CONTRIBUTION OF ISLAMIC FINANCE TO ECONOMIC DEVELOPMENT

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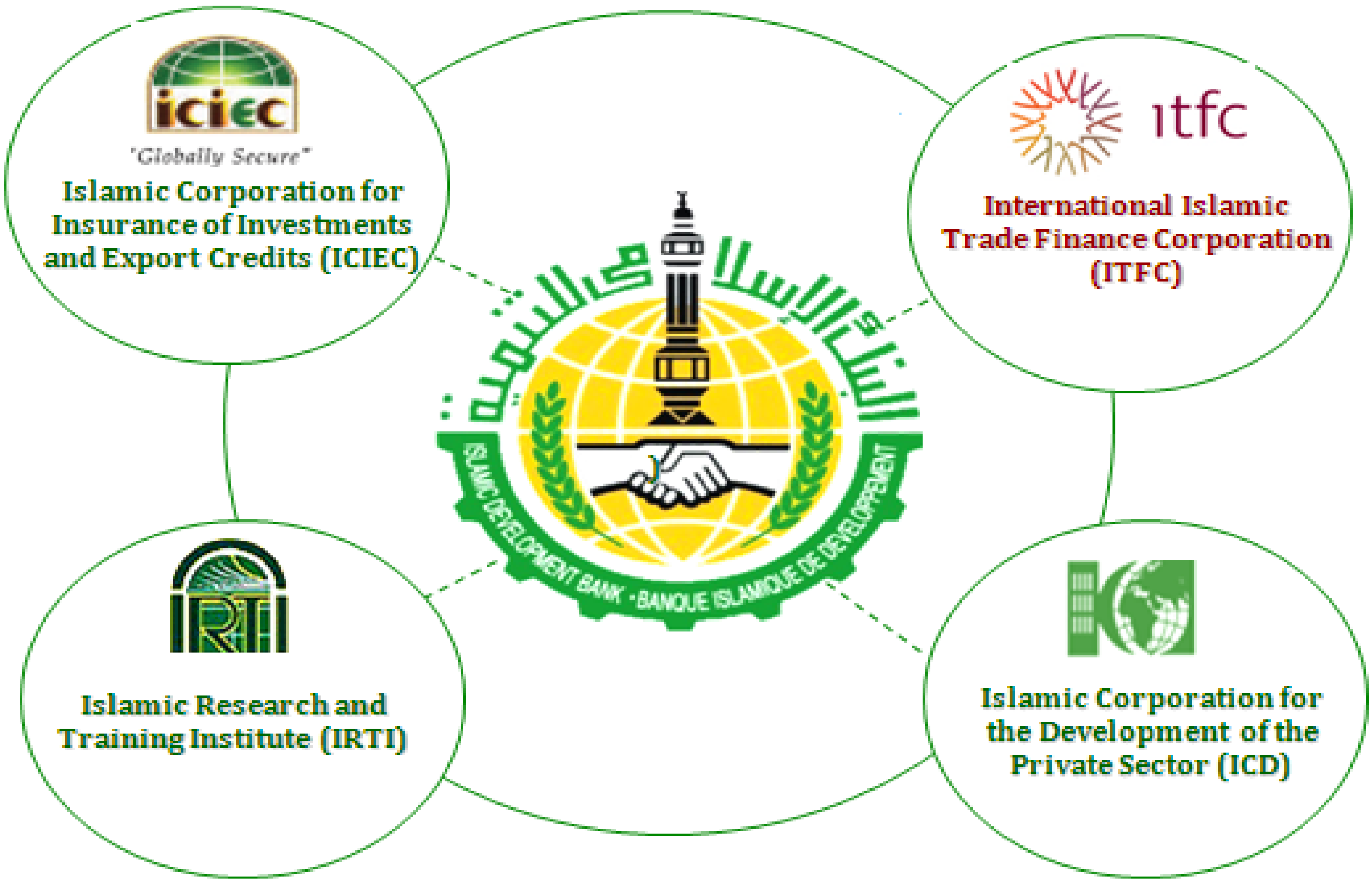
Institut Islamique de Recherche et de Formation (IIRF)
Islamic Research & Training Institute (IRTI)
Established in 1981

Membre de la
Banque Islamique de Developpement (BID)
ISLAMIC DEVELOPMENT BANK (IDB) GROUP

Source: IRTI Annual Report


iciec
'Globally Secure'
Islamic Corporation for Insurance of Investments and Export Credits (ICIEC)
itfc
International Islamic Trade Finance Corporation (ITFC)
ISLAMIC DEVELOPMENT BANK · BANQUE ISLAMIQUE DE DEVELOPPEMENT
Islamic Research and Training Institute (IRTI)
Islamic Corporation for the Development of the Private Sector (ICD)

IRTI Vision and Mission

Vision

To be the global knowledge centre for Islamic economics and finance by 1440H

Mission

To inspire and deliver cutting edge research, capacity building, advisory and information services in the area of Islamic economics and finance

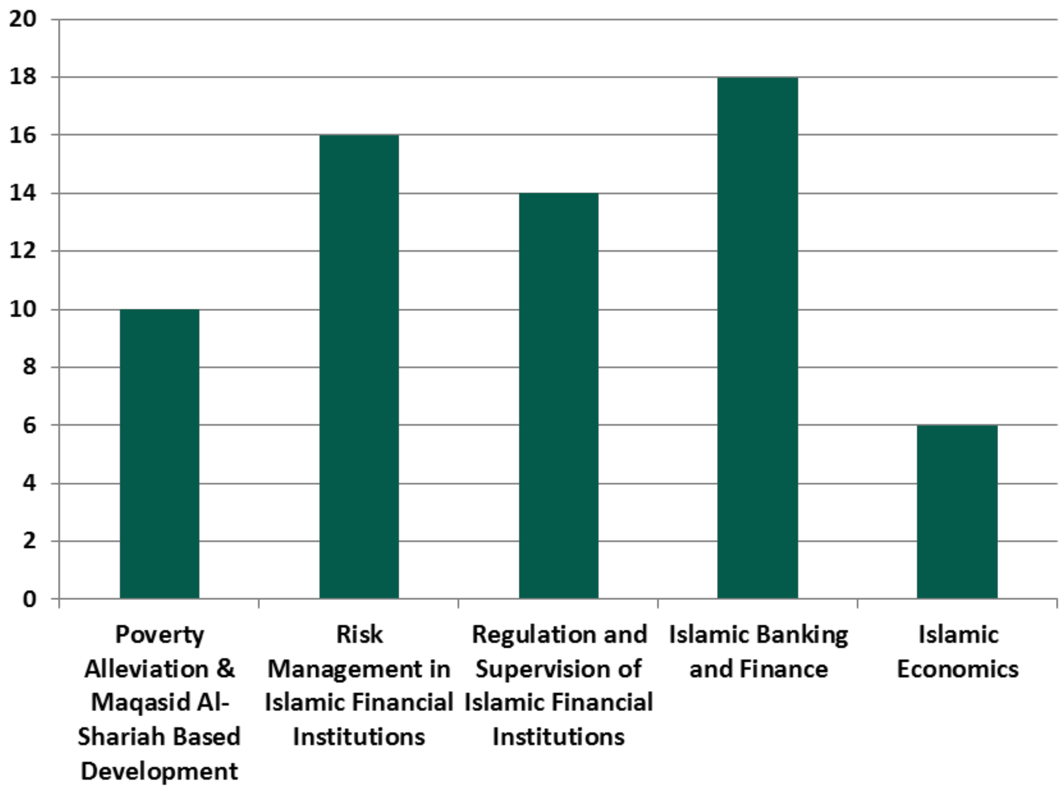
Source: IRTI Annual Report

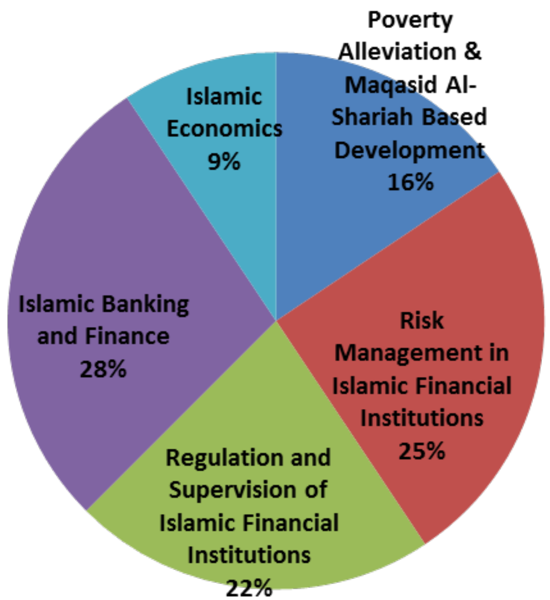
IRTI Products and Services

- Research & Publications
- Advisory Services
- Capacity Building - Trainings
- Information Services
- Learning Initiatives
- Encouragement Programmes

Source: IRTI Annual Report

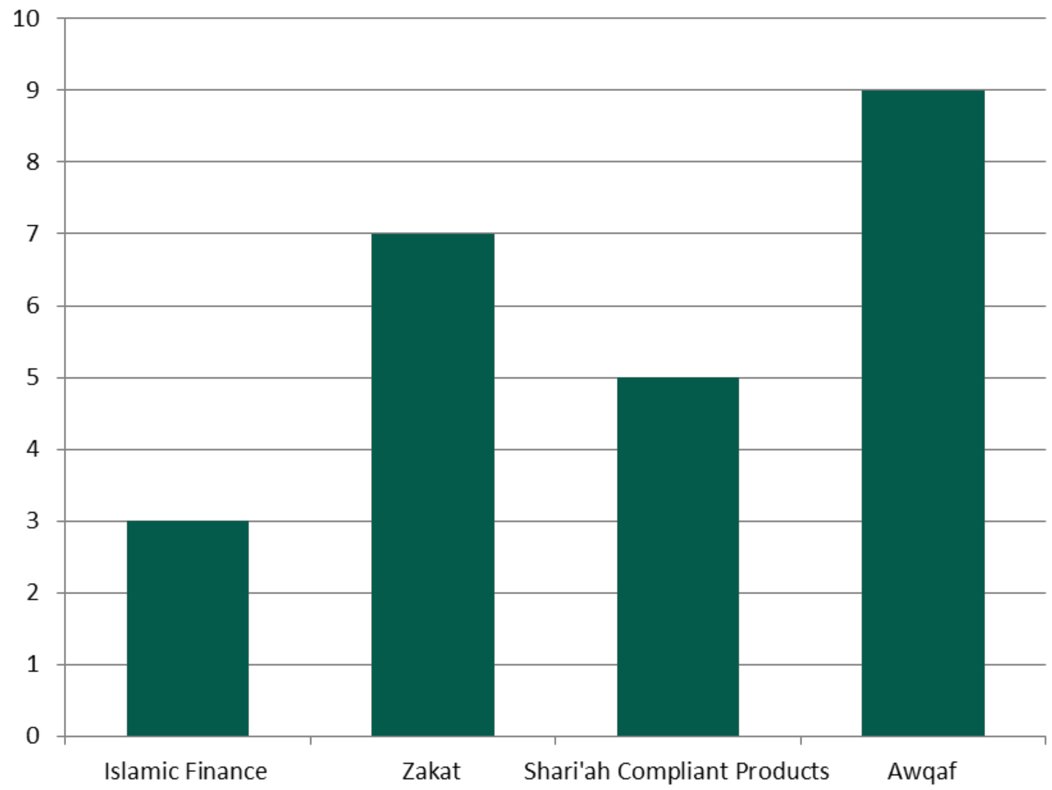
Thematic Distribution of Programmes Organised by Research Division in 2010-2012

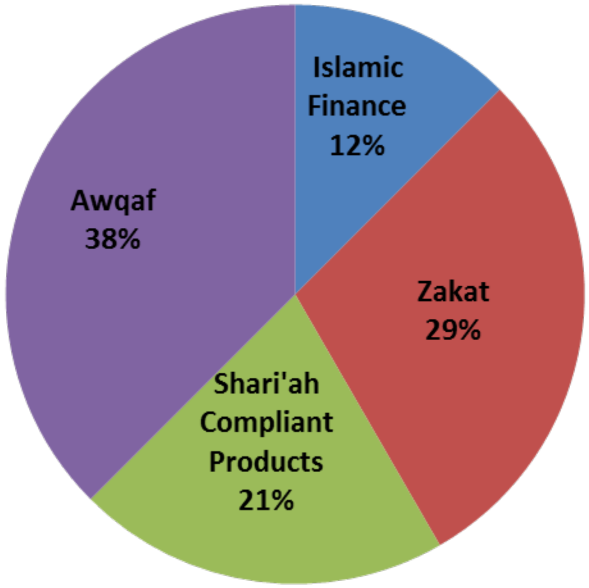




Source: IRTI database

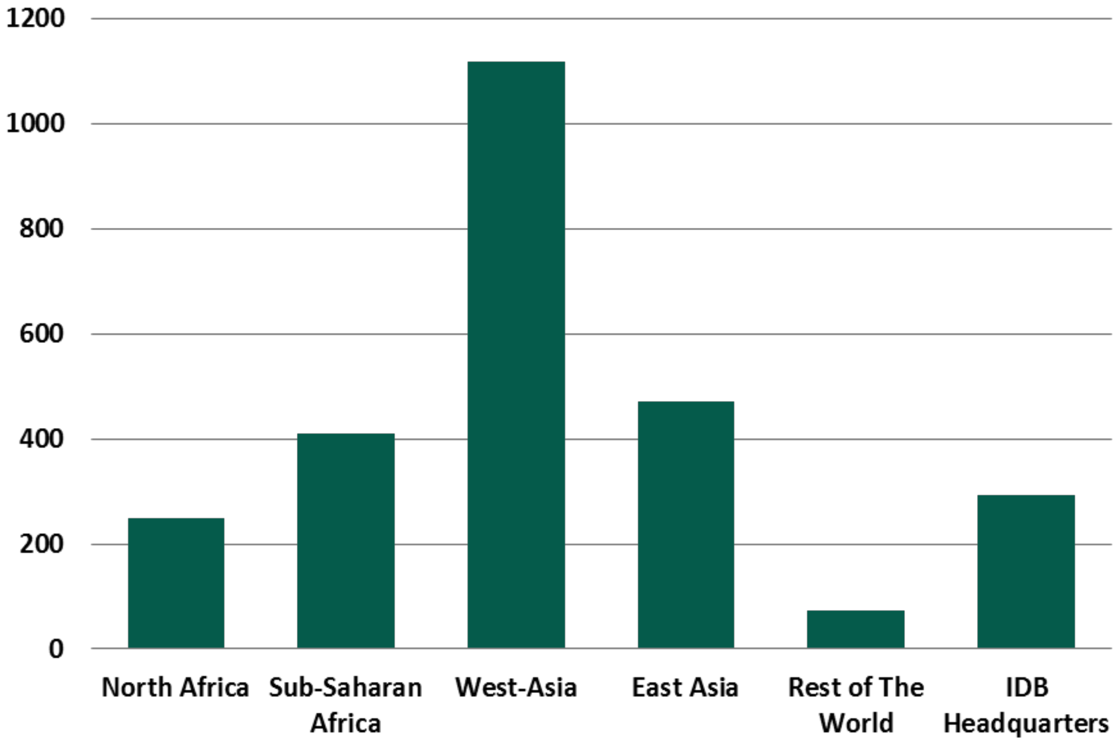
Thematic Distribution of Programmes Organised by Advisory Services Division in 2010-2012

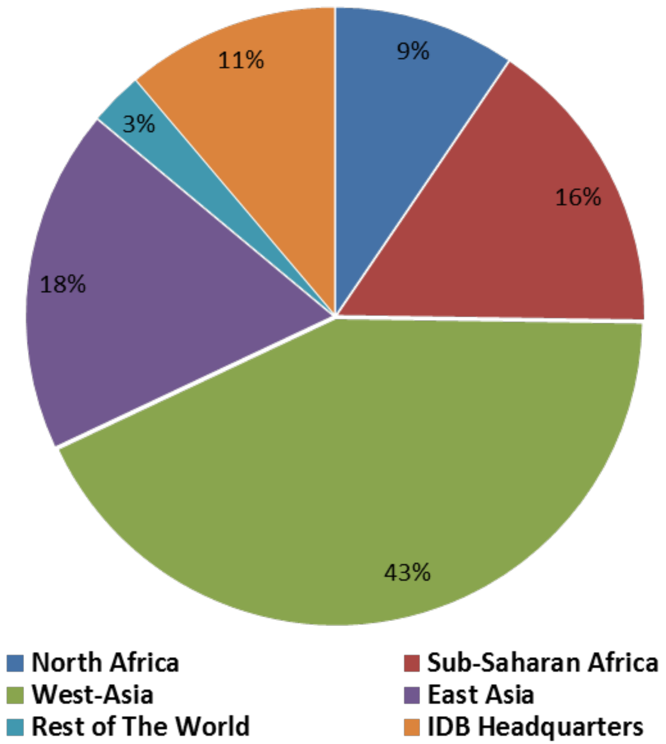




Source: IRTI database

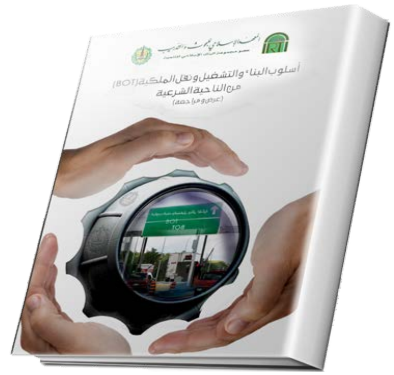
Geographical Distribution of Participants in Training Programmes in 2010-2012

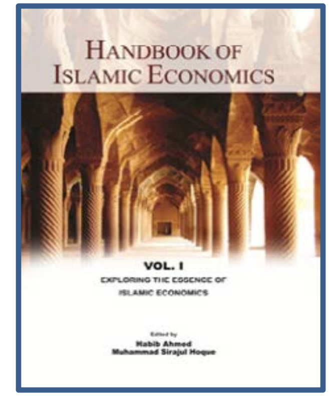


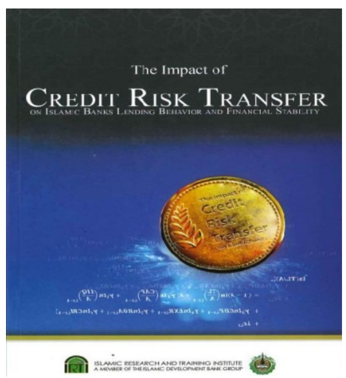


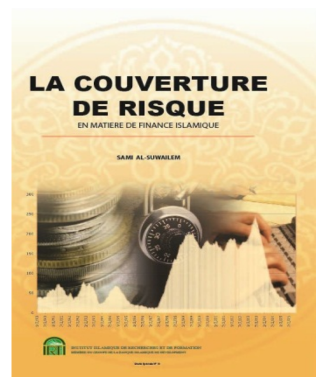
Source: IRTI database

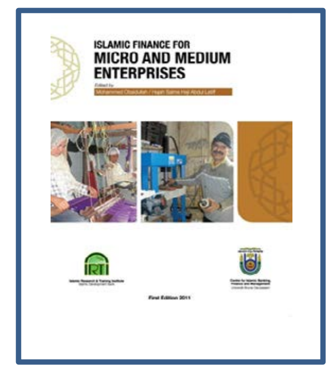
Samples of IRTI Publications







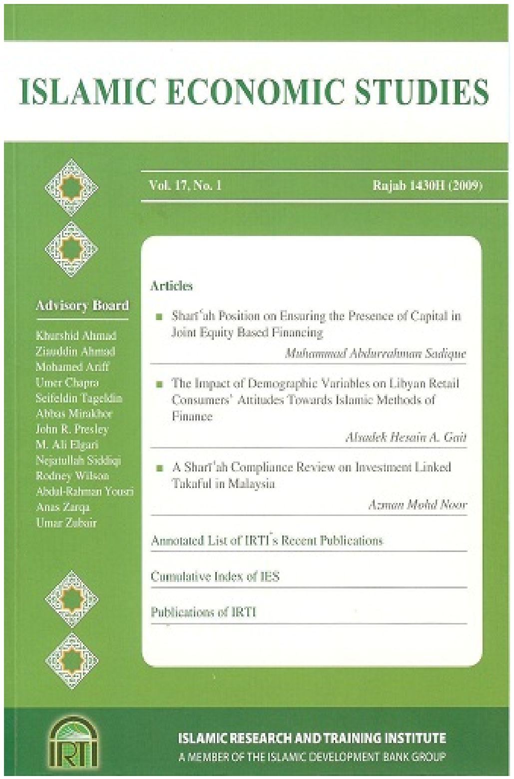


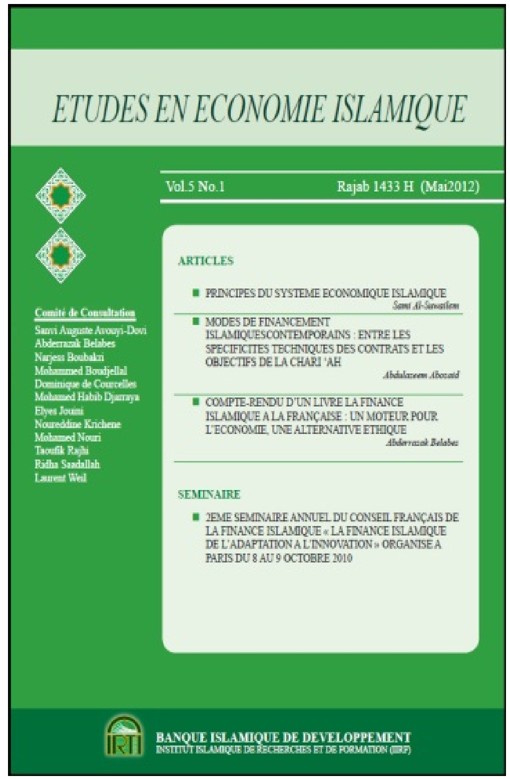


350 books / journals published in English, Arabic and French
Downloadable from IRTI website
Hard copies can be obtained

Source: IRTI website

IRTI Journals





English version **French version** **Arabic version**

Source: IRTI website

IRTI Encouragement Programmes

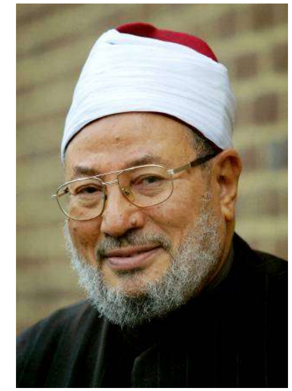
Programme	Number of Beneficiaries
IDB Prize in Islamic Economics	18 [15 individuals & 3 institutions]
IDB Prize in Islamic Banking & Finance	16 [15 individuals & 1 institutions]
IDB Solidarity for the Promotion of Trade among OIC MCs	4 Institutions
IRTI Scholarships	24 Students*
IRTI Research Grants	4 Researchers*
Visiting Scholars	7*
IDB Prize Winners Lecture Series	5*
IRTI Shari'ah Lecture Series	4*
IRTI Eminent Scholars Lecture Series	2*

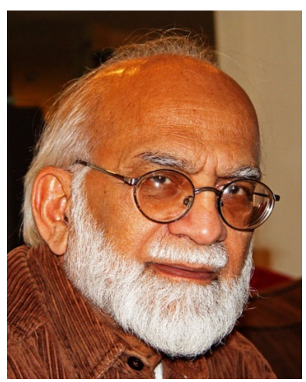
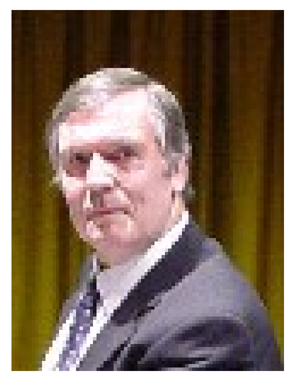
* In the last 3 years

Source: IRTI Annual Report various years

Eminent Laureates of the IDB Prize



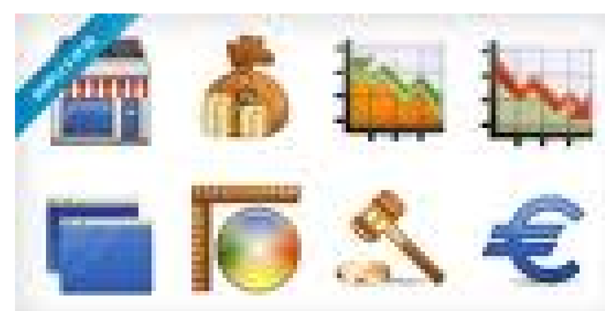




Source: IRTI Annual Report various years

Importance of Financial Development

- Finance is the blood that runs through the veins (financial institutions) of an economy.
- Financial development whether it is conventional or Islamic is very important for economic growth and development.
- However, the impact of each is different.
- It leads to efficient mobilisation of savings and efficient use of funds for investment.
- Financial development is welcomed within the boundaries of Islamic Shari‘ah.



Importance of Financial Development

- Banks and other financial institutions whether conventional or Islamic are vital financial intermediaries.
- They mobilise savings and idle funds from Surplus Economic Units and make them available to Deficit Economic Units.
- Until recently (1970s), most economists believe that no financial system can develop without recourse to interest and that any religion, like Islam, which prohibits interest, is an obstacle to economic growth and development.
- However, since the 1970s, Islamic finance has been growing at phenomenal rates of growth not only in Islamic Countries but even in non-Islamic countries.
- Not only that but it has shown greater resilience to crises than its counterpart the conventional, which made it even more attractive, despite the remaining challenges it faces.

Objectives of Financial Development

- The primary aim of any financial system, is to facilitate the flow of funds from savers who have financial surpluses, to investors who have financial deficits.
- It is very difficult to channel these surpluses to those who need them without a financial intermediary that collects surpluses and passes them efficiently and effectively to those who need them.
- Thus, the need for banks and other financial institutions to carry out this task.
- Just as money is the mediator which facilitates the exchange of goods and services instead of barter, the financial intermediation facilitates the collection and delivery of funds.

Objectives of Financial Development

- Financial intermediation is very important in order to
  - Mobilise idle funds
  - Encourage savings
  - Finance projects
  - Increase and diversify investments
  - Create new job opportunities
  - Increase and diversify production of goods and services
  - Raise national income
  - And thus contribute to economic growth and development

Differences between Conventional and Islamic Finance

	Conventional	Islamic
interest	Y	X
Commission	Y	Y
PLS modes of finance	X	Y
Debt-Like modes of finance	Y	Y
Speculation	Y	X
Derivatives	Y	X

Four Types of Financial Transactions

- Islamic financial institutions face in the course of their work four types of financial transactions:

1. Interest based transactions, which are prohibited.
2. Commission based transactions that are acceptable.
3. Suspicious transactions that are not clear whether they are acceptable or not.
4. Alternative transactions to interest based ones such as *Musharakah*, *Mudarabah*, etc..

Basic Principles of Islamic finance

- Permission of all transactions that do not involve any prohibition.
- Prohibition of *Riba* (Interest/Usury).
- Prohibition of *Qimar* (gambling), *Iktinaz* (hoarding), *Ihtikar* (monopoly), *Israf* (extravagance), *Fasad* (corruption), *Mujazafah* (speculation), *Ghish* (deception) *Tadlees* (fraud) *Kathib* (lying) etc..
- Prohibition of dealings involving *Khamr* (intoxicants), *Khinzir* (Pork), and all unethical dealings such as prostitution, stealing, etc..
- Prohibition of contracts involving *Gharar* (excessive risk).
- Selling what is not owned or possessed.
- Selling Fruits before they are ripe.
- Selling debts.

The Islamic Financial System is Based on Two Pillars

- As Sami Suweilem put it the Islamic Financial System is based on two fundamental pillars:
  - For-Profit Domain or Business Sector
  - Non-Profit Domain or Charitable Sector
- It takes a balanced approach

Basic Modes of Islamic Finance
for Profit Sector

- ***Musharakah*** (Partnership) joint venture. A contract in which two or more investors pool their funds for a project and share its profits/losses
- ***Mudarabah*** contract under which the Mudarib (entrepreneur) manages the funds of *Rabb al-Mal* (investor) for a percentage on any profits made. Financial losses to be born by *Rabb al-Mal.*
- ***Muzara'ah*** (sharecropping) joint venture in agriculture to share the proceeds of a new plantation.
- ***Musaqat*** (sharecropping) joint venture in agriculture to share the proceeds in existing plantation.

Basic Modes of Islamic Finance

for Profit Sector

- ***Murabahah*** **(Markup sale) a contract of sale in which payment is made some time after delivery of the goods transacted with a pre-agreed higher price**
- ***Bay‘ Mu’ajjal*** **sale on deferred payment: allows the buyer to pay for the goods over a series of instalments.**
- ***Bay‘ Al-Salam*** **sale on prepaid payment**
- ***Ijarah*** **(Leasing) hire of an asset for an agreed rental for a fixed period.**
- ***Ijarah waqtina’*** **(Hire Purchase) same as *Ijarah*, but that at the end of the contract the asset leased becomes the property of the lessee.**

Basic Modes of Islamic Finance

for Profit Sector

- ***Jo'alah:*** A Commission or a reward for doing a specific job or rendering a specific service.
- ***Istisna'*** commissioned manufacture made-to-order in which the manufacturer designs and makes the product in accordance with the buyer's wishes.
- ***Halal Mortgage:*** mortgage based on shared equity rental.
- ***Tawarruq***: Buying a commodity on deferred payment then selling it for cash to a different buyer than the original seller.
- ***Sukuk***: Certificates of investments in a project for a specific period with a promise of a share in the proceed of the investment.

Basic Modes of Islamic Finance

For Non Profit Sector

- ***Nafaqah:*** **obligatory spending for designated relatives: parents, family and close relatives.**
- ***Zakah*** **(compulsory charity) 2.5% of savings given annually to the poor and needy. One of the 5 pillars of Islam.**
- ***Sadaqah*** **(voluntary charity) very much recommended by Islam in addition to help the poor and destitutes.**
- ***Takafol*** **(Mutual or cooperative solidarity or insurance). Participants pool their funds as a provision against any losses to life, limb, or property that one of them may suffer.**
- ***Qard Hassan:*** **interest-free loan.**

Contribution of Islamic Finance to Development

- **There are a number of academic studies that have examined the contribution of Islamic finance to growth and development. The following are just a sample to make the point**
  - **Said Al-Hallaq "Contribution of Islamic banks to the Development of the Jordanian Economy", www.islamicfinancenews.com**
  - **Philip Moore, *Islamic Finance: a Partnership for Growth*, Euromoney Publication PLC**
  - **Hafas Furqani & Ratna Mulyani, “Islamic Banking and Economic growth: an Empirical Evidence from Malaysia”, *Journal of Economic Cooperation and Development*, Vol.30, No.2, 2009**
  - **Nadia Mavrakis, “Islamic Finance: a Vehicle for Economic Development”,**
  - **Munawar Iqbal & Ausaf Ahmad, *Islamic Finance and Economic Development*, Palgrave Macmillan**
  - **Habib Ahmad, “Islamic Financial system and Economic Growth: an Assessment”, *Journal of King Abdulaziz University***
  - **Nirvana Abou-Gabal, Asim Ijaz Khwaja & Bailey Klinger, *Islamic Finance and Entrepreneurship: Challenges and Opportunities Ahead*, Harvard University**

Contribution of Islamic Banks to Development

- As Said Al-Hallaq pointed out “Islamic banks differ from conventional banks in that their spectrum of financing is more varied.
- Their investments are more diversified in terms of maturity, liquidity and risk, ranging from the relatively short-term, more liquid and less risky mode of Murabahah to the longer term, less liquid and higher risk mode of equity (or direct Musharakah) financing.
- Each mode differs in its effect on the capital accumulation capability and resource utilization efficiency of the banks, and thus the economic growth of the relevant country also varies.
- The effect of a bank’s activity on economic growth will therefore depend on which modes of finance and investment the bank undertakes most, and how much each one of these modes contributes to economic growth”

Said Al-Hallaq "Contribution of Islamic banks to the Development of the Jordanian Economy",
www.islamicfinancenews.com

Contribution of Islamic Banks to Development

- As Abou Gabal *et al*. noticed "Data show that there is significant unmet demand for shari'ah-compliant financial services, particularly among micro, small, and medium-sized enterprises (MSMEs).
- Moreover, the risks of concentrating in real estate, corporate and government finance have been highlighted by the recent financial crisis, given their higher level of systematic risk compared to other segments like MSMEs.
- Finally, current shari'ah compliant product offerings to MSMEs are highly concentrated in leasing and asset resale contracts, with limited use of the more legitimate profit and loss sharing contracts".

Contribution of Islamic finance to Economic Development

- My colleagues from the different entities members of the IDB have already given you a pretty good idea on their contributions to economic development through:
  - Financing infrastructure projects
  - Financing intra-trade among OIC member countries
  - Insuring import and exports of member countries
  - Helping in the establishment of Islamic financial institutions such as zakat Funds and Awqaf institutions

Examples of calls for the consideration of Islamic Finance

- After the start of the Current Crisis, many quarters are calling for the consideration of Islamic Finance.
- The Vatican's official newspaper *Observatore Romano* said in an article: "The ethical principles on which Islamic finance is based may bring banks closer to their clients and to the true spirit which should mark every financial service".
- Islamic Finance is being taught at Universities all over the world as in:
  - Harvard and Rice Universities in USA
  - Bangor, Durham, Loughborough and other Universities in UK
  - Strasbourg and Paris Universities in France
- Almost all countries of the world are interested in Islamic Finance, including China, India, Singapore, Australia, etc..

Conclusion

- Islamic Finance is ethical.
- Islamic Finance is fair.
- Islamic Finance is balanced.
- Islamic Finance is more stable.
- Islamic Finance contribute towards the mobilisation of idle funds and towards the encouragement of savings.
- Islamic Finance contribute towards the investment of idle funds and of mobilised savings.
- Islamic Finance contribute towards the creation of new jobs.
- Islamic Finance contribute towards the increase in the Gross Domestic product.
- Islamic Finance contribute towards growth and development.

شكرا جزيلا

Merci beaucoup

Thank You very much

Muchas Gracias

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