

ECONOMICS IN ISLAM

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INTRODUCING 'ECONOMICS IN ISLAM'

Islamic Economics, Banking, and Finance is presented here by Dr. Waquar Anwar for the lay reader under the title: ECONOMICS IN ISLAM, in order to emphasise the roots: the early Islamic economy. Instead of depending on the contemporary literature on the subject he prefers to go back to the earliest Islamic economies. Instead of adopting conventional terminologies and categories of thought he uses the very terms the first generation of theorists, the fuqaha, used to elaborate what Islamic economic behavior would be and how Islamic economic and financial institutions would function. Add to this the information that the author is not an economist but an expert in an area indispensable to economic management, and you have a flavor of the distinct potion in front of you. Originally presented as television series, this is a good read that not only provides information but also provokes to think.

That is good as far as it goes. But there are dimensions of living Islamically in a twenty-first century plural society that deserve special attention. You have to be fair and also efficient and your project must be doable. The predominance of *murabaha* and rarity of profit-sharing arrangements (in business finance) and of *qard hasan* [interest free loans] in personal finance are rooted in the sociology of the Indian Muslim situation. Learning from the recent setback to microfinance in India, we need devising other institutions for helping the poor rather than placing the entire burden on banks. In fact an integration of Waqf-Zakat-Islamic Investment

institutions may be able to do much more than mere financial intermediaries could do.

The mention of sociology reminds one of the need of field studies. Unfortunately, empirical research has yet to find favour with Islamists, scholars as well as activists. The usefulness of publications like the one before the reader would increase manifold if they included reports on practice and application. It is valid to ask what Islamic banks are doing for the poor, but it is not wise to ignore what they have done for the rich (among Muslims). Muslim society in India, as all societies everywhere including the early Islamic society at Madinah, comprises the rich as well as the poor. The poor must be served, but it is also good to help rich Muslims manage their wealth observing the religious restraints. The next edition of Dr. Waquar Anwar's work would become more useful by taking into consideration the needs of those at the bottom as well as those at the top of the Muslim society, wealth-wise, and not ignoring the crucial middle class whose rise and rise is the latest news in India.

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San Ramon, California
1 December 2011

PREFACE

Books, articles, research papers, lectures and other forms of presentation on Islamic banking and Islamic finance abound. But Islamic economics, the basis of all these write-ups and deliberations, is seldom discussed. This book touches this hitherto less discussed topic. Of course there are some very valuable books and research papers available on Islamic economics. But there is always the scope of providing an add-on to as well as reiterating what has been said on the subject.

It is debatable whether or not Islamic economics can be described as a distinct branch of economics. Alternatively, the stress may be on presenting the teachings of Islam on the issues discussed in contemporary economics. This book chooses to be equidistant from both the positions. Hence the title *Economics in Islam*. However, the forceful writings of authors, particularly those of Syed Abul Ala Maudoodi, Dr. Umer Chapra, Dr. Mohammad Nejatullah Siddiqi and Dr. Fazlur Rahman Faridi, have delineated Islamic Economics as a separate branch. Despite that, scope for cynicism remains and further qualitative researches are required to establish that what we are discussing is a separate branch of the subject in its own right.

In order to describe the teachings of Islam on contemporary issues of conventional economics, this book delves upon the economy of early period of Islam, the economic aspect of the life of Prophet of Islam (may Allah bless and greet him) and his household, teachings of the Qur'ān and the deliberations of Islamic jurists (*Fuqahah*). A case has been formulated in support of

prohibition of interest in Islam by describing the teachings of Islam in the Qur'ān and the Prophetic traditions. Further, the classifications of goods (*Maal*) defined by Islamic jurists have been compared with the definition and classification of economic goods in the contemporary economics. Other specific discussions, inter alia, in this book relate to the Islamic teachings regarding business transactions leading to creation of debt and the justification of the Islamic approach as against the wrong done by the approach of contemporary economics.

A discussion on Islamic banking has been kept in brief so that the book may remain focussed on the underlying concepts of economics in Islam.

The subject matter of this book was presented in a series of sixteen episodes recorded by Zee Salaam, the Urdu language TV Channel. The author is thankful to Mr. Shahabuddin Yaqub, producer of Zee Salaam, for his deft persuasions, and support. The thought process got crystallised in the course of those presentations.

Each chapter of this book was published in *Radiance Viewsweekly*. The author is grateful to Mr. Sikandar Azam, Editor of the weekly published from New Delhi, for the personal care in editing the write-ups.

The author is also grateful to Mr. Shabbir Alam Khan and Mr. Shahid Jamal Ahmed for many useful feedbacks received from them.

Finally the author is deeply indebted to Dr. Mohammad Nejatullah Siddiqi for reviewing the book and writing its introduction as a foreword.

CHAPTER - I

INTRODUCTION

INTRODUCTION

Islam is proactive about worldly resources for mankind. This approach can be understood by the following verse:

And We have given you (mankind) power in the earth, and appointed for you therein a livelihood. Little give ye thanks! (The Qur'ān 7:10)

The Arabic word that has been translated as 'livelihood' is *ma'aish* that can be alternatively translated as worldly resources or economic goods. God has made earth a storehouse of required commodities and bestowed man with the opportunity, power and authority to utilise these for his livelihood. A corollary of this position is that utilisation of these worldly goods, as such, is desirable. If any element of undesirability comes in, it is because of improper utilisation of the resources. The verse as above says that generally man is not thankful for the bounties of God. This is the basic message of the Qur'ān that human beings should be aware of the kindness of the Almighty and recognise it through their thoughts (convictions) and deeds. The Qur'ān calls for such awareness, acceptance and recognition of the heavenly gratitude – the process is called *shukr* in the Islamic parlance – and to lead life in accordance therewith.

The above mentioned positive and practical approach of Islam about resources is also found in a number of traditions of Prophet Muhammad (may Allah bless and greet him). In one such tradition it is related that once the Prophet summoned one of his companions

and asked him to proceed on a mission saying that the companion will be successful in the task and he will also get wealth. The companion said he had accepted the faith for reward hereafter and not for getting wealth. The Prophet replied, "Good wealth is good for a good person [*nemal malus saleh lir rajulis saleh* – *Musnad Ahmad*]." In another tradition the wordings of the Prophet's reply recorded are, "How good is the good wealth for a good person [*neimma bil malus saleh lir rajulis saleh*]."

It means that a demarcation line between good wealth and bad wealth is required and only the wealth that can befit the expression 'good' relegating everything else in the negative list that is unfit for a believer, is recommended for a good person. Such good earning is so much desirable that another tradition of the Prophet gives the good tiding that a truthful and honest trader will be a companion of Prophets, the most righteous and the martyrs. [*Tirmidhi*].

Yet another tradition of the Prophet says that God loves a person who toils hard in search of his livelihood [*Tirmidhi*]. So much so that earning *halaal* (clean) livelihood is obligatory after obligatory prayers [*Mishkaat*]. In other words, a believer is first required to abide by the pillars of Islam and perform obligatory prayers in accordance therewith and then toil for earning his livelihood. It is the secondary obligation after the primary one. This principle can be best understood by studying the following verse of the Holy Qur'ān:

And when the prayer is ended, then disperse in the land and seek of Allah's bounty, and remember Allah much, that ye may be successful. (The Qur'ān 62:10)

The prayer referred to in the above verse is the Friday congregation. The believers are asked to respond to the call of payer first and then disperse on earth in search of livelihood. Thus an effort for earning worldly

resources is not only acceptable and advisable; it is enshrined too, provided it does not come in the way of the primacy of the faith in God and performing obligatory prayers. A true believer is required to maintain the correct sense of proportion. Further, God should be remembered even in the course of earning resources because the wealth so amassed is a divine bounty.

DIGNITY OF LABOUR

In pre-Islamic period of Arabia, as in the world today, one of the major factors on which the position of a man was decided was the nature of job he was doing. Dignity of a person was linked to the mode of his earning. The position in the world today is not much different. An executive is higher in social ranking than a clerk. A person doing manual labour is considered lower in strata than that engaged in a white collar job. Islam contradicts this position and teaches that there is no relationship between honour of a person and his mode of occupation, provided the occupation itself does not fall in the undesirable category.

The Arabs in general and those residing in Makkah in particular, at the time of Prophet Muhammad (may Allah bless and greet him), were very much conscious about the social position of a person normally determined on the basis of birth, profession, wealth, number of male children, and eloquence in the form of oration or poetry, etc. The residents of Makkah were businessmen who used to travel in caravan with goods for trading. They considered themselves to be higher in status as compared to those residing in Madinah who were farmers. Hence in the Battle of Badr when three warriors of Makkan origin came forward and challenged the Muslims and three warriors of Madinan origin responded and went ahead, the Makkans protested that

they wanted warriors of their status that meant honourable persons of Makkan origin. The Prophet withdrew those Madinan warriors and provided the match the enemies wanted. This false pride was so much deep rooted that Abu Jahl, who was injured by two youngsters from Madina and finally killed by Abdullah Ibn Masood, a poor man whose occupation while he was in Makkah was to graze the cattle of rich persons for his livelihood, expressed his dismay while dying that he was not killed by a person of his match!

Islam propagated the concept that dignity is a function of morality and religiosity; the more pious, virtuous and God-fearing a person is the more valuable he will be in Islam. Hence, worth of a person will not be judged on the basis of his vocation or occupation.

The Prophet used to do work like repairing his own dress and footwear, feeding camels and horses and milking goats himself. He was very particular about sharing the burden of other persons and participating in all work on equal basis. Once, when he was travelling with his colleagues, they stayed at a place and distributed work like cooking, feeding the animals, erecting tents, among themselves, the Prophet said he would do the work of collecting wood for the fuel. The companions insisted otherwise but he did not like any preferential treatment. He emphasised that when everyone else was working and doing some service, why he shouldn't.

When the Prophet came to Madinah, two mosques were constructed: one in Qiba at the outskirts where he had stayed for some days and the other at the place where he finally settled down. Further, a trench was dug along three sides of Madinah to safeguard the city when Makkan enemies attacked Madinah. The Prophet also worked as a manual labour along with his companions.

We come to know from traditions that Abdullah ibn Rawaha, a companion – may God be pleased with him – was singing in a loud voice while working and the Prophet was echoing in chorus along with others. The Prophet used to carry heavy stone that caused him to bow under its weight. The companions would come and request to give them the load; he would concede, give that away and then pick another stone of more or less the same weight!

In addition to leaving his example of dignity of labour, the Prophet's traditions have a number of teachings supporting this.

He said the best food of a person is the one earned by one's own hands and Prophet Daud used to do manual labour for his food. [*Bukhari*].

The hands of one of the companions had blackened because of hard manual labour. The Prophet kissed that black spot. This was a mark of recognition of the hard toil of that companion to be highly dignified!

Once, when a poor companion approached for help, the Prophet asked him to bring his belongings, got them auctioned and got an axe purchased from the proceeds. The Prophet himself prepared its wooden handle and gave it to him with the direction to cut woods for sale. After a couple of days that companion reported his better financial position and some small saving as well. The Prophet was happy and expressed that earning livelihood through one's own labour is much better than seeking help from others.

Such teachings, coupled with the practices of the exalted Prophet and his companions exemplifies the dignity of labour. Dignity of mankind is based on high moral principles.

CHAPTER - II
ECONOMY IN EARLY ISLAMIC
PERIOD

ECONOMY IN EARLY ISLAMIC PERIOD

In a bid to assess Islamically permitted economic activity, it is useful to study the sources of income and nature of expenses that were existing during the early Islamic period, particularly those in the days of the Prophet (may Allah bless and greet him). This search of the tradition of the Prophet in addition to the injunctions of the Qur'ān brings to us the concept of the 'tradition' in Islam itself.

MEANING OF TRADITION OF PROPHET

The concept of tradition of the Prophet is a summation of two words '*Hadith*' and '*Sunnah*.' *Hadith* literally means saying and *Sunnah* relates to deed and practice. Exact demarcation between what the Prophet said and what he did is not always possible because in a number of cases his exalted companions reported simultaneously both his words and actions. For example, it is reported that when the Prophet visited an ailing person, he placed his right hand over the region of pain and discomfort and said a particular prayer. (The wordings of the specific prayer were reported thereafter.) Here we find both the action and wordings of the Prophet. That is why the words *Hadith* and *Sunnah* have become synonymous and the term tradition encompasses both.

In addition to the sayings and deeds of the Prophet, another source of tradition is a practice during the days

of the Prophet which he did not disallow, dismiss or forbid. In other words, the silence of the Prophet is considered to be his approval. Obviously, he would not have let any incorrect practice continue! Such a silent approval is technically called *taqireer* (maintaining as it were).

We may study the economic activities during the days of the Prophet in the light of the traditions, referred to as described above.

SOURCES OF INCOME

The known sources of permitted income were Inheritance, Trade, Agriculture, Vocation, Engagement on Remuneration Basis, and Travel/Route guidance. This is not any exhaustive list of income generating events or activities. The sources of income of the *baitulma'al* (state exchequer) after formation of the Islamic State in Madinah have not been mentioned in order to maintain the brevity of the discussion.

Inheritance of wealth was prevalent in Arabs before the advent of Islam. Custom, specific to different clans, was the guiding principle. Often the mightier son, mostly the eldest, inherited most of the things per force. There were instances where the son took his step mother or mothers as wife/wives, as wives of the deceased persons were also considered to be 'properties' left behind that could be grabbed. Islam regulated the practice and laid down detailed laws in this regard through the Qur'ānic injunctions and the traditions of the Prophet.

People living in Makkah were mostly traders and businessmen. Their leaders had established good relations with the governments of neighbouring countries that enabled their trading caravans to visit those places for purchase and sale of commodities. This was a lucrative business. Further, the inhabitants of

Makkah were revered by the Arabs because they had very special regards for the city, which was their pilgrimage place. As a result of their respect for their place of worship and pilgrimage, the Arabs would not harm the caravan from Makkah and demand any duty or service charge for ensuring their safe passage. This was an unusual advantage for the trading caravans emanating from Makkah. By and large the inhabitants of the place were benefited by such trades and the Makkans were an affluent class.

In contrast to the Makkans, the inhabitants of Madinah were mostly engaged in agriculture. The Makkans regarded these 'farmers' as inferior. In other words, trade was considered superior to agriculture.

One cannot say that everyone from Makkah was a businessman or everyone from Madinah was a farmer. In spite of dominant economic activity at any place, we find many other activities. No economy in the world can be homogenous in this sense as both the rich and the poor exist everywhere. Able, less able, and differently able persons have all been present in every time and in all times. We find existence of other professionals like barber, goldsmith, blacksmith, physician, butcher, carpenter, weaver, mason, and etcetera. We also find that the 'grand old industry' of prostitution existed and served as 'decent' income to many 'noble' persons.

Prostitution in Arabia existed in two forms: Domestic prostitution and open prostitution in the brothel. Domestic prostitution was carried out by freed slave girls who had no guardians, or by free women who had no family or tribal support. They would take residence in a house and enter into an agreement with a number of men simultaneously for financial help in return for sexual gratification. Whenever a child was born, the mother would name whomsoever she liked as its father and the

man was accepted in society as the father of the child. Open prostitution which was carried out entirely through slave girls was of two kinds. First, the slave girls were obliged to pay a fixed heavy amount every month to the owner, which they could only earn through prostitution. The owner knew well how the money was earned. Secondly, beautiful and young slave girls were made to stay in the brothel and a flag was put at the door to indicate that a needy person could satisfy his lust there. Several prominent men of the day owned and maintained such houses of prostitution. Abdullah bin Ubayy, the chief of the hypocrites of Madinah, who had been nominated as king of Madinah before the Prophet's (Peace and blessings of Allah be to him) arrival there) himself owned a regular house of prostitution in Madinah, which had six beautiful slave girls. Not only did he earn money through them but also used them to entertain his respectable and important guests who came to see him from different parts of Arabia. He employed the illegitimate children thus born to enhance the splendor and strength of his army of slaves. When one of these prostitutes, named Muazah, accepted Islam and wanted to offer repentance for her past sins, Ibn Ubayy subjected her to torture. She complained of it to Abu Bakr, who brought it to the notice of the Prophet (peace be upon him). The Prophet (peace be upon him) ordered that the woman be taken away from the cruel man. (Ibn Jarir, Vol. XVIII, pp. 55 -58, and 103-104; Al Istiab Vol 11, p. 762; p. 762; Ibn Kathir, Vol. III, pp. 288-289)." [Towards Understanding The Qur'an, by Syed Abul Ala Maudoodi, Al-Noor 24:33, Foot Note number 59, Published by Markazi Maktaba Islami Publishers, Delhi].

Ibn Kathir in his commentary on the verse 24:33 of the Qur'an has further reported that the verse was revealed about two men who used to force two slave-

girls of theirs into prostitution. One of them was called Musaykah the and Umaymah the mother of Musaykah belonged to `Abdullah bin Ubayy. Mu`adhah and Arwa were in the same situation. Then Musaykah and her mother came to the Prophet and complain him about that.

Islam forbade prostitution and all other ill practices and corrected abhorrent and morally incorrect activities like interest and gambling prevalent in different trades and vocations and ushered in a clean and healthy atmosphere for economic activities. However, the Prophet did not touch or comment on the trade practices that were in order. His silence on something that was happening in his days is an act of approval from him, as discussed above.

We find many persons during those days doing services including manual labour for other persons on fixed remuneration basis. One such popular engagement in Makkah was grazing livestock on payment basis. The Prophet himself used to do this. History records the name of Abdullah Ibn Masood (may Allah be pleased with him), a prominent companion who was a poor person and an outsider for Makkah, doing this service.

An interesting profession was that of travel guidance. The landscape of Arabia was filled with high mountains, long mountain ranges and large deserts which were treacherous for new comers in any particular areas and it was not possible to tread the route without local assistance. Tribes living alongside trade routes charged fees from caravans passing through their areas; the fees covered charges for safe passage as well as and guidance from one point to another. It is noteworthy that Abdullah-bin-Urayqit, who was a travel guide to the Prophet during the latter's migration from Makkah to Madinah, had not embraced Islam while doing this

assigned task! Nor did he disclose any secrecy of the migration. It was a pure case of abiding by professional ethics in return to a fixed remuneration!

Here is not intended to enlist all the income generating activities during the time of early Islam. This is just to mention some prominent economic activities that generated income prevalent in the early Islamic period.

NATURE OF EXPENSES

Major guiding principles for expenses may be described as under:

1. Utilisation for self consumption;
2. Utilisation for the needs of parents, children and other relatives;
3. In the path of Allah (*Fi Sabilillah*); and
4. Other religious and social obligations.

It is advisable that if a person has good earning, he should eat and feed himself properly along with taking care of spouses, children, and parents. A person, who was not clothed properly, came to the Prophet. The Prophet told him to clothe properly because that person had income for the purpose. Another tradition of the Prophet is more specific on the matter. Anas ibn Malik (may Allah be pleased with him) reported that Prophet Muhammad (may Allah bless and greet him) said: One who strives hard to earn so as to feed his aged parents is striving in the path of Allah; one who strives hard to earn so as to take care of his children is striving in the path of Allah; and one who is striving for his own needs so that he may not have to beg to others is also striving in the path of Allah. [*Agreed Upon*]

However, two guiding principles provided by Prophet Muhammad (may Allah bless and greet him)

decide whether or not expenditure is correct. The principles are to avoid extravagance and misery.

Extravagance implies three aspects, and all these are forbidden. First is the expenditure in unlawful things. Second is the expenditure in lawful things more than what is required. And the third is the expenditure with the intent to show off riches and impress upon others. Thus the income available should be utilised for lawful purposes within the limits of available facilities without any iota of insincerity. All actions done, including utilisation of income, are required to be with total sincerity towards Allah the Almighty and any impurity of intention is disastrous.

Misery implies two aspects and both are undesirable. One is to withhold expenses on the justified self needs and on family members. Another is to withhold expenses on other rightful things. Every person depending upon his level of income is required to utilise the same for his own needs and comforts and take care of the needs and comfort of his spouse, children, parents and relatives. Further, a good person should take care of his neighbours and contribute to society at large and respond positively to other societal needs and calls of his faith.

ECONOMY OF THE PROPHET AND HIS HOUSEHOLD

The economy of Prophet Muhammad (may Allah bless and greet him) and his household may be studied in two distinct periods: one before the declaration of his prophet-hood at the age of 40 and the other thereafter. Further, in the period after the declaration of his prophet-hood, we may differentiate between his stay of about 13 years in Makkah and the rest 10 years in Madinah in

view of the vastly different conditions between these two periods.

ECONOMY PRIOR TO PROPHET-HOOD

Prophet Muhammad (may Allah bless and greet him) was born as an orphan as his father Abdullah died before his birth. His grandfather Abdul Muttalib was the most prominent leader of the tribes in Makkah. His mother, Amina, died when he was six years old and his grandfather died when he was only eight. His uncle Abu Talib, who was a poor person, became his guardian. As a result of the not so good economic condition of his uncle, the guardian, the Prophet shared the finance of the household by doing the job of grazing cattle on remuneration basis. Besides, this was a usual engagement for young men in Makkah those days. The Prophet further participated in the trading activities of his uncle. He also inherited a small amount of property from his father.

When the Prophet was 25 years old, a rich business lady named Khadeeja offered him to take her business consignments to Syria and do the trading on profit sharing basis. Khadeeja used to send her commodities for trading with different persons and when she heard about the good persona of Muhammad (may Allah bless and greet him) she made this offer that was accepted. The venture was successful and both the partners earned good and neat profit.

Muhammad (may Allah bless and greet him) later married Khadeejah (may Allah be pleased with her) and thereafter her business interest was supervised by him. This continued till he was declared Prophet by Allah the Almighty, and he had no spare time to pursue his trading and other business activities and all that was available with this reverent family was used up in their

mission to propagate Islam. The condition continued till migration to Madinah in the 13th year of prophet-hood. Khadeejah meanwhile had died.

Some of the Prophet's companions in Makkah were rich persons while most of them poor. These rich companions, including Abu Bakr (may Allah be pleased with him), helped the poor companions in many ways, and traditions describe such instances. However, no popular tradition is recorded about any financial assistance provided for the household of the Prophet in the Makkan period. On the contrary, it is reported that the camel that Abu Bakr had arranged for the migration, the one that the Prophet used, was purchased by him on credit from Abu Bakr with insistence.

PROPHET IN MADINAH

Before we dwell upon the sources of income of the Prophet's household and the manner it was utilised, it is better to discuss the relationship between him and Banu Najjar tribe of Madinah so that an element of familial and personal touch between him and the men who mainly took care of him and his household in Madinah may be understood. There is no doubt that all the followers of the Prophet in Madinah did their best to provide as much provisions as they could do, the personal element of this particular tribe may be taken as an additional factor. Perhaps this was the reason that the Prophet – under divine guidance, of course – stayed in their area. It was not a case of a guest coming to a host. Rather it was the case of a family person settling down among his people.

The great grandmother of Muhammad (may Allah bless and greet him) belonged to Banu Najjar tribe of Madinah. Hashim, his great grandfather, while going to Yemen on a business tour stayed in Madinah and married Salma bint Amr and proceeded, after staying for

a few days after his marriage, to his destination and died en route in the Gaza town of Palestine! Abdul Muttalib, the grandfather of the Prophet, was born of this marriage. The relationship between Banu Najjar tribe and the family of the Prophet was always maintained. The Prophet during his childhood had also visited Madinah along with his mother and stayed with his people there. He had once described the place where he had played with other children of his age.

The financial responsibility that the Prophet took was maintenance of, besides his family members, the poor companions known as *Ashaab-e-Suffa*, who had migrated from Makkah and other places to devote their full time to learning the religion. They were in the nature of more or less permanent guests who stayed on a raised platform in the mosque. They had no source of income of their own and all their needs were fulfilled by the Prophet. Further, there were inflows of guests who came to learn about Islam, stayed for a few days, and went back to different places. The inflows of such guests increased with the passage of time and at one stage there were hoards of them. The Prophet took care of these individuals and groups severally in person.

In the initial days of this period, the Ansars (the hosts in Madinah) marked at least one date tree respectively in their orchards for the Prophet's family and their produce was sent accordingly. Asad ibn Zurarah used to send one big cup full of cooked food daily to the Prophet's household. The practice was adopted by another companion Saad ibn Ubada (may Allah be pleased with these pious persons).

The Prophet purchased some camels, goats and sheep for milk and also received some cattle as gifts. These milk-giving cattle were kept on specified grazing grounds and the milk therefrom was received daily for

the family members of the Prophet. He had earmarked specific camels for his different wives, *ummulmomineen* (mothers of Muslims).

In the matter of receiving gifts, the Prophet did not accept for his personal or familial use things provided as religious obligations of the provider like *zakat* and *sadquat*. Such things were distributed between poor and other needy persons. Other gifts were accepted and utilised. However, he was particular to give back gifts and reciprocate the kindness.

One Jew named Mukhairiq participated in the Battle of Uhud with Muslims, and was killed. It is not confirmed whether or not he had reverted to Islam. However, he had given seven orchards to the Prophet in his will. The produce of these orchards eased out the financial condition of the Prophet's household.

Some of the wives of the Prophet – mothers of Muslims – belonged to well to do families and they inherited properties from their fathers and ex-husbands. For example, Umme Salma (may Allah be pleased with her) owned gardens in Taif and income therefrom was received in Madinah.

The Qur'ān has specified that the Prophet would get one fifth of *ghaneemat* (war booties). These war booties comprised both movable and immovable properties. Food items left by the fleeing enemy were not distributed as such and the same were taken and consumed by whoever wanted. Other items were properly valued and shared according to a fixed ratio. The Prophet used to divide that one fifth of the *ghaneemat* received equally, keeping one share for his household and for his family, giving another share to his relatives and the balance was distributed among the poor.

It is another story that the food and other items coming at the Prophet's household were also used for

filling the belies of the above mentioned permanent sort of guests, the *Ashaab-e-Suffa* and other occasional guests and poor persons, leaving the residual for the household which were nought at times!

The stories that we hear about the poverty of the Prophet's household are true. But the reason behind that stretched conditions was not that the household had not sufficient source of income. The actual reason was the generosity of the Prophet and his wives, mothers of Muslims. They distributed more than what they received! At times, the Prophet took loans from others and served the needy.

Thus we find that the source of income of the Prophet's household was varied including inheritance, business income, gifts, , share of war booties, income from properties held both movable like milk bearing cattle and immovable like date-orchids, etcetera. The utilisation of these incomes was done for self consumption, familial purposes, societal obligations, charity, and etcetera. Hence all these activities are desirable and have divine sanction!

CHAPTER - III
ISLAMIC TEACHINGS AND
ECONOMICS

ISLAMIC TEACHINGS AND ECONOMICS

Islam has not provided any detailed set of rules that can be clubbed as Islamic Economics and applied for all human beings of all times and all places. In that sense no Islamic Economics as such exists! This is true about almost all other branches of Islamic studies; be they Islamic Politics or Islamic Science or Islamic Social System. The sole exception where Islam has not left any scope for innovation and experimentation is faith which has been fully described in all possible details, and it remains relevant for every human being or society of past, present and future, and of all places.

Islam has provided basic principles relevant to specific branches and identified a list of things that have to be avoided, say a negative list. Equipped with the all embracing and fully described faith and relevant principles and the negative list, man has been left free to experiment and arrive at most suitable methods of doing things, that may be called systems, suitable to his time and place.

In other words, Islam has total faith in a willing and positive person and his society that they will devise the best methods, keeping in minds the principles and negative list provided by Islam. The system so prepared and applied by men of a particular time may only be specific to them for their time and place. It may not be advisable for all times and for all places at the same period of time. This may be understood as a

phenomenon of faith on human intellect and scope for its continuous application.

So, when we talk about Islamic Economics, we refer to the teachings of Islam relevant to Economy of man. Our endeavour is not to delineate any new branch of economics christened as Islamic Economics, as no such thing is in existence and there is no need to invent one such exclusive subject. The correct approach is to study the system in vogue at a particular place and time and apply the litmus test of relevant Islamic principles including the negative list, referred to above. The aberrations, if any, have to be corrected and things have to be set right accordingly.

There are many aberrations and humanity is suffering a lot because many things in the economic life of man in our times are not moving in the right direction. The human economic train has derailed and there is need to look afresh on many things which are considered essential facts of life that are in fact wrong facets.

Islam desists from reinventing the wheel. There is no need to erase everything from the board and then write, or rewrite, afresh. The Islamic approach is that everything that is in existence is basically correct provided that does not trespass any Islamic principles and fall within the Islamic negative list relevant to the subject. The approach is not to assess whether or not something is Islamically correct. The test is that it should not be Islamically incorrect. If it is not infringing upon any Islamic principle and is not falling in the negative area, it is in order. Islam has not listed all correct things. It has not provided a plethora of principles or a long list of forbidden and undesirable things. The beauty of this litmus test of verifying only the undesirability with reference to a very small list of don'ts is that the vast

majority of human developments gets the green signal, leaving a minuscule to be corrected.

Hence the starting point of reviewing the economic system from Islamic point of view will be the economic theory practised today. The next step will be to see what has gone wrong from the viewpoint of Islam. Finally we shall come to the point of studying the required corrective and adaptive methods.

ECONOMICS AS ON TODAY

Modern economics is based on the concept that man needs resources to satisfy his urge for maximising utility. Every person and group of persons like a society, a corporate entity, a nation, a country or a region is struggling to get as much resources as possible so that his/their desire of optimum utility may be fulfilled. In this struggle for acquiring the maximum unit of resources, those who are more efficient get more and such distribution of goods and services is justifiable. The points of contention for the individuals and group of individuals are resources in the form of factors of production that can be produced in the form of goods and services that are distributed according to the contributions severally made by those factors. The problem that an economy encounters is that such resources are scarce and these have alternative uses too.

SCARCITY

Scarcity of resources is the basic problem of economics. Unlimited human needs and wants are to be satisfied with the limited resources. This concept has emanated from the famous article of Lionel Robbins published in 1932 that has defined economics as the

study of “relationship between ends and scarce means which have alternative uses.”

A fallacy in the above mentioned definition is that it ignores human resources that cannot be said to be scarce at most of the places of the earth. A human being is considered merely to be the user, the consumer, of goods and services produced, ignoring, perhaps, his role in producing them.

An individual or a group of individuals desires to get more and more goods and services. In the parlance of economics it will be described as the human behaviour of maximising utility. In other words, consumption of goods and services satisfies the need of increasing one's utility. This would mean that economic planning of any society should aim at maximisation of utility in that economy. There is a tag of morality attached to this holy idea of ever increasing possession of goods and services by an individual or a group of individuals. This is the doctrine of utilitarianism.

The reason behind the scarcity of resources has also been discussed in the literature of economics. David Ricardo, in 1817, described this as the result of “niggardliness of nature.” Ricardo discussed this idea with reference to agriculture. It means that nature is tight-fisted and is not generous towards human beings. Had it provided more, there would not have been any scarcity and there would have been no need to study a subject like economics! As there is paucity of resources, so there is the need to study how to utilise the scarce commodities in the best possible manner.

EFFICIENCY

Competition for better share of resources leads to ensure that the economy that is successful in allocating more efficiently its scarce resources will be relatively in a

better position. Within an economy it is also true about individuals. One who is more efficient will get more, and the one who is relatively less efficient will suffer. This concept provides a justification for higher and lower allocation of resources.

But things do not move in a simple linear equation. Other factors are bound to affect. One such problem is that individuals function in different situations. The same person who is a consumer for one item seeking maximum utility may be a producer of another commodity seeking maximum profitability. They may have conflicting interests. Private interest may be quite different, if not at loggerheads, from group interest, and so on.

Classical economists have tried to resolve such problems with a number of concepts like Say's law, perfect competition and rational economic man. Say's law highlights that supplies create their own demand and so a perfect symmetry exists between private and public interests. Perfect competition implies a market without any outside interference, wrong practices and corruption where the consumer is a rational person with full knowledge about the market. In this ideal situation, the hidden hands of market will do the corrective action. Such interplay of the hidden hands of market forces is known as 'Invisible Filter Mechanism.'

In real life situation ideal conditions do not exist. Mere invisible filter mechanisms do not succeed in bringing in the much desired equilibrium in economy. Recourse to Visible Filter Mechanisms like central planning, fiscal and monetary methods, particularly taxation, become necessary for smooth functioning of market and economy.

ECONOMIC ACTIVITY

An economy grows in the cradle of a properly structured economic activity. An economic activity comprises four things: (i) Production; (ii) Exchange; (iii) Distribution; and (iv) Consumption.

Goods and services produced have to be traded on some medium of exchange. Production is the beginning of economic activity. The item produced can be supplied only if it has a demand. Supply and demand are based on their trading. In olden days the basis of trading was commodity against commodity, that is, the barter system. Precious metals took their place. Now we have paper or plastic currencies in different countries that serve as the medium of exchange. Goods and services so demanded have to be made available to the consumer through distribution for consumption. The consumption creates new demand for which fresh economic activity beginning with production commences. This goes on and on.

As the purpose of our discussion of these concepts is to shed light from the Islamic point of view, we need not go into greater details. We shall keep our attention focussed only on certain aspects of economic activity.

CONTEMPORARY ECONOMICS AND ISLAMIC ECONOMICS

The classification of economic activities into the four areas namely production, exchange, distribution and consumption has been done in a broad manner in order to keep the scope of discussion from going array, otherwise there is much scope of further sub-classifications and refinements. We shall proceed by discussing these four activities in brief.

FACTORS OF PRODUCTION

Production refers to a process by which value is added to a certain input. A set of inputs is put in the production process that results in an output or a set of outputs. The output is a commodity meant for consumption. The set of inputs for production is called factors of production in economics. These are facilitators for production apart and distinct from the basic inputs in the form of raw material.

Economists talk about four factors of production namely Land, Labour, Capital and Entrepreneurship. Other refinements in the discussion like addition of technology as a factor of production is possible. However, the purpose for which we are discussing these concepts can be served by keeping our arguments limited to the four factors.

Land refers to the natural resources that are available on our planet earth. Apart from land itself, this includes minerals, water, air, vegetations, etc. We may include wildlife and ecosystem in this concept. These are gifts of nature to man.

Labour refers to human resources. It encompasses both physical labour and mental work. So it covers manual labour as well as white-collar and blue-collar jobs.

Capital basically refers to capital goods. As against the gifts of nature covered under the concept of land, above, capital goods means manmade resources that are used to produce goods. These are themselves manufactured goods of relatively more durable nature. So these are goods used for production of other goods and as against raw material they are themselves not consumed in the production process. They remain more or less intact. Examples are machines, tools, trucks, buildings, vehicles, etc. Although capital in the form of

cash is not included in this list, it is understood that these items are provided by the entrepreneur or are purchased out of cash capital brought in or from loans arranged for the enterprise. So for all practical purposes this factor of production is simply cash capital converted into capital goods.

Entrepreneurship refers to the ability of persons who take risk of commencing the production activity. Production activity is not possible without someone daring to organise all the above mentioned factors and start the enterprise on the expectation that the venture will be profitable. Success of the enterprise cannot be ensured cent per cent. There is no method to guarantee it. Things may not move in the projected direction and failure may be faced. The entrepreneur takes the risks and goes ahead with the production process.

The contemporary economics talks about payments to these factors of production. The resources generated through the production process are distributed to the four factors as under:

- (i) Rent paid for land; (ii) Wages paid for labour; (iii) Interest paid for capital; and
- (iv) Profit paid for entrepreneurship

RELEVANT ISLAMIC PRINCIPLES

Islamic principles are basically extensions, applications and offshoots of the Islamic faith of unity of God. As God is one and no one is partner to Him, there is unity of human beings too. All men are created by the same one God and no one is inherently superior to any other person on account of colour of skin or hair, language spoken, place of birth, caste or creed, etc. So there is no scope or justification of discriminations between human beings on account of birth. As a creature everyone has same status.

Man is vicegerent of God on earth and he is not the primary owner of any resource. Man and his possessions are owned by God and whatever has been especially provided to any person has to be utilised in accordance with the will of the Almighty God. Thus man is accountable for the resources made available to him.

SCARCITY OF RESOURCES

The concept popular with the contemporary economists that resources are basically scarce is not true in the sense that God has created man on earth and provided optimum resources. The idea of niggardliness of nature as said by Ricardo is obnoxious. Nature has provided all that is needed. Now if any paucity is felt, it is because of the faults of man like greed, inefficiency, atrocity on fellow human beings, etc.

Prophet Muhammad (may Allah bless and greet him) said that man will not be ever satisfied. If he gets one valley of gold, he would desire another one. The earth can satisfy the needs of all persons, but not the greed of even one person.

Another aspect relating to this greed is that man on every part of the earth is vying for ever increasing standard of living and is utilising the resources in complete disregard to environmental risks, making the life on earth difficult. God has not made the earth a place where the so-called standard of living of everyone will be better every other day from what it was the previous day. What is happening naturally is that those in possession of resources, right or wrong, are able to increase it, by good or bad means, and those who were left behind are getting backlash continuously. The gap between the haves and the have-nots is increasing day by day.

There is a question mark on total justification of distribution of resources based on competition and efficiency, as understood in contemporary economics. Such distribution will not always entail justice and wellbeing of human beings. In fact, allocation of resources on the basis of mere efficiency leads to many kinds of injustices. There are many persons and societies who are inherently less-able or differently-able. They will not get any share in the economy or they will get less than what is needed for their survival and natural growth. These are not mere conjectures. Rather things are happening this way around the world in almost all societies.

Allocation of resources should be a function of human wellbeing. This does not mean that the role of competition based on efficiency has to be negated altogether. Rather, there is the need to inject human element in allocation of resources. Justice alone would not suffice. Equity is required along with justice so that no person or society is denied the basic needs for survival and growth on humane basis.

FILTER MECHANISM

From Islamic point of view there is no problem in the concept of visible and invisible filter mechanism. It is true that invisible market forces play their role in bringing some element of equilibrium in economy. It is also accepted that this invisible hand of market is not sufficient and the state is compelled to use the visible hands of law in the form of planning, trade laws, taxation and the like. Islam would add the third factor of Moral Filter. A set of moral laws of Islam specifically pertains to economics and commerce while overall Islam's approach towards morality is that it is binding on all walks of life, be they relate to spiritual life of man or his material and

worldly life. Morality in Islam is a permanent value, with divine sanction, de-linked from time and place. So no one is allowed to discount this filter at any part of the earth and in any era.

FACTORS OF PRODUCTION & THEIR DISTRIBUTION

Islam has a basic problem with the concept of distribution of factors of production whereby interest is considered to be a payment of capital. Islam's approach towards interest is uncompromising. Interest is forbidden without any qualification. This inhibition and unqualified prohibition is deep-rooted and it merits a full-fledged discussion (that we intend to do at a later stage).

The factors of production and their respective distribution from Islamic point of view are suggested hereunder.

(i) Rent is payable on the utilisation of land and non-cash capital goods; (ii) Wages is payable for labour; and (iii) Profit is payable for entrepreneurship along with cash capital brought in by the entrepreneur. However, profit margin may be higher on account of bringing in cash capital. For example, if a production unit is owned by more than one entrepreneur, the share of profit of those of them who have brought in cash capital may be more than that of the partner who has not put in cash in the business. In any case there is no justification for interest.

PRINCIPLES OF ISLAMIC ECONOMICS

As against the four types of remunerations/rewards to factors of production recognised in contemporary economics namely, wages, rent, interest and profit, Islam recognises three, that is, wages, rent and profit. Interest

remains the taboo. In fact, the Arabic word for wages (*ujrat*) comes from the same root as rent (*ajr*). If this logic is accepted, the rewards of factors of production in Islam fall into two distinct categories, namely *ajr* and profit.

Wages is the payment against utilisation of the services of human beings for any specific period. Rent is similarly the payment for utilising natural resources like land, minerals, vegetations, etc. for any specific period. The shape or form of both these human and natural resources does not change. It remains intact. Thus the reward is only for employment or deployment of these resources which are themselves not consumed. In other words, justification for both wages and rent emanates from usufruct rights. Alternatively, it may be understood as the opportunity cost of using these human and natural resources. For example, take the case of a taxi hired for a specific period, say eight hours, along with a driver and payments are made severally for both the hire charge of taxi and fruits of labour to the taxi driver. Both the taxi and the taxi driver get payments for their respective usufruct. In other words, these payments are in the nature of opportunity cost. The taxi and its driver were available to a particular user thereby losing the opportunity of being utilised for some other purpose, or may be by some other client. However, both the taxi and the taxi driver remain intact and in the form in which they were before their engagements.

Profit is the reward for the risk that an entrepreneur takes. His stakes, like his cash capital, capital goods, time, and goodwill, are high; all may be lost if the projections based on which he commenced the enterprise do not hold good. There is no method by which the success of any enterprise may be ensured and the uncertainty and risk involved can be avoided.

INTEREST IS UNJUSTIFIED

Capital brought in as cash does not remain intact. It changes form as it is utilised for purchasing trading goods, acquiring capital goods or meeting other expenses or investments, including payments against services. The goods and services so produced are traded, that is exchanged and distributed, in accordance with the consumption requirements of market and then any real income is generated. Profit can be computed thereafter. The real income and consequently the actual margin of profit are not known beforehand. The capital provider is justified to get any remuneration or reward only after profit is earned. The remuneration or reward that he will get will be out of the profit added to the enterprise as a result of the completion of any cycle or period of production process. And the reward will be in direct proportion to the profit.

MONEY CAPITAL AND CAPITAL GOODS

The distinction between money capital and capital goods should be understood. One may understand it by differentiating between an enterprise and the entrepreneur. A business is a separate entity from that of the business man, both being legal persona severally. This is the position from the accounting angle too as we compute accounts of business separate from that of the businessman, the owner. Thus cash capital provided by the capital provider is a liability on the business. The profit earned too is a liability because that portion is payable to the entrepreneur by the business. Loss, by this reasoning, becomes an "asset" to the business because amount due to the owner of the business is reduced by the amount!

An entrepreneur may provide his resources for the enterprise in any one of the following methods:

1. In the form of cash as capital
2. In the form of immovable properties like land, office building and capital goods like machines by transferring their ownership to the enterprise. Here valuations of these assets have to be done and it will be accounted for as if these have been sold to the business and the consideration is added to the capital account.
3. In the form of immovable properties like land, office building and capital goods like machines on hire basis. Here no valuations of these items are required and these assets are not recognised as such in the books of the business.

The remuneration/reward payable to the entrepreneur will be as under in the case of the above mentioned three conditions.

4. The entrepreneur is entitled to get profit for the cash capital.
5. The total value of assets adding to the assets of the enterprise will be added to the capital. It will be treated as if the entrepreneur has provided cash capital and these items were purchased out of that cash made available to the enterprise. The annual wear and tear in the value of these assets may be charged to the business as depreciation, thereby decreasing distributable profit. Alternatively, the depreciated value may be accumulated as a reserve so that the enterprise may have resources at the time when these are to be replaced.
6. The entrepreneur will get rent on the land and capital goods provided on hire basis because he has kept their ownership with him. The enterprise will pay the rental for the usufruct rights utilised for these items.

DISTRIBUTION OF PROFIT AND LOSS

The Islamic principle of distribution of profit and loss where there is more than one entrepreneur has some characteristic features. Its salient features are as under:

1. Profit will be distributed on predetermined and agreed ratio. While determining this ratio of distribution of profit, the entrepreneurs may give relative weightage to factors like cash to be brought in, experience and time to be given and activity (like full time, part time or active or passive partners). For example, agreed profit ratio between an active partner and a dormant partner may be equal where the active one is not providing any cash capital and the dormant is providing the cash. Here equal weightage is given to the activity of one partner and the fund of the other.
2. Full time and active entrepreneurs may be remunerated in addition to their share of profit. However, his remuneration will be subject to profit earned. Hence this remuneration of the entrepreneur cannot be added to the loss of the enterprise.
3. Loss will be borne by the entrepreneurs on the ratio of their respective capital. Thus a partner, who has no capital in the business, will not share any loss. Hence the predetermined ratio between the partners will only be a profit sharing ratio and not a profit-and-loss sharing ratio.

In contemporary economics both systems of loss sharing between partners are prevalent. Loss is shared either on the basis of predetermined profit-and-loss ratio or on capital ratio. The latter, known as Garner vs. Murray System because this was decided in England in this particular case, is consistent with the Islamic system.

AN OVERVIEW

Economic activity for a man is basically related to his following needs, desire and propensity:

Earning;

Capital Formation;

Expending;

Saving;

Investment; and

Leaving behind Wealth for his Offspring and Inheritors.

Islam, being proactive to economic activities, encourages, with some regulations, all these aspects. Basically, there is no element of undesirability in any of the above propensities. Rather they are desirable and encouraged provided they are duly regulated. The approach of the Islamic regulations is not to discourage and make these activities difficult, dull or tasteless. Islamic regulations are meant to cleanse economic activities from all harmful and unsavoury elements, both individually and collectively. Such regulated activities bring real human welfare and these worldly affairs rise to the level of moral and ethical frame. In fact, the line of demarcation between religious and secular domains becomes so much thin that, at times, they may not be seen or noted.

Man's need and yearning for earning and his attitude to go on increasing, as far as possible, his income and to go for capital formation and asset built-up is regulated to the extent that he is asked to desist from some illegal and amoral modes of earnings.

Level and mode of expenditure is related to the level of earning. Higher earning gives higher opportunity of expenditure. Thus, type, mode and extent of earning of different persons in the society are different. Islam recognises this position. However, Islam has a list of

forbidden consumptions. Keeping at bay the expenditure that are not permitted, man can utilise his earnings for the welfare of his self, offspring, and others or for other things dear to him. There is no objection to the permitted expenses, although these, on the face of it, look like temporal and mundane. The litmus test is that earnings from permitted sources are to be utilised for all permitted things only. And it may be noted, as already described elsewhere, that the Islamic approach of permissibility is that all that are not-forbidden are permitted. One may say, it is a negative test that holds good!

Man can save what he has earned. He is required to give a share of his savings as *zakat* or *ushr* so that the needs of the poor and the needy in society are taken care of. He is encouraged to share more than what is obligatory. However, the earning available after the obligatory payment of *zakat* and *ushr* or optional *sadaqua* is clean and no aspersion is to be cast on it.

A person desires to invest his savings and plough back his earnings so that he can earn more. Such urge for higher earning is encouraged. This leads to entrepreneurship and growth in economy. One is free to decide the way he wants to utilise his savings. He may or may not go for investment. This depends upon his personal disposition, preference, ability and opportunity. Islamic regulation is concerned about the desirability or otherwise of the area of investment so that no unwanted activity ushers in the economy with such application of fund. There is no problem that a rich person becomes richer by investment, rather it is desirable that earning in society and the economic activities grow as a result of this.

Life span of every person is limited. Even the richest person cannot live for ever and one day destiny makes him leave behind whatever he earned or built up. People

leave behind wealth for the wellbeing of their offspring and inheritors. Islam has provided a detailed law of inheritance, thereby curtailing the authority of a person to decide what will be done with the wealth he will leave behind. A person can decide the disposal of only one-third of his property; the rest will be distributed as per the law of inheritance enshrined by Allah. Thus assets and properties accumulated in the hands of one person get distributed to several persons. There is no concept of joint family ownership of riches once accumulated. Thus we find that although Islam lets the rich become richer, the wealth so amassed and gathered is dispersed in economy after his demise.

CHAPTER - IV
RIBA IN THE QUR'AN AND THE
PROPHETIC TRADITIONS

RIBA IN THE QUR'AN

The Arabic term for interest is *Riba* which means 'to grow, to exceed, to increase.' Technically it means 'premium' paid or payable by the borrower to the lender along with the principal amount as a condition for the loan or for the extension in its maturity. In other words, it is the extra amount, benefit or advantage received on any loan.

Riba has been discussed in the following verses of the Holy Qur'ān in chapters, al-Baqarah, Aal-e-Imran, al-Nisa and al-Rum.

"Those who swallow usury cannot rise up save as he arises whom the devil has prostrated by (his) touch. That is because they say: Trade is just like usury; whereas Allah permits trading and forbids usury. He unto whom an admonition from his Lord comes and (he) refrains (in obedience thereto), he will keep (the profits of) that which is past, and his affair (henceforth) is with Allah. As for him who returns (to usury) – Such are rightful owners of the Fire. They will abide therein.

"Allah has blighted usury and made almsgiving fruitful. Allah loves not the impious and guilty. Lo! Those who believe and do good works and establish worship and pay the poor-due their reward is with their Lord and there shall no fear come upon them neither shall they grieve. O you who believe! Observe your duty to Allah and give up what remains (due to you) from usury, if you are (in truth) believers. And if you do not then be warned of war (against you) from Allah and His messenger. And if you repent, then you have your principal (without interest). Wrong not and you shall not be wronged. And if the debtor is in straitened circumstances, then (let there be) postponement to (the time of) ease; and that you remit the

debt as almsgiving would be better for you if you did not know." (2: 275-280)

"O you who believe! Devour not usury, doubling and quadrupling (the sum lent). Observe your duty to Allah, that you may be successful." (3:130)

"Because of the wrongdoings of the Jews We forbade them good things which were (before) made lawful unto them, and because of their much hindering from Allah's way. And of their taking usury when they were forbidden it, and of their devouring people's wealth by false pretences. We have prepared for those of them who disbelieve a painful doom." (4:160-161)

"That which you give in usury in order that it may increase on (other) people's property has no increase with Allah; but that which you give in charity, seeking Allah's countenance, has increase manifold." (30:39)

INFERENCES

Dr. Mohammad Nejatullah Siddiqi has discussed at length the inferences drawn from the above verses of the Qur'ān in his book *"Riba, Bank Interest and the Rationale of Its Prohibition"* [Markazi Maktaba Islami Publishers New Delhi; P 35, 36; December 2005]. His assertion in the book may be noted:

"These verses establish a number of important points. Firstly Riba is categorically prohibited, secondly, it is stated that Riba is what is over and above the principal, and thirdly that it is unjust (zulm). It is also said that Riba is destined to destruction (mahq). And last but not the least, the worst effect of Riba mentioned in the above passage is that on human personality: Riba demeans and diminishes individuals who indulge in taking it. Significantly, the claim of equating Riba with trade is also rejected (trade being mutually beneficial whereas the benefits of Riba may well be confined to one party only)."

Finally, Dr. Siddiqi has summarised his masterly arguments under following heads:

Riba corrupts society;

Riba implies improper appropriation of other people's property;

Riba's ultimate effect is negative growth;

Riba demeans and diminishes human personality; and

Riba is unjust.

THE DEBATE

Some scholars initiated a debate whether the word *Riba* used in the Qur'ān covers interest payment by banks or not. The whole argument by such scholars is to prove that interest is not the correct translation of *Riba* as it implies only usury, i.e. high rate of interest charged by money-lenders for consumption loan. In other words, according to this line of argument, bank interest is not *Riba*, as such, as it is meant for production. Premium on production loan is not prohibited. *Riba* implies only premium on consumption loan. This distinction between consumption loan and production loan is done on the logic that persons taking loan for production purpose use that for earning profit and they should pay interest like the rent paid on land and other resources. The person who is giving loan is parting with his resource and liquidity, the cash, and so he should be rewarded positively, i.e. on fixed rate for predetermined period. Taking interest on consumption loan is not judicious so it should be discouraged, either prohibited or made soft loan where interest may be as low as possible.

TO SUM UP THE DEBATE

Maulana Syed Abu Ala Maudoodi has discussed related issues in the Foot Notes number 315-318 against verse 2:275 in *Tafheemul Qur'ān* [Towards Understanding

the Qur'ān, Volume - I; Markazi Maktaba Islami Publishers, New Delhi; P 213-16; October 2004]. A summary of the discussions therein follows:

“The proponents of this view argue that if profit on money invested in a business enterprise is permissible, why should the profit accruing on loaned money be deemed unlawful? ... Their argument runs as follows: A person who could have profitably invested his money in a commercial enterprise loans it out to somebody who, in turn, makes a profit out of it. In such circumstances why should the borrower not pay the lender a part of the profit? Such people, however, disregard the fact that no enterprise in which a man participates, whether it is commercial, industrial or agricultural, and whether one participates in it with one's organising skill or capital, or by both, is immune from risk. No enterprise carries absolutely guaranteed profit at a fixed rate. What is the justification, then, for the fact that out of all the people in the business world, the financier alone should be considered entitled to a profit at a fixed rate in all circumstances, and should be protected against all possibility of loss?....

Let us consider only the question of loans for profitable enterprises, and confine our consideration to loans made at non-exorbitant rates of interest. The question, however, remains: Which rational principle, which logic, which canon of justice and which sound economic principle can justify that those who spend their time, energy, capacity and resources, and whose effort and skill make a business thrive, are not guaranteed profit at any fixed rate, whereas those who merely lend out their funds are fully secured against all risks of loss and are guaranteed profit at a fixed rate?”

Dr. Nejatullah Siddiqi in the above referred to book has discussed this issue threadbare and proved that bank

interest too is *Riba*, the one prohibited by the Qur'ān. Another authority on Islamic economics, Dr. M. Umer Chapra has also discussed this issue and showed that *Riba* implies both interest on consumption loan and production loan [*Prohibition of Interest: Does It Make Sense?* Markazi Maktaba Islami Publishers, New Delhi; P 10-11; October 2005].

The distinction between interest and usury and between low and high rate of interest done by the supporters of bank interest on production loan is not tenable in economics. For an economist theoretically no such demarcation is possible. To him interest and usury hold the same meaning. The issue is simply a distinction between interest and profit (on trading) which the Qur'ān has highlighted by saying "*Allah permits trading and forbids usury.*"

RIBA IN THE PROPHETIC TRADITIONS

Riba, as practised prior to Islam, is described in the following tradition included in Al-Muwatta of Imam Malik.

Zayd ibn Aslam said, "*Riba* in the Jahiliya (days of ignorance - prior to Islam) was that a man would give a loan to a man for a set term. When the term was due, he would say, 'Will you pay it off or increase me?' If the man paid, he took it. If not, he increased him in his debt and lengthened the term for him."

Such increase in amount payable for extension of time of payment is called *Riba* in Islam. Numerous traditions of Prophet Muhammad (may Allah bless and greet him) have forbidden this practice. Imam Malik, while relating the above mentioned tradition of Zayd ibn Aslam, has even equated the cash credit, provided by the

lender to the borrower for early recovery, in the same category.

He said, "The disapproved way of doing things, about which there is no dispute among us, is that a man should give a loan to a man for a term, and then the demander reduces it and the one from whom it is demanded pay it in advance. To us that is like someone who delays repaying his debt after it is due to his creditor and his creditor increases his debt." Malik said, "This is nothing but *Riba*. No doubt about it."

This particular form of *Riba* relating to increase in payment for deferment of payment and extension of time is called *Riba an-nasiyah*. Another form of *Riba* is the premium which has no counter value which is referred to as *Riba al-fazl*.

SEVERITY OF *RIBA* IN HADITH

The Prophet has discouraged and disapproved *Riba* in the strongest term. The severity of related hadith may be understood by considering the strong language used in these Prophetic traditions. Seldom has Prophet Muhammad (may Allah bless and greet him) used such words for other forbidden things as well. We shall examine some related traditions in the following lines.

Abdullah ibn Mas'ud (may Allah be pleased with him) narrated that the Apostle of Allah cursed the one who accepted *Riba*, the one who paid it, the witness to it, and the one who recorded it. (*Sunan of Abu-Dawood*).

Abdallah ibn Hanzalah (may Allah be pleased with him) narrated that the Prophet said: "A dirham of *Riba* which a man receives knowingly is worse than committing adultery thirty-six times" (*Mishkat al-Masabih*, Kitab al-Buyu', Bab al-Riba). Bayhaqi has also reported the above hadith in *Shu'ab al-iman* with the

addition that "Hell befits him whose flesh has been nourished by the unlawful."

Obviously the unlawful in the above tradition means *Riba*.

Riba al-fazl (may Allah be pleased with him) narrated that the Prophet said: "*Riba* has seventy segments, the least serious being equivalent to a man committing adultery with his own mother." (*Ibn Majah*).

Abu Hurayrah (may Allah be pleased with him) narrated that Allah's Messenger said, "On the night when I was taken up to Heaven I came upon people whose bellies were like houses and contained snakes which could be seen from outside their bellies. I asked Gabriel who they were, and he told me that they were people who had practised *Riba*." (*Al-Tirmidhi*)

Abu Hurayrah narrated that the Prophet said: "God would be justified in not allowing four persons to enter Paradise or to taste its blessings: he who drinks habitually, he who takes *Riba*, he who usurps an orphan's property without right, and he who is undutiful to his parents." (*Mustadrak al-Hakim*, Kitab al-Buyu')

Ali ibn Abu Talib (may Allah be pleased with him) heard Allah's Messenger curse those who took *Riba*, those who paid it, those who recorded it.... (*Al-Tirmidhi*)

Abu Hurayrah (may Allah be pleased with him) narrated that the Prophet said, "Avoid the seven great destructive sins." They (the people) asked, "O Allah's Apostle! What are they?" He said, "To join partners in worship with Allah; to practise sorcery; to kill the life which Allah has forbidden except for a just cause (according to Islamic law); to eat up *Riba*, to eat up the property of an orphan; to give one's back to the enemy and fleeing from the battlefield at the time of fighting and to accuse chaste women who never even think of

anything touching chastity and are good believers.”
(*Sahih Al-Bukhari*)

These Prophetic traditions equate *Riba* to the most heinous and abhorring crimes.

RIBA AND RAIBAH

The following assertion of Umar ibn al-Khattab (may Allah be pleased with him) is worth noting:

“The last verse to be revealed was on *Riba* and the Prophet was taken without explaining it to us; so give up not only *Riba* but also *raibah* [whatever raises doubts in the mind about its rightfulness]. (*Ibn Majah*)

This quotation of Umar ibn Khattab (may Allah be pleased with him) does not mean that the verse in the Qur’ān related to prohibition of *Riba* is the last verse revealed on Prophet Muhammad (may Allah bless and greet him). It means that commandment relating to prohibition of *Riba* came so much late in the life of the Prophet that much detailed instructions could not be got from him.

Two points should be understood clearly. *Riba* is involved in a number of human dealings and it was neither necessary nor possible to describe all possible conditions in detail. Necessary principles on which men can understand the approach and requirements of the Shari’ah (Islamic law) have been provided. That much suffices. What Umar ibn Khattab (may Allah be pleased with him) said was meant to add an element of caution on account of the severity of prohibition of *Riba* in the Qur’ān and the hadiths. *Raib* means doubt and its derivative *raibah* would mean doubtful. So the caution is not only to keep from *Riba* (interest) but also *raiba* (doubtful deals and matters). Anything similar to *Riba* and anything of doubtful credentials should be kept at bay.

This careful approach suggested by Umar (may Allah be pleased with him) may be read in contrast with the present day approach of stretching the provisions relating to *Riba* in order to prove the validity of bank interest and other prevalent financial practices on the assertion that *Riba* in Islam relates only to usury i.e. high rate of interest on consumption loan. This stand ignores the historical fact that premium on all types of loans prevalent in the days of Prophet Muhammad (may Allah bless and greet him), either of consumption nature or of trading/production nature, were forbidden. Also this is in complete violation of economic theories where any distinction between low rate of interest and high rate of usury is not tenable. Usury may be an abhorring expression in the English literature distinct from interest but in economics such different connotations have no base. We can call this distinction to be unscientific, and illogical.

Another point that should be considered is that transformation in a society cannot begin with financial affairs, rather they may come last. We can understand the statement of Umar (may Allah be pleased with him) implying that *Riba* was prohibited in the last phase of the life of the Prophet. This need to be understood well that, like all other reforms, Islam too has a package; call it a distinct and complete system of life. Any attempt to bring in one element out of the whole package will be too frail and so is bound to fail! What comes last cannot be brought first! Beginning of reform has to be made with faith and morality and then only other things, including financial reforms, are possible.

Riba in the present day world has assumed unprecedented importance and it appears that an economy without interest is not physically possible and it

is merely a utopia. The position today is akin to the prophecy of the Prophet in the following hadith.

Abu Hurayrah (may Allah be pleased with him) narrated that the Prophet said, "There will certainly come a time for mankind when everyone will take *Riba* and if he does not do so, its dust will reach him." (Abu Dawood and Ibn Majah)

Mankind seems to be engulfed in the smoke created by *Riba*.

FAREWELL SERMON

Prophet Muhammad (peace and blessings of Allah may be to him) gave farewell sermons to a large number of his followers during the last Hajj pilgrimage performed by him. It is reported that he gave three sermons, in Mina, Arafat and Makkah, the places where Muslims visit during the Hajj congregation. In all these sermons the Prophet gave farewell messages and touched upon the most important aspects of Islam. He talked about *Riba* too in those sermons, as reported in the following hadith.

Jabir ibn 'Abdallah (may Allah be pleased with him), giving a report on the Prophet's Farewell Pilgrimage, said: The Prophet, addressed the people and said, "All of the *Riba* of *jahiliya* (period of ignorance i.e. period before the Prophet) is annulled. The first *Riba* that I annul is our *Riba*, that accruing to 'Abbas ibn 'Abd al-Muttalib [the Prophet's uncle]; it is being cancelled completely." (Muslim, Kitab al-Hajj, and Musnad Ahmad)

A point needs to be clarified here. This sermon does not mean that 'Abbas ibn 'Abd al-Muttalib (the Prophet's uncle) was engaged in the trade of providing loans on interest till the period of the Farewell Hajj of the Prophet. While forbidding *Riba*, the Qur'ān specifies that thereafter principal of loans given earlier will be

returnable but *Riba* accumulated thereon were not payable. This sermon reiterated the position that all interest accumulation due on the loans provided by the Prophet's uncle stands annulled.

DIFFERENT FORMS OF *RIBA*

The hadiths of the Prophet have clearly described different types of *Riba* and in their light we can decide a new situation arising in our times. For example, we will discuss some of these Prophetic traditions in the following paragraphs.

Abdullah ibn Abi Awfa (may Allah be pleased with him) reported that the Prophet, said, "A *najish* (one who serves as an agent to bid up the price in an auction) is a cursed taker of *Riba*." (Tabarani's al-Kabir)

In other words, false bidding in order to increase price is akin to *Riba*.

Anas ibn Malik (may Allah be pleased with him) narrated that the Prophet said, "Deceiving a *mustarsal* (an unknowing entrant into the market) is *Riba*." (Sunan al-Bayhaqi)

So if a villager comes to a town and goods are purchased from him before he reaches the market and comes to know about the prevailing price, and so is deceived, the person deceiving him practised *Riba*.

The severity of prohibition of *Riba* can be understood by following hadiths where any non-monetary or indirect benefit from providing loan, or even for recommending any benefit, has been described as *Riba*.

Anas ibn Malik (may Allah be pleased with him) reported that the Prophet said, "When one of you grants a loan and the borrower offers him a dish, he should not accept it; and if the borrower offers a ride on an animal, he should not ride, unless the two of them have been

previously accustomed to exchanging such favours mutually." (Sunan al-Bayhaqi)

Anas ibn Malik (may Allah be pleased with him) reported that the Prophet said, "If a man extends a loan to someone he should not accept a gift." (Bukhari)

Abu Umamah (may Allah be pleased with him) narrated that Prophet said: "Whoever makes a recommendation for his brother and accepts a gift offered by him has entered *Riba* through one of its large gates." (Ahmad and Abu Dawood)

Surely, *Riba* has many gates, big and small, and it can make inroads through any of them if a person is not alert to save himself from its ignominy.

CHAPTER - V
LAWS OF TRANSACTIONS AS PER
THE QUR'ĀN

LAWS OF TRANSACTIONS AS PER THE QUR'ĀN

Verse 282 in the second chapter of the Qur'ān (2:282) is the longest verse of the book. Its another characteristic feature is that it deals with the laws of transactions that arise on account of contract of debt between two persons/parties. This is popularly known as *Ayatud-dain* (the verse of transactions). The next verse (2:283) is in continuation of the related issues; so it is better to study these two together. Translation of the two verses is reproduced hereunder:

(2:282) O Believers, when you contract a debt for a fixed term, you should put it in writing. Let a scribe write with equity the document for the parties. The scribe whom Allah has given the gift of literacy should not refuse to write. Let him write and let the one under obligation (the debtor) dictate and he should fear Allah, his Lord, and should not diminish from or add anything to the terms which have been settled. But if the borrower be of low understanding or weak or unable to dictate (for any reason), then let the guardian of his interests dictate it with equity. And let two men from among you bear witness to all such documents. But if two men be not available, there should be one man and two women to bear witness so that if one of the women forgets (anything), the other may remind her. The witnesses should be from among such people whom you approve of as witnesses. When the witnesses are asked to testify, they should not refuse to do so. Do not neglect to reduce to writing your transaction for a specified term, whether

it be big or small. Allah considers this more just for you, for it facilitates the establishment of evidence and lessens doubts and suspicions. Of course, there is no harm if you do not put in writing the common transactions you conclude daily on the spot, but in case of commercial transactions you should have witnesses. The scribe and the witnesses should not be harassed: if you do so, you shall be guilty of sin. You should guard against the wrath of Allah; He gives you the knowledge of the right way for Allah has the knowledge of everything.

(2:283) If you are on a journey and cannot find a scribe to write the document, then transact your business on the security of a pledge in hand. And, if anyone transacts a piece of business with another merely on trust, then the one who is trusted should fulfil his trust and fear Allah, his Lord and never conceal evidence for he who conceals it, has a sinful heart: Allah knows everything that you do.

It is noteworthy that the Qur'ān has devoted its longest verse coupled with another verse to give detailed instructions related to an issue of this material world, an issue arising out of transactions between two persons. This is not an isolated case. The Qur'ān has similarly given detailed instructions about worldly issues like laws of succession dealing with the distribution of properties after death. In fact, the Islamic spirituality does not need negation of worldly affairs and a Muslim is required to deal with these matters in accordance with the commandments of the Qur'ān and the traditions of the Prophet Muhammad (may Allah bless and greet him).

The above two verses relating to transactions between human beings deal with some basic and important issues that have been considered by the translators and discussed by the scholars and commentators of the Qur'ān. We are hereunder noting

some of the finer points considered by the translators and elaborated by different scholars and commentators of the Holy Qur'ān, including Sheikhul Hind Mahmoodul Hasan, Fatah Muhammad Jalandhari, Ashraf Ali Thanvi, Shabbir Ahmad Usmani, Syed Qutb, Syed Abul Ala Maudoodi, Muhammad Mian Junagarhi and Abdullah Yusuf Ali (may their souls rest in peace).

1. The question of debt in any transaction arises either when full or part of the value of the transaction is due or the goods traded or services are to be supplied on a future date. Thus it is either the case of amount payable or that of deferred supplies. No other case of creation of debt is legally conceivable.
2. The time of payment of the debt and completion of any obligation arising out of the deal has to be fixed. All debt deals are valid within a time frame and they cannot be open ended with respect to period of execution.
3. The terms of the deal should be written. The language of the Qur'ān makes it obligatory which would literally mean that anything otherwise is not permitted. That would make oral contracts of debt unlawful. However, there are other examples in the Qur'ān where command in the language is used to stress importance of that thing and its literal sense is not intended. In other words, the expression "you should put it in writing" means that it is better, advisable and preferable that one should put the terms in writing.
4. There are three advantages of putting the deal in writing, namely: (i) obligation of one person will not go on the other and there will be total clarity of what is receivable or payable by which party and when; (ii) establishment of evidence will be facilitated; and (iii) possibility of occurrence of any doubt or suspicion of any of the parties will be lessened.

5. The person who is capable of writing the deal should not refuse. However, he should do this job judiciously; any cunning drafting skills like assigning otherwise meaning between the lines or expressing things in “fine prints” that are initially not noticed in the beginning but that becomes vital at times, should be avoided.
6. The person under obligation, i.e. the person who is liable to pay or to supply the goods or provide services, should dictate the writing. However, if the person under obligation (the borrower) is not capable of dictating the writing on account of any reason like infirmity, low understanding, minor in age or old age his guardian should dictate the writing with justice.
7. Two men should be witness to the written document so prepared. They should be honourable persons in the society and they should not refuse to do so. If such two men are not available then one man and two women should be made witnesses. The reason of treating one man equal to two women for the purpose of witness as elaborated in the above verse is “if one of the women forgets (anything), the other may remind her.” This unequal equivalence is related only to business and trade transactions and the logic behind is that in the Islamic familial and social system women are generally present more in the family than in the market. Though, no doubt, she is permitted to do business and go out for other engagements in addition to her household responsibilities, her presence in the market is more uncommon. Otherwise in the issues where she should be generally present, this disparity in witness does not exist. Another example will clarify the situation. The whole system of Prophetic traditions, hadīth, is based on the witness of the companions of the Blessed Prophet who related the words spoken and deeds of the Blessed Prophet. The whole structure of Islam, its cardinal faith,

laws and traditions, is based on this system of authenticity of the companions who were witness to what they heard and saw the Blessed Prophet saying and doing. Here the disparity of two women to one man does not exist. For example Ayesha (may Allah be pleased with her), the wife of the Blessed Prophet, is equal in importance to Abu Bakr (may Allah be pleased with him), the companion and father-in-law of the Blessed Prophet for the purpose of relating any hadith. So on and so forth.

8. As Allah has commanded witnesses to do the job, they cannot charge any fees for this service. To be witness is an obligation from Allah and they will get their reward from the Lord and no reward here in this material world is permitted! Thus this service should be free of cost and without any obligation to any of the party. However, any genuine cost like travelling and food may be borne or reimbursed.

9. These witnesses will be the real basis of establishment of any legal claim whereas written document will serve as a memoir, to help them remember the correct situation. In other words, in case of dispute the witness of these men and women will be legally more important than the written document.

10. The Qur'ān commands that such written document should be prepared even where the amount of debt created is low. "Do not neglect to reduce to writing your transaction for a specified term, whether it be big or small," the Qur'ān says. However, on the spot and day-to-day transactions may be done without writing them down. It is preferable that these transactions should also be recorded but this has not been made obligatory. Likewise, it is not objectionable if neighbouring shopkeepers do not record the frequent transactions that take place between them.

11. The scribe, the person who has written, and the witnesses should not be harassed. Any compulsion to write a language favouring unduly any party or to give wrong witness will be a sin. The language used by the Qur'ān can be translated in the 'active form' too meaning that the scribe and the witnesses should not harass. Thus both the translations are possible: "the scribe and the witnesses should not be harassed" or alternatively "the scribe and the witnesses should not harass." Harassment caused by the scribe or the witnesses may be to take any undue advantage of their respective position. The Qur'ān has forbidden and blocked all possible modes of corruption.

12. If any scribe is not available during a journey, transactions may be done by hypothecating something as guarantee. The Qur'ān has provided this alternative method of entering into transactions on the basis of pledge, giving something as security. Such pledge becomes collateral of the party who is liable to pay any fixed amount or supply any goods or services at the expiry of a fixed period.

13. The above mentioned alternative method of transaction on the basis of pledge has been prescribed by the Qur'ān while on journey. However, the scholars and commentators of the Qur'ān opine that this is a permitted method of transaction while the parties are stationed at home too. In other words this is an alternative method both in ordinary and extraordinary conditions. So it is possible to resort to this method even when any scribe is available to write down the deal.

14. At this point the scholars and commentators of the Qur'ān have delved upon the usufruct of the thing provided in the pledge. It is not owned by the party which is holding it temporarily for a predetermined period. Any benefit accruing out of this temporary

possession is to be passed on to the legal owner, the other party, despite the fact that he is not holding the asset in that period. For example, if any house has been hypothecated, the party in possession thereof can neither live in that house nor earn rent on the property. That would amount to interest (*Riba*) that has been forbidden as the benefit will be the premium without any counter value. However, if any milk-bearing livestock has been pledged, its milk may be consumed in lieu of the cost of fodder provided for its sustenance.

15. If the parties have total faith in each other, they can enter into transactions without giving and taking anything as security. The Qur'ān warns the one who has been trusted not to betray the trust, fearing Allah.

16. Concealing evidence covers both the cases of giving wrong witness or not giving witness at all despite being witness to an event. Both the behaviours are despised and disliked.

LAST VERSE OF THE QUR'ĀN

Popularly a small portion of verse 5:3 is understood as the last verse of the Qur'ān. Translation of the whole verse reads as under:

Forbidden to you are carrion, blood, the flesh of swine, the animal slaughtered in any name other than Allah's, the animal which has either been strangled, killed by blows, has died of a fall, by goring or that devoured by a beast of prey – unless it be that which you yourselves might have slaughtered while it was still alive – and that which was slaughtered at the altars. You are also forbidden to seek knowledge of your fate by divining arrows. All these are sinful acts. This day the unbelievers have fully despaired of your

religion. Do not fear them; but fear Me. **This day I have perfected for you your religion, and have bestowed upon you My bounty in full measure, and have been pleased to assign for you Islam as your religion.** As for he who is driven by hunger, without being wilfully inclined to sin, surely Allah is All-Forgiving, All-Compassionate. (Al-Qur'ān 5:3)

The bold portion of the translation of the verse reading '**This day...your religion**' was recited by the Prophet (may Allah bless and greet him) about 86 days before his death in Arafat while giving his sermon from *Jabal-e-Rahmat* (the mount of peace) in the course of his last Haj (*Hajjatul Wida*). For most of the Prophet's companions, one lakh twenty-four thousand strong in number, this was the last sermon heard from him and the verse of the Qur'ān they heard was the last they received directly from his mouth.

However, the popular opinion about the above mentioned portion of the verse to be the last verse is not shared by many commentators of the Qur'ān. The following commentary by Syed Abul Ala Maudoodi sums up the debate:

"According to authentic traditions, this verse was revealed in 10 A.H. on the occasion of the Prophet's Farewell Pilgrimage. The context however seems to indicate that it was revealed soon after the conclusion of the Treaty of Hdaybiyah (i.e. in 6 A.H.). All parts of the discourse in which this verse occurs are so tightly interwoven and so closely inter-connected that it hardly seems conceivable that it should have been inserted here several years later. My own estimate – and true knowledge of this lies with God alone – is that this verse was originally revealed in its present context (i.e. commenting upon the conditions prevailing at the time of the Treaty of Hdaybiyah). It is conceivable that the

true significance of the verse was not then fully appreciated. But later on, when Islam prevailed over the whole of Arabia and the power of Islam reached a high point, God once again revealed this sentence to His Messenger and ordered him to proclaim it."

(Tafheemul Qur'ān)

The companions of the Prophet who were close to him including his family members (*Ahle bayt*) and close associates including Abdullah ibn Abbas, his cousin, heard him recite another verse as the last one on 3rd Rabiul Awwal, 11 Hijri, eight days before his demise (may Allah bless and greet him). Translation of that verse follows:

*Guard against the disgrace and misery of the day
when you shall return to Allah: there everyone
shall be paid in full, for the good or evil one has
earned and none shall be wronged.*

(The Qur'ān 2:281)

It is a well-known fact that the Prophet used to instruct the placement of the verses of the Qur'ān. The need for such instruction of placement of respective portions arose from the fact that the Qur'ān as a book has not been compiled in chronological order as revealed by Allah. Rather, the Qur'ān was compiled according to the divine guidance as conveyed by Allah through the Prophet himself. Hence the placement of any verse in the Qur'ān carries a special meaning.

The last verse as above carries a general meaning, and it covers all our deeds which should be done, keeping in view the accountability before Allah, the Almighty, on the Day of Judgment. However, when we study this verse in the context of its placement in the Qur'ān, it brings into light a special concern. The importance of the issue increases manifold when we

consider that the revelation of the Qur'ān ended on this verse and thus on that particular issue and concern.

Verse 2:278 of the Qur'ān addresses the believers and commands them to give up interest due. Verse 2:279 warns them that if they do not do so, this will amount to declaration of war against Allah and His Messenger. It further declares that a person is entitled to get back the principal amount of loan. Anything over and above the principal amount amounts to causing harm. Verse 2:280 urges the believers to give time and preferably forgo the principal amount of loan in the case of debtors who are in strained circumstances.

The last verse that we are trying to understand comes after this appeal for giving up even the principal amount that a person is entitled to receive if the financial position of the debtor is bad and precarious.

The verse next to the last verse is the longest verse of the Qur'ān known as *Ayatud-dain* (the verse of transactions) which describes in detail the laws of transactions that arise on account of contract of debt between two persons / parties.

Thus we find that the last verse is placed between the verses relating to abolition of interest, right to get back the principal amount of a loan and the advisability of providing more time for the debtor in bad condition, the likeable character of forgoing the loan itself and the laws governing the transactions between two persons / parties involving a contract of debt. In this context if we re-read the last verse, the message would be that commandments of Allah relating to transactions between human beings involving debt should be taken seriously because every human being has to return to his/her Lord on the Day of Judgment and account for his/her deeds. As justice would prevail that day and "none shall be

wronged," it is better for everyone to "guard against" the possible "disgrace and misery of the day."

Obviously, the message carried in the above verse is true to all deeds of human beings. However, its particular placement in the Qur'ān highlights its special relevance to the matters between two persons involving financial liabilities and loans. We may construe such transactions to the business deals between persons. It is a necessary ingredient of human existence in this world, and so justice and equity in these matters is so much important that Allah the Almighty closed His message-in-direct-narration to man, i.e. the Qur'ān, through His last Messenger on this particular note.

THE LAST TEACHING

The discussion on the last verse of the Qur'ān leads us to the question of the last teachings of the Blessed Prophet. It is understood that the prohibition of *Riba* (interest) was one of the last teachings of the Prophet. The reason behind this understanding about *Riba* as one of the last teachings of Islam is that Umar ibn al-Khattab (may Allah be pleased with him) is reported to have said, "The last verse to be revealed was on *Riba* and the Prophet was taken without explaining it to us; so give up not only *Riba* but also *raibah* [whatever raises doubts in the mind about its rightfulness]". (*Ibn Majah*)

There is an apparent contradiction between this tradition and a number of other traditions of the Blessed Prophet on prohibition of interest which cannot be treated as occurring only in the last phase of his life. This contradiction can be resolved by appreciating the discussions we made above on the last verse of the Qur'ān that was placed by the Blessed Prophet in

between the teachings relating to the prohibition of interest, and laws of transactions involving credits.

Another proof of prohibition of interest being one of the last commandments, if not the last itself, of Allah and taught by His last Messenger Muhammad (may Allah bless and greet him) is the traditions reporting the sermons of the Prophet during *Hajjatul Wida* (The Last Hajj performed by him). These were his last public addresses among mammoth gatherings of the faithful wherein he announced emphatically the prohibition of interest.

The Prophet in his sermons of *Hajjatul Wida* announced that all dues of interest in favour of his uncle Abbas ibn Abdul Muttalib (may Allah be pleased with him) stand abrogated. A cursory reading of this tradition may give an impression that Abbas ibn Abdul Muttalib was practising interest-based transactions till that day. However, a careful reading suggests that dues in the market receivable by Abbas ibn Muttalib relating to past transactions based on interest, when this was not made unlawful, were declared not payable. Islam has a very rigid and uncompromising attitude towards interest and even treats interest payable on account of prior legal transaction as null and void. We can understand this teaching with one example. If a person reverts to Islam today, his market dues accumulated in his favour on account of prior business deals will be payable to him but he cannot claim the benefit of interest if receivable by him on previous transactions.

Thus we may conclude that the Blessed Prophet prohibited interest due even on past transactions. The announcement about making interest payable to the Prophet's uncle was made to emphasise this particular aspect.

It may further be noted that the Blessed Prophet reiterated all important teachings of Islam in his last sermons in *Hajjatul Wida* and it was not an occasion of any new commandment. Prohibition of interest including dues already accrued on its basis was one of the important teachings of Islam that was repeated and stressed upon on that occasion.

CHAPTER - VI
ECONOMIC GOODS AND THEIR
TRAITS

ECONOMIC GOODS AND THEIR TRAITS

Goods in economics mean the commodities and services that have value to people and are saleable at some price. Not all goods are good all the time and not all goods are good to all people. These are objects or services human beings like to possess and which serve their routine economic needs. These things satisfy some desire or need. These are capable of being delivered involving transfer of ownership from one person to another.

Goods are classifiable in various manners. For example, economic or commercial goods as against free goods like air that are naturally available in abundant supply. Another classification may be that of 'industrial goods' that are produced for use by industry in production of other goods; 'commercial goods' that are not required for use in production of other goods but are used in business in the form in which they are produced such as stationary, furniture, office machines, etc.; 'consumer goods' that are ultimately consumed by individuals without any further processing.

Goods are called by other names, namely Riches, Resources, Materials, Assets, Possessions, Commodities, and Products. The Arabic word *Maal* has similar connotations.

MAAL IN ISLAMIC LITERATURE

It is interesting to note the discussions relating to *Maal* in the Islamic literature. Islam is proactive about human possessions including his/her resources and riches provided it has come through permitted (*halal*) sources and is utilised in permitted manners and *Zakat* and *Ushr*, as applicable, are paid according to the *Shari'ah* (the Islamic law) on the savings, if any.

The wealth accumulated by a person is subject to distribution according to the Islamic law of inheritance. On the basis of these provisions of the *Shari'ah*, Islamic scholars have discussed in detail the related provisions and extracted laws so that issues cropping up can be resolved. It must go to the credit of such scholars that all issues were addressed and viable solutions in keeping with the verses of the Qur'ān, traditions of the Prophet (may Allah bless and greet him) and practices of the exalted and rightly guided four caliphs were suggested.

It may be noted that the rulers of the Muslim world, despite varied degree of practices of Islam in their personal life, desisted from pronouncing rulings on legal issues, ignoring the Islamic scholars whom the Muslim masses regarded as pious and eligible for the purpose.

The whole body of Islamic jurisprudence (*Fiqh*) was developed by the private efforts of such scholars who paid no heed to the wishes, commands and fancies of the rulers of their times. They did face hostile rulers and persecutions and punishments in their hands but they remained firm to their respective understanding of the correct interpretation of the Qur'ān and *Sunnah* (traditions of the Prophet). Muslim masses always had faith in them and ultimately their rulings prevailed.

CHARACTERISTICS

Past Islamic scholars defined *maal* in terms of following characteristic features.

1. It should attract human beings. Men should feel affinity and liking for it.
2. It can be possessed and kept in possession safely. A likeable thing which cannot be acquired and which is not storable is not *maal*.
3. It should serve some human need. A useless thing can never be *maal*.
4. A good number of persons must recognise it as *maal*. A particular person may develop a fancy for a particular thing and consider that thing to be useful but that cannot be considered *maal*. This preference and fondness cannot be considered worthy of consideration unless a markedly good number of persons share this affection and fondness.

Goods may be Generic or Specific in nature. Generic goods mean the items for which replacements in the form of similar goods are generally available in market. For example, provisions like eggs, rice, and sugar are generally available in market and all these items are akin. One piece of egg available in one shop is like another piece of egg available in another shop. Specific goods are just the reverse of Generic goods. These are goods whose likes are not generally available in market. Consider the case of livestock. One goat owned by one person is not like another goat with another person. These two goats may have different prices. Similar is the case of houses. Every house may be unique with regard to its construction or locality, and these may justify difference in their respective values.

The importance of this classification between Generic and Specific Goods is that in any barter system Generic goods shall have to be transacted without any difference of quantity or weight, as the case may be. Any excess in quantity or weight will be *Riba* (interest). However, Specific goods can be bartered with unequal quantities. If a person borrows three eggs from his neighbour, he will have to return three eggs in lieu of that. One cannot take the plea that the eggs borrowed were bigger, so the eggs refunded should be more in number. The difference in size, if any, shall be ignored. Refunding two eggs in lieu of three will be unjust and demanding or giving four eggs in lieu of three would be *Riba*. [*Riba* literally means excess and Islam forbids the excess that has no counter-value/justification.]

Specific goods can be bartered with unequal quantity. One can exchange one house with more than one house and this excess in quantity may be justified. So this excess in quantity shall not be *Riba* as such.

USABLE AND CONSUMABLE

Yet another classification of goods which is very much relevant to the subject of Islamic economics and finance is the classification of commodities and assets as Usable and Consumable. A proper understanding of this particular categorisation provides an understanding of the stand of Islam with regard to interest. It also provides a justification of prohibition of *Riba*. This difference between usable and consumable is generally not considered in contemporary economics and finance whereas the Islamic approach is guided by this distinction. Something that has been consumed cannot be returned in its original form. It is possible to return a similar generic item. Any excess of the item in this return will be treated as interest by Islam and shall be illegal.

Neither any excess in quantity nor any rental for the consumed commodity is permitted in Islam. The rental too shall be interest and it is forbidden. However, it is possible to give and take rent for the utilisation of the Usable goods. The item as such is returned intact.

One example will explain the position. Suppose a person borrows five litres of petrol from someone and utilises it as fuel in his car and consumes that item. Now the person who borrowed the fuel will either pay the price of this fuel consumed or purchase five litres of petrol and return. The petrol so returned is not the same petrol that was borrowed as the original commodity has been consumed. Islam will not permit any rental in money terms or excess in quantity while returning the consumed item.

Now let us consider the case of a man using a car of another person on rental basis. The car in original form is returned after using and rental for using its services is paid. This transaction is proper and fully justified in Islam.

The significance of this discussion can be appreciated when we consider the case of reward to the factors of production in economics. As we have already discussed earlier, Islam recognises payment of *ujrat* (wages) to labour against utilisation of their services for a specific period. Rent too is the payment for utilising natural resources like land, minerals, natural vegetations, etc. All these are cases of using services without changing the shape or form of these human and natural resources. They are kept intact, their services utilised for a specific period and payments are made in due recognition of these services. But the capital brought in by an entrepreneur does not remain intact. It is simply consumed because its shape and form are changed. Now Islam does not recognise any rental in the name of

interest or otherwise for the capital as the item has been consumed. Rental for utilisation of a fixed period is permitted only in the case of a Usable item and forbidden in the case of any Consumable item.

Here lies the justification and *locus standi* of prohibition of *Riba* (interest) in Islam.

CHAPTER - VII
AN INTRODUCTION OF ISLAMIC
FINANCE

AN INTRODUCTION OF ISLAMIC FINANCE

Human society is dynamic. It cannot remain static. It has to grow without any break. In economics this uninterrupted growth is ensured through economic activity. The existence of man on earth demands that there should be a continuous economic activity to cater to the ever growing needs of man on earth. If, for example, all food items produced in a year are consumed and no seed is left for further irrigation, it would be a catastrophe and continuity of man on earth will be endangered. The economic activity of using the seeds for further production of food items is a must. This example can be extrapolated for all human needs.

An economic activity comprises four things: (I) Production; (II) Exchange; (III) Distribution; and (IV) Consumption. Goods and services produced have to be traded on some medium of exchange. The item produced can be supplied only if it has a demand. The supply and demand is based on their trading through a medium of exchange. Goods and services have to be made available to the consumer through distribution for consumption. The consumption creates new demand and thus economic activity begins afresh. This cycle of production activity continues. It goes on and on.

Production requires inflow of fund. Funds available from the sale of goods and services are often belated. Money is required to pay for non-recurring expenses like machines and technology and also for recurring inputs like raw material, salary and other expenses. The outcome of all these inputs is not always positive. An

element of uncertainty and risk is ingrained in the production process. So the fund required for production has to withstand this uncertainty and risk. Arrangement of fund for production and consequent economic activity is referred to as financing.

FINANCING SOURCES

Funds required for the production process can be arranged in any of the three popular methods:

1. Savings of the entrepreneur himself;
2. Equity or borrowings from other individuals or institutions; and
3. Trade credit

These are not mutually exclusive methods. A hybrid of these modes of financing is also possible.

It is always advisable to arrange capital from own savings. But it is not always possible to depend solely on this because the quantum of fund required may be much higher than what a person can muster without any outside assistance. Entrepreneurs are compelled to seek outside help. Funds are made available by individuals who have spare money or by institutions whose business is to do so. Normally such institutions working as financial intermediaries – commercial banks, industrial banks and other financial institutions – collect small savings from different sources, particularly small savings of general masses. These financing agencies are called financial intermediaries and this process is known as financial intermediation.

Trade credit is a very commonly used source of finance. This is an age-old practice where suppliers of goods provide credit for a period and the purchasers too do not pay cash down and credit in the form of late payment has to be provided. Credit available from suppliers (creditors) is as good as getting fund in cash

and credit provided for purchasers (debtors) is similar to providing cash as loan.

Out of the popular methods of financing described above financial intermediation is a relatively new phenomenon. This has developed in the last couple of centuries. Although financial intermediaries may be traced in the older historical periods but the role and complexity of this phenomenon has increased to an extent not found earlier. One of the reasons of this increasing role of financial intermediation is that the requirement of fund for a modern business entity is so much high that it is nearly impossible for a single person, family or group of persons to arrange it.

Further, the gestation periods till commercial operations of many ventures are also very long. This has led to specialised groups for arranging the required equity and debt. These financial intermediaries are also able to collect small savings of general public. This has increased the propensity to save. In this system even a low earning person is encouraged to save and make that tiny saving a worthwhile thing. Accumulations of these small savings lead to availability of huge amount at the disposal of these agencies. Instead of the case of drops-in-an-ocean this becomes a phenomenon of drops-making-an-ocean!

ISLAMIC APPROACH

The Islamic approach of intervention in the mundane affairs of man is guided by the twin objective of eradication of all forms of injustices and increasing the efficiency of work. The end result of this approach is *falah* (human well-being) and *hayat-e-tayyiba* (good life).

Eradication of all forms of injustice can be understood in terms of the five objectives/goals of Islamic law (*Maqasid al-Shari'ah*) described by Islamic

Shari'ah scholars, namely: (i) Safeguarding Faith; (ii) Safeguarding Life; (iii) Safeguarding Intellect; (iv) Safeguarding Posterity; and (v) Safeguarding Wealth. These safeguards ensure that all forms of injustices are checked. Alternatively, we may describe the purpose of Islamic jurisprudence as establishment of justice and equity (*adl* and *ihsaan*). Establishment of *adl* and *ihsaan* in a society will in turn result in better efficiency and more productivity.

However, a note of caution is necessary that establishment of *adl* and *ihsaan* is a relatively more important objective; and if in a given condition this tells upon the economic efficiency of the members of a society, that deficiency shall be compromised. There cannot be any compromise in eradicating injustice to human beings.

ISLAMIC FINANCE

The Holy Qur'ān has forbidden the ugliest form of exploitation in economics and finance. It is *Riba* (interest). The *sunnah* (traditions) of Prophet Muhammad (may Allah bless and greet him) describes in uncompromising manners the various forms of interest that have been made unlawful. Hence prohibition of interest is the prime most object of Islamic finance.

Other prominent unlawful practices which have to be checked as delineated in the Qur'ān, Prophetic traditions (*sunnah*) and in the Islamic jurisprudence ordained by scholars while applying the commandments of the Qur'ān and *Sunnah*, are named in the following.

1. *Qimar* (gambling);
2. *Gharar* (hazard);
3. *Ghaban* (fraud);
4. *Ikrah* (coercion);
5. *Ihtikar* (hoarding);

6. *Bai al-mudhtar* (exploitation of needs);
7. *Najash* (raising prices by false bidding); and
8. *Jahl mufdhi ila al-naza* (lack of material information leading to disputes)

This is not a complete list. Such an all inclusive list is neither possible nor intended. Human beings develop new practices and judgments, severally, on them are passed by the scholars accordingly. This is an ongoing process. The list above is merely indicative for developing an understanding of the Islamic approach in economic activities including financing.

CRITICAL ISSUES

Islamic scholars in the last century faced a number of challenges thrown by the rise of capitalism and socialism. A question mark was raised on the relevance of Islam in solving modern complex economic issues, particularly the viability of an economic system without interest. Development of banking system was supposed to be the greatest challenge because this institution became the citadel of interest-based economic development and an economy without this institution was unthinkable. Islamic scholars faced the challenge effectively and proposed a viable alternative system of banking.

HISTORY

Shari'ah scholars started writing from the late thirties of the twentieth century on the ills of interest-based system of economics and the need and possibilities of reverting the trend in favour of the Islamic system, where *Riba*/interest is *haraam* (prohibited). For example, a series of articles written by Syed Abul Ala Maudoodi from 1936 to 1960 was published in book form under the titles *Islamic Economics* and *Riba* after 1960. Although we find certain apologetic writings justifying bank interest on the

opinion that it is not *Riba*. But the opinion got buried under the pile of forceful writings of *Shar'iah* scholars and Muslim economists and the Muslims' mass opinion sided with the conviction that bank interest is nothing short of *Riba*.

Muslim economists took clue from *Shar'iah* scholars and they came out with the blueprints of how to form a bank without interest. For example, Dr. Mohammad Nijatullah Siddiqi's book *Interest Free Banking* was published in the year 1968. The practical shape of these writings in the form of Islamic Finance and Islamic Banking was experimented in Malaysia and Egypt.

Malaysia became independent in 1956 and within a couple of years thereafter *Tabbung Hajji* started functioning. Individual recurring savings by Muslims for the purpose of performing *Hajj* pilgrimage were mobilised and invested in accordance with *Shari'ah*. This made the pilgrimage easier because profit earned on such savings lessened the savings required for the purpose.

Further, this concept popularised the concept of *Shari'ah*-compliant investment. This successful venture remained outside the view of the world outside Malaysia. It was noticed in 1981 at the time when proposal for formation of an Islamic Bank of Malaysia was under the consideration of the Islamic Development Bank. The experiment in Egypt remained under full public view from day one and perhaps one of the reasons of its failure in latter years was the expectation or concern it unnecessarily generated.

One visionary cum activist, Ahmad Najjar established a saving cum investment venture in a small town of Egypt named Mit Ghamr in 1963. Al Najjar had secured Ph.D degree from Germany in social economics. He wanted to operate the bank on the German Saving Bank model. He started his venture with the permission

of the Government of Egypt. It was initially successful and several branches were opened in small towns in quick successions. The Government of Egypt, sensitive as it was under the establishment of President Nasser towards Islamic movement, later became conscious that this successful experimentation may invoke Islamic revivalism and make Muslim Brotherhood strong. The government liquidated the banks in 1973.

However, the Mit Ghamr experience, despite forced liquidation, served as a beginning of the Islamic banking movement. The government of Egypt itself started a bank named Nasser Social Bank (NSB) in 1976 to fill the void created by the banishment of Mit Ghamr banks. NSB could not last long.

Earlier an experience based on the concept of a cooperative bank was done in Karachi in 1965. It was started without doing much home work and it failed because of administrative reasons.

A number of Islamic oriented financial institutions came up in different parts of the world after mid-1970s.

A landmark in the history of Islamic bank was the establishment of Dubai Islamic Bank in 1975. At this stage the new development was noticed by the Federal Reserve Bank, USA, Bank of England, World Bank, Harvard University and London School of Economics. Thereafter there has been no looking back in the development of Islamic banking on the one hand, and analysis and research of the outcomes of the movement by the academia the world over. Hundreds of books have been written on the subject and scores of research materials, articles, dissertations submitted in the western universities, have been published. Much water has flown since.

CHAPTER - VIII
RISK AND DEBT IN ECONOMIC
ACTIVITY

RISK AND DEBT IN ECONOMIC ACTIVITY

Risk is ingrained in a business activity. Total risk-free genuine enterprise is almost impossible to find. There is no available mechanism to foresee all uncertainties and take effective corrective actions beforehand so that the outcome of any enterprise is always favourable. An entrepreneur can try his level best to project all possible impediments and contingencies and plan to keep the cost of any unwanted situation in control. He may further keep shock absorbers and reserves in hand to recover from any unsavoury situation or arrange some form of insurance so that any loss suffered is compensated. But total avoidance of risk is not possible. The uncertainty involved in the outcome of an enterprise is always not negative. It may result in windfall gains and profits more than that was envisaged. This is the basic trait of a genuine production activity.

This is also the case against the incidence of interest, a fixed return on debt provided for an enterprise. As the rate of return on fund invested is not certain, the payment to the fund too should be at the same wavelength. Such payment on funds provided may be high, low, zero or negative depending upon the outcome.

It is possible for a person providing debt to keep any loss at bay by not being a party to the capital of any enterprise. In that case he will neither get any share of profit nor will share any loss. The creditor will be entitled to get back the amount of debt as per the agreement

without any increase or decrease. This is mostly prevalent in the case of trade credits.

TRADE CREDITS

Trade credit is a time tested and accepted form of providing debt. This practice is perhaps as old as the existence of economic activity. It was prevalent in the days of the Blessed Prophet and he let it continue after forbidding the abhorring practice of interest that had got associated with it. In fact, the dominant practice of interest (*Riba*) was related to trade credit. A creditor would provide lease of time in repayment of debt to a person who failed to pay in time. This extension of time on trade credit was given in lieu of a premium. The Qur'ān termed it as *Riba* (interest) and forbade it. [*Riba* literally means: premium; addendum; add-on]. No additional amount over the amount of trade credit is permitted in Islam. Following characteristics of trade credit are noteworthy:

1. Trade credit is a form of finance. Let us assume the case of any business needing money to purchase raw material. If instead of money arranged as a debt the business is able to purchase the required material on credit, the purpose of the finance required otherwise is served.
2. Trade credit is more or less a necessary characteristic of an economic activity. In particular, it is very difficult to always be in a position to purchase commodities cash-down. A basic reason is that the market demands credit and goods cannot always be sold in cash. If a business entity is not able to sell in cash, how can it manage to purchase in cash! The facility of credit purchase increases the viability of an enterprise.

3. The quantum of trade credit and the period of repayment of the debt are directly linked to the quantum and quality of business activity. The absolute amount of credit available from the market increases with the increase of business. Similarly, an enterprise with better goodwill is able to arrange more credit. We may conclude that credit available from the market is directly proportional to the goods and services produced. This is in fact a cardinal principle of a healthy economic activity where credit is created in the market because of trading and the size of debt in the economy is defined by the quality and quantity of economic activity. In other words, the credit should be backed by goods/services.

DEBT DOCUMENTS

The Blessed Prophet let the system of trade credit prevalent in the market continue after correcting the wrong practice of interest, related thereto. It sums up the Islamic approach towards economy; rectifies and amends wrong customs and lets the rest continue in their own stride.

As Islam forbids any increase in amount of debt, any document prepared in support of the debt is not tradable. It is possible to make such a trade document transferable or 'negotiable' but as its face value will remain unchanged there is no scope of its trading.

Islam leaves no scope for creation of debt-documents without any back-up of any assets like goods, commodities, or services. This ensures that debts in the market are always in proportion to the economic activities and the corresponding creation of assets. In other words, in an economy guided by Islamic principles the scope of financial sector surpassing manifolds the

size of real economic sector is not possible. The importance of this aspect of the economy can be appreciated by recalling what happened when the debt bubble burst recently causing financial tsunami.

A market study of the position of debt in the market vis-à-vis the real sector of economy during the days of the financial tsunami showed that the size of the financial sector was in between 600 to 1000 trillion US dollars as against the real economic sector of 65 trillion US dollars. In this situation a mere adverse movement of 10 per cent of financial sector is sufficient to wipe out the whole real sector of the economy. The shock-waves and the turbulence felt during the financial meltdown was a result of such adverse movement of financial sector of economy which has no real base of its existence. This size of financial sector of the economy representing debt documents without any back-up of any real economic activity like production or services or creation of assets may be termed as the Virtual Economy. Higher the gap between the real economy and virtual economy, severer shall be the turbulence in the market.

The trading of debt documents adds to the malaise relating to excessive expansion of credit.

EASY CREDIT

Availability of easy credit has dangerous effects on an economy. The financial meltdown which the world witnessed in the year 2008-09 was caused by this availability of easy credit which resulted in excessive expansion of credit. Experts have been talking about the impending dangers of the financial crisis well before the time it happened. We have on record the opinions of Dr. Umer Chapra, a renowned Islamic economist, expressed in his lecture in the international seminar on Islamic Banking organised by Jamaat-e-Islami Hind on 18-19

February, 2006. Excerpts from the lecture of Dr. Chapra are noted hereunder:

“There is a close relation between easy availability of credit and living beyond means and macroeconomic imbalances. Of course the credits could be long term as well as short term. But in the present day circumstances a substantial part of the credit is short term which is easily reversible. The borrowers are willing to get back their debt, their financing, as soon as possible whereas debtors are unable to pay. And this leads to a financial crisis...

“Let us take, for example, some countries where there has been crisis. Let us take the East Asia Crises. The countries where these crises took place were shining success stories. They had high domestic saving and investment, healthy fiscal and monetary policies. They were envy of a large number of developing countries. But in spite of this there was a crisis because there was rapid growth in bank credits in local currency. A lot of money was coming from foreign banks to these countries and the local banks kept on lending and lending and lending – a very excessive lending that cannot be used productively. Consequently there was a lot of flow of this credit to the speculative sector of the economy, the stock markets, the commodities markets, the foreign exchange markets. In such a situation the credit tends to be largely short term as for long term financing there is the need of project valuation. The foreign banks gave a large number of credits without evaluating the risks they were getting. Sixty-four per cent of the total credit was short term. Now in such a situation any shock can drive away the creditors... As a result of this, these countries were not able to export as much as they were exporting before and they were not able to get back their loans. So there was a rush to withdraw the funds. The local banks could not repay because they had given some loans on long term

and medium term. And the borrowers could not pay immediately. There could have been an international financial crisis; therefore the IMF came to the rescue of the international banks. They pumped in a lot of credits to these countries to save the Western Banks. As a result what happened, the private sector debts became public sector debts. And who is going to suffer? The taxpayers in these countries have to ultimately suffer the losses.

“Let us take the LTCM (Long Term Credit Management). This is a hedge fund in the United States. These hedge funds generally speculate. Their main purpose is supposed to be hedging but it is really not hedging but speculating. They speculate and create risks. They are highly leveraged short term lending. Leverage you know when you are able to get ten dollars against one dollar of capital the leverage is ten. But even in the case these LTCM the leverage before the crisis was 25, which means that they were able to get 25 dollars against each dollar of their own capital. A little after the crisis the leverage rose to 50 because they had to borrow more and the value of their asset also got down. So the leverage rose to 50. And before the Federal Bank came to the rescue of this institution the leverage had risen to 167.... With such a high leverage the financial system is bound to become unstable.

“Now look at the United States’ imbalances. The US has been borrowing and borrowing and borrowing, heavily – both the private sector and the public sector. As a result there is a large discrepancy in the Federal budget, also in the state budgets and the municipalities and so on. And the savings in the United States is only about one per cent of GDP. And the investment is high. Not all of this productive investment. A lot of this is in the speculative market. Any time the foreigners who are providing these funds may get scared and may refuse to

lend more. I hope this does not happen, because if it happens there will be financial crisis throughout the world. The value of dollar would go down, interest rate would rise up in the US, and the economy will go into a recession. Because the US is a very important market in the world; therefore the whole world will suffer.

“What is the way out of this situation? It is necessary to have less reliance on debt and greater reliance on equity.”

ECONOMIC RECOVERY!?

The forewarning by experts, including Dr. Umer Chapra, about the global financial crisis well before it actually occurred was not prophetic, it was merely a scientific conclusion based on the projection of economic trends. The symptoms of the impending crisis had become evident to the trained eyes of the economists before it was accepted by the political establishments the world over.

Similarly, we cannot say that the crisis period was actually a past event. The symptoms exist and the domino-effect continues although the political establishments have managed that these are not now discussed in the open and debated heatedly as was done during the so-called financial tsunami period.

The world continues to be in the grip of the crisis although the general and overwhelming masses who are at the receiving end of the ills of the crisis-in-continuation may have accepted these as fate-accomplish. In fact, cyclic fluctuations in economy, popularly known as business/trade cycle, have come to be accepted as a necessary characteristic of an interest-based capitalist economy.

TRADE CYCLE

Alternation of periods of prosperity and depression of good and bad trade is known as trade cycle. Keynes described that a trade cycle is “composed of periods of good trade characterised by rising prices and low unemployment percentages, altering with periods of bad trade characterised by falling prices and high unemployment percentages.”

We witness wave-like fluctuations in employment, income, output, and price level. Such waves like fluctuations in the indicators of economy are witnessed more or less globally. Periods of good trade in economies may be termed as expansions and the bad trade may be understood as contractions. These two phases follow each other, one period giving way to the other. The phases of contraction and expansion recur frequently and in fairly similar patterns. A full trade cycle comprises expansion, recession, contraction and revival. Such sequence of changes is recurrent but not periodic.

During expansion periods production and prices increase and interest rates come down. During recession production and prices come down and interest rates move upward. The period between expansion and recession is characterised by the crisis of confidence of consumers resulting in shortfall in demands and the consequent bankruptcies of business entities. Finally, a host of steps taken by the political establishments, in the nature of preventive and breakdown maintenance, aimed at building consumer confidence and providing liquidity in the economies, lead to the period of recovery.

A note of caution is needed to be mentioned. One period of good trade called the expansion of business is not as good for the consumers of an economy, the silent and hapless masses, as the previous period of expansion. The consumers are always at the receiving end of the

malaise. Their miseries keep on increasing. Prices go on rising as the average price level in every new period of economy, the good days of trade, is always higher than that of the immediate earlier period of expansion. The interplay of interest in the economies leads to this situation. The gap between the real economy and the virtual economy go on increasing. As we have noted earlier 'higher the gap between the real economy and virtual economy, severer shall be the turbulence in the market.'

CHAPTyer - IX ISLAMIC BANKING

ISLAMIC BANKING

Financial viability and technical feasibility of a commercial bank without interest became a challenge to the scholars of Islamic studies, including economists. Something had to be done to prove that the uncompromising attitude of Islam towards interest has an economic rationale that is relevant to the modern society, too. Islam is proactive towards all aspects of human life, including economics and finance. Development of banking industry in the last three centuries has been done squarely on interest. With the passage of time commercial banks acquired so much importance that banking almost became an essential element of a modern economy.

Now with total rejection of interest by Islam there remains no room for the types of institutional growth that developed meanwhile in these areas. Islamic scholars accepted this challenge head-on and produced a series of articles and books delineating proposed commercial banks without interest. Considerable, if not major, portions of books and articles written on Islamic economics in the twentieth century in different languages, particularly after late sixties, were devoted to possibilities of banking on Islamic principles.

Writings of Maulana Syed Abul Ala Maudoodi in Urdu, Baqi-us Sadr in Persian, Dr. M. Nejatullah Siddiqi in Urdu and English, Dr. Umer Chapra in English, Syed Qutb in Arabic and a host of others in these and other languages covered this issue. Almost all the writings related to interest-free banking placed profit and loss

model of Islamic banking as the replacement of interest-based conventional banking.

Dr. M. Nejatullah Siddiqi searched common elements in dispositions of different schools of Islamic jurisprudence (*mazhab*) in his book *Shirkat-o-Mudharbat ke Sharai Usool* so that the blueprint of Islamic banking proposed by him may become acceptable to all. Later developments did not follow this acceptable-to-all line. Rather, in contrast to this later trends were to search anything suitable in any school of jurisprudence (*mazhab*). Anything suitable in Hanafi, Shafai, Maliki or Hanbali *mazhab* is deemed acceptable!

In this later approach other discussions and deliberations in other schools of jurisprudence, like Zahiri or Jafiri, are also referred to in quest for systems that are suitable for today's situations. It may be said that in this methodology any support from any established quarter is acceptable! The true statement for today's approach will be that Islamic banking is both interest-free and *mazhab*-free. Thus in this process a new school of jurisprudence (*mazhab/fiqh*) is developing that has the ability to resolve current issues more effectively. Islamic studies are developing and enriching in this manner.

PRIMARY AND SECONDARY MODES OF FINANCE

Initial writers on the subject who presented blueprints for an Islamic bank (IB), including Syed Qutb, Dr. Nejatullah Siddiqi and Dr. Umer Chapra envisaged the contract based on *Musharakah* (Active Partnership) and *Mudharabah* (Sleeping/Passive partnership). We can refer these to be primary modes that are profit and loss sharing based methods of contracts. Other popular variations in these modes are *Muza'arah* (Partnership in Share Cropping) and *Musaqat* (Partnership in

Horticulture). These are equity based contracts. Such contracts are popular even today in collecting deposits and arranging funds for Islamic banks but are not in much use for investment of funds so collected.

The contracts that are in vogue for application of funds by Islamic banks may be called secondary modes of finance or trade-based modes of finance. These include *Murabaha* (Cost Plus Service Charge), *Ijarah* (Leasing), *Ijarah wa Istiqna* (Hire Purchase), *Bai Muajjal* (Sale on Deferred Payment), *Bai Salam* (Forward Delivery Contract) and *Bai Istisna* (Contracted Production). Such contracts involve credits.

Another possible sub-classification of secondary modes of contracts Islamic banks enter into is that of goods based contracts and fund based contracts as under:

Goods Based Contracts: *Bai Salam* (Forward Delivery Contract).

Fund Based Contracts: *Bai Muajjal* (Sale on Deferred Payment); *Istisna* (Contracted Production); and *Murabaha* (Cost plus Service Charge).

Primary contracts are riskier for banks as compared to secondary contracts. Income from investments for a bank in the case of the former is not certain and the possibility of loss in the ventures can never be avoided. In the case of deposits and other forms of collection of fund Islamic banks are willing to enter into primary contracts because the risks are shifted to the depositors or shareholders. Banks are relatively safe. But when it comes to investments and application of funds, these banks avoid primary contracts and prefer secondary contracts so that income can be predetermined.

MUSHARAKAH (ACTIVE PARTNERSHIP): Both Islamic bank and its customer, the party, invest in a

venture. The Islamic bank may appoint a person on salary basis to participate in the business on its behalf. Alternatively the bank may appoint the party itself its Managing Partner, authorising the person to run the business. Such a contract may be an ongoing method or on diminishing basis wherein the share of the bank diminishes gradually and the bank finally walks out of the deal on predetermined and agreed basis. The Managing Partner gets salary or commission for his services in favour of the bank. Profit in the venture is shared on agreed ratio whereas loss is shared on the basis of respective investments of the parties. However, in the case of loss, the Managing Partner may not get his salary and/or commission.

MUDHARABAH (SLEEPING/PASSIVE PARTNERSHIP):

This is the most popular form of receiving funds for an Islamic bank (IB). The account holders who provide fund for IB are sleeping partners while IB itself is the active partner. The account holders are called *Rabbulmaal* (Owners of Fund) and the bank is named *Mudharib* (Holder of Fund) and the process is called *Mudharabah*. Normally IB maintains following types of accounts:

Current Account: IB guarantees refund of money on call. This may also be called Call-Deposit. No profit is credited and no loss debited in these accounts. IB has to maintain sufficient liquidity to provide money on demand. The portion of current account balances over and above the liquidity requirement is included in the common pool of IB.

Saving Account: Unlike current accounts withdrawal from saving accounts cannot be served very frequently. Some discipline in this demand is enforced; say weekly withdrawal or one withdrawal a day. The cumulative average balance, calculated on the weighted average of

the product of daily, weekly or monthly balances with a number of days, weeks or months, as the case may be, is considered part of the common pool of the fund from which investments are made by IB. Alternatively, minimum balance of a particular period, say month, may be treated as part of common pool for investment.

Investment Deposit Account: This is akin to the fixed deposits for fixed periods, say three months, six months, one year, etc.

Common Pool of IB comprising average balances of saving accounts and investment deposit accounts and a portion of current account balances is utilised for investment. Profits and losses in different forms of investments are debited and credited in the common pool. Thus losses are spread out on profits earned. Profit is shared on agreed ratios. Naturally Investment Deposit Account holders enjoy more share of profit than the Saving Bank Account holder. Investment Deposits for longer periods get more share of profit than those with shorter periods of deposits. Losses remaining after spreading over overall profits will be shared on the ratio of respective balances of the parties in the pool. If the IB has its own fund in the Common Pool comprising share capital, reserves and retained profits then it will also bear the share of the net loss in proportion to its participation in the pool.

One form of investments by IB is *Mudharabah* wherein the bank enters into fund management agreement with clients. IB serves as the *Rabbulmaal* and the client concerned works as *Mudharib*. In this *Mudharabah* arrangement the bank is the passive partner and the client is the active partner. Fund of the bank is invested with the technical expertise of the client.

MURABAHA (COST PLUS SERVICE CHARGE): A simple method of cost plus deal is that a person in need of anything approaches the bank with a request to arrange that item. IB does the purchasing and sells the item after adding its element of profit/service-charge on instalment basis. The person gets the item he needed with the facility to pay the debt in instalments and the bank got the profit in the deal. In this case the element of profit to IB is predetermined under information to the client. A known amount of debt is created to be paid off in instalments.

IJARAH (LEASING): A number of leasing contracts are in vogue in Islamic banking business. One simple example is that of a building purchased by IB and sold with its element of profit to a client on deferred payment cum rental basis. The client pays off his debt in instalments. The periodic instalments paid by the client include a portion of the debt and an amount of rent. The debt goes on decreasing with every instalment and this decreases the rental too because with every payment the client is becoming owner of bigger portion of the property. With the last instalment the client becomes owner of the total property. The full ownership of the property is transferred therewith.

Leasing is the second most popular mode of contract practised by IBs. It is estimated that Cost Plus and Leasing account comprise more than 90% of the business done by IBs.

BAI MUAJJAL (SALE ON DEFERRED PAYMENT): Sale on deferred payment means credit sales where goods are supplied on credit, and payments are collected after a lapse of time either full at a time or on agreed instalments. *Mudharabah*, as discussed above also is a

deferred sale in sense. However, these two deals have basic differences. In *Mudharabah* IBs procure the item that are indicated by the prospective customers and sell that item after informing the client about its margin of profit. In *Bai Muajjal* goods are procured without specific indication by the clients and sales may be done keeping cost as a trade secret. Sharing cost may be a good practice, although not a precondition, in *Bai Muajjal* while it is a necessary in the case of *Mudharabah*.

It is debatable whether it is permissible in Islam to keep different prices for cash sale and credit sale. This debate is very much relevant for the business of an IB as more than 80% of their business is being done assuming permissibility of such differential pricing between cash sale and credit sale. *Maliki, Shafii, Hanbali* and *Ahle-Hadees* Schools of Jurisprudence (*Mazahib*) consider this differential premium for the time lag in payment and hence consider it a form of *Riba*. *Hanafi* School of Jurisprudence (*Mazhab*) permits this difference of price on the logic that it is the prerogative of the seller to keep any price he likes. The seller may demand different prices from different customers. For example, he may keep higher price from a new client than from a client with better goodwill in market.

IBs globally opt for the *Hanafi* logic!

BAI SALAM (FORWARD DELIVERY CONTRACT): It is the reverse of *Bai Muajjal*. Here goods are deferred in supply whereas price is paid in advance. Such advance payment for supply of goods at a later date in the case of production activity is called *Bai Istisna* (Contracted Production). These cases are not very much relevant for Islamic Banking business. However, in certain cases such contracts may have to be applied.

ABERRATIONS IN ISLAMIC BANKING PRACTICES

All is not well in the name of Islamic banking. There are grey areas and one should simply accept it without any hesitations so that scope for improvement may remain open. Whatever is happening in the name of Islamic banking and finance cannot be vouched. In many practices Islam in the name Islamic banking and Islamic finance appears to be misnomer. Some such aberrations are described hereunder:

PETRODOLLAR DRAIN APPROACH: An added charm of initiating an Islamic Bank in a country appears to be a drain through which petrodollar will flow in. (Alternatively, it may be called counter-drain approach.) As the economy of the members of Gulf Cooperation Council (GCC) countries in particular and other members of Organisation of Petrol Exporting Countries (OPEC) in general is rentier based, the funds saved in these countries are mostly invested outside their own respective countries. The whole world is vying for the savings available in GCC countries. A new method to attract these funds is to assure that these can be invested in their countries in a manner that is *Shari'ah*-compliant. Here we find a justification for the popularity of Islamic Banking. There is no love lost for Islam or its *Shari'ah* but a gold rush to muster the funds in this manner.

INSUFFICIENT SOLUTIONS: The economy of GCC countries is mostly rentier based. The developments of products and systems of Islamic banks have been in this environment of rentier based economies. Solutions for problems like equity participation, term lending, working capital finance, and cash-credit accommodation shall have to be addressed afresh. The solutions available

till date are not sufficient for a vibrant production based economy.

DILUTION OF CORE IDEA: The justification of Islamic Banking emanates from denunciation of *Riba* (interest). The original blueprints of the system, as proposed by scholars like Dr. M. Nejatullah Siddiqi and Dr. Umer Chapra, were prepared on the basis of replacing interest with profit. So we find that *shirkat* (partnership) and *mudharabat* (sleeping partnership) play the vital role in those proposals. The latter is the development whereby *murabaha* (cost plus contract), *ijara* (leasing) and *istiqna* (hire purchase), etc. took the place of *shirkat* and *mudharabat*. It is not any improvement of the original proposition but a dilution of the core idea of *Riba* being replaced by profit. Instead of approaching the challenges head on, the practitioners of Islamic Banking have chosen the easy route. The share of mark-up financial instruments of Islamic Banks may be more than 90 per cent. Such mark-up financing documents include trade finance by *murabaha* and investment finance by leasing. The overwhelming reliance on these financing instruments goes against the profit and loss sharing (PLS) system of Islamic economics.

MISPLACED FOCUS: The focus of Islamic Banking should be serving the *maqasid-e-shari'ah* (higher goals of law in Islam) of preserving Faith, Life, Intellect, Posterity and Wealth. We may add on the list of our concern in this regard and add Poverty Alleviation and Preservation of Environment for Quality and Continuity of Life on Earth. There can be no other justification for introducing any branch of the Islamic system if these basic concerns are not addressed properly. The Islamic Banking as practised till date has not to report home about in this area.

LACK OF SUPPORT: The system will not be noteworthy till it gets full support of Central banks and governments, and its performance outweighs the conventional banking to such a degree that the latter is made redundant if replaced by the onslaught of the new idea. The governments and central banks of most of the countries, where Islamic Banks have any presence, have not till date committed them seriously to the core idea of interest-free banking. Conventional banking continues to be the basic system in most of these places *inter alia* Iran, Pakistan, Sudan and Bangladesh. Islamic banks in these nations are in the “can-also-exist” mode. One may study the fate of Usury-free Banking Law and Islamic Banking System that became effective from 21st March, 1984, under Bank Markazi Jamhouri Islami Iran (Central Bank of Iran).

ACCEPTANCE OF FALLACY: Islamic banks are accepting the fallacy of Islamic banking window/counter in conventional banks. It is like Rooh Afza available in a beer shop! Interest-free banking is meant to replace interest-based banking. The idea of interest-free window in conventional banks is ridiculous. Sitting on the lap of what one is supposed to replace is simply a defeatist approach. It is like becoming a counter of what one had to encounter!

MAJOR CAUSES OF ABERRATIONS

Major causes of the aberrations cited above may be described as under:

SPAN OF HISTORY: Islamic banking industry is relatively new. As against the 300 plus years history of conventional banking, Islamic banking in its present form is the case history of 30 plus years. Interest has

become the dominant culture of the world today and all vested interests of financially strong and militarily powerful countries are linked to interest-based capitalist system. International financial institutions exist on this core idea of interest. Islamic banks have to face heavy odds.

DEVIATION FROM ITS BASE: Islamic economics is the theoretical base of Islamic banking. The industry has ignored, if not deviated from, the basic principles of Islamic economics. There is a mad rush for mimicking the products and services of conventional banks.

MARKET ORIENTED RESEARCH: Islamic economics as a subject emerged in the late sixties of the nineteenth century. Prior to that, scholars were presenting teachings of Islam relating to economics. Islamic economics as a distinct subject of learning with its own laws and practices was deliberated upon beautifully by many scholars. But this concentration on the subject did not live long. Almost all the experts on the subject became engaged in developing modules for Islamic banking and finance. Researches in Islamic banking and finance were market driven. Debates and delineation in Islamic economics went to the back benches.

These aberrations are challenges. These do not mean failure of the core idea of economy free of interest and injustices. Interest-based capitalist system has proved its failure and it is bringing more injustices and woes than cures. The solution lies in ethical practices based on the principles enshrined in Islam. Islamic economics is the solution. The challenge is to correct the aberrations caused by deviations from the basic principles.

DISTINCTIVE FEATURE OF AN ISLAMIC BANK

Islamic banks and conventional banks belong to two different genres, despite giving some common services to economy. In the case of universal banking system as practised in Germany, Switzerland, the Netherlands, Japan and many European countries there are more common features between conventional and Islamic banks. However, common features between Islamic banks and the commercial banks as operating in Anglo-Saxon nations and the countries following their system of banking are relatively less.

It is useful to discuss the difference between universal banks and commercials before describing the differences between a conventional bank and an Islamic bank.

Universal banking provides both 'Banking and Financial Services' through a single window. As per the World Bank, "In Universal Banking, large banks operate extensive network of branches, provide many different services, hold several claims on firms (including equity and debt) and participate directly in the Corporate Governance of firms that rely on the banks for funding or as insurance underwriters." Hence Universal banks give both loans and participate in equity financing. Its services include investment and participation in capital. The term 'Universal Banking' refers to those banks that offer a wide range of financial services beyond the commercial banking functions like Mutual Funds, Merchant Banking, Factoring, Insurance, Credit Cards, Retail Loans, Housing Finance, Auto Loans, etc. It is in practice in European countries.

In Anglo-Saxon countries like UK and USA and their former and present colonies and areas of financial influences, financial institutions are divided into two forms: commercial banks and development financial

institutions (DFIs). Commercial banks provide services like working capital, cash credit arrangement, overdrafts, bill discounting, etc. DFIs provide equity finance, long term lending and other forms of project financing. DFIs, in effect, become partners in the business of their clients and can have many forms of investment portfolios. Universal banking merges both the functions and all these services are done from the single window.

The basic difference between an Islamic bank and a conventional bank is that the former is engaged in trading activities like purchase and sale of goods and leasing of assets whereas the latter keeps such trading at bay. An Islamic bank deals with commodities and assets whereas commercial banks deal with their documents. As a natural consequence of this fundamental difference all the money outlaid by Islamic banks is backed by assets whereas this may not be true in the case of conventional banks. Such trading in goods makes Islamic banks partners to the industry which is not thinkable in conventional banks. Conventional banks while considering any proposal for loan are more concerned about securities, collateral and credit worthiness of the promoters than about a serious analysis of the feasibility report of the business. Islamic banks, as partners to the business, are involved more seriously in the viability of the proposals.

In countries where commercial banking and developmental banking are separate entities, the banking laws become a bottleneck. In that atmosphere banks are not permitted to enter into trading arrangements of goods and services. Countries where universal banking practices are in vogue can adopt the Islamic banking system more easily.

This discussion does not mean that an Islamic bank is akin to a Universal bank. The similarity lies only in the

approach towards participation in the projects of the clients. Both of them can opt for equity participation and profit and loss sharing that is not possible in the case of a commercial bank. In other words, commercial banks are non-participatory, universal banks can or cannot be participatory and Islamic banks are cent per cent participatory in nature.

The distinctive feature of an Islamic bank is, obviously, that it is interest-free and it adheres to the recognised ethical principles and the values enshrined in Islam.

Recognised ethical practices (*ma'aruf*) and specific commandments of the Book of God and His Prophet are the basic sources of Islamic law. Economics in Islam and all its other branches including Islamic finance and banking are guided by these principles and practices.

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