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Islamic Banking in Bangladesh : Its History & Socio-Economic Programmes

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ISLAMIC BANKING IN BANGLADESH: ITS HISTORY & SOCIO-ECONOMIC PROGRAMMES



Dissertation submitted for the Degree of
Doctor of Philosophy

By

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July 2004

DECLARATION


I the undersigned hereby declare that this thesis entitled "Islamic Banking in Bangladesh : Its History & Socio-Economic Programmes" submitted by me to the University of Rajshahi for the award of the degree of Doctor of Philosophy in Islamic History & Culture is an original research work and it has not been submitted earlier wholly or partly elsewhere for any degree or diploma.

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CERTIFICATE

I have great pleasure in certifying that this thesis entitled "**Islamic Banking in Bangladesh : Its History & Socio-Economic Programmes**" submitted by Dilshad Ara Bulu, Assistant Professor of Islamic History & Culture, Rajshahi University and Bangladesh University Grants Commission fellow is the candidate's own achievement and is not a conjoint work. Pertinently it may be mentioned here that the thesis has been prepared under my direct supervision and guidance.

I also certify that I have gone through the final draft of the thesis and found it satisfactory for submission to the University of Rajshahi in partial fulfilment of the requirements for the degree of Doctor of Philosophy in the Faculty of Arts.


31.7.04
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ACKNOWLEDGEMENT

Praise be Allah and His blessings to the best son of Hazrat Adam, the Prophet Muhammad (SM). Then the work would not have been possible but for the constant advice and proper guidance of my respected teacher and supervisor Professor A K M Yaqub Ali, the eminent orientalist, Department of Islamic History & Culture, Rajshahi University, Rajshahi. His valuable suggestions helped me improve the quality of my dissertation with new ideas and interpretations. I don't like to be little his greatness with the utterance of a few words of gratitude. He remains forever in the very core of my heart.

I owe my gratitude to the Bangladesh University Grants Commission, which by awarding me fellowship made it easy for me to complete the work without being financially much worried.

I remember with gratitude Professor A.B.M. Shajahan, Chairman, Department of Islamic History & Culture, Rajshahi University for his valuable help both official and academic. Besides, I thank all my colleagues in the Department who lent me their services when required.

I shall be failing in my duty if I do not express my deep feelings of gratitude to my husband, Professor Dr. Syed Zabid Hossain, Pro-Vice-Chancellor, Khulna University, Khulna, whose constant companionship and academic advice prompted me to complete the work in time.

My special thanks go to Mr. Main Uddin, Assistant Professor, Department of Accounting, Rajshahi University for providing valuable research materials which were under his disposal.

I am grateful to all the bank officials and librarians of Bangladesh who helped me in collecting necessary research materials and literature.

I am also thankful to Mr. Sayaduzzaman Milon, Assistant Professor, Department of Accounting, Rajshahi University for providing all-out support and cooperation in completing the official formalities relating to this Ph.D. work.

I am also indebted to Dr. Emdadul Haque, Associate Professor and Head, English Discipline, Khulna University for extending his help in the appropriate use of English language in the whole span of the dissertation.

I would like to express my cordial thanks to my family members, friends, colleagues and well-wishers for their constant inspiration and support, which led me to complete this study successfully. I also thank Mr. Mokhlechhur Rahman of The Active Computer Centre for formatting and Printing of my Ph.D. Dissertation.

Above all, I submit to Almighty Allah, who kept me physically and mentally fit to give a complete shape of this work.

Dilshad Ara Bulu
31.7.2004
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PREFACE

There is an increasing dissatisfaction among the Muslims about the dominant doctrines of economics and their failure to analyze and solve the economic problems of the Muslim community all over the world. The Islamic Economic Order presents a ray of hope to the Muslim Community in solving their economic problems.

Islamic economics directs and organizes economic activities of mankind in accordance with the Islamic fundamental principles. The fundamental sources of Islam are the Holy Qur'an and the Sunna (teaching and traditions) of the Prophet (SM), which provide guidelines for all economic activities, behaviour and a blueprint of how the economic system should be organized. Islam gives us a comprehensive guidance in economic matters such as prohibition of interest, compulsory Zakah, freedom of work and enterprise, concern for the poor, distinction between the Halal (permissible) and Haram (prohibited) in investments, income, consumptions, production and so on.

Islamic banking is an inseparable part of Islamic economic and financial system as well as Islamic value system. Islamic Banks provide

finance and financial services in Halal activities on the basis of profit and loss sharing agreement, which lead to mutual benefit of both the parties involved in any transaction.

In Muslim community, limited banking activity, such a acceptance of deposit, goes back to the time when the Prophet (SM) was still alive. At that time, people would deposit money with the holy Prophet (SM) and with Abu Bakr Siddiqi (R) the first Caliph of Islam. Since then credit societies and charitable trusts that lend to deserving citizens on an interest-free basis, have been existed throughout the Muslim world. Prophet (SM) introduced the system of Bayt-al-Mal (public treasury) collection and disbursement of revenues among the displaced Muhajirs and needy Answers. The Bayt al-Mal also played the role of an agricultural credit bank and also a commercial bank from the early days of the Ummayyads.

The Holy Prophet (SM) also allowed the practice of financing business ventures on the basis of Mudaraba and his companions followed the same. The Prophet (SM) himself was involved in Mudaraba contract with Hudrat Khadija (R). Hadrat Umar (R), Hadrat Usman (R) and Hadrat Abu Musa Al-Ashaari (R) were also involved in Mudaraba contracts.

Thus the concept and foundation of Islamic banking was developed fourteen hundred years ago during the lifetime time of the Holy Prophet (SM) and the guiding principles of interest-free Islamic banking has been derived from the Holy Qur'an and the Sunna of the Prophet (SM). But the history of the interest free banking in the modern perspective is not more than five decades.

The history of the modern interest-free Islamic banking could be divided into two parts. First, when it was an idea; second when it becomes a reality - by private initiative in some countries and by government initiative in others.

During sixties and seventies and in the early eighties of the last century interest free Islamic banking attracted more attention of the Muslim Umma because of the political interest it created in Pakistan, Saudi Arabia, Iran, and Sudan and in other Muslim countries and partly because of the emergence of young Muslim economists and thinkers. During that period theoretical concepts of Islamic banking and its operational rules, procedures and working guidelines have been developed by different individuals and bodies taking into consideration of the recommendations of different seminars, symposia, workshops on related issues and writings of the eminent Islamic scholars.

But Islamic Banks in reality is a very recent origin. The growth of Islamic Banks starts after the establishment of Islamic Development Bank in 1975. Since then it has been growing rapidly in the Muslim world as also in the non-Muslim world. Pakistan, Iran and Sudan have fully eliminate interest from their banking operations and they changed their banking style from interest based traditional system to interest free participative Islamic banking.

In Bangladesh few Islamic Banks have been working alongside interest based Banks. Now there are six Islamic Banks namely i) Islami Bank Bangladesh Limited (1983), ii) The Oriental Bank Limited (1987), iii) Al-Arafah Islami Bank Limited (1987), iv) Social Investment Bank Limited (1995), v) Shamil Bank of Bahrain EC, Dhaka, Bangladesh (1997), vi)

Shahjalal Bank Limited (2001), and one Non Bank Financial Institute namely Islamic Finance & Investment Limited working in Bangladesh. All these Banks are committed to manage their operations as per Islamic Shariah and establish welfare oriented banking system. They are conducting all Banking activities on the basis of interest free participative banking. They are also committed to extend cooperation to the poor, the helpless, downtrodden low-income segment of the society for their economic emancipation.

On the above Backdrop the study has presented an historical account of the Islamic banking movement in the whole world with special reference to Bangladesh starting from Bayt al-Mal to the introduction of modern interest free Islamic Banking. The study has also presented an elaborate discussion of the socio-economic programs of all the Islamic Banks in Bangladesh and how far they are successful in keeping their social and religious commitments.

Dilshad Ara Bulu
31.7.2004

Dilshad Ara Bulu

ABBREVIATIONS

AD- After Death

AIBF- Al-Arafah Islami Bank Foundation

AH -After Hijrah

AIBL- Al-Arafah Islami Bank Limited

BERB- Bangladesh Economic Research Bureau

BIBA- Bangladesh Islamic Bankers Association

BIBM- Bangladesh Institute of Bank Management

BSK- Bangladesh Sangskritic Kendra

CDD- Centre for Development Dialogue

CIIB- Citi Islamic Investment Bank E.C.

DDIS- Desired Durable Investment Scheme

DSISDP- Disaster Shelter and Integrated Social Development Project

FRS- Fixed Return Scheme

GOB- Government of the Peoples' Republic of Bangladesh

HPSM- Hire Purchase Shirkatul Meelk

IAIB- International Association of Islamic Banks

IBBL- Islami Bank Bangladesh Limited

IBF- Islami Bank Foundation

IDB- Islamic Development Bank
IERB- Islamic Economic Research Bureau
IFIL- Islamic Finance and Investment Limited
IIRO- International Islamic Relief Organization
Ltd- Limited
MBS-Muslim Businessmen Society
MMIS- Masjid Madrasah Investment Scheme
NGOs- Non Government Organizations
OBL- Oriental Bank Limited
OIC- Organization of Islamic Conference
PLS- Profit & Loss Sharing
Pilgrim's Management Fund
RDS-Rural Development Scheme
RSB- Religious Supervisory Board
RFSCN- Rotating Family Savings and Credit Net
ROSCAs- Rotating Savings and Credit Associations
SH-Sabuj Haat
SBIS- Small Business Investment Scheme
SBL- Shahjalal Bank Limited
SIBL- Social Investment Bank Limited
SLR- Statutory Liquidity Reserve
SPBP- Special Pally Binyog Prakalpa
TIS- Transport Investment Scheme
STLS- Short Term Liquidity Surplus

GLOSSARY

1. Hijrah - It means emigration. The Islamic calendar starts from the year Prophet Muhammad (SM) emigrated from the city of Makkah to Madinah.
2. Amanah-Means a trust. Something is given by one person to another to keep for some reason such as safe custody. The trustee is under obligation to return it in same condition although he may use it with the permission of the owner.
3. Al-Wadiah-Means safekeeping. This is an agreement to deposit an asset, excluding immovable fixed assets in custody of another party. The owner will give his/her consent to the custodian to make use of his/her asset/fund as long as this asset/fund remains in the custodian's hands.
4. Assalamu alaikum -Literally peace be on you.
5. Bai-Mujjal-Deferred payment sale.
6. Bai-Salam = Pre-paid purchase.
7. Bayt-al Mal= The Islamic state treasury.
8. Fadal (Riba) = A type of interest. Taking something of superior quality in exchange for giving less of the same kind of thing of poorer quality.
9. Fatwa= Islamic legal opinion(s).
10. Fiqh= Muslim jurisprudence. Fiqh is based primarily on Qur'an and Sunnah.
11. Ghanimah - One-fifth of the war booty

12. Gharar- Literally risk and uncertainty. This means the uncertainty and ambiguity in transactions, which comes from events whose happening, or not happening is subject to chance and as a result is unknown to the parties of a transaction at the time of the contract.
13. Hadith - Prophet's commentary on Qur'an
14. Hajj- Pilgrimage
15. Halal- Permissible according to Islamic law.
16. Haram- Which is unlawful or against Islamic Law.
17. Ibadah- 'Ibadah is used in three meanings: (i) worship and adoration; (ii) obedience and submission; and (iii) service and subjection. The fundamental message of Islam is that man, as Allah's creature, should direct his 'ibadah to Him in all the above-mentioned meanings, and associate none in the rendering of it.
18. Ijara- Literally leasing finance. In this contract the bank purchases the asset such as machinery, equipment or any property required by the client and then leases the asset to client for a given period, the lease rental and other terms and conditions having been agreed upon by both parties.
19. Ijma- Consensus of the Islamic jurists of a particular age.
20. Iman- Faith in the life hereafter and faith in Allah and His angles.
21. Jahanam-Most commonly understood to mean Hell. In fact, it is one of the levels of Hell. There are seven levels of Hellfire:
 - a. Jaheem - The shallowest level of Hell. It is reserved for those who believed in Allah and His Messenger (SM), but who ignored His commands.
 - b. Jahanam - A deeper level where the idol-worshippers are to be sent on the Day of Judgment.
 - c. Sa'ir - is reserved for the worshippers of fire.
 - d. Saqar - This is where those who did not believe in Allah will be sent on the Day of Judgment.

- e. Ladha - will be the home of the Jews.
 - f. Hawiyah - will be the abode of the Christians.
 - g. Hutama - the deepest level of Hellfire. This is where the religious hypocrites will spend eternity. The worst of Allah's creation are the Munafiqeen (Hypocrites), whether they are mankind or Jinn, for they outwardly appear to accept, but inwardly reject Allah and His Messenger (SM).
22. Jizya - Defense tax paid by non-Muslims living on Muslim lands (dhimmis). However, the poor, the sick and crippled, women, children, aged, priests, and monks were exempted from this.
 23. Ka'aba-The cube-shaped stone building whose foundations were built by the angels and completed by Prophet Ibrahim (Abraham) and his son, Prophet Ismael, peace be on them, in Makkah. It was rebuilt with the help of Prophet Muhammad (SM). It is the focal point towards which all Muslims face when praying.
 24. Khiraj - This is a tax on land.
 25. Khums- This refers to a levy of 20 percent which is imposed on some kinds of wealth (i.e. mines and wealth buried in land that has no owner).
 26. Mudaraba- Laterally profit sharing. An Islamic contract in which one party provides money and the other party provides expertise and management in order to share the profit on an agreed ratio. In case of loss the capital provider will bear all losses.
 27. Mudarib- A party in the contract of Mudaraba who works with the money provided by the other party on a profit sharing basis.
 28. Muqaradah- Another expression for Mudarabah which is explained above.
 29. Murabaha- Literally cost plus sales. It is a contract of sale in which payment is made some time after delivery of the goods transacted. Used as the basis of modern Islamic banking since the amount charged for deferred payment is in excess of the current market price (usually

- by an amount approximately equivalent to the prevailing rate of interest).
30. Musharaka- Literally equity participation. Islamic contract of partnership in which partners share the profit in an agreed ration but share the loss in proportion in which they supply capital.
 31. Nabi- Prophet of Allah.
 32. Nisab- This refers to the minimum amount of property liable to Zakah payment.
 33. PBUH- Peace be upon him. Somewhat English equivalent of SAW or SM used whenever the name of Prophet Muhammad (SM) is read or heard.
 34. Qiyas- Inference or analogy.
 35. Quard-e-Hasan- Benevolent loan (interest free) in which money is given to the needy without any charge so that borrower may return it at his convenience.
 36. Qirad=Mudaraba.
 37. R.A.A- Radhi Allah 'Anhu (May Allah be pleased with him). Said whenever the name of a Sahabi (companion) is read or heard.
 38. Rabb-Al-Mal- Provider of capital in Mudaraba contract.
 39. Riba- Literally Interest. More specifically, it refers to any pre-agreed excess paid or received over and above the principal in a loan contract.
 40. Riba al-Fadl- This refers to interest in barter. This indicates the excess charged in the exchange of commodities of the same kind (for instance, wheat for wheat, barley for barley, etc.). Barter transactions were common during the time of Prophet Muhammad (SM), and he did not restrict the application of Riba only to the credit transaction of cash, but to all types of barter.
 41. Riba al-Nasia- This refers to interest on debt. Nasia means a delay given to the debtor. This kind of Riba is found in all credit transactions in which a loan is advanced to a person on a payment of interest over and above the principal for the time of the debt.

42. S.A.W- Sallallahu 'Alaihe wa Sallam
43. Sadaqah- This means anything which is given or help offered to others to seek Allah's Pleasure. It also refers to a good act. If it involves spending income, this must have been earned in an Islamically permissible way.
44. Sadaqah al-Fitr- This is an Islamic levy paid in the month of Ramadan.
45. Shariah- Islamic Law.
46. Shirka- Musharaka.
47. Tabi'un- Tabi'un (singular, Tabi'i), successors, are those who benefited and derived their knowledge from the companions of the Prophet (SM).
48. Ushr- This refers to the ten percent (in some cases five percent) of agricultural produce payable by a Muslim as a part of his religious obligation, like Zakah mainly for the benefit of the poor and the needy.
49. Wa Alikum Assalam- And on you be peace. The reply to the Muslim greeting of assalamu alaikum (Peace be on you).
50. Waqf= This means assets which have been entrusted to an individual or organizations for a specified charitable purpose.
51. Zakah-This refers to a compulsory levy on each Muslim who has wealth which equal to or more than a minimum called Nisab. Zakah is 2.5% of wealth for the poor. It is one of the five pillars of Islam. This was only applicable on Muslims.

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Chapter 1

Introduction

Chapter 1

Introduction

1.1. Prelude

Islam is not a religion in western sense of the term; rather it is a *Din* or complete code of life encompassing the whole span of man's life from the cradle to the grave and the life hereafter. The concept of human creation and regulation of life are centered round the Holy Qur'an (the revealed book) and the Sunnah (teaching and tradition of the Holy Prophet), which are the primary sources of Islamic Law. This mundane life is just like a corridor to enter the abode of eternity where every species of rational being will be rewarded according to the *a'mal* or deeds done in the world. Hence the motto of every work and deed of man should be to achieve the pleasure of Allah, the creator. To weigh the good and bad side of man's activities there is a scale set up by Allah, and this is but Shariah of Islam (Islamic Law). Islam lays much stress on the corporate life of man, as it is evident from the concept of congregational prayers and other socio-religious festivals sanctioned by the Shariah of Islam. Moreover, to lead a harmonious social life as per the Shariah rules, a Muslim specially needs to earn lawful bread and to follow a sound economic program delineated in the Holy Qur'an and the Sunnah of the Prophet (SM). Extravagance in any form is condemned in Islam; in the same way stinginess is also discouraged. The leading of a modest life is praised in Islam. A Muslim is warned against spending all he has and leaving his children and dependents in economic misery at the time of his death. Islam, therefore, urges the Muslim to increase his wealth within the framework of the Shariah and to spend it in a lawful way. Thus the monetary transactions are performed in various ways through the centuries of Muslim rule in the world. With the passage of time the concept of modern banking come into being to facilitate the monetary transaction. Islamic Banking is a Shariah based concept and part of the modern economic system.

The introduction of interest free equity based financing is an outcome of Islamic Economic System. Islamic economy is as old as Islamic civilization, while Islamic banking concept is a new phenomenon. The Islamic Banking concept has come into force in the late 20th century. Islamic Banks are financial institutions that operate with the objective of implementing and materializing the economic and financial principles of Islam in the Banking arena. Islamic Banks provide finance and financial services in any Hallal (lawful) activities, which leads to mutual benefit of both the parties involved in any transaction. Islam insists that the participants in the trading process must share risk and return both. The Bank should neither pay interest to the depositors nor charge any interest on loans and advances. Instead they should enter into partnership with the businessmen as a possible alternative, sharing profit and losses if any. Interest is opposed in Islam perhaps on the ground of social divisions it creates and the hardship to borrowers. Islamic Banks in our country have started working with the concept of interest-free banking and it is proved that the new banking with interest-free concept could be successful and expanded in the country.

The main objective of Islamic banking is social welfare and helps the downtrodden people of the society and also to initiate different investment projects that conform to social responsibility for the disadvantaged and neglected segment of the society. Most of the Islamic Banks in our country have some special programs for social welfare, such as, rural development scheme, employment generation scheme, poverty alleviation scheme, cultural and religious scheme, healthcare & Medicare scheme, sanitation and pure drinking water scheme, Quard-e-Hasan scheme, development of libraries, Forquania Madrassa, Waqf properties, graveyards, Eidga etc. This study mainly concentrated on the historical origin and development of Islamic Banks in Bangladesh and their socio-economic programmes as mentioned above.

1.2. Objectives of Study

The study strives to provide a clear and vivid picture of the genesis, growth and development of Islamic banking system in the world with special reference to Bangladesh and the socio-economic programmes that have been taken by the Islamic Banks in our country. It also seeks a moral justification and cogent reasons behind Islamic banking movement and the activities of Islamic Banks. In view of the above background the specific objectives of the study are:

1. To provide an overall idea and concept of Islamic economics, Islamic finance, and Islamic banking in the light of the Islamic Shariah.
2. To present an historical observation of the origin and development of Islamic Banks in the Muslim countries as well as in the non-Muslim countries.
3. To provide an historical account and overview of the monetary system in the early days of Islam and their subsequent systematic development.
4. To present the current scenario of Islamic banking in the world.
5. To present the historical account of the origin and development of Islamic Banks operating in Bangladesh.
6. To identify the challenges and opportunities for Islamic Banks in Bangladesh and their impact on the society & economy of the country.
7. To give a picture of the social welfare activities of different Islamic Banks in Bangladesh.

1.3. Justification of the Study

This study has presented an historical overview of Islamic banking movement since the inception of Islam and the practical application of Islamic banking with special emphasis on different historical and economic issues related to Islamic banking. Islamic banking inherits its origin from the Holy Qur'an and Sunnah (teaching and tradition) of the Prophet(SM). But the history of modern Islamic banking in the world is not more than fifty years. And for Bangladesh is

about three decades only. At first it was a matter of writing, debate, and discussion in the academic forum and seminars. Islamic scholars in Bangladesh took the leading role in establishing Islamic Banks in the country. Islamic scholars and researchers, all over the world, wrote a lot of literature relating to different aspects of Islamic banking including its religious and economic feasibility, challenges and opportunities. In Bangladesh Islamic Economics Research Bureau took the initiative to bring the Islamic scholars in an umbrella to discuss and write on different policy issues on Islamic finance and banking. In mid eighties and early nineties some Islamic Banks came into the scenario of the economic horizon and the history of Bangladesh.

There is abundant literature on Islamic Economy and Banking in the Islamic Economics Research Bureau, which is easily available. Some materials, document and literature are also available in the training centres of different Islamic Banks, Islamic Foundation Library, Al-Arafah Islami Bank Library, and other libraries in Bangladesh, which could be collected with little effort. Islamic Foundation England deserves special credit for accumulation of different rare documents on Islamic finance and banking. Using modern electronic communication media like Internet and e-mail all those documents and materials could be collected. The researcher has also got materialistic support from both Institute of Bangladesh Studies and the Central Library of Rajshahi University. The researcher has completed the study within the stipulated time period through utilizing all the above facilities.

1.4. Sources and Collection of Research Materials

The research has been based on both primary and secondary sources of materials. The Holy Qur'an and the Sunnah (teaching and tradition of the Holy Prophet) are the primary sources of materials. While published research papers, articles, published and unpublished research dissertations (M. Phil and Ph.D. thesis), research reports, monographs, relevant books, journals, magazines, booklets and published annual reports of different Islamic Banks and materials available in different internet sites are secondary sources of information.

Thus the researcher has collected necessary primary or first hand information through consulting the Holy Qur'an and Books of Hadith. Secondary Materials have been collected through studying in different libraries such as Islami Bank Library at Mohammadpur, Dhaka; Islamic Economics Research Bureau Library, Puranapaltan, Dhaka; Institute of Islamic Thought Library at Farm-gate, Dhaka; Islamic Foundation, Baitul Mokkram, Dhaka; Bangladesh Public Library, Agargaon, Dhaka; Al-Arafah Islami Bank Library at Topkhana Road, Dhaka; Bangladesh Institute of Development Studies Library, Agargaon, Dhaka; Rajshahi University Library, Dhaka University Library, etc. Some secondary materials have also been collected from the Head Offices and Training Institutes of different Islamic Banks in Bangladesh. The researcher has collected some valuable books and published reports in this area. Some documents, literature and materials have also been collected from different Islamic Research Centres and libraries abroad. Besides, the researcher has visited different internet sites such as www.shahjalalbank.com.bd, www.ifil.net.bd, www.islamibankbd.com, www.prime-bank.com, www.oriental-bank.com, www.banglapedia.org, www.wu-wien.ac.at, www.use.edu, www.toutouchian.com, www.islamic-finance.net, www.thefiqh.org, www.users.bart.nl, etc. to collect necessary materials, literature and documents.

1.5. Chapter Plan

The study is divided into seven chapters. The structure of the study is presented below :

Chapter one deals with introductory section of the study. It covers prelude of the study including methodological issues such as sources and compilation of research materials; justification of the study, details study plan and limitation of the study.

Chapter two entitled 'Islamic Economy: Sources and Philosophical Background' includes concept of Islamic economics; explanation of the sources of Islamic economics such as the Holy Qur'an, the Sunnah of the Holy Prophet(SM), Ijtihad or exercise of judgment, history of the Muslims;

Philosophical background of Islamic economics; Ownership of resources from Islamic view point. This chapter provides a thorough idea about Islamic economy as compared to other economic systems and the primary and secondary sources of Islamic Economics as well as the Philosophical foundation of the system.

Chapter three entitled 'Banking in Islam: Genesis and Development from Historical Perspective, covers the concept of Islamic Banking, genesis and historical development of Islamic Banking from Bayt al-Mal to modern Islamic Banks and Financial Institutions, and the distinguishing features of Islamic Banking in the world.

Chapter four entitled 'Modes of Investment' provides a vivid picture of the different modes of investment of Islamic Banks such as Mudaraba, Musharaka, Murabaha, Quard-e-Hasan, Hire Purchase Shirktul Meelk, Bai- Salam etc. This chapter also includes the discussion of Bayt al-Mal, Riba and its elimination from the society, and profit and profiteering.

Chapter five entitled 'Islamic Banking in Bangladesh' covers the genesis of Islamic Banks in the country i.e. Islamic Banking as a concept till the early eighties and then as a reality since the establishment of Islami Bank Bangladesh Limited in 1983; the government policy and action for implementing Islamic Banking system in the country, and the description of all the Islamic Banks so far established in Bangladesh and foreign Islamic Bank working in the country.

Chapter six entitled 'Welfare programmes of Islamic Banks in Bangladesh' provides a detailed description of social welfare programmes of the all the Islamic Banks working in Bangladesh.

Chapter seven provides a conclusion of the study highlighting future prospects of Islamic Banks in Bangladesh.

1.6. Limitation of the Study

The study has some limitations. The researcher has collected some valuable information about Islamic Banks in Bangladesh through visiting

different wave sites. But unfortunately some Islamic Banks have not yet developed their wave sites and some wave sites do not contained any recent information. Some wave sites provide literature and research articles but all those wave site seldom disclose the source of those articles as such those articles could not be used as reference. Even some Banks are still new and have not yet start any welfare programs. As for example, Shahjalal Islami Bank Limited, Oriental Bank Limited (former Al-Baraka Bank Bangladesh Limited), Samil Bank of Bahrain EC, Exim Bank-Islamic Counters, Jamuni Bank Limited-Islamic Counters, Premier Bank Limited- Islamic Counters, The City Bank Limited Islamic Counter, Dhaka Bank Limited-Islamic Counters have not yet started any social welfare activities. They have agenda for social welfare but in practice they are sill not involved in any direct social welfare activities. So the researcher could not write anything about social welfare activities of those Banks. Moreover, Al-Arafah Islami Bank Limited has established Al-Arafah Islami Bank Foundation but the activities of this Foundation are very limited. Even Social Investment Bank Limited have various social welfare programs in theory but in practice they are very limited and yet to apply in practice.

The researcher collected annual reports from different Islamic Banks in Bangladesh in order to get some valuable secondary information from those reports. But unfortunately the researcher could not get very recent reports of most of the Islamic Banks. As such the researcher could not include current information of some Banks. Even all the Islamic Banks except Islami Bank Bangladesh Limited and Social Investment Bank Limited have yet to publish any booklets or literature about their social welfare activities.

Moreover, literature about Islamic Banking, finance and economics are very limited and not available in most of the libraries in Bangladesh. However this could not affect the quality of the research work because within the limited resources and time the researcher has been able to collect the requisite and available materials relating to the subject of her study and has completed the work up to her entire satisfaction as advised by the supervisor.

Chapter 2

Islamic Economy : Sources and Philosophical Background

Chapter 2

Islamic Economy : Sources and Philosophical Background

2.1 Concept of Islamic Economy

The recent past has witnessed a growing interest of the Muslim intelligentsia in the economic teachings of Islam. It is an induction of their increasing dissatisfaction with the dominant doctrines of economics and their failure to analyze and solve the problems of the Muslims. The Islamic economic order presents a ray of hope to the Muslim community to solve their economic problems.

Capitalistic and Socialistic economic orders have been subjected to criticisms on various grounds particularly on the end products of these systems in terms of economic injustice, untold human sufferings and miseries and loss of individual freedom.¹ Private property, freedom of enterprise, severe competition, great profit motive, harmful discrimination between the rights of the employers and those of employees, reliance on natural forces for growth, the principle of non-interruption by the state as the basic tenets of modern economics.² The track record of Capitalism is not very promising, 'overemphasis on the rights of individual ownership, freedom of enterprise and legislation of usury, etc. have developed anti-social character leading to the huge concentration of wealth in a few hands and pauperization of the masses at large'.³

Even in the industrially advanced countries the problems of unemployment, inflation, poverty amidst affluence, unequal distribution of wealth, frequent bouts

¹ Muhammad Loqman and Suraiya Najneen, "Islamic Economics : An Approach to Human Welfare : An Evaluation", *Thoughts on Economics*, Vol. 6, No. 2, April-June 1996, p. 34.

² Syid Abul Ala Mawdudi, *Islam Our Jadid M'ashi' Najuriyat* (Islam and Modern Economic Theories) (Delhi : Markaj Maktabah, Jamaat-e-Islam (Hind), 1980), p. 180.

³ Muhammad Loqman and Suraiya Najneen, *op. cit.*, p. 34.

of business recessions, environmental pollution and ecological imbalance, to name a few, still bedevil man's present life and threaten his future.⁴

The West has adopted 'Liberalism' as its ideology, and its belief and commitment to this ideology remains strong. From liberalism, those people living in the West have derived their social system (permissiveness), their political system (democracy), and their economic system (capitalism). Overemphasis on fulfillment of self-interest and extreme desire for profit has presented a society devoid of moral character, brotherhood, cooperativeness and fellow feeling. Man is a moral animal and no political and economic order can long survive except on a moral base.⁵ A strong condemnation of capitalistic economics comes from Syed Qutb⁶ who finds the economy to be thoroughly inhuman and unrealistic.

The defeat of socialism is too obvious to be documented after what has happened in Eastern Europe and the USSR during the last few years.

Islam gives us a comprehensive guidance in economic matters such as prohibition of interest, compulsory levy of Zakah, freedom of work and enterprise, concern for the poor, distinction between the Halal (Permissible) and Haram (Prohibited) in income, consumption and so on.

Of all the creatures on earth, man is the only one who carries the burden of responsibility: responsibility for his own welfare, responsibility for the wellbeing of his environment, responsibility before his lord, the creator of all things.⁷ Since Islam aims at constructing the entire edifice of human life and culture in the light of revealed knowledge from Almighty Allah, Islamic Economics too being an inseparable code of Islam, has got its welfare models

⁴ Muhammad Akram Khan, *An Introduction to Islami Economics* (Islamabad, Pakistan : The International Institute of Islamic Thought, 1994), p. 1.

⁵ Nigel Lowson, "Some Reflections on Morality and Capitalism", in Brittan and Hamlin (eds.), *Market Capitalism and Moral Values: Proceedings of Section (Economics) of the British Association for the Advancement of Science* (UK : Edward Elgar, 1995), pp. 35-44.

⁶ Sayyid Qutb, *Ma'rikat al-Islam Wa'l-un 'Saliyal* (Confrontation of Islam and Capitalism, 3rd ed. (Egypt, 1966), p. 1.

⁷ Muhammad Abdullah Rauf, *A Muslim's Reflections on Democratic Capitalism* (Washington : American Enterprise Institute for Public Policy Research, 1984), p. 1.

and principles for universal application for doing immense good to the whole mankind and as such, it might be a right claimant for helping the humanity to come out successfully from the present day's complex economic arena.⁸ However, the Islamic economic system does not mean any (given) system of detailed elaborate analysis that may be applicable at all times, in all places and under all circumstances. The Islamic code of life has brought some such fundamental principles on the basis of which a complete economic system can be framed at all stages, in all places and under all circumstances. In fact the holy Qur'an and the Sunnah of the Prophet(SM) have laid down the limits of all aspects and departments of human life. We have been ordained to frame the complete system of any aspect or department of life within the limits so defined. No body has the right to violate these limits. It is the duty and responsibility of the people of a period to frame, within the above limits, the detailed system of the time on the basis of the existing conditions, needs and experience. During the period following the Kaliphate our jurists devised, within the limits laid down by the holy Qur'an and Hadith, an economic system in the light of the conditions and requirements of the time.⁹

Islam views man as the agent of change through the Vicegerency (Khalifah) task assigned to him and through the accompanying free will given to him. Allah has appointed man as His deputy on this earth to carry out His will in the form of Shari'ah, which was finally revealed through Muhammad (SM) as His Messenger.¹⁰ The rules of Shari'ah cover economic, social, political and cultural life of Islamic community.¹¹

⁸ Muhammad Loqman and Suraiya Najneen, *op. cit.*, p. 34.

⁹ Muhammad Abdur Rahim, "The Philosophical Background of the Economics of Islam", *Thought on Islamic Economics* (Dhaka : Islamic Economic Research Bureau, August 1980), p. 308.

¹⁰ Muhammad Akram Khan, *Economic Teachings of Prophet Muhammad: A Select Anthology of Hadith Literature on Economics* (Islamabad, Pakistan : International Institute of Islam, 1989), p. 2.

¹¹ Syed Nawab Haider Naqvi, *Ethics and Economics: An Islamic Synthesis* (Leicester : Islamic Foundation, 1981) and Muhammad Abul Quasem, "The Islamic Doctrine of Economics and Contemporary Economic Thought," in Michael Novak (eds.), *Capitalism and Socialism: A Theological Inquiry* (Washington : The American Enterprise Institute for Public Policy Research), 1978.

The Islamic society is asked to organize economic matters in such a way that wealth does not continue to circulate only among the rich. Islamic Economics directs and organizes economic activities of mankind in accordance with Islamic fundamentals as well as their applications. The jurists have almost unanimously held the position that it is the duty of the whole Muslim society in general, and of its rich in particular, to take care of the basic needs of the poor, and if the well to do do not fulfill their responsibility in spite of their ability to do so, the state should compel them. The prophet(SM) stated: 'A Muslim is a brother of another Muslim; he neither wrongs him, nor leaves him without help, nor humiliates him'.¹² The Prophet (SM) stated: 'All Muslims in the world are like one man; if he feels pain in the eye, his whole body feels the pain; if he has pain in the head, his whole body suffers from pain'.¹³

Allah, as Qur'an points out, has created enough means on this earth to adequately meet the needs of all His creatures. It is then up to the human beings the Vicegerents of the earth to amply exploit and utilize the available resources to produce the goods they need and distribute them fairly. This process, however, involves ethical responsibilities for human beings - in the realms of what and how they produce, how they consume, and how they distribute. These are some of the areas where the economic teachings of Islam play an important role.¹⁴

'Allah would enquire from His men on the Day of Judgment as to how they treated Him when He came to them. I was naked, you did not clothe me; I was hungry, you did not feed me, etc. People amazingly would ask Allah how, could it be (for Allah) to be hungry or naked? He would reply that such and such of His men came to them destitute and the manner in which they treated them was in a sense treating Him". The Holy Quran states:

¹² Muslim, Quoted in Prof. Raihan Sharif, "Compatibility of the Socioeconomic System as a Base for Enduring Ideology", *Thoughts on Economics*, Vol. 1, No. 1, Dhaka, 1991, p. 27.

¹³ Ibid.

¹⁴ Irfan Ul Haq, *Economic Doctrines of Islam - A Study in the Doctrines of Islam and their Implications for Poverty, Employment and Economic Growth*, 1st ed. (Virginia, USA : International Institute of Islamic Thought, 1996), p. 89.

'Withhold not things unjustly due to others' (26:183)

'Deal not unjustly and ye shall no be dealt with unjustly' (2:279)

Community brotherhood and social justice requirements are opposed to unsocial inequality of wealth, income and means of production. The basic injunctions in Islam are aimed at taking steps such that concentration of wealth and income are discouraged. Thus the Islamic society is asked to organize economic matters in such a way that wealth does not continue to circulate only among the rich.¹⁵ "The jurists have almost unanimously held the position that it is the duty of the whole Muslim society in general, and of its rich in particular, to take care of the basic needs of the poor, and if the well-to-do do not fulfill their responsibility in spite of their ability to do so, the state should compel them."¹⁶

Thus Islam does not prescribe a particular system per se but provides the core elements that form the basic philosophy of a system or an economy. When an economy is developed on the basis of this philosophy and its accompanying goals and objectives, and it operates in accordance with the criteria of promoting public welfare in consistency with Islamic values, it can justifiably be called an Islamic economy.¹⁷

2.2 Sources of Islamic Economics

The guiding principles of Islamic economics and finance are derived from the following sources:

- (a) The Qur'an;
- (b) The Sunnah of the Prophet (SM)
- (c) Ijtihad or Exercise of Judgment
- (d) History of the Muslims

¹⁵ Raihan Sharif, "Compatibility of the Socio-Economic System as a Base for Enduring Ideology", *Thoughts on Economics*, Vol. 1, No. 1, Dhaka 1991, p. 28.

¹⁶ Ibid.

¹⁷ Irfan Ul Haq, *op. cit.*

2.2.1 Al-Qur'an

The original source from which all principles and ordinances of Islam are drawn is the Holy Book called Al-Qur'an.¹⁸ The name Qur'an is frequently mentioned in the book itself (2:185; 10:37, 10:61; 17:106, etc.). The book also states to whom, when, in what language, how, and why it was revealed.¹⁹ It is revealed to the Prophet Muhammad (SM) in the month of 'Ramadan' (2:185). It was revealed in the Arabic language. 'Surely we have made it an Arabic Qur'an that you may understand' (43:3). 'It was revealed in portions, every portion being written and committed to memory as soon as it was revealed, and the revelation of it was spread over twenty-three years of the Holy Prophet's life, during which time he was occupied solely with the reformation of a benighted world. It was not the Prophet who spoke under the influence of the Holy Spirit: it was a Divine Message brought by the Holy Spirit or Gabriel, and delivered in words to the Holy Prophet who delivered it to mankind'.²⁰ 'The Holy Spirit has brought it down from thy Lord with the truth' (16:102). It consists of 114 Chapters of varying length, each of which is called a Surah meaning literally eminence or high degree, and also any degree of a structure. All the chapters, with the exception of the last thirty-five, are divided into sections (Ruku), each section dealing generally with one subject, and the different sections being inter-related to each other. Chapter 2, the longest, comprises of 268 verses (in Quranic terms a verse is an ayah, meaning originally a sign or a communication from Allah) and Chapter 108, the shortest, consists of 3 short verses. It has been preserved since it was revealed. It was written during the life of the Holy Prophet (SM) and was duplicated for distribution shortly after his death. To all Muslims the Holy Qur'an is the most important book on earth.

¹⁸ Maulana Muhammad Ali, *The Religion of Islam: A Comprehensive Discussion of the Sources, Principles and Practices of Islam* (Lahore, Pakistan : The Ahmadi Yyah Arjuman Isha'at Islam, 1935), p. 17.

¹⁹ Ibid., p. 18.

²⁰ Ibid., pp. 18-19.

'Every verse of it, every word in it, every dot, comma or colon in it is Allah's and so it is valuable. Any knowledge from it is the most valuable knowledge'.²¹

Though the Holy Qur'an was revealed piecemeal, as pointed out above, yet the entire revelation is one whole, delivered in one and the same manner.²² It is the main source of Islamic guidance for the conduct of human beings. 'On economic matters, too, it provides a set of fundamental principles to guide human conduct. Consistent with these principles, the super-structure of the economy has to be built, in each age, according to the particular circumstances of that age. The injunctions of Al-Qur'an are immutable and applicable to all societies and are valid for all times to come. Al- Qur'an is thus the primary source of Islamic economics'.²³

2.2.2 The Sunnah of the Prophet (SM)

The Sunnah is the speech, action or tacit approval of the Prophet (SM) as recorded in the book of traditions.²⁴ It is the second source of Islamic law. It is next to Al-Qur'an in authority. 'Sunnah literally means a way or rule or manner of acting or mode of life, and Hadith, a saying conveyed to man either through hearing or through revelation. In its original sense, therefore, Sunnah indicates the doings and Hadith the sayings of the Holy Prophet; but in effect both cover the same ground and are applicable to his actions, practices, and sayings, Hadith being the narration and record of the Sunnah but continuing, in addition, various prophetic and historical elements..... Any student of the Holy Qur'an will see that the Holy Book generally deals with the broad principles or essentials of religion, going into details in very rare cases. The Holy Prophet(SM) himself generally supplied the details, either by showing in his practice how an

²¹ Ibrahim Hassan Hannatu, "Economic Teaching of the Holy Qur'an", in Dr. Sule Ahmed Gusau (eds), *Islam and the Contemporary Economic Problems* (Sokoto, Nigeria : Department of Economics, Usman Danfodiyo University, 1992), p. 3.

²² Maulana Muhammad Ali, *op. cit.*, p. 20.

²³ Muhammad Akram Khan (1994), *op. cit.*, p. 49.

²⁴ *Ibid.*, p. 50.

injunction shall be carried out or by giving an explanation in words'.²⁵ The Ahl Sunnah generally recognizes six books under the heading, being the collections made by Muhammad ibn Ismail, commonly known as 'Bukahari' (d. 256 A.H.), Muslim (d. 261 A. H.), Abu Dawud (d. 275 A.H.), Trimidhi (d. A.H.), Ibn Majah (d. 283 A. H.) and NasaI (d. 303).

'The literature on traditions of the Prophet (SM) covers the entire orbit of life, including the economic aspects. Although most of the traditions are general and applicable for all times there are some whose relevance is time-bound. Therefore, the knowledge of the exact status of each tradition is essential to understand its relevance for the present age. Knowledge of the traditions containing injunctions about economic activities is an essential part of the training of Muslim economists'.²⁶

2.2.3 Ijtihad or Exercise of Judgment

Ijtihad is the third source from which the Islamic laws including economic laws are drawn. It is the means by which a decision may be arrived at when there is no direction in the Holy Qur'an or Hadith. The word itself is derived from the root 'jahd' which means exerting oneself to the utmost or to the best of one's ability, and Ijtihad, which literally conveys the same significance, is technically applicable to a lawyer's exerting the faculties of mind to the utmost for the purpose of forming an opinion in a case of law representing a doubtful and difficult point.²⁷ Reasoning or the exercise of judgment, in theological as well as legal and economical matters, plays a vital role in Islam, and the value of reasoning is recognized in the Holy Qur'an. Those who do not exercise their reasoning faculty are condemned. 'They have hearts with which they do not understand, and they have eyes with which they do not see, and they have ears with which they do not hear; they are as cattle; nay, they are in worse error'

²⁵ Maulana Muhammad Ali, *op. cit.*, p. 58.

²⁶ Muhammad Akram Khan (1994), *op. cit.*, p. 50.

²⁷ Ibid.

(7:179). The Qur'an recognizes revelation as a source of knowledge higher than reason, but at the same time admits that the truth of the principles established by revelation may be judged by reason, and hence it is that it repeatedly appeals to reason and denounces those who do not use their reasoning faculty.²⁸

The following Hadith is regarded as the basis of Ijtihad in Islam: "on being appointed Governor of Yemen, Mu'adh(R) was asked by the Prophet(SM) as to the rule by which he would abide. He replied, 'by the law of the Qur'an'. 'But if you do not find any direction therein, asked the Prophet(SM). 'Then I will act according to the Sunnah of the Prophet(SM)', was the reply. 'But if you do not find any direction in the Sunnah,' he was again asked. Then I will exercise my judgment (ajtahidu) and act on that,' came the reply. The Prophet(SM) raised his hands and said: 'Praise be to Allah Who guides the messenger of His Messenger as He pleases" (Abu Dawud, 23:11). This Hadith shows not only the Holy Prophet(SM) approved of the exercise of judgment, but also that his companions were well aware of the principle, and that Ijtihad by others than the Prophet was freely resorted to when necessary, even in the Prophet's lifetime.²⁹

The great Mujtahids of Islam tried their best to meet all the legal requirements of the Muslims - religions and secular, adopting various methods of Ijtihad, such as, Ijma (Ijtihad of many) Qyias (analogical reasoning). Before proceeding further, a brief description of these methods may be given to show how new laws are evolved by adopting them.

2.2.3.1 Ijma (Consensus of the Opinions of Jurists)

Ijma means of consensus of opinions of the companions of the Prophet(SM) or of Muslim Jurists (Mujtahids) of any particular era on a particular question of law, the solution of which cannot be directly trace into Holy Qur'an and Hadith.

²⁸ Ibid., p. 97.

²⁹ Ibid.

All the four Sunni Schools of Islamic Jurisprudence have accepted the validity of Ijma as a source of laws. The election of Hajrat Abu Bakar to the Khilafat by the unanimous votes of the people is the first instance of Ijma in Islam. According to the accepted opinion of the Muslim Jurists only the Mujtahids alone have a voice in Ijma. An Ijma is absolute and binding of the Muslims when all the Muslim jurists of the age unanimously agree on a particular question of law.³⁰

Thus Ijma is Ijtihad on which all or majority of the Mujtahids of a certain generation are agreed and the Ijma of one generation of Muslims may be set aside by the Ijma of another generation except the Ijma of the companions of the Holy Prophet. Ijma is widely used in settling different contemporary issues in Islamic economics and finance.

2.2.3.2 Qiyas

It is an analogical deduction from Qur'an, Hadith and Ijma. All the Sunni Schools of Jurisprudence agree that in matters which have not been provided for by any Quranic verse or Hadith or by the consensus of the jurists the law may be deduced from any of these authorities by the use of Qiyas. Imam Sbu Hanifah was the first man who directed attention to the great value of Qiyas or analogical reasoning in legislation. But it is not equal to the previously mentioned sources and the Qiyas of one generation may be rejected by a following generation. It is one of the most important sources of law relating to Islamic economics and finance.

2.2.4 History of the Muslims

The history of the Muslims contains much scattered material about the economic life of the people. But the economic history of the Muslims has not yet

³⁰ Md. Shahadatullah, "Principles of Islamic Shari'ah and Jurisprudence in Relation to Financial Transactions", in A.K.M. Fazlul Haque (eds), *Readings in Islamic Banking* (Dhaka : Islami Bankers Association, 1984), p. III-5.

been chronicled except for some elementary accounts of the early period. We hope that with the growth of the subject the historical sources will also develop.³¹

2.3 Philosophical Background of Islamic Economics

There is a philosophy behind every sphere of science and learning as there is a seed behind the origin of every tree.³² The sphere of economics is one of the aspects of complete Islamic code of life. The fundamental philosophy of the Islamic code of life is also the philosophy of Islamic Economics. Thus to get ourselves convinced in accepting Islamic economics as an approach to human welfare, we need to understand the relationship between religion and economics from philosophical point of view. It is a morally directed economy, being part of a whole moral philosophy: Islam. Islam has its own view about the way man recognizes his economic activities. The well-known Iranian economist Abbas Mirakhar recently wrote, 'Islam posits a priori, a unique relationship between Allah, man, society and the divine law. This relationship directly affects the workings of the economic system'.³³ Islam suggests a unique relationship between, Allah, man, society and Divine law, which has a direct impact on the economic system. Man is the vicegerent of Allah on earth. 'He is responsible to develop his potentialities and create a just, moral social order on earth. To discipline his life, he is provided with a network of injunctions, attitudes and rules that represent Divine will. This includes specific codes of behavior, and by accepting this through his free choice; a person becomes Muslim and lives his private, social and economic life according to these codes'.³⁴

³¹ Muhammad Akram Khan, *op. cit.*, p. 51.

³² Abdur Muhammad Rahim, *op. cit.*, p., 20.

³³ Abbas Mirakhor, "The Economic System in an Islamic Society", *Middle East Insight*, Vol. 5 (Washington D.C. : International Insight, Inc., 1987), p. 32.

³⁴ Kabir Hassan and Shah Abdul Hannan, "An Inquiry into the Contribution of Islam to Modern Economic Science", *Thoughts on Economics*, Vol. 4, No. 1 & 2, Dhaka, January-June 1994, p. 2.

Acquisition of material goods and services is a normal phenomenon of life. Allah has created sustenance for all His creation. Qur'an states, 'He has made for you the earth 'spread out (like a carpet)' (43:10).

'All that the earth contains is created for your benefit' (2:29). But material gain is the means not the end. 'Islam advises human being to earn material gain to help make the life a success in hereafter. And the success of life in hereafter completely depends on worldly activities guided within ethical framework'.³⁵ Thus the material dependency along with ethical values focuses the characteristics of Islamic economy.

Islamic economic ethics and norms are founded on Qur'anic - Sunnatic values. However, they are subjected to interpretation through Ijtihad for efficiency and public interest purposes.

The main streamline of Islamic philosophy is based on three ethical aspects, such as Tawhid, Resa'lat and A'khirat. Now we will explain the framework under which the concept of Tawhid, Resa'lat and Akhirat influence the Islamic economics.

2.3.1 Tawhid

'Tawhid' or unity of Allah is the basic consideration for the Islamic way of life. 'Tawhid' implies that the universe has not come into existence without a creator and that creator is Allah. He is one and none is here in this universe to share his power or authority. He is not only the creator but also the director and controller of the whole universe. He is the sole Owner of the entire wealth, resources, land, power and authority of the world. Man is the representative of Allah on earth. 'This caliphate is not only in politics; it extends to the sphere of economics also. In the terminology of Political Science it may be stated thus- the

³⁵ Md. Abdul Jabbar, "Philosophical Background of Islamic Economics", *Thoughts on Economics*, Vol. 1, No. 1, Dhaka, 1991, p. 64.

Sovereignty of Allah exists not only in the domain of politics but also in that of economics. And the later is more significant'.³⁶

Allah has suggested laws for human beings. The entire human life, all its affairs and activities are to be guided by these Laws. 'The key to economic philosophy of Islam lies in man's relationship with Allah, His Universe and His people, i.e. other human being, and the nature and purpose of man's life on earth'.³⁷ Thus Tawhid lays the rules of Allah-man and man-man relationship. It is a coin with two faces: one implies that Allah is the creator and the other that men are equal partners or that each man is brother to other men. Tawhid is based on the above two axioms. The first axiom has two aspects: (a) everything on heaven and earth has been created (b) the creator is Allah and He has no partner. Qur'an states.

'If there were, in the heavens and the earth, other Gods besides Him, there would have been confusion in both' (21:22).

'It is He who created all things and ordered them in due proportions. He created the Sun, the Moon, and the Stars. Laws under His command govern all. He rules all affairs from the heavens to earth.' Thus Almighty Allah is the only creator. He has created every thing on heaven and earth. Man's ownership of property is merely a trusteeship. Allah Himself is the real owner. 'To Him alone belong all that is in heaven and all that is in the earth and all that is between them, and beneath the soil' (20:6).

Your brothers are your servants. Feed them from what you eat, dress them from same quality of your own clothes, and do not charge them with a burden beyond their ability; if you should do, you must assist them.³⁸

³⁶. Abdur Muhammad Rahim, *op. cit.*, p. 306.

³⁷ S.M. Ali Akkas, "Theoretical Foundation of Islamic Economics", *Thoughts on Economics*, Vol. 8, No. 1 & 2, Dhaka, July-December 1998, p. 44.

³⁸ Sahih Muslim, Vol. 11, pp. 132-133.

While the second axiom, the universal brotherhood, suggests that human beings are descendent of Hadrat Adam and Hadrat Hawa. Human beings should love one another as brothers of Islam. 'Oh, mankind, I have created you from one single pair of a male and female' (49:13).

'Mankind was one single nation but differed later' (10:19).

'Oh servants of Allah, live as brethren (one another)' (Muslim).

Implications of brotherhood concept are equality and co-operation. The concept of brotherhood is given emphasis in the Holy Qur'an as a means of improving people's welfare and enhancing development.

'..... help ye one another into righteous and pious duty,' (5:2). 'They belong to me (spiritually) and I belong to them," the Prophet(SM) spoke praising the Ash'arite tribe of the Yemen, because, he said, "In time of hardship, they pooled together all food they possessed for their common benefit, sharing it equally'.³⁹

By Allah, he is not a true believer; he who goes to bed with a full stomach while his neighbor is hungry.⁴⁰ Islam enjoins that human beings should help each other, share the bounties of Allah with each other and cooperate with each other in all that are good. The Qur'an reads, 'Help you one another in benevolence and piety, but help you not one another in sin and rancour' (5:2). Similarly, there are many verses that call on believers to spend from their own wealth on the kith and kin, on orphans and the needy, on the wayfarer and in the general welfare of society and humanity at large. The Qur'an says: 'Believe in Allah and His apostle and spend on others out of that which He has made you trustees of, for those of you who have attained to faith and who spend (in His cause) shall have a great reward' (57:7).

³⁹ Muhammad Al-Mubarak, *Nizam Al-Islam Al-Iqtisad* [The Economic System in Islam] (Beirut, 1978), p. 134.

⁴⁰ Al- Musnad, Vol. 1, p. 55.

'So give the kinsman his due and to the needy and to the wayfarer, that is for those who seek Allah's countenance and such are successful' (30:38). Islam comes in for removal of the inequalities, for establishing full co-operation, harmony and justice through its own moral, political, social and economic codes'.⁴¹

Thus the responsibility of man is to materialize the sole ownership of Allah on all worldly resources. The only way to implement this philosophy is to conduct the whole affairs of production, consumption, saving, utilization, distribution, preservation, etc. of wealth according to the divine rules suggested in the Holy Qur'an and not in accordance with the doctrines and system derived from the thought and imagination of human being.

2.3.2 Resa'lat

The Almighty Allah has selected his representative from among men to promulgate His divine rules. 'The Arabic word for prophet is 'Nabi'. A Nabi is the man who gives information about Allah, and this is further explained as the man to whom Allah gives information concerning His Unity and to whom He reveals secrets of the future and imparts the knowledge that he is His prophet. A Nabi is also called a Rasul, which means an apostle or messenger. The two words Nabi and Rasul are used interchangeably in the Holy Qura'an, the same person being sometimes called a Nabi and sometimes called Rasul; while occasionally both names are combined. The reason seems to be that the Prophet(SM) has two capacities, viz., he receives information from Allah, and he imparts the message to mankind. He is called a Nabi in the first and a Rasul in his second capacity, but there is no difference'.⁴² According to Holy Qur'an, there is not a nation in the world in which a prophet has not been raised up. 'Every nation has had a messenger' (10:47). A belief in all the prophets of the world is thus an essential principle of the religion of Islam, and though the faith of Islam is summed up in two brief sentences, there is no god but Allah and

⁴¹ Muhammad Abdur Rahim, *op. cit.*, p. 310.

⁴² Maulana Muhammad Ali, *op. cit.*, p. 219.

Muhammad(SM) is His Messenger, yet man who confesses belief in Muhammad(SM), in so doing accepts all the prophets of the world, whether their names are mentioned in the Holy Qur'an or not'.⁴³

The Holy Qur'an has prescribed basic guidelines for life. And the Prophet (SM) had explained and implemented those guidelines into practice.⁴⁴ To execute divine guides, the Prophet(SM) required establishing an integrated social, economic and political system. In economic arena all the problems have been dealt with the basic principles of Islam. And it is the demand of the time to find out Shari'ah based ways in handling different complicated and contemporary economic issues.

There are questions of production, distribution, exchange of views, price determination, savings, formation of capital, employment, wage-rate, surplus value, determination of rights on earned resources etc. The prophet has been sent to give the basic principles for regulating the above. Hence, it is the demand of time to find out various ways to be applied in accordance with divine guidelines.⁴⁵

2.3.3 A'khirat

Faith in a life after death is the last of the basic principles of Islam. The world generally used in the Holy Qur'an to indicate this life as al-akhirah; and akhir is the opposite of awal (which means the first), and thus signifies that which comes after or the future, or the last.⁴⁶ 'What is the life of this world but play and amusement? But best is the home in the hereafter, for those who are righteous. Will ye not then understand?' (6:32). 'Whoever believes in Allah and the last day and does good, they shall have their reward from Allah' (2:62). 'And whoever is blind in this life shall also be blind in the Hereafter' (17:72). Thus, 'human beings are accountable to the Almighty Allah for his deeds or misdeeds he does herein. He

⁴³ Ibid., p. 223.

⁴⁴ Md. Abdul Jabbar, *op. cit.*, p. 65.

⁴⁵ Ibid.

⁴⁶ Maulana Muhammad Ali, *op. cit.*, p. 264.

must have to reply in hereafter for all his works and receive reward or punishment accordingly. This sort of belief producing controlling sense 'having been inside an individual is an effective tool to regulate every aspect of life'.⁴⁷

The scope of study in the Islamic economics is entirely different from the western economics. It studies and suggests means to achieve falah rather than material well being of the people. Falah is a materially advanced life in this world plus a successful life in the Hereafter. The Islamic economics endeavors to study the relationships, which ensure falah for man. This obviously is a much wider field of study.⁴⁸

2.4 Ownership of Resources from Islamic Viewpoint

Islam recognizes the right to absolute ownership of resources for Allah only. Everything in this universe belongs to Almighty Allah (2:284). He is the real owner of everything (2:107), (3:189), (5:17), (5:18), (5:40), (5:120), (67:1) and has the right to determine the mode of utilization of all forms of property (6:57), (12:67), (28:70), (28:88). 'To Allah belong to all that is in the heavens and on earth.....' 3:109, 4:137, 10:55, 10:66, 11:23). Allah in His mercy allows human beings to inherit wealth, own it and use it subject to His laws as evident from the following verses :

- i) The land belongs to Allah. He allows it to be inherited by whomsoever he pleases (7:128).
- ii) Do they not see that we have created for them ----- among the things fashioned by us ---- cattle of which they become owners?

In early Islam there were three kinds of ownership: private, common and state ownership.

The right to private ownership is qualified by the principle of vicegerency. This is the most important element that characterizes an Islamic economic

⁴⁷ Md. Abdul Jabbar, *op. cit.*, p. 66.

⁴⁸ Muhammad Akram Khan (1989), *op. cit.*, p. 4.

system. It implies that the individual can own whatever he/she wants to, provided that what he/she owns is used for the purpose for which they were created, that their use does not hurt anybody (including the owner), and its use causes growth'.⁴⁹ Human being has been granted the right to benefit from the resources of the earth. Islam recognizes private ownership within given limits. Man is allowed to earn his livelihood through lawful (Halal) means. He is not totally free to consume, save or invest his earnings in any way he likes. There are definite moral limits on his right to earn, consume, save and invest. Within this general framework, Islam accepts the right of a person to sell bequeaths and leaves for heirs the property, which he happens to own. Thus the Islamic concept of property limits human freedom to the use of the resources of the earth. It holds everyone accountable to Allah for the proper use of those resources at the termination of this worldly life and placed at his disposal as vicegerent to Allah (8:28), (39:49), (64:15). The requisite mode of utilization of resources has been granted in the Shari'ah. "To ensure an uninterrupted discretion to use these resources, the Shari'ah has recognized the right to own property as legitimate and authentic; this right has been conceived in the overall framework of Allah's sovereignty."⁵⁰ Ownership in the Islamic concept is not the right to use and abuse the possessed objects as capitalists claim, but is the obligation to look after the bounty of Allah entrusted to His servants who are commanded to make the best use of it and to use it for the good of themselves and others.⁵¹ Thus the private ownership accorded by Islam is not absolute and unconditional. This ownership does not afford the right to earn, produce, spend (consume) and invest as one likes. The ownership is a kind of trust only..... He is to regulate the uses as per the laws of Allah, the real owner. He has no right to make any violation of these laws'.⁵²

⁴⁹ Abu-Saud Mahmoud, "The Islamic Economic Framework : A Conceptualization", in Zaidi Sattar (eds), *Resource Mobilization and Investment in an Islamic Economic Framework*, 1st edition, Proceedings of the Third International Islamic Economics Seminar, 1990 (Herndon, Virginia : The International Institute of Islamic Thought, 1992).

⁵⁰ Muhammad Akram Khan (1989), *op. cit.*, p. 8.

⁵¹ Abu-Saud Mahmoud, *op. cit.*, p. 12.

⁵² Muhammad Abdur Rahim, *op. cit.*, p. 311.

Islam has also recognized a right of common ownership in certain things such as water, grass, fire, pastures and graveyards. They are for common good and cannot be owned by anyone including the state. Instead, everyone is equally entitled to derive benefit from those common things.⁵³ The state owned mines, rivers and large tracts of land. After the conquest of Syria and Iraq, these lands were made state lands and were not allowed to go into private ownership.⁵⁴

Islam considers wealth as the lifeblood of the community, which must be constantly in circulation; therefore, its possession excludes the right of hoarding. The implication is that lawfully earned wealth must be invested within the community to improve its economic wellbeing. Investing wealth is not only measured by the monetary gain associated with it, but also by the benefit, which accrues, to the society. The needs of the society, therefore, must be a consideration for the owner of wealth.

Wealth has been a subject of study since time immemorial. In Islam wealth does not hold a central position in the social matrix. Instead it has been visualized, as an instrument to lead life on this earth is to obey the commandment of Allah and to implement His will as His vicegerent.⁵⁵ The Quran says: 'And (remember) when your Lord said to the angels, verily I am going to make a vicegerent on the Earth (2:30). 'Eat of the provisions of your Lord and render thanks to Him (34:15). 'And strive with your wealth and your lives in the way of Allah' (9:15).

Allah has created resources for all human beings and has made man their trustee. Allah would like man to use these resources to achieve falah. The fundamental idea is that the attainment of wealth should not be the focus of all activities of the world. Instead wealth should be acquired, prepared and used to attain a higher level in the obedience of Allah. This is the major point of

⁵³ Muhammad Akram Khan (1989), *op. cit.*, p. 8.

⁵⁴ Syed Abul Ala Maududi, *Tafhimul Quran, Tafsir of Surarur Hasr*, Vol. 17. (Dhaka : Adhunik Prokasoni, 2000).

⁵⁵ Muhammad Akram Khan (1989), *op. cit.*, p. 15.

departure from the Western concept of wealth, where economic pursuits have come to occupy a central place in the life of the individual and state.⁵⁶

According to Islamic scholars man is not the real owner of resources and he is not independent in deriving benefit from them. He is required to harness the benefits from those resources according to the directives of Allah. Moreover, Allah has created everything on this earth with a specific purpose. The resources of the earth are meant to provide livelihood to the creatures of Allah. Therefore, no one should block these resources for his own self as well as others of their use. The Prophet(SM) said that 'whosoever makes accumulation of wealth the ultimate aim of life, Allah will make the specter of poverty ever present in front of his eyes'.⁵⁷ 'Should the son of Adam get in his possession so much gold as to fill a wide valley, he will still crave for more'.⁵⁸

Islam does not regard the accumulation of wealth as a blameworthy pursuit, even when the motive is the individual's craving for greater security or his desire to improve his worldly material condition. The only stipulation, as indicated earlier, is that wealth should be earned through lawful, honest means and that the alms due to the poor are fully paid. The prophet said: 'No matter how much wealth you may accumulate, you gain from it only what you eat, which perishes; and what you dress, which wears away; and what you pay in charity, which lasts for you! That which remains will only benefits your heirs!'.⁵⁹ Three things follow a dead person on his journey to his grave; his family, his wealth; and his deed. As soon as he is laid to rest in his grave, his family and his wealth forsake him, and only his work will remain with him in his grave.⁶⁰ The overall spirit of Islam is that either one should use the resources one has come to possess or release them for others.

⁵⁶ Ibid.

⁵⁷ Ibn Majah Sunnan, Vol. 18, p. 1375.

⁵⁸ Sahih Muslim, Vol. 7, pp. 138-139.

⁵⁹ Sahih Muslim, Vol. 4, pp. 24-26; Vol. 18, p. 94.

⁶⁰ Ibid, Vol. 18, p. 95.

Allah has created sufficient resources for His creatures (41:10). Therefore, the apparent scarcity of resources may be either due to their improper use or imbalance distribution. Islamic economics studies resources from the point of view of 'adequacy' rather than scarcity. It is not the main object of Islamic economics to study the allocation of 'scarce' resources on multiple ends, which is the focus of mainstream economics. Islamic economics is mainly concerned with the *falah* of the people. It starts from the premise that the natural resources of the earth are adequate to achieve *falah*. Therefore, if some degree of 'scarcity' is being encountered, ways and means should be found to restore the natural state of adequacy. This could probably be achieved by broadening the resources or curtailing human wants. Scarcity of resources is a man-made situation and Islamic economics explores the ways and means to rectify it. There is also a moral dimension to this question. Man is accountable for his deeds in the life hereafter. He will also be held accountable for manner in which he uses these resources. Islam lays down standards propriety for acquisition, utilization and transfer of resources. These standards have a high moral content. Islamic economics takes into account these standards and judges human behavior in their light.

The motive behind accumulating wealth for its own sake or for the sake of greater security is not regarded as a sin so long as it does not lead to prohibited practices such as gambling and trading in liquor and provided that alms are duly given. The danger arises when wealth becomes the focus of attention, because then Allah and the desire to serve him is no longer central.⁶¹ As the Qur'an therefore warns:

O you who believe! Let not your wealth or your children distract you from remembrance of Allah. Those who do so are indeed losers (64:9).

⁶¹ Muhammad Abdullah Rauf, *op. cit.*, p. 8.

Your wealth and your children are only sources of temptation; whereas Allah! With Him is an immense reward (64:15).

Islam has given human beings certain rights in the wealth of the individuals. The Holy Qur'an has reportedly mentioned about meeting the rights of the near relatives after meeting the rights of Allah and the parents. Following the rights of relations, the neighbors and the needy have been given rights in the wealth of the well to do of the society. There is high presser to safeguard these rights. There are also orders to spend in the way of Allah.⁶²

⁶² Abdur Muhammad Rahim, *op. cit.*, p. 313.

Chapter 3

Banking in Islam : Genesis and Development from Historical Perspective

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3.1 Concept of Islamic Banking

Modern banks both conventional and Islamic – play a catalytic role in the economic development of a country. Banks mobilize the society's savings for investment in productive avenues and act as middlemen between the savers and businessmen. It also provides essential financial services as well as facilitates for domestic and international trades. The basic difference between the two banking systems is that Islamic-banking business operates on the principle of interest-free transactions; on the other hand conventional banking business runs on the principle of interest oriented transactions. However, in true sense, Islamic banking is much more than the conventional banking. A fixed return scheme (FRS) is the backbone of the western financial system. It is prohibited under the Islamic system for moral as well as economic reasons. The fundamental sources of Islam are the Holy Qur'an and Sunna (teaching and traditions) of the Prophet(SM), which provide guidelines for all economic activities, behavior and a blueprint of how the economic system should be organized. "We recognize capitalism as an economic system, though its basic characteristics are only the recognition of the private right of ownership and freedom of economic activity for the individual. Likewise, socialism is treated as an economic system, even though its only basic characteristic is the social ownership of means of production. Islam gives us a much more comprehensive guidance in economic matters such as prohibition of interest, compulsory level of Zakah, freedom of work and enterprise, concern for the poor, distinction between the Halal (permissible) and Haram (prohibited) in income, consumption and production and so on".¹

¹ Shah Abdul Hannan, "Objectives and Characteristics Features of Islamic Economy," *Readings in Islamic Banking* (Dhaka : Bangladesh Islamic Bankers Association, 1984), pp. II-1.

Islamic banking is an inseparable part of Islamic economic and financial system as well as Islamic value system. In all banking policies whether lending, investment, fund allocation or whatsoever there is a gulf of difference between conventional banking and Islamic banking. "The western style banks assures guaranteed return to the depositors (at a pre-fixed rate), leaving the risk of investment entirely to the borrowers. Islamic banks seek to achieve a just balance among the interests of all the parties i.e. depositors, bankers and the businessmen by realizing and sharing variable return. The former operates on rigid fixed cost (interest) basis; contrarily the latter operates on variable cost and variable return (profit & loss) basis, allowing for necessary flexibility, according to the conditions in the economy. An Islamic bank is not only a financier but also a partner to care for the success of the financial activity/enterprise. The near consensus amongst Islamic economists suggests that while Islam wants to discard all fixed return (interest) schemes in respect of investment operations it aims on establishing an economy where equity participation becomes the chief mode for financial operations.

Islamic economics is as old as Islamic civilization, while Islamic economics is a new phenomenon. The Islamic-banking concept has come into practice in the late 20th century. The idea of an interest free bank remained a blue print for a long time, while the introduction of Islamic banking is not more than three decades. Islamic banks are financial institutions that operate with the objective of implementing and materializing the economic and financial principles of Islam in the banking arena. Islamic banking in the modern context came into being in the early 1970s, when research institute focusing on Islamic economics and finance began to spread throughout the Muslim world. In early 1974 the organization of the Islamic Conference (OIC) summit in Lahore voted to create the inter-governmental Islamic Development Bank (IDB). This became the cornerstone of a new banking system inspired by religious principles.

The Organization of Islamic Conference (OIC) define an Islamic bank as "a financial institute whose statutes, rules and procedures expressly states its commitment to the principles of Islamic Shari'ah and to the banning of receipt and payment of interest on any of its operations" Islam not only prohibits dealing in interest but also liquor, pork, gambling, pornography and anything else, which the Shari'ah (Islamic Law) deems Haram (unlawful).

Thus Islamic banks provide finance and financial services in any *Halal* (lawful) activity which lead to mutual benefit of both the parties involved in any transaction.

3.2 Genesis and Historical Development

In Muslim community, limited banking activity, such as acceptance of deposits, goes back to the time when the Prophet Muhammad(SM) was still alive. At that time, people deposited money with the Prophet(SM) or with Abu Bakr Seddiq (R), the First Caliph of Islam. Since then credit societies and charitable trusts that lend money to deserving citizens on an interest-free basis have existed throughout the Muslim world.

Prophet Muhammad(SM) introduced the system of Bayt al-Mal (Public Exchequer) for collection and disbursement of revenues among the displaced Muhajirs and needy Ansars. "The Bayt al-Mal came to be identified as a trust of Muslims and Caliph was its trustee. He was accountable for each penny spent from it".² Whatever, came as Zakah, Ghanimah, Jizyah (Tithe) and Kharaj were distributed then and there by the Prophet(SM). Hadrat Abu Bakr Siddiq(R) followed the Prophet(SM). He distributed ten dirham to every one in the first year and twenty dirham to every one in the second year of his Khilafat (13-14H/ 632-34A.D). The non-Muslims were also allowed to get financial assistance form Bayt al- Mal.³

² Muhammad Akram Khan, *Economic Teachings of Prophet Muhammad: A Selected Anthology of Hadith Literature on Economics* (Islamabad : International Institute of Islamic Economics and Institute of Policy Studies, 1989), pp. 172-173.

³ S.M. Imamuddin, "A Historical Background of Modern Islamic Banking", Md Sharif Rushdi (eds.), *Thoughts on Islamic Banking* (Dhaka : Islamic Economics Research Bureau, 1982), p. 175.

Hadrat Umar Faruq (R), the second Caliph of Islam (13-14H/632-34 A.D), did census of the Muslims and appointed a Diwan to keep the records of the recipients of pensions and to deal with the social welfare of the people of the expanding Islamic state. Hadrat Umar's (R) proposal for establishing a permanent treasury at Madinah and its branches in the provinces was approved by the Majlis al-Shura in about 15H/636-7 A.D. The head of the provincial Bayt al-Mal was the Amir and that of the centre the Caliph himself. The main sources of revenue were Zakah, Ghanimah, Sadaqa, Jizyah, 'Ushr and Kharaj, taxes on mines, Khums and al-Fayy land (income from state lands). The income from Zakah paid by the Muslims formed the part of revenue resources of Bayt al-Mal al-Muslimin and was spent on the needy and indigent Muslims, collectors of Zakah, the emancipation of slaves, military enterprises, debtors, and thieves etc. This ideal tax, which is levied on idle as well as productive wealth, discourages the accumulation of wealth and ensures its investment for productive and beneficial purposes. 'Zakah is a major instrument for providing social security, eradicating poverty, curbing excessive economic disparities, and stimulating economic activity by transferring substantial purchasing power to the have-nots'.⁴ Ghanimah is the wealth obtained during the wars, one-fifth of which was deposited in the Bayt al-Mal. The Jizyah is a tax levied on non-Muslims only. The amount of Jizyah is much less than the Zakah. The non-Muslims paying Jizyah were exempt from compulsory military service in a Muslim state but were entitled to full protection. The Jizyah being a military tax was collected from able and earning adult members of the Dhimmis only when the Muslims were sure of giving protection to the life and property of the protected non-Muslims. The Kharaj is the annual levy paid by the conquered countries to the Muslims. The income from earliest al-Fayy land was spent for the Prophet's relatives, the orphans, the indigents, and the beggars and for the general welfare of the Muslim community.⁵

⁴ Muhammad Akram Khan, *An Introduction to Islamic Economics, The International Institute of Islamic Thought* (Islamabad : Institute of Policy Studies, 1994), p. 81.

⁵ S.M. Imamuddin, *op.cit.*, pp. 176-177.

The Public treasury of Bayt al-Mal also played the role of an agricultural credit bank and also a commercial bank from the early days of the Umayyads. Hajjaj b. Yusuf (D. 73H/714 A.D.), the great economist, according to the Muslims geographer Ibn Khurdadbiḥ (d.229-33H/844-884 A.D.), had lent to the peasants two million dirham from Bayt al-Mal without interest.⁶

During the time of Abu Musa al-Ash'ari, the governor of Kufah, Ubayd Allah ibn 'Umar borrowed money from the public treasury of Basrah, bought goods and sold in Hijaz and paid to the Bayt al-Mal of Hijaz at Madinah what he owed to that of Basrah. This type of loan is called Muda'raba. 'In these arrangement people with surplus money entrust their funds to those who have the skills and experience for utilizing it for productive purposes. The amount of return on the fund invested in Muda'raba is not pre-determined. The amount of profit (or loss) depends on the operational result of the economic activity undertaken. Profits to be distributed between the provider of funds and the businessman in any agreed proportion'.⁷ Any loss resulting from an unsuccessful business venture is borne exclusively by the investor(s); the borrower is in no way liable for a loss of this nature, loosing only his expended time and effort.⁸

Money lending through Muda'raba was an institution in Pre-Islamic period and Islam confirmed it. It was in existence in Babylonian and several other countries in the olden times. It was also prevalent in Arabia long before the advent of Islam. The Holy Prophet (SM) allowed this practice and his companions followed it. The Holy Prophet (SM) involved in Muda'raba contract with Hadrat Khadija(R). Hadrat Umar(R), Hadrat Usman(R) and Hadrat Abu Musa Ashaari(R) were also involved in Muda'raba contracts. Hadrat Aisha (R) and Hadrat Abdullah b. Umar(R) used to invest orphans' money and other

⁶ Ibid., p. 177.

⁷ Nawazish Ali Zaidi, *Eliminating Interest from Banks in Pakistan* (Karachi, Pakistan : Royal Bank Company, 1987), p. 178.

⁸ Abraham L. Udovitch, *Partnership and Profit in Medieval Islam* (New Jersey : Princeton University Press, 1970), p. 180.

money left in their safekeeping in Muda'raba.⁹ Imam Sarakshi states: "On the authority of Qasim bin Muhammad who said, we had some money (as deposit) in the hands of Hadrat Aisha (R). She used to invest it on Muda'raba. Allah blessed us and gave profit through her effort".¹⁰

Now it is the most popular technique of financing among Islamic banks and about two-thirds of the financial operations of some Islamic banks belong to this category. Hence it may be inferred that the concept and foundation of the Islamic banking had been developed fourteen hundred years ago during the lifetime of the holy prophet(SM).

In recent years steps have been taken towards Islamization of banking and financial system in a number of Muslim countries in the Middle East, Africa and Asia. The abolition of interest is the fundamental issue in Islamization of banking.

The history of interest-free banking could be divided into two parts. First, when it was an idea; second, when it became a reality -- by private initiative in some countries and by government initiative in others.

3.3 Islamic Banking as an Idea

Islamic banking is a very recent origin. The earliest references to the reorganization of banking on the basis of profit sharing rather than interest are found in Anwar Qureshi (1946), Naiem Siddiqi (1948) and Mahmud Ahmad (1952) in the late forties, followed by a more elaborate exposition by Mawdudi in 1950's.¹¹ Muhammad Hamidullah's 1944, 1955, 1957 and 1962 writings too should be included in this category. They have all recognized the need for commercial banks and the evil of interest in that enterprise, and have proposed a banking system totally free from interest.

⁹ Imam Al-Sarakhsi, *Al-Mabsut*, (Mesir: Cet al-Sa'adah, 1324H), p. 22: 18.

¹⁰ *Ibid.*, p. 22: 18-9.

¹¹ M.N. Siddiqi, *Muslim Economic Thinking: A Survey of our Contemporary Literature* (U.K : Islamic Foundation, 1980).

In the next two decades interest-free banking attracted more attention, partly because of the political interest it created in Pakistan, Saudi Arabia, Iran, and Sudan and in other Muslim countries and partly because of the emergence of young Muslim economists. Works specifically devoted to this subject began to appear in this period. The first such work is that of Muhammad Uzair (1955). Another set of works emerged in the late sixties and early seventies. Abdullah al-Araby (1967), Nejatullah Siddiqi (1961, 1969), al-Najjar (1971) and Baqir al-Sadr (1961, 1974) were the main contributors.¹²

Early seventies saw the institutional involvement. Conference of the Finance Ministers of the Islamic Countries held in Karachi in 1970, the Egyptian Study in 1972, First International Conference on Islamic Economics in Mecca in 1976, International Economic Conference in London in 1977 were the result of such involvement. The involvement of institutions and governments led to the application of theory into practice.

The subject matter of writings and conferences in the eighties have changed from the concepts and possibilities of interest-free banking to the evaluation of their performance and their impact on the rest of the economy and the world. Conference on Islamic Banking: Its Impact on World Financial and Commercial Practices held in London in September 1984, Workshop on Industrial Financing Activities of Islamic Banks held in Vienna in June 1986, International Conference on Islamic Banking held in Tehran in June 1986, International Conference on Islamic Banking and Finance: Current Issues and Future Prospects held in Washington, D.C. in September 1986, Islamic Banking Conference held in Geneva in October 1986, Conference 'Into the 1990's with Islamic Banking' held in London in 1988, and the Workshop on the Elimination of Riba from the Economy held in Islamabad in April 1992 belong to this category. Several articles, books and Ph. D. theses have been written on Islamic Banking during this period.

¹² Ibid.

3.4 Islamic Banking a Reality

The first attempt in this regard was made in Pakistan during 1950's as a pilot scheme, but unfortunately it did not succeed. Most of the scholars and researchers are in the opinion that the first Islamic bank in the modern context was Mit Ghamr Savings Bank. It was also an experimental project offering interest free banking in Egypt. It was established in July 1963. The bank was very popular initially and led to the opening of four new branches by 1967. In the same year, eight new small scales "interest-free" saving banks were established. But they were publicly not Islamic for fear of offending the political authorities. These savings banks did not pay interest to their depositors as well as charge interest to their borrowers. These banks had been lending money to the businessmen on the basis of profit and loss sharing. All these banks were closed down in 1971 due to adverse political climate prevailing in Egypt during that period. Thus the attempt to continue interest-free Islamic banking did not succeed due to political pressure. The first modern Islamic bank, established in Egypt in 1972, was named Nasser's Social Bank. Its objectives are more social than commercial.

Islamic scholars are of the opinion that the concept of an "Islamic Bank" was come into being from the Islamic Summit in Lahore, Pakistan in 1971, which recommended the creation of an Islamic Development Bank. The issue was seriously considered at the Islamic Conference of Foreign Ministers of OIC countries in Jeddah in 1973. Another Islamic Conference followed this in 1974, the deliberations of which led the establishment of the Islamic Development Bank (IDB) in 1975 with its head office in Jeddah. The Islamic Development Bank is an international financial institution. The purpose of the Bank is to foster the economic development and social progress of member countries and Muslim communities individually as well as jointly in accordance with the principles of Shari'ah i.e., Islamic Law. The bank is also responsible for providing technical assistance to member countries, extending training facilities for personnel, and undertaking research for enabling the economic, financial and banking activities in

Muslims countries to conform to the Shari'ah. IDB has already promoted a number of Islamic Banks in the member countries and participated in their share capital and management. The present membership of the Bank consists of 55 countries.

The establishment of IDB accelerated the Islamic banking movement. In the late 1970s several Islamic banks were established in the Middle East such as the Dubai Islamic Bank in 1975, the Faisal Islamic Bank in Sudan and in Egypt in 1977. The Kuwait Finance House and Islamic Investment Co. of the Gulf were also established in the same year. The Bahrain Islamic Bank, the Sepah Islamic Bank of Iran, the Islamic Investment Company Ltd in Emirates, the Jordan Islamic Bank for Finance and Investment all opened in 1979. In 1980s a good number of Islamic Banks and financial institutions were set up. The International Bank for Investment and Development in Egypt; Bank Misr- Islamic Branches in Egypt; Islamic Investment Co., Bahrain; Islamic Finance House Co., Jordan; Banker's Equity Ltd., Pakistan; Pakistan House Building Finance Corporation-Islamized, Investment Corporation of Pakistan- Islamized, and Islamic Muda'bara Companies all established in 1980. Arab Banking Corporation ("ABC"), established in 1980, is headquartered at ABC Tower in the Diplomatic Area of Bahrain. In 1982, Malaysian Islamic Bank, Saudi Islamic Bank in Saudi Arabia, Islamic Investment House in Jordan, and Investment House in Kuwait were established. In 1983 Faisal Islamic Bank, Bahrain; Qatar Islamic Bank; Islamic Investment Co., Qatar; Islamic Bank for Western Sudan; Islamic Corporation Development Bank, Sudan; Al-Baraka Islamic Bank, Sudan; Saudi-Tunisian Finance House; and Sudanese Islamic Bank, Sudan were established. Arab Gambian Islamic Bank Ltd is a Gambian Bank commenced operations in January 1997 to carry on banking business in accordance with Islamic Shariah. Al-Baraka Islamic Bank is a leading Islamic Bank operating in Bahrain, covering Saudi Arabia, UAE, other Gulf countries, Bangladesh and Pakistan. Al-Baraka Bank was incorporated and licensed to operate from Bahrain as an offshore bank on 21 February 1984. Around the world, there are 23 banks and financial institutions working under the name of Al-Baraka.

In 1984 Al-Baraka Investment and Development Co., Saudi Arabia; Al-Baraka Islamic Bank, Sudan; Al-Baraka Islamic Bank, Bahrain; Faisal Islamic Bank, Guinea; Faisal Islamic Bank, Niger; Islamic Investment Co., Niger; Tadamon Islamic Bank, Sudan; Islamic Investment Co. Sudan; and Faisal Islamic Bank, Senegal were established. Al-Baraka Islamic Bank, Mauritania; Faisal Finance Institution, Turkey; and Al-Baraka Turkish Finance House were established in 1985. Saudi-Egyptian Finance Bank, Egypt; and National Islamic Bank, Jordan were set up in 1988. Turkish-Kuwait Finance House, Qatar was set up in 1989. Arab Islamic Bank, Bahrain was established in 1990. Noriba Bank was incorporated in the Kingdom of Bahrain on May 19, 2002. The Switzerland's UBS Group wholly owns the Bank.

The Malaysian government set up "Pilgrim's Management Fund" in 1962 to help prospective pilgrims to save and profit. Bank Islam Malaysia commenced operation in July 1983, following the passage of the Islamic Banking Act 1983. This act is a milestone in Malaysian history for the growth of indigenous Islamic banks and financial institutions. Since then some 50-60 institutions have been established.

In 1977 President Zia-ul-Haq announced his program for creating an interest-free economy in Pakistan. In June 1980, the Zakah and Usar systems were instituted while article 38 of the revised Pakistan constitution said that the 'state shall eliminate Riba (interest) as early as possible'.

On September 9, 1977 the President of Pakistan assigned Council of Islamic Ideology with the task of preparing a blueprint for an interest free economic system. In November 1977 the Council appointed a Panel of Economists and Bankers for compiling their recommendations on elimination of interest.

The banker-members of the Panel were assigned with the job of drafting interest free commercial banking framework and this sub-committee completed its report on January 02, 1978. The panel presented its final report to the Council of Islamic Ideology in February 1980 and with some modifications and substitutions the council adopted this report on June 15, 1980.

From January 01, 1981 all the 7000 branches of nationalized banks of Pakistan started accepting deposits on the basis of profit & loss sharing. This operational phase was voluntary, as people were free to deposit their funds either on the new basis of profit & loss sharing or to continue on the old basis of interest. The response from the public was very good.

The Pakistan Supreme Court has given a clear decision in Ramadan 1420A.H/ 1999 A.D, to pen through all laws that support interest based financial system. The court orders the central government of Pakistan to bring all existing financial institutions in line with the Islamic Shari'ah. It is a remarkable and worth mentioning decision towards Islamisation of financial system of a country. The public responded whole-heartedly to the system and it has been working smoothly for the last few years. Thus Pakistan became the first country to embark on a full Islamisation of its banking sector.

The Government of Iran has also taken decision to abolish interest from the banking system. A new banking law was enacted in Iran in August 1983 to replace interest based banking by interest free banking. Sudan followed the path of Pakistan and Iran in order to Islamize the banking system. The first attempt was made in 1984 when a presidential decree was issued directing all commercial banks to stop interest based dealings with immediate effect and to negotiate the conversion of their then existing interest bearing deposits and advances into Shari'ah acceptable forms.

Islamic banking system also appeared in the financial horizon of Bangladesh. Since independence, Bangladesh saw a new trend in banking both at home and abroad. At home, some entrepreneurs were actively working for introduction of Islamic banking. Two professional bodies "Islamic Economics Research Bureau" (IERB) and "Bangladesh Islamic Bankers Association" (BIBA) took practical steps for imparting training on Islamic economics and banking to a group of bankers and arranged some national and international seminars, symposia, and workshops to create public awareness. Their professional and right-thought activities were streamlined by a number of enthusiastic and pious

businessmen in Bangladesh. The continuous and dedicated work of the above groups and individuals and active support from the Government, Islamic banks could be established in early eighties. The Government of the People's Republic of Bangladesh allowed private entrepreneurs to take initiative to establish banks in the beginning of 1980s. Taking that opportunity a few dedicated Bangladesh Muslims and internationally important personalities, and institutional investors then came forward to establish an Islamic Bank named Islami Bank Bangladesh Limited (IBBL) for the first time in Bangladesh. In the year 1983, the Bank started its operational activities. Some renowned personalities and institutions are sponsors and directors of this bank. Prior to opening of the Bank, several seminars and symposia were held in different parts of the country to disseminate the concepts of Islamic banking.

Now there are six Islamic Banks in the private sector of Bangladesh viz. (1) Islami Bank Bangladesh Limited (1983), (2) The Oriental Bank Limited (1987), (3) Al- Arafa Islami Bank Limited (1995), (4) Social Investment Bank Limited (1995), (5) Shamil Bank of Bahrain EC, Dhaka (1997) (6) Shahjalal Bank Limited (2001). Besides, Prime Bank Limited has opened two Islamic branches and Dhaka Bank Limited has started operation of an Islamic counter along with traditional banking since commencement of the Bank on 05 July 1995. One foreign Islamic bank named Faisal Islamic Bank of Bahrain EC has opened a branch in Dhaka in 1998. These Islamic banks are not only serving the needs of the Muslims but also extending their operations to serve the non-Muslims of the country. All these banks have been extending credit and banking services to millions of the urban and rural people of the country. Social Investment Bank Limited and Islami Bank Bangladesh Limited have some special programs for providing finance to the poor segment of the society in various income generating activities. All the above mentioned Banks have created a new era of Islamic Banking in Bangladesh having social, ethical and moral dimension in each of their activities ranging from credit to construction, trading to transport, farming to fishing, manufacturing to mining and so on. These Banks have also some special programs for development of various religious and social service

oriented institutions. Within these programs, Mosque, Maktab, Waqf, Charitable organizations etc are modernized and activated.

Islamic banking operations are not limited to Islamic countries, but are spreading throughout the world. Islamic Banks have extended their wings to the Western world. Islamic Banking System International Holding, for example, was established in Luxembourg in 1978, become the first Islamic institution on Western soil. The Islamic Investment Company was in set up in 1979 in Geneva, followed by Dar al-Mal al-Islami, Switzerland and Bahamas in 1981. Islamic Finance House in UK, European Islamic Bank in Switzerland, Islamic Bank International of Denmark, Ankara Islamic Bank and Istanbul Islamic Bank in Turkey, Interest Free Monetary System in Australia, Faisal Islamic Bank, Cyprus; Philippine Amanah Bank; and Islamic Finance House, UK were established in 1982. Islamic Bank International of Denmark was established in 1983. Dar al Mal al Islami, Geneva; Islamic Investment Service Co., Geneva; and Al-Baraka International Bank, UK were set up in 1984. Al- Baraka Islamic Bank, Mauritania; Faisal Finance Institution, Turkey; and Al-Baraka Turkish Finance House were established in 1985. In the following year (1986) Al-Ameen Finance & Investment Co., India was set up. In 1988 Islamic Bank, South Africa was established. All those banks were set up on the basis of Islamic Shari'ah. 'The collapse of the Soviet Union was an opening for a new frontier for the Islamic banks. Al-Baraka group now has its own bank in Kazakhstan by the name of Al-Baraka Kazakhstan Bank and this group is aiming for a new joint venture in Uzbekistan. Arab Islamic Bank is also setting-up an investment bank in Albania'.¹³

In this connection it is worth mentioning that western banks such as ANZ Grind lays Bank and HSBC have Islamic banking units in order to serve clients in Islamic countries. Citi Islamic Investment Bank E. C. ("CIIB") was established in July 1996 in Bahrain. It is a sister organization of Citibank.

¹³ Sudin Haron, "Islamic Banking : A New Vehicle in Fostering Entrepreneurship", *Journal of Islamic Banking & Finance*, Vol. 13, No 3, July – Sept 1996, Summer Issue, p. 29.

Islamic Banking made its debut about quarter a century ago. At present about 200 Islamic Banks and Financial institutions are operating in 27 Muslim and 16 non-Muslim countries.¹⁴ It's a remarkable success in a very short span of time.

3.5 Main Features of Islamic Banks

3.5.1 Prohibition of Interest (Riba)

Islam prohibits Muslims' from giving, taking, accounting and witnessing Riba (interest) regardless of the purpose for which such loans are taken and regardless of the rate at which Riba is charged. Riba is the Qur'anic term for usury or interest, and the definition of Riba as given in the Qur'an is very clear and unambiguous. "Riba is an extra payment received over and above the principal amount, regardless of the fact that extra amount is significant or insignificant".¹⁵ Islamic banks cannot pay interest to their depositors and also cannot demand or receive any interest from borrowers. They are not even allowed to witness or keep accounts of these transactions. In different revelations in the Holy Qur'an prohibition of Riba (interest) is mentioned.

In Sura Ar-Rum the term Riba is used in the following words:

"Whatever you pay as Riba (interest), so that it may increase in the property of (other) men, it does not increase with Allah" (30:39). Thus interest deprives the wealth of Allah's blessings.

In Sura Al-Nisaa the term Riba is mentioned in the context of sinful acts of Jews in the following words:

"And because of their charging while they were prohibited from it" (4:161).

In Sura Al-i-Imran wherein the prohibition of Riba is stated in the following manner:

¹⁴ Shahid Hasan Siddiqui, "Islamic Banking: True Modes of Financing", *Journal of Islamic Banking & Finance*, Vol. 16, No. 4, October-December 1999, Autumn Issue, p. 7.

¹⁵ Muhammad Mohasin Ali and Md. Abdul Awwal Sarker, "Islamic Banking : Concept, Features and operational Methodology", *Thoughts on Economics*, Vol. 5, No 3 & 4, 1995, p. 27.

"O believers take not doubled and redoubled interest and fear Allah so that you may prosper." (3:130). Thus Muslims are advised to keep themselves away from interest if they want their own welfare.

In Surah Al-Baqarah; where a clear demarcation line is drawn between trading and interest. This revelation also encourages the believers to do good deeds, establish Salah, and pay Zakah. The verses are as follows:

"Those who benefit from interest shall be raised like those who have been driven to madness by touch of the Devil: this is because they say: 'Trade is like interest' while Allah has permitted trade and forbidden interest" (2:275-281).

Allah destroys Riba and nourishes charities. And Allah does not like any sinful disbeliever. Surely those who believe and do good deeds, establish Salah and pay Zakah have their reward with their Lord, and there is no fear for them.

Islam insists that all the participants in the trading process must equitably share the risk and returns. The basic principle is that Allah permitted trade but prohibited Riba. 'Thus banks should neither pay any interest to the depositors nor charge any interest on loans. Instead they should enter into partnership with businessmen as a possible alternative, sharing profit and losses if any'.¹⁶

Interest is opposed in Islam perhaps mainly on the ground of the social divisions it creates and the hardship to borrowers. 'Riba leads to injustice (ZULM) and Islam is against all forms of injustices and exploitations and pleads an economic system which aims at extensive socio-economic justice'.¹⁷

There is lot of examples of prohibition of Riba 'the Old Testament also recommends loans to poor (Deuteronomy 15:7-9), with loans free of interest and with loans to be cancelled every seventh year (Deuteronomy 15:4, 5, 13), except loan to foreigners'.¹⁸

¹⁶ Anwar Iqbal Qureshi, *The Fiscal System of Islam* (Lahore : Institute of Islamic Culture, 1978).

¹⁷ Shahid Hasan Siddiqui, *op.cit.*

¹⁸ H.A. Dar and J.R. Presley, "Islamic Finance: A Western Perspective", *International Journal of Islamic Financial Services*, Vol. I, No. 1, 1999.

Cummings et. al.¹⁹ stated four reasons for the prohibition of interest in Islamic finance:

1. Interest enhances the tendency to accumulate wealth in a few hands and thereby decrease man's concern for his fellow men.
2. Islam does not allow gain from financial activity unless the beneficiary is subjected to the risk of potential loss.
3. Islam encourages the accumulation of wealth through personal initiative and hard work instead of interest.
4. Accumulation of wealth through interest is exploitation to the society and termed as selfish activity. Interest rates hamper investment and employment.

3.5.2 Sharing Profit and Loss between the Borrower and the Banker

Islamic banks never lend money; they just invest money with the anticipation of profit. One of the main features of Islamic financial system is that both the provider of capital (bank) and the user of capital (businessman) have to share the risk of business ventures, whether those are manufacturing firms, service firms, or simple trade deals. While in traditional banking system, all the pressure is on the businessman (borrower). The borrower must have to pay back his loan with predetermined interest, regardless of the success or failure of his business. Traditional banks try to realize loans along with predetermined interests from borrowers. But borrower wants to maximize his profit/ earning through the investment of loan amount. Thus two parties of a loan agreement have two conflicting objectives of earnings; one is the interest and the other is the profit. Contrarily, under Islamic banking both the parties hold a common objective of sharing future earnings/profits out of the loan investment between a banker and a borrower.

¹⁹ J.T. Cummings et al., *Islam and Modern Economic Changes*, Syracuse University Press, 1980, p. 25.

3.5.3 Making Money out of Money is not Permissible in Islam

Money is a medium of exchange, a way of defining the value of a commodity. Therefore, money should not be allowed to gain an "increase" (Riba), simply by keeping in a bank or lent to someone else. Entrepreneurial skills, initiative, and risk involved in a productive venture are more important than the money used to finance the same. Lending money represents a transfer of property right. Therefore, until and unless the money is used to generate incremental wealth there is no claim from both the borrower and the lender to a share of that additional wealth guaranteed.²⁰

In fact, money represents purchasing power only and this purchasing (money) can not be used to make more purchasing power (money) without undergoing the intermediate step of it being used for the purchase of commodities and services.

3.5.4 Gharar (Uncertainty or Speculation) is prohibited in Islam

Another significant feature of Islamic finance is that all transactions should be free from uncertainty and speculation. Gambling is prohibited in Islam since it tends to transform all economic activities into an imaginary one, such as betting etc. It is a Zero-Sum Game i.e. the gain of one at the cost of other. The rationale behind the prohibition gambling is the intention to protect the weak from exploitation of the strong.

3.5.5 Investment and Financial Transaction should only Support *Halal* Activities

Under Islamic Shari'ah any Muslim or financial institutions are not allowed to invest in any business, which is considered as Haram (prohibited). Trade in liquor, pork, Haram meat, involving in gambling or nightclub activities, lotteries, pornography etc, for example would not be financed by Islamic banks. Similarly, an Islamic bank cannot extend real estate loan for the construction of a Casino. Islam strikes at the root of all evils and wants to establish a just and fair society.

²⁰ H.A. Dar and Presley, *op.cit.*

Islamic banks perform banking services like transfers, acceptance of current deposits etc against fees or charges, as is done by other banks, and these services are not prohibited in Islam.

3.5.6 Reliance on Productivity Rather than Security

Conventional banks give more emphasis on collateral securities rather than productivity. The "conservative principle" of banking does not allow conventional banks to participate in the losses of the enterprises where they have extended credit facilities. They make loans against collateral securities. Traditional banks hardly bother about the success or failure of the business of the borrower. They are obsessed with collateral. Contrarily Islamic banks give more emphasis on productivity and profitability of the projects financed by them rather than collateral offered by borrowers. Islamic Banks give due importance to the purpose and output of each loan operation. Islamic banks believe in Non-zero-sum game wherein both the borrower and the banker can gain through better economic decision as well as high productivity and profitability of the business venture of the borrower.

Chapter 4
**Modes of Investment in
Islamic Banks**

Chapter 4

Modes of Investment in Islamic Banks

4.1 Investments Instruments of Islamic Banks

Islamic Banks cannot charge interest on loans and pay interest on deposits. 'The Holy Qur'an forbids the consumption of interest, dead animals, blood, pork, alcoholic drinks, etc ; but the commandment against dealings on interest has been conveyed in the most severe terms and tones obviously due to its damaging consequences to the society'.¹ Therefore, Islamic Banks have to find other ways of financing based on Islamic Shari'ah.² But a change over to Islamic principles involve a complete transformation in the nature and mechanism of interest based banking. The verse 29 of Sura Al-Nisa in the Holy Qur'an states that "O ye who believe! Devour not each other's wealth among yourselves through wrong means except it be a trade by mutual consent". In the light of the injunction of the Holy Qur'an and the Sunna of the Holy Prophet (SM), the Islamic alternative for gainful use of one's savings is to adopt trading either directly or to enter into participatory arrangements with others on the basis of profit and loss sharing. 'Many Muslim scholars held the view that Islamic financing approach should primarily be based upon a principle whereby the rate of return on financial capital should vary in accordance with the variation in the return of the whole enterprise'.³ Depositors as well as users of Bank's funds have to enter into a trading arrangement with the Bank. Islamic Banks use the term 'investment' to denote their 'borrowing activities'. Islamic investment instruments fall into two groups:⁴

¹ Nawazish Ali Zaidi, *Eliminating Interest from Banks in Pakistan* (Karachi, Pakistan : Royal Bank Company, 1987), p. 146.

² Ataul Hoque, *Readings in Islamic Banking* (Dhaka : Islamic Foundation, Bangladesh, 1987), p. 15.

³ Mozer Kahf and Tariqullah Khan, "Principles of Islamic Financing (A Survey)", Research Paper, No. 16, 1st ed., (Jeddah: Islamic Research and Training Institute, Islamic Development Bank 1992), p. 16.

⁴ Abdur Rahim Hamid, *Islamic Banking: Conceptual Framework and Practical Operations* (Islamabad : Institute of Policy Studies, 1992), p. 15.

- a) Participative financing and thereby sharing in the profit and loss. This arrangement can either be in the form of Muda'raba or Musharaka but both are a variation of the concept of profit and loss sharing.
- b) Acting as intermediaries through a variety of sales and rental contracts. Islamic Banks acquire or 'own' the goods on behalf of would be partners before reselling or renting (at a higher margin) them.

4.1.1 Participating Finance

4.1.1.1 Mudar'aba-Qira'd/Muqa'rada ('Agency' Partnership)

Muda'raba means that one party provides capital and the other utilizes it for business purpose under the agreement that profit from the business will be shared according to a specified proportion.⁵ It is a partnership between finance and management and the institution so created is called a Muda'raba. 'In these arrangement people with surplus money entrust their funds to those who have skills and experience to utilize it for productive purposes. Unlike the interest-based system, the amount of return on the fund invested in Muda'rabah is neither fixed nor predetermined. The quantum of profit (or loss) depends on the operational results of the economic activity undertaken'.⁶ In this context Udovitch states:

'It is an arrangement in which an investor or a group of investors entrusts capital or merchandise to an agent-manager, who is to trade with it and then return to the investor(S) the principal and a previously agreed upon share of the profits. As a reward for his labor, the agent receives the remaining share of the profits. Any loss resulting from the exigencies of travel or from an unsuccessful business venture is borne exclusively by the investor(s); the agent is in no way liable for a loss of this nature, loosing only his expended time and effort.'⁷

⁵ Muhammad Nejatullah Siddiqi, Partnership and Profit-Sharing in Islamic Law (Leicester, UK : The Islamic Foundation, 1985), p. 15.

⁶ Nawazish Ali Zaidi, op.cit., p. 178.

⁷ Abraham L. Udovitch, Partnership and Profit in Medieval Islam (New Jersey : Princeton University Press, 1970), p. 170.

It is one of the popular techniques of financing by Islamic Banks. In a Muda'raba contract the Bank provides capital and the client provides his time & initiative. The client does not claim any wage for conducting the business. It fulfils an important economic function of the Islamic community through encouraging "the hiring of capital" and the "the hiring of skills".⁸ Islam forbids transaction on the basis of Riba (interest), but permits profit-loss sharing in all modes of business transactions. 'The concept of profit and loss sharing is the Islamic alternative for the functioning of commercial banks, investment companies and other business enterprises.'⁹ In this type of contract, the Bank supplies "full financing" to an agent-manager (Mudarib) for trading or industrial purposes and the agent would contribute only his work and experience.¹⁰ Profits are shared between the two according to a clearly defined proportion agreed upon before hand.¹¹ No fixed amount can be paid to any party.¹² If loss occurs from normal business or natural disasters, the Bank (Rab al-mal or capital provider) bears the loss and the 'Mudarib' (client) receives no reward for his efforts. In case of more than one capital suppliers provide capital the amount of loss is to be shared by the providers of capital only in strict proportion to the capital provided by each. Loss occurring due to negligence or breach of agreement by the Mudarib (client) must be borne by him.

The famous Muslim theologian al-Marghinani elaborates the meaning of Muda'raba in his book "Al-Hadaya" as under:

"Muda'raba is derived from the word Darb (striving and journeying) on earth. It has been so named because the Mudarib (user of capital) deserves the profit on account of his efforts and work. It has been allowed (in Shari'ah) because of its necessity, as there are several types of people. There are some

⁸ D.M. Qureshi, "Mudaraba and Its Modern Applications", Journal of Islamic Bank & Finance, Vol. 2, No. 1, Jan-March, Winter Issue, Islamabad, 1985, p. 12.

⁹ Nawazish Ali Zaidi, op.cit., p. 178.

¹⁰ Abdur Rahim Hamdi, op.cit., p. 15.

¹¹ D.M. Qureshi, op.cit., p. 7.

¹² Muhammad Nejatullah Siddiqi, op.cit., p. 14.

rich in wealth but without talents to use it, and others capable of using it but empty handed. There occurs thus a necessity for such utilization. It reconciles the welfare for all the unskilled and the resourceful, the poor and the rich. People practiced it in the days of the Prophet(SM) who confirmed the legality. The companions of the Prophet(SM) were also evolved into similar contracts.

In this contract the capital is a trust in the hands of the user and he is authorized to use it (with his own discretion) as he gets the possession with the sanction of actual owner, not on account of exchange or pawn. He is an agent as he uses it with the sanction of the owner. He shares the profit when it accrues on account of his authority over it and his work. When the contract is violated (on account of the owner) it will be treated as employment on wage till the user gets a wage equivalent of similar work anywhere else. When (the user) violates the contract, he becomes a usurper on account of misuse of owner's wealth.¹³

The four Arabic terms Muda'raba, Muqa'rada, Dirab and Qira'd are used interchangeable with no essential difference in meaning or connotation among them. The divergence in terminology was probably originally due to geographical factors. 'This type of trade organization of pre-Islamic Arabia was known as Al-Qira'd or Al-Muqa'rada (from Qa'rada, a derivative of Qarada – he lent capital for a share in the profit), which means to advance to anyone the capital (or the merchandise) for purpose of trade, on condition that they will both share the profit earned'.¹⁴ "The people of Heja'z called this practice, Al- Qira'd and the people of Iraq named it Al-Muda'raba or Dirab (from Qaraba; he went out in search of subsistence or, on a trade-journey) meaning a transaction in which the owner of the capital gives it to the trader, with the stipulation that the profit will be divided between them, or his share of profit will be fixed".¹⁵ It is known as Commenda in the Italian law.

¹³ Al-Marghinani, Al-Hidiaya, Vol. 3, p. 241.

¹⁴ Ibn Manzu'r, Lis'n al-Arab, Vol. X (Beirut : 1956), p. 84. Also Al- Shrakhsi, al-Mabsu't, Vol. XXII, p. 18.

¹⁵ Al-Zurqa'ni Shara Muwatta Imam Ma'lik, Kitabul-Qira'd, Vol. III, (Egypt: 1954) p. 345. Also Al-Shawka'ni, Nail al-Awta'r, Vol. V (Egypt: 1952), pp. 278-82.

In general, the Hanafiyyah, Hambaliyyah and Zaydiyyah Schools of Muslim Jurisprudence have used the term Muda'raba, while the Malikiyyah and Shafi'iyyah have preferred the term 'Qira'd' and to a lesser degree, Muqa'rada.

Thus Muda'raba is an ancient concept and it was in existence in Babylonian and several other countries in the olden times. Al-Marghinani states 'And there is no difference of opinion among the Muslim jurists about the legality of Qira'd (Muda'raba). It was an institution in Pre-Islamic period and Islam confirmed it. In this form of investment a person gives to another person an amount of capital that he uses in his business. The user gets according to the condition, some specified proportion of the profit, i.e. any proportion they agree: one-third, one-fourth, or even one-half'.¹⁶

Although this type of trade organization is pre-Islamic, the Holy Prophet (SM) allowed this practice and his companions followed it. The Holy Prophet(SM) is reported to have said, 'That a man who is bringing up three daughters is like a prisoner; so, O slaves of Allah, do Muda'rabah with that man, lend him'.¹⁷

Hazrat Khadija (R) appointed the Holy Prophet (SM) as an agent in a Muda'raba investment. 'The Prophet(SM) undertook a trade-journey carrying the commodities of Hazrat khadijah(R) to the market of Busra. This was a partnership-venture of Qira'd. Ibn Hisham says that Hazrat Khadijah(R), the merchant lady of Mecca, who used to advance her capital to the traders on the partnership principle, heard about the Prophet's(SM) truthfulness, loyalty and nobility of character. She sent for him and offered him her goods to be taken to Syria as a trade-venture; and that she would give him profit greater than the profits she had given to other merchants.... The Prophet accepted her offer and took her goods. He went out on a trade-journey... and reached Syria. The prophet(SM) sold out all the goods he had brought there and with the money he bought whatever he wanted and then brought his caravan to Mecca. When

¹⁶ Al-Marghinani, Al-Hidaya, Vol. 3, p. 241.

¹⁷ Al-Sarakshi, op.cit. , p. 19.

he reached Mecca, Hazrat Khadijah (R) sold all her goods, thus making cent percent profit on the capital involved.¹⁸

Hazrat Umar(R), Hazrat Usman (R) and Hazrat Abu Musa Ashaari(R) were also involved in Muda'raba contracts. Hazrat Aisha (R) and Hazrat Abdullah b. Umar (R) used to invest orphans' money and other's money left in their safekeeping in Muda'raba.¹⁹ Hazrat Umar (R) concluded a Muda'raba contact with Hazrat Zaid Ibn Khulaida.²⁰ and had also concluded a Muda'raba contact on behalf of the Bayt' al-Mal.²¹ Imam Sarakhsi states: 'On the authority of Hazrat Qasim bin Muhammad (R) who said, we had some money (as deposit) in the hands of Hazrat Aisha (R). She used to invest it on Muda'raba. Allah blessed us and gave profit through her effort'.²²

Hazrat Ibn Mas'ud(R), a prominent companion of the holy Prophet (SM), and 'Abbas bin 'Abd al-Muttalib, the uncle of the Holy Prophet (SM), were also engaged in Muda'raba trading, the latter having obtained Muhammad's (SM) approval for the conditions he imposed upon agents to whom he entrusted his money.²³ In this context, Ka'sa'ni, the author of 'Badai' states.

'It is narrated on behalf of Hazrat Ibn Abbas(R) that Abbas bin Abd al-Muttalib, when he would provide finance on Muda'raba, made it a condition that he (the user) would not take the capital to the oceans nor he would enter a valley, nor he would trade with it in the sick cattle. If, however, he did any of these things, he (the user) shall be responsible for the loss. When the

¹⁸ Zia-ul Haq, "Inter-Regional and International Trade in Pre-Islamic Arabia", Islamic Studies, (Karachi: Journal of the Islamic Research Institute, September 1968), Vol. VII, No. 3, , pp. 228-289.

¹⁹ Al-Sarakhsi, op.cit., p. 18.

²⁰ Ibid.

²¹ Ima'm Ma'lik, Kita'bul Qira'd, op.cit..

²² Al-Sarakhsi, op.cit., Vol. 22, pp. 18-19.

²³ Asl Shaybani, Mudaraba, fol. 42a.

Prophet(SM) knew of these conditions he allowed the same'.²⁴ Hazrat Hakim Ibn Hizam (R) has also been reported to adopt the same conditions in a partnership of Qira'd whenever he advanced his capital to any trader.²⁵

The Muslims jurists emphasized this mode of investment for mutual cooperation.²⁶ 'It is possible that one party having capital is not only unable to employ it himself but thinks it proper to choose a good working partner. The second person, by virtue of his knowledge, experience and business expertise may find it more appropriate to enter into a business contact with another working partner on the basis of Muda'raba. If the person owning capital in such a situation gives it on the basis Muda'raba to a second party who gives it again on the basis of Muda'raba, this opens the door for cooperation amongst all three parties. This form of two-tier Muda'raba is useful for all and there is nothing in it that goes against Shariah'.²⁷

Under Muda'raba the financial liability of the party providing capital will be limited to the amount provided by him except where he has increased his own liability by permitting the working partner, on his behalf, to borrow or to purchase on credit.²⁸ The Muda'raba agreement ends with the death of any one of the parties. Besides, any party may terminate Muda'raba agreement any time. In both the cases, if the number of remaining parties is more than two, the remaining parties may continue the agreement.²⁹

²⁴ Ka'sa'ni, 'Ala' al-Di'n Badai al-Sanai, (Egypt : Mutba'ah Abu Bakr bin Mas'ud Jam'liyah 1910), Vol. 6, p. 79.

²⁵ Al-Sarakshi, op.cit., Vol. 22, p. 19.

²⁶ Ibid.

²⁷ Muhammad Nejatullah Siddiqi, Partnership and Profit-Sharing in Islamic Law (Leicester, UK : The Islamic Foundation, 1985), p. 14.

²⁸ Ibid., p. 18.

²⁹ Ibid.

4.1.1.2 Musha'raka (Partnership)

It is another type of financing utilize by Islamic banks. Under such scheme, an Islamic Bank participates in Shari'ah approved partnership, provides part of the required capital to the businessman and takes part in decision making. It is a legitimate mode of financing recognized in Islam. It is based on equity participation (musharaka) in which the partners use their capital jointly to generate a surplus. Profits or losses will be shared between the partners according to some agreed formula depending on the equity ratio. This differs from Muda'raba in a small way. In this form of financing Banks provide less than 100 percent finance; while in Muda'raba Bank provides full financing of the project. 'As stated earlier all the partners including the Bank have the right to participate in the management of the project. Any one or all of them also have the right to wave this right. The profits shall be distributed according to agreed ratio, which may not be the same as capital proportion but loss shall have to be shared exactly in the same proportion in which different partners have provided capital'.³⁰ Muda'raba and Musha'raka constitute, at least in principle if not in practice, the twin pillars of Islamic banking.

4.1.1.3 Qard-e-Hasan

This is benevolent loan that obliges a borrower to repay the lender the principal amount borrowed on maturity of the loan. The borrower, however, has the discretion to reward the lender for his loan by paying any sum over and above the principal amount.³¹ 'In case money is extended as a loan no surplus can be claimed over and above the principal (2:275, 279). Thus Islam permits only an interest-free loan called Qard-e-Hasan. Muslims extend Qard-e-Hasan to meet a moral obligation and that is why no interest or profit is claimed on it.

'Abdullah bin Abi Rabi'a reported his grandfather saying, on the authority of his father: The Holy Prophet(SM) borrowed forty thousand dirham from me. The revenue came into him and he paid it to me by saying: May Allah bless your

³⁰ Ahmed, op.cit., p. 20.

³¹ Haron Sudin, "Islamic Banking : A New Vehicle in Fostering Entrepreneurship", Journal of Islamic Banking & Finance, Vol. 13, No. 3, July-Sept 1996, Summer Issue, p. 33.

family and your property. Verily, the only reward for a loan is the thanks giving and the repayment'.³²

The Holy Qur'an categorically states in Sura Al-Baqarah (278-280) as under:

'O believers fear Allah and forego the Riba (interest) that owes, if you really believe. If you do not, beware of war on the part of Allah and His Apostle. But if you repent, you shall keep your principal. Oppress none and no one will oppress you. If a debtor is in want give him time until his circumstances improve; but if you forego (the debt) as charity, that will be your good, if you really understand. 'The institution of Qard-e-Hasan has a distinctive characteristic of the Islamic economic system which has a highest human consideration'.³³ "It is an element of the overall scheme of social insurance founded at different tiers of household, family, locality and nationality. It is the primary responsibility of the members of one's family to extend Qard-e-Hasan to needy members. In case they are not capable of doing so people living in the neighborhood are responsible to meet their social obligation. In an overall context, the state may undertake to provide this facility in those cases where the family and neighbors have failed to help. In any case the institution has to be organized so that no needy person is exploited by some one due to non-availability of Qard-e-Hasan.³⁴ Providing loan to some one is also considered 'desirable' in Shari'ah because lending implies the provision of relief to one's Muslim brother, the fulfillment of his needs and the extension of help and support'.³⁵ Moreover, if the borrower is in financial difficulty, the lender should give more time to the borrower for repayment of loan. The Holy Qur'an also

³² Muhammad Akram Khan, *Economic Teachings of Prophet Muhammad: A Selected Anthology of Hadith Literature on Economics* (Islamabad : International Institute of Islamic Economics and Institute of Policy Studies, 1989), p. 162.

³³ Mohammad Yousuf Adil, "Islamic Modes of Financing", *Journal of Islamic Banking & Finance*, Vol. 16, No. 3, July-Sept. 1999, Summer Issue, p. 40.

³⁴ Muhammad Akram Khan (1989), *op.cit.*, p. 151.

³⁵ Ibn Qudama (Died 671H), *Muwaffaq Al Din*, (Beirut : Dar al Kitab al' Arabi Publishers 1393H), Vol. 4, p. 353.

tells about rescheduling (granting more time) the payment of debts. 'If the debtor is in a difficulty, grant him time till it is easy for him to repay...' (2:280).

Islamic banks provide a portion of their investment funds to the poor segment of the society without interest for their economic emancipation. The bank gets back the original amount after the period of loan is over. In this connection some contemporary Muslim writers suggested that Islamic banks may provide Qard-e-Hasan from the Zakah fund or by the banking system as practiced by the nationalized banks in Pakistan after Islamization in the area of loans to students and other needy segment of the society.³⁶ It is clear from the above discussion that Islamic banking goes beyond the pure financing activities of interest-based banking. Islamic banks engage in equity financing and trade financing. By its very nature, Islamic banking is a risky business compared with interest-based banking. For, risk sharing form is the very basis of all Islamic financial transactions.

4.1.2 Trade Financing

This is also done in several ways. Those are:

- i. The most commonly used mode of financing seems to be the 'mark-up' (Profit) device which is termed as Murabaha. In a Murabaha transaction, the bank buys an item for a client and the client agrees to repay the bank the price with an agreed profit later on. 'This is a common form of sales in Islam. 'This is basically the sale of goods at a price covering purchase price plus profit margin agreed upon by both the parties concerned, which transforms a traditional lending activity into a sale and purchase agreement, under which the lender buys goods wanted by the borrower for resale to the borrower at a higher

³⁶ Mozer Kahf, "The Economics of Muslim Minorities" in *Outlines of Islamic Economics*, (Indianapolis, Indiana: Association of Muslim Social Scientists, 1977), pp.93-117; Mozer Kahf and Tariqullah Khan, "Principles of Islamic Financing (A Survey)", Research Paper, No. 16, 1st ed., (Jeddah: Islamic Development Bank : Islamic Research and Training Institute, 1992), p. 16; M. Umar Chapra, *Towards a Just Monetary System*, (Leicester : The Islamic Foundation, 1985), p. 162.

price agreed upon by both parties'.³⁷ In this form of investment Islamic banks are no longer to share profits or losses, but assume the role of a normal business entity. So both seller and buyer know the original cost price of the commodity and also the profit element of the contract. It may appear at first glance that the mark-up is just another term for interest as charged by conventional banks, interest thus being admitted through the back door. What makes the Murabaha transaction Islamically legitimate is that the bank first acquires the asset and in the process it assumes certain risks between purchase and resale. The bank takes responsibility for the good before it is safely delivered to the client. The services rendered by the Islamic Bank are therefore regarded as quite different from those of an interest-based bank, which simply lends money to the client to buy the good. The mark up principle is justified on the basis of a generally accepted axiom that time may be valued provided it is incorporated in a sales transaction.³⁸

- ii. Islamic Banks also purchase and resale of properties on a deferred payment basis. This sort of investment is termed as Bai- Muajjal. It is considered lawful in Islamic Shariah (jurisprudence) to charge a higher price for a good if payments are to be made at a later date. According to Islamic Jurisprudence, this does not amount to charging interest, since it is not a lending transaction but a trading one.
- iii. Reference must also be made to pre-paid purchase of goods, which is termed Bai-salam, as a means used by Islamic Banks to finance production. Here the price is paid at the time of the contract but the delivery would take place at a future date. This mode enables a business to sell his output to the Bank at a price determined in advance. Islamic Banks, in keeping with modern times, have extended this facility to other manufacturing goods as well.

³⁷ Haron, op.cit., p. 32.

³⁸ Kahf and Kahn, Monzer Kahf and Tariqullah Khan, "Principal of Islamic Financing" (A Survey), Research Paper, No. 16, 1st ed, (Islamic Development Bank: Islamic Research and Training Institute, 1992), p. 350.

- iv. Islamic Banks also frequently practice Leasing or Ijara. Under this mode the bank buys an equipment or machinery for a client and leases it out to the client who may opt to buy the items eventually, in which case the monthly payments will consist of two components, i.e., rental for the use of the equipment and installment towards the purchase price.
- v. Hire-purchase where the bank buys an item for the client and hires it to him for an agreed rent and period, and at the end of that period the client automatically becomes the owner of the item.
- vi. Sell-and-buy-back where a client sells one of his properties to the bank for an agreed price payable now on condition that he will buy the property back after certain time for an agreed price.
- vii. Letters of credit where the bank guarantees the import of an item using its own funds for a client, on the basis of sharing the profit from the sale of this item or on a mark-up basis.

4.2 Bayt al-Mal

To discuss the development of Islamic banking one is to start with the time of Prophet Muhammad (SM) who introduced the system of Bayt al-Mal for the collection and disbursement of revenues among the displaced Muhajirs and needy Answers.³⁹ The Idea of Bayt al-Mal in abstract form existed from the time of the Prophet (SM) when the mosque of the Prophet(SM) was regarded as such and that at the time of Abu Bakr (R) an actual building was acquired for it and that a treasurer was appointed.⁴⁰

It was a special department of the government supervised and directed by its one particular officer designated as khazin Al-Mal or Sahib Al-Makhzan and

³⁹ S.M. Imamuddin, "A Historical Background of Modern Islamic Banking" in Md. Sharif Rushdi (eds.), *Thoughts on Islamic Banking* (Dhaka: Islamic Economic Research Bureau, 1982), p. 175.

⁴⁰ Gusau Sule Ahmed, *Islam and Contemporary Economic Problem*, (Sokoto: Nigeria Usmanu Danfodiwo University Press, 1992), p. 65.

the provincial treasurer was called khazin or Amin. The chief treasurer being an important official of the state had many assistants as scribes and accountants most of whom were non-Arabs. A good number of them might have been Jews and Christians. The supreme head of the central Bayt-al-Mal was the Caliph himself and the provincial one his Amir (Governor) both being responsible for the smooth running of all the departments under their control.⁴¹ 'Abdullah(R) reported that Allah's Messenger (SM) said: 'every one of you is a guardian of the people and he is accountable for his charge. Thus, the Amir is a guardian of the people and he is accountable for them. And a man is guardian of his household and he is accountable for them; and a woman is in charge of the house her husband and her children and she is accountable for them: and a slave is a guardian of his master's property and he is accountable for it. Beware, every one of you is a guardian and every one of you is accountable for his subjects'.⁴²

The Bayt al-Mal was a welfare agency, not only for the property of Muslims alone but of 'Dhimmis'.⁴³ Out of the Bayt al-Mal the state was obliged to support needy Dimmis as well as indigent Muslims. Whatever came in the Bayt al-Mal as Jizyah, Zakah or Ghanimah were disbursed immediately by the Prophet (SM). 'In fact there was no state treasury during the time of the Prophet. And as such whatever came as booty or revenue were distributed then and there by him. In the second year of the Khilafat, Abu Bakr (R) built a treasury but there was only one dirham in it at the time of his death. Following Prophet Muhammad (SM), he distributed all what he received, ten dirham to every one in the first year and twenty in the second year of his Khilafat regardless of age, status or race'.⁴⁴ Hadrat Umar al-Faruq, the second Caliph continued this practice. After

⁴¹ S.M. Imamuddin, *Some Aspects of Banking in Medieval Muslim Countries (661-1258 A. D.)*, K.T. Hossain (eds.), *Thoughts on Islamic Economics*, Dhaka : Islamic Economics Research Bureau, August, 1980, p. 181.

⁴² Muhammad Akram Khan, *op.cit.*, p. 173.

⁴³ Non- Muslims living in Muslims state having revealed books.

⁴⁴ S.M. Imamuddin, *A Political History of the Muslims (holy Prophet and pious Caliphs)* (Dhaka : Najmah & Sons Ltd., 1965), p. 241.

the conquests of Egypt, Iraq, Persia and part of the Byzantine Empire, there was rapid inflow of funds into the national exchequer.

Hadrat Umar's (R) first declaration was;

"In my view there are three things to be done with respect to the (public) money. It should be collected with due right, it should be given to whom it is due, and it should be denied improper use.⁴⁵

Hadrat Umar al-faruq raised a proposal before the Majlis al-Shura for founding a permanent treasury at Madinah and its branches in the provinces. The Majlis al- Shura approved the proposal in about 15 H/ 636 A.D. "Umar(R) took census of the Muslims and established Diwan a Persian Institution to register the names of the recipients of pensions. Aishah(R) topped the list and received 12000 dirham annually. According to the gradation, the ahl-bayt, emigrants and helpers received 4000 to 5000 dirham annually. An ordinary soldier received 500 to 600 dirham while women, children and clients received 200 to 600 dirham a year.⁴⁶

The revenue of the state was deposited into the Bayt al-Mal (Public Treasury). Under Prophet Muhammad(SM) there were six sources of revenue, which are discussed below:

- i. Zakat – 2.5% of wealth for the poor. This was only applicable on Muslims.
- ii. Jizya - defence tax paid by non-Muslims living on Muslim lands (dhimmis). However, the poor, the sick and crippled, women, children, aged, priests, and monks were exempted from this.
- iii. Ushr – a special land tax on especially large holdings (one tenth of the production).
- iv. Khiraj – a land tax

⁴⁵ Bukhari, op.cit. Vol. 4, p. 224.

⁴⁶ S.M. Imamuddin (1965), op.cit., p. 242.

- v. Ghanimah - one-fifth of the war booty. A tax on non-Muslim merchants and traders (because they didn't pay Zakah, while Muslim traders did).
- vi. Taxes on mines, khums and al-fayy (income from state land)
Details descriptions of the main sources of revenue are provided below:

Zakah, which literally means growth and purity, is a tax on Muslim capital owned beyond a certain minimum. It is an ordinance (Fard). According to the Holy Prophet of Islam (SM), it was to be taken from the rich among them in order to be given to the poor. This beneficial tax is called Zakah. The Zakah is a tax levied on capital goods and is due when one is in possession of full ownership of a productive Nisab (minimum) of property; and its rate is 2.5 percent of the value of possessions other than land. Tithe (Ushr) is a tax levied on the agricultural produce of the land. The Holy Quran enjoins upon the faithful to pay this tax in these words: "And on the day of its harvest give its Right" (6: 142). The Prophet (SM) determined its rate as, 'In what has been irrigated with rainwater, one tenth and in what has been watered with buckets or water wheels, one half of the one tenth'.⁴⁷ (Mishkat). Both these taxes were charged from Muslims only. The Zakah (growth tax) is distinguished from the other taxes because it is spent exclusively on poor and needy persons. The Holy Quran states, 'the charities are (exclusively) for the poor and needy and those who collect it and those whose hearts are to be reconciled and to free the captives and debtors and for the cause of Allah--a duty imposed by Allah' (9: 16). This tax has throughout the centuries contributed immensely to ameliorating the condition of the poor and has raised their standard of living by bringing them nearer to rich--economically and socially. This ideal tax, which is levied on idle as well as productive wealth, discourages the accumulation of wealth and ensures its investment for productive and beneficial purposes. The Prophet once remarked, 'Among you who are the guardians of orphans who possess property? Then let them trade with it and not leave it idle. So that the Zakah

⁴⁷ Mishkat.

Taxes due on it do not swallow it up'.⁴⁸ The other sources of wealth obtained in abnormal times are Ghanimah, Jizyah and Kharaj.

Ghanimah is the wealth obtained during the wars, one-fifth of which was deposited in the Bayt al-Mal (Public Exchequer). The Jizyah is a tax levied on non-Muslims in lieu of military service which is compulsory for Muslims but not for non-Muslims. The amount of Jizyah is much less than the Zakah, which is levied on Muslims only. The non-muslims paying Jizyah were exempt from compulsory military service in a Muslim state but were entitled to full protection. The Kharaj is the annual levy paid by the conquered countries to the Muslims. 'The earliest al-Fayy land was the Fadak, the income from which was spent on the Prophet's relatives, the orphans, the indigents, the way-farers and on the general welfare of the Muslim community'.⁴⁹ The public offer in which the wealth obtained through all the above-mentioned sources was deposited was known as Bayt al-Mal. In the days of the Khulafa-i-Raashidin (Pious Caliphs) when the principles of Islam were strictly followed, the Bayt al-Mal played a vital role in building up the sound economy of the Muslims. From the Bayt-al-Mal, spending was made for the welfare of the people as well as for the poor and needy. Out of this Public Treasury the needy, destitute; orphans and other charitable institutions were financed. The weak and disabled, both Muslims and non-Muslims, were granted allowances. A person who became an invalid or too old to earn his living received maintenance allowance from the Bait-al-Mal. Children without guardians were brought up at state expense.

The canals for irrigation purposes were also built from the public revenue. During Umar's(R) reign a canal was made which joined the Nile to the Red Sea. This canal facilitated transport of grains from Egypt to the Arabian Peninsula.

There was no needy person among the Arabs due to Bayt al-Mal. Earlier they constituted one of the poorest nations in the world. The faithful adherence

⁴⁸ AI-Tirmizi.

⁴⁹ S.M. Imamuddin (1965), op.cit., p. 242.

to payment of Zakah tax and the strict maintenance of Bayt al-Mal during the time of the Holy Prophet(SM) and his four companions led to the prosperity and the raising of the standard of living in Muslim countries. Thus the saying of 'the Prophet of Islam came to be true, 'Give Sadaqat freely, as a time is to come when people will offer Sadaqat and there would be none (needy person) to receive them'.⁵⁰ (Mishkat). In the short period of 30 years, the Arab economy was established on a sound footing. But during the Umayyad regime, the Bayt al-Mal was misused and instead of utilizing this fund for purely charitable and public purposes, the Caliphs henceforward used it for furthering their personal interests. Since that time the Bayt al-Mal, ceased to possess any importance and degenerated into an ordinary Imperial Treasury. Undoubtedly there were a few exceptions and Muslim rulers like Hazrat Omar Bin Abdul Aziz, Sultan Nasiruddin of Delhi and Aurangzeb Alamgir of Delhi refrained from spending money out of the public treasury. The Waqf (estate) has been instrumental in financing and thus ensuring the smooth running of a large number of public and charitable institutions all over the Muslim world, such institutions include mosques, madrassas (Islamic educational institutions) orphanages and hospitals. Large estates are attached to some of the big public institutions in Muslim countries.

'The public treasury of Bayt al-Mal played the role of an agricultural credit bank and also a commercial bank from the early days of the Umayyad. During the time of Hajjaj b. Yusuf (d. 73H/ 714A.D.), the greatest economist, according to the Muslim geographer Ibn khurdabih (d. 229-33 H/ 844-848 A.D.), lend to peasants two million dirham. Ahmad Ali says that we have no details about the conditions of this loan but surmises that no interest was charged for it".⁵¹ To facilitate the commercial activities it worked as clearing house for the merchants and advanced them money on loan. The merchants borrowed money in one place and paid back to the nearest Bayt-al-Mal in another place where the amount was credited to the account of the Public Treasury from where the money had been

⁵⁰ Mishkat.

⁵¹ S.M. Imamuddin(1965), op.cit., p. 177.

originally drawn".⁵² Money lending was an old custom approved by 'Umar b. Khattab (R). It is said: Aba Allah and Ubayd Allah, the two sons of the Caliph while passing through Iraq were given by Abu Musa Al-Ashaari the share of their mother from the public treasury of the Muslims. They invested this amount in trade, gave the amount to their mother and kept with them the profit they made. 'Umar(R) coming to know of this, said: 'I do not think that you being sons of the Caliph of the Muslims have any right to gain any undue advantage'. They enquired, 'If we had lost the money, would we not have been obliged to restore it?' Umar(R) responded, "Yes I" Hearing this one of those present there said, 'It should be treated like a loan'. His suggestion was accepted. This incident gives proof of the 'existence of money lending for trade.⁵³

4.3 Riba

Riba is an Arabic word which means 'increase', 'addition', 'expansion', or 'growth' and refers to the additional amount which a lender recovers from the borrower according to a fixed rate over and above the principal amount.⁵⁴ In the pre-Islamic period the word Riba was used conventionally to mean a class of business transactions. The common feature of these transactions was that a fixed amount was required over the principal due. The Arabs used to lend money to each other on the agreement that after a certain period of time the borrower would repay an excess amount over an above the principal sum due.⁵⁵ Another form was that a person sold a product to someone on the agreement that a specified price was payable at some future date. If at the end of the stipulated time the buyer did not pay the price, then the seller would increase

⁵² S.M. Imamuddin, *Some Aspects of Banking in Medieval Muslim Countries (661-1258 A. D.)*, K.T. Hossain (eds.), *Thoughts on Islamic Economics* (Dhaka : Islamic Economics Research Bureau, August, 1980), p. 182.

⁵³ S.M. Imamuddin(1965), *op.cit.*, p. 183.

⁵⁴ Shahid Hasan Siddiqui, "Riba, Usury & Interest-Historical and Quranic Concept", *Journal of Islamic Banking & Finance*, Vol. 10, No. 4, Oct - Dec 1993 Autumn Issue, p. 43.

⁵⁵ Shahid Hasan Siddiqui, "What is Riba?" *Journal of Islamic Banking & Finance*, Jan-Mar 1995, Vol. 12, No. 1, Winter Issue, p. 53.

the price and extend the payment period.⁵⁶ Yet another form of Riba was that Arabs would make a loan to someone on the basis of a monthly fixed return over the principal sum and if at the end of the loan period the borrower was unable to repay they would increase the monthly fixed return.⁵⁷ 'The word Riba is rendered into English as usury for want of a better substitute for it in that language'.⁵⁸ Similarly, 'the word Riba has been used for Sood (interest) in the Qur'an'.⁵⁹ Few translators of the Holy Qur'an, translated the word 'Riba' as usury and not as interest. Any rate of interest as high and low is a relative consideration but as Riba has been prohibited without any qualification, any rate above zero will be included in it for all practical purposes.⁶⁰ Confusion is created by considering the difference between the word 'interest' and 'usury' in English literature. The former is ascribed to simple interest, which is said to be permissible, and the latter is associated with compound interest, which is strictly forbidden. But Islam does not make any such distinction.

In the New Encyclopedia Britannica, usury is explained as compensation for the use of money regardless of the amount according to earlier English Law. The Oxford Advanced Learner's Dictionary, however, defines usury as 'the practice of lending money to people at unfairly high rates of interest'.⁶¹ In Islamic jurisprudence it is defined as 'an increment of money or goods having no compensation in a transaction'.⁶² It is sometimes argued that Riba means only usury, i.e. interest at excessive rate (doubling and redoubling) for consumption loans, while modest rate (interest) for productive loans are permissible. Considering the established methodology for interpretation of Qur'anic verses,

⁵⁶ S.A. Maududi, Sood (Interest) (Urdu), (Lahore : Islamic Publications, 1977), pp. 150-151.

⁵⁷ S.A. Maududi, op.cit., pp. 150-151.

⁵⁸ Muhammad Asad, The Message of the Qur'an, 1980, p. 623.

⁵⁹ S.A. Maududi, op.cit., p. 147.

⁶⁰ Muhammad Ayub, "Meaning of Riba", Journal of Islamic Banking & Finance, Vol. 10, No. 4, Oct-Dec 1993, Autumn Issue, p. 39.

⁶¹ The Oxford Advanced Learner's Dictionary (Sixth ed), p. 1433.

⁶² Abdul Azim Islahi, Economic Concept of Ibn Taimiyah (UK : Leicester, The Islamic Foundation, 1988), p. 128.

historical evidences of Pre-Islamic Arabia and contemporary economic arguments, the Federal Shaiah Court of Pakistan clarified.⁶³

- that the literal meaning of Riba is "increase' and that it denotes taking anything in access or giving less than the capital;
- that not only usury with excessive rates but any interest charged on loans or giving on deposits by the banks falls within the definition of Riba
- that it makes no difference whether a loan is taken for consumptive or productive purposes (like trade, commerce, industry);
- that indexation of loan or debt implies an excess over, and above the sum lent and thus becomes interest which is prohibited.

Thus an excess over the principal amount is Riba and it covers usury and interest both. This is strictly prohibited in Islam as it is considered unjustified enrichment and monetary advantage without a counter value.⁶⁴ Maulana Maududi treats Riba and interest as synonymous terms. He has laid down three conditions to qualify a benefit that is reaped from a loan to be treated as interest in terms of Shariah. They are:

- i. increase in the capital sum;
- ii. the increase should be related to time for which the loan is granted;
and
- iii. the basis of the transaction should be a stipulation that the borrowed would be paid back with an increase in it.⁶⁵

Imam Shafai, Imam Karkhi, and Allama Shaukafi took the same view.⁶⁶ But Imam Abu Hanifa, Imam Ahmed and Imam Maalik have differed partly. According

⁶³ Volker Nienhaus, "Conceptual and Economic Foundations of Islamic Banking", Thought on Economics, Vol. 4, No. 3 & 4, Dhaka, 1994, p. 1.

⁶⁴ Imam Al- Sarakhsi, Al-Mabsut, Vol. 13, p. 109; Al-Marghinani, Kitab al-Buyua, Vol. 3, p. 61.

⁶⁵ Syed Abul Ala Maududi, op.cit., p. 153.

to them a condition to payback more money does always make the consequential increase Riba but there can be cases of Riba without such a condition.

'For us the choice is clear because we have in support of our view the acts of the Holy Prophet (SM). It is well known that he sometimes paid more money to his creditors than was borrowed by him and termed the excess to be gift. In other words the debtors can provide benefit to the creditor as present. This permissibility militates against general provision of increase in the capital sum. If absence of a condition for paying more money than was borrowed did not make the increased payment unobjectionable the Holy Prophet (SM) would never have made such a payment. He paid more than the borrowed money as an act of kindness. He is also known to have returned a better animal than was lent to him and felt well satisfied with that benevolent act.⁶⁷

4.3.1 Elimination of Riba from the Economy

One of the important features of an Islamic financial system is that the prohibition of Riba from the economy. The Holy Qur'an specifically says that; 'Give up what remains of your demand for Riba' (2:278) and 'you shall have your capital sums' (2: 279). In view of this clear and unambiguous directive of the Holy Qur'an, all the arguments that prohibition of Riba does not cover bank interest do not merit any consideration and are automatically invalidated. Thus according to the injunctions of the Holy Qur'an, in money lending transactions, any thing recovered in excess of the principal amount is specifically prohibited by whatever name it is called, Riba, usury or interest. The controversy about Riba and interest must, therefore, come to an end, once and for all.⁶⁸ There are verses in the Holy Qur'an which are pertinent to Riba are as follows:

Sura no. 2, Al-Baqarah

⁶⁶ Maulana Ashraf Ali Thanvi, *Imdadul Fatawa*, Part III (Karachi : Darulum), pp. 185 and 269.

⁶⁷ Justice (Retd) Qadeeruddin Ahmed, *What is Riba?* Vol. 12, No. 1, Jan-March 1995, Winter Issue, p. 43.

⁶⁸ Shahid Hasan Siddiqui, "What is Riba?", *Journal of Islamic Banking & Finance*, Jan-Mar 1995, Vol. 12, No. 1, Winter Issue, p. 53.

Verse 275: Those who devour riba
 Will not stand (on the
 Day of Judgment) except
 As stands one whom
 The Evil One by his touch
 Hath driven to madness.
 This is because they say:
 "Trade is like riba".
 But Allah hath permitted trade
 And forbidden riba.
 Those after receiving
 Admonition from their Lord,
 Desist, shall be pardoned
 For the past: their case
 Is for Allah (to Judge):
 But those who repeat
 (The offence) are
 Companions of the fire: they will
 Abide therein (for ever).

Verse 276: Allah will deprive
 Riba of all blessing.
 But will nourish
 Acts of charity;
 For he loveth not
 Creatures ungrateful
 And wicked.

Verse 278: Those who believe!
Fear Allah, and give up
What remains of your demand
For al-riba if ye are
Indeed believers.

Verse 279: If ye do it not,
Take notice of war
From Allah and His Apostle:
But if ye turn back,
Ye shall have
Your capital sums:
Deal not unjustly,
And ye shall not
Be dealt with unjustly.

Verse 280: If the debtor is
In difficulty,
Grant him time
Till it is easy
For him to repay.
But if ye remit it
By way of charity,
That is best for you
If ye only knew.

Verse 281: And Fear the day
 When ye shall be
 Brought back to Allah.
 Then shall ever soul
 Be paid what is earned.
 And none shall be
 Dealt with unjustly.

Sura no. 3, Al-Imran

Verse 130: O ye who believe.
 Devour not riba
 Doubled and re-doubled
 But fear Allah so that
 Ye many (really) prosper.

Sura no.4, Al-Nisa

Verse 160: For the inequality of the Jews
 We made unlawful for them
 Certain (foods) good and wholesome
 Which had aforesaid been
 lawful for them:
 Because they had blocked off many
 From Allah's way.

Verse 161: Since they took riba
 Through they were forbidden:

And that they devoured
 Men's possessions wrongfully;
 We have prepared for those
 Among them who reject Faith
 A grievous punishment.

Sura no. 30, Al-Rum

Verse 39: That which ye lay out in riba
 So that it may increase through
 the property of (other)
 people, will have
 No increase with Allah:
 But that which ye lay out for
 charity, seeking
 The countenance of Allah
 (Will increase): it is
 These who will get a
 recompense multiplied.

Thus, the starting point of the theory of Islamic Banking and finance is that Islam prohibits Riba but permits trading. As mentioned earlier Riba is an extra payment received over and above the principal amount, regardless of the fact that extra amount is significant or insignificant. It is unjust for lender to demand a fixed return over the principal loan irrespective of what happens with the loaned money. 'The reality is that any rate of interest being high or low is a relative consideration but as Riba has been prohibited without any qualification, any rate above zero will be included in it for all practical purposes'.⁶⁹ There is a

⁶⁹ Muhammad Mohasin Ali and Md. Abdul Awwal Sarker, "Islamic Banking : Concept, Features and Operational Methodology", Thoughts on Economics, Vol. 5, No. 3 & 4, July-December, 1995, p. 35.

consensus among the Islamic jurists and scholars that Riba is an additional payment over and above the amount lent and the same is prohibited according to Islam Shariah. From Anas Ibn Malik: The Prophet (SM) 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'.⁷⁰ The Islamic Fiqh Academy established by the OIC, in its second session held in Jeddah, Saudi Arabia, from 22-28 December, 1985 declared that 'any increase or profit on a loan which has matured, in return for an extension of the maturity date, in case the borrower is unable to pay, any increase or profit on the loan at the inception of the loan agreement, are both forms of usury's (Riba), which is prohibiting under the Shariah'.⁷¹ However, Islam does not disapprove the sharing of benefits of productive loan by the supplier of funds if it is taken in the form of profit. The same verse of the Holy Qur'an, which prohibits interest, approves profit (2: 275).

4.3.2 Types of Riba

Riba are of two kinds such as Riba al-nasia and Riba al-fadl. The word nasia means 'delay granted to the debtor'. It is used in this sense because the lender, so to say, overlooks the delay in payment of the debt in consideration of something in excess over the principal. The word fadl signifies the excess charged in the exchange or sale of things of homogeneous nature or similar of the same species. There is marked difference between the two. While nisia relates to the excess charged in loan transactions, fadl relates to the excess charged in sale transactions. Riba al-nisia relates to financial transactions only and in each of those transactions an excess amount of money demanded over the principal sum loaned for a specified period of time. Riba al-fadl refers to the barter trade of identical commodities. There is an authentic Hidith:

⁷⁰ Siddiqui, Shahid Hasan, "What is Riba?" Journal of Islamic Banking & Finance, Jan-Mar 1995, Vol. 12, No. 1, Winter Issue, p. 54.

⁷¹ The Islamic Fiqh Academy, Organization of Islamic Conference, Resolution No. 10 concerning the ruling on dealing with Islamic Banks, adopted in its second session held in Jeddah, Saudi Arabia, from 22-28 December 1985.

Abu Sa'id Khudri said: The prophet Muhammad (SW) told that 'gold in return for gold, silver in return for silver, wheat in return for wheat, barley in return for barley, dates in return for dates and salt in return for salt, can be traded if and only if they are in the same quantity and that should be hand to hand. If someone gives more or take more, than he is engaged in Riba and accordingly has committed a sin'.⁷²

The gain, which has been banned by Qur'an, is Riba al-nesa which expression refers to the monetary benefit that accrues on a debt. It is also called the Qur'anic Riba, or Real Riba or Manifest Riba or Riba al-jahiliyya. 'Since it was a practice of the pre-Islamic period of history, it called Riba al-jahiliyya also means Riba of the ignorant era. All are agreed that the Holy Qur'an directly forbids this kind of Riba only and no other. The undue gain, which was found in sales and exchanges, has not yet been dealt within the Qur'an. It was prohibited by Holy Prophet (SM) by his own directives and is known as Riba al-Fadl. The origin of the first category is the Qur'an and that of the second is Sunnah. ... The distinction is so clear that Maulana Maududi has called the second category, namely, Riba al-fadl to be an adjunct of Riba and not Riba.

It is, thus, important to appreciate that Riba al_fadl is involved in transactions of sales and exchanges and has been prohibited by Holy Prophet(SM), whereas Riba al_Nasia represents the benefit that accrues on a debt and has been prohibited by Holy Qura'an. The fiqh agree that there has not been slightest doubt regarding prohibition of Riba al-nisia. The judgment of Federal Shariat Court of Pakistan on interest (Riba) observes;

'There is no commentator of the Holy Qur'an, no narrator of Hadith, and no jurist of Islamic Fiqh worth the name who has even expressed or even mentioned any doubt regarding any obscurity or ambiguity in its meaning. The

⁷² S.A. Maududi, op.cit. p. 165; and Mufti M Shafi, Mas'ala-e-Sood (The Problem of Interest) (Updated), (Karachi : Idarat-ul-Ma'arif), p. 18.

difference of opinion whatever is found is regarded "Riba al_fadl" and that is out of discussion in the context of bank interest which is under our consideration'.⁷³

4.4 Profit

Profit means excess of income over expenditure i.e. revenue minus cost. Revenue means the value of the products or services produced by the business and cost means the amount expensed to produce the same. If the difference between revenue and cost is negative than it is called loss. 'By profit we mean the operating surplus which is always a futuristic concept at investment point. It can of course be forecast to a reasonable extent, but can not be calculated for certain till the enterprise has worked for sometime and the surplus has accrued or is realized'.⁷⁴ Profit is the reward of the owners for investing money and taking risk. A risk for loss is associated with profit. Contrarily, interest is risk-free.

'Islamic Banks permit and encourage various forms of ownership and co-ownership with their clients against appropriate profit sharing agreement. To calculate bank's share of profit (also loss) merely the bank's own records of capital accounts are not enough. The records of the business are also needed to find out the total profit and the bank's share in it'.⁷⁵

One of the basic changes envisaged in the wake of the Islamic transformation of a modern economy is the replacement of the institution of interest by profit sharing, in pursuance of the Qur'anic percept: 'Allah has permitted trade and forbidden interest (2:275).

The permission of trade implies the permission to profit thereby. 'In Islamic Jurisprudence literature, profit is defined as the increase in the value of

⁷³ Shahid Hasan Siddiqui, "What is Riba?" Journal of Islamic Banking & Finance, January-March 1995, Vol. 12, No. 1, Winter Issue, p. 55.

⁷⁴ K.T. Hosain, "Running an Economy without Riba", K.T. Hosain (eds.), Thoughts on Islamic Economics (Dhaka : Islamic Economic Research Bureau, August, 1980), p. 160.

⁷⁵ M Azizul Huq, "Islamic Banking : Concept & Practices", Thoughts on Economics, Vol. 2, No. 1, (Dhaka : Islamic Economic Research Bureau, 1981), p. 14.

assets (fixed or mobile) actually realized in exchange'.⁷⁶ In the Holy Qur'an the term profit is used only once:

'These are they who have purchased error in exchange for guidance. Their trade has brought them no profit' (2:16).

'According to Islamic concept of economic activity and profit, the provider of capital and the businessman bear together the risks of investment. As per priori agreement profit is shared between the two parties after the recovery of capital'.⁷⁷ Thus profit is the joint product of capital investment and business effort. It is the consequence of a successful business venture. Profit means an addition to capital, while loss means a reduction of capital. In case of loss no addition to capital is possible in spite of business effort.

Profit is related with the purchase, re-purchase, and sale of goods and services or like that item but interest is related with loan and times. Profit is uncertain whereas interest is pre-fixed and certain.

4.5 Profiteering

Profit that is unreasonably high and does not conform to general welfare of the society is called profiteering. It is also prohibited in Islam and avoided by Islamic Banks.

⁷⁶ Monzer Kahf and Tariquillah Khan, "Principal of Islamic Financing" (A Survey), Research Paper, No. 16, 1st ed, (Islamic Development Bank: Islamic Research and Training Institute, 1992), p. 350

⁷⁷ Muhammad Mohasin Ali and Md. Abdul Awal Sarker, "Islamic Banking : Concepts, Features and operational Methodology", Thoughts on Economics, Vol. 5, No. 3 & 4, (Dhaka: Islamic Economics Research Bureau, July-December 1995), p. 34.

Chapter 5
Islamic Banking in
Bangladesh

Chapter 5

Islamic Banking in Bangladesh

5.1 Genesis

Bangladesh is one of the largest Muslim countries in the world. The people of this country are deeply committed to Islamic way of life as enshrined in the Holy Qur'an and the Sunnah. But it remains a deep cry in their hearts to fashion and design their economic lives in accordance with the norms and values of Islam.

Unfortunately Bangladesh inherited an interest based banking system, which was introduced here by the Colonial Government when it was a part of British Colony for about 200 years. Bangladesh became a part of Pakistan in 1947 and continued till independence in 1971. When Bangladesh was a part of Pakistan, the banking system obviously came under the Muslim control but the system did not change. The then Muslim administrators did not take any practical steps to implement a financial system based on Islamic Shariah.

Immediately after independence Bangladesh Government nationalized almost all the financial institutions and Banks in Bangladesh. But due to failure in administering them properly the Government returned most of the banks to their owners within a short span of time. The Islamic banking system with a view to operating interest-free welfare banking appeared in the financial horizon of Bangladesh only two decades ago. In view of the emergence of Islamic banks in a number of Muslim countries, Bangladesh as a member of the Organization of Islamic Conference and a founder member of the Islamic Development Bank had been making careful study of the various issues connected with the establishment of interest free Islamic banks in the country. On the basis of various studies and recommendations of the seminars on Islamic Banking held in the country, the Government had decided on principle to allow operations of Islamic Banks in the country. At present there are over 50 Banks working in the country, out of which only six Banks (including one foreign Bank), one non-

banking financial institution and two Islamic banking branches of a traditional bank, Prime Bank Limited have been conducting their businesses on the basis of Islamic Shariah.

Two professional bodies 'Islamic Economic Research Bureau' (IERB) and 'Bangladesh Islamic Bankers Association' (BIBA) were taking practical steps for imparting training on Islamic Economics and Banking to a group of bankers and arranging some national and international seminars/workshops to mobilize local and foreign people and attract investors to come forward to establish Islamic banks in Bangladesh. Their professional and right thought-out activities were reinforced by a number of Muslim entrepreneurs working under the aegis of Muslim Businessman Society (MBS). The body concentrated mainly on mobilizing equity capital for the emerging Islamic bank. Due to the continuous and dedicated work of the above groups and individuals and active support from the government, Islami Bank Bangladesh Limited could be established in early eighties'.¹

Islamic Banks have been working in Bangladesh for two decades with Western style interest based Banks. At present there are six Islamic Banks and one non-bank financial Islamic institution operating in Bangladesh:

1. Islamic Bank Bangladesh Limited (1983)
2. The Oriental Bank Limited (1987) (Al Baraka Bank Bangladesh Limited was renamed as the Oriental Bank Limited)
3. Al-Arafah Islamic Bank Limited (1995)
4. Social Investment Bank Limited (1995)
5. Shamil Bank of Bahrain EC, Dhaka, Bangladesh (1997)
6. Shahjalal Bank Limited (2001)
7. Islamic Finance & Investment Limited (2001), a Non-bank financial Institution

¹ Md. Abdul Awal Sarker, "Islamic Banking in Bangladesh : Performance, Problems and Prospects", *International Journal of Islamic Financial Services*, Vol. 1, No. 3, October-December 1999, p. 2.

Besides, Prime Bank Limited has opened two Islamic Banking Branches and some other Commercial Banks in the private sector have opened Islamic Bank counters.

1. Exim Banks Limited: Islamic Counters
2. Jamuna Bank Limited: Islamic Counters
3. Premier Bank Limited: Islamic Counters
4. The City Bank Limited: Islamic Counter
5. Dhaka Bank Limited: Islamic Counters

5.2 Government Policy towards Islamic Banking

The attitude of the Government of the People's Republic of Bangladesh (GOB) towards Islamic banking and Islamic financial system has been all through positive. Government of Bangladesh supports Islamic Banking movement within and outside the country but as a strategy it believes in a gradual and cautious implementation of the system. This fact is revealed in the following official statements and actions:

- i) As one of the twenty-six members, Bangladesh signed the charter of the Islamic Development Bank in the Finance Ministers Conference of the Muslim Countries held in Jeddah in August 1974. According to the charter, the Islamic Development Bank is assigned with the responsibility of providing technical assistance to the member countries, extending training facilities for human resources development of the member countries and to undertake research for enabling the economic, financial and banking activities in the Muslim countries (obviously including Bangladesh) to conform to the Shariah.

By signing and adopting the above provisions of the Islamic Development Bank charter, the member countries including Bangladesh have implicitly agreed to bring the economic, financial and banking systems in their respective countries in line with the Shariah.

- ii) The Islamic Foreign Ministers Conference held in Dakar, Senegal in April 1978, recommended to the members of the Organization of Islamic Conference to make systematic efforts to establish Islamic Banks gradually. Bangladesh, as a member of the Organization Islamic Conference, participated in the conference and subscribed to the above recommendation.
- iii) Islamic Foreign Minister Conference was held at Islamabad in May 1980, where Bangladesh proposed that steps should be taken for the development of an Islamic International Banking system with branches in all the Islamic countries so as to coordinate and expand credit facilities within the Islamic community.
- iv) The Third Islamic Summit Conference was held in Makka and Taif in January 1981. In that conference Shaheed President Ziaur Rahman of Bangladesh suggested that 'the Islamic countries should develop a separate banking system of their own in order to facilitate their trade and commerce. Both in public and private sectors the Islamic countries would promote joint ventures and financial institutions, which could profitably use Islamic investments. We (the Islamic countries) should propose an Islamic Development Authority or Corporation, which could function primarily on a commercial basis. The activities of the Islamic Development Bank should be expanded considerably not only in terms of project financing but also in the field of research and consultancy'. The statement of Shaheed Prsiden Ziaur Rahman indicated favorable attitude of the Government of the People's Republic of Bangladesh towards establishing Islamic Banks and Financial Institutions in the country.

The inference from the discussion above is that the Government of the People's Republic of Bangladesh is inclined to develop a national banking system, which could meet the needs of the Muslim community.

5.3 Government Level Actions

In line with the above policy the following official actions were taken in respect of the introduction of Islamic banking in Bangladesh.

- i) In November 1979, Mr. Muhammad Mohsin, the then Ambassador of Bangladesh in the United Arab Emirates sent a letter to the Foreign Secretary, Ministry of Foreign Affairs, GOB recommending establishment of an Islamic Bank in Bangladesh in line with the Dubai Islamic Bank. He also enclosed a report on Islamic Banking Seminar organized by Dubai Islamic Bank.
- ii) In December 1979, the Banking Wings of the Banking and Investment Division, Ministry of Finance, Government of the People's Republic Bangladesh wrote to Bangladesh Bank seeking their opinion for the establishment of an Islamic Bank in the country.
- iii) In November 1980, Mr. A. S.M. Fakrul Ahsan, the then Director of Research, Bangladesh Bank was deputed to study the workings of a few Islamic Banks working in the Middle East. He visited the following Banks:
 - a) Dubai Islamic Bank in Dubai
 - b) Faisal Islamic Bank of Egypt
 - c) Naser Islamic Bank of Cairo, Egypt, and
 - d) The Cairo Office of the International Association of Islamic BanksMr. Ahsan submitted his report to the GOB recommending the establishment of Islamic Bank in the country.
- iv) On 15 December 1980 the then Governor of Bangladesh Bank inaugurated an international seminar on Islamic Banking in Dhaka. The seminar was participated by, amongst others, the delegates from the Islamic Development Bank and the Saudi Arabian Monetary Agency.

The Bangladesh Bank Governor in his inaugural speech recommended early introduction of Islamic banking in the country.

- v) On 18 and 19 March 1981 Bangladesh Institute of Bank Management, the apex-training institute in the banking sector organized a national seminar on Islamic Banking. The seminar was inaugurated by the Deputy Governor of Bangladesh Bank and attended by a large number of professional bankers and economists of the country. In that seminar a resolution was adopted by recommending an early introduction of Islamic banking in the country.
- vi) In March 1981, the Bangladesh Bank Governor attended a meeting of the Governors of Central Banks and Monetary Agencies of the member countries of the Organization of Islamic Conference held in Khartoum, Sudan to consider a report on the promotion, regulation and supervision of Islamic Banks. They took a decision to prepare a common framework for the purposes.
- vii) In early April 1981, Banking and Investment Division of the Ministry of Finance, GOB wrote a letter to Bangladesh Bank advising the latter to undertake an experiment in the matter of Islamic banking by opening a counter and maintaining separate ledgers in all the branches of the nationalized commercial banks in line with that of Pakistan.
- viii) On 13 April 1981 the representative from the six nationalized Banks and two Specialized Banks of the country met the Governor of Bangladesh Bank. They discussed the proposal of the Finance Ministers mentioned above. The meeting was presided over by the Governor of Bangladesh Bank. Initiating the discussion on this subject, the Governor stated that Pakistan had introduced counters for Profit & Loss Sharing (PLS) Islamic Banking with separate ledgers in all the branches of the nationalized Banks with effect from 01 January 1981 after making adequate preparation during the last several years, particularly after completing

large-scale training of personnel during the last two years. Moreover, introduction of Islamic banking was the constitutional obligation in Pakistan. Since our nationalized commercial banks do not yet have any experience or necessary preparations, it would not be advisable to undertake the task of opening separate Islamic Banking counters with separate ledgers in all their branches at a time, but at the same time the Governor felt that introduction of Islamic Banking on a manageable scale should also not be differed any longer. After thorough discussion at the meeting they decided that the introduction of Islamic Banking must not be delayed any further but initially it may be limited to the metropolitan cities and the district towns instead of spreading it to over 4000 branches.

- ix) From 9 to 11 June 1981 an International Seminar on Islamic Banking and Insurance was held at Geneva. GOB deputed a senior executive of the Bangladesh Bank to participate in the above seminar. A thorough discussion was held on different issues of Islamic banking and Insurance.
- x) From 29 August to 17 September 1981 an Advanced Course on Islamic Banking was held at Cairo. Professional bankers from different Muslim countries participated in the program. Bangladesh deputed 4 (four) senior bank officials: two from Bangladesh Bank and two from the Nationalized Commercial Banks to the above-mentioned program.
- xi) From 29 October to 24 November 1981, a 30 (thirty) days full time training course on Islamic banking was held at Sonali Bank Staff College, Dhaka. The course was attended by 37 (thirty seven) senior and mid-level executives from the Bangladesh Bank, 8 (eight) from Public Sector Banks, Bangladesh Institute of Bank Management, and the proposed private sector Islamic Bank i.e. the International Islamic Bank of Dhaka Limited (the name was changed latter on as Islami Bank Bangladesh Limited).

- xii) From 18 to 30 January 1982, Bangladesh Institute of Bank Management (BIBM) organized the second training course on Islamic banking in the country. It was participated by 32 (thirty two) professional bankers from Bangladesh Bank, six Nationalized Banks and two Specialized Banks.
- xiii) On 17 October 1982 the representatives of the six Nationalized Banks and two Specialized Banks of the country met again under the chairmanship of the Governor, Bangladesh Bank and reviewed their earlier decision taken on 13 April 1981. The bankers discussed the working paper prepared by Bangladesh Bank on Islamic banking. After detailed discussion it was decided that all Nationalized Commercial Banks would start Islamic Banking on experimental basis in all districts, either through a separate Branch or a Booth at the option of the Bank.
- xiv) On 01 November 1982 an Appraisal Mission from Islamic Development Bank- Jeddah arrived at Dhaka. The purpose of the mission was to study and report on the feasibility of the proposed joint venture Islamic bank in the private sector and to decide about Islamic Development Bank's participation in its equity. The Islamic Development Bank Mission stayed in Dhaka till 08 November 1982 and met the senior executives of Bangladesh Bank, and Ministry of Finance. Their opinion was in favor of the establishment of an Islamic Bank in the private sector in Dhaka.
- xv) Bangladesh Islamic Bankers Association (BIBA) a voluntary association of bankers committed to the cause of a banking system based on Islamic Shariah conducted a 30(thirty) days long evening training course on Islamic Banking. The program was participated by 211 (two hundred eleven) senior and mid-level executives of different Banks and allied Institutions.

xvi) In August 1982, Islamic Economics Research Bureau (IERB), Dhaka conducted an evening course on Islamic Banking which was participated by 30 mid-level bankers and economists.

xvii) During 1977 to 1982 as many as five seminars were held in the country to create awareness among the general public regarding the necessity of Shariah based banking in Bangladesh:

Period	Venue	Sponsors
July, 1977	Dhaka	Islamic Economic Research Bureau, Dhaka
Dec., 1980	Dhaka	Islamic Economic Research Bureau, Dhaka
Jan., 1981	Dhaka	Working Group for Islamic Banking in Bangladesh
March, 1981	Dhaka	Bangladesh Institute of Bank Management
April, 1981	Chittagong	Baitush Sharf Islamic Gabeshana Partistan
Dec., 1982	Dhaka	Islamic Foundation of Bangladesh

All these seminars drew large attendance from all walks of life and called upon the concerned authorities to introduce Islamic banking in Bangladesh within the shortest possible time.

xviii) Similarly, the elite groups of the society have shown equal interest to Islamic banking. Rotary Club and Lions Club arranged the following indoor lectures on Islamic banking in 1982:

Period: 1982	Venue: Dhaka	Sponsors
February 28	Hotel Intercontinental	Lions Club
April 2	Hotel Sonargaon	Rotary Club
August 17	Hotel Intercontinental	Rotary Club

Mr. M Azizul Huq, a senior banker and executive of a nationalized commercial bank (Sinali Bank) delivered all those lectures. The lectures were followed by thread bear discussions by the members present. The members welcomed Islamic Banking.

xix) Bangladesh Bank issued license for establishment of the first Islamic Bank in Bangladesh in 1983. The Government provided money for five

percent share in the paid up capital of the newly established Islamic bank. Bangladesh Bank has granted some preferential provisions for Islamic banks in Bangladesh. Those are:

- Islamic Banks in Bangladesh are allowed to keep Statutory Liquidity Requirement (SLR) at 10 percent of the total deposit, while it is 20 percent for interest-based banks.
- Islamic Banks are allowed to fix their profit-sharing ratios and mark-ups ratios independently commensurate with their own policy and banking environment. This has provided Islamic Banks to follow Shariah principles independently.

5.4 Islamic Banks in Bangladesh

5.4.1 Islami Bank Bangladesh Limited

The establishment of Islami Bank Bangladesh Limited (IBBL) is the first step towards materializing a long cherished dream of the people of Bangladesh for doing their banking transactions in line with what is prescribed by Islam. It is incorporated on 13 March 1983. The Bank obtained license from Bangladesh Bank on 28 March 1983 and began its functions on 30 March 1983 with the commitment of Shariah based banking system through its main branch in Dhaka. This Bank is the first of its kind in Southeast Asia. It is committed to conduct all banking and investment activities on the basis of interest-free profit-loss sharing system. It introduced a full package of banking services on 12 August 1983. It is a Multinational Bank of 22 private sponsors of Bangladesh, the Government of Bangladesh, Islamic Development Bank, and 13 Banks and Financial Institutions of the Middle Eastern Muslim countries.² The foreign sponsors contribute 64% of the total capital and the local sponsors contributed 36% of the same. With the active co-operation and participation of Islamic Development Bank (IDB) and some other Islamic Banks, financial institutions, government bodies and eminent personalities of the Middle

² Source, Internet: <http://www.banglapedia.org/>, copyright by Asiatic Society of Bangladesh.

East and the Gulf countries, Islami Bank Bangladesh Limited has by now earned the unique position of a leading Private Commercial Bank in Bangladesh. The names of the foreign and local sponsors are mentioned below:

a) Foreign Institutional Sponsors are

- i) The Islamic Development Bank (IDB), Jeddah, kingdom of Saudi Arabia
- ii) Kuwait Finance House, Kuwait
- iii) Jordan Islamic Bank, Jordan
- iv) Islamic Investment and Exchange Corporation, Doha, Qatar
- v) Bahrain Islamic Bank, Bahrain
- vi) Islamic Banking System International Holdings-S.A. Luxemburg
- vii) Al-Raji Company for Currency Exchange and Commerce, Kingdom of Saudi Arabia
- viii) Dubai Islamic Bank, Dubai, United Arab Emirates
- ix) Public Institution for Social Security, Kuwait
- x) Kuwait Ministry of Awqaf and Islamic Affairs, Kuwait
- xi) Ministry of Justice, Department of Minor Affairs, Kuwait

Two eminent personalities of Saudi Arabia are also the sponsors of Islami Bank Bangladesh Limited:

- xii) Fouad Abdul Hameed Al-Khateeb(late), Kingdom of Saudi Arabia
- xiii) Ahmed Salah Jamjoom, Kingdom of Saudi Arabia

b) Local sponsors are:

- i) Mohammad Abdur Razzaque Laskar(Late)
- ii) Mofizur Rahman(Late)
- iii) Barriester Tamizul Haque
- iv) Mohammad Younus

- v) Mohammad Shafiuddin Dewan
- vi) Mohammad Bashiruddin
- vii) Mohammad Hussain (Late)
- viii) Nasiruddin Ahmed
- ix) Mohammad Mosharraf Hossain
- x) Mohammad Malek Minar
- xi) Zakiuddin Ahmed
- xii) M.A. Rashid Chowdhury
- xiii) Engineer Md. Mustafa Anwar
- xiv) Mohammad Abdullah
- xv) Serajuddowla
- xvi) Mohammad Nuruzzaman
- xvii) Abul Quasem
- xviii) A.K. Fazlul Haque
- xix) Engineer Mohammad Dawood Khan
- xx) Shah Abdul Hannan (Representative, Ibn Sina Trust)
- xxi) AKM Nazir Ahmed (Representative, Bangladesh Islamic Centre)
- xxii) Prof. Mohammad Sharif Hussain (Reprehensive, Islamic Economic Research Bureau)
- xxiii) Moulana Mohammad Abdul Jabbar (Late) (Representative, Baitush Sharaf Foundation Limited)

The capital is distributed as under:

Foreign Sponsors	70%
Local Sponsors	15%
Bangladesh Government	5%
Local Public	10%
Total	100%

A 23-member Board of Directors elected by the shareholders manages the Bank. Of the Directors, 9 are foreigners and 14 are local. One Bangladeshi Director is selected as the Chairman of the Board.³ To assist the Board there is another powerful body of the Islami Bank Bangladesh Limited named 'Executive Committee'. The Board nominates six members of the committee. A representative from the Shariah Council also takes part in the above committee.

There is a 10-member Shariah Council comprising of prominent Ulema, reputed Bankers, renowned Lawyers and eminent Economists. The Shariah Council has been playing a vital role in advising and guiding on the implementation and compliance of Shariah principles in all the activities of the Bank particularly on the Modes of Investments. Members of the Shariah Council meet frequently and deliberate on different issues confronting the Bank on Shariah matters. Total number of such meetings was 13 during 2000.⁴ The members of the Shariah Council also conduct inspection of Branches so as to ensure that the Shariah principles are implemented and complied with by the Branches of the Bank.

The Bank started its banking operations with an authorized and paid up capital of Tk.500 million and Tk.67.5 million respectively. The capital is divided into ordinary shares of Tk.1000 each. The Reserve Fund of the bank stood at Tk.1759.65 million as on 31 December 2000.⁵ Total deposits stood at Tk.32, 113 million and total number of depositors rose to 1,116,006 as on 31 December 2000.⁶ The modes of investment include Muda'raba, Musharaka, Hire Purchase (under Shirkatul Meelk), Bai-Murabaha, Bai-Muajjal, Purchase and Negotiation, and Quard-e-Hasan. The modes of deposits include Muda'raba Savings Deposits,

³ *Islamic Bank : An Era of Progress* (Dhaka : Public Relations Department, Islami Bank Bangladesh Limited, July 1995), p. 10.

⁴ *Annual Report-2000*, p. 25.

⁵ *Annual Report-2000*, p. 13.

⁶ *Annual Report-2000*, p. 15.

Muda'raba Special Notice Deposits, Muda'raba Term Deposits ranging from 6 to 36 months, Muda'raba Hajj Savings Deposits, Muda'raba Special Savings (pension) Deposits of 5 and 10 years, and Muda'raba Savings Bond of 5 and 8 years. The Bank also provides all sorts of banking services to its customers.

'Moreover, the Bank performs some other social development activities as part of its social commitment and for establishing the values of Islam and to create a social environment which is directed by the Creator, Allah'.⁷

'The special feature of the investment policy of the Bank is to invest on the basis of Profit Loss Sharing System in accordance with the tenets and principles of Islamic Shariah. Earning profit is not the only motive and objective of the Bank's investment policy rather emphasis is given in attending social good and in creating employment opportunities".⁸ The bank adopted a 7-year Perspective Investment Plan in January 1995 and put into implementation. The Plan envisages composition of the investment pool with 2.5% for Agriculture & Rural Investment, 18% for Industrial Term Investment, 13% for Industrial Working Capital, 10% for Housing & Real Estate, 4% for Transport & Communication, 0.5% for Electricity, Gas, Water & Sanitation Services, 2% for Storage, 43% for Import, Export, and Local Trade & Trade related activities, 1% for Poultry and Dairy, 2% for Rural Development Scheme, 2.5% for other Special Schemes, 0.5% for Micro Industries and 1% for other productive purposes by the end of the plan period i.e. the year 2002.

Keeping the same in view, side by side, with commercial and industrial investment operations, many Special Investment Schemes like i) Rural Development Scheme, ii) House-hold Durable Scheme, iii) Investment Scheme for Doctors, iv) Transport Investment Scheme, v) Mirpur Silk-weavers'

⁷ Jahangir Alam, "An Attempt to Measure Productivity of Islamic and Conventional Banks in Bangladesh : A Comparative Study", *Thoughts on Economics*, Vol. 10, No. 3 & 4, (Dhaka: Islamic Economic Research Bureau, July-December 2000, p. 24.

⁸ *Islamic Bank : An Era of Progress* (Dhaka : Public Relations Department, Islami Bank Bangladesh Ltd., July 1995), p. 15.

Investment Scheme, vi) Small Business Investment Scheme, vii) Agricultural Implements Investment Scheme, viii) Car Investment Scheme, ix) Housing Investment Scheme, x) Poultry Investment Scheme, xi) Small Transport Investment Scheme, xii) Micro-Enterprise Investment Scheme, xiii) Real Estate Investment Program, targeting different economic groups, have been introduced by the Bank over the years.⁹

i) Special Features of Islami Bank Bangladesh Limited:

Islami Bank Bangladesh Limited is committed to manage its operations as per Islamic Shariah. Islami Bank Bangladesh Limited through its steady progress and continuous success has, by now, earned the reputation of being one of the leading Banks of the country. The special features of Islami Bank Bangladesh Limited are summarized below.¹⁰

- All its activities are conducted on interest-free basis according to Islamic Shariah.
- Investment is made through different modes permitted under Islamic Shariah.
- Investment Income of the Bank is shared with the Mudaraba depositors according to a ratio to ensure a reasonably fair rate of return on their deposits.
- Its aims are to introduce a welfare-oriented banking system and also to establish equity and justice in the field of all economic activities.
- It extends socio-economic and financial services to the poor, helpless and low-income group of the people for their economic emancipation particularly in the rural areas.
- It plays a vital role in human resources development and employment generation particularly for the unemployed youths.

⁹ *Annual Report-2000*, p. 16.

¹⁰ *Annual Report-2000*, p. 13.

- Its aim is to achieve balanced growth & equitable development of the country through diversified investment operations particularly in the priority sectors and in the less developed areas.

ii) Aims and Objectives of Islami Bank Bangladesh Limited:

The main objective of Islami Bank Bangladesh Limited is to offer interest-free banking system based on Islamic Shariah. In addition to the main objective Islami Bank Bangladesh Limited have the following objectives.¹¹

- To establish participatory banking instead of banking on debtor-creditor relationship
- To invest on profit and risk sharing basis
- To accept deposits on Mudaraba & Al-Wadiah basis
- To establish a welfare-oriented banking system
- To extend cooperation to the poor, the helpless and the low-income group for their economic emancipation
- To play a vital role in human resources development and employment generation
- To contribute towards balanced growth and development of the country through its investment operations particularly in the less developed areas
- To contribute in achieving the ultimate goal of the Islamic economic and financial system

iii) Functions of Islami Bank Bangladesh Limited

Islami Bank Bangladesh Limited renders almost similar services to its customers like interest based conventional banks. The functions of Islami Bank Bangladesh are appended below:¹²

¹¹ *Islamic Bank : An Era of Progress* (Dhaka : Public Relations Department, Islami Bank Bangladesh Ltd., July 1995), p. 11.

¹² *Islamic Bank : An Era of Progress* (Dhaka : Public Relations Department, Islami Bank Bangladesh Ltd., July 1995), p. 10.

- To maintain all types of deposit accounts
- To make investment
- To conduct foreign exchange business
- To extend other banking services

5.4.2 The Oriental Bank Limited

Al Baraka Bank Bangladesh Limited is the second Islamic Bank of the country now renamed as Oriental Bank Limited. It is a joint venture Bank with Al Baraka Group of Saudi Arabia, Islamic Development Bank, Jeddah, Kingdom of Saudi Arabia; and the Government of the People's Republic of Bangladesh & Local sponsors.¹³ 'The bank was incorporated on 30 April 1987 as a public limited company to undertake and carryout all banking, financial and business activities, transactions and operations in strict compliance with the principles of Islamic Law (Shariah) avoiding usury in credit and sales transactions and any practice which amounts to usury'.¹⁴ The Bank has been authorized by the Bangladesh Bank to carry on the banking business in Bangladesh with effect from 04 May 1987. However, it commenced banking operations on 20 May 1987 with an authorized capital of Tk.600 million and paid up capital of Tk.150 million divided into 150,000 ordinary shares of TK.1000 each. The paid up capital increased several times and stood at TK.259.6 million on 31 December 1999.¹⁵ 'In March 2001, the Bank had 35 branches'.¹⁶ Its Head Office is at 63, Dilkusha Commercial Area, Dhaka.

A 13-member Board of Directors elected by the shareholders manages the Bank. Among the members one is elected as Chairman and another one as Vice Chairman of the Board. As the Board of Directors could not meet frequently the day-to-day affairs of the Bank is managed by an Executive Council of Seven

¹³ *Annual Reports-1999*, p. 2.

¹⁴ *Annual Report-1999*, p. 25.

¹⁵ *Annual Report-1999*, p. 24.

¹⁶ Source, internet: www.banglapedia.org.copyright by Asiatic Society of Bangladesh.

Directors. The executive president is the Chief Executive Officer of the Bank. The Bank has a 3-member Shariah Council. Among the three one is Chairman, one is Vice Chairman and the remaining one is a Member of the Shariah Council. They ensure compliance of Islamic Shariah (Law) in all of its banking and financial activities.

On 31 December 1999, the total deposit of the bank was Tk.8834 million. (It increased to Tk.10, 736.5 million on 31 December 2000.¹⁷ The types of deposits accepted by the Bank include:

- i) Muda'raba Term Deposits
- ii) Muda'raba Deposits
- iii) Al-Wadiah Current Deposits
- iv) Muda'raba Short Term Deposits
- v) Contingency Deposits, Deposit in Foreign Currency, and Deposits in other accounts
- vi) Monthly Profit Scheme
- vii) Marriage Savings Scheme
- viii) Higher Education Savings Scheme
- ix) Savings Scheme for Children
- x) Future Deposit Savings Scheme for 5 Years and 10 years
- xi) Housing Savings Scheme
- xii) Privileged Citizen Scheme
- xiii) 6 Years Double Growth Scheme

On 31 December 1999 the amount of total investment stood at Tk.6187.8 million. The amount of investment increased to Tk8760.6 million on 31 December 2000. The modes of investment comprise:

¹⁷ Source, internet: www.banglapedia.org. copyright by Asiatic Society of Bangladesh.

- i) Mudaraba Investment
- ii) Musharaka Investment
- iii) Murabaha Investment
- iv) Bai-mujjal Investment
- v) Hire Purchase Investment
- vi) Commodity Finance, and Investment in Shares, and Other Investment

5.4.3 Al-Arafah Islami Bank Limited

Al Arafah Islami Bank Limited was established (registered) as a public limited company on 18 June 1995. The inaugural ceremony took place on 27 September 1995 and has already completed successful 7 years of operation. Its Head Office is located at Rahman Mansion, 161, Motijheel Commercial Area, Dhaka. Few renowned Islamic personalities and pious businessmen of the country are the sponsors of the Bank. As on 31 December it had 40 branches throughout the country. The authorized capital of the Bank is Tk.1000 million and the paid up capital is Tk.506 million as on 31 December 2003. The total reserve fund as on 31 December 2003 stood at Tk.268.8 million. The special features of the Bank are as follows:

- All activities of the bank are conducted according to Islamic Shariah where profit is the legal alternative to interest. Instead of taking interest the Bank invests through different modes, like Mudaraba, Musharaka, Murabaha, Bi-muajjal, Hire Purchase on the basis Shirkatul Meelk, Leasing, Qard-e-Hasan, etc. which are legal in the eye of Islamic Shariah.
- The bank is committed towards establishing welfare oriented banking system.
- The Bank strives to improve the economic condition of the poor segment of the society.

- According to the needs and demands of the society and the country as a whole the Bank invests money in different Halal businesses. The Bank participates in different activities aiming at creating jobs, implementing development projects taken by the government and developing infrastructure.
- The Bank is committed to establish an economic system through social justice and equitable distribution of wealth. It is committed to bring about changes in the underdeveloped rural areas for ensuring balanced socioeconomic development of the country through micro credit program.
- According to Mudaraba system, the depositors are the partners of the investment income of the Bank. The Bank distributes 70% of the investment income among the Mudaraba depositors.
- The Bank provides excellent services to the customers imbued with Islamic spirit of brotherhood, peace and fraternity and by developing an institutional cohesion.
- The Bank is contributing to economic and philanthropic activities side by side. Al Arafah Islami Bank English Medium Madrasah and Al Arafah Islami Bank library are among others mention worthy.

The total deposits and investment of the bank were Tk.8643.3 million and Tk.7932.8 million respectively as on 31 December 2003.¹⁸ The Bank has, in the meantime, introduced the following schemes for mobilization of deposits and the schemes are popular day by day:

i) Mudaraba Terms Savings Deposits:

Deposits in monthly installment of Tk.200/-, Tk.300/-, Tk.500/-, Tk.1000/- Tk.1500/- & Tk.2000/- is obtained from the depositors under this scheme for a

¹⁸ *Annual Report-2003*, p. 44.

period of 5, 8, 10, and 12 years and the same is withdraw able with profit at the end of the period.

ii) Term Deposit for 5 years with Monthly Payment of Profits:

Under the above scheme, deposits of TK.1.0 Lac, 1.1 Lac, 1.2 Lac, 1.25 Lac and multiple thereof are accepted for a term of 5 (five) years and the Bank gives monthly profit on the amount. The monthly rate is adjustable at the close of the year.

iii) Monthly Hajj Deposit:

Hajj deposits at monthly installment from 1 (one) year to 20 (twenty) years are accepted under this scheme to enable the account holder to perform Hajj out of the accumulated savings with profit.

iv) One-time Hajj Deposit:

Under this scheme, fixed amount of Hajj deposits are accepted from the clients for a particular period and as per rules. Profit is accumulated thereon.

Under this scheme, the guardians may also open Hajj Account to enable their successors to perform Hajj. The Bank pays highest amount of profit in the above types of deposit.

v) Savings Investment Deposit:

Deposit under the scheme is accepted by monthly installment and after the expiry of the term; the Bank as per choice of the depositors gives double amount of such savings as investment in feasible sectors. Any body saves under the scheme can start business by utilizing the amount saved as well as availing Bank investment.

vi) Marriage Savings Deposits and Investment Scheme.

Fixed monthly installment for a particular period is to be deposited to defray the expenses of marriage and the bank allows double of saving or

Tk.30,000/- which is higher as investment to produce ornaments, furniture, fixture, etc., repayable in 24 monthly installments.

vii) Savings Bond Deposit.

Under this scheme the Bank has introduced Saving Bonds of Tk.10, 000/-, Tk.25, 000/- and TK.100, 000/- for 3, 5 and 8 years. After the completion of the period the deposited money may increase from 1.5 to double.

In order to keep pace with other competing Bank Al-Arafah Islami Bank introduces new attractive Shariah approved products from time to time and has continuous effort to popularize these schemes. A new product viz. Student Savings Scheme will be lunched in near future.¹⁹ The Bank provides investments to the clients under the following modes of investment:

i) Murabaha

Murabaha mode of finance means purchase of commodities as per request of the client permissible by Shariah and sale thereof with profit to the client. Purchase price and profit are disclosed to the client.

ii) Bai-Muajjal:

Bai-Muajjal means cost plus sale of the commodity on differed payment basis. The commodity is procured at the instruction of the client from a third party as per firm agreement between the client and the bank. The client pays the sales price (Bank's dues) within the stipulated period of time.

iii) Bai-Salam (Advance sale):

Under this mode the Bank buys the goods from the producer/ supplier in advance after entering into a firm contract. The goods are supplied to the Bank at a future specified date. In a contract of Bai- Salam quantity, quality, shape, size, price and time of delivery of the goods are clearly specified.

¹⁹ *Right Share Offer Documents* (Dhaka : Al Arafah Islami Bank Limited, 10 June 2003), p. 23.

iv) Ijara Bil-Bai (Hire Purchase Sirkatul Meelk)

Both the Bank and the client purchase machinery, equipment, vehicle etc. on equity participation and that durable item is handed over to the investment client on rental basis. The Bank enters an agreement with the investment client that (s)he shall pay the principal amount within a certain period of time by installments. Rent is to be paid on the principal outstanding till the ownership is transferred to the client on payment of the entire principal amount.

v) Mudaraba

The bank provides entire capital of the business venture against firm assurance of the businessman that (s)he will manage the business properly and efficiently. The businessman manages the business as Manager. The Bank shares profit with the client as per agreed proportion, while loss, if any, is borne by the bank alone. Bank can supervise such investment if and when desired/required but cannot participate in the management of the business.

vi) Musharaka

The Bank and the investment client jointly provide capital on the basis of Shirkatul Innan principle of the Islamic Shariah (partnership). Profit is shared as per agreed proportion and loss is shared on equity proportion. The Bank supervises the utilization of investment and takes part in decision making.

vii) Qard-e-Hasan

The Bank also allows Qard-e-Hasan in very special cases. Service charge equal to cost of fund is recovered on Qard amount.

viii) Special Investment

The Bank has, in the meantime, introduced the following schemes for the fixed wage earners, small traders and for the poor people:

- a) Desired Durable Investment Scheme (DDIS)
- b) Masjid Madrasah Based Investment Scheme (MMIS)

- c) Small Business Investment Scheme (SBIS)
- d) Special Pally Binyog Prakalpa (SPBP)
- e) Transport Investment Scheme (TIS)

The Board of Directors consists of 26 (twenty six) members who manage the Bank.²⁰ The board meets every month to review operations and give general instructions to the management. The Board of Al-Arafah Islami Bank Limited comprises four committees viz. Policy Committee, Executive Committee, Recruitment Committee, and Audit Committee. In addition to the above, the Bank has four Management Committees (viz. Fund Management Committee, Recovery and Follow up Committee, Credit Committee and Purchase Committee) headed by the Managing Director. The main activities of these committees are to utilize funds efficiently, recovery and follow up the investment, sanctioning and monitoring of investment and purchasing Bank's daily necessities. The Board approves all Executive Committee meetings and appraises the operational results'.²¹

The Shariah Council of the Bank consists of 7 (seven) members including 5 (five) Fukihs (eminent Shariah juries); who provide decisions in various banking issues as per Shariah. They give Shariah directives and also review operational procedures of the Bank from the point of Shariah.²² They ensure whether all banking operations are transacted in accordance with Islami Shariah i.e. Qur'an, Sunnah, Ijma and Iztihad. The Shariah Council advises everybody concerned to comply Shariah requirements and render all out effort to increase the standard of services rendered to the clients.²³

²⁰ *Annual Report-1999*, p. 6.

²¹ *Right Share Offer Documents* (Dhaka : Al Arafah Islami Bank Limited, 10 June 2003), p. 24.

²² *Right Share Offer Documents* (Dhaka : Al Arafah Islami Bank Limited, 10 June 2003), p. 8.

²³ *Annual Report-2003*, p. 23.

Muraqibs (members) of the Council visit all branches of the bank over the year to observe the Shariah compliance, give necessary instructions on the spot and submit report to the Council.

5.4.4 Social Investment Bank Limited

It is fourth interest free Shariah based commercial Bank in Bangladesh. It was incorporated on 05 July 1995 and started its banking operations on 22 November 1995 with an authorized capital of Tk.1, 000 million divided into 1 million ordinary shares of Tk.1,000 each. The initial paid up capital was Tk.118.4 million fully owned by its 38 sponsors including 3 Arab nationals. The paid up capital was enhanced several times and stood at Tk.260 million on 31 December 2000.²⁴

Targeting poverty, this Bank is committed to implement the principle of participatory economy with human face approach to credit and banking on interest free basis. The Bank strives to empower the family, as family is the foundation of a society. The Bank extends all types of commercial banking services and it conducts business on the Islamic Principles of Mudaraba, Musharaka, Bai-Muajjal and the Hire Purchase transactions. The broad spectrum operational aspects of the Bank have been set out to encompass three sectors banking model into one: (1) Formal, (2) Non-Formal, and (3) Voluntary Third Sector, with a comprehensive program for total socio-economic development for all.

In the Formal Sector the Bank offers banking services through deposit and investment accounts, and other banking business. In the Non-formal Sector the Bank involves in opening and introducing various savings and investment schemes for the poor. The Voluntary Third Sector promotes development and management of Waqf and Mosque properties, management of inheritance properties, and joint venture projects relating to religious affairs and charitable activities. The list of sponsors of Social Investment Bank is furnished below:

²⁴ Source, internet: www.banglapedia.org.copyright by Asiatic Society of Bangladesh.

Sponsors of the Bank:

1. Prof. Dr. M.A. Mannan Founder Chairman
2. H.E. Dr. Hamid-al-Gabid, Secretary General, Organization of Islamic Conference, Jeddah
3. H.E. Dr. Abdullah Omar Nasseef, Deputy Speaker of Consultative Council, Saudi Arabia
4. H.E. Ahmed M. Salah Jamjoom, Former Commerce Minister, Kingdom of Saudi Arabia
5. Islamic Solidarity Fund and its Waqf, Organization of Islamic Conference
6. International Islamic Relief Organization (IIRO), Saudi Arabia
7. Islamic Charitable Society (Lajnad Al-Birr Al-Islami), Jeddah, Saudi Arabia
8. Shabir A. R. Battacherjee
9. Major (Retd) Dr. Md. Rezaul Haque
10. Mohammed Ibrahim Miyan
11. Dr. Md. Jahangir Hussain
12. Mohammed Abdul Malek.Mr. M. Abdul Hakim.
13. Bangladesh Social Peace Foundation
14. Dr. J. H. Gazi
15. M. Nurul Amin
16. Mohammad Shah Alam
17. Alhaj Sultan Mahmood Chowdhury
18. Alhaj M. Nesaruddin
19. Abudl Awal Patwary
20. Anisul Huq.
21. Nagris Mannan
22. Fatama Begum

23. Zohara Alam
24. Shamsun Nahar Begum.
25. Al-Haj A. K. M. Saiquatul Islam, Representing Islam Import and Export Associate Limited
26. Al-Haj Nasiruddin
27. Kamal Uddin Ahmed
28. Ahmed Akbar Sobhan
29. Hasina Akther
30. Al-Haj Sk. Mohammad Rabban Ali
31. Md. Aynul Haque
32. Mohammad Azam
33. Md. Aminuddin
34. Dr. (Mrs.) Reshmi Mannan Siddique
35. Dr. Ghalib Mannan
36. Sadat Sobhan
37. Al-Haj S. N. Haque

The management of the Bank is vested on 28-member Board of Directors headed by a Chairman. There is a 5-member Shariah Council of the Bank to ensure compliance of Islamic rules in its activities. The Bank has also 13 (thirteen) honorary foreign members in the International Advisory Council to advise the Bank on international business affairs especially with Islamic countries.²⁵

5.4.5 Shahjalal Bank Limited

Shahjalal Bank Limited was established in 2001 after the name of a Muslim saint Hajrat Shahjalal (R) who dedicated his life for the cause of peace in this world and hereafter and served the humanity. Shahjalal Bank Limited is an interest-free Bank with modern outlook. In an effort to do banking without

²⁵ *Annual Report-1999*, pp. 4-5.

interest Shahjalal Bank Limited avoids interest in all its transactions and provides all available modern banking services to its clients and wants to contribute in both moral and material development of human being. No sustainable material well-being is possible without spiritual development of human being. Thus the Bank stands not only for material well-being but also for ethical development of its customers.

i) Objectives of Shahjalal Bank Limited:

The main objective of Shahjalal Bank is to serve the people for attainment of their economic goal and success in life here and hereafter. The specific objectives of the Bank include:

- To establish interest-free and welfare oriented banking system
- To help in poverty alleviation and employment generation
- To contribute in sustainable economic development

ii) Deposits Schemes of Shahjalal Bank Limited

Shahjalal Bank accepts deposit on the basis of Muda'raba in the following types of accounts and pays profit except Al-Wadiah Current Account. The relationship between the depositors and the Bank is not like debtor-creditor. The depositors are partners in business with Shahjalal Bank. The Bank maintains the following types of accounts:

- Mudaraba Short Notice Deposit Account
- Mudaraba Savings Account
- Mudaraba Term Deposit Account
- Other Scheme Deposit Accounts

On an average 70% of the profit earned by the bank is distributed proportionately among depositors annually.²⁶ iii) Various Special Savings Schemes:

²⁶ Source Internet: Shahjalal Bank-Home page, www.shahjalalbank.com.bd.

In addition to the above deposit schemes the Bank has introduced so far the following special savings schemes:

- Millionaire Scheme

The Millionaire Scheme has been introduced for the formation of social capital through savings. This scheme encourages people to save. Under this scheme depositing Tk.1,65,000 with monthly installment of only Tk.550, one can get on maturity a sum of Tk.1,000,000.

- Monthly Income Scheme

In this scheme service holders can keep their retirement benefits with the bank and earn a fixed income every month to meet their day-to-day family expenses. Under this scheme depositing a sum of TK.50,000 (fifty thousand) only, one can get Tk.500 per month.

- Hajj Deposit Scheme

There are many religious minded people who cannot perform Hajj due to indecision. Under this scheme they will be able to perform Hajj on investment of TK.3 Lac with the Bank for a certain period.

- Monthly Deposit Scheme

Under this scheme the depositors deposit a particular amount of money every month for a certain period and can cash profit with the deposited amount at the end of the period. This scheme helps fixed income people to save for their future. This scheme requires a depositor to deposit installment of TK.500 monthly for ten years and earn a total sum of Tk.118,000 at the end of the period.

- Double Profit Muda'raba Savings Scheme:

Social Investment Bank has introduced Double Profit Mudaraba Savings Scheme to provide an opportunity for safe deposits and profits. The invested money will be doubled within six years. Through this scheme the Bank has been playing a leading role in mobilizing internal savings of the country.

- Expatriates Service Scheme:

A remarkable portion of Bangladeshi people is working in other countries of the world. They are sending a huge amount of foreign currency every month to the country. The purpose of the project is to provide them opportunity to invest in this fund for assisting up projects/industries, residential schools/colleges, technical institutes, construction of flats and providing help to non-resident Bangladeshi engineers/ medical professionals.

v) Modes of Investments of Shahjalal Bank Limited:

To offer interest-free banking Shahjalal Bank Limited has adopted the following investment schemes:

- Musharaka (equity participation on the basis of sharing profit and loss).
- Mudaraba (Sharing of profit and loss in business where one of the partners involves business and the other partner provides capital)
- Murabaha (buying and selling goods with profit).
- Bai-Muajjal (credit sale with profit)
- Ijara (leasing for rent)
- Hire Purchase or Shirkatul Meelk
- Bi-Salam (Advance purchasing of agricultural products before production)
- Istisana (Advance purchase of industrial products)

In addition to the above the Bank has introduced the following investment schemes:

- Household Durable Scheme:

This scheme allows the middle-income segment of the society to buy various household goods, car etc.

- Investment Scheme for Women:

Women constitute near about half of our total population. But they are not coming forward to undertake business due to our traditional social system and lack of capital. This scheme has been introduced with the aim to encourage women to start business with bank investment and become self-reliant.

- Small Investment Scheme:

The Bank provides financial assistance to those reputed and established shop owners who are not able to expand their business due to shortage of capital.

- Self Employment Scheme:

There is sharp increase in educated unemployed people in Bangladesh due to high population growth. The Bank has introduced Self Employment Scheme to help those unemployed educated people to undertake income-generating activities and make them self-reliant.

vi) Management of the Bank:

The management of the Bank is entrusted with 21-member Board of Directors. There are 8 sponsors Directors in the 21-member Board. One Chairman and two Vice Chairmen are elected from amongst the members. There is an Executive Committee consisting of one Chairman, one Vice Chairman, and six other members. There is an Audit Committee comprising of one chairman and two members.

5.4.6 Prime Bank Limited

Prime Bank Limited started its operation with the slogan 'Bank with Difference' in 1995. Opening of Islamic Banking Branches within the framework of interest base conventional banking is one of its achievements. Prime Bank Limited started its Islamic Banking operation by opening its first Islamic Banking Branch at 19, Dilkuhsa Commercial Area Dhaka on 18 December 1995. The Bank opened its second Islamic Banking Branch at Amberkhana, Sylhet on 17 December 1997. Prime Bank established a Shariah Board to advise and provide

guidance to conduct all businesses of Islamic Branches as per the principles of Islamic Shariah. The Shariah Council consists of nine members including one Chairman and one Vice Chairman. They have vast knowledge in Islamic Shariah relating to banking operations.

i) Features of Islamic Branches of Prime Bank Limited:

The distinguishing features of Islamic Banking are:

- To conduct all activities of Islamic Branches as per Islamic Shariah
- To conduct all transactions free of interest
- To establish banker-customer relationship on the basis of partnership rather than debtor-creditor relationship
- To invest on the basis of Islamic principles
- To develop the living standard of the poor and disadvantaged segment of the society
- To conduct welfare related activities for the people

ii) Deposit Accounts

Deposit Accounts of Islamic Branches of Prime Bank Limited is divided into two categories:

a) Al-Wadiah Current A/C

Islamic Banking Branches maintains Al-Wadiah Current A/C as per Islamic Shariah. In this form of deposit the Bank is committed to pay the deposit amount to the depositor on demand. On the contrary the Bank takes permission from the depositor to the effect that the Bank will invest the money as deposited by the client. The client can withdraw the money when he needs. The Bank does not pay profit on Al-Wadiah Current deposits.

b) Mudaraba A/C

Islamic Branches of Prime Bank conducts Mudaraba Deposit A/C as per Islamic Shariah:

- Mudaraba Savings Deposit Account
- Mudaraba Term Deposit Account
- Mudaraba Short Term deposit Account
- Mudaraba Education Savings Scheme
- Mudaraba Monthly Contributory Scheme
- Mudaraba Monthly Benefit Savings Scheme

In these accounts Prime Bank is treated as 'Mudarib', while the client is treated as 'Shahib Al-Maal'. Bank invests the deposit money on behalf of the depositors and distributes 75% of profit earned out of investment at the end of the year.²⁷

iii) Islamic Modes of Investment in Prime Bank Limited

Besides interest based conventional investment banking, the bank has undertaken the following modes of investment according to Islamic Shariah. These may be classified as under:²⁸

Buying-Selling System.

a) Bai-e-Murabaha b) Bai-e-Muajjal c) Bai-e-Salam (advance sale)

2) Partnership Business:

a) Muda'raba b) Musharaka

3) Ijara Bil-Bai (Hire Purchase Shairkatul Meelk)

4) Quard –e-Hasan.

The Bank has a plan to open more Islamic branches all over the country to fulfill the demand of the people of the country.

²⁷ Source: Internet, Prime Bank- Home Page; www.prime-bank.com.

²⁸ Source: Internet, Prime Bank- Home Page; www.prime-bank.com.

5.4.7 Islamic Finance and Investment Limited

Islamic Finance & Investment Limited (IFIL) is a Shariah based financial institution. It was incorporated on 27 February 2001. The formal inauguration was held on 03 March 2001. But actually Islamic Finance & Investment Limited started its business on 19 April 2001. The sponsors contributed 70% of its capital. The Head Office of Islamic Finance & Investment Limited is situated at 66, Dilkusha Commercial Area, Dhaka.

i) Objectives of Islamic Finance and Investment Limited:

IFIL has the following objectives:

a) Introducing Islamic Financing System:

Although Islamic Banking system is very popular in the Banking arena of Bangladesh, non-banking financial institution is yet to adopt financing system based on Islamic Shariah. Islamic Finance & Investment Limited is fully committed to establish Shariah based financing system in Bangladesh.

b) Introducing Welfare Oriented Financing System:

Islamic Finance & Investment Limited is very eager to introduce welfare oriented financing system through its business activities.

c) Simplification of Financing System:

Islamic Finance & Investment Limited wants to simplify the financing system for giving easy and quick service to the clients.

d) Creating Entrepreneurs for the Development of Business:

Islamic Finance & Investment Limited strives to extend all out cooperation to create new entrepreneurs for the overall development of the country.

e) Playing Role in Socio-economic Development:

Islamic Finance & Investment Limited has been playing an important role in the socio-economic development of the country.

ii) Programs of Islamic Financing and Investment Limited:

Islamic Financing and Investment Limited operates all its activities according to Islamic Shariah. The Major programs of Islamic Finance & Investment Limited are as under:

a) Deposits Schemes:

1) Term Deposits:

Islamic Finance & Investment Limited receives term deposits under Muda'raba system for the term of 12, 24, or 36 months or so on. On maturity the depositor gets the deposit along with earned profit. The depositor can get monthly profit from his deposit if he wants. In this case he needs to invest at least TK.1 (one) Lac for a minimum period of three years. Provisional profit is given to the depositors with condition to adjust the same on completion of final accounts in due course. The depositors can withdraw the money before the period is expired. In case of emergency the Bank may extend Quard-e-Hasan facilities to the clients against those deposits.

2) Deposits under Various Schemes:

Islamic Finance & Investment Limited also receives deposits under various schemes. Presently Islamic Finance & Investment Limited has the following two schemes:

- Home Owning Scheme:

Under this scheme a person can be owner of a home if (s)he deposits a minimum amount of TK.1000 on monthly basis for a minimum period of 2 years and a maximum period of 10 years. Higher amount may be deposited on quarterly basis. Depositors under this scheme will get investment facilities equivalent to their deposits. As for example, if some one deposits Tk.10 Lac during the period, (s)he may avail an investment facility of Tk.10 Lac enabling him/her to have Tk.20 Lac at a time with provision to refund IFIL's portion within a maximum period of 10 years with rent/profit.

- Higher Education and Marriage Scheme:

Under this scheme one can deposit a minimum amount of TK.25000 on lump sum basis to open an account on behalf of his / her child aged between 1-5 years. The child will get more or less Tk.1000 as his/her educational cost on monthly basis when (S)he will get admission in Degree/Honors class. After or before completion of his/her education, taking more or less TK.1 (one) Lac for her/his marriage or other purpose the beneficiary may close the account.

c) Investment Schemes:

Islamic Finance & Investment Limited has the following modes of Islamic financing for its clients:

- Bai-Murabaha

Under this scheme Islamic Finance & Investment Limited sells certain specific goods (permissible under Islamic Shariah and the Law of the Land) to the buyer at a cost plus agreed profit payable in cash or on any fixed future date in lump sum or by installment. The profit may be fixed in lump sum or in percentage of the cost price of the goods.

- Bai-Muajjal

Under this agreement IFIL sell goods to the client purchased by IFIL as per order or specification of the client. The client will make payment at a certain fixed future date in lump sum or within a fixed period by fixed installments.

- Hire Purchase under Shirkatul Meelk

Under this mode of investment Islamic Finance & Investment Limited may supply machinery/equipment/goods to the client on rental basis. The ownership will remain with Islamic Finance & Investment Limited but the client will be authorized to possess the equipment or machinery for certain period. The client after completion of the installments will be the owner of the machinery/equipment/goods.

- Mudaraba

Under this scheme Islamic Finance & Investment Limited provides money while the client provides the expertise and management to run the business. Here Islamic Finance & Investment Limited is called the "Sahib-Al-Maal" and the client is called as the "Mudarib". Any profits accrued are shared between Islamic Finance & Investment Limited and the client on a pre-agreed basis. But capital loss is exclusively borne by Islamic Finance & Investment Limited.

- Musharaka

Musharaka or Sirka is a mode of investment in Islamic Banking. It is a partnership business wherein two or more persons or firms invest capital for business, conduct business and share in profit and loss of the business. In this system Islamic Finance & Investment Limited and the client invest fund as per requirement of the project. There is no hard and fast rule in providing the share of fund. It may be 50:50 between the bank and the client or 75:25, or any percent. The ratio of capital is decided as per discussion between IFIL and the client.

- Bai-Salam

Under this mode Islamic Finance & Investment Limited executes purchase contract with the client and make payment against purchase of product, which is under process of production. Bai-Salam contract is executed before making any investment showing price, quality, quantity, time, place and mode of delivery. The profit is to be negotiated.

- Lease/Ijara

It is a contract under which Islamic Finance & Investment Limited rent out an asset to the client called lessee for a certain periodical rent.

In fact Islamic Finance & Investment Limited has no specific investment area. Any investment proposal, which is permissible by Islamic Shariah and

consistent with the investment policies of Islamic Finance & Investment Limited, is normally allowed. At present Islamic Finance & Investment Limited is providing investment facilities under Bai-Muajjal, Hire Purchase Shirkatul Meelk(HPSM) and Leasing of Industry, Business, Agriculture, Transport, Real Estate, Household Durables, etc. The procedures of taking investment facilities are very easy and simple. One can get immediate decision about their investment proposals.

5.4.8 Shamil Bank of Bahrain EC, Dhaka

Shamil Bank of Bahrain EC started business in Bangladesh as a branch of Faysal Islamic Bank of Bahrain EC (Islamic Bankers) on 06 March 1997, after obtaining necessary permission from Bangladesh Bank. The parent Bank is a member of the Dar Al-Islami Group, Geneva, Switzerland. In June 2000, Faysal Islamic Bank of Bahrain EC and Islamic Investment Company of the Gulf (Bahrain) EC merged together into a new Bank Shamil Bank of Bahrain EC (Islamic Bankers). The principal activities of its Bangladesh branch are to provide all kinds of commercial banking services to the customers on the basis of Islamic banking principles. On 31 December 2000, the assets of the Bank were valued at TK. 1,282.2 million. The total deposits were Tk964.53 million comprising Muda'raba Term Deposits, Savings Deposits, Bearer Certificate of Deposits, and Current, contingency and other accounts.²⁹

The Bank has Religious Supervisory Board (RSB). The Bank's operations are checked by this RSB to ensure Shariah compliance. The same board is also monitoring the activities of Bangladeshi Branch.

5.4.9 Other Foreign Islamic Banks Operating in Bangladesh:

Besides Shamil Bank of Bahrain EC, there are three more branches of three Pakistani Banks have been working in Bangladesh such as Habib Bank

²⁹ Source, internet:www.banglapedia.org., copyright by Asiatic Society of Bangladesh.

Limited, National Bank of Pakistan, and Muslim Commercial Bank Limited. In Pakistan all these banks are operating in accordance with Islamic Shariah. But unfortunately in Bangladesh these banks are operating as conventional interest based banks. Only the activities of Shamil Bank of Bahrain EC are considered appropriate from Islamic Shariah point of view.

5.4.10 Islamic Banking in Conventional Banks

As mentioned earlier that in Bangladesh some other conventional Banks have taken the initiative of introducing limited Islamic banking within their present conventional set up. Some Banks have opened Islamic Bank Counter(s) with conventional Banking. The businesses of these counters are on the basis of Islamic Shariah.

Chapter 6

**Welfare Programs of
Islamic Banks in
Bangladesh**

Chapter 6

Welfare Programs of Islamic Banks in Bangladesh

6.1 Social Welfare from Islamic Perspective

Welfare related activities are essential and an integral part of Islamic way of life. Islam views work as the primary means of earning leading to consumption, savings, investment, and social welfare. A well known example can be cited here. A beggar approached the Holy Prophet (SM) for alms. The Prophet(SM) asked the beggar to bring what he had in his house. Accordingly, the man brought a blanket, which he had in his house. The Prophet(SM) sold the blanket and with the money he purchased an axe and gave it to the man (Beggar). The Prophet (SM) told him to cut wood from the jungle and sell at the market for income. Thus, instead of begging, he could be self-reliant, which was a more dignified life than begging. Therefore, employment and self-employment and consequently income become the primary source for buying necessities such as food, clothing, shelter, household goods, transportation, fuel, medicines etc. But if income is not sufficient to purchase necessities of life, then welfare becomes essential in a society to maintain the minimum standard of life of the society people. In fact, in every society, there are many people who lack necessary income due to unemployment and under-employment and consequently maintain poor lifestyle and cannot fulfil the minimum necessities of life. Their condition cannot be improved if welfare services remain absent and concentration of wealth remains in a few hands of the society. The Holy Qur'an states 'wealth should not circulate only among the rich' (59:7).

The Qur'an also encourages people to contribute generously to social welfare activities and helping the needy in the society. 'They will ask you as to what they should spend on others. Say [O Muhammad (SM)]: whatever of your wealth you spent shall be for your parents, and for the near of kin, and the orphans and the needy and the wayfarer; and whatever good you do, verily,

Allah has full knowledge thereof' (2:215). Thus Islam calls for meeting the basic needs of the poor segment of the society through welfare services like Care for others and Zakah.

The Islamic banks as a part of the financial system, should conduct their activities with the objective to implement the social and economic principles of Islam. The objective of Islamic banks is not to earn profit but to do good for the society and bring welfare to the society people.

There are different forms in which social commitment of Islamic banks is manifested. For example, many Islamic banks have introduced a practice of providing interest-free loans to their clients in case of terrible and unexpected situations.

Many Islamic banks establish social funds specially designed to help the poor and needy for alleviating their economic hardship. This fund is usually financed through collection of Zakah annually.

Islamic banks in Bangladesh usually work within a traditional environment and have working relationships with traditional banks. As such they often accumulate interest balance in their accounts with traditional banks. But according to Islamic Shariah earned interest cannot be treated as profit or income and the same is to be disposed of to the poor in a way that does not directly benefit the bank. Thus Islamic banks in Bangladesh that happen to earn interest spend them on social welfare activities. Moreover, many Islamic banks contribute a lot of amount to human resources, research and community development activities.

The present chapter deals with both pure welfare and non-investment services offered by Islamic banks in Bangladesh to their clients as well as general public. This also includes welfare activities of Islamic banks for the rural poor through extending financial support to them.

A description of various welfare activities of different Islamic Banks working in Bangladesh is presented below:

6.2 Social Welfare Programmes of Islami Bank Bangladesh Limited (IBBL)

One of distinguishing features of IBBL is that all its activities are directed towards the welfare of the society. Since its inception, the bank has dedicated itself for the economic emancipation of the helpless and the poor segment of the society. To achieve this goal the Board of Directors of IBBL created a welfare fund named "Sadaqah Tahbil" on 4 July 1983. On 20 March, 1991 the Sadaqua Tahbil was reorganized and enlarged under the name of "Islami Bank Foundation" with a fund of Tk.38.0 million in order to conduct social welfare activities on a wider scale. 'This foundation was established for providing financial assistance to the poor and needy people of the society through income generating, healthcare, relief and rehabilitation, education, humanitarian activities, dawah and special programs'.¹ It was registered with Registrar of Joint Stock Companies of the Government of the People's Republic of Bangladesh under no. S-1214 (25) 1988 dated 25 June 1988. It was also registered with NGO Affairs Bureau under no. 668, dated 24 November 1992'.² The Foundation is a sister organization of IBBL having separate accounts and administration. The Foundation has been working with unique and special programs for the welfare of distressed humanity and to make the poor, downtrodden, landless and asset-less people self-reliant.

In addition to the social welfare activities of Islami Bank Foundation the Islami Bank Bangladesh Limited itself is implementing some socio-economic development programs such as Rural Development Schemes, Quard-e-Hasen etc.

i) Aims and Objectives of Islamic Bank Foundation

The aims and objectives of Islami Bank Foundation are to serve the distressed humanity, promote people oriented mass education, extend health and Medicare facilities to the poverty-striking people of the country, create facilities for productive self-employment and develop human resources for improving economic condition and quality of life, assist healthy growth of culture, art,

¹ *Annual Report 1996*, p. 24.

² *Welfare Programmes*, (Dhaka: Islami Bank Foundation, October 1999), p. 6.

literature, science and technology, sports, research and propagation of Islamic teachings.³ The Foundation has already taken a number of programs covering the whole of Bangladesh. Those programs are discussed below:

ii) General Programs:

a) Income Generating Programs:

Access to necessary finance and other related inputs might help many unemployed poor to become self-employed. In absence of any such opportunity the unemployed youths of our society may engage themselves in different anti social activities. Considering the severity of the problem Islami Bank Foundation has, therefore, taken up self-employment projects for the unemployed people:

- Rickshaw/ Van
- Fishery
- Poultry keeping
- Milch Cow, Goat Rearing, Beef Fattening
- Small Trade
- Sewing
- Rural Health Service

b) Educational Programs

Education is the backbone of a nation. Developed nations are developed because they are developed in education. Building awareness, developing skill through training, access to information and technology- all depend on education. But, unfortunately, our literacy rate is very low and gender discrimination exists there. Most of the children are deprived of basic education due to poverty, lack of sufficient low cost educational institutions, non-availability of textbooks and equipment.

Islamic Bank Foundation has, therefore, taken up the following programs to improve the literacy rate and the overall educational scenario of the country:

³ Ibid.

- Support to model Forquania Maktab.
- Financial support to educational institutions.
- Scholarship/ lump-sum grant for poor and meritorious students.

1. Health and Medicare Programs:

Health and Medicare facilities are basic and fundamental rights of each and every human being of a country. Being a poor country Bangladesh cannot provide the health and Medicare facilities to its entire population. To overcome this problem the Islamic Bank Foundation has so far taken the following programs:

- i) Establish Child and Maternity Centres, and Hospitals
- ii) Support Charitable Dispensaries
- iii) Provide lump-sum grants for medical treatment
- iv) Install Tube Wells for the supply of pure drinking water
- v) Set up Sanitary Latrine

Such assistance is also extended to the members of Rural Development Scheme (RDS) of Islami Bank Bangladesh Limited.

2. Humanitarian Assistance Programs

Humanitarian assistance is being provided to the poor, disabled persons, families affected by river erosion and for marriage of poor girls. Besides, the program extends assistance to orphanages, assist indebted people, help distressed wayfarers.

a) Emergency Relief and Rehabilitation Programs

The Foundation provides emergency relief among the people affected by natural calamities like flood, tornado, tidal surge etc. The Foundation donates to the relief fund of the Government. The Foundation has also taken up schemes for permanent rehabilitation of the flood, tidal bore, and river erosion affected people by constructing houses and making provision for self-employment. The

Foundation also extends hands of assistance to the Muslim brethren elsewhere in the world. It is worthy to be mentioned that the Foundation extended relief for war affected people of Bosnia-Herzegovina, Victim of earthquake in Iran in 1997 and in 2003, and relief for distressed Muslims of Kosovo, who were brutally tortured by the Serb and the Government of Yugoslavia in 1999.

b) Dawah Programs

One of the main objectives of Islamic Bank Foundation is to propagate and disseminate the true knowledge and teachings of Islam. The Foundation has, therefore, taken up various programs to enlighten the people and make them aware about the teachings, norms and values of Islam as a religion. The Foundation publishes research journals, magazines, and other Islamic literatures, booklets etc. and distributes the same among the researchers, academicians, judges, lawyers, high officials, and elites of the society, and also among important libraries and institutions of the country. The Foundation has also been working among the prisoners for their moral reforms.

v) Special Programs of Islamic Bank Foundation:

a) Islami Bank Hospital:

The Foundation has so far established four modern hospitals named Islami Bank Hospital at four Divisional Headquarters- Dhaka, Rajshahi, Khulna and Barisal. The objective is to provide low-cost curative services to the less affluent segment of the society.

General practitioners and specialists in different fields like Medicine, Surgery, Gynecology, Pediatric, ENT, Eye, Skin, Urology, Neurosurgery, Orthopedic, etc. are providing services in these hospitals. These Hospitals are equipped with standard diagnostic, medical and surgical equipment. The Foundation has a plan to establish Modern Hospital at each Divisional Headquarter of the country.

b) Islami Bank Community Hospitals

The Foundation has planned to assist local initiatives in setting up Hospitals at district levels. The objects of these Hospitals are to create an integrated and comprehensive healthcare and Medicare systems at low and affordable cost for the poor and moderate-income segments of the society. These Hospitals are providing qualitative, reliable and readily available healthcare and medical treatment to the common people. Through this project the Foundation has been trying to create self-employment opportunities for the young and educated doctors and encourage them to engage themselves in the district, thana and rural areas. Under this project several Hospitals have been set up in different areas of the country. Several others are in the pipeline.

c) Islami Bank Technical Institutes

The Foundation has also established four Vocational Training Institutes named Islami Bank Technical Institute: two at Dhaka, one at Bogra and the other at Sylhet for imparting vocational training to the unemployed youths so that they can get jobs at home and abroad. All these Institutes are providing training facilities in Basic Computer Literacy, Secretarial Science, Vehicle Driving, Electrical Works, Maintenance and Repairing of Refrigerators and Air Cooler, Radio, Television, and also Tailoring and Garments etc. The objective is to turn a large number of unemployed people of the country into human assets through taking up all the above-mentioned Human Resource Development Programs. The Foundation has also taken initiative to establish a Global Standard State of the Art Information Technology Institute.

d) Islami Bank Model School and College

Dhaka is the capital of Bangladesh. A large number of English Medium Schools have been established in this city, which follow course curriculum not conforming to Islamic ideology, norms and values and also to the country's need. As an attempt to combine modern education with Islamic values for total development of a child, the Foundation has established an English Medium School and College at Dhaka in 1998. The Foundation is also planning to

establish a Bangla Medium School affordable by lower and middle class people of the society.

e) Monorama (Sales Centre for products of Distressed Women)

The Foundation has established a sales centre at Dhaka named Monorama, which is playing a significant role for economic upliftment of poor and distressed women through providing sales opportunities of their products. The project is located at 23, Paribag, Sonargaon Road, Hatirpul, Dhaka. Through this sales centre homemade garments, handicrafts and other items produced by the distressed women under Self Reliant Scheme of the Foundation are sold. The main objective of the project is to create conducive and healthy atmosphere in which women can contribute to the family income keeping themselves within the boundaries of Shariah. The other objective of this project is to develop designs of women-wear, which will conform to the principles of decency and fashion as laid down by Islam and at the same time comparable with the modern-day-fashions.

f) Islami Bank Physiotherapy and Disabled Rehabilitation Centre:

There are a large number of disabled unfortunate persons in Bangladesh who have no other means of income except begging. They are a burden to the society. The Foundation has been working through this centre for their rehabilitation. The Foundation has established a centre named 'Islami Bank Physiotherapy and Disabled Rehabilitation Centre'. This centre provides temporary food and shelter for the disabled and also arranges health checkup, physiotherapy and occupational therapy and look for a job placement through internship in various factories and trading houses.

g) Service Centre

To save the people of the coastal and river belt from natural disaster and land erosion a special project has been taken up by the Foundation named 'Service Centre' (Disaster Shelter and Integrated Social Development Project).

Under this Project pucca structures are constructed in the coastal areas, river belts and offshore islands for providing safe shelters for the people of these localities during natural calamities. These buildings are also used for integrated social development of the people. Three such Service Centres have already been established at 'Abdullah Mair Hat' of Noakhali; 'Horirampur' of Manikganj; and other at Feni.

h) Bangladesh Sangskritic Kendra (Cultural Centre)

Culture is an important and leading factor for the identity of a nation. Now- a- days, no country can conquer other country through applying force. But a country can conquer other countries through cultural infiltration and imposing ideas, beliefs, and also by influencing the thinking process. The affluent segment of the society and the new generation of Bangladesh are presently motivated by Western and Indian culture which is very much harmful for the nation. The Foundation has, therefore, established 'Bangladesh Sangskritic Kendra' (Cultural Centre) at Dhaka for upholding and promoting national culture and heritage of the country and to resist the cultural aggression from the west and across the boarder.

i) Centre for Development Dialogue

Now-a-days Non Government Organizations (NGOs) of the developing world are playing increasing role in experimenting Development Models alongside the government efforts at the national level. Unfortunately most of the NGOs are implementing development techniques, which are against the social norms and beliefs of the people. Most of the renowned NGOs have their own training centre(s) where they train their own people and also rent out the facilities for others. Islami Bank Foundation has decided to establish a training centre of its own named "Centre for Development Dialogue" which will create opportunity for imparting training facilities for its own staff members as well as the staff members of other development organizations.

vi) Other Projects

Besides the above-mentioned programs, Islami Bank Foundation runs projects like:

1. Legal Aid Project for the welfare and legal support to the victims and their family members, holding of seminars and symposia on the rights of the vulnerable (women, children, disabled, etc.) and human rights, opinion mobilization against various forms of social ills etc.
2. Talimul Qur'an project for propagating the teachings of the Holy Qur'an. The foundation has also drawn up a plan to look after the Education, Health, and Medicare requirements of the people of the area where the Bank has launched Rural Development Scheme.

'Development is a continuous process. Development of few without the development of vast majority is not meaningful. With limited resources Islami Bank Foundation has been trying to diversify its activities and spread all over the country. The Foundation is looking forward for assistance and cooperation from philanthropic persons and institutions at home and abroad to materialize its objectives and to continue the above mentioned multiple social welfare activities for the helpless and poor segment of the population.

The Foundation spent Tk.216.02 million during the year 2000 for Income Generating Projects, Education, health & Medicare, Humanitarian, Relief & Rehabilitation, and Dawah activities, and also for Local Committee and Special Projects etc.

a) Rural Development Scheme of Islami Bank Bangladesh Limited (RDS):

Bangladesh with its 60% percent people living below poverty line and 30% living in absolute poverty is suffering from acute rural-urban economic disparity coupled with illiteracy. The country's economy is basically an agrarian one with vast majority living in rural areas. The agriculture is unable to provide any further scope of employment resulting in influx of rural population towards

urban areas. Unemployment and under employment is a regular phenomena in rural economy. This result in uneven distribution of income which causes serious set back in balanced geographical growth as well as growth of GDP.⁴

Islami Bank Limited has designed an investment policy to take care of the requirement of all the economic groups of the country by ensuring reduction of rural-urban disparity in investment and income. With this end in view the Bank has introduced Rural Development Scheme. The main objective of this program is to meet the investment needs of agriculture and rural sector in order to create employment opportunities of the rural mass and raising income and living standard of the rural people.

- Objectives

The distinguishing features of the scheme are:

1. To diversify investment opportunities for farming (agriculture) and off-farming activities in the rural areas.
2. To provide capital to the rural unemployed youths and the rural poor in order to create self-employment through income generating activities.
3. To eliminate rural poverty through integrated rural development approach.
4. To meet the needs of pure drinking water, sanitation and housing of the rural poor and the disadvantaged segment of the society.
5. To provide education, health service and Medicare facilities to the down –trodden people.

- Target Area

Initially the program has been started as a pilot scheme in rural areas of certain districts under the direct supervision and control of the nearby Branches of Islami Bank Bangladesh Limited. The bank has a plan to extent this program gradually in the districts through its branch network all over the country.

⁴ *Rural Development Schemes* (Public Relations Department, Islami Bank Bangladesh Limited), p. 5.

- Target Group
 - i) Farmers having maximum 50 decimal of land permanently residing in the selected village.
 - ii) Sharecroppers, having no cultivable land, with consent from the landowners.
 - iii) Persons engaged in off farming activities having no land or land up to maximum of 50 decimal.
 - iv) Destitute women and downtrodden people can avail investment facilities for poultry, hatchery, beef fattening, goat rearing, milch cows, re-excavation of ponds and fish cultivation and other suitable off-farm activities to raise their income and consumption level.
- Group Formation and Other Rules thereof

The main feature of the program is 'Group Approach'. Allah loves those 'who conduct their activities by mutual consultation' (42:38). In this scheme all decisions are taken on mutual consultation of the group members. The guidelines for group formation and group decision-making are as follows:

1. A Group is formed consisting of 5 (Five) members of same profession or occupation.
2. Each group selects its Group Leader and Deputy Leader from among the members of the group to coordinate the group activities. The field officer meets the Group after formation of the same and gives recognition to the Group through issuance of a Pass Book.
3. Group Leader needs to ascertain the following:
 - Members' liability from other banks, NGOs and other sources.
 - The size of land holdings of each and every member of the Group and whether he cultivates land as owner or sharecropper.

- Identify the member(s) engaged in off farm activities and ensure their participation in Group activities.
- Help the Field Supervisor in selecting genuine client members. The Group Leader should have full command and control over the Group members.
- The Group Leader ensures regular attendance of all the Group members in the weekly meetings and deposit of the personal savings. The weekly compulsory savings is minimum Tk.5 per member. This saving may, however, be withdrawn by the member if he does not have any other liability with the Branch in any way.
- The member(s) who is illiterate and cannot sign, (s)he must learn to put signature. The Group Leader helps in selecting eligible members, who will get investment facilities. Application forms are supplied to the eligible members of the Group. The Bank officials help in filling up the forms. Two members of the group are allowed to get investment facilities after three months from the date of formation of the Group. The remaining members will be eligible to get investment facilities after regular payment of installments for at least one month by the two members who availed investment facilities earlier. The Group Leader also ensures the recovery of the installments from client members of the group.
- In case any member of a Group fails to comply with the principles of the Group activities, the other members of the Group are bound to compel him/her to observe Group discipline and in case of default other members are responsible for recovery of the defaulted money. Consequently, the defaulter member will be expelled from the Group for breach of Group discipline. The expelled member will not get any investment facility and other benefits from the Bank in future. If any

member of a Group becomes a defaulter other members will be liable to pay his default money. Each member of the Group gives guarantee for the other members of the Group. If one is become defaulter other members will be liable to pay his default amount.

- Minimum 2 and maximum 6 groups of the same locality form a Centre. Each Centre selects a Centre Leader and a Deputy Centre Leader from amongst the Group Leaders and Deputy Group Leaders to coordinate the centre activities.
- Each member of the Group deposits minimum Tk.1.00 per week in the Centre Fund. The Branch keeps this money in a Centre Fund Account in Muda'raba Savings Account. This fund is used for the welfare of the members by way of Qard-e-Hasan as per decision of the Centre in the weekly meeting. Centre Leader and Deputy Centre Leader operate the fund jointly. This fund is refundable.
- The Field Supervisor organized all the Centre meetings. Centre Meetings are held on weekly basis. The meetings are organized in a particular place, day and time as decided by the members of the Centre. The resolutions of the Centre meetings are recorded in a Resolution Book along with signatures of the members. The following activities are conducted in the centre meeting:
 - Attendance of all the members present is kept.
 - Members discuss ideas, opinions, moral values, and norms and rules of the Scheme.
 - In Centre meetings the Field Supervisor collect installments and personal savings from the members and give entry into members' Pass Book. The Field Supervisor duly signs the pass after any entry is made in Pass Book.

Recording of resolution in the Resolution Book will be duplicated. The original copy is sent to the Branch on the same day for recording and posting in the respective ledger account of the client with the Branch. The Field Supervisor keeps the carbon copy of the resolution.

- Investment Proposals are prepared in the Centre Meeting. The Field Supervisor prepares the list of eligible clients with details purposes and terms of disbursement and repayment with the norms of the Program. After finalization of the investment proposals, the list of the selected client members supported by application forms and other related papers is submitted to the Branch Manager duly signed by the Group Leader, Centre Leader, Field Supervisor and Project Officer.
- The Investment Committee at the Branch gives its observation and sanction the investment if found suitable. The applications are disposed off within seven days from the date of receipt of the applications till the date of disbursement of the investment. In case of rejection the decision is conveyed to the applicants within 7 days of receipt of the application.

vi) Security Requirements for Obtaining Investment Facilities:

Generally, no security is required for investment under this Scheme. In all cases each member of the Group gives personal guarantee for himself and for other members of the Group. Therefore, all the members of a Group are individually and collectively responsible for default of each and every members of the Group.

In case of investment for the purposes of pond fishery, agriculture, and irrigation implements, the investment clients are to keep their original documents with the branch as security of investments by way of simple deposit of the title deeds through a memorandum of deposit executed by the client owner.

- Purpose, Repayment Period and Ceiling of Investment:

Purpose	Period	Maximum Limit
a) Crop Production	1 year	Tk.10000/
b) Pond Fishing	3 years	Tk.25000/
c) Other Off Farm Activities	1 year	Tk.10000/
d) Irrigation Charges	1 year	Tk.5000/
e) Agriculture and Irrigation Equipment	3 years	Tk.25000/
f) Rickshaw/ Van and other Rural Transport	2 years	Tk.5000/
g) Hand Tube-well for Pure Drinking Water	3 years	Tk.3000/
h) Construction Materials for House	3 years	Tk.15000/

viii) Other Investment Facilities:

The investment requirements of the deserving clients who are not covered under the Scheme may be accommodated under other existing /proposed Scheme of the Bank:

- Small Business Investment Scheme
- Agriculture Implements Investment Scheme
- Micro Industries Investment Scheme
- Dairy Investment Scheme
- Others

ix) Mode of Investment:

The concerned Branch selects any of the following modes depending upon the sector and purpose of investment:

a) Bai-Muujjal

Under this mode the concerned Branch sells goods to the client on differed payment basis. The payment is to be made in installment / lump sum on predetermined future date.

b) Hire Purchase Shirkatul Meelk(HPSM) or Leasing:

Under this mode the concerned branch supplies equipments on rental basis. The Bank retains the ownership of the equipment while the bank authorizes the client to possess the equipment for certain period. Under this scheme the client is to contribute minimum 10% of the purchase price of the equipment as cash security and the bank contributes the rest of the purchase price. Under leasing system Bank pays full purchase price of the equipment while client deposits down payment of the equipment equivalent to 2 installments prior to availing the investment, which is kept as cash securities and is refunded at the expiry of lease term.

c) Mudaraba

Under this mode of investment Bank supplies capital to the Mudarib (agent) for conducting business, purchase inputs, and commodities. The client will repay the amount on a future date.

d) Musharaka

Under this mode certain branch extends investment on profit and loss basis. The bank provides 80% of the total capital while client contributes 20% of the same.

e) Bai-Salam

Under this mode Branch executes advance purchase contract with the client and makes payment against the purchase of product, which is under process of production. A Bai-Salam contract is executed before making any investment showing price, quantity, quality, time, price and mode of delivery.

f) Murabaha

Under this sale contract the particular Branch purchase a certain commodity for the client as requested and specified by him which are deliverable to him on payment at a predetermined price. Under this mode the client is to pay 20% of the cost price as cash security.

x) Recovery of Investment

The Branch judiciously determines the installments to ensure the recovery of investment in stipulated time. Installments are fixed keeping in view the income generating capacity of the project and the time thereof:

- In case of off-farm activities installments are fixed on weekly basis.
- In case of agriculture/ crop production the installments are fixed on quarterly basis or on the basis of the harvesting period of the crop.

xi) Support Project of the Rural Development Scheme by Islami Bank Foundation (IBF):

Deployment is a multi-dimensional approach with continuous progress. But no development is possible without sustainable development in education, income, consumption, health and Medicare. It is, therefore, necessary to take integrated approach in these areas. Islami Bank Bangladesh Limited being a business institution can hardly afford time and attention to areas other than income generation. Education, health and Medicare are still not high profitable.

Considering the above facts Islami Bank Foundation, a social welfare organization, has taken initiative to promote these social welfare activities. As a non-profit welfare organization it is relatively easier for Islami Bank Foundation to operate in the areas of education, health and Medicare and as such the Foundation has taken up a support project of the rural Development Scheme (RDS) of Islami Bank Bangladesh Limited.

a) Aims and Objectives

The principal aims and objectives of the project are to provide mass education, health and Medicare services for the integrated development of the villages covered under RDS of Islami Bank Bangladesh Limited. The specific objectives are as under:

- To provide elementary education with fundamental teachings of Islam to the children of the villages under Rural Development Scheme.
- To eliminate illiteracy from the villagers under Rural Development Scheme. To encourage educated people to establish libraries in the rural areas to create opportunities for learning.
- To encourage the villagers under the Scheme to follow Islamic way of life.
- To encourage the villagers under the Scheme to follow Islamic teachings regarding healthcare and cleanness and also to create awareness among the people about health and hygiene.
- To create awareness among the people under RDS to use pure water for drinking and other household activities and also to make arrangement for supply of pure drinking water.
- To encourage the villagers in the use of sanitary latrines and help them to establish water sealed sanitary latrines.
- To create opportunities for primary healthcare and to introduce immunization program.
- To create opportunities for treatment of critical and vulnerable patients in villages under RDS.

b) Programs Offered by Islami Bank Foundation:

Islami Bank Foundation has two types of Programs in the villages covered under Rural Development Scheme:

1. Education Program
2. Health and Medicare program.

1) Education Program:

The Education Program includes the following:

a) Establishment and Operation of Forquania Madrasah:

Under this scheme the Foundation establishes and operates Forquania Madrasah in the villages covered by the Rural Development Scheme. The objective is to create opportunities for basic Islamic teachings for minor boys and girls who are deprived of the light of Islamic education. The course curriculum includes Surah Qerat, Quida, Ampara, and the Holy Qu'ran.

Generally a Forquania Madrasah is allowed for two three Centres in the same locality and the number of teachers depends on the number of students and proficiency of the teachers.

Mosque, Madrasah, School, or open floor of the dwelling house or any other open place is used to run the Madrasah. No separate accommodation is required for the purpose. A signboard showing 'Forquania Madrasah, Managed by Islamic Foundation' will be affixed in front of each of the Madrasah.

A total of 5 to 7 member Management Committee is formed comprising of representatives of the enlisted local voluntary organizations of the Foundation, Centre Leader (S) and Group Leader (S) of Rural Development Scheme and any other respectable persons of the locality. The Field Supervisor of the Rural Development Scheme will be the Secretary of the Management Committee. The manager of the nearest Branch of the Bank will be the ex-officio Adviser of the committee. The Management Committee is responsible to manage the operation of the Madrasah.

A fund is created out of the subscription of the members of the Centres of the Rural Development Scheme. The subscription is realized in the weekly/monthly installments. The Foundation bears a major part of the total expenditure of the Madrasah. The donation of the Foundation is reduced every year at the rate of 10% per year so that the Madrasah become self-reliant.

b) Establishment of Mass Education Centre, Library and Cassette Club:

The Foundation also helps establish Mass Education Centres in the villages under Rural Development Scheme. The illiterate members of the RDS Centres acquire the skill of reading and writing in addition to the ability of signing. The members of the Centre after completing their day-to-day activities attend classes in the evening in the Mass Education Centre. Usually one of the educated member of the Centre or a teacher of the Forquania Madrasah takes the responsibility of teaching the illiterate members of the Centre. Each Centre establishes Centre Library with authenticated religious books of cheaper edition to enrich the knowledge base of the members. The members' purchase books out of their own resources. The member(s) who can read will read by rotation and the other will listen. The Group members of the Rural Development Scheme form a management Committee to run the library. In each village under Rural Development Scheme there is a Cassette Club established by the members to get an opportunity for recreation after their daylong laborious work. Through this Club the members make arrangement so that they can hear Islamic songs, religious lectures and speeches etc. The Foundation provides a cassette recorder that would cost approximately Tk.3000/ along with a set of cassettes to each Cassette Club. A house is required to set up a Mass Education Centre, Library and Cassette Club, and for arranging various types of functions. If the member of the RDS can manage a piece of land, the Foundation provides Tk.10000/ for the construction of the house. The house may also be used for the Forquania Madrasah and Charitable Dispensary.

c) Health and Medicare Program:

1. Preventive Program:

Prevention is better than cure. Preventive measure is less costly but more fruitful. It is better to prevent the disease before it attacks. The following projects are undertaken for the purpose:

- Installation of Tube Well:

The Foundation supplies tube well to the Group members of the Rural Development Scheme for pure drinking water at a cost of Tk.1500/ only. The amount is realized within one year in weekly installment basis.

- Sanitary Latrine Project:

The RDS members whose attendance in the meetings, savings, and repayment of installments is 100 % and other performance is satisfactory are allowed to get Tk.500/ for the construction of a sanitary latrine. The amount is realized within one year in weekly installment basis.

- Immunization Program:

The Foundation launches immunization program in the villages covered under Rural Development Scheme to prevent the deadly diseases like tuberculosis, polio, measles, tetanus, diphtheria, whooping cough etc. The foundation provides training to the Rural Health Workers.

- Health Education Program:

Health Education Program is also undertaken by the Foundation in the villages under Rural Development Scheme to create an opportunity for primary health care of the villagers. The Foundation provides six-month health care and Medicare training to the local energetic Youths having SSC/HSC or equivalent degree under the Rural Health Workers Training Project. They look after the primary health care and Medicare services of the villagers under Rural Development Scheme. In each village one male and one female are provided with health care and Medicare training. They stay in their own village and provide primary health care and Medicare services to the villagers in exchange of reasonable fees. The Foundation bears the cost of food and lodging. But the trainees bear the cost of transportation. The male health workers provide primary health care facilities to all. The female health workers provide primary Medicare to the children and give advice to the pregnant women. The

Foundation also offers training to the common people about health care, cleanliness, nutrition, immunization etc.

2. Curative Programme

- Rural Health Centre

The Foundation has been establishing Rural Health Centre in the villages covered by the Rural development Scheme to render primary health care services to villagers. The Rural Health Centre establishes link with nearest government hospital and private clinics and Islami Bank Hospital.

These Centres provide facilities for the treatment of common diseases, child and mother care, prenatal check up, first aid, referred advice for critical patients, routine pathological tests etc. with reasonable fees.

The Rural Health workers who received training under the Rural Health Worker Training Project of the Foundation usually get the opportunity to be appointed in these Health Centres. One or more qualified doctor(s) of the nearest area is/are engaged in these Health Centres on specific days of a week. The doctors get reasonable fees for the purpose.

- Easy Available Health Service:

The critical Patients of the villages under Rural Development Scheme are referred to Islami Bank Hospital or nearest private clinics or government Hospitals for better treatment. Good relationship to be established with those Hospitals through the Rural Health Worker, RDS Supervisor and the representatives of the enlisted local voluntary organizations of the Foundation so that the referred patient can receive treatment at reasonable cost.

6.3 Welfare Programmes of Social Investment Bank Limited

Social Investment Bank Limited has some welfare programs under its non-formal and voluntary sector of Banking. The Bank's social welfare programs

are directed mainly to uplift the socio-economic conditions of rural and urban poor. In case of non-formal and voluntary sector banking operation, the Bank goes to the clients, and organizes and motivates them into viable income generating household, family or group. The main objective of this program is to transfer power to the powerless through Micro Credit and Micro Enterprise Family Empowerment Scheme. This voluntary sector is also involved in the development and management of Waqf and Mosque properties, management of inheritance properties, joint venture projects for management of Hajj affairs, development and management of non-profit foundations, charitable trusts and organizations, development and management of funds involving welfare of women and non-Muslim minorities and so on.

In Non-formal Banking Sector Social Investment Bank Limited has started implementing Environment Friendly Program with Small Traders of Tokai (mainly street children of distressed parents) with recovery rate of 100%, Real Life Tokai Non-formal School Management, and Family Credit Program involving modest investment with beneficiaries around 10, 000 in various parts of the country in a modest scale.⁵ The welfare programs under Non-formal and Voluntary sector are discussed below:

a) Environment Friendly Business with Small Traders of Tokai:

Under this scheme the distressed children have been organized. It is one of the important strategic projects. Tokai are those homeless, guardian less floating children or youth who pick up wastage from dustbin, roadside, and other garbage centres of the town. They not only collect the wastage but also keep clean the roads, drains and dwelling locality. But they are living inhuman lives.

Others always exploit them although they are engaged in environment friendly recycling program. It is quite possible to make this program a great

⁵ *Annual Report 1997*, p. 11.

success. During 1997, seventy-seven groups consisting of 1522 members have been formed at Hossain Market, Uttar Badda, Gulshan Thana; and Mohammadpur, Mirpur and other areas. Micro credit of Tk.8.80 million had been invested. The members of the groups made a saving amounting to Tk.1.76 million. The recovery rate was 100% against this investment.⁶ This modest beginning has great potentials. The further expansion of the project is going on.

b) Real Life Tokai Non-formal School Program:

As part of environment friendly program, the Bank is committed to educate the Tokai and this has a world wide strategic value. Social Investment Bank Limited has arranged non-formal schooling for the Tokai. 'Under this scheme, schools are started for them to give them education with Islamic orientation. In the process of learning the Tokai develops a habit of saving under Bank's supervision⁷. Along with basic education Tokais are also provide with knowledge of healthcare and sanitation. The course curriculum includes Bangla, Arithmetic, Religion and social awareness. In addition, they learn as to how they should manage their business.

c) Benarashi Sharee Weaver's Project

Thousand of workers are engaged in producing Benarashi Sharee. Most of them are engaged on daily wages basis. This type of workers will never be the owner of any loom or factory due to financial constraints. Social Investment Bank Limited provides financial assistance to these skilled weavers to have their own looms or factories. The Bank also extends financial assistance to the owners of one or two looms who cannot purchase their necessary raw materials.

⁶ *Annual Report 1997*, p. 12.

⁷ Shah Abdul Hannan, "Islamic Banking in Bangladesh: Impact and Prospects", *Thoughts on Economics*, Vol. 10, No. 3 & 4, July-December 2000, p. 13.

The bank ensures family participation (husband & wife both) at the time of investment. Thus the aim of the Bank is to select successful entrepreneurs among them and convert their initiative into micro enterprise projects.

d) Small Traders Family Financing Project:

This project includes small factories like shoe making, rickshaw workshops, general shopkeepers, restaurants, bamboo & cane making, vegetable cultivation, vegetable & other grocery shops, tailoring shops etc. Investment is made as working capital and for expansion of business of small traders whose own capital is around TK.1 (one) Lac. The aim of this project is to improve the financial condition of ill-fated small traders' family who cannot avail formal banking facilities due to lack of collateral security.

e) Monipuri Tribal Family Financing Project:

Most of the women of Monipuri tribe are engaged in producing hand made special dress like Lungi, Chadar, and Bedcovers etc. These special items have wide demand in the market due to their design, colour and fashion. But they cannot produce and supply these items in bulk due to lack of capital. Social Investment Bank Limited, thus, provides financial assistance to these women to increase their production of special dress.

f) Rotating Family Savings and Credit Net and Group Installment Credit Scheme:

This credit program is aiming at alleviating poverty from the society. Under this scheme a small number of individuals, typically six to forty form a group and select a leader who periodically collects a given amount (a share) from each member. The money collected (the fund) is then given in rotation to each member of the group. The leader receives no special consideration (other than the possibility getting the first fund). He may also get commission, who in return may assume liability for defaults. Loans are interest free.

At the grass root village and local level it is directed towards landless day laborers, marginal farmers, small artisans (e.g., blacksmith, carpenter, and potter and handicraft producer), urban unemployed, small traders, rural industries, and small to medium scale business enterprises.

g) Micro Credit Line:

Currently Social Investment Bank Limited is investing a maximum amount of Tk.25000/ per family without collateral security under Micro Credit Program as permissible by Bangladesh Bank. This amount is considered insufficient for the purpose of crossing the border of poverty line. The credit ceiling should be raised to at least TK.50000/ per family.

Besides, the Bank has already introduced Rotating Family Savings and Credit Net and Group Installment Credit Scheme for any group of individual. In the light of this experience, Social Investment Bank Limited is also in the process of developing program to assist Agriculture Cooperatives in providing tailor made credit package to achieve their objectives in rural setting.

h) The "Sabuj Haat" project:

The Sabuj Haat (SH) project is indeed an innovative Banking product, involving integration of formal, non-formal and voluntary sector banking operations all at a time. The establishment of a mini village mall or bazar consisting of carefully planned ten to fifteen mall shops, built preferably on Waqf or Trust properties. A small Rural Branch (Palli Shaka) of the bank, a Community Centre and an Health Unit will be an integral part of the "Sabuj Haat" complex. It is a social revolutionary concept intended to extend credit to family and make it available at their doorsteps with provisioning for non-formal training and marketing. It would start with micro-credit program of a cluster of family at the grass root level. The graduates of such program, a first generation of small entrepreneurs will be given an opportunity to make a move upward on a social scale by allocating micro-enterprise shops of the 'Sauj Haat' to them mainly on rental basis. A credit line will be extended to them to finance their small

businesses under the overall supervision of a local branch manager. These mini shops will sell the basic needs of village household based on a careful household survey which will be undertaken to determine their income, consumption pattern, credit need and occupational structure. As a matter of rule, a Rural Branch will be established on a Waqf land, would extend micro-credit to cluster of families, ensuring joint liabilities of husbands and their wives, without collateral securities and finance micro-enterprises as well as provide formal banking credits. This is how the concept of "Sabuj Haat" would integrate formal, non-formal and voluntary sector banking activities into one for reversing the process of current pro-urban banking operations, financing patterns and anti-poor development strategies. The wheels of development would move forward from the grass-root level'.⁸

The Board of Social Investment Bank Limited in its 20th Emergent Meeting held on 22 November 1999 approved the establishment of 400 Rural Branches (Palli Sahaka) under its "Sabuj Haat" project and 60 urban branches throughout Bangladesh to make a massive attack of poverty within a short span of 5 to 7 years.⁹

- Main Features of the "Sabuj Haat" Project:

The main features of the "Sabuj Haat" project are furnished below:

- To initiate development process from grass root family level through extending suitable credit facilities at their door-step and mobilizing their savings and investments.
- To push forward the family beyond the poverty line and reduces internal migration.
- To push forward local voluntary sector activities through financing the development initiative of Waqf and Non-Muslim Trust properties.

⁸ *Annual Report, 1999*, p. 7.

⁹ *Annual Report 1999*, p. 8.

- To pull the poor family to join the village development movement and reduce the problems of unemployment, social alienation and moral degradation.
- To prevent marginal farmers to become landless.
- To create both participatory and self-employment opportunities for the rural poor.
- To help the poor students of local Schools, Colleges, and Madrasah through student scholarship program.
- To open up new frontiers of human freedom of vertical social mobility.

The Bank under its voluntary banking sector started implementation of the following programs:

i) Mosque and Waqf Property Development Program:

The Bank intends to develop Mosque and Waqf property so as to make it economically self-sustaining and socially most effective. The construction of Mini Market at Kazi Bari Mosque, Uttar Khan, Uttara, Dhaka, consisting of 4 shops has been completed where Bank has invested TK. 147, 000. Credit facilities were also allowed to all the shopkeepers for expanding their businesses. The recovery rate is almost 99%.¹⁰ Another project is going to be implemented at Saver, Dhaka.

i) Cash Waqf Certificate:

In this voluntary sector, Social Investment Bank Limited has introduced Cash Waqf Certificate, a new product for the first time in the history of banking for mobilizing and capitalization of social savings. This scheme has been well received by the public in general for its unique feature. 'Generally, Waqf means the permanent dedication of any property by a Muslim for any purpose recognized by Islamic law as religious, pious or charitable. A research study showed that 'Cash Waqf' is also recognized in Islam. Its use can be traced during the Ottoman era as well as in Egypt¹¹. The guidelines for operation of this scheme are stated below:¹²

¹⁰ *Annual Report 1997*, p. 13

¹¹ *Annual Report 1998*, p. 13

¹² *Annual Report 1999*, p. 21.

- Cash Waqf is an endowment in conformity with Shariah. Bank manages the Waqf on behalf of the waquif.
- Cash Waqf amount earns profit at the highest rate offered by the Bank from time to time.
- Cash Waqf amount remains intact and only the profit amount is spent for the purpose(s) specified by the Waquif. Unspent profit amount automatically adds to Waqf amount and earn profit to grow over time.
- Waquif can also instruct the bank to spend the entire profit amount for the purpose specified by him/her.
- Waquif has the opportunity to create cash Waqf at a time. Otherwise he/she may declare the amount he/she intends to build up and may start with minimum deposits of Tk.1000/ (one thousand) only. The subsequent deposits may also be made in thousand or in multiple of thousand.
- Waquif has the right to give standing instruction to the bank for regular realization of Cash Waqf at the rate specified by him /her from any other Accounts maintained with Social Investment Bank Limited.
- Waquif has the liberty to choose the purpose(s) to be served either from the list of 32 purposes identified by the bank covering i) Family empowerment credits, ii) Human resource development, iii) Health, sanitation, and social utility services or any other purpose(s) permitted by Shariah.

The list of 32 purposes identified by Social Investment Bank Limited is furnished below:

- Family Rehabilitation:
 1. Improving the conditions of poorest of the poor living below the poverty line.

2. Rehabilitating physically handicapped and disadvantaged segment of the society.
 3. Rehabilitating beggars.
 4. Rehabilitating destitute women.
 5. Upliftment of Urban slum dwellers.
- Education & Culture:
6. Education of orphans' i.e. supplying books free of cost.
 7. Expansion and development of appropriate education for skill development.
 8. Informal education facilities of children at home (i.e. mother's education program, children literature).
 9. Physical education and sports facilities.
 10. Supporting local culture and heritage and art promotion.
 11. Conducting Dawah activities.
 12. Supporting education of deserving students in the form of scholarship.
 13. Supporting vocational education in general.
 14. Supporting education of a specific area.
 15. Financing specific Madrasah/ school/college of a particular area.
 16. Educating deserving descendents.
 17. Supporting any projects in the area of education, research, religious and social services in the memory of farther, mother and any descendants.
 18. Establishing education chair.

- Health & Sanitation:

19. Village health care and sanitation.
20. Supplying pure drinking water (to households, schools, mosques, slums, etc.).
21. Establishing Hospitals, clinics, health care programs especially for the poor.
22. Health research grant, research in particular disease.

- Social Utility Service:

23. Settling disputes (e.g. village litigation).
24. Providing legal aid to deserving women to establish their lawful rights.
25. Assist in arranging dowry less marriages of the poor girls.
26. Maintenance of public roads and tree plantation in the village.
27. Providing assistance to peace loving non-Muslim and solving their problems.
28. Creating social awareness to prohibit gambling and other anti social activities.
29. Construction, installation and development of public utility services.
30. Maintenance of a specific mosque with an income-generating project.
31. Maintenance of a specific graveyard with an income-generating project.
32. Maintenance of a specific Eidga with an income-generating project.

- Voluntary Sector Other Investment Bond/ Certificate:

The Social Investment Bank Limited is going to introduce a number of bonds with different sets of rules in conformity with the Shariah namely Mosque

Properties Development Bond (general/specific), Mosque Property Qard-e-Hasan Certificate, Waqf Properties Development Bond (general/ specific), Non-Muslim Trust Properties Development Bond etc. The Bank gives guarantee to the Bondholders regarding payment against surrender of the instruments on maturity.

6.4 Social Welfare Programmes of Al-Arafah Islami Bank Limited

The bank has been spending a portion of its income on philanthropic activities. Among others Al-Arafah English Medium Madrasah and Al-Arafah Islami Bank Library are worthy to be mentioned.

a) Al- Arafah English Medium Madrasah

Al-Arafah Islami Bank Foundation established Al-Arafah English Medium Madrasah at Dhanmondi, Dhaka in 1999. The aim of the project is to prepare the next generation according to the ideas of peace and equality of Islam and to establish financial system, banking system and other aspects of life in the way of Islam. This Madrasah has been contributing towards developing human resources of the country. Such Institution up to O level of its kind is the first time in Bangladesh.

b) Al-Arafah Islami Bank Library

As we know library is the career and reservoir of knowledge. Al-Arafah Islami Bank Foundation has established a public library at 32, Topkhana Road, Chittagong Bhaban (1st floor) Dhaka. The aim of this project is to contribute significantly in the field of storing and sharing knowledge and thus strengthening social development. It contains 23,000 reference books for the researchers, students, professionals, bankers, physicians, engineers, politicians, writers, journalists, and even for kids. From 2000 it is opened for all and well located and accessible to everybody. It collected some exceptional books on Religion, Economics, Banking, Computer Science, Information Technology, Business Administration, Sociology, English and Arabic Language and juvenile literature in Bengla, English, and Urdu & Arabic, which are very useful and popular.

Verities of books have been collected, but the main driving force behind the collection is to enrich Islamic Knowledge, Culture and Values. If religion is not attached to education the real attitudes towards life & Values will not develop. It is essential to read Elem-e_Din to govern our life in the right way of Islam Shariah. In order to achieve this goal Al-Arafah Islami Bank Library started Dars-ul-Qur'an (Teaching of Qur'an) program. This program covers translation with detail explanation of Qur'an. Dars-ul-Qur'an program takes place every Monday after Magrib prayer. Al-Arafah Islami Bank Library also arranges shows of feature films or documentary films on Islamic way of life & culture. Besides, Al-Arafah Islami Bank Foundation has distributed so far a total of 1084 copies of Arabic-Bangla 'Torjomatul Qur'an' to the poor literate people.

c) Staff Welfare Project

Al-Arafah Islami Bank is always kept a careful eye on the economic security, benefit and good working condition of its staff and officers. The Bank keeps a contributory provident fund, a social security & benevolent fund and a gratuity fund for its employees. The bank paid Tk.30 Lac from the fund to the families of late officers & staff of the Bank till 31 December 2003. A separate Board of Trustees manages these funds.

- Micro-credit Program for the Rural Poor

Al-Arafah Islami Bank has been expanding its service coverage through opening new branches all over the country. At present out of its 40 (till 31 December 2003) branches 5 branches are situated in rural areas. The Bank offers micro investments in rural areas by its 3 branches. The Bank provides micro investment for Poultry, Fish Culture, Beef Fattening, Milch Cows, Rural Health Project, Small Vehicles, and Small Traders Investment Project etc.

Chapter 7

Conclusion

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Conclusion

Islam, is not only a religion in the western sense of the term, rather it is a *Din* or a complete code of life covering all aspects of man's entity from the cradle to the grave. It seeks to direct human being to the right path vouchsafed by Allah in this world and pinpointedly urges to locate the ways of salvation in the next world. It controls the affairs of man in society under the framework of the Shariah. Islam aims at establishing a peaceful society based on equity, fraternity, justice and economic egalitarianism. To realize this end Islam prescribes lawful bread and abhors illegal earnings. There is no denying of the fact that lawful bread is the prerequisite of acceptance of all the prayers sanctioned by the Shariah of Islam. Hence from the inception of Islam steps were taken by the Prophet (SM) and his earnest followers for the economic equilibrium based on Divine revelation. In the hey days of Islam and the age of Khilafat *Bayt al-Mal* functioned as a lawful instrumental for the transaction of economic enterprises of the Muslim Ummah on the *Minhaj ash Shariah*. The concept of modern Islamic banking might have been borrowed from that legal economic system of Islam.

The basic principles of Islamic banking originate in the axioms of justice and harmony with reality and the human nature. Islamic Bank is a financial institute whose statutes, rules and procedures expressly states its commitment to the tenets of Islamic Shariah and to the banning of receipt and payment of interest on any of its operations. Islam prohibits Muslims from giving, taking, accounting and witnessing Riba (interest) regardless of the purpose for which such loans are taken and regardless of the rate at which Riba is charged. Islamic Banks cannot pay interest to their depositors and also cannot demand or receive any interest from borrowers on loans. Islamic Banks never lend money; they just invest money with the anticipation of profit. One of main feature of Islamic

Banking is that the provider of capital (Bank) and the user of capital (businessman) have to share the risk of business venture.

The Islamic system assigns private property the corner stone of its socio-economic order. The owner has the full right to the increase, growth, benefit and profit that results from one's property. This is also consistent with human nature. If a property is entrusted to some one else (through financing), the user's efforts that contribute to growth and profit must also be recognized. The result or actual outcome of such cooperation should fairly be distributed among the two parties and nothing else.

Banker- customers relationships in Islam are established on profit-loss sharing arrangement instead of predetermined interest. Under interest based banking system, the borrower is obliged to pay a predetermined rate of interest on the borrowed money even though he may have incurred a loss. In a loss situation the fixed interest based system could lead to bankruptcy in some cases.

The interest based Banking does not ensure distributive justice of investment financing. Distributive justice means distribution of risk and returns between the financier, depositors and entrepreneurs in such a manner that no body is to receive or bear an undue share of benefit or loss. In case of loss the interest based banks shift it altogether to the client. Interest based Banks demand sound collateral securities with the intention that if the borrower for some reason is unable to repay the claims of the bank, the money (Principal + Interest) can be realized from the sale of the collateral securities. This is sheer injustice according to Islamic Shariah.

Interest is completely prohibited in Islam. There is no objection in getting a return on capital if the provider of capital enters into a partnership such as Mudaraba and Musharaka with the client and is prepared to share in the risk and returns between them. The Bank would not be entitled to claim a predetermined return (interest) on the capital provided by it to the client. But the Bank can enter into a profit-loss sharing arrangement with him. In the Mudaraba

arrangements, the Bank provides full finance of the project. Profits are shared in pre-agreed proportions but loss, if any, is entirely borne by the Bank. There is no financial loss of the client except his labor and time. In case of Musharaka arrangements the Bank and the client jointly contribute to the capital of the project. Profits are shared in pre-agreed proportions but the loss, if any, is shared in proportion to the capital contributed by the bank and the client. Similarly, the depositors of the Bank may not be guaranteed a predetermined return on their savings, but they would be entitled to share in the actual profits earned by the Bank.

The religious principles on which Islamic Banks are based are integrated with the ethical and moral values to the extent that these new institutions cannot detach themselves from socio-moral considerations even if they try.

There are different forms in which the socio-moral commitments of Islamic Banks are manifested. For example, many Islamic Banks have developed a practice of extending interest-free credits (Qard-e-Hasan) to their clients in case of dire need or unexpected circumstances. The Prophet (SM) has advocated for Qard. Ibn Masud narrated that the Prophet(SM) said: whoever gives two loans will have a reward (equivalent to the reward) of one of them (be it given as charity).¹ Hazrat Anas (R) narrates that the Prophet (SM) said: The night I was taken up to the Heaven, I saw written on the Heaven's gate ' Charity is (multiplied) ten times and a Qard is (multiplied) eighteen times. I said 'O Jibril, why is a Qard better than a charity? He said " because a beggar (may) ask while he has (wealth) and a borrow would not ask for a Qard except out of need"² Ibn Qudama argues that "giving Qard is considered "desirable" in the Shariah because lending implies the provision of relief to one's Muslim brother, the fulfillment of his needs and the extension of help and support."³ Considering the above facts Islamic Banks have been providing several types of loans and

¹ Ibn Majah, Vol. 2, p. 812.

² Ibid.

³ Al Marghinani, *Al-Hidiaya*, Vol. 4 (Beirut: Dar al Kitab al Arabi Publishers), p. 353.

investment opportunities such as Qard-e-Hasan (benevolent loan), Mudarabah and Musharaka (partnership), Bai Salam⁴ Murabaha⁵, Ijara (leasing), Hire Purchase Sirkatul Meelk⁶, etc.

Many Islamic Banks have also established social funds especially designed to alleviate hardship of the poor and the needy. This fund is usually financed from the yearly Zakah dues on shareholders' capital as well as many investment deposits who give their consent to the Bank's management for the deduction and distribution of Zakah annually. . Customers are also encouraged to deposit their Zakah to the Zakah Funds of the Islamic Banks. A unique aspect of the Islamic system is Zakah, which is known as the third pillar of this religion. It comes, after prayer, as the second most important worshipping ritual, and is simply a financial religious duty on the rich for the support of the poor. Islam is the only system, and the only religion, that gives the poor a direct right in the wealth of the rich in a legal sense. The Zakah Fund does have a target-oriented program. The target groups consist mostly of the poorest and disadvantaged segment of the society. It may be noted that Zakah is a charge on the economic assets of the rich. Hence the Zakah-based program of the Islamic Banks is a mechanism for redistribution of the society's assets from the rich to the poor. As such, it widens the relationship of the banker and the customer.

Different Islamic Bank in Bangladesh have established social welfare Foundations such as Islami Bank Bangladesh Foundation, Al-Arafah Islami Bank Foundation, and Al-Baraka Bank Foundation to promote social welfare activities targeted to the downtrodden and disadvantaged segment of the society. These Foundation are to promote people oriented mass education with religious outlook, extend health and Medicare facilities to poverty striking people of the country, create facilities for productive self employment and develop human

⁴ Purchase in advance when commodities are in the process of production.

⁵ Sale of goods adding certain amount of profit with cost.

⁶ Bank buys an item for the client and hires it to him for an agreed rent and period, and at the end of period client automatically becomes the owner of the item.

resources for improving economic condition and quality of life, assist healthy growth of culture, art, literature, science and technology, sports, research and propagation of Islamic teaching. Among the Foundations, only Islami Bank Foundation has been promoting different social welfare programs as part of its social commitment. The Al Arafah Islami Bank Foundation has so far established Al Arafah English Medium Madrasah and Al Arafah Islami Bank Library, and introduced Staff Welfare Project and Micro-credit for the Rural Poor. While Al Barak Bank Foundation renamed as Oriental Bank Foundation has not yet started any social welfare programs.

'The charters of many Islamic Banks make specific mention of Islamic socio-economic objectives being the guiding force of their activities.'⁷ As such Islamic Banks should contribute positively towards the achievement of a pattern of growth best suited for the eradication of poverty, equitable distribution of income and wealth, establishment of socio-economic justice through the practice of adl and ihsan and creation of sufficient opportunities for gainful employment.⁸ "The proportion of total profit paid to the depositors, rate of return charged from the client for various activities, proportion of total capital allocation made to the rural areas (including the agricultural sector) and extending helping hands to the needy in times of distress are the criteria by which the practice of adl and ihsan of an Islamic Bank may be judged."⁹

However, only Islami Bank Bangladesh Limited and Social Investment Bank Limited have given due attention to finance activities aiming at attaining these objectives. Other Islamic Banks in Bangladesh could not rank to steer up their programmes with multidimensional in character. Their published annual

⁷ Professor Shah Muhammad Habibur Rahman, "Islamic Banking Revisited", *Thoughts on Economics*, Vol. 11, NO. 3 & 4 (Dhaka : Islamic Economic Research Bureau), July-December 2001, p. 68.

⁸ Ziauddin Ahmad, "Islamic Banking in the Crossroads", A.H.M. Sadeq *et al.* (Eds.), *Development and Finance in Islam*, International Islamic University Press, Malaysia, 1991, and M. Umar Chapra, *Towards a Just Monetary System* (U.K. : The Islamic Foundation, 1985).

⁹ Professor Shah Muhammad Habibur Rahman, "Islamic Banking Revisited", *Thoughts on Economics*, Vol. 11, NO. 3 & 4 (Dhaka : Islamic Economics Research Bureau, July-December 2001), p. 68.

reports, booklets, and posters express their commitment to the establishment of a just society free from all sorts of exploitation. But in practice little progress has yet been achieved in this respect. Contrarily, these Banks have been providing credit facilities to well established businessmen and enterprises that often obtain credit facilities from both interest based Banks and Islamic Banks without any real commitment to free them from 'haram' means of financing. Thus they are deviating from their commitments, which they should take care of.

Many Islamic Banks also provide interest free loan to their employees. Moreover, Islamic Banks contribute to research and community development and assign sometimes-substantial amounts for these objectives.

Additionally, Islamic Banks in our country usually work within a traditional environment, and have working relationships with traditional Banks. Therefore, they often accumulate interest balances in their accounts with traditional Banks. According to the Islamic Shariah's, earned interest cannot be considered an income and it is to be disposed of to the poor in a way that does not directly benefit the Bank. Hence, those Islamic Banks that happens to earn interests spend them on the benevolent activities.

The biggest challenge Islamic Banks in Bangladesh have faced since their inception is how to narrow the gap between theory and practice. Islamic Banks in our country are competing with interest-based Banks in doing their business. They have been facing a number of problems in their operations especially in the area of financing investment. Some of the problems faced by Islamic Banks in Bangladesh are presented below. Most of these problems could be generalized for Islamic Banks all over the world:

- Investment activities of Islamic Banks are mostly concentrated on short-term trade financing. In theory they are using a combination of different investment modes acceptable to Islamic Shariah. But in practice they are

using mainly Murabaha, Bai-Muajjal, and Ijara modes of investment because these modes appear to be more convenient compared to profit-loss sharing system. Moreover, the risk involved in profit sharing seems to be so high that most of the Islamic Banks have resorted to those techniques that bring them a fixed return. They are in competition with interest-based banks and as such they want to earn a return on their investments, which is roughly comparable to prevailing interest rates. This can easily be achieved by investing in the above-mentioned modes as the "mark-up" (profit) can be fixed in a manner, which assures the required return. 'As a result, there is lot of genuine criticism that these Banks have not abolished interest but have in fact only changed the nomenclature of their transactions.'¹⁰

There is wide apprehension among Islamic scholars that little difference can be found between mark-up practiced by Islamic banks and interest based banks. Financing techniques like Murabaha, Bai Muajjal, and Ijara, which involve a pre-determined return on capital, cannot be regarded as commendable substitute for interest, and should only be used when absolutely needed. The Islamic jurists and scholars have argued that real substitute of interest in an Islamic financial system is the profit and loss sharing i.e. Mudaraba and Musharaka along with Qard-e-Hasan. They are in the opinion that the provider of capital should share the risk with the investment client if he wishes to earn profit.

- The repeated criticism against Islamic Banks, which is valid in many counts, is that it takes recourse to excessive use of Murabaha mode of financing investment. While Murabaha is suitable only for trading operations. As a result the lion share of the money deposited in Islamic Banks is invested in trading activities. Predominance of Murabaha

¹⁰ Muhammad Akram Khan, "A Survey of Critical Literature on Interest-free Banking", *Journal of Islamic Banking and Finance*, Vol. 6, No. 1, Karachi, 1989.

financing by the present day Islamic Banks in Bangladesh has been a hot agenda of discussion and a matter of writing. One study shows that Islami Bank Bangladesh Limited, Al-Arafah Islami Bank Limited and Social Investment Bank Limited have used 54%, 76% and 65% respectively of their investment funds by resorting to Murabaha mode.¹¹ Though Murabaha is a Shariah approved mode of financing investment, the Islamic scholars have traditionally prescribed for its limited application. Moreover, for balanced growth and development of the economy, Islamic Banks should judiciously invest in all sectors of the economy on the basis of priority: industry, agriculture, service, and non-formal & voluntary sectors for creation of self-employment and social welfare.

- Owner of the high return projects prefer borrowing from interest-based banks where the cost of borrowing turns out to be lower. That means Islamic Banks are not able to invest on projects with high return. Only the low-income projects whose rates of return are equal or below the market rate of interests are left for Islamic Banks. This leads to limiting the application of profit-loss sharing modes such as Mudaraba and Musharak. At this situation Islamic Banks switch over to other modes of financing such as Murabaha, Bai-Muajjal, Leasing, Hire Purchase, etc. Evidences indicate that Islamic Banks in Bangladesh can survive within conventional banking framework by switching over from profit –loss sharing to trade related modes.
- As regards financing social aspects Islamic Banks are accused of following the same practice like interest-based banks. Most of the Islamic Banks working in Bangladesh have no social welfare and rural development activities and are not serious about social agenda. Moreover,

¹¹ M. Azizul Hoque, "Islamic Banking in Bangladesh with a Brief Review of Operational Problems", paper presented in the seminar held at BIBM on 24 June 1996, p. 9 (unpublished).

Islamic Banks did not pay much attention to the development of banking services in some socially desirable sectors, except in few cases. The management of waqf estates, trusts, orphanages, graveyards, eidgha, charitable and religious organizations like charitable dispensaries, mosques, and fourkania mudrasha etc has remained out side the area of interest of most of the Islamic Banks in Bangladesh. Only Islami Bank Bangladesh Limited and Social Investment Bank Limited have a full range of social welfare activities as well as programs for the disadvantaged segment of the society. Al-Arafah Islami Bnak Limited has a few social welfare programs. While Shahjalal Bank Limited, Samil Bank of Bahrain EC, Dhaka, Oriental Bank Limited, and Prime Bank Limited- Islamic Branches have not yet started any direct social welfare programs and poverty alleviation schemes to fulfill their social obligations and commitments.

- In case of delay in repayment of loan interest-free banks can charge compound interest for the excess period. Islamic Banks cannot do that. They realize comprehension at the rate of profit. But the comprehension so realized is not added to profit income rather added to Sadaqa Tahabil for social welfare activities. This decline profits of Islamic Banks. This may place Islamic Banks in weaker position in terms of profit figure as compared to interest based Banks.

Besides, Islamic Banks are to make a compulsory levy of 2.5% of its profit earned each year and add to the Sadaqa Tahabil, which also decreases Banks' profit. This is unlikely the case with interest based Banks.

- Islamic Banks are blamed for their lack of cooperativeness among them. Most of the Islamic Banks have not yet taken memberships of the International Association of Islamic Banks. The Association has not yet

been successful in unifying their regulations and establishes relationship and promotes understanding among them. Even the idea of establishing a " Bank of Islamic Banks" is still a proposition. But there is an urgent need for its establishment to coordinate the functions of Islamic Banks and establish cooperation among them. And as result of its absence, Islamic Banks have lost hundreds of millions with the collapse of the Bank of Credit and Commerce International. Hundreds of millions Islamic funds continue to go into investment houses doing business in the West while Muslim world remains thirsty for shortage of investment resources.

Considering the prons and cons of the situation we are but to say that the Islamic banking is now a reality and its entity can never be denied. Most of the Islamic Banks are working efficiently and doing well as compared to the interest based Banks in the country. But to be more cogent and successful our society should be geared on Islamic principles, values and teachings. The Government also should strive sincerely to create a thriving environment for the implementation of the Islamic financial system in the country. Islamic banking in Bangladesh has not yet achieved the desired level of success due to the absence of Shariah based legal framework to carry out smooth operation of Islamic banking activities in the country. It is simply impossible for a few Islamic Banks to change the direction of the economy and improve the socio-economic conditions of the country till the Government of the country decides to Islamize the total banking sector and the economy as whole. Islamic Banks can satisfy most of the efficiency conditions if they can operate as a sole system.

Islamic Banks in Bangladesh have been trying hard to meet the other challenges through several means. The first is to work for a better understanding of the concepts upon which their operations are based. Now traditional banks are mostly cooperative and accommodative. Bangladesh Bank

has also come forward with new ideas of better methods for supervision and control to suit the operations of Islamic Banks.

Another means is to train their staff in this new form of banking and to press for more banking and financial innovations, which are required for the new modes of financing investment.

Nonetheless, many challenges still remain, not the least to the predominance of Murabaha (sale mode) in the operations of some Islamic Banks, as well as the relative scarcity of short-term Islamic financial instruments.

The prospects of Islamic banking and finance will depend extensively on the ability of Islamic Banks to continue facing challenges with resources and creativity, in addition to bring worthy of trust and understanding.

The gradual expansion of Islamic banking all over the world coupled with growing awareness of the people about its economic and social commitments makes it clear that this Millennium is the Millennium of Islamic banking and Islamic economy. Bangladesh in her Islamic banking sector, we think, will not lag behind, but will foster congenial atmosphere to elevate her multidimensional programmes to the optimum.

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