

Assignment # 1

Solution:

Islamic Banking:

Islamic banking is commonly defined as a form of banking which operates without the norm of interest. A critical review of the literature on Islamic banking and an evaluation of the so-called Islamic banks operating globally lead to a startling but significant revelation: Islamic banking both in theory and practice is nothing more than a mythology. This mythology has socio economic implications which cannot be ignored at any cost.

By its definition, structure and functions, a bank cannot exist without interest. These two concepts are too intertwined to be separated. Because of the inseparability between a bank and the interest rate, it can be concluded that Islamic banking is a mythical and a contradictory concept. If the objective is to abolish interest, the entire banking system will have to be scrapped altogether. In other words, if the foundation of the banking superstructure, namely the norm of interest has to be eliminated, the entire superstructure would have to be dismantled.

The **first and the primary myth** which has gained common currency throughout the Islamic world is based on gross misinterpretation of the Quranic verses on Riba, which have led to the conclusion that Riba prohibited in the Quran and the bank interest are identical and as such interest must be abolished from all tiers of the economy including banking.

The **second myth** around which the concepts of Islamic economy are developed, points out that interest is the basic cause of the ills from which modern economy suffers such as unemployment, inflation, depression, income inequalities, poverty etc. Remove the norm of interest and economic system would be fully purified (Islamised) with no unemployment, no inflation, and no income inequalities.

The **third myth** is in the form of the popular claim that there are as many as 200 banking units of banking companies which operate around the globe without interest and that these banks represent alternative models to interest-based banking. Even the western secular banking companies are now opening branches of Islamic banks or Islamic windows as these companies are convinced of the superiority of Islamic banking over the interest-based banking.

The **fourth myth** is that the mode of profit-loss-sharing (PLS) is truly an Islamic mechanism and as such it can best serve as the basis of Islamic banking.

The **fifth myth** is that J.M. Keynes as one of the greatest economist of the twentieth century, in his numerous writings, has propounded and approved the structure of an economy which is free from interest. The interpretations forbidding interest are thus supported by the worldly economist such as J.M. Keynes.

The **sixth myth** stipulates that Islamic banking will become a reality once the Islamic economic system is established in its totality.

The mythology of Islamic banking is being propagated as a new gospel throughout the Islamic world. Scholars in Pakistan, Indonesia, Malaysia, Bangladesh, Sudan, Saudi Arabia etc. have invested immense energies on themes of Islamic banking, Islamic economics etc. Their innovative research bizarre interpretations and newly defined models have only led them to camouflage the norm of interest under esoteric nomenclature such as mark up, rates of return, profit ratio etc.

The interest remains the foundation of Islamic banking institutions. At the same time the Muslim world continues to suffer from a collective self-conceit that the banking system has been baptized the Islamic way. However, in the real world scenario, if interest is abolished through an ordinance or an administrative fait, the Muslim world would face an unparalleled predicament of economic disorder and disaster.

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