

Socio-Ethical Dimensions of Islamic Economy and Issue of Modern Interest and RIBA: An Analysis in the Light of the Economy of the Muslim World

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Abstract

This article analyzes the issue of *riba* and capitalist banking interest in the light of the ethics of Islamic economics. It provides that many of the Muslim countries are Under Developing and dependent upon interest-based foreign aid for their survival. In this context, it seems impossible to establish an economy on the basis of zero rate-interest. In the light of the historical and contextual development of *riba* and capitalist interest it reveals that both have a different background. The former was a way of exploitation of the poor segment of society while the later was legalized to help poor segment of the society, to control the fluctuation of monetary value, to ensure capital growth and above all has become an unavoidable element of contemporary economic transactions. Hence, this article suggests that the contemporary mode of capitalist interest should be declared permissible by way of well recognized interpretive principles of necessity which means that necessity makes a prohibited thing permissible (*al-darurat tubihu al-mahzurat*) and public interest.

Keywords: Economic Ethics, Riba, history, interest-based economy, conclusions and recommendations

Introduction

Economics is a science to study human behavior as a relationship between ends and scarce means which have alternative ends.

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An economic system may be defined as a set of rules, an ideology to justify them in the individual's conscience which makes him strive to carry them out (Robinson,1962, p.13).

At present the economic policy of a state is set out by the government in the light of labor-market, gross national product and fixing of interest-rate under the influence of the concerned political chauvinism, policies of the World Bank and International Monetary Fund etc. The economic development of a country ensures the fulfillment of basic needs of the people, fair distribution of wealth and resources, equal opportunity to develop, access to education and health facilities and protection of the lives and properties of the people etc (Hobson,1929, p.34). To ensure socio-economic development of the Muslim society, the Qur'an provides a complete guideline regarding past economic behavior, the present actual economy and expected future realities and urges exploitation-free economy. To enable him to perform his duties well, man has been given intellect and free will to enact and to maintain law and order in a society in the light of the fundamental principles of the Qur'an and the Sunnah (pbuh). For a comprehensive study of Islamic ethics of economy and its objectives, it is necessary to have some knowhow of the prevailing system of economy and economic institutions of the developed Western World.

1. Ethical Philosophy of Economics

A sound system of economics is based on some general ethical principles to proceed from generality to the speciality in order to ensure scientific objectivity as well as clarity of thought (Hobson,p.35).

Economics' ethics in the words of Thomas & Edward (1995) may be defined in the meaning of a code encompasses all aspects of business from issues of pricing to marketing, production method and employment practices etc (p.12). In historical perspective, Greek philosophers were the first who studied rules of the economics in a limited sense in perspective of house-hold management as Josef (1954) pointed out that economics as an independent branch of learning was not touched upon by any philosophers until the 18th century and nobody dealt with an economic topic for its own sake (p.23). Aristotle (384-322 B.C.) and Plato (423-347 B.C.) however, discussed ethics of economics and the concept of private property, communism and *usury* (riba) in the light of the general philosophy of the state and society (Aristotle, 1965, p.34).

Ethical economics as an independent science is a recent development in the Western philosophy and J. A. Hobson (1921,p.12) was the first economist who influenced by the Christian socialist movement and wrote about the relationship between economics and ethics and attempted to derive a human standard of value and declared it preferable to a monetary value.

Among the contemporary economists who studied economics and ethics are Daniel Hausmann and Michael McPherson (1993) wrote almost 350 books and articles concerned with the interaction between economics and ethics (Vol.31,p.671).

So far as concerned the religious impact over economic ethics, almost all religion of the world focus on the building of strong ethical prospect of human life including economic dimension as Jacob (1989) stated that over 3000 years Jew's history provided a rich tradition of spiritual thinking and ethical rules in all aspects of life including economy and in the same manners, Torah the Holy Book provides explicit guidance how to conduct business with gentiles and condemn inequalities in the economy (Pp.8-18). Each society has its ethical code of business which reflects from its overall behavior. For instance, in a secular society business ethics are seen as input into professional and managerial decision making while a society running under the umbrella of a religion is seriously affected by its religious beliefs and restrictions. Honesty, justice, and equilibrium in economic transactions and a concern for the dignity of the poor are hallmarks of all the religions of the world (Rodney,1997,pp.13-15). In the history of socialist economy, Karl Marks was the first who pointed out (during the 19th century), the specificity of economic laws to the particular economic regime and who declared that no economics regime could be understood without reference to the social structure in which it was implanted (Raymond, 1968, p.231).

In the same manners, Islamic legal system consists of certain ethical principles of economy such as knowledge, equilibrium, unity, freedom of expression, mutual consent, liability, efficiency, growth, employment and industrialization etc (Siddiqi, p.58). The system of economy must be based on the principle of equilibrium to maintain balance among all the aspects of the economy, i. e., Production, distribution and consumption (Khurshid Ahmad, 1980, p.120). As economics' activity of a man is dependent upon dynamic principle of cultural and ethical dimensions of a particular society, so, is the case of Islamic economy.

It must be in accordance with the ethical and cultural environment of the society keeping in view the principle of utility and public interest. Islamic ethical philosophy of economics has divided the socio-economic utility into a three level hierarchy that are necessities (*daruriyyat*), needs (*Hajat*) and luxuries (*Tahsinat*). (Shatibi,1341 A.H., pp.9-14). Justice (*Adl*) and benevolence (*Ehsan*) however, should be correctly interpreted to face modern economic challenges under the capitalist supremacy (Asghar Ali,1980,pp.13-23).

The Qur'anic provisions regarding economy reveal that Islamic economics has a dual character. It is positive as it studies economic problems as they are. It is normative because it also concerns with the future scope and the consequences of a contemporary problem. In this way, both positive and normative aspects of Islamic economics are so interlinked that they cannot be separated from each other and thus, lead that the economic problems and the issues should be viewed in their totality (Mannan,1986,pp.5-8). To ensure social justice in changed scenario, Islam just provided a frame-work to analyze changed circumstances and changed techniques arising from the system of dynamism and left the detail at the discretion of the believers to decide. This is the reason that the Holy Prophet (PBUH) declared: "If something belongs to the domain of your affairs, then you know all about it. (You are the best judge thereof and have the right and the capacity to deal with it according to the Shari'ah" (Ibn Majah,1988, Vol.2, p.34).

2. Institutions of Economy in Historical Perspective

In the history of economics, certain institutions have been recognized and practiced by all and nations of the world from time immemorial such as trade, partnership, *riba*, rent and *mudarbah*. The fact is that Islam did not introduce any distinctive system of the economy rather recognized those institutions of economy which were not against its objectives such as trade, partnership and *qirad/mudarbah* while those means of earning which were based on the principle of exploitation and resulted in social discrimination were declared prohibited by the divine revelation such as *riba*, gambling, hoarding of wealth etc. To establish a well-fare state, the Holy Prophet (PBUH) interpreted the legal texts of the Qur'an in the light of the changed context. For instance, in addition to the prohibition of *riba al-nasi'ah*, the Prophet (PBUH) prohibited *riba al-Fadl*. (Ali Hasbillah,1976,p.226).

The companions particularly, the *Khulafa-e-Rashdin* adopted the same policy and brought certain changes in the existing institutions of the economy to cope with the changed scenario in the guise of the doctrines of necessity (*darurah*) and public interest. For instance, Hadrat Umar prohibited Muslims from tilling the soil either themselves or by employing others and to have landed properties which in fact, are permissible by the Qur'anic provisions. (Sarakhsi,1376A.H. 1:126). Moreover, he made the wealth of the people under the direct control of the state and introduced a salary system for scholars and judges (Abu Yusuf, n.d.p.89).

As far as concerned the institutions of *riba* (usury), it was existed and practiced over the centuries in Europe, North Africa, and Middle-East in its extreme exploitative form and caused to create a highly unequal relationship between the money lenders, owner of large estates and the borrower, the poor and the suppressed class of society and it was this reason that all the religions condemned usury (*riba*) and prohibited it (Rodney, p.32). For instance, The Jewish Holy Book, Leviticus declared: "If one of your countrymen becomes poor and is unable to support himself . . . help him . . . do not take usury of any kind from him. . . You must not lend him money on usury or sell him food at a profit (25:35-36). Likewise, Christian's view about *riba* (usury) is also based on their religious ethics of the economy and it is stated in the Deuteronomy: "Do not charge your brother usury whether on money or on food or anything else that may earn usury/interest"(19:19). There were circumstances under which Christian could deal with credit such as in the conduct of trade (Leon, 1977, p.16).

Towards the end of the 16th century, the idea of interest based economy introduced in the European societies to condemn feudalism, to ensure capital growth and to provide benefit of the capital to the creditors (Tawner,1977, p.234). John Calvin was the first who presented the idea of interest to reconcile secular and religious opinion and to break through the stagnant intellectual environment of feudal-dominated medieval Europe (Maxime,1974, p.104). This idea was based on the assumption as pointed out by Tawney (1977) that "why should a creditor who may himself be poor, make a loan gratis, in order to put money into the pocket of a wealthy capitalist who uses the advance to corner the wool crop or to speculate on the exchange" (p.185). It was argued that in a society where production is largely of subsistence, borrowing should be resorted to. The borrower should return not only the amount advanced but a certain percentage of the principal as interest.

The rate of the interest on the loan advanced depends on a number of factors such as the degree of the competition between the lender and the borrower, the accessibility to the credit market and the bargaining position of the borrower. The contemporary theory of the interest declares that interest maintains a macro-economic equilibrium which best guarantees growth and full use of all productive resources. It adjusts the supply of the saving to the demand of the credit (Surayni,1968,p.145). Like the western people, the 'Arab had to deal with many types of *riba* and interest which linguistically means to grow or to increase (Ibn Manzur,13 A.H.,Vol.3,p.56).

Among them two extreme types were addressed by the Qur'an and the Sunnah of the Prophet (PBUH): *Riba al-Nasi'ah* where one person had to borrow money from other for a certain period on the understanding that he (debtor) would pay a fixed amount every month until the prescribed period would mature. On maturity, if the debtor still appeared unable to return the loan, the term prolonged and the interest increased and in this way, the excessive amount of interest charged by the debtors resulted in the amount far larger than that of the principal amount and *Riba al-Fadl* which prohibited *riba* in the food upon which life is sustained like gram, rice and other commodities of necessities such as if one measure of wheat is sold for two measures of the same quality and quantity (Al-Jassas,1375 A.H., Vol.2,p.324). In that particular context, God Himself defined *riba* and declared: "O You who believes! Devour not *riba* (usury), doubling and quadrupling, the sum lent (The Qur'an,3:130). God prohibited *riba*, because it was based on the social exploitation and resulted into unbalanced and unjust financial relationships between both segments of the society, the lender and the borrower.

In this way, the Qur'an prohibited *riba* to put an end a transaction caused for exploitation of the debtor and to create a balanced and exploitation-free economic system. The Holy Prophet (PBUH) and the companions took the provisions of the Qur'an against *riba* in the specific meaning of above mentioned transaction of consumption loan which involved intense exploitation. They did not took the provision in its general meaning that might be "interest" rather the early Muslim jurists among the companions had extensive doubts concerning the meaning and the application of the term "*riba*" and thus, avoided to apply the provision to the all type of the interest existed and practiced by the people at that time. It is reported that during the lifetime of the Holy Prophet (PBUH) and the four righteous Caliphs, the Muslims had to borrow money at interest from non-Muslims.

Not only was that but the companions avoided intentionally to interpret or touch upon the issue of *riba* in detail rather wished might the prophet of God himself explained and interpreted the term *riba* (Fazlur Rahman, 1963,p.32). The traditional Muslim jurists however, discussed the issue of *riba al-fadl* and differed regarding its status whether it is prohibited or not? Some of them contended that both types of *riba* are prohibited while others declared prohibited only *riba al-Nasi'a* which has been declared prohibited categorically by the Qur'anic injunctions (Ibn Qayyim, 1976, Vol. 1, p.203).

Even during the Abbasid period credit was made available and interest was to be charged by both Muslims and non-Muslims to fructify capital. Whenever, the Muslim themselves indulged in the financing activities such as in case of money lending or borrowing with other religious communities, they dependent on the institution of interest for the accumulation of capital and to ensure the augmentation of capital delay in repayment of debt and declared harmful to the creditors as it caused to reduce monetary-value of the capital (Ibn Qayyim, Vol.1,p.256). Moreover, the traditional Muslim jurists declared many of the roundabout methods of economy permissible by way of ruses (*hiyal*) even though they had the possibility of *gharar* and involved interest just because they were practiced by the then societies to provide ease to people and to remove difficulty and harm from them in the light of the principle of necessity (Darurah) and public interest (*maslahah mursalah*) which are the most implemented principles of interpretation in Islamic legal system to cope with the changing of time and change needs of the people.³ However, after the 16th century, the European colonialism conquered the Muslim societies and capitalism began to penetrate them and made the Muslim societies dependent economies (Rodenson,p.123).

3. Contemporary Situation of Muslim World's Economy

Looking at the reality and practical situation of the economy of the contemporary Muslim world, the majority of the Muslim states is considered as Under Developed Countries (UDCs) and is trapped by a nasty circle of poverty.

³ For instance, a person A, sells an object to another person B, for rupees 110 to be paid after a year but promptly, buys it back for rupees 100 only, payable immediately. This transaction was declared permissible just by way of *hiyal* to pretend that no interest payment is involved, this however equivalent to a single transaction in which A lends to B rupees 100 for one year at 10% interest. See for detail study, Ibn Qayyim, *I'lam al-Muwaqqi'in*, 4:23; Abdur Rahman. *Majmu al-Fatawa*.29:430.

Many of them are facing problems of absorptive capability restraints and have a scarcity of infrastructure, management, and technical proficiency. (Todaro,2000, p.591). The Muslim countries are facing both "Investment Deficit" and as well as the "Deficit in Balance of Payments" (BOP) and seeks for foreign aid (Johan,2005,pp.612-624). Here, the question arises that if Muslim countries are unable to utilize their own resources without foreign aid or do not have enough resources to finance their needs for the growth of the economy how could they get rid of interest based financing? To answer this question a critical analysis of the issue of *riba* and interest is necessary.

4. Issue of Capitalist Banking Interest and Qur'anic Prohibition of Riba

The most critical issue facing the contemporary Muslim Ummah is the issue of banking-interest prevailing and practiced in the majority of the Muslim countries whose economy is dependent upon foreign aid which is based on the principle of interest without which the Muslim countries cannot have foreign aid or cannot get foreign loans and hence, cannot achieve their economic growth. Foreign aid encompasses all official grants and concessional loans, in currency or in resources (Todaro,p.529). The loans and the credits are generally given on concessionary interest rates and have longer payback periods (Hans, 1962,p.96). It is important to note that the institution of capitalist Banking interest is an innovation developed during the last two hundred years while the issue of *riba* (usury) existed and practiced over the centuries before the dawn of Islam and has been addressed and condemned by all the religions of the world including Islam. The modern interest-rate was introduced as a result of the struggle to eliminate the exploitation of feudalism. It thus, leads that the problem does not lie in the prohibition or permission of *riba* as it is categorically declared prohibited by the Qur'anic provisions. The problem in fact, lies in the correct understanding of the term *riba*, its pros and cons, practice by the primitive societies and above all its consequences and impact over a socio-economic structure of a society.

This problem occurred due to the expansion of the capitalist system of interest, its general acceptance and its effects on the economic policies of the contemporary global world including Muslim world. To resolve the issue of interest and according to the dynamic process of *ijtihad*, it was the duty of the then present Muslim jurists to probe into the case of the interest and the *riba* in the light of the changed context.

For this purpose, the contextual study of the institution of *riba*/usury, its practice by Arab and other societies at that time and its consequences and impact over the economic growth of those particular societies might be taken into consideration. The Muslim scholars might do a scientific study of the problem and its relevant issues such as in what meaning the term *riba* should be taken? In its general meaning which leads simple excess of capital (even though minor) without labor or in its specific meaning (doubling and tripling) which includes only a particular type of exploitation-based interest and results in a grave scarcity of the economic growth and unequal treatment of both segments, the lender and the borrower? The other issue to resolve was to decide what was the exact object behind the prohibition of *riba*?

Whether the objective was to put an end an exploitative economy based on the usurious transactions which lead to an obvious exploitation of the debtor or to discourage commercial and profitable transactions which involve some interest to protect the value of the lending money? (Ashmawi, 1987,pp.71-89). What is object of the modern interest based economy? Should interest charging be permissible to compensate inflation? Would the modern practice of the "interest" is needed to secure the value of the money in the sense that when the loan is paid back the actual value of the principal would not be less than that he had originally lent or not? Above all to consider the contemporary status of the Muslim world as a submissive and underdeveloped world and to weigh up the issue that today majority of the Muslim states is dependent upon foreign aid from the developed countries of the West whose fiscal policies are made in the light of interest-rate, would the stance for prohibition might cause hardship for the people and for the Muslim governments? Under such circumstances, the contemporary Muslim jurist-economist might think how the interest based economy of the contemporary world be justified or modified in the light of the changed context which might not hurt the objective of Shari'ah behind the prohibition of *riba*?

But except few of them, the majority of the contemporary scholars however, took the provisions of the Qur'an and the Sunnah regarding *riba* in limited sense just as a prohibition of fixed rate return or interest and held that the principle of levying interest of the modern times is similar to *riba al-nasi'ah* and hence prohibited and *haram* (Khalilur Rahman,2008,p.118).

This *fatwa* however, was issued without deep understanding of the sciences of the modern economy, its pros and cons, merits and demerits, scientific study of the fiscal policies of the contemporary Muslim states and the system of the global economy in the light of the flexible principles of *ijtihad* (interpretation) such as necessity makes a prohibited thing permissible (*al-darurat tubih al-mahdurat*) and public interest (*maslahah mursalah*). Moreover, they ignored the fact that neither the Prophet (pbuh) nor the companions defined or described the exact meaning and scope of the term *riba* (Al-Ghazali, 1976, Vol.1, p.23). Few of the contemporary Muslim jurists however, opined that the capitalist banking interest is different from *riba* and thus, not prohibited.

Among the jurists who recognized modern Banking interest permissible were Muhammad 'Abduh (1905), Rashid Rida (1927), Muhammad Sharur (1992), Fazlur Rahman (1963) and Ashmawi (1987) who were the most influential jurists of the 20th century and described the differences between *riba* and modern interest in detail in the light of the fundamental principles of Islamic economy and changed context (Adams, 1993, pp.17-23). For instance, the Egyptian jurist Muhammad Sa'id Ashmawi (1987 Pp. 108-109) pointed out that "the reality must be taken into notice that the Qur'an intended to put an end, not to commercial and profitable transactions, but to exploitation by way of usurious transactions amounted to a flagrant exploitation of the debtor. And it is for this reason alone that *riba* was declared prohibited. In the modern economy on the other hand, no such exploitation of this sort exists." Further, Naqvi (p.110) stated that a thorough and deep study of the provisions of the Qur'an regarding prohibition of *riba* leads some important domino effects such as that the abolition of *riba* is a way (among many others) to establish an exploitation-free economy in a Muslim society so that only those economic policies be adopted which do not make worse social injustice particularly those arising out of the inequalities of income and wealth. Secondly, a zero rate interest occurs whenever an Islamic economic system occurs but presence of zero rate interest does not necessarily means the existence of an Islamic economy.⁴

⁴ Second point asserts that a zero rate interest is sufficient for the establishment of an Islamic economy is false. It also leads that with the abolition of *riba* all *gharar* transactions which are also prohibited by Qur'an are not eliminated automatically rather it requires additional actions such as pure speculative deals, forward trading, etc. It can be argued that such isolated step may lead to a divergent movement away from the goal of an Islamic economic system. It is not the sole purpose rather the basic thing is to bring about a structural change in the basic production and consumption relationship, the saving investment nexus and the process of money creation. See for detail, Syed Nawab Haider Naqvi, *Ethics and Economics: An Islamic Synthesis* (1981). London, The Islamic Foundation. p. 110.

Fourthly, Islam does not abolish interest arbitrarily through an administrative fiat rather it aims comprehensive reform to establish an exploitation-free economic system (Naqvi, pp.112-113). Further, under the practical situation of the modern economy, if the lender is not allowed to levy interest, he may be on the losing side and this will surely, result in a situation in which no one would be willing to make his money available for borrowing (Ashmawi, p.107). The fact is that the interest in the modern economy performs an equilibration function (Jomo, 1993, pp.29-30). Elimination of interest from the banking side seems impossible as many Islamic Banks involve in practices that amount to interest in disguise such as *Bai al-muajjal* which is intended for short term loans to industrialists, farmers and traders (Report Council of Islamic Ideology, Pakistan, p.119).

Likewise some anomalies also found in the institution of "*Ijarah Sukuk*" such as incomplete contract of sale which does not make a party real owner of a particular object and thus, cannot hire it in the light of the principle of Shari'ah. Second, it is binding upon the holder of *Sukuk* to sell property again to the government that is also against the spirit of Islamic contract which is based on the principle of mutual consent (Council Report, 2008-9, pp.18-83). Interest is unavoidable in case of large amounts of foreign exchange lend to the industrial sector by state-control financial institutions which are in turn financed by foreign countries and International finance institutions (Ayaz, 1984, pp.3-5). In such a context, it is impossible to set an isolated interest-free economy by the nation that itself submissive to the economic policies of others.

Conclusions and Recommendations

In the light of the above discussion, this article concludes that generally, all religion such as Buddhism, Christianity, and Islam condemn *riba* (usury) and other means of the exploitation of man by man on ethical and religious grounds and because of their adverse economic consequences as such a society can neither be economically healthy nor socially stable.

It is also concluded that in the majority of the Muslim states, socio-economic exploitative factors existed and practiced by the Muslim governments but are being ignored by the contemporary Muslim scholars who are just focusing theoretically just to condemn interest by declaring it *riba*.

Likewise, the Muslim scholars could not brought a radically new social or economical order anywhere in the world. (Nabil,1986,p.59).

It is also concluded that like the modern system of economy, the system of economy in the Muslim countries developed under the influence of the contemporary prevailing economic practices and the politics of a particular state like the recognition of the feudalism by the Muslim jurists under the influence of the Umayyad dynasty which is originally prohibited. Moreover, economic growth with a zero rate interest is not possible in the real world because the contemporary Muslim World is dependent upon the Western developed World and World Bank regarding their economic survival. Under such circumstances, it is beyond logic to claim for an isolated and idealistic interest-free economy.

It is also concluded that the unscientific understanding of the contemporary economic institution of the "interest" caused to create many problems for the contemporary Muslim Ummah and put them into doubt regarding work and earning at an interest-based institution like Conventional Banks and made them confused regarding their wealth earned in a society whose government (Muslim) adopts interest-based policy and seeks interest-based foreign aids.

Recommendations

It is suggested that the study of the principles of Islamic economics should be based on the rationale, scientific theory and empirical evidences. Priority should be given to eliminate the evils of prevailing economic systems in the Muslim countries.

It is also suggested that the modern Muslim economists and scholars should not be confined to the study of the *fatawa* of the traditional Muslim jurists in stagnant manners. It has been condemned by Allah almighty in these wording: "And when it is said to them: "Follow that which Allah has been sent down", they say: "Nay, we shall follow that which we found our fathers" (The Qur'an:31:32). Rather it is duty of the contemporary scholars to evaluate in scientific manners how the companions and the traditional Muslim jurists legalized many existing customary economic practices which involved *gharar* and interest just to provide ease to people and to remove hardship from them in the light of the changed context irrespective of the fact that at that time the Muslims were in a dominant position.

The current subservient condition of the Muslim states and their dependent interest-based economies should not be ignored by the modern Muslim philosophers. It is suggested that the issue of *riba* must be taken in the meaning of exploitation which is prohibited in Islam in its all forms not merely as a fixed rate of interest. Lastly, it is suggested that the modern capitalist Banking interest should be recognized by the Muslim scholars by way of necessity to provide ease to people and to remove hardship from them as it has become an unavoidable part of the Muslim's earning directly or indirectly. It is the only way to satisfy the honest and religious minded segment of the society and to justify the contemporary interest-based economic policies of the Muslim countries.

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