948.9	2001
5130.0	2002
5262.400	2003
6189.200	2004
7744.300	2005
9761.900	2006
11295.600	2007
13044.300	2008
13317.200	2009
14451.400	2010
15851.200	2011
17829.800	2012
18939.700	2013
19274.500	2014
21103.500	2015

(Annual Report of the Central Bank of Jordan, 2015)

**Banking Deposits:** This is the process whereby the customer deposited a sum of money in his/her account at the bank. Thus, he/she have access to the money in the banking investment. Also, the bank pays interest to the customer. Basically, some types of deposits include: current or demand deposits, savings deposits, and time deposits.

However, both local and foreign currency, majorly in US dollars, can be deposited in banks in Jordan. Also, the Jordanian Dinar has a fixed exchange rate with the US dollar (Shabib, 2015). Table 2 below shows the size of the deposits of working banks in Jordan.

Table 2. Banking deposits

Banking Deposits(m)	Year
8224.5	2000
8721.3	2001
9367.7	2002
9969.4	2003
11564.1	2004
13119.3	2005
14591.9	2006
15988.1	2007
18102.6	2008
20298.4	2009
22504.8	2010
24377.9	2011
24969.7	2012
27593.2	2013
30261.000	2014
32598.5	2015

(Annual Report of the Central Bank of Jordan 2015)

**Economic Development:** This is the process of increasing the real national income and the continuation of this increase for a long period of time. This is done so that this increase will be greater than the rate of increase in population such that there is a change in the restructuring of the economy in the state.

In another definition, economic development can be defined as the increase in the national output of goods and services for the period of time (one year), but with the need for a technological, technical, and organizational productivity changes in the existing institutions.

### Importance of Economic Development

1. It is a tool to reduce the economic gap between the developing countries and the developed countries. Thus, there are two groups of factors.

#### A. Group-economic factors

- Economic dependency
- Sovereignty single mode of production
- Widespread unemployment

#### B. Group non-economic factors: Examples are:

- Great increase of population
- Low level of health
- Low level of education

2. It is a development tool for economic independence.

However, the access of developing countries to political independence is not a basis for economic development, but it is a must for it to be economic independent (Jmon, 2004).

**Gross Domestic Product (GDP):** It is defined as the monetary value of all kinds of final products (goods and services) that was produced during a certain period of time, usually a year (Al-Shammari, Shrouf, 2007). Thus, Table 3 below shows the size of the GDP.

Table 3. Gross domestic product

GDP at Current Market Prices	Year
5998.6	2000
6363.7	2001
6794.0	2002
7228.8	2003
8090.7	2004
8925.4	2005
10675.4	2006
12131.4	2007
15593.4	2008
16912.2	2009
18762.0	2010
20476.6	2011
21965.5	2012
23851.6	2013
25437.1	2014
26637.4	2015

(Annual Report of the Central Bank of Jordan 2016).

### 5.2 Previous Study

Consequently, there are many studies that address The Role of the Jordanian Banking Sector in Economic Development. Therefore, the most important of these studies are:

1. The Study of Yusuf (2010) entitled "The Role of the Banking System to Finance Economic Development in Syria."

The study problem was represented in answering a series of questions, including: Is there alignment between the Syrian regime and economic trends and the banking system in Syria? Is there any specify way through which the banking system funded Economic Development in Syria? The importance of this research is to identify the

reality of the Syrian banking system and the reasons for its inability to respond to economic developments in Syria, as well as to identify the bank credit size in Syria.

Furthermore, the study concluded that there is a strong relationship between bank deposits and semi cash local and GDP .In addition, the study recommended the development of credit facilities as a percentage of deposits so as to be able to finance the Economic Development.

2. The Study of (Sarwer, Ramzan, Ahmad, 2013) entitled "Does Islamic Banking System Contribute to Economy Development."

This study, with the aid of a group of economic experts, aims to study the impact of Islamic banks in the Economic Development of Pakistan. The study used eight questions attached to the role of Islamic banks in human resource mobilization. Also, it urged customers to deal with Islamic banks and the allocation of the financial resource and financial crises, internal and external inflation and recruitment of human resources, and domestic and external trade and GDP. The study concluded on the opinions of experts on the existence of a significant role for Islamic banks in economic development. Therefore, the development of the provided services should aim to support economic development.

3. The Study of (Al-oqool, okab,bashayera, 2014) entitled "Financial Banking Development and Economic Growth: A Case Study of Jordan."

The study aimed to test the relationship between the growth of financial services offered by Islamic banks and economic growth in Jordan during the period from 1980-2012. In addition, the researcher studied the relationship between the total funding and total savings, and their impact on the economic growth was measured by GDP.

The study showed the presence of a bi-directional relationship between the total funding and GDP. However, this reflects the contribution of the Islamic banks towards Economic Development. There is an existence of a one-way relationship between savings deposits for Islamic Banks and GDP .Thus, this reflects the liquidity problem in Jordanian banks in general and Islamic banks in particular.

4. The Study of Rashed (2011) entitled "The Role of Commercial Banks in the Economic Development: An Empirical Study of the Banking Experience in Kurdistan Province - Iraq for the Period (2007-2010)."

The research importance shows the great role of commercial banks in supporting economic development. This study places emphasis on the important interest of Iraq's Kurdistan Regional Government and commercial banks to activate its role in financing economic sectors. Additionally, the problem of the region has much national resources

Nevertheless, the government doesn't benefit from these resources, but they depend on the export of goods .Therefore, the government should study the obstacles of banks in fostering economic development.

5. The Study of Naji (2016) entitled "The Role of Commercial Banks in the Financing of Economic development – An Empirical Study of the Bank of Agriculture and Rural Development."

The problem of the study is in identifying the role of banks in Economic Development, and the role played by the commercial banks, in particular, in terms of development. This is because commercial banks have a pivotal role in terms of funding for productivity projects. Also, they help to identify the role of the Agriculture Bank and Rural Development in economic development.

Therefore, the objective of the study is to identify the role of the loans provided by commercial banks in the financing of Economic Development. It helps to determine what aspects of the funding that is required for economic development .Thus, this is because the Bank – Biskra Branch – provides a variety of financial products to economic projects. In addition, this includes several other types of loans that results to development of the Algerian economy. Furthermore, the study recommended the encouragement of individuals to set up productive projects that can serve Economic Development.

6. The study of Wesam (2013) entitled "The Role of Commercial Banks in Financing the Small and Medium Enterprises: An Empirical Study of Agriculture and Rural Development Bank in the State of Biskra."

The study shows that small and medium enterprises sector in Algeria are suffering from drastic problems. Also, their contribution towards the growth of the Algerian economy is weak .Subsequently; the problem of finance is a major problem plaguing this sector. As a result, the study supports the banking sector and other vital sectors of the economy.

The most important study shows the fact that small and medium enterprises are of considerable importance to the economy. The sector has been given much attention in the Algerian economy most recently, but it needs more

support. Thus, the study aimed to identify the reality of small and medium enterprise in Algeria and its role in the development of the economic institutions sector. Furthermore, the most important modes of financing were provided by the Agriculture Bank and Rural Development in supporting small and medium projects.

The study concluded on several results such as the importance that the bank offers to all kinds of finance for the small and medium enterprises. Also, this study should think about alternatives to financing for these projects in order to contribute well to the economic development of Algeria.

7. The study of Albkai (2013) entitled "The Role of Islamic Banks in the Achievement of Economic Development: A Case Study Syrian Arab Republic."

The aim of the study is to indicate the role of the Islamic banks in financing the development and the importance of better distribution of wealth to achieve economic balance. The study problem is aimed at answering a series of questions such as: Is there any alignment between the Syrian regime, the economic trends, and the banking system? Is there any specific way in which the Islamic banks funded Economic Development in Syria?

Therefore, the important of the research is in understanding the reality of the Syrian banking system and to identify the reasons for its inability in responding to economic developments in Syria. The study concluded on the existence of a strong impact and relationship of bank deposits and semi cash in the composition of GDP. The researcher recommended the need to change the structure of the banking system to be able to finance Economic Development.

## 6. Study Method

### 6.1 Methodology of the Study

For the purposes of testing the hypotheses of the study and to address the research question of the study, the study relied on descriptive and analytic method, as well as field study. With regard to siding the descriptive, the study gave an accurate picture of the effect of the Jordanian banking sector on Economic Development that was measured by the Gross Domestic Product (GDP). Through previous studies, as for the side of the field; the study collected the necessary data from the sites of the central bank of Jordan.

### 6.2 The Population of the Study (Scope of the Study)

The population of the study represents the working banks in the Jordan which offers various banking services to customers. The study made use of the data of the GDP, data of credit facilities, and banking deposits for the working banks in Jordan for the period (2000 -2015).

### 6.3 Tools of the Study

The tool of the study was the data of credit facilities, banking deposits for Jordanian banking sector, and gross domestic product that were collected from the annual financial statement of Jordanian Central Bank for the period (2000-2015).

## 7. The Results of Hypotheses Testing

### 7.1 Descriptive Statistics

This section contains the results of the study aimed to ascertain the effect of the Jordanian banking sector on Economic Development that was measured by the Gross Domestic Product (GDP). The study used the Statistical Package for Social Sciences (SPSS) software to extract the averages, arithmetic mean, and standard deviations of the variables. Thus, the result of the descriptive statistics test is shown in Table 4.

Table 4. Descriptive statistics of the variables

Std .Deviation	Mean	Maximum	Minimum	
5751.3282	11793.150	21103.5	4546.5	Credit facilities
8044.6881	18265.775	32598.5	8224.5	Banking deposits( m)
7363.0475	14740.238	26637.4	5998.6	GDP

### 7.2 Test of the Study's Appropriate Model

#### Normal Distribution Test

To check how close is the data from normal distribution, the study used Kolmogorov-Smirnov test where the decision rule is to accept the null hypothesis (data followed a normal distribution) if the probability of a test (k-s) is more than 5%.

In Table 5, the result of normal distribution test showed that the probability (k-s) for all variables is greater than 5%. This means that all the variables follow a normal distribution.

Table 5. Normal distribution table

Kolmogorov-Smirnov Test		
Sig	(k-s)	Variable
.877	.590	Credit facilities
.986	.455	Banking deposits( m)
.806	.641	GDP

**Pearson Correlation of Independent Variables**

Table 6 shows that there is a high correlation between Credit facilities and Banking deposits where the R value is 99%. Thus, this result shows a linear correlation subscribe problem that requires a VIF test.

Table 6. Pearson correlation of independent variables

		Credit Facilities	Banking Deposits( m)
Credit Facilities	Pearson Correlation	1	
	Sig. (2-tailed)		
Banking Deposits( m)	Pearson Correlation	.99**	1
	Sig. (2-tailed)	.000	

**Collinearity Test**

To achieve this, Collinearity Statistics scale was used .It calculates the coefficient (Tolerance) for each variable of the independent variables .In addition, it founded another coefficient (Variance Inflation Factor VIF). This test is a measure of the impact of the correlation between the independent variables. Table 7 shows the value of VIF for all the independent variables which is the largest (5). This means that the study model contains the interference and subscription problem .Therefore the study studied the independent variables using a separate model.

Table 7. The linear overlap of the independent variables

VIF	Variables
56.330	Credit facilities
56.330	Banking deposits( m)

**7.3 Results of Testing the Hypotheses**

**7.3.1 Test of the First Hypothesis**

To test the first hypothesis been used, linear regression test and the result in Table 8 show that there is a significant impact of independent variables on the dependent variable .This, however, shows that there is a good relation between Credit facilities and the Gross Domestic Product (GDP), the value of Sig. less than 0.005, and the value of Pearson correlation ( $R^2$  ) = 98%. This results to the rejection of the null hypotheses and the acceptance of the alternative hypotheses.

Ho1: There is significant statistical impact of the Credit facilities granted by the banking sector in the Gross Domestic Product (GDP) at  $p \leq 0.05$ .

Table 8. Linear regression test

First model		symbol	Credit facilities
SIG.	Coefficient	$\alpha$	(Constant)
.005	-523.410		
.0000	.457		Credit facilities
	10.26		F- Statistic
	0.000		SIG.
	.98		$R^2$

**7.3.2 Test of the Second Hypothesis**

To test the second hypothesis been used, linear regression test and the result of Table 9 shows that there is a significant impact of independent variables on dependent variable .This refers to a good relation between the Deposits of the banking sector and the Gross Domestic Product (GDP), the value of Sig. less than 0.005, and the value of Pearson correlation ( $R^2$  ) = 96%. In addition, this leads to the rejection of the null hypothesis and the acceptance of the alternative hypothesis:

Ho2: There is significant statistical impact of the Deposits of the banking sector on the Gross Domestic Product (GDP) at  $p \leq 0.05$ .

Table 9. Linear regression test

Second model		Symbol	Banking deposit
$GDP = \alpha + \beta_1 \text{Banking deposits (m)} + e$		$\alpha$	(Constant)
SIG.	Coefficient		Banking deposit
.010	-1382.435		F-Statistic
.0000	.588		SIG.
	9.187		$R^2$
	.000		
	.96		

## 8. Summary and Concluding Remarks

This study attempts to investigate the impact of the Jordanian banking sector on Economic Development that was measured by the Gross Domestic Product (GDP). Thus, the findings of the study can be summarized below:

1. There is a significant statistical impact of the factors (the Deposits of the banking sector, Credit facilities) on the Gross Domestic Product (GDP).
2. The study rejected the null hypothesis and accepted the alternative hypothesis for the two hypotheses.
3. There is a good statistical relationship between the factors (the Deposits of the banking sector, Credit facilities) and the Gross Domestic Product (GDP).
- 4- The Jordanian banking sector has a major role to play in Economic Development.

## 9. Recommendations

However, the study recommended the following:

1. The Jordanian banking sector should expand in the granting of credit facilities to all economic sectors.
2. The Jordanian central bank should encourage and provide incentives for the banks to finance the small and medium enterprises.
3. The Jordanian central bank should increase banking awareness among customers to increase the volume of bank deposits because it is the main source of the bank's money.

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