**Islamic Financial System: Fiction or Possibility**

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Recently, there has been much commotion about the rapid expansion of the Islamic Banking system and the introduction of Islamic Financial tools in Pakistan. Islamic financial system is not at the heart of the banking system in Pakistan despite its popularity and many still argue about its legitimacy. However, what has never been explored is if it truly is the solution to Pakistan’s poor financial management or whether a solution at all.

A simplistic description of the Islamic financial system as “interest-free” is inaccurate and tends to cause confusion. While barring the receipt and payment of interest is the core of the system, it is backed by other Islamic doctrines promoting the rights and responsibilities of individuals, property rights, equitable distribution of wealth, risk-sharing, obligation fulfilment, and contract purity. In addition to prudent and sound regulations, the Islamic financial system also encompasses insurance, capital production, capital markets, and all forms of financial intermediation, implying that moral and ethical considerations must be incorporated into the regulatory framework.

The Islamic finance industry has expanded rapidly over the past decade, growing at 10 to 12 per cent annually. Today, Sharia-compliant financial assets are estimated at roughly US $2 trillion, covering bank and non-bank financial institutions, capital markets, money markets and insurance (“Takaful”).

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The conceptual basis of an Islamic financial system transcends the interaction of production variables and economic behaviour. Only in the framework of Islam’s teachings on business ethics, wealth distribution, and social and economic justice, which are at the heart of a moral economy, can the Islamic financial system be completely understood. Whereas the conventional financial system focuses primarily on the economic and financial aspects of transactions and their material outcomes, the Islamic system places equal emphasis on the ethical, moral, social, and public interest dimensions in order to promote equality and fairness, as well as the role of the state.

The core of this system lies in the ethical economy, which according to the article on Islamic Financial System by Zamir Iqbal, a World Bank publication, can be understood through the following objectives:

. To be true to the Shari’ah principles of equity and justice;

. Should be free from unjust enrichment;

. Must be based on the true consent of all parties and

. Must be an integral part of a real trade or economic activity such as a sale, lease, manufacture or partnership.

There are endless benefits of a truly implemented Islamic financial system. The sustainable development of Islamic finance supports economic growth, poverty reduction, and the promotion of shared wealth. Due to its direct connection to tangible assets and the real economy, Islamic finance can contribute greatly to economic growth. Utilizing profit-and-loss sharing arrangements encourages the supply of financial assistance to productive firms that can improve output and create jobs. The emphasis on tangible assets discourages financial speculation by ensuring that the industry supports only transactions with a meaningful purpose. Islamic finance promotes the growth of the financial sector and increases financial inclusion. By broadening the scope and availability of financial goods, Islamic finance could improve financial access and promote the inclusion of individuals without access to financial services. Islamic finance stresses partnership-style financing, which could be effective in increasing the poor’s and small firms’ access to capital.

These are extremely desirable benefits for Pakistan to reap, but given the true pre-conditions of establishing a desirable environment for the Islamic Financial Management System, it might be unlikely. The truth about Pakistan’s economy is known to all, whether politicians, economists or bankers. We operate under a system that is largely undocumented; our Shari’ah compliance is under a huge question mark, and unjust enrichment is embedded in our business practices. Unfortunately, the possibility of introducing active and effective Islamic Financial Management in Pakistan is a distant dream. The absence of a suitable environment has been a significant barrier to the realization of the objective of an interest-free economy. Unfortunately, little has been done by the government or public figures to create an ideal or almost ideal Islamic environment.

An inflation-free economy is a crucial aspect of the perfect environment. Inflation erodes the real value of money, so a person who lends a sum of money and receives the same amount back one year later has actually lost money. Deficit financing is a primary cause of inflation. The devaluation of the public’s currency as a result of the printing of notes to cover a budget deficit is, in fact, an injustice to the public. In this regard as well, the government’s performance is dismal. Government borrowings at high-interest rates have reached an unsustainable level, as have the government’s domestic and foreign debts. In addition, no effort has been made to modify the taxation structure in accordance with Shariah.

Even though the publications across major financial institutes such as the World Bank and Asian Development Bank are hugely in favour of the Islamic Financial model to reap the benefits of this rapidly growing industry. In essence, the Islamic Financial Model can not be truly implemented without creating a social and economic structure that is based on the principles of ethical economics.

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