1. Why Islamic finance?

1.1 INTRODUCTION

This chapter is about the motives for Muslims to advocate the use of financial instruments that obey specific Islamic requirements. The movement for an Islamic economy and an Islamic financial system in particular started in the second half of the nineteenth century with a new Islamic awakening but took a different turn after the First World War. A new impetus was given with the rise in oil wealth in a number of predominantly Muslim countries after the 1973–74 oil crisis and the success of Malaysia as a fast grower; both of which may have contributed to a new self-confidence that made it possible for Muslim governments and firms to develop new financial instruments, often in close cooperation with Western firms and without the feelings of resentment harboured by reformers of the 1930s and 1940s. The history of the movement towards Islamic finance, and Islamic economics in general, is outlined and the chapter concludes by highlighting the diversity of views among Muslims on the desirability of the direction it has taken.

1.2 THE ORIGINS

Right from the early days of Islam, Islamic scholars have discussed the ways to apply Islamic principles and prescriptions to the economy. However, from about the time of the Renaissance, economic topics, and indeed scholarly activities in general, came to be dominated by Europe and it was not before the second half of the nineteenth century that an Islamic awakening took place (Islahi 2015). In the nineteenth century the Islamic world was rudely confronted with the fact that European countries were far ahead in science, education, medicine, transport, military organization, industry and communication and that the gap was widening rapidly. Strongmen such as Muhammad Ali Pasha, who ruled Egypt as Ottoman viceroy from 1805 to 1849, and Mahmud II, who reigned as the Ottoman sultan from 1808 to 1839, enforced modernization, ruthlessly suppressing all opposition (de Bellaigue 2018). Islam played no role in the achievements of nineteenth-century progress and Europeans, joined by intellectuals from the Islamic world, saw it as an obscurantist remnant. There were, however, Muslims who agreed that Islam had become fossilized but preached a much more liberal form of Islam than what had become the mainstream. One man who stood out was Jamal al-Din al-Afghani (1839–97). As European countries became more openly imperialist as the nineteenth century wore on – Tunisia for instance became a French colony in 1881 and Britain took control of Egypt in 1882 – aversion to European influence grew. Building on this aversion al-Afghani inspired a pan-Islamist movement that united the Muslim world against European imperialism. This was possible thanks to much better communication as travel became ever easier and the printing press at last became common in the Islamic world, offering a propagation mechanism for revolutionary ideas as it had done more than three centuries earlier in Western Europe for Martin Luther's assaults on the abuses of the Roman Catholic Church.[1] In 1899 al-Afghani's pupil Muhammad Abduh (1849–1905) was named Grand Mufti of Egypt, the highest authority on Islamic jurisprudence and the head of Egypt's religious law courts, by the khedive (Ottoman viceroy).[2] Abduh propagated an enlightened Islam that no longer denied a place for human reasoning. He even maintained that the Quran, the holy scripture of Islam, could be interpreted differently according to time and place and that it might contain errors, introduced by humans. This was, and is, anathema to mainstream Muslims and met with fierce opposition. Instrumental in spreading his ideas was Muhammad Rashid Rida (1865–1935), who published a journal, *al-Manar* (The Beacon), to which Abduh contributed legal rulings and reformist essays (de Bellaigue 2018, chapter 5; Hashmi 2004a, 2004c). The First World War and the resulting break-up of the Ottoman empire put an end to pan-Islamism and liberal reformist currents gave way to movements that attempted to make an alleged 'pure' Islam, not tainted by liberal secular notions, fit for governing life in the twentieth century. An important role was played by the Muslim Brotherhood in Egypt, founded in 1928 by Hassan al-Banna (1906–49). Similar movements sprang up in other parts of the world with a large Muslim population. Muslim intellectuals in British India and, after the 1947 Partition, in Pakistan distinguished themselves specifically by developing ideas on how to organize the economy of an Islamic society. A pioneering role was played by Maulana or Mawlana Sayyid Abu'l-A'la Maududi (1903–79) (see Box 1.1).[3] Maududi (also spelled Mawdudi or Maudoodi) wrote, as editor of a journal he founded in 1932 for Muslims in British India:

> The plan of action I had in mind was that I should first break the hold which Western culture and ideas had come to acquire over the Muslim intelligentsia, and to instil in them the fact that Islam has a code of life of its own, its own culture, its own political and economic systems and a philosophy and an educational system which are all superior to anything that Western civilization could offer. I wanted to rid them of the wrong notion that they needed to borrow from others in the matter of culture and civilization. (Quoted in Slomp 2003, p. 240)

The economic system thus figured explicitly in his plans for an Islamic revival (Kuran 2004, chapter 4). After delivering an address on the subject in 1941 (Maududi 1941), he went into more detail in several works on the principles that should govern an Islamic state (Maududi 1963, 1999). Others in India and later in Pakistan followed in his footsteps, in particular Anwar Iqbal Qureshi in 1946 (Qureshi 1946), Naiem Siddiqhi in 1948 and Mahmud Ahmad in 1952 (see Gafoor 1996, p. 37; Mahmud Ahmad 1999). They not only expounded their thoughts on the Islamic society but also attacked Western economic thought, in particular impugning interest theories and justifications for asking and paying interest (extensively in Qureshi 1946, chapter 1). Mahmud Ahmad even states that intellectual bankruptcy is the hallmark of every theory of interest (1999, p. 30).

BOX 1.1 MAULANA MAUDUDI

Maududi was born in 1903 in Aurangabad, in the Muslim state of Hyderabad in the Deccan. His family belonged to the upper crust of Indian Muslims and claimed to descend from the relatives of the Prophet. His father was strongly under the influence of a movement that, in reaction to the European values that had come to India with the British, strove to purify Islam from syncretistic practices and revive the strength of the Muslim community. Maududi himself, as editor-in-chief of a variety of Muslim journals, was opposed to Muhammad Ali Jinnah's All-India Muslim League and its ideal to found an independent Muslim state, because Islam pretends to express universal values and should not be used as an ideological foundation for a nation state. He would rather bolster the Islamic community in order to prepare for life in an independent India dominated by Hindus often hostile to the Muslim minority (Kuran 2006, pp. 83–4). Some people suspect a personal antipathy vis-à-vis Jinnah (Mazari 1998). Nonetheless, after the Partition he moved to Lahore and propagated the view that the moral and ethical principles of Islam can only be put into practice if the state imposes them.

In 1941 Maududi founded a movement, the *Jamaat-e-Islami* (Islamic Society or Party), that evolved into a political party. This party, which is still active in Pakistan and its former eastern part, Bangladesh, is based on the idea that all present-day problems can be solved with the help of the Quran and the *sunna* (from *sunnat al-nabi* or practices of the Prophet, see Chapter 2), as transmitted in the *ahadith*, or traditions. Maududi combined a strictly literal interpretation of the Quran with modern political terminology in order to show the relevance of the Quran and the sunna for twentieth-century society. Maududi's ideal society was the supposedly pure one under the

Prophet and his four successors before the Umayyad dynasty took over, Abu Bakr, Umar, Uthman and the Prophet's cousin and son-in-law Ali, collectively known as the *Rightly Guided Caliphs*.[4]

It was all well and good to have a Muslim state, or a state for Muslims, but that was still far removed from an Islamic state. What Maududi was after was a fundamentalist theocracy, which he dubbed a 'theo-democracy', a form of government that should not only be forced upon Pakistan or the Muslim world, but on the whole human race. The Muslim population should freely choose a leader, but with the choice restricted to people, or rather males, with an impeccable sunna-respecting track record. He only differed from traditionalist *ulama*, or religious scholars, in that he still left a small place for the modernization of Islamic law, as he realized that traditional Islamic law does not have the answer to each and every problem confronting present-day Muslims. His views did not go down too well with the modernists in the Pakistani government and the army, nor were they enamoured of the well-oiled Jamaat-e-Islami machinery that spread his message.

Maududi was imprisoned several times and in 1953 he was even sentenced to death by a court martial, but under public pressure the sentence was commuted to two years' imprisonment. He died in 1979 in New York, where he had gone for heart surgery. In the same year his follower Kurshid Ahmad became a cabinet minister (1979–80) under President Muhammad Zia ul-Haq (1977–88), who declared Pakistan an Islamic state and began to enforce sharia law (for more information on Maududi see Adams 1966; Aziz Ahmad 1967; Otto 2001; Slomp 2003).

Maududi, like other contemporary reformists, held strong views on the way society should be run. He advocated strict gender separation and was firmly in favour of the death sentence for apostates, even if prominent Muslim scholars argue that in the early times of Islam the death sentence was only issued for soldiers that converted to Judaism or Christianity in order to evade military service (Slomp 2002). Muslims should, in Maududi's eyes, not spend money on leisure and cultural activities. They should not only stay away from such things as wine and gambling, but also from 'music and dances and other means of self-indulgence' and are furthermore forbidden to wear silken dresses, to use golden ornaments and jewels (except in the case of women, parentheses Maududi's), or to decorate their house with pictures and jewels (Maududi 1999, p. 31).

The political and economic system of the West was capitalism. Communism, however, was deemed no better than capitalism as, to quote Maududi, Islam does not approve of any political or economic organization that seeks to submerge the individual within the society and stultify the flowering of his personality (Maududi 1999, p. 5). Nationalization of all means of production would lead to social regimentation, read: dictatorship (pp. 5, 27). Fascism and national-socialism are as bad as communism in this respect (pp. 28–9, this is still from his 1941 address). On the other hand, Islam also abhors capitalism, first of all in its laissez faire form, as that would open the way for individuals to pursue their own ends at the cost of society as a whole. Capitalism is associated, in Maududi's view, with the French revolution, which propagated individual liberty, liberalism, capitalism and the system of secular democracy (p. 107). It is probably fair to say that 'French revolution' here stands for 'enlightenment'. A fundamental flaw of both capitalism and communism in his view is their lack of a moral foundation, including neglect of the family (Chapra 2004).[5]

Scholars from the Middle East meanwhile continued to contribute to the discussion, though they were less specific on the design of the economy. Muhammad Baqir al-Sadr (1935–80), a Shiite cleric from Iraq who was later executed by Saddam Hussein, wrote a voluminous book on economics, *Iqtisaduna* (*Our Economics*, 1968) that was to a large extent a study of comparative economics, explaining what distinguishes an Islamic economy from Western capitalism and, much more extensively, from communism. He was also critical of both capitalism and communism because they lack the ethical principles that characterize Islam, and it is ethics that should lie at the basis of an Islamic society where social justice should prevail (Machlis 2018). He later wrote a book on Islamic finance that suffered from his lack of knowledge of contemporary monetary theory (Wilson 1998; El-Ashker and Wilson 2006, pp. 392–9). In Egypt, Sayyid Qutb (1906–66), a prominent exponent of the Muslim Brotherhood who preached violence action, first of all against leaders of Muslim countries who were seen to betray Islam, and was executed by the Nasser regime in Egypt, wrote in the same vein, emphasizing the idea of social justice in Islam (Damir-Geilsdorf 2018, Qutb 2000). His first major publication on this subject appeared in 1949 (Hashmi 2004b).

Islam encompasses a Muslim's whole life. Islamic family law already applied for the Muslim population in the Ottoman Empire and many of the Asian countries under Western rule. Muslims in varying degrees have always followed injunctions about food. Clothing is another area where Muslims have a tradition of distinguishing themselves from others, especially in women's clothing. It was only natural that Muslim reformists developed ideas about Islamizing society completely in Muslim-majority countries, including the economy. The financial industry in particular was a field where prevalent practices were felt to be grossly at variance with Islamic principles and ideas on Islamic alternatives started to become more detailed in the 1940s. An Islamic financial sector got off the ground in the 1970s, with firms having affiliations in various countries and cooperating in international organizations. This has been followed by an increasingly internationally active Islamic ‘modest clothing’ industry for women, a specialized Islamic travel industry, an Islamic pharmaceuticals industry, an Islamic cosmetics industry and an Islamic media and recreation industry (see Thomson Reuters 2017). In this way the post-First World War reformers’ ideal of an Islamic economy is more and more taking shape, though they would perhaps not approve of the direction Islamic finance has taken. It is often seen as conventional banking made more complicated, not without some justification, as Chapters 4 and 5 will make clear.

1.3 DIGRESSION: THE ISLAMIZATION OF THE FINANCIAL SYSTEM IN PAKISTAN – A CHEQUERED HISTORY

The ideas about what an Islamic economy should look like took some time to develop. For the founding fathers in British India and later Pakistan it was a process of trial and error; they did not start out with a detailed blueprint. Harsh realities also impeded a fast adoption of the principles of Islamic economics. Anwar Iqbal Qureshi notes that he, as economic adviser to the Government of Pakistan after Partition, actively tried to introduce interest-free banking, but did not pull it off because of practical difficulties (Qureshi 1991, p. 199). He fails to note, however, that his ideas also suffered from not being completely coherent. On one page he states that banks should accept deposits and lend money without paying and asking interest, with the state paying the costs of running the banking mechanism. This is because finance can be seen as an essential service, like hospitals and public utilities. Two pages further on, he advocates partnerships between banks and their clients which would yield profits, apparently without any need for the state to step in (Qureshi 1946, pp. 156–9). A government agency should furthermore regulate a tax on bank deposits, such that new loans stay roughly in line with loan repayments. The tax could be used for insurance, among other things, either on an individualistic or a collective basis (Qureshi 1946, chapter 4).

An important step in the process of Islamization was that President Muhammad Zia ul-Haq, who had seized power in 1977, in February 1979 decided that interest-based transactions were to be phased out. Banks were ordered to offer interest-free alternatives to conventional savings accounts and to completely switch to interest-free banking within five years. Zia started in the same year by making three financial institutions interest free. Even if some specialized credit institutions were quick to shift to interest-free financial products, in the commercial banking field the process proved time-consuming and the government itself did not refrain from fixed-interest borrowing activities. Maududi’s follower Khurshid Ahmad held a cabinet post under Zia ul-Haq.

In the mid-1980s the Islamization of the financial sector ran out of steam, but the Federal Sharia Court of Pakistan became active with a verdict given in December 1991 under which a number of laws based on *riba* or interest were declared unlawful. The governments that followed upon Zia's death in a suspicious plane crash in 1988 did all they could to stymie the efforts of the court and its supporters.[6] The Federal Sharia Court had ordered the government to eliminate interest from the economy by 30 July 2002. Appeals by Pakistani banks and other financial institutions against this judgement filed in the Sharia Appellate Bench of the Supreme Court were joined by the government, which claimed that the initial ruling was flawed because the constitution placed a duty upon the federal government, and not on the Federal Sharia Court or the Sharia Appellate Bench, to abolish riba 'as soon as possible', and these bodies therefore had no right to set a deadline (Rammal and Parker 2013). The government also argued that interest-free banking would create financial anarchy in the country. On 24 June 2002 the Supreme Court, a few weeks before its earlier deadline, duly reviewed the earlier judgement and remanded the case back to the Federal Sharia Court for a fresh decision. The gentlemen were bid to take their time: 'we are of the considered view that the issues involved in these cases require to be redetermined after thorough and elaborate research and comparative study of the financial systems which are prevalent in the contemporary Muslim countries of the world' (Supreme Court of Pakistan 2003, pp. 35–8).[7]

1.4 ISLAM AGAINST THE REST OF THE WORLD?

Islamic finance was born out of ideals to Islamize Muslim societies and even to establish Islamic states based on Islamic religious law, the sharia. This *political Islam*, propagated by such movements as the Muslim Brotherhood and the Jamaat-e-Islami, is the antithesis of pluralistic liberal-democratic ideology, which draws on notions of individual liberty as developed by John Stuart Mill, among others (Mill 1974). In the eyes of Sayyid Qutb, inspired by Maududi, people have to choose between 'God's absolute rule' and 'total pagan ignorance' (*jahiliyyah*). People who are deemed not to follow 'God's absolute rule' have to be struck by *takfir*, that is, they are declared unbelievers, *kuffar* (sing. *kafir*). Muslims that become unbelievers are guilty of apostasy and deserve the death penalty (Krämer 2004).

The Quran says that if a believer kills another believer intentionally 'his punishment is hell to live therein forever' (Quran 4:92–3), and declaring fellow Muslims unbelievers is thus required to free the way for attempts on their life. Through takfir, killing Muslim rulers that stand in the way of the establishment of a fully Islamized society can be justified. The Muslim Brotherhood and similar movements attacked, after their countries gained independence, the ruling classes in their own societies, who they felt were guilty of social injustice and oppression. A return to what they preached to be the true Islamic way of life was seen as necessary to end these evils (Hoebink 2008). As a reaction, some argue, the ruling classes embraced the cause of Islamic finance in order to legitimize their rule and evade takfir (Barenberg 2004–2005). Timur Kuran (2006, pp. xii, 73), for instance, suggests that in countries where the propagandists of political Islam or Islamists do not eschew violence, such as Pakistan, politicians and intellectuals have supported efforts to introduce Islamic economic institutions, including Islamic banks, not out of conviction, but for fear of being branded insufficiently Islamic. In countries such as Egypt and Turkey, where critics have been assassinated, intellectuals hesitate to speak out openly against the economic ideas of Islamists. This trend seems to have been reversed in Egypt, after the Muslim Brotherhood government under Mohamed Morsi that came to power after the 2011 revolution was overthrown in 2013 by the Egyptian army. In Turkey, by contrast, the AKP governments in power since 2002 have under Recep Tayyip Erdogan increasingly been active in promoting Islamic finance.

Advocates of a distinct Islamic way of life and Islamic institutions, though, come in all shapes and sizes. Maulana Maududi and Sayyid Qutb hold no monopoly. Apparently, there is more than one way to read the Holy Scriptures. Against the voices advocating an Islamic economic system totally different from and even isolated from the non-Muslim rest of the world, there are people such as the leading Muslim economist Mohammad Nejatullah Siddiqi, who takes his brethren and sisters to task for what he sees as a 'hostile-West syndrome', which puts the blame for all the Muslim countries' woes upon the pernicious influence of the West (Siddiqi 1994). He deems it futile to try and develop an Islamic economic system that is totally different from the West. To him, Islamic finance and Islamic economics are more a question of ethics and morality. He sees these as a step forward in the development of more equitable economic and financial arrangements which the whole world needs, and in which Muslim individuals and countries should participate (Siddiqi 2002). This shows that embracing Islamic finance can follow without any antagonism to non-Muslims. Many Muslims who take their religion seriously are eager to obey what they see as the precepts of the Quran and the sunna as much as possible, even if they are not inclined to impose their views on those who do not share their convictions or to shut themselves off from the non-Muslim world. The ideas regarding Islamic economics may have been developed as a reaction to colonialism and capitalist and communist economic systems, and it may be true that Islamization of the financial sector in Iran was an instrument in the hands of the revolutionaries who had overthrown the Shah, but it still seems to be the case that these ideas can be adopted without necessarily accepting, at the same time, the political ideas of Maududi or Sayyid Qutb. Many Muslims have no compunction towards making use of the services of Islamic windows of American and European banks in predominantly Muslim countries. Western banks such as HSBC, Citigroup and Deutsche Bank have been at the forefront of developing Islamic financial instruments. Moreover, the International Monetary Fund and the World Bank have built up cordial relationships with the Islamic financial world and the Institute of Islamic Banking and Insurance, set up in London in 1991, calls it a good omen that major international financial organizations are involved in Islamic finance and that there is an active interaction between those organizations and Islamic bodies. Others find that it is only to be applauded if non-Muslim institutions accept sharia conditions and offer sharia-compliant products (Yaquby 2000). Such an attitude may be fed by satisfaction about a growing role of Islam in global affairs.

It seems that Islamic finance may fulfil different roles in different circumstances. In countries where it is the only form of finance allowed, it is clearly part of an Islamization drive that leaves their citizens little choice. If, however, Islamic finance is offered alongside conventional finance, the range of products available to the public is widened. Greater choice is in principle a good thing, provided there are no forces working behind the scenes towards completely replacing conventional finance with Islamic finance in the end. As so often in the Muslim world (and anywhere else), opinions differ widely. One observer, the Turkish columnist Uğur Mumca, saw Islamic banking as part of, in the words of Timur Kuran (2006, p. 55) ‘a sinister ploy to advance Islamism, isolate Muslims from global civilization, and force Muslim nations into a despotic political union established on medieval principles’. Mumca was murdered in 1993, and there are strong indications that this was on orders from Iran. Similarly, a Pakistani writer, Izzud-Din Pal, sees the whole drive to introduce Islamic finance and an Islamic economy as a plot by traditionalist religious scholars, the ulama, and their political supporters to revive the institutional framework of the Middle Ages (Pal 1999, p. 143). He deplores the fact that there is little place for ‘Islamic modernism which embraces those Muslims who believe that the Qur’anic verses should be examined in the context of the social framework in which they were revealed and their message reconstructed in the light of modern times’ (p. ix). Muhammad Abduh’s legacy is still alive. Pal does not hesitate to label the brand of Islam which dominates the mainstream literature in Pakistan as pharisaic (p. xx). In the same vein, Mahmoud El-Gamal calls the Islamic norms observed by the Islamic finance industry those of a hopelessly outdated, medieval jurisprudence that also contributes to an unfortunate separatist Islamic identity fanning feelings of superiority (El-Gamal 2007a).[8]

Generally, the world of Islamic finance itself gives the impression that the interest in earning money in a sharia-compliant way is more prevalent than any antagonism to others. Still, some theorists of an Islamic economy and some politicians may have stronger Islamist convictions and aims than the practitioners while the development of internationally active Islamic 'modest clothing' and other specifically Islamic industries mentioned above, alongside the Islamic finance industry, arguably points to the growth of specific Islamic enclaves both in Muslim-majority countries and in countries where Muslims are a minority, possibly exerting pressure on fellow Muslims to conform to their specific lifestyle. Different groups have different agendas.

1.5 CONCLUSIONS

Islamic finance offers an alternative to conventional finance. As long as it operates alongside conventional finance it widens the choice available to users. Another positive point is that it may help part of the Muslim population in a jurisdiction to live according to what they believe are the tenets of their faith. It may also contribute to a feeling on their side of being taken seriously. However, Islamic finance may be used as an instrument by politicians and clerics to Islamize their society, which, from an economic point of view, will ultimately restrict the freedom of choice. In a country where Muslims are a minority, it may be used as an instrument to separate Muslims to a considerable extent from their fellow citizens and exert pressure on them to conform, which, again, restricts their freedom of choice.

NOTES

1. The Ottoman political and religious leaders were horrified when they saw how Luther's subversive ideas went viral thanks to the printing press and took care not to let anything similar happen in their empire (Rubin 2017, chapter 6).
2. A mufti is an Islamic lawyer who is authorized to issue a fatwa or legal opinion, see Chapter 2, end of Section 2.2.
3. 'Maulana' or 'mawlana', literally 'our master', is an honorific title for religious Muslim scholars in South Asia.
4. The four Rightly Guided Caliphs were the successors of the Prophet as both spiritual and political-military rulers of the Islamic world after his death. In the hereditary caliphates that followed the caliphs were its political-military ruler. The principal caliphates were the Umayyad caliphate, founded in 661, and the Abbasid caliphate, which in 750 succeeded the Umayyad caliphate. The Abbasid caliphate ended in 1258 when the Mongols sacked Baghdad. Later, the sultans of the Ottomans assumed the title of caliph. This happened in 1517 when they conquered Egypt and with this gained control of the holy cities of Mecca ad Medina. Turkey's ruler, Kemal Atatürk, abolished the sultanate in 1922 and the end of the caliphate followed in 1924.
5. M. Umer Chapra is a research adviser at the Islamic Research and Training Institute of the Islamic Development Bank, Jeddah. Earlier he worked for several decades at the Saudi Arabian Monetary Agency and at American and Pakistani universities. He is one of the foremost writers on Islamic economics.

6. See Maududi's disciple Khurshid Ahmad (n.d., probably 1997) for an account from the point of view of Maulana Maududi's Jamaat-e-Islami Party.
7. See Mehmood (2002) on the history of the attempts to Islamize Pakistan's economy.
8. Mahmoud Amin El-Gamal is an Egyptian-born United States citizen who is Professor of Economics and Statistics at Rice University, Houston, Texas. He is a prolific writer on Islamic finance.