TOWARDS A JUST MONETARY SYSTEM

FOREWORD

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Not long ago Islam's prohibition of interest (riba) was generally regarded as an almost impossible proposition - even among most Muslim intellectual circles. The situation has changed dramatically over the last few decades. The intellectual as well as the institutional hegemony of interest has been challenged, particularly by Muslim scholars and economists. There is a greater flow of literature on the subject, showing substantial increase in quantity as well as quality. Moreover, the debate is no longer confined to theoretical argument; there is now a rich and expanding tradition of experimentation and institution-building. The monetary economics of Islam is beginning to come of age.

Looking back over the last fifty years, one can discern at least three somewhat distinct phases in the development of the discipline. It was during the mid-thirties that, among others, some of the 'ulama' (Islamic religious scholars) - who, though they had no formal training in economics, yet had a clear grasp of the socio-economic problems of the age and Islam's approach towards them - addressed themselves to the problems of interest. They brought a fresh approach to the subject, distinct from the modernists and apologists who were trying to explain away Islam's injunctions about interest. Instead of changing the Islamic teachings to suit the current practice, these scholars boldly reaffirmed the Islamic position, without making any compromises, and invited Muslim economists and bankers to strive to change economic institutions in order to achieve conformity with Islamic norms and principles. Some Muslim economists and bankers responded to this clarion call but their efforts were of an elementary nature and their impact limited. Nevertheless, a new opening was made.

This led to the second phase in which, over the last twenty years, Muslim economists have applied themselves more rigorously to developing certain aspects of the monetary system of Islam. An economic analysis of the Islamic rationale for the prohibition of riba was expounded and the major contours of an alternate system of banking and finance free from riba were delineated. Significant contributions in the field were made at the First International Conference on Islamic Economics held at Makkah in 1976, the International Conference on Islam and the New International Economic Order held in London in 1977, the two seminars on Monetary and Fiscal Economics of Islam held at Makkah (1978) and Islamabad (1981), the conference on Islamic Banking and Strategies for Economic Cooperation held in West Germany at Baden-Baden (1982) and the Second International Conference on Islamic Economics held at Islamabad (1983). Over a dozen books and monographs have been produced containing papers and discussions emerging out of these conferences and seminars. Perhaps the most significant intellectual-cum-operational contribution has been made by Pakistan's Islamic Ideology Council which, on the basis of a Report of its Panel of Economists and Bankers, has produced the first comprehensive and systematic blueprint for the elimination of riba from a modern economy. In the opinion of the present writer, this report represents the high point of contemporary Muslim contributions towards developing a model of an interest-free economy. It is also a consummation of the original work done by Muslim economists during this period.

A parallel development during the last decade represents the third phase and consists of efforts to develop interest-free banking and financial institutions in the private as well as the public sector. Presently thirty-eight banks and financial and investment institutions are operating on an interest-free basis in three continents: Asia, Africa and Europe. At least two of these institutions, Islamic Development Bank, Jeddah, and Darul Mai al-Islami, Bahamas and Geneva, are operating multi-nation ally. Though they are very young and they still have a long way to go, these institutions are a living vindication of the Islamic theory of finance.

Islamic monetary economics is now entering its fourth phase which calls for a more integrative as well as a more critical approach to the entire theory and practice of money and banking in Islam. The pioneers have blazed the trail, but now is the time to seek for greater refinement and sophistication. The economists are faced with the challenging task of reviewing the whole situation in at least three areas.

Firstly, to bring together the work done by different economists into a comprehensive view of the monetary system of Islam in its fullness, as against concentrating on specific, sometimes even disjointed, elements of money and banking. The time has come to distinguish the wood from the trees.

Secondly, to review critically the different models of Islamic banking presented over the years in the context of the practice of Islamic banking with a view to refining the theory as well as improving the practice. Now is the time to test the theories and to examine and evaluate the emerging institutions against the touchstone of the objectives of Islamic banking and finance.

Thirdly, it is essential to put the whole theory and practice of Islamic banking in the perspective of an Islamic economy and the Islamic moral and social order. Any element of the Islamic system, however important, cannot produce the desired results, if it is allowed to operate in isolation. It must lead to other complementary changes to complete the process. Elimination of ribd is only one aspect of the Islamic economic programme. It must be accompanied by, and strengthened through, other motivational and structural changes. Islamic banking is only a part of the process, and not the be-all and end-all of the process.

This integrative and critical approach will lead to the development of a comprehensive theory of Islamic monetary economics. Many gaps in knowledge and practice have also to be filled and new ideas experimented with, refined and perfected. It is in this context that I welcome the present work of my brother and colleague, Dr. Muhammad Umer Chapra, Towards a Just Monetary

System. In my humble view, if the Islamic Ideology Council's Report on the Elimination of Interest from the Economy is the crowning work of the second and third phases, Dr. Chapra's treatise heralds the beginning of the fourth phase. I deem it a privilege to contribute this foreword to his pioneering work and take genuine pride in presenting this book in the Islamic Economics Series of the Islamic Foundation.

Muhammad Umer Chapra is an eminent economist and a committed Islamic scholar. In him one can see the approximation to the new model of Islamic scholarship, wherein the modern and the traditional streams of knowledge embrace each other. Educated in Karachi (M.Com.) and Minnesota (Ph.D), he has the best from the modern centres of economic learning. He has worked hard, very successfully, to acquire a command of Arabic and study Islam from the original sources. He has served in many important teaching and research positions. He taught Economics as Assistant and then Associate Professor in America, and worked as Senior Economist, Pakistan Institute of Development Economics and Reader (Associate Professor), Central Institute of Islamic Research in Pakistan. For the last nineteen years, he has been working as Economic Adviser to the Saudi Arabian Monetary Agency. His experience thus covers a broad range of teaching, research and policy-formulation. Monetary economics has been his specialisation. He has participated in a large number of international conferences, including most of the conferences and seminars on Islamic economics and finance and has contributed significantly on these occasions. Towards a Just Monetary System represents the sum and substance of his thinking and contributions on the subject to date.

In my view, this book is unique in many respects. First, it is the first comprehensive and integrative study of the Islamic monetary system, presenting the whole mosaic and not merely some of its pieces. It also puts the monetary economics of Islam in its proper perspective. In this respect it fulfils a great need and constitutes an antidote to some ill-placed complacency that might have shown in Islamic circles. It not only restates the Islamic position on money, banking and finance in a precise, comprehensive and authentic manner, but also identifies the gaps in some of the prevalent approaches. It is also a timely warning against piecemeal approaches. Dr. Chapra's emphasis on structural change, on the need to cleanse economic life of all forms of exploitation and inequity and on the interdependence of different elements of the Islamic scheme of life is not only a timely reminder but also constitutes a powerful agenda for future reform and reconstruction.

The second characteristic of this work is its integration of theory with practice. Dr. Chapra has very ably developed the Islamic rationale of the prohibition of riba and has demonstrated with academic rigour not only the viability but the superiority of the equity-based financing system. He has not only critically reviewed the current Islamic banking but has also come up with original suggestions to improve it and to enable it to achieve Islamic objectives more effectively.

Thirdly, the book has raised the level of debate on Islamic monetary economics by rigorous analysis of some key concepts, by a critical evaluation of some of the new ideas developed during the last decade and by presenting some new insights and policy-relevant suggestions. In this respect, I would particularly invite the reader to his discussion on joint stock company, on the reform of the stock-exchange system, on government borrowing needs and on non-bank financial institutions. His idea of a deposit insurance corporation and investment audit corporation deserve to be examined seriously. His evaluation of some of the proposals of the earlier-mentioned Islamic Ideology Council's Report has enriched the debate. His views on credit creation and indexation merit very serious consideration although this cannot be treated as the final word and some of us may continue to show sincere reservations.

Finally, I regard the two appendices as extremely valuable contributions. The first on 'Riba in the Qur'an, Hadith and Fiqh is not only a masterpiece of scholarship but a statement that should finally settle the controversy on what constitutes riba. The second on ‘Mudarabah, Shirkah and the Corporation would serve as an invaluable groundwork for those economists who do not have access to the sources. The concepts have been so clarified that they can be used as building blocks for developing new business institutions in an Islamic economy in the form of new combinations and permutations.

While the book covers a vast area in monetary economics, the discussion on international monetary relations and how to cleanse them of riba and other forms of exploitation requires to be developed, strengthened and expanded in many respects. I am sure Dr. Chapra and other Muslim economists will continue to face the challenge that comes from the world monetary system and develop more vividly the vision of an international monetary system that is free from riba and leads to the emergence of a just world economic order.