



# A paradigm of Islamic money and banking

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Masudul Alam Choudhury and Md. Mostaque Hussain  
*Department of Accounting, College of Commerce and Economics,  
Sultan Qaboos University, Muscat, Oman*

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## Abstract

**Purpose** – Theological perspectives in ethics, values and their functional application in the real world are vividly covered by the theory and practice of Islamic banking in recent times. This paper seeks to formalize the theological paradigm of the unity of God (*Tawhid*) and to make the groundwork of unity of knowledge in the context of the money, finance and real economy linkages.

**Design/methodology/approach** – The paper combines narrative with argument and analysis.

**Findings** – On the basis of this the structure of the balance sheet of Islamic banks with no interest rate as an ethical condition of Islamic financing is delineated. This topic is followed by a discussion on the experience of Islamic banks in recent times in the area of mobilizing resources and gaining profitability, popularity and stability by the Islamic financing methods and the direct mobilizing of financial resources into the real economy. In this way, the Islamic banks are shown to attain the much-needed complementary relations between social well-being for clients and financial efficiency for the banks.

**Originality/value** – Adds insights to the theory and practice of Islamic banking.

**Keywords** Islam, Banks, Religion, Law, Finance

**Paper type** Research paper

## Introduction

Islamic banks as a novel phenomenon in the financial world since the mid-20th century have been construed as financial intermediaries that mobilize resources in the direction of projects approved by the Islamic Law (the *Shari'ah*) using Islamic financing instruments (Siddiqi, 1983). Islamic modes of financing comprise two basic principles, namely the interest-free financing instruments in the private sector and the development financing instruments based on both cost and profit sharing. Some of the principal instruments involved in such forms of resource mobilization are as follows (various Islamic Development Annual Reports):

- (1) trade financing and cost-plus mark-up on traded goods (*murabaha*);
- (2) profit-sharing (*mudarabah*) and equity participation (*musharakah*) in which cost-sharing among partners is also included;
- (3) rental on purchased equipment (*ijara*); and
- (4) Islamic banking portfolio using secondary financing instruments, such as shares and stocks revolving around the above-mentioned instruments.

However, the financial resources are to be mobilized with the important condition of keeping the *Shari'ah* in view. They are therefore to be directed into the *Shari'ah* recommended goods, projects and goals. Thereby, socio-economic development and ethical prerogatives become part and parcel of the Islamic financing modes. Being so, Islamic banks have a mandate that extends beyond simply serving their clientele by



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securing funds in the above-mentioned kinds of portfolios. They become development institutions, and thereby, play an important role in the economic and moral uplift of the Islamic society or community from the viewpoint of the *Shari'ah*. Islamic banks are thus to co-operate between themselves and with other national development institutions in accordance with the spirit of co-operation upheld by the *Shari'ah* for the benefit of all.

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### **Precepts of the *Shari'ah* and the goals and instruments of Islamic banks**

What are the precepts of the *Shari'ah* in the financial field? They are to establish social security, property rights and the rights of progeny. In the extensive domain of the *Shari'ah* these goals are combined with the mandate of preservation of the Islamic State.

Within the mix of the above-mentioned *Shari'ah* precepts, we find that the social, economic and political goals are taken up together with the financial ones. These together comprise the totality of the social, economic and political development issues of an Islamic society. Hence, when Islamic banks are linked with such a comprehensive network of goals in the light of the *Shari'ah*, the totality of the socio-economic and socio-political goals along with the financial ones would predominate in the objective criterion of an Islamic bank. For example, in the attempt to secure the funds of its clientele in the *Shari'ah* recommended ways, which comprise the tenet of securing property rights, the Islamic bank must embrace the other *Shari'ah* tenets as well. Thereby, socio-economic development goals become important in the *Shari'ah* determined social well-being function.

### **The social well-being objective criterion of Islamic banks**

The social well-being function as the objective criterion of Islamic banks serving the tenets of maintaining social security, protection of progeny and preservation of the Islamic State, becomes a description of ways and means of financing resource mobilization that establish sustainability and the high ideals of the Islamic faith. This ideal goal involves the principle of *Tawhid*, that is the oneness of *Allah* (God) as the highest principle of Islam. The model of implementing the principle of *Tawhid* in the socio-economic, financial and political order involves organizing the modes of resource mobilization, production and their financing in ways that bring about complementary linkages between the *Shari'ah* determined possibilities. In this way, there appears co-determination among the possibilities, evolution of the instruments to be selected and implemented by many agencies in society at large. Islamic banks form a part and parcel and interconnecting mediums of a lively developmental organism.

The developmental possibilities are realized both by the medium of discourse between management and shareholders of an Islamic bank as well as in concert with other Islamic banks, the central bank, enterprises, government and the community at large. In this way, a vast network of discourse related networking and relational system is established between the Islamic banks and the socio-economic order as a whole. Such unifying relations as participatory linkages in the economy wide sense convey the externalized meaning of *Tawhid*. This highest principle is now understood as the unity of knowledge emanating from the oneness of *Allah* as the one, who is complete and absolute in knowledge. The external meaning of *Tawhid* is now explained in terms of an increasingly relational, participatory and complementary

developmental order wherein possibilities unify among themselves. This unification process and sign in the externalized world is a meaning of the principle of *Tawhid* as we live it. The discourse related process and institution of determining such unifying possibilities by Islamic banks within the comprehensive outlook of *the Shari'ah* is called the *Shura* of the Islamic banks.

In the end, by combining the totality of the *Shari'ah* precepts, Islamic banks become as much investment oriented financial intermediaries as they are agencies of sustainability of the socio-economic order, the socio-political order and preservation of community assets. It is now obvious that Islamic banks even when using the most modern kinds of instruments to attain such goals and sustain them over the long term would promote human resource development. In this way, the internal efficiency of Islamic bank and its informed connection with the community at large can be harnessed. Yet human resource development as a powerful instrument that causes Islamic banks to become development centered financial organisms in the total life of the Islamic community must be appropriately determined in the light of the *Shari'ah*.

Take for example the questions relating to analytical methods of project evaluation. While it would be necessary to understand the complex methods of asset valuation from the viewpoint of interest-based concepts of the time value of money and the like, yet the truly Islamic methods of project evaluation would be central to the training of human resources in Islamic banks. In the same light, such training is to be imparted to the community through educational and practical training programs.

Likewise, human resource development for project evaluation, technical assistance and feasibility report preparation on projects must keep in view the integrated outlook of the Islamic economy keeping the goals of the *Shari'ah* in mind. This can be realized by using a model of linkages among economic sectors that together can mobilize money into real economic activities and thus deter funds from speculative ventures, portfolio investments, bonds and money market funds.

On the other hand, resource mobilization in all avenues of the *Shari'ah* recommended possibilities should be promoted so as to create a close link between monetary aggregates and real productive activities. The nature of money now turns out to be endogenous through its circulation in the real economy as a "quantity". Money is not determined in this case by demand and supply concepts, since it does not have a market of its own, as in the case of goods and services. Instead, there are markets only of real goods and services that value the worth of money in the first place. Besides, such goods and services are those that are recommended by the *Shari'ah* in the light of well-being and linkages to generate complementary relations between various possibilities. On the basis of such real market exchange, real returns are measured in terms of prices, output and profits. These in turn determine the return on money. Islamic banks thus become important links between the national central banks, the economy and community in realizing such endogenous money-market interrelations.

### **The nature of balance sheet of an Islamic bank**

Given below is a model of the balance sheet of an Islamic bank, in the absence of interest-based financing, in the light of the above-mentioned kind of general system of interactive, integrative and dynamic relations between money and the real economy. It reflects the valuation of asset and liability in the perspective of the endogenous

interrelationship between financial flows and the real economy in view of a developmental outlook. This is seen as the sure way to reduce interest rates in an economy wide sense (Choudhury, 1997).

*Model inter-Islamic bank balance sheets in the case of endogenous money*

In Table I, let us explain the relationship between the reserve ratio,  $r'$ , and inter-bank loan flow as demand for liquidity for undertaking investments or spending. Spending of all kinds in the “good things of life” as prescribed by the *Qur'an* gives the meaning of resource mobilization. Since inter-bank loans for liquidity will increase in the face of increased demand for investment (spending), therefore, the reserve ratio,  $r'$ , will decrease. Now the change in the quantity of money ( $M$ ) is related to the change in the demand for liquidity ( $D$ ),  $dD$ , by the multiplier,  $dM = dD/r'$ .  $dM$  is inversely related with  $r'$ . Investment (spending) demand increases as  $r'$  decreases and vice versa. See Choudhury (1998) for details.

B1 and B2 are two Islamic banks engaged in inter-bank loans. In a joint financing of venture (*mudarabah* and/or *musharakah*), let  $g_1$  denote the return to B1. This return then forms an asset of B1. Let  $g_2$  denote the return to B2, which then forms a liability to B1. Likewise,  $g_2$  forms a return to B2 and  $g_1$  forms a liability to B2.

New money in the economy equals the amount of investment (spending) equal to  $IID \cdot g_2$ . In this way, in a multiple inter-Islamic bank loan-flow under joint venture, the total quantity of new money or investment capital (spending) arising from IID of initial spending equals,

$$g_2 + g_2^2 + g_2^4 + g_2^8 + \dots = g_2(1 + (g_2/(1 - g_2^2))) \tag{1}$$

The total amount of spending,  $Sp$ , which must be matched by the quantity of endogenous money in circulation is now given by,

$$Sp = IID + g_2 + g_2^2 + g_2^4 + g_2^8 + \dots = (1 + g_2 - g_2^3)/(1 - g_2^2). \tag{2}$$

To a linear approximation the above expression reduces to,

$$Sp = \text{new money} = 1 + g_2. \tag{3}$$

Likewise, for  $MID$  of initial spending as endogenous money, the total money creation or new spending equals  $M(1 + g_2)$ . Since  $g_2$  is determined by the growth of real sector output, therefore, money is created in exact equivalence with this growth rate. For the concept of endogenous money see Choudhury (1997).

Balance sheet for Islamic bank B1	Balance sheet for Islamic bank B2
Initial deposit = ID 1.00	Initial deposit = 0
Reserve ratio = $r' = 0$	New deposit = $1 \times g_2$
Retention = $1 \times g_1$	Retention = $1 \times g_2 \times g_3$
Loan = investment (spending)	Loan = $1 \times g_2 - 1 \times g_2 \times g_3 = 1 \times g_2^2$
In joint venture = $1 \times g_2$	
ID = Islamic Dinar	

Table I.

One of the many healthy consequences of endogenous money is that inflation remains controlled, since the value of transactions (as a reflection of investment or spending demand) per unit quantity of money in circulation remains stable. Another implication of endogenous money in Islam is that it creates a currency-denominated economy rather than demand-supply of money based on promissory notes and thus on an interest-bearing reserve ratio set both between the central bank and commercial banks and by the excess reserve ratio set by commercial banks.

**A contrasting view between endogenous and exogenous money supply by banks**

The contrast between endogenous and exogenous monetary systems is this. Assume that IID = \$1. Table II

The central bank reserve is 10 per cent. Hence,

$$dM = [dD/0.10]\$ > ID \quad dD; \tag{4}$$

$$Sp = IID + g_2 + g_2^2 + g_2^4 + g_2^8 + \dots = \$0.90(1 + g_2 - g_2^3)/(1 - g_2^2) < ID \quad 1(1 + g_2 - g_2^3)/(1 - g_2^2). \tag{5}$$

**Contrasting exogenous money**

The following shows the contrast between the two monetary systems with respect to the goals of economic stabilization and economic growth. Stabilization in the exogenous (fractional reserve monetary system) is passed on to the central monetary authority using the reserve ratio. Besides, the central bank reserve is positively related with the interest rate, in that, as the savings increase with higher interest rate the central bank reserve increases by the amount of the new deposits. Furthermore, if there is pursuit of aggressive monetary policy by the central bank, both the reserve ratio and the prime rate of interest may move upwards together. Now a higher amount of monetary contraction occurs by the twin decrease in *dD* and *r*. This can be seen in the expression (4). This will cause even a lower difference in the much-desired reserves of the central bank for transaction purposes in the exogenous fractional monetary system than in the 100-per cent reserve requirement monetary system.

In both of the above cases with exogenous money in fractional reserve monetary system, *Sp* decreases, so that the role of the real economy in terms of spending in the *Shari'ah* outlets (socially productive and useful) for economic stabilization is reduced and taken over by the central bank's function affecting reserve ratio and the prime rate

Balance sheet for conventional bank B1

Balance sheet for conventional bank B2

Initial deposit = \$1.00  
Reserve ratio = *r'* = 10 per cent  
Retention = 0.90 × *g*<sub>1</sub>  
Loan = investment (spending)  
In joint venture = 0.90 × *g*<sub>2</sub>

Initial deposit = 0  
New deposit = 0.90 × *g*<sub>2</sub>  
Retention = 0.90 × *g*<sub>2</sub> × *g*<sub>3</sub>  
Loan = 0.90 × *g*<sub>2</sub> - 0.90 × *g*<sub>2</sub> × *g*<sub>3</sub> = 0.90 × *g*<sub>2</sub><sup>2</sup>

Table II.

of interest. The withdrawal of resources from spending causes a lower rate or a volatile rate of return in economic and financial activities. Consequently, the growth rate of the money-real economy relationship in 100-per cent reserve requirement monetary system, which is the feature of endogenous money in circulation, is higher than the growth rate of the fractional reserve requirement monetary system.

### Spending as the resource mobilization

The example given above brings out the nature of spending in the *Shari'ah* recommended market activities as the source of economic stabilization, economic growth and social well-being. The concept of social well-being was explained above substantively in terms of the *Tawhidi* principle of universal complementarities (complementary relations) between all *Shari'ah* recommended goods and services.

Total spending variable,  $S$ , can be related to real output by the equation,

$$S = A(Q/p)^a, \quad (6)$$

where  $Q$  denotes nominal GDP;  $p$  denotes the price level;  $A$  is a constant;  $b$  denotes the spending elasticity of  $Q/p$ .

Expression (6) is written in terms of growth rates as,

$$g_S = a_1 g_Q + c g_u \quad (7)$$

where  $g_S$  denotes the growth rate of spending;  $g_Q$  denotes the growth rate of output;  $g_u$  denotes the growth rate of an unaccounted for random variable.

It is known that the real aggregate demand (spending) function would be flatter than the supply curve of real output. Hence,  $g_S < g_Q$ . Therefore, the rate of growth of real output growth is expected to be higher than the real spending rate.

The above result is affirmed by Metwally (1989), who found statistically significant relation between real output growth and investment growth, investment being the second major component of total spending in the aggregate demand function. Since real output growth rate is an indicator of real productivity growth we conclude that inflation is checked when the rate of growth of real productivity exceeds the rate of growth of spending and which in turn is a significant positive function of real M1.

### Interest rate effect on money supply

Metwally also estimated that the rate of interest has a significantly negative relationship with the rate of growth of money demand (M1). Now by combining the above results we deduce the following results:

$$i \downarrow \Rightarrow \text{Spending} \uparrow \Rightarrow \text{Investment} \uparrow \Rightarrow \text{rate of return, } r \text{ increases and stabilizes} \uparrow \quad (8)$$

$$\Rightarrow \text{stability in M1} \uparrow \Rightarrow \text{inflation stabilizes.}$$

Expression (8) can be extended to the following circular relationship under the effect of a sustained reinforcement of the result of expression (7) on the basis of preferences to spend in the "goods things of life" as the *Qur'an* encourages to spend in "moderation" on the *Shari'ah* recommended goods and services.

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$$\begin{aligned} \text{Stable } r \Rightarrow \text{inflation stabilizes} \Rightarrow \text{further spending} \uparrow \Rightarrow M1 \uparrow \\ \Rightarrow \text{circular causation} \end{aligned} \quad (9)$$

A strongly endogenous relationship in this circular relation is proven by the 95 per cent level of significance in the *t*-statistic for the estimated coefficients in Metwally's regression system.

The continuity of the circular causation in expression (9) would depend on the formation of preferences towards productive spending in accordance with the *Shari'ah*, that is in accordance with the usage of the *Shari'ah*-based financial instruments that generate complementary relations between money and the real economy and thus bring about linkages in the general equilibrium system of interaction, integration and creative evolution of the money and spending variables. The preferences so formed are carriers of the knowledge production in the general equilibrium system of interrelations centered on *Tawhidi* causality of unity of knowledge between the *Shari'ah* possibilities. The final implication then is that Metwally's results, which were time-dependent regression estimation, do not produce the circular causation as we have implied out of the first round in the one-directional results of expression (8). Only recursive continuity of knowledge formation can regenerate the process shown in expression (9). This requires institutional sensitivity to the *interrelated* process in the case of the money-real economy linkage issues.

### Evolution and historical performance of Islamic banks

We have now explained the Islamic banking concept in the framework of a general system of relations. Islamic banks are seen to involve themselves as financial intermediaries and investment-oriented institutions in bringing about well-being of the community, society and the economy in the light of the *Shari'ah*. Next we will examine what role Islamic banks have played in recent times in these directions.

We first examine the recent portfolio of financing made by the consortium of Islamic banks globally (International Association of Islamic Banks, 1988). First we will examine the Islamic banks' balance sheets during the early years. We will then examine the recent performance of Islamic banks in different parts of the world. We will infer what structural change has taken place in recent times from the past trends in Islamic banks' financing. Specific cases will be mentioned here including the experience of the Islamic Development Bank (IDB). It should be remembered nonetheless that the IDB being a regional development bank, functions differently from an Islamic bank. An Islamic bank is a private sector financial intermediary. It is subject to the statutory monetary policy requirements of the central bank of the parent country of the bank.

In the early years between 1987 and 1988 alone, the aggregate balance sheets of Islamic banks showed an increase in the balance of accounts by 7.4 per cent. This increased further by 14.9 per cent in 1989 over 1987. Total assets increased by 107.4 per cent between 1987 and 1988. Shareholder's equity increased by 12.4 per cent from US\$469.3 million in 1987 to US\$527.3 millions in 1988. Net distributed income increased from US\$230.3 million in 1987 to US\$280.1 million in 1988, a growth rate of 21.7 per cent. Rate of return on total investments was 15.8 per cent between 1987 and 1988. Equity volumes increased by 50.3 per cent, while the rate of return on equity was

18.6 per cent between 1987 and 1988. Total rate of return on capital was 18.6 per cent in 1988. Net profit rate was 11.1 per cent in 1988.

Much of the high returns were due to concentration of resource mobilization in trade financing (*murabaha*). Equity financing and joint ventures formed a distant small ratio. Hence in the aggregate, Islamic banks performed remarkably well during this early period of time as far as financial returns on *murabaha* were concerned. Shareholders' wealth was thus well protected by this financial instrument. The 1988 sectoral allocations of selected Islamic banks resources are shown in Table III. We note from it that agricultural and social allocations were minimal, except in the case of the Sudan Islamic bank.

### Recent performance of Islamic banks

In recent times, Islamic banking and financing services have increased phenomenally around the world. There now exist 150 such banks spread over most countries of the world. Yet, the same trend in financing with a concentration around *murabaha* (trade financing) is found to intensify. Equity participation and profit sharing have remained distant minimum in the total allocation of resources. Secondary financial instruments in accordance with the *Shari'ah* could not be developed so as to give rise to a viable

<i>Faisal Islamic Bank of Egypt</i>	
Industry	30.6
Trade	30.4
Agriculture	3.0
Other sectors	36.00
Total	100.00
<i>Dubai Islamic Bank</i>	
Trade	90.6
Services and family	7.6
Other sectors	1.8
Total	100.00
<i>Sudan Islamic Bank</i>	
Agriculture	34.0
Industry	23.5
Trade	10.8
Transportation	10.0
Other sectors	21.7
Total	100.00
<i>Faisal Finance Institution Inc. Turkey</i>	
Metal industry	26.3
Chemical and petroleum	17.8
Clothing	16.7
Food	7.9
Tools	5.7
Paper and printing	5.3
Agriculture	16.9
Contracting	3.4
Total	100.00
<b>Source:</b> IAIB (1998)	

**Table III.**  
Sectoral allocation of investment of Islamic banks (percentages of total financing) 1988

Islamic capital market. Islamic financial instruments are therefore traded in conventional stock markets. As a result, neither the developmental aspects of Islamic banking in favour of realizing an Islamic economy nor the distributive goals for the poor and marginal enterprises could be attained.

*Bank Islam Malaysia Berhad*

Bank Islam Malaysia Berhad (BIMB), one of the most progressive Islamic banks in the world today, quoted the following proportions of their *mudarabah* and *musharakah* funds (BIMB, 1994). *Mudarabah* financing stood at 0.21 per cent of the total financing in 1993 and 0.34 per cent in 1994. *Musharakah* financing stood at 1.85 per cent and 1.81 per cent, respectively, for the same years. These funds held by shareholders did not involve any active stakeholding and participation in decision-making except for major shareholders. The bank acted as management participant, *mudarib*, on behalf of its customers to make all decisions singly. Thus a principal-agent relationship existed in financial management and decision-making. *Mudarabah* and *musharakah* became a sleeping partnership in financial contracts between the clientele and the bank (Choudhury, 2001).

*Al-Rajhi*

In the case of Al-Rajhi banking and Investment Corporation in Saudi Arabia, Islamic banking services have shown good share values in its various Islamic financial instruments. This is indicated by their appreciating unit values. As shown in Table IV for Al-Rajhi banking services, unit shares of all funds increased within the span of a mere single week. Yet the condition behind all these instruments is their nature of fixed deposit without dividends allowed to be withdrawn in the short-term (Al-Rajhi Banking & Investment Corp., 2001).

In April 2001, Al-Rajhi Islamic banking service posted 17.5 per cent increase in its profits over the first quarter a year ago. Equity shareholders' capital increased by 8 per cent, that is to Saudi riyals (SAR) seven billion. Customer deposits rose to SAR 37 billion and operating revenue stood at SAR 904 million.

Al-Rajhi has much of its Islamic funds in fixed deposits revolving around several kinds of Islamic financing instruments. Fixed deposits although good for affluent investors, who do not need to cash off in the short run, are not conducive for the marginal depositors and enterprises. Financial needs and exigencies affect marginal clientele continuously over the short run, particularly in financial markets and the economy that have become volatile these days. Hence a good degree of liquidity should

Name of fund	(This week)	Unit price (Last week)
Commodity <i>mudarabah</i> fund	\$1,580.73	\$1,579.31
Local shares fund	SR3,651.81	SR3,636.02
Global equity fund	\$139.98	\$138.37
Fund for Egyptian shares	\$55.60	\$53.65
Middle East equity fund	\$92.69	\$91.08
Balanced fund-1	\$1.1129	\$1.1079

Source: Al-Rajhi Banking & Investment Corp. (2001)

**Table IV.**  
Al-Rajhi Islamic banking  
services: current unit  
price

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be available to marginal depositors upon demand. Flexibility of cashing off without penalty to depositors should mark the feature of such funds. This would establish one of the conditions of the *Shari'ah*, which is easy access to property rights by the needy depositors.

It is also found that some of the unit values are too high and may preclude small-scale investors from enjoying such financial instruments. It might be good to think of diversifying the large unit value shares into shares of smaller ones with affordable unit values. The result would be both product and risk diversification without diminution in the total unit value of shares. A good area to so diversify the shares is unit trusts with sectoral diversification. Linkages between sectors can then be generated by means of the Islamic financing instruments as a sign of economic development.

#### *Islami Bank Bangladesh Ltd*

The Islami Bank Bangladesh Ltd (IBBL) is one of the most successful and prominent of Islamic banks in the world. From a cursory examination of its performance data we can deduce the level of popularity and financial stability of IBBL. Much of the information given below is sourced from Rahman (2001).

Table V gives the ranking of IBBL with respect to selected prominent private sector banks in Bangladesh. The level of popularity of IBBL can be deduced from her significantly highest volume of deposits. The highest volume of investment made by IBBL shows the effective mobilization of the deposits into productive outlets rather than holding them in the form of liquid saving. Consequently, the investment/deposit ratio is the second highest. Her financial productivity measured by income/employee is near to the highest. It is also found that the highest volume of investment results in attractive dividends out of total income. This aggregate figure on investment as resource mobilization over-rides a slightly lower investment per branch. This consequence shows up in a slightly lower net profit level. But such an indicator is a signal to the common shareholders' well-being that IBBL keeps in view. Despite the lower retained income after dividends are declared, this indicator of popularity of IBBL does not result in lower incomes, which is seen to be near to the highest level. The popularity and competitive position of IBBL is also pointed out by her number of branches, which is higher than all other banks. Total employment figure is therefore the highest, although manpower per branch is the lowest. But when tallied against the investment per branch, the technical efficiency (investment per branch/manpower per branch) is the highest. This again reflects the highest technical productivity level of IBBL of all the other banks compared with. The highest efficiency level of IBBL is shown by her lowest cost of fund per branch, which over-rides the slightly higher total cost of fund. This again is an indicator of client-friendly banking procedures, which increases the popularity of IBBL among clients, especially among the microenterprises in Bangladesh.

#### *International consortium of Islamic banks*

On the financial stability indicators we find that total assets of IBBL increased at a handsome steady rate (Table VI). Likewise, in comparison with several banks IBBL's statutory reserve is sound (Table 5). Revenue stream and equity streams are likewise competitive (Table VI).

No.	Particulars	IBBL	NBL	ABBL	UCBL	CBL
		(Taka in million)				
1	Paid up capital	318	391	373	230	1,602
2	Statutory reserve	282	321	286	191	263
3	Investment loss offsetting reserve	539	Nil	Nil	75	Nil
4	Normal capital	1,429	1,020	743	496	172
5	Provisional short-fall	Nil	342	Nil	493	584
6	Adjusted capital	1,429	677	743	3	(412)
7	Total deposit	16,557	15,036	10,506	9,187	8,500
8	Total investment	13,095	12,364	6,742	5,152	5,820
9	Investment per branch	131	187	118	65	77
10	Investment deposit ratio (per cent)	79	82	64	56	68
11	Total income	1,368	1,456	1,049	887	918
12	Income per employee	72	78	68	45	49
13	Cost of fund	838	756	575	461	453
14	Establishment expenditure	360	425	335	306	289
15	Total expenditure	1,198	1,181	910	767	742
16	Cost of fund per branch	8	11	10	6	6
17	Net profit	170	275	139	120	251
18	Dividend	21 per cent	Nil	10 per cent	Nil	Nil
19	F. Ex. business imports	17,370	18,082	9,114	10,176	6,180
20	F. Ex. business exports	14,469	12,651	5,181	4,529	1,450
21	No. of branches	100	66	57	79	76
22	Total manpower	1,903	1,856	1,540	1,948	1,855
23	Manpower per branch	19	28	27	25	24

**Notes:** BIBB: Al-Baraka Investment Bank of Bahrain; FIBB: Faysal Islamic Bank of Bahrain; DIB: Dubai Islamic Bank; JIB: Jordan Islamic Bank; BIMB: Bank Islam Malaysia Berhad; BIB: Bahrain Islamic Bank; IBBL: Islamic Bank Bangladesh Ltd.; FIBE: Faysal Islamic Bank of Egypt; KFH: Kuwait Finance House; QIB: Qatar Islamic Bank

**Source:** Rahman (2001)

**Table V.**  
IBBL *vis-à-vis* private  
sector banks in  
Bangladesh (as on 31  
December 1997)

We turn next to many such Islamic banks, which together have performed with sound financial stability and have been popular among their clients. Table VI shows that except for some volatile movement in deposits for BIBB, in deposits, equity, assets and revenue for FIBE and BTFH, most other Islamic banks have recorded medium to healthy growth in all the critical financial indicators.

Finally, Table VII shows that the Rate of Return on Assets and the Rate of Return on Equity have both been significantly positive and on an increasing trend between 1990 and 1998. These figures being positive, they indicate that Islamic banks internationally are fairly solvent.

### *The Islamic Development Bank*

In recent times, the Islamic bank financing concentration in foreign trade has continued because this instrument was found to be the most profitable and attractive by its low risk. Foreign trade financing comprised 72 per cent of total financing of IDB on a cumulative basis between 1976 and 1995. Of this, much was on short-term trade financing. Long-term trade financing comprised a mere 2.87 per cent of total trade financing between 1976 and 1995. Yet foreign trade financing instrument is not of a developmental type. Dependence upon imported goods and inputs from non-Muslim

**Table VI.**  
Annual growth rates for  
some key variables of  
selected Islamic banks  
(1990-1994 and  
1994-1998)

Bank	Total equity			Total deposits			Total investment			Total assets			Total revenue		
	1990-1994	1994-1998	1990-1998	1990-1994	1994-1998	1990-1998	1990-1994	1994-1998	1990-1998	1990-1994	1994-1998	1990-1998	1990-1994	1994-1998	1990-1998
RBIC	7.7	7.5	7.6	13.9	7.7	10.8	12.0	7.3	9.6	11.8	7.1	9.4	0.5	11.2	5.7
KFH	14.4	21.0	17.6	2.7	3.3	3.0	9.9	6.2	8.0	4.2	6.2	5.2	11.2	11.8	11.5
BIBB	0.2	3.1	1.6	-12.2	5.5	-3.8	-10.5	3.8	-3.6	-9.3	5.1	-2.3	14.9	23.3	19.0
BIB	17.6	2.4	9.7	5.8	4.6	5.2	7.1	4.5	5.8	6.7	4.5	5.6	-2.0	11.9	4.7
FIBB	16.3	5.4	10.7	5.2	4.3	4.7	4.3	4.8	22.6	31.4	-8.8	9.5	23.9	2.8	12.8
FIBE	-15.2	12.2	-2.4	-2.4	5.6	1.6	4.5	9.3	6.8	-1.2	5.1	1.9	-13.8	17.1	0.4
DIB	8.0	34.1	20.3	17.0	6.9	11.8	12.2	9.7	11.0	13.8	9.2	11.5	14.4	8.6	11.5
JIB	32.2	6.4	18.6	22.0	5.2	13.3	21.2	6.5	13.6	21.9	5.1	13.2	17.8	0.6	8.9
QIB	-1.3	11.9	5.1	6.2	4.1	5.1	10.4	3.6	7.0	11.7	4.1	7.8	2.9	12.5	7.6
IBBL	12.1	25.2	18.5	18.5	13.4	15.9	21.4	9.3	15.2	18.8	13.3	16.0	12.0	14.0	13.0
BIMB	24.1	30.8	27.4	21.1	-2.4	8.7	21.7	1.3	11.0	21.5	3.3	12.0	19.9	7.6	13.6
BTFH	-12.1	35.4	9.1	20.1	9.8	14.8	14.8	12.0	13.4	10.0	10.7	10.4	49.9	-27.9	4.0
Simple av.	8.7	16.3	12.0	9.8	5.7	7.6	10.7	6.5	10.0	11.8	5.4	8.4	12.6	7.8	9.4
Wt. av.	7.9	12.6	10.2	8.8	5.7	7.2	11.3	6.9	9.1	9.3	6.4	7.8	11.2	3.7	7.3

**Notes:** BIBB: Al-Baraka Investment Bank of Bahrain; FIBB: Faysal Islamic Bank of Bahrain; DIB: Dubai Islamic Bank; JIB: Jordan Islamic Bank; BIMB: Bank Islam Malaysia Berhad; BIB: Bahrain Islamic Bank; IBBL: Islamic Bank Bangladesh Ltd.; FIBE: Faysal Islamic Bank of Egypt; KFH: Kuwait Finance House; QIB: Qatar Islamic Bank  
**Source:** Rahman (2001)

	ROA		ROE	
	1990-1994	1994-1998	1990-1994	1994-1998
RBIC	3.8	3.7	25.9	25.6
KFH	0.4	2.2	6.6	29.3
BIBB	1.2	2.4	3.6	7.3
BIB	0.9	1.1	10.8	11.1
FIBB	5.45	4.9	16.8	15.9
FIBE	0.2	0.1	3.7	1.3
DIB	0.5	0.6	8.7	8.5
JIB	0.9	0.8	19.2	11.3
QIB	0.4	1.1	-2.3	16.4
IBBL	1.4	1.4	32.9	28.8
BIMB	1.1	0.9	13.2	13.2
BTFH	1.8	1.3	42.9	38.3
Simple average	1.9	2.3	19.9	22.1

**Notes:** BIBB: Al-Baraka Investment Bank of Bahrain; FIBB: Faysal Islamic Bank of Bahrain; DIB: Dubai Islamic Bank; JIB: Jordan Islamic Bank; BIMB: Bank Islam Malaysia Berhad; BIB: Bahrain Islamic Bank; IBBL: Islamic Bank Bangladesh Ltd.; FIBE: Faysal Islamic Bank of Egypt; KFH: Kuwait Finance House; QIB: Qatar Islamic Bank

**Source:** Rahman (2001)

**Table VII.**  
Percentage rate of return  
on assets (ROA) and rate  
of return on equity (ROE),  
Islamic Banks  
Internationally,  
1990-1998

countries can increase the debts of importing countries. This problem was in fact noted with the foreign trade portfolio of IDB during the 1980s. In spite of the concentration of IDB financing in foreign trade, inter-communal trade among the member countries is a mere 9-10 per cent of their global trade for many years now. Member countries' global share of trade was a mere 7 per cent in 1995.

Over the 20 years period, 1976-1996, IDB had financed only three profit-sharing projects. Financing in these comprised only 0.15 per cent of total project financing (IDB, 1996). Recently, IDB has established a number of co-operative projects with Islamic banks. The emerging Islamic Banks' Portfolio for Investment and Development is a fund jointly established by IDB and Islamic banks along with other participants. Between 1988 and 1996, a total of US\$100 million was allocated in syndicated operations. IDB's participation was 24.5 per cent. Islamic banks' portfolio comprised 8.7 per cent. IDB's Unit Investment Fund comprised 5.8 per cent. Pension Funds comprised 3.5 per cent. Other Islamic banks held 57.5 per cent of their assets in this portfolio. Such syndicated operations have been opened up in only two countries, Pakistan and Egypt, and then too they comprise only lease and trade financing operations. It had only 5.5 per cent of total IDB financing between 1976 and 1995. Participation in Islamic banks' portfolio is of a shareholding type, that is *mudarib* type, whereby IDB acts as the manager of the Islamic banks' portfolio.

### Inferences drawn

From the quantitative picture given above it is clear that Islamic banks have done well in being profitable institutions towards maintaining the liquidity position of their depositors and shareholders. Yet the element of socio-economic development and a better prospect for diversification of project financing instruments is lacking. Consequently, the full impact of Islamic banks in development financing and in

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establishing sustainability of an Islamizing community remains a potential. Social well-being of the type we have explained in this paper in terms of measuring and directing *Tawhidi* based complementary relations among the *Shari'ah* recommended possibilities, needs more extensive networking and linkages between the financial and socio-economic development goals in accordance with the tenets of the *Shari'ah*.

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### Conclusion

We have noted in this paper that Islamic banking in accordance with the *Shari'ah* precepts is a landmark in new paradigmatic thinking interrelating finance, economy, community and society. Islamic banks are therefore to carry out their operations and organize their plans and programs according to such a general systems outlook of finance with socio-economic development. It would then combine the goals of economic efficiency (growth) and social justice into complementary relations with each other. Such a model of socio-economic development is very different from the financial, economic and social models we are facing in the present age of capitalist globalization. To achieve the complementary goals and so actualize well-being for all, Islamic banks ought to focus on both financing as well as development in accordance with the tenets of the *Shari'ah*. We have laid down this perspective in this paper.

We have also noted that Islamic Banks worldwide have done fairly well in terms of their financial stability and popularity among clients. In accordance with the arguments of this paper respecting the complementarities between economic/financial efficiency and social perspectives, the simultaneously good performance on the popularity indicator and financial stability brings out this point of the well-being objective of Islamic banks measuring such complementary relationship. This is a most powerful implication of the unity of knowledge in systems according to the *Tawhidi* paradigm that we have presented.

These are indications that there is a rich premise for the normative principles of ethics and values emanating from Islam to be incorporated in the matters of money, finance, accountability and the real economy. In the context of volatile capital markets it is all the more necessary to start thinking of and organizing along lines of the money, finance and real economy linkages within corporate and national accounting systems. Such a bold experiment could save the prevalent equity markets from the vagaries of short-term interest-based fluctuations and the jitteriness of investor and consumer preferences. In recent times, volatile preferences have pervaded capital markets in terms of uncertain capital movements across risky portfolios of securities, shares and bonds yielding low rates.

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