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IAFIE BULLETIN is published six times a year by the Indian Association for Islamic Economics. It aims to create awareness of the latest development in theory and practice of Islamic Economics.

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Interest and the Modern Economy

A major misunderstanding regarding the prohibition of interest is that such a law will make it impossible to earn a return on capital. As a consequence, investments will dry up and growth of the economy will be reduced or eliminated. In fact, Islamic law provides for a number of permissible alternatives to interest, and hence allows for earning a return on capital. The economic function, which the interest rate performs, can be fulfilled without using the particular form, which takes in modern banking. This may seem surprising since the opposite is frequently asserted in popular press, but this point is well understood by economists. For example, one of the leading texts in macroeconomics, Obstfeld and Rogoff (1996), states in the presence of profit-sharing or other arrangements '*the ban on... interest... would not interfere with the efficiency of the economy.*'

A second misunderstanding concerns the critical role of credit in the nature of modern investment and business spending. Contrary to popular misconception, the majority of funds, which finance business needs in the US, for example, are raised as equity (and not loans) on the open market (that is, common stocks, which are perfectly permissible under Islamic law). Kester (1986) lists debt-to-equity financing is much more prevalent than (interest-based and Islamically prohibited) debt financing. This amount of debt would be reduced even further were it not for the artificial tax advantage of debt-based financing in these countries (since interest payments can be written off). As a practical matter, equity financing is widely used and has many advantages over debt-based financing, listed in many texts on corporate finance.

There is no reason to suppose that investment will decline under a switch to the Islamic system. Implementation of the Islamic law would eliminate returns on risk-insulated fixed returns (on credit), it bring into existence other types of return not only on entrepreneurial capital but also on permissible credit-like transactions. For example, Islamic law permits profits on purchase and re-sale of goods with a mark-up (*murabahah*), which banks can use to fulfill the businessman's need for credit to finance the purchase of assets. This is a very common mode of financing in the Islamic banks and financial organizations that have been created. This method is virtually risk free and creates an instrument for credit very much like conventional interest-based loans. At the other end of the spectrum, we have Islamically permissible common stocks, which have high returns and high risks. What is relevant here is that while the mix of financial instruments available would change in an Islamic system, they would not differ much in functionality form the mix currently available in a modern economy.

Arshad Zaman and Asad Zaman

Indian Muslim Ask for 'Minorities Bank'

It is the first time that Indian Muslim have asserted that the nationalized bank in the country so far have failed to help remove the economic backwardness of Muslims. The Minorities Action Group of India (MAGI) has demanded setting up of a "Minorities Bank" for bailing out the community from their predicament.

This demand forms part of a 16-point resolution passed by the National Convention for Educational and Economic Development of Minorities during their meeting in New Delhi on July 24 organized by the Action Group. The convention demands that the Union Government instruct Reserve Bank of India to issue licence for Indian Minorities Development Bank", the resolution said. The details of the resolution were announced at a media briefing addressed jointly by the former Union Minister, Mr. C.M. Ibrahim, the National Minorities Development and Finance Corporation Chairman, Mr. Qari Mohammad Mian Mazhari, and the National Commission for Minorities Member, Mr. S. Shamim Kazim.

"Establishment of this Indian Minorities Development Bank will help in removing economic difficulties of minorities particularly the 240 millions Muslims of the country", Mr. Ibrahim said. Referring to the resolution, which said that Government should contribute 40 per cent of the proposed bank's share, Mr. Ibrahim said; "Even if they do not contribute anything, and just give us the license, we will raise the amount of our own."

Stating more than 60 million Muslims were living below the poverty line, Mr. Mzhari said that so far the nationalized banks have failed to come to the rescue of the of the community 'Establishment of the bank is the need of the hour for which minorities have prepared themselves'. (*The Hindu*)

IAFIE Kerala Offers Fellowships

Calicut: The IAFIE Kerala Chapter has decided to give fellowships to the brilliant scholars in Kerala who intend to do M. Phil./Ph.D. in Islamic Economics. Besides the fellowships, guidance will also be provided by an expert group formed under the auspices of IAFIE. The aim of this project is to create experts in this subject. The value of the fellowship is Rs. 1500 per month for M.Phil. programme and Rs. 2500 per month for Ph.D. Application form can be obtained free of charge from office of IAFIE Kerala Chapter, P.B. No. 833, Calicut 4.

IAFIE Workshop: The Kerala Chapter of IAFIE is now conducting bimonthly workshops for its members and associates to study the subject matter of Islamic economics. The subjects discussed are Economic Development an Alternative approach, Management of Zakah in a Secular Society, Economic Growth in Islamic Economic System. Around 25 Economists are participating in each programme.

IDB Prize Shared by two Muslim Economists

The Islamic Development Bank Prize for year 2001 (1421H) in Islamic Economics was awarded jointly to Dr. M. Hasanuzzaman, a Pakistani economist and Dr. Monzer Kahf, an American economist. The Prize is awarded on the recommendation of an international selection committee, which is constituted of experts and scholars from outside the IDB.

Fifth International Conference on Islamic Economics and Finance

Revised Dates and Deadlines for:

Theme:

Sustainable Development and Islamic Finance in Muslim Countries

Venue: University of Bahrain, Bahrain

Dates: **January 6-8, 2003**

Deadlines:

Submission of Outline – December 30, 2001

Acceptance of Outlines- January 15, 2002

Submission of Papers – July 30, 2002

Comments on the Papers- September 15, 2002

Submission of Final Papers- October 30, 2002

Notes of Acceptance – November 30, 2002

(Note: For details see the previous issue of the *Bulletin*, July-August. 2001.)

Next Shah Wali Allah Award in Islamic Economics

New Delhi:

The Shah Wali Allah Prize for the year 2002 will be given in the field on Islamic Economics as announced by the Chairman Institute of Objective Studies, Dr. M. Manzoor Alam. The award, established by the institute in year 2000, consist of a citation plus one Lakh Indian rupees, is given to individuals for their outstanding contributions in the field of Islamic learning. The previous two awards have been given to late Maulana Syed Abul Hasan Ali Nadvi in the year 2000 and to Qazi Mujahidul Islam Qasmi in 2001 respectively.

Ph.D. Student enrolled at A.M.U

Aligarh:

Faculty of Commerce, A.M.U., has enrolled a Ph.D. student under the title "Financial Engineering need for Specialised Mutual fund schemes and their Marketing Strategies" This is the first study of its kind in India which would concentrate on the study of ethical mutual funds catering to the requirements of religious minorities in the country specially Muslims. The research would focus on developing Shariah compliance mutual fund schemes by applying advance financial engineering tools. Professor S.M. Waseem would guide research.

New Books And Articles

Book Review

Books:

1. BENDJILALI, Boulem, *An Intra-Trade Econometric Model for OIC Member Countries: A Cross-Country-Analysis* (Research Paper No. 55), Jeddah, Saudi Arabia: Islamic Research and Training Institute, Islamic Development Bank, 2000, 45pp.
2. KHAN, Javed A., (com.), *Social Sciences in Islamic Perspective: A Bibliography Of Contemporary Literature*, New Delhi, India: Institute Of Objective Studies, 2001, pp.300

Articles:

1. AHMAD, A. Rahman Yousri, 'Riba, its Economic Rationale and Implications', *New Horizon* (London), No.109, May-June, 2001, pp.9-14
2. AHMAD, Mehboob, 'Shah Wali Allah's Theory of Economic System and Social Ethics', *Thoughts On Economics* (Dhaka, Bangladesh), Vol.11, No.1&2, Janu
3. KHAN, M. Akram, 'Eliminating Interest from the Economy', *New Horizon* (London), No.109, May-June, 2001, pp.21-30
4. KHAN, M. Ali, 'Globalization of Financial Markets and Islamic Financial Institutions', *Islamic Economic Studies* (Jeddah, Saudi Arabia), Vol.8, No.1, October 2000, pp.19-67.
5. KURAN, Taimur, 'The Discontents of Islamic Economic Morality', *American Economic Review*, Vol.86, 1996, pp.438-442.
6. 'Report on Fourth International Conference on Islamic Economics and Banking, Loughborough, UK', *Islamic Economic Studies* (Jeddah, Saudi Arabia), Vol.8, No.1, October 2000, pp. 171-78.
7. SIDDIQUI, Shahid Hasan, 'Islamic Banking: True Modes of Financing', *New Horizon* (London), No.109, May-June, 2001, pp. 15-20.
8. SIRAGELDIN, Ismail, 'Eliminating of Poverty: Challenges and Islamic Strategies', *Islamic Economic Studies* (Jeddah, Saudi Arabia), Vol.8, No.1, October 2000, pp. 1-16.
9. THOMAS, Richard and MORTIMORE, Mark, '*Ijarah* Leasing, Contract as a Shariah compliant Investment', *New Horizon* (London), No.109, May-June, 2001, pp. 34-37.
10. USMANI, M. Taqi, 'The Adverse Effect of Interest on Society', *New Horizon* (London), No.109, May-June, 2001, pp. 3-9.

Participatory Finance through Investment Banks and Commercial Banks:

By A.L.M. Abdul Gafoor:

Published by: Aptech Publication, Barkenlaan, 75, 9741 JL Groningen, The Netherlands, 1996 pp. 100

The author presents a model of Participatory Financing, which is also the title of the book. His model is developed to test it through Investment Bank and Commercial Bank on account of their different characteristics.

The author develops his model with the assumption that all wealth is kept in the form of cash, which is either used for immediate consumption or left for future consumption (saving). A person having unused money can go for three options depending upon the purpose or objective of the holder; keeping it safe, lending it or investing it. A person whose objective is to keep his money safe and readily available for any of his future requirements will go for the first option; keeping with himself, with some body he relies or with the current account of the bank. Second option would be enjoyed by the person whose objective is to keep his money safe and also to earn some profit or interest on it by lending it to some reliable person or keeping it in the saving account of the bank. A person whose aim is to earn profit would use third option, he will invest the money in some business or project or in the banks as fixed deposit. Author argues all the options since depend upon the objective would be dealt accordingly, first would invoke Zakah, second is subject to Riba and therefore completely prohibited and the third would come under the *Shariah* rule of commerce and *Riba* as well.

All the three options with their economic implications are discussed in detail by the author in the following chapters and subsequently a model is developed where a person can fulfill his objectives by simultaneously earning some profit or income without contravening any *Shariah* rule. As the book proceeds some complex issues like credit creation and inflation has also been discussed. The novel idea of this book is the attempt to use the credit creation power of the commercial banks to the national and community development. The mathematical relationships among different variables are derived and presented in Appendix A followed by Appendix B which describes Banking terms and processes.

The book also covers the financing projects through Participatory Financing by commercial banks and its importance and relevance to Muslims especially in developing countries.

Shariq Nisar

Invitation for Nomination

The Islamic Development Bank (IDB) has established a Prize to be awarded on an annual basis alternating between Islamic Economics and Islamic Banking. The Prize consists of the following:

- a) A Citation, carrying the Bank's emblem
- b) A cash award of 30,000 Islamic Dinar (approx. US \$ 40,000)

The IDB Prize for the Year 2002 (1422H) is in the area of Islamic Banking.

Invitation for Nomination:

The Islamic Development invite individuals, universities, academic, financial and Islamic institutions throughout the world to nominate whoever they deem eligible to awarded the IDB Prize for the year 2002 (1422H) in the field of **Islamic Banking**.

Organizations or individuals may nominate Candidates.

1. Self-nomination and posthumous nominations are not acceptable.
2. The nomination letter, written either in Arabic, English or French, should give full justification for the nomination.
3. Last date for receiving nomination is October 31, 2001, (Wednesday, 15 Sha'baan 1422).
4. Nomination should be mailed to the address given below:

Chairman:

IDB Prize Preparatory Committee, IRTI

P.O. Box 9201, Jeddah 21413

Kingdom of Saudi Arabia

Tel: 966-2-6361400/6466129, Fax: 63789271

E-mail: IDB-Prize@isdb.org.sa

Call for Paper

The Department of Economics and Management Science International Islamic University Malaysia is organising a Special session at the Western Economic Association International's (WEAI) 77th Annual Conference during June 29- July 3, 2002 at the Westin Seattle, U.S.A under the Title "Topics in Islamic Economics"

Contributions are invited for the session. The papers may be theoretical in orientation or may deal with policy issues of interest to Muslim countries.

Dates to be Observed:

Submission of detail out line by October 31, 2001

Submission of Complete Paper by March 31, 2002

Address for Communication:

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The Second Book File of Islamic Economics Bulletin

On completion of 10 years of this Bulletin, the Association is bringing a book file of its past issues from volume 1 to volume 10 in limited numbers, for the benefit of scholars and record of libraries. The volume is appended with an Index enhancing its usefulness. The collection of ten volumes H.B. cost Rs. 500 (Overseas US\$ 100) and P.P. Rs. 200 (Overseas US\$ 50) inclusive of packaging and postal charges. A few copies of volume 1 to 5 are also available at discounted price; interested Scholars and Libraries may contact the Editor in this regard.

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