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ECONOMIC RESEARCH CENTER
FOR MIDDLE EASTERN AND ISLAMIC COUNTRIES
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SYMPOSIUM ON
ORIENTATION IN ISLAMIC ECONOMICS

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MARMARA ÜNİVERSİTESİ YAYINEVİ

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MARMARA ÜNİVERSİTESİ YAYINEVİ

SYMPOSIUM ON ORIENTATION IN ISLAMIC ECONOMICS

Edited by Dr. Mustafa AYKAÇ

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EDITOR'S INTRODUCTION

For about 14 centuries, Islam, making up the most important basis of individual and society for consciousness and identity in islamic societies has offered a social, political and economic order humanity. The idea, that politics, economics, law and society constitute an inseparable totality in Islam, has been a very important fact. Both for worshipping to Allah and arranging their relationship with other people, Muslims have acted in accordance with the principles of the holy Koran's and Prophet's practice of life. As a result, a law and a series of rules with very a high standard and coverage have developed. Islam, establishing individual and social life on the basis of the holy revelation, has emphasized on the need for a class of scholars, who will read and interpret the Koran, in both theory and practices.

Throughout the 20th century, Muslims scholars, faced intensive challenges from West, have turned their focus to the islamic roots for resructuring their view of the world. The economic success of western societies and the very level they have reached have effected deeply Muslims scholars. This prompted them for new searches. In the field of economics, stressing on the importance of clearly distinctive and much superior aspect of Islam regarding individual and social life has become one of the significant purposes. This, on the one hand, will contribute to the Muslim's atempt to regain their self-confidence, it will, on the other hand, help to abate the crisis of Western thought and life style.

It can be said that the endeavor to put the Islamic economic thought and the system on the agenda of the Islamic World has given its fruits in a very short time. This started initially as a simple and modest trial, but it has become widespread throughout the Islamic world nowadays. This is a significant source of richness and an alternative for the world economic literature. The symposium on 'Orientation in Islamic Economics' was held by the participation of distinguished scholars, who have substantially contributed to this field, from Turkey and other countries. During the symposium new subjects and developments were discussed. Along with the researchers and writers who presented paper, those who participated in the discussions considerably contributed to the symposium. However, in this book we are only able to include the papers presented. These papers which analyze the Islamic economics with its aspects such as zekah, finance, insurance, corporation and common market, economic growth, labour and work are going to be a significantly illuminating source for academics, researchers and practitioners.

Dr. Mustafa AYKAÇ

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FOREWORD

The symposium on "Orientation in Islamic Economics", organized by our institute in collaboration with the Islamic Research and Training Institute of the Islamic Development Bank was held on 20-28 October 1994 with the participation of many distinctive academicians and researchers.

The researchers created an useful scientific milieu. Publishing these papers and discussions as a book and disseminating the discussed topics to a large body of readers are significant. This is the aim of this publication.

In the realization of this conference, the chancellor of the University of Marmara, Prof. Dr. Ömer Faruk Baturel had a significant share. The realization of his conference at the international level was made possible by the generious contribution of Islamic Research and Training Institute of Islamic Development Bank. I would like to thank to Prof Haşmet Başar for not only spending much effort to develop the idea of organizing this conference, but also to accomplish it.

I would like to appreciate the contributions of Assoc. Prof. Dr. Mustafa Aykaç, Assoc. Prof. Dr. Kamil Uslu and Prof. Dr. Ömer Dinçer in organizing the symposium.

I would like to acknowledge the contribution of the Metropolitan Municipality of Istanbul and MUSIAD considerably to the realization of this conference and to Fehmi Akın for his close interest. Special thanks will go to Dr. Musafa Aykaç for editing this volume.

I would like to thank to Fahri Solak and Yaşar Bülbül who coordinated the translation of the papers and to Dr. Adnan Büyükdeniz, Erol Özvar, Şaban Bıyıklı, Tahsin Özcan, Hakan Büyüktuna and Yaşar Bülbül who translated the papers.

Finally, I also would like to express my deep gratitude to the research assistants who participated either as organizers or participators and to other participants. I would like to thank to Kalibre Graphic and Cihat Torun who urgently published the book by offsetting the delay.

Prof. Dr. Ahmet Tabakoğlu
Director of Institute
of Middle Eastern and Islamic Countries

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KEYNOTES SPEECH-I

Mr. Director, Distinguished Guests

On behalf of Marmara University, I warmly welcome all of you to the Seminar and our fabulous city of Istanbul. It is a pleasure for us to host such meeting jointly organized by our Institute of Middle Eastern and Islamic Countries and the Islamic Development Bank, Islamic Research and Iraining Institute.

Based on its honorable past and today's outstanding achievments, my University through hosting this seminar believes in contributing more Turkey's efforts to have better undersanding with the Islamic World and Policies.

Tracing the common origins of economic systems, it is argued that capitalism has the ethics based on christianity. Together with the importance of economic factors in the emergence of capitalism, ideas and beliefs embedded in protestanism had also considerable influence. In other words, understanding Protestant Ethics or Calvinism would be very helpful to access the basis of capitalism. The rationale was quite simple. Rational capitalist is concerned with "inner worldly asceticism." The properties and prerequisites of rational capitalism based on protestant ethic: The appropriation of the physical means of production by the entrepreneur, freedom of market, free labour, a commercialized economic life, rational technology and rational law. In this system goverment only perpetuates law and protects individual right.

As oppesed this outlook, İslam, based on, balanced other worldly and inner wordly ascetism, does not allow to emerge capitalism. The linkage between inner and other worldly affairs impose constraints one's consumption and production decisions. The vast literature on Islamic Economics has been devoted to enlighten this linkage and distorsions caused by current economic systems. I feel confident that discussions in this seminar will be stimulating, challenging and fruitful in this respect. The issues debatable in this context should not be confined with and adopted as any unique country or regional policy matter. I'm convinced that this Seminar will be both profitable and valuable to all participants. Among the participants I would like to respect the pioneers of this field Prof. Sıddıki and Prof. Zaim.

I cordially thank once again my collegue Professor Tabakoğlu, and other sponsors who have contributed generously in the preparation of this friendly gathering and consider it a privilige to host you in our beatiful country which have roots venerable, ancient culture and which is on the other hand on the threshold of technical progress and industrial enterprise.

Let me extend to all of you a very cordial welcome and wish you much success and very pleasant stay in our splendid city.

Prof. Dr. Ömer Faruk Baturel
Rector of Marmara University

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KEYNOTES SPEECH-II

Mr Governor,
Mr. Mayor,
Mr. Director,
Dear participants, distinguished scholars, guests, ladies and gentlemens,

I would like to welcome you to the International Seminar on "ORIENTATION IN ISLAMIC ECONOMICS", organized by Marmara University- Institute of Middle East and Islamic Countries and IDB/Islamic Research and Training Institute.

We have all known that we are living in a world in which global capitalism is a dominant system. In such a world, unfortunately, the best position that could be attributable to the Islamic World is, if not slavery, at least dependency" to that capitalist system. This position of Islam naturally gives us the right to blame and thus criticize capitalism with the psychology of opposition.

Yes, we accuse of capitalism because of the fact that it is responsible for creating a world in total turbulence, continuous exploitation and resultant wars. Furthermore, this system has also dramatically alienated human beings to their nature and spiritual being.

Even a short picture of the present situation can easily highlight the point in agenda. Capitalism created a dual world. On the one side, we observe nations where massive deaths because of wide-spread starvation is prevailing, while, on the other side, a small minority is absorbing the natural resources of the world and wealth of nations. That is, they have established their existence to this exploitation in the world. That is why every movement towards independence and cooperation among the Islamic World is going to be repressed by "The New World Order", a system based on the scenarios for the continuation of such a system with the new alliances, including the famous ex-enemies such as Russia that western system created on purpose. The shameful story of Bosnia-Herzegovina, Palestine, Algeria and others is the practice of such a considerations.

As a result of this injustice hegemony all over the world has caused huge and continuously deteriorating gaps and differences at regional and national levels. Furthermore, environmental pollution has exploded, cultural heritage of nations was destroyed to a greater extent, dependency of under-developed countries on western technology and aid became dramatic.

Beyond all of these, coexistence of both inflation and unemployment, that is stagflation, characterized the economies that neo-classical economics has dominated. Contrary to their theoretical arguments, development within that paradigm became an unreal fancy.

As followers of Islam, we attribute the responsibility of all deceases to the western philosophy of economics. Therefore, we believe that it is not possible to get rid of these cri-

ses by making some simple changes in the hard-core postulates of the orthodox western paradigm of economics. It requires a total paradigm shift at the level of both ontology and epistemology.

But theoretically and practically, the potentiality of western civilization, fortunately, is unable to provide such an alternative because of, at least, two depiciencies of that system:

An alternative system that human kind needs today necessarily must possess the aim of universality. Western ideology, based on the continuous Darwinian quarrels, that is the "survival of the fittest", preserving a life of "jungle", can not generate such a universal values from the western philosophy because of its alienating, non-humanitarian and non-spiritual characteristics which can not replace and permeates the multiplicity of human kind.

In addition to that, regardless of the content of their paradigms and their promises, psychologically these characteristics can not be taken as a criteria because the repressed nations of the world will remember the heritage of this system based on the blood and the tears of the non-western nations.

This old and unfriendly civilization is going to be questioned in front of the hisbory, but the present job for such an hope to be realized is to offer an alternative with its unique characteristics. That Is Islamic Economics. But the statement of Islamic economics should not lead one to the mis-conceived idea that means Islamic capitalism. We have already declared the capitalism as an enemy of open society and market and thus, of course, can not be attributable to the Islamic economics.

Islamic economics as a projection of Islam is the only universal and ultimate framework of human kind which can offer a viable, feasible and rational and natural projects to the contemporary economic crisis that either secular economic orthodoxy fails to solve or even this theory created itself.

What we hope to do in this symposium is this. I believe that this seminar will be an initiative and creative extension of this era. In fact, One of the responsibilities of Islamic Scholars is to provide this horizon to the world "mazlums" that is the repressed nations.

On the behalf of my institute, would like to welcome you again. I should thank to some distinguished instutions for their benevolence financial helps. These are, among others, Islamic Development Bank, Musiad, Kuveyt-Türk Evkaf Finans Kurumu, Al-Baraka Türk, Faisal Finans. Finally I should present my unlimited thanks and respeds to the persons, academicians and research assistants from the several departmants of our universities, particularly, Marmara University, and to the overseas paracipant scholars.

There are several our friends that spent their valuable and limited times for the realization of this ptoject. We are unable to mention their names separately. If they would not help, this project could not be realized. The names of all the contributians will be kept in the collective memory of the next generations and recorded to be remembered hereafter as well.

Thank you very much.

Prof. Dr. Ahmet Tabakoğlu
Director of the Institute
of Middle Eastern and Islamic Countries

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DEVELOPMENT OF THEORY OF ISLAMIC ECONOMICS

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Introduction

Economics of Islam must by definition be as old as Islam. But Islamic economics refers to a discipline which emerged in the middle of the twentieth century. In this lecture we do not trace the develolopment of Islamic economics as a whole[1]. Rather this lecture focuses on development of the Theory of Islamic economics during the last half century.

A theory captures the essentials which help man understand a particular aspect of reality. A theory of Islamic economics comprises those concepts and precepts which mark out its domain from the rest of Islamic studies, e.g. Islamic law, Islamic history, etc. Simultaneously it also serves to project the distinctive identity of Islamic economics within economics so that it can be distinguished from capitalist (neoclassical) or socialist (Marxsian) economics. A theory of Islamic economics is a tool for organising the material available to Islamic economist, both positive and normative. It has criteria for excluding what is not relevant and including what is relevant to the discipline of Islamic economics. Lastly, a teheory of Islamic economics is not only a guide to its past and present It is also the scientific route to its future. It provides us with a framework within which Islamic economics is likely to grow and the directions in which its current research priorities are likely to take it.

As we proceed to study development of theory of Islamic economics we keep in view the functions noted above; viz

(i) distinguishing Islamic economics within Islamic studies,
(ii) distinguishing Islamic economics within economics,
(iii) offering criteria for exclusion and inclusion,
(iv) generating research priorities and indicating future direction.

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The core concepts and precepts performing these functions constitute a theory of Islamic economics. In Section One we spell out these concepts and precepts as presented in the early days of Islarnic economics. We relate them to each of the four functions noted above and formulate the theory as it stood at the end of the Nineteen Seventies. In section Two we trace the-development through eighties and nineties focusing on important new ideas and significant new activities. In the Third and last section we attempt looking into the future with its problems and prospects.

Section One, Theory of Islamic Economics: The Essentials

The concepts of property, enterprise and accountability and the precepts of moderation, sharing and caring stand out among the essentials the theory of Islamic economics comprises since its inception, They are rooted in the Quran and Sunnah. The same sources spell out the purposes which are to guide man in economic affairs. Then the Islamic scholars proceeded to search in other Islamic sciences like figh, usool figh, and Islamic history whatever unfolded the implications of or exemplified the implementation of these essentials.

Wheareas property and enterprise were to be natural, albeit reinforced by divine endorsement, accountability was instilled by faith. Economic agents were seen exercising ownership and making economic efforts concious of their obligation toward God and man. This awaraness -based on belief in God, His prophet, peace be upon him, and the life hereafter is seen as the distinctive characteristics of a "muslum" economic agent.

Moderation, sharing and caring about the weakc and the deprived were enjoined on every one who owned, acted or esercised the God-given powers and faculties. Some of these Islamic teachings found form in such Islamic institutions as Zakat and prohibition of interest. They were supposed to influence behaviour of all economic agents.

The state was perceived as the ultimate overseer in these respects. It was expected to devise policies leading to fulfillment of basic needs, lessening disparities and securing development.

A sincere commitment to Islamic beliefs and values chanced every thing in economics: consumption, production, exchange, distribution. Islamic economists though using conventional economic terminology averred that their connotations changed under influence of Islam. The more the influence on an economic agent the deeper the change. In this they sought to draw general support from early Islamic history, especially the first forty years after hijrah. They also proceeded to 'analyse' how Islam in operation will ease the human situation and solve econo-

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mic problems. Their study of economic reality as it existed focused on how man's disregard of moral values in general and the institutution of interest in particular resulted in undesirable consequences. In contrast they sought to projeck the economy "as it would be" if interest was abolished and moral values were adhered to.

Moral values such as truth, honesty, fairness, compassion and mercy conpled with such rules of conduct as moderation and avoidance of waste as well as laws like zakat, inheritance and abolition of interest and gambling provide a fremawork in wich Islamic economist evaluate their enviroment and seek to rearrange it.

Islamic Economics and Shariah Sciences

The same framework helps in identifying in the Islamic legal source in particular and the Islamic heritage (historical, cultural, etc.) in general what is relevant to Islamic economics. It is very important, for example, to know what constituted riba at the time Islam abolished it, only to enable the scholar to answer the pratical question: what constitutes riba in contemoprary transactions. This answer itself becomes very important when it is going to be the basis of a venture of far reaching consequences: devising a modern financial system free from riba (or, to put it differently, reforming the modern financial system so that it is freed of riba).

This example helps us understand how Islamics entered the world of shariah sciences only to come out with something unique. None of these traditional Islamic sciences can lay exclusive claim to an interest free banking model that Islamic economics presented. Neither can economics. The middle of twentieth century witnessed the emergence out of the old of something new. Though rooted in the old it was not there before.

The same is true of the entire discipline of Islamic economics.

Islamic Economics and Economics

Price determination by supply and demand as the core of the science of economics is acknowledged by Islamic economists as by anybody else. The same is the case with tools like indifference curves. But when it comes to maximisation of utility by consumers and maximisation of profits by entrepreneurs the situation changes. The main reason why this could not be accepted without qualification and reservations lay in the emphasis on moral values. It was rightly perceived that maximisation of private gain could sometimes conflict with dictates of morality. Sometimes moral considerations call for behaviour or policy different from the one derived on the basis of economic calculus.

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Since Islamic economics envisaged economic agents under influence of moral values they refused to accept analysis based on the assumption of 'economic man' as valid for all times and places. That the analysis did apply some times to some places nobody disputed. In this manner Islamic economics envisaged economic behaviour and economic policy inspired by morality which served two distinct purposes. Firstly it indicated what ought to be / was likely to be, as more and more economic agents internalised Islamic values. Secondly it provided a moral critique of modern economics by comparing and contrasting the expected results of morally inspired economic behaviour and policy.

That seems to be the distinctive feature of Islamic economics. Its focus is on problems with a moral side to them. Even though every economic problem is amenable to study by Islamic economics, it is where morality is involved that it has special contribution to make. Within the discipline of economics, Islamic economics is distinguished by its emphasis on morality.

Principle of Inclusion and Exclusion

Once the place of Islamic economics in relation to Shariah sciences and economics is understood it is possible to evolve criteria for identifying what belongs to Islamic economics and excluding what does not belong to it. Let us take for example Zakat. It is an important subject in Islamic economics. The obligation of the wealth owners to pay and the entitlement of specific category of people to benefit from it are of great economic significance. The principle of transfer payments, the target groups of recipients, and the public purpose served by the provision are the crux of the matter so far as Islamic economics is concerned. But the details of the law of zakat, especially those relating to the time of its inception, belong to Islamic law and not to Islamic economics.

There is, however, a close relation between Islamic economics and Islamic law. Islamic economics can help jurists in formulating operational details of the law of zakat in modern circunstances by tracing economic consequences of rules and regulations and their impact on public purpose. Once the target beneficiaries in a modern society are defined, for exanple, economics can indicate the most efficient means to deliver the benefits to them. Islamic economic analysis can also enlighten the jurists on how not to deliver benefits to target groups by pointing out such economic consequences of certain means of delivery as work against public purpose due to their negative effects on incentive to work, etc.

Generating Research Priorities

Islamic econonics was launched by general works on Islamic economic system and the economic philosophy of Islam. With the passage of time, however, new

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research priorities emerged. By the close of the seventies the theory of Islamic economics, as distinguished from other Islamic sciences and from economics, had its priorities sorted out. There was no denying the fact that Islamic financial institutions were at the top of its agenda.

Next came the teaching of Islamic economics. This in effect was an effort to take the ideas in the above mentioned general works to the class-room. For doing so, these ideas were rearranged in accordance with the conventional arrangement of econonmics: consumption, production, exchange, distribution, public finance, development, etc. By the end of the seventies most universities in the Arab and Islamic world were teaching some courses in Islamic economics. These were followed by some western universities in the eighties.

With teaching went research. Dozens of doctoral dissertations were producted in the western universities on subjects ranging from Islamic economic doctrines, to Islamic economic system to Islamic banking. The number of dissertations produced in the Arab and Islamic countries would be many times more.

This was a development of great significance to the theory of Islamic economics. Just as the practice of Islamic banking was now pr-oviding some feed back to the theory of Islamic banking (which preceded practice), so teaching and research was helping in refinement of concepts and a better formulation of precepts. For the first time theory and practice were able not only to reinforce each other but also to introduce significant changes in each other. The most prominent example is the introduction, in late seventies, of **murabaha** in an exercise which was earlier supposed to be based mainly on **mudaraba.**

The State of the Art

If one compares the state of Islamic economics in 1979 with that in 1950 he would be inpressed by the near explosion in the number of publications on the subject. Also a much larger group of people was now involved in Islamic economics. Further more, it was a much more diversified group than those who launched Islamic economics. Those who had something to say on Islamic economics did not comprise only academics. They now included bankers, insurers, merchants, dealers in real estate, money changers, even finance ministers!

The result was a lively debate at a number of forums, including the classroom, the research seminar, the press conference, the pulpit and the council of ministers. Though it remained necessary as always to separate the chaff from the grain, it gave a boost to the development of the theory of Islamic economics.

As we leave behind us the thirty years since the emergence of Islamic economics in the middle of twentieth century, some important ideas contributed during the period can be noted:

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1. Tempering self interest by morality and maximisation of private gain by a concern for public purpose as behavioural assumptions.

2. Two tier mudaraba as a model of banking, replacing fixed interest by profit sharing in depositor - bank and bank- business relationships.

3. Murabaha as a means of decreasing risk in the placement of funds by Islamic banks. The Business client requests bank to buy what it agrees to purchase from the bank adding a markup to purchase price, with deferred payment.

Section Two Contributions in Eighties and Nineties

The most significant new idea contributed during the next fifteen years (1980-1994) is the inherent relative stability of the Islamic financial system in contrast to capitalism notorious for its tendency towards instability.

It was argued that a switch over from interest to profit- sharing removed a basic contradiction from the conventional system. The entrepreneur (the firm) has to pay back fixed amounts of money at specific dates to the financier (the lender). But the revenue accruing to the entrepreneur from sale of products is uncertain in amount and not bound by any time table. When revenue falls short and fails to occur in time the resulting default the borrower destabilizes the whole system.

Not so in the interest free system. The synchronisation between payment obligations and revenue in a two tier mudaraba model of Islamic banking would greatly weaken if not remove the forces causing big fluctuation in economic activity in a free economy.

Another distinctive feature of interest free Isiamic system was expansion in money supply through investment process rather than lending process, as in case of capitalism. As a result expansion in money supply had a much greater chances of being accompanied by inerease in real production. This feature made further contribution towards stability of the system.

Applied Islamic Economics

A significant development during the last fifteen years has been empirical studies testing hypotheses based on the extant Islamic economic literature in the light of the corresponding reality.

Does a reality corresponding to Islamic economics exist in the present day world? The answer in the middle of the century would have been a categoric no. In fact some writers emphasised that the contemporary muslim economic behaviour, institutions and policies, especially government policies were deviating far away from Islam. To many this implied that Islamic economics had no referent in the real world.

No longer so. Two things have changed the perception. A number of countries are trying to rid their economies of interest and to put in its place a financial system free from interest. Pakistan, Iran, Sudan all started doing so in early eighties. Malaysia, in the late eighties started erecting an interest free financial structure parallel to the conventional one. Some countries are also collecting and disbursing Zakat.

Secondly it is being realised that contemporary muslim behaviour is not all deviant. It is a mixed affair. Many muslims try to follow the teachings of Islam as consumers, producers, employers, etc. There are also Islamic institutions which cannot be ignored , like the awgaf (charitable endowments). It would be fair to treat each case on merit so far as the Islamicity of government policies, role of social institutions and behaviour of economic agents is concerned. A blanket rejection is not justified. It is also counter productive.

There is an upsurge in applied and empirical studies. Majority of subjects approved for writing doctoral dissertations now belong to this category, whereas not a single dissertation was written on such a subject in the earlier period. This is also an indicator of current research priorities. Operationalisation of Islamic economics is getting more attention than mere description and adulation. Also the naive tendency to build models on assumption of exemplary ideal Islamic behaviour on part of economic agents is being moderated by introducing middle level conformity and second best behaviour.

Globalisation and a Universal Approach

Islamic economics is also taking note of globalisation and its far reaching implications. Earlier the focus was on the national economy. How Islamic economic system works in a closed economy and how a country can transform its fiscal and financial system in accordance with Islam, have been the subject of a large volume of literature. Now more and more attention is being paid to international economc relations. The financial system in any one muslim country has to interact closely with the rest of the world as movements of capital and flow of financial information is beyond control of national governments. The need for a global approach to reforming the financial and monetary systems so that they are freed of interest and gambling is being realised.

The increasing uneasiness with mainstream economics which failed to meet the ecological and environmental challenge is also having some impact on Islamic economics. As Islamic economists pay more attention to global economic issues they become more aware of the fact that the entire humanity must join hands to deal with them.

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The net result has been to draw Islamic economics closer to focusing on the practical problems of the day, those facing the muslim people as well as those facing the entire humanity. The issue is no longer to establish that Islam has an economic system distinct from Capitalism and Socialism. That is a thing of the past. Then, to expound the superiority of Islamic system over other systems does not seem to be the most important thing to do when almost all muslim countries and communities are beset with poverty, unenployment, disparities, indebtedness, etc. It seems more rewarding to participate in the universal search for ways of restoring the ecological balance, prenting environmental disasters, lessening conflict between peoples and designing a sane and stable monetary and financial system more conducive to justice and equity. It is in projecting Islamic teachings with the potential of contributing in this task that the future of Islamic economics may lie.

Simultaneously Islamic economists have to promote the application of Islamic economic precepts in muslim societies and use Islamic economic concepts in making an agenda for Islamic economic reform for specific muslim countries.

Even though the two tasks seen separate and independent of one another they are in fact closely inter-related. Firstly, it is only in the context of a global approach that a realistic agenda for reform and progress of any specific muslim country can be drawn. Secondly Islamic economic contribution to the universal search for viable solutions to modern man's economic problems can be credible only when Islamic economics makes visible progress at home.

Section Three Theory of Islamic Economics: The Future

When Islamic economics appeared on the scene during the middle of twentieth century, poverty and underdevelopment prevailed all over the muslim world. The emphasis on economic development and a bid to relate Islam to developmental efforts, so common in early Islamic economic literature, are understandable in that context.

The twenty-first century is going to dawn on a world of Islam with half of the OIC member countries outside the list of world's most poor countries. Though development is still inportant in all especially the poor half, there are other issues making people in muslim countries anxious. Currency values are fast deteriorating in many muslim countries. Foreign indebtedness is on the increase, intra-Islamic trade is declining.

Macro-management is the issue.

On the other hand at least two muslim countries have been able to make a break-through with export led growth. Malaysia and Indonesia with annual growth rates above six percent may serve as role models for many other muslim countries.

This is happening in a world in which the most advanced countries, indeed the entire developed world, is struggling hard to reach and maintain a three percent annual rate of growth and to help their large number of unemployed find a job.

Then we have the latest UNDP report (for 1994) naming a number of muslim countries making "big advance" up the HDI (Human Development Indicators) ladder: Iran, Turkey, Malaysia and Tunisia."[2]

The message is clear: No one is condemned to poverty and backwardness for all time to come, as no one is assured of being at the top for ever. It is works that count.

What can Islamic economics contribute? Are there any signs it is going to make some difference? When, where, and what is espected?

The most likely place seems to be the universities, to begin with. The most promising subject is a sane and sound system of money and finance for which the search is on.

There is also the possibility that some muslim countries manage to have sustained growth over the next few decades, accompanied by improved Islamic living. Of special importance in the context of Islamic living will be the family.

If a drug free, crime free, ecologically balanced growth which is every heart's desire materializes in some muslim countries within the next few decades Islamic economics will have made a significant impact. Practical results are, after all, the ultimate touch stone for theory. The event itself is sure to lead to further refinement and development of the theory of Islamic economics.

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1. For that see the authors Muslim Economic Thinking, Leicestur, The Islamic Foundation, 1988.
2. Financial Times, 2 June, page 5.

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FISCAL AND MONETARY POLICES FROM ISLAMIC PERSPECTIVE

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Managed money is a new phenomenon which has gained prominence after the collapse of the Bretton Woods system in August 1971. There is no possibility of finding a precedence for it in the days of the Prophet, may the peace and blessings of God be on him, or in early Islamic history. A number of questions are, therefore, continually raised about the monetary system that a Muslim country may adopt. Is it necessary to go back to the then-prevailing system or is it justifiable to continue the managed money standard that now prevails almost in every country around the world, including the Muslim countries? If so, what constraints may have to be placed upon this system to enable it to help realise the maqasid al-shar'iah (goals of Islamic teachings, referred hereafter as the maqasid), and what policy instrument may be used to realise these goals? This paper tries to answer these and some other related questions.

1. THE HISTORICAL PERSPECTIVE: THE EVOLUTION OF MANAGED MONEY

Historical records indicate that the monetary system prevailing during the Prophet's days was essentially a bimetallic standard with gold and silver coins

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(dinars and dirhams) circulating simultaneously. The ratio prevailing between the two coins at that time was 1:10. This ratio seems to have remained generally stable throughout the period of the first four caliphs.[1] Such stability did not, however, persist continually. The two metals faced different supply and demand conditions which tended to destabilise their relative prices. For example, in the second half of the Umayyad period the ratio reached 1:12, while in the Abbasid period, it reached 1:15 or less.[2] In addition to this continued long-term decline in the ratio, the rate of exchange between the dinar and the dirham fluctuated widely at different times and in different parts of the then Muslim world. The ratio at times declined to as low as 1:35, and even 1:50.[3] This instability tended to make the bad coins drive good coins out of circulation, a phenomenon which became referred to in the 16th century as Gresham's Law.[4]

When the United States adopted bimetallism in 1792, the gold-silver price ratio was 1:15. However, the fluctuating prices of both metals led the U.S. to demonetise silver in 1873. Experience of several other countries suggests that bimetallism was a fragile standard. There was no dependable way to tie together full-bodied gold and silver coins at fixed rates. This was the main cause of its universal demise.[5]

Monometallism hence took its place. In the beginning, silver and gold both competed, but silver continued to lose ground and the gold standard became prevalent around the world. It emerged as a true international standard by 1880 following the switch by a majority of countries from bimetallism and silver monometallism to gold as the basis of their currencies.[6] Under this standard, the value of a country's currency is legally defined as a fixed weight of gold, and the monetary authority is under an obligation to convert the domestic currency on demand into gold at the legally prescribed rate. Historically there have been three variants of the gold standard: the gold coin standard, when gold coins were in active circulation; the gold bullion standard, when gold coins were not in circulation but the monetary authority undertook the obligation to sell gold bullion against the local currency at the official rate; and the gold exchange standard (or the Bretton Woods system), when the monetary authority was required to exchange domestic currency for U.S. dollars which could be converted into gold at a fixed parity.

The U.K. was on a gold coin standard until 1914 and then a gold bullion standard from 1925 to 1932. The rules of the gold standard required deficit countries to deflate and the surplus countries to reflate their economies. This seemed unrealistic during the Great Depression when the deficit countries had no alternative but to reflate their economies to reduce unemployment. The United States and France, the two major surplus countries, also did not find it practical to follow the

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rules of the game. Instead of reflating their economies, they persistently sterilised their balance of payments surpluses, thus accentuating the deflationary pressure on the deficit countiries. Such policies undermined the effective operation of the gold standard and it was abandoned after the Great Depression.

The financial needs of the Second World War and of post-War reconstruction made the return to the gold standard even more difficult and the Bretton Woods system became universally adopted after the Second World War. The U.S. Dollar became the corner-stone of this system because at the end of the Second World War. The U.S. held around two/thirds of the world's monetary gold. By the late 1950s, the growth of the world's monetary gold stock was insufficient to finance the growth of world output and trade.[7] The dollars supplied; by the U.S. deficit helped provide the needed liquidity. This could not, however, be a permanent solution. The persistent U.S. deficits led to a continuous decline in its gold holdings and undermined its ability to maintain the dollar's convertibility into gold. Ultimately the U.S. was forced to demonetise gold in August 1971. This led to the end of the Bretton Wood's system and ushered in a new era of fully-fledged managed money standard having absolutely no link with gold. Exchange rates are now generally floating with no official par values. This system, which at first became adopted by the force of circumstances, acquired an official character after the ratification of the Second Amendment to the IMF Articles of Agreement in April 1978.

Thus the international gold standard lasted for almost a century, while the Bretton Woods system was able to endure for only about 25 years (in reality even less). This is because the classical gold standard had some intrinsic strengths. It ensured an intrinsic value for the currency. Even the paper money in circulation was representative monev and could be converted into gold coins or bullion on demand. This subjected the monetary authorities to a discipline. It was not possible for them to resort to excessive monetary expansion. In contrast with this, the now-universally-prevalent managed monetary system does not subject the monetary authorities to a built-in discipline. This has made it possible for the governments to finance large budgetary deficits.

Monetary expansion has hence been generally excessive, leading to high rates of inflation. This is clearly borne out by historical data. From the beginning of the eighteenth century until the eve of World War II, there were considerable fluctuations in prices but the overall increase was relatively small, about 33 percent, over a period of more than two centuries. During the 1940s, prices nearly doubled as a result of the War. Between 1951-1970 concumer prices of industrial contries rose by about two-thirds while those of the world as a whole more than doubled. However, between 1971-1990, consumer prices of industrial countries ha-

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ve risen by more than three-and-a-half times while those of the world as a whole have risen by more than nine times. This is so in spite of a substantial decline in the rates of inflation since the early 1980s. One of the major causes of the high rates of inflation is the rapid expansion in money supply during the period 1971-90 - more than five times in industrial countries and nearly twelve times in the world at large.[8]

In addition to a relatively high rate of inrflation, the period since 1911 has also been plagued by a high degree of exchange rate volatility. It is generally agreed that persistent exchange rate volatility deprives policy makers of an effective anchor and contributes to misallocation of resources both domestically and internationally. The European attempts to stabilise exchange rates through the ERM (Exchange Rate Mechanism) has not proved to be successful. The ERM crises of 1992 and 1993 as well as the steep Dollar decline in June-July 1994 have clearly demonstrated that it is not possible to stabilise exchange rates without disciplined fiscal and monetary policies. One of the primary factors behind the lack of indiscipline will be addressed later on in this paper.

2. IS MANAGED MONEY ACCEPTABLE?

In view of the high rates of inflation and the excessive exchange rate volatility, some Muslim scholars have felt nostalgic about a monetary standard based on precious metals. However, since both bimetallism and the gold standard have also created difficulties, it seems that Muslim countries may not possibly have any alternative to the managed money standard that now prevails. The question is whether this is acceptable from the point of view of the Shari'ah and, if so, is it possible to make the monetary system perform better in an Islamic environment.

There is no specific text in the Qur'an or the Sunnah that would make it incumbent upon the Muslim ummah to use continually the bimetallic standard prevailing during early Islamic history or a full bodied metallic standard. This is clearly demonstrated by the fact that 'Umar, the Second Caliph (d. 23/644), once thought of introducing camel- skin coins. These would have been in the nature of fiduciary money, the then equivalent of the now-prevailing paper money. However, the problem that might have perplexed him most was probably the control of its issue. When he was advised by experts that it would be impossible to do this and might not only lead to an excessive creation of money but also to the disappearance of camels through their excessive slaughter, he abandoned the idea.[9] This idea of the issue of fiduciary coins has, however, been generally reflected in the writings of a number of prominent jurists throughout Muslim history. For example, according to Ahmad ibn Hanbal (d. 241/855), there is no harm in adopting as currency anything that is generally accepted by the people.[10] Ibn Hazm (d.

456/1064) also does not find any reason for the Muslims to confine their currency to gold or silver.[11] According to-Ibn Taymiyyah (d. 505/1323) the dirhams and dinars are not desired for their own sake but because of their ability to serve as media of exchange. Hence, there are no natural or Shar'i specifications for them: their acceptance depends on custom and usage.[12] In modern times also, the jurists have almost unanimously recognised fiduciary money. This recognition acquired the character of near ijma' (consensus) when it became formalised by the juristic verdicts of the internationally constituted fiqh committees of the Rabitah al-'Alam al-Islami in 1982 and the Organisation of the Islamic Conference in October 1986.[13]

This does not, of course, mean that anyone can issue currency in any amount. The jurists have almost unanimously emphasised that the currency must be issued by the ruling authority and must have a stable value, to enable it to perform efficiently its functions as a measure of value, a medium of exchange, and a store of purchasing power.[14] This emphasis of the jurists on stability in the internal and external value of money is rightly deserved because of the unequivocal stress of the Qur'an on honesty and fairness in all measures of value (6:152, 7: 85, 11:84-85, 11:35 and 26:181). This obligation to be honest and fair does not apply only to individuals but also to the society and the state; it need not, moreover, be confined to merely conventional weights and measures, but should rather encompass all measures of value. Money is also an important measure of value and any continuous and significant erosion in its real value is bound to have an adverse effect on the realisation of socio-economic justice and general wel-being. Stability in the value of money should hence receive priority in the field of monetary management.[15] However, price stability is only one of the goals. As it is commonly realised now, it helps in the realisation of the other goals which, in the field of economics, may be said to be the universally-desired goals of general need-fulfilment, equitable distribution of income and wealth, optimum real rate of economic growth, full employment, and economic stability.[16]

Even though the importance of all these goals is recognised, no country around the world, irrespective of whether it is rich or poor, Muslim or non-Muslim, seems to have been able to realise them simultaneously in the present-day world. There may be a number of reasons for this failure. One of the most important of these may perhaps be the lack of an enabling strategy. The discussion of a comprehensive strategy for readlising the desired socio-economic goals would be beyond the scope of this paper.[17] It would be naive to assume that a single state policy could help realise all these goals, It may rather be necessary for all government policies to converge in the direction of their realisation. Monetary management cannot be an exception. It must also make a positive contribution toward

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the realisation of all these goals, even though priority may be given to the goal of price stability.

Since monetary management is influenced by both monetary and fiscal policies, it would be ideal to discuss both of them. This would, however, make the paper too long. I shall, therefore, confine myself primarily to a discussion of the role and instruments of monetary policy in the monetary management of an Islamic economy. Fiscal policy would be referred to only to the extent to which it affects successful monetary management.

3. MONETARY MANAGEMENT IN MAINSTREAM ECONOMICS

The discussion of monetary management generally revolves around the determinants of money demand and money supply. Since both of these are extremely important, it may not be desirable to assume anyone of these as exogenous. It is rather necessary to discuss both and to show how they could be brought into equilibrium in a way that would be conducive to the realisation of the desired goals.

Money, and particularly fiduciary money, is not demanded for its own sake. It is demanded for a number of purposes. It is needed, firstly, as a medium of exchange to finance the transactions of households, firms and government for their day-to-day purchases of goods and services related to consumption, investment, imports and exports (Y); the capacity of any economy to supply these is relatively limited in the short-run. Secondly, it is needed by way of precaution to satisfy unforeseen needs, which it is not possible for anyone to predict precisely. Thirdly, it is also needed for earning through speculation in the commodity, stock, foreign exchange and financial instmunents markets. However, not every household, firm or government agency has enough money for all these purposes. Some have a deficit while others have a surplus. The interaction of both the deficit and the surplus sectors determines the rate of interest. This, in turn, influences the demand for money for all these three purposes.

Thus the demand for money (M_a) is said to be determined by the money value of total output (Y) as well as the rate of interest (r), as reflected in the following generally used equation:

$M_a = f(Y, r)$.

It varies directly with Y and inversely with the rate of interest. The rate of interest thus occupies a central place in the discussion of money demand in mainstream economics.

If money supply is considered to be an exogenous variable, then then a specific money supply, the greater the demand for precautionary and speculative purposes, the less may be available for transactions purposes. However, the entire

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transactions demand may not necessarily be for need-related consumption and productive investment, it may also be for conspicuous consumption and unproductive investment. Hence it may be stated that the greater the ability of an economy to reduce the money demand for precautionary and speculative purposes as well as for conspicuous consumption and unproductive investment, the greater may be its ability to satisfy the money demand for need fulfilment and productive investment and to realise its socially-desired goals. If fhe money demand rises for all purposes and the needed balancing does not take place, there may be excess demand, leading to imbalances, higher real rates of interest and inflationary pressures. Therefore, the allocation of money supply among the three components of money demand is extremelv crucial. It would determine in an important way whether the economy concerned may, or may not, be able to realise its desired goals. Money demand that is conducive to the realisation of all socially-desired goals may be considered to be 'efficient' and 'eqitable, and money demand that does not contribute to, or frustrates, goal realisation may be considered to be 'inessential', and 'unproductive'.

If money supply is not considered to be an exogenous variable then one needs to explain the major domestic sources of money supply, which are primarily savings and money creation. These become reflected in the sum of currency in circulation and deposits. The greater the contribution of savings to money supply, the greater may be an economy's ability to meet money demand in a non-iuflationary manner. However, the greater the ability of a system to promote inessential and unproductive demand for money, the lower may be its ability to generate savings and to expand money supply in a non-inflationary manner.

The best strategy for monetary management may thus be one that does not only help make money demand efficient and equitable but also brings money supply into equilibrium with such money demand in a non-inflationary way. Money demand and money supply are thus closely related and may be compared with two sides of the same coin. It seems, however, that management of money demand in an efficient and equitable manner may be more crucial, and probably more difficult, than management of money supply.

3.1 FRUSTRATION OF GOAL REALISATION

Enzler, Conrad and Johnson have found compelling evidence to conclude that in the United States "the existing capital stock is misallocated -probably seriously- among sectors of the economy and types of capital."[18] This misallocation may be due to a number of factors. The fact that most major religions, including Hinduism, Judaism, Christianity and Islam have prohibited interest, leads one to hypothesise that the use of interest as a mechanism for allocation of money supply

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among the various constituents of money demand may perhaps be one of the major reasons for this misallocation. It is hence the contention of this paper that the nature of this misallocation is such that it would necessarily tend to frustrate the realisation of the generally-desired goals of need fulfilment, optimum rate of economic growth and full employment, equitable distribution, and economic stability. Let us see how.

3.11 Need Fulfilment

The criteria for satisfying money demand in an interest-based economy are the ability of borrowers to provide acceptable collateral to guarantee the repayment of principal, and sufficient cash flow to service the debt. End-use of financial resources does receive attention, but does not normally constitute the main criterion. Hence, financial resources go to the rich, who fulfill both these criteria, and also to governments who, it is assumed, will not default. However, the rich borrow not only for productive investment but also for conspicuous consumption and speculation, while the governments borrow not only for development and public well-being, but also for excessive defence buildup and unprofitable public sector enterprises. This contributes to a rapid expansion in the demand for money for unproductive and wasteful spending and, besides accentuating macroeconomic and external imbalances, squeezes the resources available for need fulfilment and development. This may help explain why even the richest countries in the world like the United States have been unable to fulfil the essetial needs of all their people in spite of abundant resouarces at their disposal.

3.12 Optimum Growth and Full Employment

The unproductive and wasteful spending which the collateral-linked, interest-based financial intermediation has the tendency to promote, has led to a decline in savings. In the major industrial countries, net national saving as a percentage of gross national product declined by almost 4 percentage points from 13.5 percent to 10 percent between the 1960s and the 1980s.[19] This saving shortfall has been one of the major factors responsible for the persistently high levels of real interest rates during the eighties and the nineties and for the lower rates of growth in investment and employment.

Unemployment has hence become one of the most intractable problems of all countries, including the rich industrial world. Unemployment stood at 8.5 per cent in OECD Europe in 1993, nearly three times its level of 2.9 per cent in 1971-73.[20] If 'discouraged workers' (those who have dropped out of the labour force because of the poor job 'prospects) and workers in involuntary part-time employment are also included, the overall rate of unemployment may be around 12.5 percent.[21] It is not expected to fall significantly below this level in the near future because

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a real rate of economic growth of 3.5 percent is required to prevent unemployment from rising, and European growth has generally been below this benchmark since 1976. According to the BIS, the rate of growth that the older industrialised countries can hope to achieve without courting inflationary pressures is around 2.5 per cent.[22] Even more worrying is youth unemployment of around 25 percent, excluding the 'discouraged' youth.[23] This hurts their pride, dampens their faith in tile future, increases their hostility towards society, and damages their personal capacities and potential contribution.

Given the budgetary constraints and the ever-looming threat of inflation, the prospect of attaining high growth rates and full employment in the foreseeable future is not very bright in the Western world. A decline in wasteful spending and a rise in savings and investment could be very helpful, but this is not possible when the value system encourages both the public and the private sectors to Live beyond their means, and the interest-based financial intermediation makes this possible by making credit available relatively easily without due regard to its end use.

3.13 Equitable Distribution

The inequitable allocation of financial resources in the conventional interest-based financial system is now widely recognised. According to Arne Bigsten, "the distribution of capital is even more unequal than that of land" and "the banking system tends to reinforce the unequal distribution of capital."[24] The reason is, as already indicated, interest-based financial intermediation relies heavily on collateral, giving inadequate consideration to the strength of the project or the ultimate use of financing. Hence, while deposits come from a cross-section of society, their benefit goes mainly to the rich.

As Mishan has rightly pointed out: "Given that differences in wealth are substantial, it would be irrational for the lender to be willing to lend as much to the impecunious as to the richer members of society, or to lend the same amounts on the same terms to each."[25] The established practice of banks is hence to lend mainly to those individuals and firms who have the necesary collateral to offer and who have, as Lester Thurow has observed, "large internal savings, regardless of whether they are earning above average rates of return on their investment." The result is that "the winners are, as in a lottery, lucky rather than smart or meritocratic."[26] Even Morgan Guarantee Trust Company, sixth largest bank in the U.S., has admitted that the banking system has failed to "finance either maturing smaller companies or venture capitalists," and "though awash with funds, is not encouraged to deliver competitively priced funding to any but the largest, most cash-rich companies."[27] Such behaviour of interest-based financial institutions tends to ac-

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centuate, rather than reduce, inequalities of income and wealth.

3.14 Economic Stability

The rate of interest has become one of the most important destabilising factors in the present-day world economy. Milton Friedman, a Nobel laureate, attributed the unprecedentedly erratic behaviour of the U.S. economy to the erratic behaviour of interest rates.[28] The high degree of interest rate volatility injects great uncertainty into the financial market and makes it difficult to take long-term investment decisions with confidence. This uncertainty drives borrowers and lenders alike into the shorter end of the market, makes short-term speculative investments more attractive and generates a great deal of heat in the commodity, stock and foreign exchange markets. This heat has been one of the important sources of instability in the world economy. According to a report of the Bank for International Settlements, the total turnover in foreign exchange markets amounted to $880 billion per business day in April 1992.[29] A substantial part of this turnover is related to derivatives (futures and options contracts), whose total outstanding value is currently estimated to be around $15,000 billion.[30] The derivatives contracts are highly leveraged and, in the case of some money centre banks, several times their capital and reserves. If the assertion normally made by bankers that they give due consideration to the end use of funds had been correct, such a high degree of leveraged credit extension for financing speculative transactions would perhaps not have taken place.

The dramatic growth in financial transactions over the past two decades, of which derivatives are only the latest manifestation, has resulted in an enormous expansion in the payments system. Such a large volume of transactions implies that if problems were to arise, they could quickly spread throughout the financial system exerting a dominoes effect on financial institutions. The volume of transactions handled by the payments system every day is nearly 120 times the sum of merchandise imports and exports of all countries.[31] Accordingly, Mr. Crockett, the General Manager of the Bank for international Settlements, has been led to acknowledged that "our economies have thus become increasingly vulnerable to a possible breakdown in the payments system."[32] The large value of transactions has also other adverse effects. It has been one of the major factors contributing to the continued high real rates of interest which have tended to discourage productive investment. It has also tended to inject excessive instability into the foreign exchange markets. The effort by central banks to overcome this Instability through small changes in interest rates or the intervention of a few hundred million dollars a day has generally proved to be ineffective.

In an equity-based system, the entrepreneur's share in the total return on ca-

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pital would depend on the profit-sharing ratio and the ultimate outcome of the business. The profit-sharing ratio between the entrepreneur and the financier would not fluctuate from day to day or even month to month like the rate of interest, because it would be determined by custom and considerations of justice, and remain contractually stable throughout the duration of the financing agreement. Since the ultimate outcome of business depends on a number of factors which do not change erratically, therefore, equity-based financial intermediation is likely to be more conducive to economic stability than loan-based intermediation. This has been recognised by a number of prominent Western economists, including Henry Simons, Hyman Minsky and Joan Robinson.[50]

3.2. CONCLUSION

Thus it may be seen that the effort to regulate the various components of money demand on the basis of interest tends to accentuate, rather than minimise, money demand for unproductive and speculative uses. This has the effect of reducing the resources available for need- fulfilment and productive investment, thus frustrating goal realisation. Moreover, since the demand for money related to conspicuous consumption and speculation tends to be relatively more unstable than that for need-fulfilment and productive investment, a high degree of instability gets injected into the whole economy. No wonder recent empirical studies have revealed great instability in the aggregate money demand function as well as its major components.

4. MONETARY MANAGEMENT IN ISLAM

4.1. MONEY DEMAND

Islam does not therefore find interest to be an appropriate mechanism for the management of money demand in an efficient or equitable manner. Consequently, it tries to regulate money demand by a strategy that relies on a number of instruments, three of which are particularly important.[51]

Firstly, since values and institutions play a crucial role in practically all aspects of human life, it does not have an anathema to value judgements. It is rather positively oriented towards them and tries to create an enabling environment for making these effective in actualising an allocation and distribution of resources that is in conformity with its maqasid. It declares all resources to be a trust from God and makes their efficient and equitable use a major subject of human accountability on the Day of Judgement. While these values and institutions sanction money demand for need-fulfilment and productive investment, they do not sanction it for unnecessary and unproductive spending. This Islam tries to do even before the demand gets expressed in the market place.

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Secondly, since values may be disregarded, it tries to reinforce them by a number of social, economic and political Institutions. One of these is the price mechanism, which it upholds for greater efficiency in the use of resources. While the price mechanism may by itself not be able to bring about allocation of resources in conformity with goal realisation, it may be able to make a positive contribution when reinforced by the value system.

Thirdly, since interest-based financial intermediation has the tendency to promote conspicuous consumption, speculation, and unproductive investment, Islam prohibits interest and reorganises financial intermediation on the basis of profit-and-loss sharing. The linking of the return to the ultimate outcome of the business financed would help ensure that financing does not become available to satisfy money demand for any purpose just because the borrower has an acceptable collateral to offer and sufficient income to service the debt. It would rather be available if the money demand is for a worthwhile project and is accompanied by the necessary ability to manage the project efficiently. Even a poor but competent entrepreneur may thus qualify if he has a worthwhile project. This would not only help minimise demand for money for wasteful and unproductive purposes but also enable the society to harness the pool of entrepreneurial ability from among the poor and to tap the rich contribution that such entrepreneurs can make to output, employment and need-fulfilment.

If the demand for money even from the public sector were subjected to the test of project performance, the lender may be compelled to take a greater interest in the nature of the project and its satisfactory management. Financing may not then be undertaken on the assumption that a sovereign debtor does not go bankrupt; it may rather be available mainly for projects about the productivity of which the financier is confident. Governments may not be able to get financing for excessive defence build-up and unprofitable public sector enterprises. The application of such a test before satisfying the demand for money may tend to create difficulties in the short-run. In the long-run, however, it may prove to be a blessing because, by reducing budgetary and macroeconomic imbalances in an efficient and equitable manner, a healthy dimension may be injected into the economy, which a rise in interest rates may not necessarily be able to accomplish.

In addition to reducing the money demand for unproductive and speculative purposes, Islam tries to minimise the holding of idle cash balances by the levy of zakat. This would tend to induce savers to get into productive investments to save their net wealth from being eroded by zakat.

Since need-based consumption and productive investment tend to be more stable than conspicuous consumption and speculative investment, the demand for money may tend to be more stable in an islamic economy. What may further re-

inforce this is that expectations about rates of profit do not fluctuate daily or weekly like the rate of interest. Thus the various elements of the Islamic economic system may not only help minimise the instability in the aggregate demand for money but also influence the different components of money demand in a way that would promote greater efficiency and equity in the use of money. The relatively greater stability in the demand for money in an Islamic economy may also introduce greater stability in the velocity of circulation of money.

The demand for money in an islamic economy may thus be represented by the following equation:

$M_d = f(Y_S, S, \pi)$ where

Y_S = goods and services that are related to need fulfilment and productive investment and are in conformity with the values of Islam;

S = all those moral and social values and institutions (including zakat) that influence the allocation and distribution of resources and that can help minimise M_d not only for conspicuous consumption and unproductive investment but also for precautionary and speculative purposes; and

π = the rate of profit or loss in a system which does not permit the use of the rate of interest for financial intermediation.

It may, however, be charged that even in Muslim countries Y incorporates conspicuous consumption and unproductive investment. Hence, the characterisation of Y_S above is normative, not reflecting the existing reality. It may also be argued that 'S' stands for a complex of values and institutions which may not necessarily be quantifiable and which may not even be visibly practised. While both these objections seem to be valid, the important point is to realise that if the actualisation of goals is important, then Y needs to be cleansed of all elements that frustrate this objective. It is also important to realise that when there are a number of values and institutions that influence goal realisation then there seems to be no logic behind concentrating only on r, which, as shown above, has proved to be ineffective in influencing money demand in a way that would help goal realisation. This realisation may induce economists to identify at least the major values and institutions that affect resource allocation and to develop techniques of measuring, to the extent feasible, their effect on resource allocation. This may also lead to the identification of non-coercive ways of actualising these values and institutions and making them more effective in curbing the inessential and unproductive part of M_d. Economists would not then be concerned with just an explanation of what exists but also with what needs to be done to realise the maqasid.

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4.2 MONEY SUPPLY

Once money demand has been stabilised and related to the needs of general well-being and development, there arise the questions of, firstly, how to bring aggregate money supply into equilibrium with such money demand, and secondly, how to bring the allocation of this money supply in conformity with the needs of goal realisation without using coercion. The first question acquires further significance because two of the most important instruments of monetary management in the capitalist economy, discount rate and open market operations in interest-bearing government securities, would not be available in an Islamic economy.

4.21 Monetary Targets

To create an equilibrium between money demand and money supply, the most practical approach may be to estimate the demand for money that is consistent with the realisation of desired socio-economic goals and then to establish a target range for money supply growth that would help satisfy this demand adequately.[35]

The targeted growth in money need not, however, be followed rigidly and mechanically. This is because monetary targeting presumes that the income velocity of money is reasonably predictable over relevant periods. While, as indicated earlier, this may be expected to be truer in an Islamic economy, it may, nevertheless, be affected by domestic and external economic shocks. The targets should, therefore, be reviewed quarterly, or as often as necessary, and changed whenever this is warranted .

It may also be possible to consider the simpler Friedman rule of adopting a fixed annual rate of growth in M in keeping with the secular growth in output and change in velocity to avoid the frequent 'tinkering which is otherwise necessary.[36] However, if such a formula is adopted, it should be because of the ease it offers, and stripped of Friedman's excessive free-market commitment. The positive role of the state and of fiscal policy cannot be dispensed with in an Islamic economy.

4.22 Attaining the Targeted Growth in M

This takes us to the instruments that may be used by the central bank to create harmony between the targeted and the actual growth in money supply. Since deposits constitute a substantial part of money supply, it may not be possible to regulate money supply without retgulating total deposits. Deposits may also, for the sake of analysis, be divided into two parts: 'primary deposits', wich provide the banking system with high-powered money 'commercial banks' cash in vault plus deposits with the central bank), and 'derivative deposits' vich, in a proportional reserve system, represent money created by banks in the process of credit

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extension, The higher the savings, the greater may be the share of primary deposits in total deposits and the lower may be the need for expansion of derivative deposits. The expansion in derivative deposits may hence need to be regulated in accordance with the needs of goal realisation, particularly stability in the value of money. Since it is generally recognised that the growth in derivative deposits is closely related to the growth in M_O; or high-powered money, the centrcal bank has no option but to regulate closely the growth in M_O.[37]

There are three important sources of high-powered money: government borrowings from the central bank, central bank credit to the commercial banks, and balance of payments surplus. The first of these has probably been the largest source after the Second World War, because of the unduly large government budgetary deficits in most countries. Excessive fiscal deficits put the entire burden of monetary stability on the central bank and make the pursuit of healthy monetary policy extremely difficult. It is not possible to control monetary expansion unless this major source of high-powered money is properly regulated. It may hence be unrealistic for Muslim governments to talk of Islamisation of their economies without making a serious effort to regulate their budgetary deficits in accordance with the demands of the maqasid, particularliy price stability.

It may always be possible for the central bank to control successfully its own lending to the commercial banks. However, the abolition of interest and its replacement by profit-and-loss sharing vould further reinforce this ability. Since central bank lending to commercial banks would take the form of mudarabah advances, not only, would the central bank be more responsible in its lending to the commercial banks but also simultaneously the commercial banks would be more cautious in lending to their clients in both the public and the private sectors, particularly for speculative and unproductive purposes. It may thus be possible to check the expansion in derivative deposits without resort to the prohibitive 100 percent reserve requirement which some scholars have suggested.[38] However, if at some stage this is felt necessary, the central bank should not hesitate to resort to it.

There may be a rare Muslim country which enjoys continued balance of payments surplus. However, even if such a surplus is experienced, it may be possible to sterilise it to the extent desired by using the instruments of monetary policy available even in an Islamic economy.

4.3 INSTRUMENTS OF MONETARY POLICY

Even if high-powered money is regulated by controlling government budgetary deficits, there are bound to be short-term fluctuations in its volume as well as its relationship with derivative deposits. The central bank may, therefore, have

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to use the quantitative instruments at its disposal to even out the impact of these short-term fluctuations on money supply. It may also have to adopt certain measures to help ensure an allocation of credit that is conducive to the realisation of socio- economic goals.

4.3.1 Quantitative Controls

Some of the instruments that the central bank; may be able to use for quantitative control of bank credit are:

a) Statutory Reserve Requirement

Many central banks have been reducing or eliminating reserve requirements to make banks more competitive. This may not be possible in an Islamic economy where reserve requirements may constitute an important instrument of monetary policy. Banks may be required to hold a specified proportion of their demand deposits with the central bank as statutory reserve. This would not only serve as an instrument of monetary policy but also as an independent source of income for the central bank. Small variations in this requirement may change commercial banks' free reserves by a substantial amount and significantly effect their ability to expand derivative deposits.

The rationale behind a statutory reserve requirement only against demand deposits is the equity nature of mudarabah deposits in an Islamic economy. Since other forms of equity are exempt from a reserve requirement, there is no reason to subject mudarabah deposits to such a requirement. This would tend to matter them less profitable compared with other forms of equity and thus put the commercial banks at a disadvantage by inducing a shift of mudarabah deposits from commercial banks to other financial institutions. It may also be argued that in practice the distinction between demand and savings or time deposits is hazy. This possibility may be substantially reduced in the Islamic system because of the equity nature of mudarabah deposits and the sharing in risk which this would necessitate.

It may also be argued that the statutory reserve requirement against total deposits does not aim mainly at regulating the quantity of credit. It is also concerned with ensuring the safety of deposits and adequate liquidity of the banking system. These other objectives may, however, be achieved through higher capital requirement and well conceived and properly enforced regulations, including a suitable liquidity ratio. These measures may be supplemented by an effective bank examination system. The adoption of such an approach may be preferable to the immobilisation of a part of mudarabah deposits through a statutory reserve requirement.

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b) Credit Ceilings

While the statutory reserve requirement may help the central bank in bringing about the desired adjustment in high-powered money, credit expansion may still exceed the desired limit, This is because: firstly, it is not possible to determine accurately the flow of funds to the banking system, other than those provided by the mudarabah advances of the central bank, particularly in an inadequately developed money market like that of Muslim countries; and, secondly, the relationship between commercial bank reserves and credit expansion is not very precise. The behaviour of money supply reflects the interaction of a number of various complex internal as well as external factors, and it may be desirable to fix ceilings on commercial bank credit to ensure that total credit creation is consistent with monety targets.

c) 'Moral Suasion'

The normally suggested tool of 'moral suasion', may also acquire a relatively more important place in Islamic central banking. The central bank, through its personal contacts, consultations anld meetings with banks, may be able to keep, itself abreast of the strengths and problems of banks and to suggest to them measures that would help overcome difficulties and achieve desired goals.

In addition to these instruments, there are two others which may be utilised by the central bank to create a more direct impact on commercial bank reserves than what even open market operations are able to create. These are: government demand deposits with the commercial banks.

d) Government Deposits

The central bank may be enabled to shift government demand deposits to or from the commercial banks, thus directly influencing their reserves. This instrument has proved to be a useful instrument of monetary policy in Saudi Arabia where it has performed the same function directly that open market operations perform indirectly in other countries in influencing commercial bank reserves.

f) 'Common Pool'

The 'common pool' may also be effectively used by the central bank in the same way as the rediscounting facilitiy is used by the conventional central banks to solve the liquidity problems of commercial banks. The banks may be the central bank to contribute to this pool a certain specified proportion of their deposits by way of a cooperative arrangement between them to overcome their liquidity problems on condition that the net use of this facility by any bank over a given period is zero.

Some other instruments have also been suggested in the literature on Islamic

banking. The merit and effectiveness of two of these for monetary policy purposes are briefly discussed below.

g) Equity-based Instruments

One of these is the use of equity-based instruments for open market operations [39] It may not, however, be desirable to do so far a number of reasons. Firstly, while the central bank's purchase and sale of the stocks of public sector companies may not raise objections, its purchase and sale of private sector companies may be questionable. Secondly, equity-based instruments may not have the necessary depth that government securities tend to have. Open market operations in such instruments may, therefore, influence their prices significantly unless used to a very limited extent. This may not be adequate for monetary policy purposes. Thirdly, variations in the prices of equity-based instruments brought about by central bank open market operations may unnecessarily benefit or penalise the shareholders of companies whose shares are used for this purpose, This may not be desirable because the primary objective of such operations is to increase or reduce private sector liquidity and not to introduce inequities in the stock market. Fourthly, the possibility of raising the price of stocks through their purchase by the central bank, specially when their fundamentals do not justify such a rise, may induce corruption.

h) Changes in the Profit-and-Loss-Sharing Ratio

The Pakistan Council of Islamic Ideology as well as some scholars have suggested variations in the profit-and-lass sharing ratio for mudarabah advances provided by the central bank to the commercial banks and for prescribing the depositors' and the entrepreneurs' share on the mudarabah deposits and the financing provided by the commercial banks.[40] While the indication of a reasonable range of profit sharing ratios between depositors, banks and entrepreneurs may be helpful as a guide, it may not be desirable for the central bank to regulate these ratios, as the Council has suggested.[41] This is because the ratio may be determined by profitability, which depends on a number of factors differing from sector to sector in business and industry and even from firm to firm in the same sector. Hence prescribing a uniform ratio may not be equitable while prescribing a band may not be meaningful, particularly if it is wide.

Even if, in accordance with the Council's suggestion, the ratio is regulated by the central bank to "reduce unhealthy competition among the financial institutions", it may not be desirable to vary this ratio frequently as a monetary policy instrument. The central bank may itself, being a non-profit institution, not mind taking a lower share in the interest of realising certain nationally cherished goals, but why should the depositors, commercial banks or entrepreneurs be coerced to

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accept less than a just and reasonabale share of profit? Moreover, if there is a loss, the Shari'ah requires that losses be borne strictly in accordance with the ratios in which financing has been provided, irrespective of whether the financing comes from the central bank or the private sector. While the commercial banks may be happy to get a higher ratio in profit, if such a ratio is prescribed by the central banks, why would the depositors or the businesses being financed be willing to accept a correspondingly lower ratio, if it is out of proportion with their loss-sharing ratio? In addition, once the ratio has been set contractually, which is essential according to the Sharī'ah, the ratio cannot be changed before the end of the contract. To change it even for new contracts may also not be desirable because this would introduce inequities.

Hence it may be better to leave the determination of the ratio to the negotiating parties in conformity with their perception of market conditions and profitability. The central bank or the government may, however, intervene when it is necessary to do so to ensure equity or eschew unhealthy competition. Tinkering with the ratio for purposes of monetary policy may not be desirable.

4.32. Realising Socio-economic Goals

a) Treating the Created Money as Fay:

The creation of M_0 by the central bank resulls from the exercise of its social prerogative and leads to seigniorage (created money minus the cost). Since this leads to command over resources without effort, it may have to be considered in the nature of fay' and used primarily for financing projects that would help uplift the socio-economic condition of the poor and reduce inequalities of income and wealth.[4] It would not be proper for the government to use even a part of it for projects whose benefit would go to the rich.

To fulfil this requirement, the central bank may make the total M_0 created by it available partly to the government and partly to the commercial banks and the specialised financial institutions. The proportion of M_0 diverted by the central bank to each of these three sectors may, like the total size of M_0, be determined by the dictates of monetary policy. The part of M_0 made available to the government may be an interest-free loan to enable the government to finance its social welfare projects designed to uplift the socio-economic condition of poor, including the provision of housing, medical facilities and education to the poor. The part of M_0 made available to the commercial banks and the specialised credit institutions may be in the form of mudarabah advances and used mainly for providing self-employment opportunities to the rural and urban poor, who may not be able to obtain adequate funds for this purpose from these financial institutions.

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b) Goal-oriented Allocation of Credit

Since bank credit comes out of the deposits of all sections of the population, its allocation may be able to satisfy the norm of socio-economic justice in Islam only if its benefit goes to an optimum number of businesses and leads to the production and distribution of goods and services needed by all sections of the population.[3] The appropriate way to achieve these objectives may not be an elaborate network of controls. Since the operation of market forces has been recognised by Islam, it may perhaps be better to overcome the reasons for the less than desired contribution of commercial banks for the realisation of these objectives.

The reason normally given by the commercial banks for diverting a very small proportion of their funds to small businesses is the greater risk and expense involved in such financing. Hence small firms are either unable to get financing from banks or do so at highly unfavourable terms (in terms of cost and collateral) compared with their larger counterparts. Thus the growth and survival of small firms is jeopardised even though they carry a great potential for increased employment and output and improved income distribution.

It may, therefore, be desirable to reduce the risk and expense of such financing for banks. The risk may be reduced by introducing a loan guarantee scheme underwritten partly by the government and partly by the commercial banks. In the case of Islamic banks, the guarantee scheme need not guarantee the repayment of loan with interest as is the case in the conventional system. The scheme should, however, be able to relieve the bank of the need to ask for collateral in the case of small businesses whose general credentials have been registered with or certified by the guarantee scheme. The scheme may do this after a proper investigation of the firms concerned. It may also arrange to train the businesses to maintain proper accounts and be prepared even to have these accounts properly audited where necessary. A large number of small businesses may thus be able to offer the collateral required by the conventional banks. The bank will receive its money back in case of moral failure of the business. The scheme may also be made to include must nan-commercial risks desired to be covered for increasing the availability of funds to small businesses. In case of market failure and the resultant loss, the bank will of course share the consequences with the business in proportion to the financing provided by it.

The additional expense incurred by the commercial banks in evaluating and financing small businesses may be partly or wholly offset by the government depending on the nature of the case and the objectives to be served. The cost to the government exchequer arising from the above two schemes may be justifiable in the larger interest of the goals of the Islamic economy. However, it may be possible to offset the cost partly or fully by graduated fees to be collected by the go-

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vernment out of profits earned from such financing by the banks and the small businesses. In addition, the central bank may even accept a relatively lower profit-sharing ratio if this is considered necessary for realising the objective of distributing commercial bank financing to an optimum number of businesses for the production of the goods and services which are most needed.

5. CONCLUSION

There seems to be nothing in the Shari'ah that would stand against the adoption of a managed money standard by the Muslim countries. In fact they do not probably have any alternative to this standard after the demise of bimetallism, which prevailed during a substantial part of Muslim history, the international gold standard, and the Bretton Woods system. What is necessary, however, is to ensure that this standard is operated in a manner that does not only not violate the Islamic imperative of price stability but also helps realise other socio-economic goals.

The prohibition of riba and the reorganisation of financial intermediation on the basis of profit-and-loss sharing may in fact help in this task. It would help minimise the inessential, unproductive and speculative elements of aggregate money demand which it does not seem to be possible to realise in an interest-based system. The minimisation of these elements of money demand would tend to promote greater efficiency and equity in the use of scarce resources and also help reduce the macroeconomic imbalances that accentuate inflationary pressures and economic instability and vitiate the realisation of socio-economic goals. Once money demand has been managed in a manner that is conducive to goal realisation, it may not be very difficult to bring money supply into equilibrium with such money demand. This may be done with the help of some of the well-known instruments of monetary policy that would be available even in an interest-free Islamic financial system.

It would, however, be necessary to regulate the generation of high- powered money at source. Since a preponderant source of high-powered money is government budgetary deficit financed by borrowing from the central bank, it may not be possible to have an effective monetary policy without substantially reducing government borrowing from the central bank. International experience has shown that only a strong central bank is able to resist dictates from the government to lend amounts which it considers to be beyond the dictates of price stability.[11]

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16 For a brief discussion of these goals, see M. Umer Chapra, Islam and the Economic Challenge (Leicester, U.K.: The Islamic Foundation, 1992), pp. 7-9 and 209-13.

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35 Monetary targetting has become an important instrument of monetary management over the last two decades and widely accepted by a growing number of central banks, particularly among the OECD countries, because monetary management has been found to be fairly successful if this approach is adopted. (See, Bank for International Settlements, The Monetary Base Approach to Monetary Control (Basle: BIS, Sept. 1980), p. 7; Economists Advisory Group, Banking Systems and Monetary Policy in the EEC (London: Financial Times, 1974), p. 116; and OECD, Monetary Targets and Inflation Control (Paris: OECD, 1975), p.1-2). The BIS has strongly supported the use of monetary targetting by stating that "Published objectives of the monetary aggregates will no doubt continue to play a useful role in guiding the conduct of monetary policy and in signalling to the markets the eagerness of the authorities' intentions. The approach was adopted in the industrial countries after other kinds of policy had proved ineffective in preventing inflation from building up and it provides a useful framework for stabilising expectations" (Annual Report, 1981-82, pp. 88-9). The Bundesbank first publicly announced a monetary growth target for 1975; since then such targets have been an important aid to German monetary policy. The Federal Reserve began reporting to the Congress specific numerical "targets" for the growth of the monetary aggregates in 1975. The reporting of growth targets for monetary aggregates was formalised into law in 1978 with the enactment of the Humphrey-Hawkins Act, which requires the Federal Reserve to present annual targets for monetary and credit aggregates to the Congress each February and to review these targets each July. Howêver, In recent years monetary targets have been give 'less emphasis in the U.S., Japan and the U.K., but are still used in Germany, Switzerland, France, Italy, Spain and Greece (see BIS Annual Report, 1994, pp. 128- 29).

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The principal conclusion of a study by Aghevli, et., al., is that "targetting monetary policies as opposed to policies aimed at fine-tuning the economy, are better suited to the circumstances of the Asian countries" (B.B. Aghevli, M. S. Khan, P.R. Narvekar and B. K. Short, 'Monetary Policy in Selected Asian Countries," IMF Staff Papers, December 1979, p. 816).

36 Milton Friedman, A Program of Monetary Stability (New York: Fordham University Press, 1915), pp. 90-91. The controversy over rules versus discretion in the conduct of monetary policy is over a century old but still continues unabated and unsettled. This is reflected in the following views. Supporting the role of discretion, Sayers emphasises: "The essence of central banking is discretionary control of the monetary system.... And working to rule is the antithesis of central banking. A central bank is necessary only when the community decides that a discretionary element is desirable" (R.S. Sayers, Central Banking After Bagehot, Oxford:Clarendon Press, 1957, p. 1). More recently, Sargent and Wallace have emphasised the importance of rules by stating: "There is no longer any serious doubt about whether monetary policy should be conducted according to rules or discretion. Quite appropriately, it is widely agreed that monetary policy should obey a rule' (T. Sargent and N. Wallace, "Rational Expectations and the Dynamics of Hyperinflation", in Studies in Monetary Economics, Federal Reserve Bank of Minneapolis, June 1915, p. 1). With respect to the developing countries, Coats concludes that: "In the light of strong theoretical and empirical support for a simple constant growth-rate rule in developed economies, a priori considerations make the case for a simple rule even more compelling for LDCs... If the lags between the need for change in monetary policy and its ultimate effect on the economy are long and troublesome in the developed economies, the difficulties arising from these are surely more serious in the LDCs where economic data are less plentiful, less accurate and less quickly available" (W. L. Coats, Jr., "The Efficacy of monetary Rules for LDCs" in W. L. Coats and D.R. Khatkhate, Money and Monetary Policy in Less Developed Countries: A Survey of Issues and Evidence Oxford: (Pergamon Press, 1980), pp. 166-7).

37 In their survey of the issues and evidence on money and monetary policy in less developed countries, Coats and Khatkhate conclude that "In LDCs, base money is a major determinant of the money stock and the deficit financing of government expenditure, which is often tantamount to the creation of central bank credit, is a principal factor affecting base money" (W. L. Coats and D.R. Khathate, eds., Money and Monetary Policy in Less Developed Countries: A Survey of Issues and Evidence, (Oxford: Pergamon Press, 1980, p. 32).

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41 The Council's Report (1983), pp. 19-20.

42 Fay'refers to wealth surrendered by the enemy without actual fighting having taken place. Its distribution is governed by the following Qur'anic verse: "Whatever Allah restored to His Messenger

from the people of the towns is for Allah and His Messenger, the near of kin, the orphans, the needy, and the wayfarer, so that wealth does not circulate among your rich" (59:7). This verse stipulates the division of the entire wealth that becomes available to Muslims without effort into five parts and used for reducing inequalities of income and wealth. There has, nevertheless, been a difference of opinion among the fuqaha on the distribution of the total amount of Fay' among the five heads specified in the Qur'an after the death of the Prophet, peace and blessings of Allah be on him. Imam Shafi'i felt that the total amount should be divided equally into the five he ads even after the Prophet's death. The share of Allah and His Messenger should, however, be used for general well-being. Imams Abu Hanifah, Malik and Ahmad did not consider such a strict division to be necessary. They felt that the entire amount of Fay' should be spent for the well-being of all Muslims, particularly that of the poor. Whatever the interpretation, if the principle of Fay' is applied to seigniorage, it would help bring about greater general welfare with more equitable distribution of wealth.

43 While deposits of less than Rs 10,000 provided 37 percent of total commercial bank deposits in Pakistan, advances of less than Rs 10,000 absorbed only 2.2 percent of total commercial bank advances. As compared with this while deposits exceeding Rs 10 million contributed only 11 percent to total deposits, advances exceeding Rs 10 million absorbed 39 percent of total advances. The inequity becomes even More glaring when we see that 29 percent of resources provided by 24.7 million depositors were advanced to only 2,136 privileged borrowers (Based on data for September 1989 in the October 1990 issue of the State Bank of Pakistan Bulletin).

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THEORY AND PRACTICES OF ISLAMIC BANKING

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INTRODUCTION

The Islamic Banking is meant to be, as it is known, the practice of banking business in conformity with Shari'ah. The main factor of violation in the modern banking system is the interest which is usury.

There is a very little knowledge about banking in Islam. What is known that services are allowed and investment is subject to contractual relation based on mudarabah and musharakah. In the golden ages of the Islamic civilization, there were various aspects of banking transactions including cheques drawn, paid and rejected. One of these cases was recorded in poetry when a poet called Jahtha El-Barmaki who lived in Baghdad (from 340-420H) received a cheque of five hundred dinar and this cheque was not paid by the exchanger (the drawee) due to the shortage of the drawer's balance. The poet sent back the cheque to the drawer after he had written on the back of that cheque two verses of poetry:

"If your giving were only a writing without any payment.

Then I would write you a million Dinar without any replacement."

The incident which is recorded to happen in that old time, would be helpful to give us an idea about the possible advanced system where cheques were drawn and returned. The Western historians recorded the first incident of drawing a cheque in London in 1675. This means the cheque of Al-Barmaki was before that English cheque nearly 600 years.

Anyhow, the new wake-up of our generation came to the stage to see banks only on the Western type where believers of Islam stood away. The start for the modern Islamic banking came in its first steps from Egypt where the first saving fund was established in 1963 in Meat-Gamr, a small town near Cairo.

The scholars started to discuss the methods and practices.

Only scholar from Najaf pointed out, in his book "Albank Allarabawi Fit Islam" The Interest Free bank in Islam," the difference between two phases:

Phase 1: to have an Islamic bank in a society where other traditional banks are existed.

Phase 2: to reach the complete Islamic banking system that is governing all practices in a Muslim society.

In our seminar, I am going to tackle the two phases in brief, then I come to the conclusion.

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PART 1
THE ISLAMIC BANK IN A CO-EXISTENCE PRACTICE

Preamble

The modern Islamic banking came to existence in our modern days as a kind of reaction. It was noticed that sincere believers of Islam did not deal openly with banks especially when the matter is related to depositing and borrowing.

The theoretical studies came in the same period where practical steps were taken to establish the first commercial Islamic bank in Dubai in 1975. In 1976 the first complete study about Islamic banking was discussed in Cairo University. This unique aspect of this study was based on the fact that the author, by the time of discussion, was a traditional banker of around 20 years.

Then the Islamic banks were known and they were established in various places, in Egypt and Sudan (the Faisal Islamic bank), in Kuwait (Kuwait Finance House), in Bahrain (Bahrain Islamic Bank), in Qatar (Qatar Islamic Bank) and so on.

The main common feature among these Islamic banks that it was established on the basis of co-existence with the traditional banks.

This idea of the possibility of co-existence pushed some of the-traditional banks, like Misr Bank to open specialized branches for Islamic transactions. Citibank in London established a division for Islamic banking dealings as a method of attraction to channel a part of the Islamic financial resources.

Anyhow, the practices of these Islamic banks were characterized by marginal activities. They were looking only for a way of living without violating the main principles of Islam.

This is natural attitude, but unfortunately, it spreaded its shadow upon this type of Islamic banks. In this part, I am going to tackle some of these results.

1. The methods of financing

Although it was clear to the Islamic bank's founders that modes and methods of financing in Islam were numerous, it was obvious that murabahah was a contract whereby the Islamic bank would buy a specific commodity upon the request of the customer under a concrete promise from the orderer to buy the same commodity on cost-plus profit. This contract was easy to handle and very near to the idea of credit assessment.

Mudarabah, where the unique aspect of combing the capital down to be at the service of human effort, did not find an open door of welcome by most of the Islamic banks. There was a small portion to be occupied by Al-mudarabah in spite of the fact that there was a great need for such a contract to be put again in practice.

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To be fair, one should admit that the society is not ready yet for such honest and sophisticated dealing. The laws, which mostly are translated from the Western Codes do not give coverage to such deals. The standard of accountancy is not up to the level of providing an accurate result.

Other modes of financing such as salam, istisn'a, muzara'a were not and they are yet not developed in our present time to serve the purpose of the real development.

Therefore, it is not strange to see in the true analysis of the balance sheet of an Islamic bank that 90 % of its investment would be classified as Murabahah.

2. The standard of services

Although the financial services are a rewarding business, the Islamic banks in general did not care for providing advanced services to their customers. The relations with customers were kept within the ordinary business ties. Transfer of money, collections of checks and promissory notes, issuing drawing cards and other similar services are not enough for a Moslem banker. There is a need for the social service relations. The guidance of customers to know their financial rights in Islam is a part of the Islamic banking service. The acknowledgement of a widow as how she can take care of the inherited money to support herself and her children is another part of the Islamic banking service. The execution of a moslem's well also is a part. The Islamic bank should not be a business entity only, but it should be as cooperative family.

3. The relation with the central banks and monetary authorities.

The Islamic banks were in most cases not openly welcome by the central banks and the monetary authorities. There was in fact no legal coverage for the establishment of these new forms of banking institutions. Therefore, in some cases the establishment af an Islamic bank was based on a special law (such as the case of the Jordan Islamic bank) or in other cases where the establishment came as a result of a Presidential or an Ameeri decree (such as Dubai Islamic Bank).

Some of the Islamic banks thought that it was better to their safety to be outside the central bank's control, others did find a way of cooperation with the central bank and the monetary authorities.

In all cases, most of the Islamic banking business would contradict in a way or another with the prevailing regulations which are governing the banking business in general.

In very rare cases, some of the Islamic banks did find a way to make a special arrangement with the central bank related to its role as a last resort.

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Still there is a legal gap to be filled between the Islamic banks and many of the central banks where the banking system is open for both methods, the traditional and the Islamic banking. In some countries like the Untied Arab Emirates and Malaysia there are special laws and regulations related to Islamic banking. Turkey made special regulations for the financing institutions which do not charge interest. But still the other laws as the commercial law and the Company's law are not adjusted to cover the Islamic dealings and practices. Also, there is no real coverage to the Islamic based Shari'ah companies like mudarabah, Anan, Wujooh... etc. The Islamic countries are in need for an Islamic companies law which is based on Shari'ah.

While in the commercial law of the State of illinois, there is an article stating that a person or an institution which do buy a commodity or equipment to sell it within 30 days is not a trader, we find that our old fashioned commercial laws taken from the French code consider any person who would buy anything under a purpose to sell is a trader. Consequently, the Islamic banks are considered to be traders and banks are not allowed for trading-business.

Another legal aspect is related to the margin of profit. while interest is deductible in the income tax law, the similar treatment to the margin of profit in Al-murabahah deals was discussable in many countries.

4. Facts and results

The Islamic banking practice has been lead in such an atmosphere to an unfavorable situation as explained below.

A. In most çases the margin of profit in Al-murabahah deals was linked to the interest rates which were prevailing in the same country. This similarity caused some criticism against the Islamic banks which were accused to be using the sale deal as a trick for the mark-up.

B. In the absence of the support, most of he Islamic banks did not play a positive role towards the society. The investments did not enter al-mudarabah and Al-musharakah in an influential manner. The result was a long story of criticism against the Islamic banking practices.

C. The Islamic banks faced the problems of lacking the facilities of having a concrete support as a last resort from the central banks in most of the cases.

Consequently, these banks were obliged to keep a high percentage of liquidity without having a base for a developed Islamic capital market. These banks cannot buy treasury bills which are based on interest discount. In the mean time the Islamic countries do not know the methods of issuing islamic treasury bills to meet the need of the Islamic banks. Therefore, the liquidity was high, the return was low and the result was to accuse the Islamic banks on the basis of lack of efficiency.

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D. The Islamic banks being a part of the divided Moslem world did not succeed on the practical level to cooperate in the field of establishment an international holding Islamic banking company.

Between Pakistan and Bangladesh which they were forming one state in the past, the transfer of US$1000 is still has to be covered by Chase-Manhattan as a payee bank in New York. While it was much easier if the Islamic banks agreed to establish a united Islamic bank to be based in Bahrain, for example, to make such a transfer as a book- keeping entry to debit Islami Bank Bangladesh Umited account and to credit the Muslim Commercial Bank Limited, Karachi.

The lack of cooperation in the field of services did lead to the lack of cooperation in the field of investments.

The Moslemummah like the old description of the Arabic poet who said about the camels moving in the desert, thirsty, while the water is carried on their back.

This is the situation of the Islamic banks with its positive and negative aspects. Is the matter much better where the banking system is totally Islamized ?

This is the subject of the second part Inshallah ta'ala.

PART II

THE ISLAMIC BANKING IN A TOTAL ISLAMIC ECONOMIC SYSTEM

INTRODUCTION

The Islamic economic system is like a building in which each part do support the other parts.

As for the Islamic banking system, it is obvious that the situation should be more clear and prosperous.

While the Islamic banks in the so-called coexistence atmosphere were mainly commercial institutions, the image of these banks should be different where the researcher would expect to find the Islamic industrial bank together with the Islamic agricultural bank besides the commercial Islamic bank.

In addition to the complementary aspect of-the types of the Islamic banking institutions, there are various aspects of the proposed harmony in the system. The most important aspects are the central bank's law and practice, the monetary and credit policy, the capital market and the various supporting laws such as the company's law, income tax law and the commercial law.

While in theory the coexistence Islamic banking procedures came before the practice; the case in the whole changed system, the practice was faster than the theory.

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In this part, I shall tackle some points which are related to the Islamic banking in a built-in system as in the case of Iran, Pakistan and Sudan.

1. The purity of the application

The first point which should be clear in a complementary Islamic banking system is to free the murabaha from the influence of the rate of interest. The margin of profit can be measured on a socioeconomic basis. The central bank can use the margin of profit as a directive for the use of Financing.

For example, in case of trade in Food Stuffs, the margin of profit should be low 6 % while in case of trade in luxury items such as Television sets, the margin can be doubled up to 12 %. For industry, the raw materials to be traded in on a margin may be 8 % and so on.

As for the percentage of the distinction of profit in Mudarabah and Musharakah, there should be a clear understanding of the social purpose. While making profit, the system should not forget the duty of building the society. The percentage of profit to the Islamic bank can be limited as to be between 20 %-30 % of the net profit of any project. And if it appeared by calculation that the 20 % when compared with the capital is still high, the extra can be returned to the other partner as a refund. It is known generally that, the profit is according to the agreed upon conditions and losses are distributed according to ownership of the capital.

In muzara'a and musaqat, the same principles of musharakah can be applied. And in Salam the discount in the price should not exceed a certain percentage as if it is a murabaha deal with a higher margin of profit because of the high risk involved.

By this liberation form the interest, the funds of the banks can be directed to the different sectors of production.

Therefore, in a complete Islamic banking system there should be no apology for increasing al-murabahah and decreasing al-mudarabah and al-musharakah. There is no excuse for competition by the traditional banks. The important thing is the sound distribution of the facilities according to the economic and social needs of the society.

2. The Complementary of the Institutions:

The banking institutions are in the complete system parts of a team. The commercial banks should be directed by the central bank to deposit in investment accounts with the specialized banks (agriculture and industrial) a certain percentage of their total deposits. This arrangement should be as of the liquidity and cash reserve requirements.

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The central bank shall play the role of the last resort as a depositor and not as a lender. The adjustment also should be noted where the cash money is concentrated in the capital and the big cities, while the urban districts are suffering form the shortage of capital and cash.

3. The social role against unemployment-

The social role of a complete Islamic banking system is very important. Every able man or woman should be given an opportunity to produce. From a driver - to be owner of his rent-a-car project, to a housewife lady managing a three tricomachine factory, there is a place for production on the participation basis. Money has no meaning to stay as a balance in the bank's books. The place of money is to be used in production. No land should be allowed to be kept unplanted. The farmers are ready, then give them the machinery and the right guidance.

The producing people is the target of any Islamic banking system. This is our goal. No idle money and no idle brains or hands.

4. The Islamic Capital Market

As an alternative for the governmental treasury bills, there are many responsibilities to issue Muqaradah bonds, participating income bonds and Murabaha bonds for the public financing in any project where the profit can be shared or arranged.

The banks would act as a mediator between the citizens and the central bank. they can use these bonds for their purposes as a possible window for investing the surplus liquidity.

The provinces can issue bonds for their own projects, and the central government can do the same for bigger schemes.

5. The necessary revision of the related laws

The commercial law, the company's law, the central bank and banking law, the investment law and other laws should be reviewed to be in harmony with the new change in the banking system.

Murabaha, mudarabah, musharakah, muzara'a etc. should take its place in the commercial law as part of trading practices.

The court should consider bank cases as urgent case. No delay is allowed to be used as a killing factor for the right investment of the public money.

Misconduct, dishonesty and cheating of a bank should become public crime where a system of black-list should be introduced for those who misbehave in their dealings with the Islamic banks.

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6. Attracting expatriate capital

The immigrating capital is a big problem in the Islamic world. There should be steps taken to endourage such a capital to return home. Not only the money but also the persons.

With the rise of an Islamic banking system should be a rise of trust and freedom. Come back home and be assured you are safe. The whole people in any modern society are in need for each Dollar, Mark or Pound which is invested or deposited abroad. Certain projects which are related to export should be directed for expatriate investments.

These are the ambitions in its theoretical image.

Where are the applications on the ground?

This is our role to find it out, It is the old story about the difference between theory and practice.

Conclusion

By the end of this presentation one would conclude the followings:

1. The possible liberation from the influence of the interest in Murabaha deals of new idea of social-based measure were suggested.

2. The need for complimentary banking institutions. Such as Islamic Agricultural banks, Islamic Housing banks,etc. There should be no limitation to have only Islamic commercial banks.

3. The planned role of the Islamic banks in building up the cooperative Islamic society. More involvement in mudarabah and decreased participation should be looked at.

4. For the building of an Islamic capital market with its suitable instruments as a culmination to total Islamization of the banking system. The government was in need for the arrangement of the suitable type of the Islamic financing and the needs would not wait.

5. There are laws and regulations which are in need to be reviewed as a part of the harmonization.

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ECONOMICS OF ZAKAH

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Introduction

The study of the economics of zakah is based on the assumption that zakah is substantial enough to have an effect on the economy of any society. In other words, if the proceeds of zakah represent a very small percentage of GNP, say 1 per 1000, it may not have any effect on the behavior of the economic units, nor on the economic aggregates and there will be no need for studying the economics of zakah.

It is a basic knowledge about Islam that zakah is the third pillar of this religion. One may even argued that as long as Islam has its own economic system, Zakah must be the first or second pillar of this system.[1] Zakah's place within the framework of the Islamic religion implies that it must have a visible or substantial effect on the human behavior, whether on the individuals sphere or on the sphere collective relationships in the society. Zakah is made very often the twin sister of prayers as it is mentioned, side by side with prayers many times in the Qur'an, and since the Qur'an puts so much weight on the performance of prayers: "For prayer restrains from shame and unjust deeds" (the Qur'an 29:45). Zakah must also adjust human economic behavior in such a way that directs it toward good and away from evil.

Therefore, zakah proceeds must be substantial enough to warrant such an effect on the zakah payers, zakah receivers and the society at large, and this study goes on the assumption that zakah proceeds represent no less than a few percentage points of GDP.[2]

In the present paper, the economics of zakah will be approached from two angles: The economic effect of zakah on individual behavior and on the macro economic aggregates, and issues related to the estimation of zakah in a contem-

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porary Muslim society. Issues related to zakah estimation will be discussed in section six at the end of this paper. The effects of zakah on the economy will be discussed in five sections. Section one will deal with the effect of zakah on individuals both as payers and recipients. Section two deals with the macro- economic effects of zakah on consumption. Section three deals with zakah effect on investment and on aggregate demand. Section four discusses the role of zakah in the macro- economic model of an Islamic economy, thus discussing its inter-action with the principles of the prohibition of riba and of Islamic financing. Section five will discuss the amenability of zakah to be used as a policy tool by the islamic Government.

Section I: Effect of Zakah on Individuals

It is useful to recall at the outset of this section that zakah is a religious financial obligation on the rich to be given primarily to the poor. From economic point of view, it is thus a transfer of resources from the have to the have not. On both sides, this transfer payment, zakah is supplemented by religious and spiritual values.

The effect of zakah on the recipients is obvious. It represents an increase in their real income, whether it is paid in money terms or in kind. In either case, it increases the recipients' command on goods and services available in the society. It, therefore, increases the recipients' welfare. Recipients of zakah are the eight categories mentioned in the Qur'an (9:60). Practically speaking six out of them fall in the low-income segment, one way or another (poor, needy, slave-ransom, people under debt, stipends to fighters for the sake of Allah and wayfarer). The remaining two categories, namely workers for zakah administration and people whose hearts are being reconciled to the truth, are not paid zakah on the basis of poverty. Workers are given zakah against their productive labour utilized in the administration (collection and distribution) of zakah operations, thus zakah contributes here to the generation of income through employment. The heart reconciliation payments are pure grants for religious and political objectives.

This implies that zakah provides income to the poor, income against employment to its administrative workers and income to other people by religious motifs. In all 3 cases, zakah must affect the individual behavior of its recipients through the effect of income increase. Regardless of the income/consumption theory we adhere, to the consumption and saving of recipient categories must increase as long as income influences consumption. It should be noted, however, that zakah may be paid to recipients in cash, in kind as consumable goods, such as foodstuff, in terms of capital goods that can only be used for production, such as craftsman's tools and machinery, or in terms of consumer durables, such as resi-

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dential housing and furniture. The way zakah is paid then affects the distribution of the incremental income obtained as zakah by zakah recipients.[5]

On the other hand, the distribution of zakah improves the welfare of the poor as it represents an increase in the provision of food, health, housing, etc. These welfare improvements should have an effect on the productivity of the poor by reducing the number of days of illness, improving the physical abilities of the poor, etc. This positive effect on productivity may be further enhanced if part of the zakah distributed is given in the form of capital goods, or if it is used by the poor to buy capital goods. The increase in productivity of the poor as a result of the zakah distribution would increase total outcome of the society and adds to the welfare effect that results from zakah.

The Effect of Zakah on its Payers

From the point of view of zakah payers, zakah is a tax, though backed by religious feelings and spiritual endorsement. As derived from the text of the Qur'an and Sunnah, zakah is a tax on income and wealth together with certain conditions and exemptions. Normaly income taxes are levied on personal earnings of individuals and companies, with certain differentiation in tax rates based on source of earning whether it is labour, capital services, gifts or inheritance. Income tax is very often progressive and it provides exemptions for low income categories. On the other hand, capital taxes or taxes on personal assets are usually imposed on assets owned by an individual including real estates, productive machinery and equipment and very rarely common stocks or equities owned in business.

Zakah is levied on the rich as declared by the Prophet (PBUH) in His famous saying when He sent Mu'adh as a governor to Yemen. It is imposed on Amwal (plural of mal) which fit both wealth and income in our contemporary economic terminology. Consequently, zakah is imposed on agricultural output (income in our common jargon), trade net worth (which covers assets at the beginning of the period plus the part of income that was not used for consumption during the year), the total quantity of livestock at the end of the zakah year (this covers the wealth item at the beginning of the year plus whatever increments accumulated during the zakah year), the stock of cash, gold and silver and financial assets at the end of the year (this also covers what we usually call wealth at the beginning of the period plus the accumulated increments that are defined as the saving part of the yearly income.

This leads to an effective rate of zakah on capital higher than its nominal rate, the known 2.5 % in most of the cases, because this nominal rate is not only applied to savings the year but also to tilt: principal stock at the beginning of the year. Thus zakah encourages efficient and productive investment of one's wealth

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because it seems to be putting some kind of a floor for expected rate of return on capital, especially with the encouragement specifically expressed by the Prophet (PBUH) that one must not allow his wealth to be eroded by the consecutive payment of zakah. In other words, if the effective rate of zakah on one's wealth is say 4 %, then one must seek a rate of return that equals at least 4 % in order for one's assets to be preserved, without declining as a result of the repetitive deduction of zakah year after year, if we assume that all capital return is saved and added to the principal invested. This means that effective rate of zakah on capital represents a minimum zakah payers seek in order to protect their wealth from erosion by the effect of zakah.

Moreover, since zakah is imposed on cash money (including bank deposits of all form and maturities and on jewellery and similar assets kept away from productive use, zakah seems to penalize those who leave their assets off the production line. This provides an incentive for reducing this kind of unproductive use of resources or lack (and lag too) of action in using them productively.

A third kind of effect on the zakah payer may be added if we look at the way of zakah collection. In principle, zakah should be collected in a manner that is easier for the payer as long as this does not hurt the cause of the poor as a recipient of zakah. This means that zakah must in principle be collected in kind as much as possible. This obviously reduces the inventory of zakah payer and enhances better circulation of goods in the society.[1] It may not be difficult to find ways and means for in-kind collection and distribution in contemporary society, especially if the zakah administration can issue promissory notes to be handed to the zakah recipients (poor and needy) for in-kind goods that can be exchanged at zakah payer's for delivery of the specified goods.

Section II: The Effect of Zakah on Aggregate Consumption

To understand the effect of zakah on aggregate consumption we should look into the implicit assumptions that underline this effect. Zakah simply redistributes income essentially from the rich to the poor (and also to employees of zakah administration). If the proportion of this increment of income assigned by the poor for consumption is higher than the proportion of consumption to income forgone by the rich as a result of decline in the latter's income, then aggregate consumption increases as a result of the distribution of zakah, and vice versa. Thus the whole argument centers around the marginal propensity to consume of the rich and the poor, the size of basic indispensable consumption needs of the poor and the time lag between collection and distribution of zakah.

One may argue that if we consider a Keynesian theory of income in which the-

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re is one aggregate consumption function that applies to all members of the society, rich and poor, and assuming that this function is linear represented by the equation C = a + b y. Then the marginal propensity to consume (b), is the same all over the function, implying that an increase of the income of the poor on the lower levels of income results in an increase in consumption that equals the decrease coming from the decline in the income of the rich.

This is true as long as the poor is on the right side of the vertical axis, but if the poor has zero income, i.e. at the point a on the C axis, he/she still has to spend o¯a on consumption to meet the basic needs for survival, (this amount of consumption is necessary regardless of income, and below it the person does not survive). The same amount of consumptin is also needed if income is negative; i.e, at negative income, the function becomes horizontal at a height of o¯a. This means that zakah paid to the very poor, with negative income will all go to consumption until one exceeds y = o. In other words, at negative income, any increment in the poor's income, as a result of zakah disbursement, will all be consumed as it falls below the minimum level of consumption. In this case only, the redistribution of income under the above mentioned assumptions increases aggregate consumption.

Similar argument may also be stated with regards to the permanent income theory represented by the equation C = b y, whereby an increase of the income of the poor as a result of zakah receipt increases aggregate consumption by an amount equal to the decline of consumption resulting from the rich's reduction of income.

Actually the discussion of the effect of zakah on aggregate consumption must then take a different approach. It may fairly be argued that the society consists of at least two income categories, rich and poor and that these two categories have different propensities to consume. The marginal propensity to consume of the poor is higher than that of the rich. In terms of the Keynesian income theory (and the same applies to the permanent income theory), we are faced with two separate consumption functions, one applies to the rich category and the other applies to the poor categories. These two functions have different slopes, i.e. b in the above equation differs from the poor to the rich. Moreover, the poor's b is higher in value than the riches. In this case, a transfer through zakah from the rich to the poor increases total consumption in the society, i.e, it increases the slope of the aggregate composite consumption function which is derived from the addition of the two consumption functions of the poor and the rich.[5]

However, if the Government or the Zakah Agency decided to distribute zakah in kind instead of in cash, which is equivalent to forcing the poor to consume what has been distributed, the increase in consumption will be equal to the amo-

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unt of zakah distributed. A close result could be obtained if zakah is collected in-kind, because in-kind collection of zakah reduces inventory of zakah payers, not their money income. This does not necessarily reduce their consumption.

The effect of the size of basic needs, or the part of consumption that is independent of income can be seen from the previous analysis. Basic needs are not the same in all societies because there are social, cultural and religious ingredients in their determination in addition to the biological needs.

Lastly, because zakah transfers income from the rich to the poor, the timing of its collection and distribution influences its consumption effect. If zakah is collected in period 1 and distributed in period 2, aggregate consumption declines in period 1 and it has to wait until period 2 for the compensatory effect that comes as a result of its distribution. This time lag effect on consumption may be reversed if zakah is distributed (say, on loans from the central bank) before the collection time.

Section III: Effect of Zakah on Investment and Aggregate Demand

If we can fairly conclude that zakah may have a positive effect on aggregate consumption. This would be reflected as an increase in aggregate demand which would be an encouraging signal for economic activity.

With regard to saving and investment effect of zakah, we have on one hand a reduction in the income of the rich by the amount of zakah paid. This reduction would effect a decline in the rich's savings and their investments, but this may or may not be compensated by the effect of two other elements : first, part of zakah disbursement goes in terms of capital goods to the poor and needy, which is an increase in investment, and secondly, the rise in the poor's productivity resulting from improvement in their health, nutrition and social environment as well as from newly acquired capital, increases the income of the poor segment of the society. This leads also to an increase in their savings (funds available for investment) and in their consumption (further upward push in aggregate demand).

The final outcome, as far as the zakah effect on saving is concerned, depends on which of these effects is quantitatively higher.

As for investment, their ought to be a market signal calling for an increase in investment resulting from the zakah caused increase in aggregate consumption. The response to this signal would be an increase in investment under relevant assumption if equilibrium is assumed to be maintained. There are two main sources for this kind of signal related to zakah: (1) the increase in consumption of the poor caused through their income effect on consumtpion as well as through productivity increases, and (2) the in-kind distribution of zakah proceeds, whether in

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the form of consumption goods (durable as well as perishable) or in the form of capital goods,

However, one may take into consideration the Islamic values regarding consumption that call for elimination of extravagance, vanity and waste. These values help increasing investment by redirecting resources away from these forms of consumption.

Moreover, we have noticed that zakah is also imposed on items of wealth left idle, as cash money, demand deposits, jewellery, etc. Zakah on these items encourages their use in production or in consumption because it represent a form of penalty on leaving them idle.

Finally, it should be noted that all the amount of zakah distributed in the form of new capital goods represents an increase in invesment.

Section IV: Zakah and Micro-models in Islamic Economics

The essential idea of the role of zakah in macro-modelling in Islamic economics is based on a combination of zakah and the prohibition of riba as known in shari'ah.

There are several attempts to build a macro-economic model in the Islamic economics ventured by several Muslim writers. All of these models are one way or another based on macro and growth models in the western literature.

M.M. Metwalli derived his Islamic macro-model from the well known IS-LM economic model after introducing the following changes

a) The inclusion of zakah in the model is assumed to create an upward shift in the consumption function in addition to a change in its slope as a result of a higher marginal and average propensities to consume that is created by shifting income from persons with lower marginal propensity to consume to persons with higher marginal propensity.

b) Since zakah rate is given by revelation, the writer added a tax variable whose rate is left to be determined by the Islamic Government as a policy tool.

c) He substituted the rate of interest in-the investment function by an expected rate of return on investment and secondly, while the relationship between the rate of interest and investment is negative in IS-LM model, the relationship between expected rate of return and investment is positive in the Metwalli's variant.

d) He eliminated speculative demand for money from the money demand function. This saved him the hustle of liquidity trap. Thus the money demand becomes a function of income alone.

Then Metwalli proceeded to discuss the effect of an increase (decrease) in

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the rate of taxation as it is known in the IS-LM analysis.

Mukherji uses a variant of Cambridge growth model in which he added the zakah, with its known main salient features, whereby zakah is imposed on the stock of wealth as well as wealth increments with the exemption of the part of wealth that is used as production equipment, zakah is also levied on the saving part of income (the part that is not used for consumption) whether it comes from wages or from profit, and finally, zakah is proportional not progressive. Mukheji proceeded with his analysis concluding that the equilibrium growth condition can be fulfilled in any economy in which zakah is collected and distributed at a positive rate of growth in the two cases where zakah is collected from the rich on their growing wealth and distributed to the poor in the form of wage substitutes, and also in the case in which zakah is collected on both the stock of wealth and its increments at the same time.

Al Jarihi derived his model from the growth model known as Kaldor-Pasinetti's. He incorporated zakah in the model by dividing the society into zakah payers and zakah recipients. The income of each group is derived from wages and profits since both groups own productive properties while working for wages at the same time. Obviously, zakah is taken from payers as a reduction of their income while not all of its proceeds is given to the poor as an increment in their incomes since some policy-determined percentage is given to other recipients of zakah as mentioned in verse 9:60 of the Qur'an.

Al Jarihi's conclusion is that, in contrast with the Kaldor-Pasinetti model, the income shares of the rich and the poor not only depends on themarginal propensity to save the capitalist class but also on the marginal propensities to save the rich, the poor and other users of zakah proceeds. Also the income shares in the economy are influenced by the size of zakah and by the policy-determined share of zakah proceeds given to the poor. Factor shares are also influenced by the presence of zakah as well as its distribution.

In comparison with the Kaldor-Pasinetti model, Al Jarihi concluded that an Islamic economy in which zakah is implemented and riba is prohibited (i.e. idle resources are not only forbidden from earning an income as it is the case in the capitalist system of interest, but also penalized by imposing zakah on them), saving must all be channelled to physical investment and there will be less income disparity between the rich and the poor, higher rate of return on capital and higher rate of growth at the steady state.

Section V: Zakah as a Tool of Economic Policy

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It is useful to remember at the beginning of this section a few important points related to the role of the Islamic Government vis-a-vis zakah implementation. Zakah collection and distribution are essentially a responsibility of the Islamic Government. The Qur'an (9:103) addresses the Prophet (PBUH) as Head of State to collect zakah. Consequently, the Prophet (PBUH) used to appoint zakah collectors and distributors to go around the different part of the then Muslim land collecting zakah and distributing it to deserving recipients. Additionally, when the Prophet (PBUH) sent Mu'adh as a governor of Yemen, He told him to inform the then new Muslim Yemenis that God imposed zakah "to be taken from the rich and given to the poor". This practice continued in the Muslim countries until the fall of the Ottoman State." Only when the state neglected, or abstained from, the collection of zakah that individuals went on paying it personally to deserving recipients in order to fulfill their religious duty towards Allah. This means that the Islamic state is essentially the body that is required to take necessary action and decisions regarding the collection and distribution of zakah. In other words, the necessary condition for the use of zakah as an economic policy tool is satisfied by the fact that zakah management is basically put in the hand of the Islamic Government.

In order to see whether the sufficient condition is satisfied, we should look into the question of the extent of the power the Islamic has with regard to zakah. From the texts of Quran and the Sunnah and from our fiqhi heritagewe may find the following points

The rates of zakah on different items of wealth and income are determined by revelation (Sunnah); this cannot be altered by any authority including the Islamic Government and its Shura.

Also some clear cut exemptions that are indicated in the Sunnah cannot be brought into zakatability by any legislative action. These include, for instance, personal foodstuff stored at home, clothing, residence, personal transportation, household items, etc.

3) This still leaves a vast area for ijtihad in political decisions with regard to zakah coverage of items disputed fugaha, especially with regard to new forms of wealth and income including productive fixed assets, productive equities, jewellery, ornaments, decorative items, wages, salaries, professional income, etc. In this area the Islamic state can adopt any opinion that suits the level of its economic development without violating the principles of social and economic justice.

4) Another vast area left for political decision-making relates to the procedural matters of zakah collection and distribution. This area includes the following:

a) Collection of zakah in-cash and/or in-kind:

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In the collection of zakah, the Islamic Government can select any combination of in-cash and in-kind that suits a given economic situation, and promotes the economic objectives of zakah in specific and those of the Islamic state in general.

b) The distribution of zakah in-kind and in-cash:

Also here the selection of the percentage in-cash distribution of total zakah allows the Islamic Government to take the distributive decision that is most suitable for fulfilling the objectives of zakah. By the same token, the selection of goods and services utilized in the distribution of zakah is equally important from the point of view of the use of zakah as a policy tool. For instance, zakah may be distributed in the form of consumer goods or capital goods or consumer durables in order to enhance certain economic objectives. As an example, suppose the Government has a wealth redistribution targets, it can achieve it by distributing equity titles in common stock companies owned by the rich.

c) The timing of zakah collection and distribtuion:

Keeping in mind that zakah is basically an yearly levy, shari'ah has no strict fixation of any special day of the year whereby zakah should be collected and distributed, especially in a contemporary industrial society.[7] The Islamic state can select any suitable gap in timing between collection and distribution in order to serve its economic objectives.

d) Delay of collection of zakah and its collection in advance:

The Islamic Government can delay the collection of zakah in certain years because of economic depression or crisis. It can also choose to collect zakah in advance for one year or more to come in order to inflict certain quick and important structural changes in the distribution of wealth and income in the society.

e) Geographical location of collection and distribution:

It is known in shari'ah that, in principle, zakah should be distributed in the same locality in which it was collected; but it is also permissible for the Government to transfer zakah from one locality to another at times of crisis, pressing needs or important interests of the ummah that can be served by such a transfer.

Flexibility of political decisions with regard to above mentioned five areas makes out of zakah an important tool for social and economic changes. By using these zakah policy tools, the Islamic Government can incorporate structural as well as current changes in wealth and income distribution; it can manipulate aggregate consumption and investment, by taking proper action to encourage aggregate consumption at time of recession or discourage it at time of boom.

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Section VI:
Issues Related to the Estimation of Zakah in a Contemporary Islamic Economy

The objective of estimating the proceeds of zakah in a contemporary Islamic economy is to see the expected size of transfer payment that zakah can do, and assess the resources available for use by the zakah authority in fulfilling its disbursement objectives. This kind of estimation is no doubt important in the decision-making in the Islamic society where zakah is actually implemented. The estimation of zakah proceeds is also important from a theoretical point of view in order to analyze the potential effect of zakah collection and distribution in an Islamic economy and to estimate the zakah empirical effects, if it were to be collected and distributed by Islamic Governments in today's world.

If we want to estimate the proceeds of zakah in a contemporary Islamic economy, we will be faced with two major kinds of problems: Fiqhi problems and information problems.

Fiqhi problems of zakah estimation

The fiqhi set of problems arises from two facts: first fiqhi opinions were developed many centuries ago in economies that have essential differences from ours, especially from the point of view of zakatable items. Hence, before industrial revolution and, more specifically, before the rise of modern technology, fixed assets investment were a small ingredient in any industry; whereas in today's technology fixed assets represent huge wealth necessary for the production of goods and services. Additionally, contemporary technology of financial assets manipulation allows owners of wealth, who seek to maximize their return, to shift the use of their assets from one business to another in a short time, much quicker than could be imagined at the time when the fiqhi rules were developed.

Moreover, new forms of assets are invented that were not at the time of development of fiqhi rules and the relevant weight of certain forms of assets and sources of income has undertaken deep changes, especially after the technological and informational revolution.

All these call for new religious opinion and new ijtihad about these new assets and sources of income.

The second cause of fiqhi problems results from the fact that we have different fiqhi opinions on many of the issues related to zakah. Three examples of these opinions may explain this: (1) the degree of zakah coverage of agricultural products varies between all kinds of products to only wheat, barley, date and raisin; (2) the extent of zakatability of only livestock grazing on free pasture and inclu-

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ding farm raised livestocks; and (3) the nisab of cows is not settled among Muslim scholars, keeping in mind that, in all Muslim societies, cows are now in much more use than camels whose nisab is undisputed.

These fiqhi difficulties can however be dealt with even at the cost of extra hardship on the part of researchers. For instance, the researcher may identify different sets of opinions and make zakah estimation on the basis of one or more of these sets. He/she may take the Hanafi views or the Al Qaradawi views and estimate zakah accordingly.

Information Problems

The information problems in estimating zakah arise from the fact that data necessary in zakah estimation are not usually available in published statistics of the Muslim countries. For instance, there is no data about the total amount of bank deposits that belong to persons owning nisab above. By the same token, published agricultural statistics do not distinguish between farmers producing more than nisab and those who are producing less than nisab. Also there is no data published on personal wealth, and whenever it exists, it is not itemized in such a manner that allows to consider the exemptions of personal effects known in shari'ah. All these statistical difficulties impose on the researcher important limitations that would require a combination of searching in the raw data, that only exists in the offices of statistics departments in Muslim countries, from which aggregate figures are normally derived, and making many guessing assumptions on many zakatable items.

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1. If we consider Oneness of God, to Whom heavens, earth and all that is in between belongs, as the first pillar of the Islamic economic system, then zakah becomes its second pillar.

2. In a study on the estimation of zakah in some Muslim countries, Monzer Kahf concludes that Zakah proceeds may be between 2 % and 8.5 % of GDP in 8 Muslim countries selected to represent oil producing as well as non-oil producing countries (Financial Potential of Zakah in Muslim Countries", unpublished study, Monzer Kahf, IRTI, 1986). Abdallah Al Taher estimates zakah proceeds between 4.2 % and 14.2 % in 18 Muslim countries, see Abdallah Al Taher, "Zakah Proceeds and Social Development in Financial Resources of the State in Contemporary Society from Islamic Perspective (Arabic), Monzer Kahf, editor, publisher: IRTI, Jeddah, 1959).

3. It may be difficult to think of salaries of zakah workers paid in real terms, but it is not difficult to pay the poor and needy who represent the essential objective of zakah as a transfer payment in terms of real goods whether consumable, consumer durables or capital goods.

4. In-kind collection of zakah used to be the rule at the time of the Prophet (PBUH) not an exception.

5. The same may be represented by a non-linear unified consumption function, at which the marginal propensity to consume at lower levels of income is higher than what it is at higher levels.

6. It also continued, uninterrupted, in Yemen until today.

7. It is known that zakah on agriculture is due at the time of harvest and zakah on livestock is due at the time of grazing in open pasture (to be collected on drinking fountains and ponds). These dates are only suggested in the Sunnah for convenience of zakah payers and both items may not represent a high percentage of total zakatable wealth and income in a contemporary industrial society. Furthermore, even these dates are not strictly binding on the Islamic Government as it can alter collection to a different date in the year if it is more convenient to all parties.

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ECONOMIC COOPERATION AMONG ISLAMIC COUNTRIES

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I. IMPORTANCE OF ECONOMIC COOPERATION FROM THE ISLAMIC PERSPECTIVE

Cooperation is not a new concept for the Muslim societies. The Holy Qur'an stresses the importance of cooperation as the effective tool for the realization of socio-economic goals for the individual as well as for communities by mentioning the word "taawun" and its derivatives in different places. Furthermore, Islam pays special attention to human problems and their solutions from a special angle that of brotherhood and cooperation. The word "society" (jem'ia) which signifies a process of people drawn close together is used in many places and in different fashions in the Qur'an and Hadith.

In fact, one of the important features of Islam compared to other religions is its concept of the community of brotherhood with its instructions for society. Furthermore, contrary to what obtains in western societies, community in Islam is not considered as a group of people in a location or in a region but is described in a larger concept which exceeds regional and national boundaries.

It is also interesting to note that despite the fact that the words "cooperation" and "society" originated from Latin they were not practically used until the 18th century A. D. Perhaps the English language coined these terms because of the changing socio-economic conditions in that century. History points out that the concept of a society based on cooperation and a cornerstone for balanced human development was first perceived and introduced by Islam much earlier than western societies. Among many ayats in the Holy Qur'an especially the ayah second of the surah V (Maidah), the 104th, 105th, 110th and 114th of sura III (Al-i-Imran),

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the 41st and 71st ayats of the Surah IX (Toubah), 41st Ayah of the Sura Hajj XXII, put a special emphasis on the importance of cooperation and collaboration among Muslims.

Apart from the Holy Qur'an, the prophet Muhammad (pbuh) strongly advised his followers to cooperate and help each other in order to set up a strong and prosperous society. (Sahih Bukhari Vol. II. p.1368). The practices during his era and the later periods proved that whenever the Muslim were united they held a strong position in the world economy and political order. Having lived a glorious history it is the new time for the Muslim countries to readopt the concept of Islamic cooperation and carry out the necessary actions to regain at least same part of our previous power.

It was in this outlook that a number of meetings, conferences were organized, economic and political groupings were encouraged so that closer connections through regional scenes could be forged among Muslim countries.

II. SOCIO-ECONOMIC CONDITIONS OF ISLAMIC COUNTRIES

Statistics on socio-economic conditions of the Islamic countries show the following facts:-

It is calculated that 60 % of the world area belongs to developing countries and 40 % is covered by the industrialized nations. Islamic countries hold 19 % of the world total land, 13 % of the arable and productive zones, of which only 6 % is subject to irrigation. Furthermore application of modern technological facilities is very limited. For example, in 1991 the number of tractors in 47 Islamic countries was less than 1,5 million (5 % of the world total figure of which half of it was being operated in Turkey). A similar situation was apparent in the use of other operational inputs such as insecticides, chemicals and pesticide. Since half the Islamic countries are badly affected from hunger and poverty conditions they have to divert more resources to the agricultural sector and food security areas.

Statistics indicate that by 1992 the world population was exceeding 5.5 billion of which 4.5 billion or 82 % were living in the developing countries. It should be noted that although official population figures of the IDB's 47 member countries were over 1.1 billion in 1992. With the addition of newly independent Central Asian Republics, the Muslim communities of non-member countries like India, Russia and China and other parts of the world this figure climbs to 1.5 billion. In fact, the fast growing population rate of 2.3 % (some countries like Jordan with 4.7 %, Saudi Arabia with 4.6 % and Oman with 4.2 %, hold world records) will bring the Muslim population total to nearly three billion by the year 2025 which means that one-third of the world population will be Muslim in less than three decades. The

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average population growth in the industrialized world on the other hand is less than 1 % with a resultant dropping of their share of the world population from 15 % (822/5350) in 1991 to 11 % (922/8247) by 2025.

Despite having a larger share in the world population, the average life expectancy at birth of the Islamic countries is only 58. This figure is 64 for the average of the developing countries 66, for the world average and 77 for the industrialized nations. In other words the citizens of the wealthy nations have a 30 % higher life span than the average Musims. Sectoral distribution of the population shows that nearly two thirds of the population in Islamic countries live in rural areas and are engaged in agricultural activities. Because they cannot utilize technological inputs, their income depends on the mercy of nature. Unfavorable internal and external market structures and organizational weaknesses exert an extra burden on the farmers of these poor nations.

The latest statistics indicate that the Islamic countries should give priority to combating illiteracy. Currently 46 % of the whole Muslim world cannot read or write. Consequently, nearly 450 million people suffer from illiteracy, face various socio-economic, cultural and political problems and contributes very-little to the developmental activities of their countries. The gloomy picture of the Islamic countries can also be observed from National Income statistics. Average per capita income in the industrialized countries was over U.S$ 15,000 in 1992. It was U.S$ 3,000 world-wide, whereas in the Islamic countries taking into account oil producer countries, it was U.S$ 2,000. Closer analyses show that among Islamic countries only 4 oil producing countries (Brunei, UAE, Qatar and Kuwait) were among the high income group, and 7 other oil producing nations (Saudi Arabia, Bahrain, Oman, Libya, Malaysia, Iran, Algeria) were in the upper middle income economies. Five countries (Turkey, Tunisia, Jordan, Syria and Morocco) were in the lower middle income countries. Thirty of them were categorized in the lower income earners, of which 20 were known as the poorest nations on the world with less than U.S$ 500 per capital income.

Despite having very limited economic and financial resources, authorities of Islamic countries gave priority to spending for defence and military purposes rather than channeling their efforts towards educational and health projects. The U. N. statistics confirmed that in 1992 industrialized countries on an average allocated 9 % of their central government expenditures on defence purposes, 12 % for education, 13 % for health and 40 % for the social welfare purposes. These ratios were 18 %, 11 %, 3 % and 6 % respectively for the Islamic countries. In other words the Muslim world has devoted enormous amount of resources for military purposes (18 % instead of 9 %) but very little for health and social welfare programs. It

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has been frequently argued that misallocation of resources has caused delays in the socio-economic development of the Islamic countries.

The industrialized nations have been dominating world trade. Controlling 80 % of export and import transactions. During the last ten years the share of world trade of the 47 Islamic countries did not exceed 8 %. Despite the fact that intra-trade among them is around 9 %, 85 % of their exports and 90 % of their imports are shared among the high income group countries.

Another alarming fact is the dependence of the Islamic countries on Western capital through external debt arrangements. Total debts of the Islamic countries were nearly U.S.$500 billion (30 % of the world total) in 1993. As part of this burden the Muslim world was forced to pay U.S.$35 billion in annual installments and another U.S$20 billion in interest payments for a total of over U.S.$55 billion to be paid to the financial institutions and governments of the western countries. The World Bank statistics show that the external debts of the Islamic countries is nearly two-third the value of their Gross National Products (The highest being Guinea Bissau at 325 % and the lowest being Iran at 11 %).

III. A GENERAL OUTLOOK OF THE INTERNATIONAL ISLAMIC ORGANIZATIONS' INTENT TO PROMOTE ECONOMIC COOPERATION

The economic and social conditions which have been briefly highlighted above indicate the difficult task faced by the national regional and international organizations which intend to promote economic and social cooperation among the Islamic countries. It may be attributed to a number of reasons.

First of all, 90 % of the Islamic countries received their freedom and independence soon after the Second World War, especially during the 1950-1965 period, having lived under the colonial rule of British, French and other European nations for centuries. The concept of inter Muslim cooperation was a new phenomenon for them. They were interested in solving their problems on an individual basis rather than looking for partners. Secondly, the borders as designed by the colonial powers brought problems rather than peace and security to the region. Consequently soon after independence most neighbors became enemies rather than close friends and allies. Thirdly, the area covered by the Islamic nations stretches from Senegal in West Africa to Indonesia in the far orient and Albania in the north to Uganda and Yemen in the South. Between these four directions over 51 countries are situated of which 23 of them in Asia and 28 of them in Africa. Statistics demonstrate that over 85 % of the Islamic countries' export is based on three core commodities in the case of the oil producers countries nearly 95 % of the external income is based on crude or refined petroleum products, whereas

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two main agricultural products hold over 90 % of the export revenue of 28 Islamic countries. Apart from the international institutions the Organization of Islamic Conference (OIC) and the Islamic Development Bank (IDB) almost all the cooperation schemes have been based on the regional, sub-regional and neighborhood levels. Furthermore, it is clear that some collaborative actions have been based on temporary friendships or defensive purposes of leaders and presidents, rather than on sound, long-term, feasible projects and strategies.

The official documents indicate that 115 institutions were established within the OIC region partly to accelerate socio-economic development through cooperation with other nations and partly to create a better image on an international scale as well as to meet the demands of the western governments and financial institutions during the last four decades. As shown in the appendix the regional break down of these institutions can be summarized as follows:

Number of institutions in	
Africa	17
Asia	13
Arab Regions	26
International Islamic Organizations	20
United Nations	24
Other categories	15
Total	115

The above table confirms that large numbers of organizations and institutions are involved in promoting various socio-economic and financial cooperation schemes, plans and strategies in the Islamic World. Consequently the problem is not only to establish an institution, an organized committee or a commission, but also to make a clear-cut definition of the objectives and the effectiveness of each establishment.

A further analysis of the existing institutions shows that one third of them are mainly concerned solely with trade and economic development issues of the OIC member countries. The rest of them aim to promote general economic, financial, trade and development activities, including improving relationships with the non-member sates.

It is interesting to note that emphasis on economic Cooperation among some Islamic countries, in particular the Arab states started as early as the 1950's. Soon after the formation of the UN Economic and Social Commission for Asia in 1947, the League of Arab States (LAS), and the Arab Economic and Social Council

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(AESC) were established in 1950. These were followed by the establishment of the West African Economic Community (1959), the Organization of African Unit (1963), the African Development Bank (AfDB) 1963, the Arab Common Market (1964), Council for Arab Economic Unity 91964), Arab Educational, Cultural and Scientific Organization (1964), the Central African Customs and Economic Union (1964), the Economic Cooperation Organization (1964) and finally the Organization of the Islamic Conference (1969).

The second wave of establishment of Regional or Sub-Regional Organizations to promote economic cooperation within the OIC zone took place from 1970 to 1980 particularly Arab and African region. During this period 23 organizations were established mainly the Middle East and North Africa where the increase in oil prices played an important role. These institutions can be cited briefly as follows:

- Arab Fund for Economic and Social Development (1971)
- Arab Organization for Agricultural Development (1972)
- U. N. Economic and Social Commission for Western Asia (ESCWA,1973)
- African Development Fund (1973)
- West African Development Bank (1973)
- Islamic Foundation (1973)
- Arab Bank for the Economic Development of Africa (1974)
- Arab Fund for Technical Assistance to African and Arab Countries (1974)
- Asian Clearing Union (1974)
- International Fund for Agricultural Development (1974)
- U. N. World Food Council (1974)
- Inter-Arab Investment Guarantee Corporation (1974)
- Islamic Development Bank (1975)
- Central African Development Bank (1975)
- Arab Monetary Fund (1976)
- Arab Petroleum Investment Corporation (1976)
- Arab Authority for Agricultural Investment and Development (1976)
- Economic Community of the Great Lake Countries (1976)
- Islamic Commission for Economic, Cultural and Social Affairs (1977)
- Center for Research in Islamic Economics (1977)
- African Fund for Guarantee and Economic Cooperation (1977)
- Statistical Economic and Social Research and Training Center for Islamic Countries (1978)
- Islamic Center for Technical and Vocational Training and Research (1979)

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The third wave of establishments concerned with various aspects of cooperation were generally formed at the OIC level. Their aims is to give service more on an international level than to restrict themselves to limited areas. These organizations include the following:-

- Islamic Foundation for Science Technology and Development (1981)
- Islamic Research and Training Institute (1981)
- Islamic Fiqh Academy (1981)
- Islamic Center for Development of Trade (1983)
- Standing Committee on Culture (COMIAC), Economic (COMCEC) and Science (COMSTECH) (1983) and specialized universities in Islamic Affairs in Pakistan, Malaysia, Niger and Uganda.

The Arab countries were also active in forming a number of regional organizations to foster economic, financial and political cooperation among themselves. Some of these establishments like the Gulf Cooperation Council made important attempts to form a common economic policy within the Gulf region whereas some other institutions like the Arab Cooperation Council and the Arab Magreb Union were able to fulfil only some of their objectives.

It was realized in the early 1970s that cooperation among various Islamic Organizations was also an important issue. Consequently two major establishments - the Organization of the Islamic Conference (OIC) and the Islamic Development Bank (IDB) put an emphasis on coordinating their activities. The OIC reviews the activities of its various organs and committees twice a year and finalizes its economic strategies at the COMCEC meetings in Istanbul. The IDB Executive Directors hold at least six meetings a year. Board of Governors of the Bank (usually the Finance and Economic Affairs Ministers of its member countries) gathers at the General Assembly where all the activities are reviewed policy issues are discussed and future strategies are decided. Furthermore, representatives of Islamic Banks and National Development Agencies attend.

Among other responsibilities the Organization of the Islamic Conference (OIC), as a supreme body of all member countries, is also responsible for defining and implementing the economic and social policies for the well being of Muslims around the world. This important duty is mainly by three basic organs of the OTC. These are:

Standing Committee for Economic and Commercial Cooperation (COMCEC) founded in Ankara in 1984; Since then the Chairman has always been the President of Republic of Turkey. The main objective of COMCEC is to implement the resolutions adopted by the Islamic Conference in the economic and commercial

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fields, to examine all possible means of strengthening cooperation among Islamic states, and to put forward programs and proposals likely to improve the capabilities of Islamic states in these countries. COMCEC has been working very closely with the Islamic Development Bank as well as the other organs of the OIC, such as the Ankara and the Casablanca Centers, and monitoring the preparations of the required documents. The Statistical, Economic and Social Research and Training Center of the Islamic Countries (SESRTRIC) known as Ankara Center was established in 1977. Since its inception it has organized over 40 seminars and published 50 books, documents, research papers as well as a much sought after and well respected "Journal of Economic Cooperation". The Islamic Center for Development of Trade (ICDT) known as Casablanca Center collects, and publishes the data, and organizes research and training programs on trade issues in the Islamic countries.

Apart from formulating the new strategies for the OIC countries, the Standing Committee for Economic and Commercial Cooperation among Islamic Countries (COMCEC) also looks after the promotion of relationships in trade, agriculture, industry, transport, communications, energy and improvements in the social and technical sectors.

In the field of trade promotion the following actions are being taken:-

a. Steps were undertaken in 1988 for the establishment of Trade Information Network for Islamic Countries (TINIC). The Islamic Center for Development of Trade (ICDT) and the Islamic Development Bank (IDB) are collaborating with the TINIC. By October 1994, 21 contries had appointed their focal points. The OIC General Secretariat makes frequent calls to other member countries to nominate their focal points, to finance the project and to support it.

b. The preparation of all the related documents, agreement on "Export Credit Insurance and Investment Guarantee Scheme" was assigned to the Islamic Development Bank in 1986. After necessary actions were carried out Articles of Agreement of the Scheme was introduced to the member states. By October 1994 it was signed by 28 and ratified by 9 member countries which intend to implement it in the very near future.

c. The document on Multilateral Islamic Clearing Union was initiated by the COMCEC, prepared by the Islamic Development Bank, reviewed by the Governors of the Central Banks and finally submitted to the Eighth session of the COMCEC in 1992. It is still in the finalization process.

d. The Longer Term Trade Financing Scheme (LTTFS), considered as one of the adhievements of COMCEC was established by the Islamic Development Bank in 1987. Its main objective is to promote trade through supplying longer term fi-

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nancing facilities upto sixty months. By June 1994 US$281 million had been provided to 99 projects in nine member countries.

e. A special document "Methodology for the Harmonization of Standards among the OIC Member countries" was prepared on the initiative of COMCEC and the Turkish Standards Institute in 1992. The comments and suggestions are expected from the related establishments in the member countries.

f. COMCEC encourages the participation of the OIC member countries to the Islamic Trade Fairs which can play an important role in promoting commercial links between the countries. So far five trade fairs have been organized. The sixth Fair will be held in Iran in 1995 and the seventh will take place in Lebanon in 1996.

IV. STATEGIS FOR ECONOMIC COOPERATION AMONG ISLAMIC COUNTRIES

The first offical document on the Islamic countries was the 1981 Makkah Declaration, endorsed by the Heads of Islamic States at the Summit Meeting in Taif in 1981. The ten sectors were specified to tackle in the first place were:-

1. Agricultural Development and Food Security
2. Trade
3. Industrial Development
4. Transport
5. Communication and Tourism
6. Energy
7. Science and Technology
8. Labor and Social Security
9. Health and Population
10. Technical cooperation.

The Fourth Islamic Summit Conference held in Casablanca in 1984, reviewed the possibility of implementation of above the target and reduced the priority areas into six sectors which were:-

1. Agricultural Development and Food Security
2. Trade
3. Industry
4. Science and Technology
5. Transport and Communication
6. Energy

Developments in the global economic and political conditions and experiences during the last decade forced the authorities to review and reassess the First

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Plan of Action. It was discussed at the Foreign Ministers Meeting and the Sixth Summit Conference in 1991.

Finally COMCEC assigned OIC Ankara Center to prepare a document on New Strategies for strengthening Economic Cooperation among Islamic Countries. The draft of the document of the CENTER was discussed several times in detail at consultative meetings where all the experts of relevant OIC institutions attended. Later on it was submitted to the COMCEC meeting in October 1994. The document envisaged an integrated OIC community and examined issues related to 10 main sectors which are:

1. Food, Agriculture and Rural Development
2. Industry
3. Energy and Mining
4. Foreign trade
5. Transport and Communication
6. Tourism
7. Money and Finance
8. Technology and Technical Cooperation
9. Human Resources Development
10. Environment

Perhaps the most significant aspect of this document which makes it different than the previous declarations is its approach to the current issues in the Muslim world. The document describes the importance of each topic for the member countries and then sets its objectives, defines, reviews the modalities of action and assigns duties to the related OIC organs and bodies.

The Ankara Center of OIC (under the auspices of COMCEC) has already obtained remarkable achievements to foster economic cooperation among Islamic countries in various fields. Such as:

a. Agriculture and Food Security: Four OIC Ministerial Conferences and 2 International Symposium were held. 1991-1999 period has been declared as the Food Security period for the Islamic Countries.

b. Industry: Four OIC Ministerial Conferences and two International Symposium were held. Joint venture projects were identified.

c. Transport: A special ministerial meeting was organized concurrently with the Third session of COMCEC in Istanbul on 7-10 September 1987. Since then documents were prepared to foster cooperation in road, railway and maritime transportation systems.

d. Communication: A Special ministerial meeting took place concurrently

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with the Fourth session of COMCEC in Turkey in 1988. The Second Ministerial gathering was held in Indonesia in 1991 and the Third was organized in Iran in 1993. The final recommendations were sent all the member countries.

e. Energy: The first ministerial meeting on energy issues was held in istanbul in 1989 concurrently with the Fifth Session of COMCEC. Recommendations to develop the energy resources and power network was communicated to the OIC member countries.

f. Infrastructure and Public Works: The first ministerial meeting on this subject was held in Istanbul in 1991 concurrently with the Seventh Session of COMCEC. The OIC General Secretariat and the COMCEC sent five reports and the recommendations of this meeting to the member countries and urged then to implement the decisions.

g. Labor and Social Security: "Expert Group Meetings" were started in Malaysia in 1984 and later on repeated in Jordan (19S5), Turkey (1989) and Egypt 1993. The expert groups produced agreements on Labor Exchange and social security subjects and submitted for consideration of related institutions.

h. Technical Cooperation: The first ministerial meeting was held concurrently with the Sixth Session of the COMCEC in Turkey in 1990 where urgent collaboration among the focal points was requested. Furthermore, four expert meetings took place during 1990-1994 period, reports were produced importance of training programs emphasized.

Furthermore as a result of the efforts of the OIC General Secretariat, Ankara Center and COMCEC six statutes and agreements were prepared and submitted for the signature and ratification of the member countries. These were:-

1. General Agreement on Economic and Commercial Cooperation adopted by the ICFM, Tripoli. Libya on 2-5-1977, Objectives: To encourage investment and capital transfer, exchange of data and technical information. Signed and ratified by 26 member countries: Bahrain, Bangladesh, Cameroon, Comoro, Egypt, U.A.E., Guinea, Indonesia, Iraq, Jordan, Kuwait, Libya, Malaysia, Mali, Morocco, Mauritania, Niger, Oman, Pakistan, Palestine, Qatar, Saudi Arabia, Senegal, Syria, Tunisia, Turkey.

2. Agreement on Promotion, Protection and Guarantee Investments: Adopted by the ICFM, Baghdad, Iraq on 5-6-1981 - Objective: To promote capital transfer, to protect investment against commercial risks, to guarantee the capital transfer. Signed and Ratified by 14 member countries: Brunei, Egypt, UAE, Indonesia, Kuwait, Mali, Morocco, Uganda, Pakistan, Palestine, Saudi Arabia, Somalia, Tunisia, Turkey.

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3. Framework Agreement on Trade Preferential System among OIC Member Countries: Adopted by the COMCEC Sixth session, Istanbul, Turkey on 10-10-1990. Signed by six member countries - Indonesia, Libya; Senegal; Sudan, Chad, Turkey. Objectives: To promote intra-trade among OIC member states.

4. Articles of Agreement on Export Credit insurance and Investments Guarantee Corporation. Adopted by the COMCEC, Third Session, Istanbul, Turkey 10-9-1987. Signed and ratified by 8 countries - Saudi Arabia, Egypt, Tunisia, Jordan, Indonesia, Chad, Pakistan and Bangladesh. The article is not yet in force.

5. Statute of the Islamic Civil Aviation Council - Adopted by ICFM, Niamey, Niger on 26-9-1982. Signed and ratified by six countries: Bangladesh, U.A.E., Niger, Palestine, Senegal, Tunisia. The article is not yet in force.

6. Statute of the Islamic States Telecommunication Union: Adopted by ICFM, Sana, Yemen on 22-12-1984. Signed and ratified by Bangladesh, Egypt, UAE, Jordan, Libya, Uganda, Palestine, Senegal. The article is not yet in force.

OIC General Secretariat is also concerned with other socio-economic and legal problems of the member countries, carried out necessary studies and prepared resolutions for the approval of related bodies, such as Conference of Foreign Ministers of Islamic countries and the Summit meetings of the Heads of States. The Secretariat lately finalized the preparations of the documents related with environmental problems. Combating against epidemic diseases, controlling the drug trafficking and environmental issues in the Islamic world.

V. COOPERATION IN FINANCE AND BANKING: SOME REFLECTIONS ON THE ACTIVITIES OF THE ISLAMIC DEVELOPMENT BANK

The Islamic Development Bank (IDB), established by the Member States of the Organization of Islamic Conference (OIC) as the principal financial institution of the Islamic world in 1975. Over the last two decades membership has increased to 47 states and its total financial operations reached to nearly US$15 billion by August 1993.

As stated in its statute the main aim and objective of the IDB is to foster economic development and social progress of member countries and the Muslim communities in non- member countries according to principles of the Islamic religion. Consequently the IDB aims:

- to participate in equity capital of productive projects
- to provide loans to private and public sector companies
- to invest in infrastructure projects
- to support foreign trade operations

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- to extend training facilities and to undertake research
- to cooperate with the relevant organizations.

The necessary conditions for membership of the IDB is that the country should be a member of the OIC and accept the above described objectives. Due to changes in the world economic environment and needs of the member countries the authorized capital of the Bank increased from ID 2 billion to 1D 6 billion in 1992.

Operations of IDB can be classified into three main categories:-

1. Project Financing
2. Trade Financing
3. Special Assistance Operations.

In deciding type and amount of operations the Bank authorities put a special emphasis on economic feasibilities of the project and its link with the development plan of the concerned country as well as priority areas of the Bank. For example every year a certain percentage of the resources have to be allocated to targeted sectors (i.e. agriculture) and specified operations must be performed in the Least Member Countries. On top of the these activities the IDB always tries to promote projects with higher employment opportunities, pays attention to economic cooperation and joint venture principles. Experiences show that the Bank is mainly interested in reasonably sized projects and participation to consortiums rather than providing resources to giant investments plans. With this spirit IDB financed number of projects with the World Bank, Asian and African Development Banks, the Arab Development Finance institutions and the AOPEC Fund.

As far as modes of financing are concerned unlike other international financial institutions IDB does not deal with interest, can only charge a service fee for its lending amounts to cover major administrative expenses. A large proportion of its loan financing is directed to infrastructure investments in agriculture, transport, health and education where Least Developed Member Countries had been receiving special treatment in terms of periods of grace and repayment. Since the first application of loan transactions upto June 1994. US$ 1.2 billion worth of loan was provided for 202 projects in 44 countries.

Despite high risk involvement due to its constitutional commitment the IDB has put emphasis on equity participant in its early years. However, due to non-existence of stock exchange in many countries facing difficulties in selling shares forced the IDB to support - small and medium sized enterprises through National Development Financial Institutions. Available documents indicate that the IDB allocated US$250 million to direct equity and US$66 million for line of equity participations in the member countries.

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The IDB has also developed special modes of Islamic financing on leasing, instalment and profit sharing arrangements. For this purpose nearly US$ 2 billion was allocated, of which US$ 721 million was directed purely for leasing, US$ 752 million was devoted to instalment sale, US$ 38 million was channeled to Profit sharing projects. The rest was utilized in line of leasing, line of instalment sale, line of equity etc.

As part of IDB's mission to foster economic cooperation among member countries the Bank agrees to finance the purchase of a commodities and to resell them to the beneficiary against a guarantee. Apart from exceptional cases (non-availability, quality, quantity, price restrictions) the imports have to be made from member countries. By June 1994 the Bank has channeled US$ 8.4 billion to finance the short term trade financing activities. In order to finance 18 to 60 months intra trade facilities the Bank and 18 member countries established a scheme (LTTFs) in 1987. So far 99 projects worth US$280 million was financed through this mode.

The Islamic Development Bank has provided financial and technical help for the progress of Islamic Banks around the world in particular in its member countries, contributed US$ 47 million to the capital of 15 institutions. The Bank has extended its cooperation with the Islamic Banks in other fields and jointly established the Islamic Banks portfolio in 1987 and Islamic Trading Company in 1990.

It has already been stated that 20 out of 47 member countries of IDB are classified as LDC which needs special care. In this connection US$50 million was provided to drought affected West African US$ 14 million was given to locust damaged North African countries. Statistics show that the IDB has been doing its best for the least developed member countries. Since the inception of the Bank upto 1994 almost one billion dollar (one third of the total project financing (3.2 billion) and two third of the special assistance operations US$ 304 out of 430 million dollar was channelled to help the most needy Muslim states. Furthermore in 1993 a special fund with US$ 100 million dollar was established to provide 25-30 years loan including 10 years grace period. The Bank will charge only 0.75 per cent per annum service fee to recover part of its administrative costs.

The Islamic Development Bank is also concerned with socioeconomic cultural and religious problems of the Muslim communities in non-member countries, supported 167 projects in different part of the world from India, Vietnam, Russia, United States and South Africa provided over US$127 million to fulfil the objectives. It must be pointed out that since 1990 assistance to muslim Republic and communities in the former Soviet Union and Eastern Europe has received a special atten-

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tion. Consequently the islamic Development Bank has provided a financial support of US$ 6 million to help the implementation of various educational, social investment of which half of this amount was spent to build schools, hospitals and relief organizations. The Bank authorities has granted US$ 3 million for feasibility studies of 10 different project in Central Asia and approved US$ 21 million assistance program for Bosnia Herzegovina of which US$ 6 million is designated for relief organizations and US$ 15 million for reconstruction purposes. According to the rolling plans of the Bank during 1995-1997 period U.S$ 40 million will be devoted specially for the projects Central Asian Republics and another US$ 5 million will be provided to support the technical assistance activities.

As part of IDB's devotion to help economic development and to foster the relationship in the Islamic world Islamic Research and Training Institute (IRTI) was established in 1981. By October 1994 published papers were approaching to 90 and total number of Training programs were 110 of which almost half of it was specially dealing with Islamic economics, banking, finance and cooperation. During the last decade more than 3000 officials from the member countries have participated to IRTI programs. To accelerate the economic cooperation IRTI experts are working on OIC Information System Network OICIS-NET) and collection information to serve the purpose.

Apart from keeping very close relationship with the relevant institutions in member countries the islamic Development Bank has established a close relationship with other national, regional and international Islamic, non-Islamic establishment, United Nations organizations, Inter-Governmental (IGO's) and non-Governmental (NGOs) organizations. Among them UNESCO, UNCTAD, UNIDO, FAO, IFAD, EU, OECD, ASEAN brougt fruitful results for the collaborating especially with the IMF, World Bank, Asian and African Development Banks for member countries. The Bank has also been maintaining very contacts with the OIC General Secretariat, Ankara Research and Training Center (SESRTRIC), Casablanca Trade Development Center (ICDT), Jeddah Science Technology Foundation (IFSTAD), Jeddah Fiqh Academy, as well as Development Funds of number of Gulf countries and Economic Cooperation Organization (ECO).

In brief statistics confirms that the Islamic Development Bank has made a remarkable progress in promoting financial and economic cooperation among the Islamic countries. Consequently, it has increased its membership from 22 to 47 and total operations exceeded 14 billion dollars within less than two decades. In order to be ready for the conditions of the 21 century the Bank has prepared a long term plan and started to implement it to bring more efficiency and effectiveness in bringing its service to the member countries.

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VI. CONCLUSION

One of the basic principles of Islam is to apply the rules of cooperation for achieving fulfillment in every aspect of life, including economic and social activities. Regarding this beside Ayats in the holy Qur'an, and the Hadises of the Prophet (pbuh) pointed out the importance of cooperative actions in successfully meeting the goals of individuals, institutions and the governments.

Due to economic, political, financial developments after the Second World War Islamic countries have set up a large number of organizations, establishments and institutions. The process was speeded up during 1970-1980, high petrol income period with the number of related organizations was totalling 115 by October 1994. Their effectiveness and efficiency however have not attained desired level. Only the islamic Development Bank and some organs of the Organizations of the Islamic Conference have shown an impressive performance. A possible solution to this challenge might involve the integration of some institutions, a reduction in their number and emphasis on quality work. A frequent assessment of the activities of each organization and a cost / benefit analysis of them can serve as a yardstick for future strategies. Most of the establishments are suffering from lack of financial resources and qualified, devoted manpower.

In order to promote an effective economic cooperation scheme of economic cooperation in coming decade beside official channels of government organizations substantial incentives should be offered to the universities as well as the representatives of the private sector. In this connection specialized research institutes in the universities chambers of commerce, industry and agriculture as well as well represented businessmen, Industrialists' associations can play a very significant role.

In applying new strategies designed for the conditions of the 21st century the concerned Islamic organizations should pay particular attention to the problems of the newly independent states in Central Asia and Europe and given hand in solving the difficulties of the Muslim communities. Furthermore the governments must be mindful of the opinion of their people at the grass root level and cooperate with each other not only to realize political goals but also to create a wealthy and prosperous Islamic world.

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APPENDIX

SELECTED STATISTICS ON SOCIO-ECONOMIC CONDITIONS OF THE ISLAMIC COUNTRIES

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LIST OF OIC MEMBER COUNTRIES

1 AFGHANISTAN	ISLAMIC STATE OF AFGHANISTAN
2 ALBANIA	REPUBLIC OF ALBANIA
3 ALGERIA	PEOPLE'S DEMOCRATIC REPUBLIC OF ALGERIA
4 AZERBAIJAN	REPUBLIC OF AZERBAIJAN
5 BAHRAIN	STATE OF BAHRAIN
6 BANGLADESH	PEPOLE'S REPUBLIC OF BANGLADESH
7 BENIN	REPUBLIC OF BENIN
8 BRUNEI	BRUNEI DARUSSALEM
9 BURKINA FASO	BURKINA FASO
10 CAMEROON	REPUBLIC OF CAMEROON
11 CHAD	REPUBLIC OF CHAD
12 COMOROS	FEDERAL ISLAMIC REPUBLIC COMOROS ISLANDS
13 DJIBOUTI	REPUBLIC OF DJIBOUTI
14 EGYPT	ARAB REPUBLIC OF EGYPT
15 EMIRATES	THE STATE OF UNITED ARAB EMIRATES
16 GABON	REPUBLIC OF GABON
17 GAMBIA	REPUBLIC OF GAMBIA
18 GUINEA	REPUBLIC OF GUINEA
19 GUINEA-BISSAU	REPUBLIC OF GUINEA-BISSAU
20 INDONESIA	REPUBLIC OF INDONESIA
21 IRAN	ISLAMIC REPUBLIC OF IRAN
22 IRAQ	REPUBLIC OF IRAQ
23 JORDAN	HASHEMITE KINGDOM OF JORDAN
24 KUWAIT	STATE OF KUWAIT
25 KYRGYZTAN	REPUBLIC OF KYRGYZTAN
26 LEBANON	REPUBLIC OF LEBANON
27 LIBYA	SOCIALIST PEOPLE'S LIBYAN ARAB JAMAHIRIYA
28 MALAYSIA	MALAYSIA
29 MALDIVES	REPUBLIC OF MALDIVES
30 MALI	REPUBLIC OF MALI
31 MAURITANIA	ISLAMIC REPUBLIC OF MAURITANIA
32 MOROCCO	KINGDOM OF MOROCCO
33 NIGER	REPUBLIC OF NIGER
34 NIGERIA	FEDERAL REPUBLIC OF NIGERIA
35 OMAN	SULTANATE OF OMAN
3 PAKISTAN	ISLAMIC REPUBLIC OF PAKISTAN
37 PALESTINE	STATE OF PALESTINE
38 QATAR	STATE OF QATAR
39 SAUDI ARABIA	KINGDOM OF SAUDI ARABIA
40 SENEGAL	REPUBLIC OF SENEGAL
41 SIERRA LEONE	REPUBLIC OF SIERRA LEONE
42 SOMALIA	REPUBLIC OF SOMALIA
43 SUDAN	REPUBLIC OF SUDAN
44 SYRIA	SYRIAN ARAB REPUBLIC
45 TAJIKISTAN	REPUBLIC OF TAJIKISTAN
46 TUNISIA	REPUBLIC OF TUNISIA
47 TURKEY	REPUBLIC OF TURKEY
48 TURKRKMENISTAN	REPUBLIC OF TURKMENISTAN
49 UGANDA	REPUBLIC OF UGANDA
50 YEMEN	REPUBLIC OF YEMEN
51 ZANZİBAR	ZANZIBAR

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LIST OF IDB MEMBER COUNTRIES

1 AFGANİSTAN	AFGANİSTAN İSLAM DEVLETİ
2 ARNAVUTLUK	ARNVUTLUK CUMHURİYETİ
3 CEZAYİR	CEZAYİR DEMOKRATİK HALK CUMHURİYETİ
4 AZERBAYCAN	AZERBAYCAN CUMHURİYETİ
5 BAHREYN	BAHREYN DEVLETİ
6 BANGLADEŞ	BANGLADEŞ HALK CUMHURİYETİ
7 BENİN	BENİN CUMHURİYETİ
8 BRUNEI	BRUNEI DARUSSALEM
9 BURKİNA FASO	BURKİNA FASO
10 KAMERUN	KAMERUN CUMHURİYETİ
11 ÇAD	ÇAD CUMHURİYETİ
12 KOMOROS	KOMOROS ADALARI FEDERAL İSLAM CUMHURİYETİ
13 CİBUTİ	CİBUTİ CUMHURİYETİ
14 MISIR	MISIR ARAP CUMHURİYETİ
15 EMIRATES	THE STATE OF UNITED ARAB EMIRATES
16 GABON	GABON CUMHURİYETİ
17 GAMBİYA	GAMBİYA CUMHURİYETİ
18 GİNE	GİNE CUMHURYETİ
19 GUINEA - BISSAU	GUINEA- BISSAU CUMHURİYETİ
20 ENDONEZYA	ENDONEZYA CUMHURİYETİ
21 İRAN	İRAN İSLAM CUMHURİYETİ
22 IRAK	IRAK CUMHURİYETİ
23 ÜRDÜN	HASHEMITE KINGDOM OF JORDAN
24 KUVEYT	KUVEYT DEVLETİ
25 KIRGIZİSTAN	KIRGIZİSTAN CUMHURİYETİ
26 LÜBNAN	LÜBNAN CUMHURİYETİ
27 LİBYA	LİBYA SOSYALSİT ARAP CEMAHİRİYESİ
28 MALEZYA	MALEZYA
29 MALDIV	MALDİV CUMHURİYETİ
30 MALİ	MALİ CUMHURİYETİ
31 MORİTANYA	MORİTANYA İSLAM CUMHURİYETİ
32 MOROKO	MOROKO KRALLIĞI
33 NİJER	NİJER CUMHURİYETİ
34 UMMAN	UMMAN SULTANLIĞI
35 PAKİSTAN	PAKİSTAN İSLAM CUMHURİYETİ
36 FİLİSTİN	FİLİSİN DEVLETİ
37 KATAR	KATAR DEVLETİ
38 SUUDI ARABİSTAN	SUUD ARABİSTAN KRALLIĞI
39 SENEGAL	SENEGAL CUMHURİYETİ
40 SIERRA LEONE	SIERRA LEONE CUMHURİYETİ
41 SOMALİ	SOMALİ CUMHURİYETİ
42 SUDAN	SUDAN CUMHURİYETİ
43 SURİYE	SURİYE ARAP CUMHURİYETİ
44 TUNUS	TUNUS CUMHURİYETİ
45 TÜRKİYE	TÜRKİYE CUMHURİYETİ
46 UGANDA	UGANDA CUMHURİYETİ
47 YEMEN	YEMEN CUMHURİYETİ

source: IRTIC

TOTAL POPULATION, (In millions)

	1989	1990	1991	1992
Afghanistan	15.8	16.1	16.4	17.5
Albania	3.2	3.3	3.3	3.4
Algeria	34.3	25.0	25.7	26.4
Azerbaijan	7.1	7.2	7.2	7.3
Bahrain	0.5	0.5	0.5	0.5
Bangladesh	106.5	115.6	118.7	122.3
Benin	4.6	4.7	4.9	5.0
Brunei	0.2	0.3	0.3	0.3
Burkina Faso	8.8	9.0	9.2	9.5
Cameroon	11.5	11.5	11.9	12.2
Chad	5.5	5.7	5.8	6.0
Comoros	0.5	0.5	0.6	0.6
Djibouti	0.4	0.4	0.5	0.5
Egypt	51.8	53.2	54.7	55.2
Gabon	1.1	1.2	1.2	1.2
Gambia	0.8	0.9	0.9	0.9
Guinea	6.7	6.9	7.1	7.2
Guine-Bissau	0.9	1.0	1.0	1.1
Indonesia	179.1	179.3	187.8	189.5
Iran	54.2	54.6	57.7	60.7
Iraq	17.5	18.1	18.7	19.3
Jordan	3.9	4.0	4.1	4.3
Kuwait	2.1	2.1	2.1	1.5
Kyrgzstan	4.3	4.4	4.5	4.5
Lebanon	2.7	2.7	2.7	2.7
Libya	4.4	4.5	4.7	4.9
Maiysia	17.4	17.8	18.3	18.6
Maldives	0.2	0.2	0.2	0.2
Mali	8.0	8.2	9.5	9.8
Mauritania	2.0	2.0	2.0	2.1
Morocco	24.4	25.1	25.7	26.4
Niger	7.5	7.7	8.0	8.1
Nigeria	105.0	108.5	112.1	115.7
Oman	1.5	1.5	1.5	1.5
Pakistan	108.7	112.0	115.5	115.5
Qatar	0.5	0.5	0.5	0.6
Saudi Arabia	14.4	14.9	15.4	15.9
Senegal	7.1	7.3	7.5	7.8
Sierra Leone	4.1	4.2	4.3	4.4
Somalia	8.5	8.7	8.9	9.2
Sudan	24.5	25.2	25.9	26.7
Syria	11.7	12.1	12.5	12.9
Tunisia	7.9	8.1	8.4	8.5
Turkey	54.9	56.1	57.4	58.8
Turkmenistan	3.6	3.7	3.8	3.9
Uganda	18.1	18.8	19.5	20.0
U.A.E.	1.6	1.6	1.6	1.7
Uzbekistan	20.1	20.5	21.3	21.5
Yemen	11.3	11.3	12.1	12.5
OIC total	981.4	1008.6	1044.1	1066.0
WORLD total	5206.0	5262.0	5351.0	5430.0
OIC share in world total (%)	18.9	19.2	19.5	19.6

Source: IMF. International Financial Statistics, March 1993;UN Monthly Bulletin of Statistics, August 1993 The Economist Intelligence Unit. World Development Report, 1991, 1993.
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COMPOSITION OF GDP OIC COUNTRIES AS AVARAGE OF 1988-91

(In percent)

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	Agriculture	Industry	Manufacture	Services
Albania	34.8	42.8		22.4
Algeria	14.3	45.2	11.4	40.8
Bangaldesh	37.5	15.4	8.6	47.0
Benin	40.6	13.3	6.4	13.0
Burkina Faso	36.3	23.8	13.7	40.1
Cameroon	36.6	26.4	13.0	47.1
Chad	39.4	18.1	15.8	42.6
Comoros	39.8	10.2	3.8	49.2
Djibooti	2.8	18.1	5.0	79.0
Egypt	18.3	29.7	15.3	51.9
Gabon	9.8	45.0	8.3	45.2
Gambia	34.2	11.1	6.4	54.7
Guinea	28.8	33.5	3.9	37.5
Guinea-Bissau	46.3	14.9	9.9	38.9
Indonesia	22.2	38.7	19.5	39.0
Iran	21.1	22.5	9.2	56.4
Iraq	6.7			
Jordan	6.9	26.8	12.8	66.2
Kuwait	1.0	54.3	9.3	44.7
Malaysia	22.2	43.0	28.1	34.8
Maldives	28.5	13.4	5.4	58.0
Mali	47.4	12.1	7.5	40.3
Mauritania	30.8	26.5		42.5
Morocco	17.0	33.0	17.8	50.0
Niger	37.4	14.8	6.6	47.7
Nigeria	34.4	39.0	10.8	26.3
Oman	3.3	63.8	4.6	33.5
Pakistan	26.3	24.9	16.9	49.0
Saudi Arabia	7.8	46.3	8.0	46.8
Senegal	20.7	18.1	12.7	61.3
Sierra Leone	39.2	14.4	5.1	46.2
Somalia	65.0	9.3	5.0	25.7
Sudan	32.7	15.5	8.7	51.8
Syria	29.5	21.0	9.0	49.5
Tunisia	15.5	32.3	16.6	52.3
Turkey	17.5	34.7	24.9	48.1
Uganda	63.0	8.4	4.3	28.5
U.A.E.	2.0	55.0	8.7	43.3
Yemen	23.3	25.6	13.3	50.9

Source: World Development Reports. 1990, 1991, 1992, 1993. OIC Economic Report 1993.

TOTAL MERCHANDISE IMPORTS OF OIC COUNTRIES (CIF, million US $)

	1989	1990	1991	1992
Afghanistan	1355	1551	1623	1692
Albania	224	233	281	120
Algeria	8909	10372	9045	8375
Azerbaijan	2184	2400	3747	-
Bahrain	2944	3839	3964	4311
Bangladesh	3615	3654	3421	3732
Benin	420	545	632	736
Brunei	1499	1723	1779	2281
Burkina Faso	431	523	520	515
Cameroon	1343	1555	1345	1312
Chad	167	142	161	155
Comoros	76	91	124	110
Djibouti	197	215	426	491
Egypt	7477	9175	7862	13373
Gabon	836	860	1076	1074
Gambia	191	227	304	385
Guinea	490	594	695	775
Guinea-Bissau	129	129	146	126
Indonesia	16467	22005	25863	27606
Iran	12746	15789	21339	23196
Iraq	9841	6506	426	647
Jordan	2136	2600	2643	3257
Kuwait	6394	4042	5093	5843
Kyrgyzstan	1459	1738	578	
Lebanon	2236	2526	3743	4203
Libya	4393	5561	5898	5293
Malaysia	22589	29170	36749	39927
Maldives	143	138	161	178
Mali	486	607	588	666
Mauritania	351	388	482	581
Morocco	5470	6506	7684	8432
Niger	390	414	401	473
Nigeria	4405	6521	7845	9180
Oman	2257	2725	3194	3769
Pakistan	7107	7383	8432	9375
Qatar	1326	1695	1720	1880
Saudi Arabia	21144	24069	29074	37933
Senegal	1223	1429	1343	1384
Sierra Lione	183	224	270	280
Somalia	415	398	175	211
Sudan	1352	1185	1281	1081
Syria	2084	2401	2768	3545
Tunisia	4434	5944	5447	6516
Turkey	17051	24486	21045	24095
Turkmenistan	431	397	846	-
Uganda	457	466	458	415
U.A.E.	9546	11472	171154	20214
Yemen	1944	1606	2026	-
OIC Total	192945	228219	251876	279742
WORLD total	3001300	3436400	3570800	3846100
OIC share in world total (%)	6.4	6.6	7.1	7.3

Source: Direction of Trade Statistics, 1993, International Financial Statistics, March 1993.
OIC Economic Report 1993.

TOTAL MERCHANDISE EXPORTS OF OIC COUNTRIES (FOB, million US $)

	1989	1990	1991	1992
Afghanistan	722	803	929	999
Albania	133	123	72	65
Algeria	9281	12650	12211	10909
Azerbaijan	701	519	1283	-
Bahrain	2716	2844	3008	3008
Bangladesh	1305	1672	1688	2040
Benin	114	115	125	125
Brunei	1921	2270	2538	2365
Burkina Faso	133	166	175	152
Cameroon	1765	2026	1910	1770
Chad	72	94	93	73
Comoros	26	23	28	28
Djibouti	41	48	55	58
Egypt	2594	2572	3659	5172
Gabon	1521	2461	2558	2316
Gambia	138	171	166	590
Guinea	587	627	666	590
Guinea-Bissau	7	21	31	31
Indonesia	21936	25675	29135	33840
Iran	11282	15476	16428	15807
Iraq	12257	10421	302	557
Jordan	1098	923	1161	1220
Kuwait	11044	8145	685	2990
Kyrgyzstan	81	88	23	
Lebanon	485	494	539	560
Libya	8617	10773	10661	9740
Malaysia	25049	29420	34405	40709
Maldives	45	52	54	77
Mali	197	289	303	301
Mauritania	451	468	518	507
Morocco	3290	4161	5399	5749
Niger	304	275	247	202
Ngeria	10459	13055	13081	12233
Oman	4363	4584	5399	5749
Pakistan	4660	5587	6494	7267
Qatar	2491	3291	3176	3488
Saudi Arabia	28384	44416	44062	51771
Senegal	665	718	747	661
Sierra Leone	138	150	180	150
Somalia	120	150	104	109
Sudan	603	518	368	323
Syria	3006	4218	3432	3080
Tunisia	3035	3954	3886	4183
Turkey	11823	13724	13645	14792
Turkmenistan	197	148	1187	
Uganda	262	190	175	173
U.A.E.	17596	23505	24392	24742
Yemen	727	696	506	390
OIC Total	208444	254765	253859	273348
WORLD total	2909300	3329800	3448700	3687000
OIC: share in world total (%)	7.2	7.7	7.4	7.4

Source: Direction of Trade Statistics. 1993: International Financial Statistics, March 1993.
OIC Economic Report 1993

TOTAL EXTERNAL DEBT (1) OF THE OIC COUTRIES (In millions of US dollars)

	1989	1990	1991
Algeria	28574.0	29794.0	28636.0
Bangladesh	10702.0	12222.0	13051.0
Benin	1185.0	1225.0	1300.0
Burkina Faso	717.0	834.0	956.0
Cameroon	4790.0	5990.0	6278.0
Chad	376.4	504.7	606.3
Comoros	174.1	184.7	175.2
Djibouti	180.1	210.4	196.7
Egypt	51498.0	40104.0	40571.0
Gabon	3181.0	361.0	382.0
Gambia	340.5	352.2	350.7
Guinea	2167.0	2478.0	2626.0
Guinea-Bissau	499.7	595.8	653.3
Indonesia	53672.0	67232.0	73629.0
Iran	6518.0	9021.0	11511.0
Jordan	7395.0	8328.0	8641.0
Lebanon	1186.7	1965.1	1858.3
Malaysia	17829.0	18173.0	21445.0
Maldives	66.8	78.3	80.4
Mali	2145.0	2432.0	2531.0
Mauritania	2044.0	2207.0	2298.0
Morocco	21710.0	23620.0	21219.0
Niger	1587.0	1827.0	1653.0
Nigeria	31977.0	34557.0	34497.0
Oman	2967.0	2541.0	2697.0
Pakistan	18299.0	20645.0	22969.0
Senegal	3286.0	3737.0	3522.0
Sierra Leone	1093.0	1177.0	1291.0
Somalia	2159.0	2366.0	235.0
Sudan	13844.0	15340.0	15907.0
Syria	16881.0	16446.0	16815.0
Tunisia	6940.0	7713.0	8296.0
Turkey	41387.0	49170.0	50252.0
Uganda	2231.0	2637.0	2830.0
Yemen	5590.0	6322.0	6471.0
OIC total	365192.3	395670.2	412089.9
All developing countries	1098799.0	1177987.0	1236682.0
WORLD total	1253852.0	1345731.0	1417459.0
OIC share in total debts (%)	29.1	29.4	29.1

Source: The World Bank. World Debt Tables. 1992-33. OIC Economic Report 1993.

Note (1): Total debt stocks consist of public and publicly guaranteed long term debt, private non-guaranteed long term debt the use of IMF credit, and estimated short term debt.

RATIO OF TOTAL EXTERNAL DEBT TO GNP (In percent)

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	1989	1990	1991
Algeria	53.3	51.6	70.4
Bangladesh	52.4	54.9	56.0
Benin	79.2	65.6	69.4
Burkina Faso	33.2	32.4	34.9
Cameroon	47.7	56.3	57.5
Chad	39.1	43.2	47.0
Comoros	83.3	74.4	72.0
Djibouti	42.4	47.2	42.1
Egypt	165.4	126.7	130.2
Gabon	89.7	80.3	88.1
Gambia	128.9	110.5	110.9
Guinea	99.0	96.9	94.8
Guinea-Bissau	299.2	322.9	323.8
Indonesia	59.7	66.1	66.4
Iran	5.2	7.6	10.8
Jordan	181.5	237.6	225.3
Malaysia	50.5	44.6	47.6
Maldives	82.4	86.9	81.7
Mali	104.9	98.7	104.9
Mauritania	216.8	224.6	214.7
Morocco	100.1	94.6	80.0
Niger	79.9	73.9	72.9
Nigeria	11.9	107.4	108.8
Oman	40.4	26.6	28.6
Pakistan	44.4	50.3	50.1
Senegal	73.8	66.4	63.1
Sierra Leone	115.4	136.3	167.5
Somalia	212.8	283.4	
Sudan	133.4	175.7	221.7
Syria	169.2	118.1	
Tunisia	71.6	64.0	66.2
Turkey	53.5	46.2	48.1
Uganda	76.7	96.4	109.2
Yemen	89.8	101.0	88.1
OIC Countries	60.1	58.9	63.7
Developing countries	41.3	40.6	41.8

Source: The World Bank.World Debt Tables. 1992-93. OIC Economic Report 1993

OIC COUNTRY RISK RANKING AND RATINGS

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INTERNATIONAL RANK				RATING		
1992	1991	1990	Country	1992	1991	1990
26	37	44	Saudi Arabia	78.59	53.9	60.0
27	42	50	U.A.E.	76.46	52.7	56.0
30	41	44	Bahrain	74.99	52.9	60.0
31	26	24	Malaysia	73.61	76.0	75.8
33	72	106	Kuwait	72.46	36.9	27.9
34	33	29	Brunei	71.90	56.5	72.1
37	40	54	Turkey	66.20	53.1	54.0
38	50	71	Qatar	64.40	47.5	44.8
40	32	35	Indonesia	63.53	57.3	65.7
42	48	46	Oman	60.88	49.8	59.0
50	64	60	Tunisia	52.52	39.1	50.0
56	60	75	Morocco	44.29	40.0	42.5
65	56	57	Pakistan	39.61	41.3	53.0
66	83	64	Algeria	37.78	36.9	35.8
67	73	89	Gabon	37.71	36.9	35.8
75	103	122	Syria	34.14	25.2	22.3
81	86	85	Cameroon	32.13	31.6	37.0
84	82	84	Senegal	31.93	33.1	37.8
86	80	80	Egypt	31.09	34.5	39.6
88	92	99	Gambia	30.45	29.5	28.9
89	96	81	Bangladesh	30.39	28.7	39.3
90	102	97	Jordan	29.94	25.7	31.0
92	95	103	Niger	29.32	28.7	28.6
96	88	96	Nigeria	28.06	31.0	33.0
97	112	102	Libya	27.97	22.8	28.7
99	58	93	Iran	27.38	40.5	33.8
103	98	116	Djibouti	25.54	28.6	25.2
111	94	87	Mali	24.71	29.0	36.8
127	110	125	Uganda	22.3	23.1	19.4
133	113	108	Chad	21.02	22.7	27.2
140	105	121	Mauritania	19.00	24.4	22.8
141	126	124	Lebanon	18.74	15.4	19.6
159	100	99	Sierra Leone	13.17	27.2	28.9
163	124	131	Sudan	11.66	16.8	14.5
168	130	129	Iraq	6.07	1.9	18.4

Source: Euromoney, September 1991 and 1992. OIC Economic Report 1993.

ISLAMIC DEVELOPMENT BANK

Summary of IDB Financing (June 1994)

No. of Operations	No. of Countries	Type of Financing	Approved ID/mill.	Approved US$/mill.
		PROJECTS FINANCING + T.A.		
192	36	LOAN	913.541	1097.824
10	8	LOAN (LDMC PROGRAM)	11.806	15.602
62	24	EQUITY (*)	200.807	249.036
62	18	LEASING	586.714	720.746
5	4	PROFIT SHARING	29.680	38.556
73	23	INSTALMENT SALE	589.885	751.602
188	38	TECNICAL ASISTANCE (MEMBER COUNTRIES)	67.513	81.798
5	3	TECNICAL ASSISTANCE (NON MEMBER)**	0.818	1.138
5	3	LINE OF EQUITY	27.541	33.569
3	3	LINE OF LEASING	27.200	30.200
4	4	LINE OF INSTALMENT SALE	32.250	43.614
20	17	LINE OF EQ/LSG/SALE	118.605	138.645
629		SUB TOTAL(1)	2606.360	3202.150
		SUB-PROJECTS		
54	7	LINE OF EQUITY (UTILIZED)	27.840	33.106
12	5	LINE OF LEASING (UTILIZED)	11.683	15.387
23	10	LINE OF INST.SALE (UTILIZED)	22.376	29.715
89		SUB TOTAL	61.899	78.208
		FOREIGN TRADE FINANCING		
730	29	IMPORT TRADE FINANCING	6869.932	8379.072
99	9	LONGER TERM TRADE FINANCING	205.579	281.223
829		SUB TOTAL (2)	7075.511	8660.295
1458		TOTAL (1)+(2)	9681.871	11862.445
SPECIAL ASISTANCE OPERATIONS* **			**MEMBER COUNTRIES**	
82	20	ISLAMIC CAUSES	88.594	111.984
4	3	MUSLIM MINORITIES	4.195	5.311
53	23	NATURAL DISASTERS	132.470	151.767
8	6	SPASST. LOAN	27.867	34.428
147		SUB TOTAL (3)	253.126	303.490
			NON MEMBER COUNTRIES	
158	49	MUSLIM MINORITIES	107.995	125.618
1	1	NATURAL DISASTER	0.150	0.170
8	2	SPECIAL ASST. LOAN	1.803	1.867
167		SUB TOTAL (4)	109.948	127.655
314		TOTAL (3)+(4)	363.074	431.145
		CANCELLATIONS		
104	22	PROJECT FINANCE+T.A.	547.486	656.182
167	30	FOREIGN TRADE FINANCING	806.143	1057.909
271		SUB TOTAL (5)	1353.629	1714.091
2043		GRAND TOTAL (1)-(2)+(3)+(4)+(5)	11398.574	14007.681

* Including additional Equity projects.

** T.A. for Non Member Muslim Central Asian Republics

*** Number of operations do not include utilization for sub-projects.

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HUMAN RESOURCES DEVELOPMENT IN ISLAMIC COUNTRIES

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Introduction
- The definition and concept of Human Resources Development.
- Challenges facing the Islamic World.
- Current Situation of Human Resources in the Islamic World.
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- Human Resources Development in The Islamic World.
- Conclusion and Recommendations.
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Introduction:

The human resources aspect is the most important element in the nation development process and the axis for economic development in human societies in both the industrialized and the developing countries.

Human resources constitute the basis for development in both its realization or the economic returns that accrue to it.

Development of the human resourses is one of the most important issue which face the Islamic World in the light of the challenges which face it particularly after the emergence of the World's power Blocs and the international agreements governing world trade liberalization.

This study deals, with the concept of human resourses development in the Islamic World and the significance of such development especially in this critical stage the Islamic nation is facing.

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The government in the Islamic countries must direct part of its resources to develop their human respources especialy in the area of education, training, health care and social development in order to face the great challenges in the area of competition in goods and services that will flow to the Moslem countries markets in the coming decades. This study will discuss these issues.

1- The Human Resources Develoament Concept:

The human element is considered the basis for economic activity as it constitutes one of the central Pillar for the production process which is made up of the following elements:

Land: represents the natural resources.

Labor: respresented in human resouces i.e. manpower.

Capital: represented in the productive capacity, capital and equipments .

Organization: represented in the administrative and organizational capacities.

The fact that the optimum utilization of some or all of these economic resources which is limited in quality or quantity or both is regarded as one of the main reasons which have contributed to the relative reduction in the economic activity (1).

The human element is regarded as the central pillar for all the production processes other constituent elements. It is they who manage and operate factories, hospitals and other institutions, do the managing, improve the ways of working and the performance.

The experiences of both the developing and the industrialized countries proved that development needs are not restricted to the projects' material needs but rather extends to the qualified manpower needed for executing such development projects. Hence developing the human resources constitute the main entry to social growth and development since development projects are to a large extent dependant upon the availability of the human resources (2) .

Viewpoints on the concepts of human development varied as some regard human development as those individual efforts to realize and fulfil all human needs in society rather than their restriction to the basic needs (3) .

Others see human development as restricted to the social sectors like health care and education whose growth and development result in benefits for individuals hence the increase in their productivity and their contribution to economic development.

Others also point out that human development constitute the process of fulfilling the basic needs of the developing nations while excluding the industrialized countries from this definition.

Another viewpoint human development is concerned with all activities beginning with production processes to the change in establishments to the organized

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political dialogs since such development is focused on the people and their welfare as well as its concern for generating economic growth and its distribution. It is also concerned with the basic needs as well as human expectations in their entirety. It is also considerate of the people's concerns in the North and the deprivation experienced by the people in the South.

The United Nations Report on human development in 1990 stated that human development is a process of expanding the available options before the people, the most important of which is the realization of a long life free from disease, characterized by acquisition of knowledge and a decent living standard.

From the foregoing we see that the majority of definitions stress on the human development as the human person is considered the axis for development in society and the fact that development projects depend upon the efficiency and competence of the human person and his/her skills in doing the work.

2. The Challenges which face the Islamic World:

The Moslem world constitutes about a quarter of the world population (i.e. 932.9 millions) and this man-power is confronted by countless challenges in the current and the coming decades. The most glaring of those challenges are:

1- As a result of the end of the cold war esp. after the collapse of what was known as the Soviet Union, military spending has been reduced considerably which means shifting that item of national expenditure and energy toward development. This in turn makes it a must for the Moslim World to utilize and develope its human resources to catch up with the march of the world's economic development.

2- After the signing oft he GATT and the most significant impact of that is the opening up of the world markets on each others which dictates that the developing Moslem countries should meet such developments by working toward developing their human resources to achieve more productivity which in turn will change Moslim countries into exporters rather than importers only.

3- Despite signing the GATT yet there is a negative aspect, which is, as a result of the absence of equal opportunities in World markets, the developing world, the majority of which are moslem countries, are still suffering much from economic and social hardships and challenges represented in the reduction of the human development indicators. Hence an increase in poverty in many countries which results in the rich getting richer with the ensuing rise in their growth rates and the poor getting poorer resulting in the fall of their growth rates.

4- The 1992 U.N. Report chapter 5 has pointed out that there are some negative aspects represented in wrong practices by the international organizations which affect the world nations growth & development e.g. the International Mo-

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netary Fund, the World Bank and the General Agreement on Tariffs & Trade "GATT" (4) whose policies most often serve the interests of the industrialized countries.

5- Of the challenges facing the Islamic World is the fact that the European Economic Group is now heading for the realization of complete internal E.C. unity through the removal of all the financial, material and technical stumblingblocks towards realizing full freedom of movement of goods, people and capital between the E.C 12-member states. As regards banking, it is expected that western banks including Japanese and U.S. banks will nearly fully dominate the E.C with the result that Arab and Islamic banks in Europe would vanish in the light of the biased Basle committee's criteria. This shrinkage began to take shape on a large scale in Arab banks which forced some of them to close their business e.g. Al-Baraka Bank-London and the collapse of the Bank of Credit and Commerce London. On the other hand, Eastern Europe has attacted West European economic activity and efforts are currently underway to form the so-called "European House". This trend might grow during the 1990s which might mean a reduction in the volume of business between Europe and the Third World including the Moslem countries.

6- The decades of the 1990s have become characterized by four main characteristics esp. after the events in Eastern Europe and the Soviet Union as follows:

- Demand for respect of human rights.
- Stressing the importance of religion in people's lives despite attempts to make it dormant for more than 70 years.
- More political democracy.
- Running national economies through market mechanisms rather than direct government orders.

It is expected that the winds of change must in the end blow in the Moslem countries (5).

3. Human Resources Situation in the Islamic World:-

The Islamic World's population was 932.9 millions in 1988 and is expected to grow to 1.273 millions in the year 2000 (6) .

The population growth rate in the Moslem World is at 3 % whereas in America and Russia it is at 0.8 % (7). In 1985 the percentage of the labor force (manpower) to population in the developing countries was 43.5 % while it is 46 % in the industrialized countries.

This table shows a comparison of the proportions of the elementary, intermediate secondary and university education attendance in the Arab, developing and

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the industrialized countries) as follows:-

Region	elementary attendance %	Secondary attendance %	university attendance %
Arab World	58.3 %	64 %	15.7 %
Developing World	79 %	50 %	12.1 %
Industrialized World	91 %	93 %	38.8 %

If we look at the Arab World which constitutes 65 % ofthe Moslem Nation's population, we realize that the percentage of education there is larger than in the developing countries but by far lesser than the percentage in the industrialized world esp. in the elementary stage.

The adult illiteracy percentage is very high in the Islamic countries reaching 44 % approx, in Pakistan and 41 % in Bangladesh and 31 % in Nigeria.

These percentages are reduced among non-school-age children in Pakistan at 33 %, and Bangladesh at 19% and Nigeria at 11 %, but vacillates in the moslem world between 17 % in Indonesia and 1 % in UAE.

It is observed that spending on education and human resources development has been reduced in the Islamic World.

The majority of the Arabian Countries are indentical in their being developing moslem countries, and a comprehensive look at the Arab world shows that it is generally short in scientific specialization including professional and technical specialities esp. the middle prefessional specialities e.g. technicians, supervisors, observers and highly-skilled labor.

As for the administrative positions, there is not a conspicuous shortage in this field, but it needs skills required by modern methods in management and organization. As regards top management and the specialized technical areas, we find that there are educated elements but have no experience, as a result of being cut off from new sources of knowledge (9) .

The ordinary or middle skills labor come from the country side or from the trades who are in the majority of cases illiterate which results in ignorance of the technical aspects and of being out of step with the new Industrial technology.

Some specialist studies in some developing countries have come up with facts which project and magnify the danger of illiteracy i.e. professional ignorance, a matter of great urgency of which (10):

1- The lost time as a result of absences or going to work late in some industries and trades, is more than 25 % of the whole time allocated for the work.

2- The loss percentage due to negligence and incompetency in performance is more than 18 % in the services sector and more than 13 % in the form of ot-

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her industrial loss.

3- The loss percentage due to training insufficiency is 17 %.

Of the problems facing the Moslem World currently is unemployment in some sectors. Some countries have a dangerous shortage in some specializations required for development projects which dictate the urgency of cooperation between Moslem countries to make up for the shortage in labor force in countries where manpower is in short supply. Thus benefiting from countries with large surpluses in such manpower. This, of course, because the percentage of the educated unemployed vis a' vis the total unemployed in some countries has come up to 146 % in Yemen & in Indonesia 14.4 %, 27.8 % in Syria while in some countries it may drop to 2.5 % such as in Turkey and 4.5 % in Malaysia.

On considering the analytical studies of U.N. Report 1990 it has been found out that:

• In the Moslem countries the Individual average share of the Local Product at end of 1987 amounts to $582.6 which is less than its opposite numbers in the developing countries which stands at $1970 and with a large difference compared to its opposite number in the industrialized countries where it is approx $ 14260.

• Average per capita income of GNP in Islamic countries at end 1987 amounted to $ 660 approx vis a'vis $ 650 in developing countnes. But as regards industrialized countries it amounted to $ 10760

• Table 2 shows categorization of the Moslem World as follows:

a) Categorization according to Human Development totals :-

• **Low human development (less than 0.500):** they number 17 states and the lowest in Niger (0.116) and the highest is Morocco (0.489).

• **Middle Human Development (0.500 - 0.799):** 15 countries with Egypt the lowest (0.501) and the highest Albania (0.790).

• **High Human Development (0.800+) including two states only:** Malaysis (0.800) and Kuwait (0.839) .

b) Categorization according to per capita income of GNP:-

• **Low-income Moslem countries (less than $500):** restricted to 15 countries as follows: Afganistan, Bangladesh, Chad, Ghana, Ginie, Indonesia, Mali, Mauritania, Niger, Pakistan, Nigeria, Somalia, Sudan, Tanzania, Democratic Yemen.

• **Middle-income Moslem countries ($500 - $5999):** 15 Moslem countries as follows: Albania, Algeria, Egypt, Iraq, Jordan, Lebanon, Lybia, Malaysia, Morocco, Amman, Senegal, Syria, Tunisia, Turkey, Yemen Arab Republic.

• **High-income Moslem countries (more than $6000):** about 3 countries: Kuwait, Saudi Arabia, U.A.E.

c) The lowest-growth Moslem countries:-

Around 11 states: Niger, Mali, Chad, Ginie, Somalia, Mauritania, Afghanistan, Sudan, Yemen Arab Republic, Democratic Yemen, Tanzania.

Table No: 1

Idicators of Human Resource in The Islamic Countries. Individual Average Share of the Local and National Product in Islamic Countries Compared to the industerialized, Developing countries and The World

Description	Number of Population (Million)		Total Local Product 1987 $ Billion	Total National Product 1987 $ Billion	Individual Avarage Share ($)	
	1988	2000			Local Product 87	National Product 1987
Islamic Countries:						
- Countries of Low Human Development	487.5	699.6	124.6	141.6	255.6	290.5
- Countries of Medium Human Development	426.5	59.6	369.8	417.2	867	978.2
- Countries of High Human Development	18.8	23.8	49.1	56.9	2597	3010.6
Totol of Islamic Countries	932.9	1273	543.5	615.7	582.6	660
Industerialized Countries	1200	1270	12310	11170	14260	10760
All Developing Countries	3900	4960	2210	2320	1970	650
Other Countries	5100	6330	14530	13490	4110	3100

* Taken from tables of UN Report o Human Development for 1990.

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Table No: 2

Classification of Islamic Countries

According to totals of Human Development						According to individual Share of the Total National Income			Countries of Least Growth rates
Low Human Development		Medium Human Development		High Human Development		Low Income less than $ 500	Medium Income from $ 500 to $ 5999	High Income from $ 6000 and above	
Country	**less than 0.500**	**Country**	**from 0.500 to 0.799**	**Country**	**from 0.800 and above**	**Country**	**Country**	**Country**	
AL NAIJAR	0.116	EGYPT	0.501	MALAZIA	0.800	AFGANISTAN	ALBANIA	KUWAIT	ALNAJAR
MALI	0.143	OMAN	0.535	KUWAIT	0.839	BANGLADESH	ALGIER	SAUDI ARABIA	MALI
CHAD	0.157	INDONESIA	0.591			CHAD	EGYPT	U.A.E.	CHAD
GINY	0.163	ALGIER	0.608			GANA	IRAQ		GINY
SOMALIA	0.200	TUNISSIA	0.657			GINY	WORDAN		SAMALIA
MORITANIA	0.208	IRAN	0.660			INDONESIA	LEBANON		MORITANIA
AFGANISTAN	0.212	SYRIA	0.691			MALI	LEBIA		AFGANISTAN
SUDAN	0.225	S. ARABIA	0.702			MORITANIA	MALAZIA		SUDAN
SENIGAL	0.27	LIBYA	0.719			ALNAIJAR	MORROCO		A. YEMEN
BANGLADESH	0.318	LEBAON	0.735			PAKISTAN	OMAN		D. YEMEN
NIJARIA	0.332	TURKEY	0.751			NIJERIA	SENIGAL		TANZANIA
ARAB YEMEN	0.338	JORDAN	0.752			SOMALIA	SYRIA		
GANA	0.360	IRAQ	0.759			SUDAN	TUNISSIA		
D. YEMEN	0.36	U.A.E.	0.782			TANZANIA	TURKEY		
TANZANIA	0.13	ALBANIA	0.799			D. YEMEN	A. YEMEN		
BAKISAN	0.433								
MORROCO	0.489								

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4: Islamic Perspective for Human Resource Development

Islam gives great concern to the human being and favours him to all other creatures, Allah Taa'La said, "We have honoured the sons of Adam, provided them with transport on land and sea, Given them for sustenance things Good and Pure and conferred on them special favours, Above a great part of our Creation. " (Al Isra: 70)

Allah Subhanu Wa Taa'La creates Man for a wise purpose: " I have only created Jinns and men, that they may serve Me. No Sustenance do I required of them, Nor do I require that they should Feed Me. For God is He who Gives (all) Sustenance - Lord of Power - Steadfast (for ever)". (Al Zariyat : 56)

Allah Subhanu Wa Taa'La commands man to populate and flourish earth, God Said, "Worship God: ye have no other God but him. It is He Who hath produced you From the earth and settled you There in: then ask forgiveness of Him, and turn to hun (in repentance): for my Lord is (always) near, ready to answer." (Hud: 61). and He said, "It is he Who has made the earth manageable for you, so traverse ye through its tracts and enjoy of the Sustenance which He furnishes: but Unto Him is the Resurrection." (AL Mulk: 14) .

It is obvious from the above mentioned verses (Ayat) that Man is the center of concern in Islam and he is assigned to populate and nourish earth in response to Allah Command, populating earth is the major means of development and its purposes to achieve the main goal for which Allah Creates Man, that is to worship Him. Therefore, it is essential to give great concern to develop the human resource through Islamic education based on Islamic principles, and to provide the useful sciences assisting in execution of Allah commands.

According to this Islamic perspective, the values, ideals and morals must be developed in every Muslim capable of work, the Islamic Sharia includes basic guidances to be observed by every Muslim which can be classified as follows: (11)

- Belief guidances.
- Moral guidances.
- Behavior guidances .

a - Belief Guidances

The Muslim must believe that his deeds must be related to true values of his righteous doctrine, which the belief that Allah Subhanu Wa Taa' La is the sole and true possessor and proprietor of money and that Human beings are only heirs, Allah Taala said "Believe in God and his Apostle, and spend (in charity) out of the (substance) Whereof He has made you Heirs. For, those of you who believe and Spend (in charity), ... for them is a great Reward". (Al Hadid: 7).

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So, the Muslim must be bound by Allah Sharia, Who is the true owner of wealth, and the Muslim must never violate any Sharia rule and must believe that populating earth is the highest level of worship which is related to work. Allah Ta-a'La Said "And when the Prayer is finished, then may ye disperse through the land, and seek of the bounty of God:" (A1Jamua: 10)

The muslim must always feel that Allah Taa'La is monitoring his works and actions and that he is accountable for them, God said "Not a word does he Utter but there is a sentinel by him, Ready (to note it.)" (Qaf: 18), and it is obligatory to beleive in perfect accounting by God on the Day of Judgement, God said "We shall set up Scales of justice for the day of Judgement, so that not a soul will be dealt with unjustly in the least, And if there be (no more than) the weight of a mustard seed, we will bring it (to account): and enough are We to take account." (Al Anbiyaa: 47).

b- Moral Guidances

There are many moral Islamic guidances which govern Muslims life for they are considered basic elements of productivity, they are:

Trustworthiness: As commanded by God "Ye that belive! Betray not the Trust of God and the Apostle, Nor misappropriate knowingly things entrusted to you". (Al Tauba : 119).

Truthfulness: As commanded by God, "Ye that believe Fear of God and be with those who are true (in word and deed). " (Al Tauba: 119).

Proficiency: The prophet (peace by upon Him) said "God would like any of you who is assigned to a work to do it proficiently.

c - Behavior Guidances

The Muslim observation of the perfect belief and moral guidances will lead him to the nght behavior and good relationships with other people, resulting in rational and prudent conduct such as cooperation, brotherhood, patience and forgiveness.

Some researchers indicates -in defining Islamic concept of economic development- that Islam gives great concern to the economic development problem and handle the problem as part of a greater problem -that is- the human development which is considered one of the major concerns of Islam accomplished through directing the development process towards the right track within the framework ofthe comprehensive Islamic development (12) and the development process should start with providing the needs, then necessities, then Luxuries, to achieve the

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five Sharia goals i.e self- preservation, protection of religon, money, honour and progeny.

Most important of the characteristics of the economic development according to the Islamic concept (13) are the following:

(1) Comprehensiveness: to include all social, political and economic aspects of the community.

(2) Balance: so that development aimed at just distribution beside increase of production.

(3) Realism: to mean idealism derived from the proper religious values.

(4) Justice: since the Islamic Jurisprudence aimed to implement Justice between people.

(5) Responsibility: to specify responsbility of the community members towards each other, and responsibility of the state towards the community.

(6) Suffeciency: to achieve sufficiency to all community members.

(7) Aimed at Humans: since Man is the final goal of the Islamic economic development.

5: Human Resource Development in the Islamic Countries

Development of human resource in the Islamic world requires a plan containing many objectives according to the requirements of Islamic countries which must agree with the islamic values mentioned earlier, and the plan must include estimations of the human resource available in the community to be directed to different production and services sectors to achieve the desired development purposes.

The United Nations report on Human Development for 1990 included analysis performed on a majority of countries worldwide (industrialized - developing) discussing "Growth" matters resulting in three major conclusions we summarize as follows: (14)

1- Investment rate is one of the essential elements influencing growth, so in order to maintain the required growth standards countries must aim to achieve investment rates ranging between 15 %, 20 % of the total national product.

2- Most important, the technical changes must be accompanied by scientific and technological means to develop the human capabilities, so the human development is not important by itself only but considered as one of the major elements of the growth process .

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3- The enveironment of the general policies is considered essential for effective use of the investment resource and for adoptation to the world changes in such a way to provide for continuous growth, it is worth mentioning here that these analysis also state that to achieve growth together with justice is the ideal method to create the required conditions to obtain the desired objectives of human development.

The report also indicates decrease of government expenditure on education and health during the period 1972-1987, and the present increase of this expenditure to the double is a moderate estimation compared to what is actually needed, and it will not be possible to achieve human development objectives unless a high increase in the general resource available is achieved first.

Countries which achieved higher levels of success in the field of human develompent mostly depend on reconsidering the government spending inside the social sectors to rearrange priorities from therapeutic to prophlaxis measures in the area of health, the social spending needs about 25 % - 30 % of the total development appropriations to maintain a suitable balance between social and economical progress.

Many countries allocate a higher percentage ofthe budget for defence, and the military spending in the developing countries increased at the rate of 7,5 % during the last twenty five years whereas in the industrialized countries it reached oniy 2.9 %.

Individual average income in the developing countries is only 6 % of its counterpart in the industrialized countries, in spite of this, the military spending is three times more than the military obligations of the industrialized countries, in the developing countries -which the Islamic countries constitute the great part of it- the military spending exceeds the total spending on education and health compared to a little more than half in the industrialized countries, it reached 104 % whereas it is only 59 % in other countries.

It is essential for developing countries to prepare for the commercial challenges of the Nineties particularly the world economy is changing into services economy, where the great technological achievements of the last two decades especially in the field of traditional services make the human skills an essential element in modern activities such as banking and financial businesses, advertisement, communications, business and public administration.

In the world of today, services represent the major part dominating the economy where they achieve 70 % of the total national product and work opportunities in the industrialized countries, but in the developing countries they are still underdeveloped representing 48 % of the national product and 18 % of work op-

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portunities (15), and emergence of the world new service economy gives advantage to the population rather than natural resource.

Conclusion and Recommendations:

It is obvious from the above mentioned that the human element is the pivot and core of the development process since man is the main actuator of all elements, and development levels depend mostly on human skill and efficiency and performance standards.

The Islamic countries must strive to develop the human resource which is considered the most important element of production so as to meet the expected challenges, this must be done through plans to develop the human resource having into consideration development of the human skills and proficiency to obtain the maximum use possible of the human element in the production process, the human resource development plan in the islamic world must be prepared with regards to the Islamic guidances and the needs of Islamic countries to achieve social and economic development.

In order to achieve the human development in islamic countries the development plan must include the following requirements:

1- Increase of investment spending on education, technical training and health care.

2- Promotin of education, educational curriculum and training programmes in conformity with the development requirements in Islamic countries.

3- The human resource development plan must include all the state modern and traditional sectors.

4- The development plan must be based on the Islamic guidances and values for developing the Muslim attitude towards work and performance

5- To achieve better utilization of human resource available by means of preparation and development together with taking the necessary procedures to use these resources.

6- To increase the investment rate to more than 15 % of the total national product.

7- Availability of policies encouraging investment, development of existing human resource after rehabilitation according to Islamic principles, and to benefit from the modern technologies.

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LABOR ECONOMICS FROM ISLAMIC PERSPECTIVE

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1. Introductory General Framework

To understand labor in Islam, a comprehension of the general ecnonomic system is necessary. Islam brings principles and systems which are applicable in every age and circumstances even after radical social and economic changes. These principles embody Islamic economic and social systems and structures, like a seed embodies a tree (Karakoç 1980:20). Further, unlike capitalism and sociatism, Islam has an internal consistency which relies between individuals, groups and institutions in the society. Both of these systems characterized by extreme and unbalanced approaches to solving man's economic problems. Islam has been protected as the midway incorporating the good points of both systems and free from their imbalances (Siddiqi 1980:235-6).

In Islam, man is the purpose and means of the social and economic system, whereas socialism-communism-liberalism-capitalism over emphasize economy itself and ignore human factor. According to these systems economic development is a magic concept that determines all phenomena. However, the Islamic concept of development has a comprehensive character and includes moral spiritual and matenal aspects together. The focus for development effort and the heart of the development process is man. Islam insists that man is an indispensable factor for the economic development (Ahmad 1980: 179).

Capitalism is by definition, a capital oriented system, thus it makes capital dominant over labor. On the other hand, socialism denies capital which is actually an accumulated form of labor. Both systems neglect labor directly or indirectly. In Islam labor is the essence, but capital is also valuable if it is connected with labor

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and earned in "halal" ways. Therefore, Islam takes Both factors in a just system (Siddiqi 1980:236-43). Capital and labor are not conflicting factors but complementary in Islam. There exists parallels between the interests of employer and employee. These fact provides these interests with an opportunity to develop together without conflicting each other, and also motivates economic growth and development (Ahtar 1994:39). Both parties stimulate capital and labor and share in the profit earned by partnership (Abu Saud 1980:68; Siddiqi 1980:206).

Labor relations, in Islam, can be seen as a reflection of the general characteristics of Islamic society. Islam regulates the society as a system through various rules and institutions. Islam also practices the Divine System via individuals who behave according to Islamic ethics. Islamic society is a social system composed of individuals who relate "faith" and life in their legal and economic activities. Therefore, Islamic society's stability is based on the coexistence and the development of "homo-Islamicus" employee and employer. The actors of the economic life are composed of such muslims.

The concepts of "utility" and "satisfaction", which are the foundations of modern economics are confined to individual and secular dimensions. However, in Islam, these concepts include dimensions related to hereafter i.e. "ahira" as well as social aspects in this world "dunya".

The paradigms of the modern economics and the Islamic economics are different. Homo-economicus gets satisfaction only at the degree of his personal utilization of goods and services, while homo-Islamicus gets even more satisfaction from sharing with others and helping to others (e.g. moving a stone on the road off, making charity, sadaqa al-fitr, zakat.). As a result, utility concept in Islam is not confined to the worldly activities. The absolute and eternal utility and reward will be harvested in hereafter.

This view is also valid for labor relations in Islam. Islamization of labor relations depends on the degree of individual's Islamic sensitivity and fidelity to the principles of Islamic ethics. Another must for this is of course, the availability and sovereignty of Islamic rules in the society. Although modern labor and industrial relations is developed after industrial revolution, labor relations is as old as humanity. Islam regulated labor relations within the economic and social context during the ages when the Islamic system was dominated in the society. The legacy of Islam is the rules, determined by "nass", the Islamic institutions and norms of Islamic behavior and ethics, and also Islamic experiences.

As this legacy is given, the Islamic system requires the implementation of this legacy to the changing economic and social conditions at different ages and periods. In this respect, two aspects of Islamic labor relations can be observed. The

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first is the analysis of the Islamic "nass", behavior and practices under the modern labor economics and industrial relations disciplines. The second is the adoption and application of this theoretical system to the modern and current life and circumstances. Further, the reality of the rapidly changing world and the rising new values make the consideration of the future prospects vitally important.

2. Labor Relations in Islam

In Islam, the labor relations system stands on a tripod: Employee, employer and the state ("al-dawlat'ul Islamiyya"). Employee and employer are the natural elements of the system. The state, acting in the name of an Islamic society, has a regulative and supportive function. In this respect, Islamic labor market is an institutional and protective market where supply of and demand for meet freely. Howver, since Islamic economy, like any other social fact, is required to maintam the normative characteristics of the Islam, the operation of this market should not be considered as completely outside of any restriction. "Akd al-ijarah" (contract of labor hiring) constitues a sufficiently explanatory example of this. Although akd al-ijarah depends on free desire of employer and employee, this means that parties are free to make the decision of accepting or refusing, determining the conditions between themselves, etc. in beginning once they agree on the contract, akd al-i jarah becomes an act which creates as det relations between employer and employee Thus, the work, wage and duration must be pre-determined and the nature of the work must be legal according to Islamic code, "shari ah" (Tabakoğlu 1983-9).

Before examining Islam view abaut labor unions collective barganing strike and lockout, it is important to give a brief historical perspectve and functions of these institutions. Labor unions and collective barganing are the products of post-Indusrial Revolution era. Industrial society conceptualizes the shift from labor intensive mode of production to capital intensive one. In this sense, capial-intensive mode of production represents small-scale industries and production. Thus, we can conclude that mass production is synonym of industrialization and capitalism.

The industrialized capitalist system which emerged in Western society exploited the wealth of Far-Eastern and African countries, thus obtained the natural resources hat were necessary as production unputs. Africa and just explored new continent, america, were the source of old and silver from which, the bourgeoisie, or entrepreneurs which accidentally emer-ged, benefited as capital.

The small enterprises which could not compete with the rapid development of industry collapsed and their unemployed but qualified human resources provided the vitally factor of production: Labor. However, this very soon became insuffici-

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ent to satisfy the increasing needs. Thus rural population that moved to urban areas after they had got their freedorn following the French Revolution came to constitute main source of labor supply. The basic institutions of labor economics and industrial relations were introduced under such in human conditions and in an atmosphere where there was no place for concepts such as mercy and goodwill.

The role of unions in this system was to defend and develop the interests of workers There was a continuous and natural conflict between employer and employee hence, unions, sometimes, had to use to pressurize employer to obtain workers' demands.

The modern industrial system divides labor and capital into two hostile camps, whose interests always conflict and lead to a great waste of capital and manpower in the capitalist countries. In spite of legislative measures to protect the rights of labor, the conflict has not decreased but has, in fact, increased in recent years, especially in the UK and USA. The trade union movement has mostly failed to realize its objectives and consequently, unofficial strikes and industrial action have become the common feature of almost all industries in these countnes. Considerable amount of orders are lost every year annually by the Western counries, the UK in particular, as strikes and unofficial industrial actions prevent the delivery of goods in time.

This conflict and rivalry between labor and capital cannot arise in an Islamic society. Islam links both labor and capital through fraternity and brotherhood in such a way that their interest do not clash. It encourages among the believers noble sentiments of mutual trust, goodwill, respect for others' rights, equality, equity and love and affection. A Muslim entrepreneur cannot remain as a true believer ifhis sole intention in production is to profit. On the contrary, he will invest his capital in those industries and enterprises which will benefit the whole community and will, then, be grateful to Allah for any profit he makes. His main object of investment in industrial and other undertakings will always be the service of humanity for the pleasure of Allah. It is true that he will also try, like other capitalist, to increase his productivity, but this not be his sole (or even chief) motive in production. He will always consider the greater good of society, as well as of those who assist him in production, and will never execute his plan of achieving higher productivity at the cost either the common good or the welfare of the people working for him.

This is because of the spirit of goodwill and Allah for others which Islam has developed in the true believers. And Islam has fostered good relations between capital and labor mainly through moral teaching and practical examples from production the lives of the Prophets of Allah. There is a lesson for us in the story of

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Moses to improve industrial relations and put an end to this conflict between labor and capital. After killing a man in Egypt, Moses turned to Madyan and the daughter of Shu'aib advised her father to employ a healthy and trustworthy worker in these words: "O my father, engage him on wages; is (the) man who is strong and trustworthy."(28:26). After describing the necessary qualities of a worker, the Holy Qur'an mentions the good qualities of an employer in the fonowing words: " That you serve me for eight years; but, if you complete ten, it will, and I intend not to place you under a difficulty. If Allah pleases, you will find me one af the righteous." (28:27).

Here is the lesson for the capitalists to be merciful and just to their employees in paying them their deserved remuneration and in providing better working conditions and for ule workers to be hard-working and honest in their duty to their employers and the community. Thus both the employer and the anployee are made to realize their duties and responsibilities to one another.

After this discussion, the contrast between two system becomes clear. Thus, it is obvious that the roles and features ofthe labor union system mentioned in the beginning of this section and the ones of a potential labor union in the Islamic working order would be significantly different from each other. Making a static comparison between these two institutions and their content and contrasts in a comparative manner would definitely be misleading and this would atso be systematically incorrect.

This a fact that we cannot find collective bargaining and labor unions system during the era when Islamic rules dominated the society. This is caused by the lack of collective labor relations, which is a result of the structure and characters of the economy. In fact, this, argument is true for pre-industrialized era of Western societies as well. This should not directfy imply that collective bargaining and labor unions cannot play any roles in Muslim societies, nor can they take place. When there is a need, new institutions that Islamic law permits or at least does not prohibit may be introduced or developed naturally. However, we should first answer the question that whether there is a need for a system and institutions which came about from the facts of and needs of an industrialized capitalist society. Even though Islamic law does not bring any prohibitions, the basic differences in fundamentals and perspectives of these systems may not allow to establish these institutions into the economical and social structure of Islam.

3. Importance of Labor

Labor means any exertion of body or mind undertaken for some monetary reward. It includes all kinds of work, whether manual or intellectual.

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The Holy Qur'an has placed great emphasis on human labor. This is evident from the following verse of Surah al-Najm:

"There is nothing for man but what he strives for."(53/19). It is explicity stated in this verse that the only way to obtain anything from nature is by hard work. The success and progress of man on this earth is dependent on his efforts. The harder he works, the richer he gets. This principle is further clanfied in Surah al-Nisa:

"For men is the benefit of what they earn. And for women is the benefit of what they earn." (4/32).

Again in Surah Fussilet:

"There is a guaranteed share for those who seek and endeavor." (41/10).

Therefore, it is obvious that Islam considers labor as a whole, consisting of material and moral aspects and regards it as the most auspicious means of production and living. The best reward is the result of hand labor as stated in a Prophet's saying:

"No one consumed anything more blessed than the result of his own work." (Tabakoglu 1983:3-4).

The Holy Qur'an puts a significant emphasis on work and indicates very clearly that man is created to work hard for his livelihood in this world. This is mentioned in Surah Al- Balad:

"Verily We have created man into toil and struggle." (90:4).

The description of life in Paradise is a reminder to man that his happiness and comfort on earth also depends upon his labor. An easy and affluent life is promised to those who work and not waste their time in idleness. Anyone who has worked hard for his livelihood will enjoy a peaceful and prosperous life; while the one who has wasted his time in idleness will be thrown into a life of misery, hunger and degradation.

There is also reference to intellectual labor in ahe Holy Qur'an. A dialogue between the Prophet Yusuf and the king of Egypt throws some light on this subject: "And the king said, "Surely you are in our presence today dignified, trusted". He (Yusuf) said: "Set me over the storehouses of the land. I will look after them (for) I am a skilled custodian (organizer)". And thus did We give to Yusuf power in the land He had mastery in whatever he liked. We bestow our Mercy on whom We pleased, and We waste not the reward of the doers of good". (12:54-56).

The Holy Prophet also emphasized the importance of labor on various occasions and often appreciated the efforts of workers and artisans in their work. Once he remarked: "Allah loves those who work and strive (for their livelihood)".

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Almost all the Prophets had to work for their living. The Holy Prophet himself worked. His pasturing of sheep and advising others to adopt that profession for earning their living is a clear indication of the great importance of labor in Islam. In Gazwa Ahzab, when a ditch was dug to defend Madinah, from the invading armies, the Holy Prophet was seen working and lifting earth and stones like an ordinary worker atong with other Muslims.

In addition to encouragement of work, on the issue of labor supply Islam also orders the development of the quality of labor. Islam emphasizes physical and moral health, mental fitness of labor. Also factors such as knowledge, education and training which to increase efficiency are encouraged in Islam.

From the perspective of labor economics, Importance of labor in Islam is emphasized by many Muslim academicians, thinkers and also by leaders of Islamic movements (Siddiqi 1980: 229-30). Labor is not considered only as an extremely respectful concept: Such that even decision making process is recommended to be realized through cooperation between labor and capital on a mutual consultation basis (Hameedullah:213-233; Chapra 1970:54). The Pakistani thinkers, and labor expert of the Jamaat-i Islami Abdul Majeed Qureshi, brings a new concept into discussion, "depreciation of labor" (Siddiqi 1980:229).

According to Qureshi depreciation of labor must be paid for: This which means that maintenance of health and medical aid should be totaly internalized in cost accounting. Thus a new equilibrium between labor and capital should be introduced such that the privileged position oflatter be taken away in the favor ofthe former. (Qureshi A:40-45, B24-28).

4. Mobility of Labor

Movement of labor from one geographical area to another or from one occupation to another is called mobility of labor. Mobility of labor has a great bearing on the economic condition of workers. If workers can easily and freely move from one place (or occupation) to another where they can get better wages, they can improve their standard of living. If on the other hand there are restrictions on the movement of labor from one place (or occupation) to another place (or occupation) many workers, especially in the backward areas, would not be able to easn a decent wage. Workers working in the areas (or occupations) with scarcity of labor will be able to earn more in comparison with the areas (or occupations) with an ample supply of labor.

Islam has recognized this right of workers and has granted them full liberty of movement from one place to another as wen as from one occupation to another to seek better markets. In Surah Al-Nisa, it is said:

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"He who forsakes his house in the cause of Allah (in order that his economic condition may improve) finds much refuge and abundance (of wealth) in the earth".(4:100).

It is also stated in Surah Mulk: "it is He who has made the earth manageable for you sotraverse ye thorough its tracts and enjoy of the sustenance which he furnishes: But unto him is the resurrection". (67:15).

In these lines, the Holy Qur'an has stated a fundamental principle which, if practiced without restriction by the people of different countries, could check an undue fall in international wages and maintain them at a reasonable level. There is no doubt that international wages would be stabilized at a reasonable and equitable level by way of free internal and external mobility of labor. And mobility of labor, according to the Holy Qur'an is a very effective and appropriate method of solving many of the economic and socio-political evils of modern times. There would be less friction and inequality between capital and labor and the world would be happier if all the members of the United Nations realized what damage is being done to world peace and prospenty due to restrictions imposed by some of the member countries.

Every lawful occupation is open to all men, irrespecitive of color caste or creed and every man is free to adopt any profession he likes. There is sufficient evidence to prove that Islam by teaching people to respect their brethren regardless of their occupation gave dignity and status to manual labor. It encouraged people to do all kind of work to earn their living without hesitation. The Holy Qur'an quotes many examples from the lives of great prophets who worked with their hands to earn their living. We are told how the Prophet David made coats of mail and armored himself and the Prophet Noah built the boat with his own hands. Abraham, Moses, Jesus, all great Prophets of God, bfed and reared sheep themsehres. The Holry Prophet gave practical training to the Muslims not to hesitirte in adopting even the meanest of occupations to earn their living. There are many sayings of the Holy Prophet which reveal how, by his own practical example, he trained his disciples in high moral ideas and the dignity regardless ofhis occupatation.

5. Freedom of Occupation

There is complete freedom of work and of movement in Islam. Everyone can do any work he likes and can move feely from one occupation to another and from one place to another without any restnctions. In other words, there is complete mobility (geographical as well as occupational) of labor in Islam as shown in the following verse of the Haly Qur'an:

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" (The will) say: Was not Allah's earth spacious, so that you could have migrated therein? And whoever flees in Allah's Way, he will fuld in the earth many a place of escape and abundant resources". (4397-98).

Here is a clear indication of geographical mobility of labor. The Muslims are advised to move from places with scarce means to other places where they can find abundant resources and great prospenty. This helps to raise the wages of low-paid workers and also to stabilize wages throughout the country. If this principle were practiced without restriction by all countries, it would facilitate standardization of wages all over the world. Taking into consideration that one of the important problems of the modern world economy is the differences in wages between regions and countries, the significance of this principle can be better understood.

6. Rights of Labor

The fact that wealth is jointly produced by labor and capital is fully recognized by Islam. It reminds them both of their duty to Allah and His creatures and enjoins them to look after the interests of others as their own. But as labor is ul a comparatively weaker position and its interests is likely to be threatened by capital. Islam takes special care to protect its rights. The Holy Prophet treated his servants as members of his family andd advised his companions to treat them well. He is reported to have said:

"Your employees are your brothers whom Allah has made your subordinates. So he who has his brother under him, let him feed him with what he feeds himself and clothe him with what he clothes himself and not burden him with what overpowers him. If you do then help him".

The basic rights of labor may be summarized as follows:

1) The worker is entitled to a wage which enables him to enjoy a decent standard of living.

2) He should not be given any work which is beyond his physical strength: and if at any time, he is entrusted with heavy work, he should be provided with assistance in the form of more labor or capital or both.

3) He shoutd be provided with suitable medical care when sick and paid adequate sick pay for that period. It would be mosl desirable from a the contributi-on of labor and capital towards sick pay were supplemented by governmental assistance (possibly from the zakat fund).

4) Reasonable provision should be made for the payment of an old-age pension to the worker. The employer and the employee may be asked to make so-

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me contribution towards this fund but mainly it will be contributed by the Islamic State from zakat.

5) Employers should be encouraged to give all their sadaqas (voluntary charity) on their employees and their children.

6) They shold be paid unemployment benefit during periods of unemployment from the zakat fund. It will strengthen their bargaining power and will assist in stabiliang the wage rates at a reasonable level in the country.

7) They should be paid adequate compensation for accidents during work.

8) Goods manufactured in the factory should be given to them free or at cheaper rates.

9) They should be provided gently and politely and forgiven if they make any mistake during work.

10) They should be provided with decent accommodation so that their health and efficiency may not be adversely effected.

Fines: Islam forbids the employer to impose any fines on hts employees in case of damage to goods or appliances during work. The principle that the employer should, under no circumstances, be entitled to impose fines on labor was stated by Imam Ibn Hazm in these words: "The worker, whether a partner or an artisan, cannot be subjected to a fine, if goods are damaged by him during work unless it is proved that he did it deliberately and witnesses are available; otherwise hir, statement with affidavit in support of his defense will be accepted."

All the Muslim jurists, including Imam Abu Haneefa and Imam Malik, agree that no frne can be legally imposed on a servant (worker), who is employed for any period of time on fixed wages for damaging goods (or tools) unless it is proved that he did it willfully and purposely.

7. Conclusion

When the current situation of the world economy, is analyzed it can be seen that human kind is facing with crucial and very serious prblems. Capitalist and socialist systems due to their secular charactenstics, separate economical life from sacred element, a problem of discrimination. Materialistic way of thinking does nat leave any other values than its own ones to man; thus individuals denies everything except the ones that they can physicany feel. It is true that positivism led to improvements in sciences and promoted development in technology, but on the other hand the moral values are kept out of consideration and spiritual development concept is completely neglected. This ongoing development and advanced technology, ultimately, leads to enormous and incredible poverty and misery.

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Exploitation of oppressed people by powerful riches increases every day, the social economical disequilibrium and inequalities between and even within nations are getting worst. While technology is reproducing and developing itself by its innovations, the natural resources of the world is consumed rapidly and unfortunately technology is not developed in accordance with human needs. Economic recessions, floating, shortages and conflicts threaten and most of the time destroy the world peace which is not already extensive.

However, world economy is experiences a structural change. The myth of mass production which have eliminated been determining all the aspects of the life, is may be coming to its end. Industrial Revolution terninated small-scale industry and home-production; to a large extent but nowadays the trend is returning towards its original direction. As Toffler mentions (Toffler 1991:50-2) Third wave economics represent the decline of the industrialism. In fact, these are both socialism and capitalism which are declining. A new understanding of technology, new forms of working individualization, social differentiation and pluralism, new kinds and models of production emerge. These innovations, announce the liberation of production, consumption, communication, cultural life and even family structure from one standard type. The indicator of being developed becomes being differentiated and pluralistic structure.

This change affects the type of labor and worker, as well. New worker is more independent, more prottuctive and more specified. New technologies and flexible industries do not need "old fashioned" workers who do only repetitive and standard tasks. New system requires productive, innovating challenging, individualistic and qualified type of worker. Working class concept or masses of workers that communism targeted has already lost its importance and even its significance; now its time for mass production to model end, too.

It is argued that all this developments siginal that conflictng interests of employer and employee will soon disappear and a cooperative model will arise. Islam, does not only cormbines all dimensions of the life, establishes equilibrium between material rtnd spiritual aspects of the life. But it also comines he life and the other world "hereafter" Thus, Islam will provide the only humanstic basis for labor economics and industrial relations, because this is only system which protects and defends human values. Islamic economical system is getting more and more important as an alternative economical approach. The revival thet we are observing all over the Islamic world in social, cultural and political areas promotes this fact. Because Islam the religion of Allah-u Teala, the religion of "fitrah" will be the unique way out for all human beings from the "zulumah" of "cahiliyyah" to "al-nour al-Islamiyyah".

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ISLAMIC INSURANCE

SOME THEORICAL CONSIDERATIONS AND PRACTICAL IMPLICATIONS

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INTRODUCTION

Insurance has been one of the leading issues in Islamic Economics, closely scrulinized and detailly studied by a number oi prominent Muslim Jurisprudents for many years SIiII, it has been the subject of continuing contraversy amongst the Muslim Jurisprudents who have come up with widely differing opinions and judgements as to the permissibility of insurance with respect to Islamic values.

The widely divergent opinions of It Muslim Jurisprudents can be grouped under the following broad categories:

(a) those Muslim jurisprudents who approve all forms of insurance;

(b) those who disapprove all forms of insurance;

(c) those who accept general insurance lubject to certain limitations and qualifications.

In disapproving all forrns of insurance, the typical approach has been either of the following :

(i) compare and contrast insurance (as a particular type of contract) with traditfonally approved fomrs of contracts under the Isramic Jurisprudence, and if it does not conform to any of these forms, disregard and reject insurance as an acceptable category,

(ii) without a close look at and due consideration to the basic principle and thtr sirnple scheme of insurance, consider modern-day (existing) insurance system as one and the only possible form of insurance, and reject it on the ground that it contains certain elements in it, which are repugnant to islamic values.

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This paper first examines the major objedions raised against insurance in the light of the basic principle of insurance, and shows that such objections do not relate to the essence of insurance. And then, as the exisling (modern-day) insurance system is belived to contain certain elements which are not acceptable under the Islamic belief system, an alternative insurance system (co-operative insurance) is outlined, as implemented at present by certain insurance groups in the world, which remove such unacceptable elements.

I. A BRIEF AŞSESSMENT OF OBJECTIONS RAISED AGAINST INSURANCE

Whilst the basic principles of insurance (as abstracted from the niodern-day commercial insurance system) are approved by majority of Muslim Jurists, there exist various objections raised against insurance at conceptual as well as practical level.

A closer and careful examination of these objections suggests that they largely stem from not being able to comprehend the basic principles of insurance properly, ancl from accepting the existing (commercial) insurance system as the one and the only possible form oi insurance.

Insurance is a type of contract, and for it to be an Islamically acceptable contract, it must be free from certain elements which are prohibited by Islamic Jurisprudence. An Islamically permissible transaction or contract must, for instance, be free from interest (riba), uncertainty (gharar), gambling (maisir), fraud and cheatins, ignorance and other similar evils. If the basic principle and the simple scheme of insurance does not contain any of the elements (evils) not permitted under Islamic Law, then it can be considered as a permissible form of contract (transaction).

In this section; we intend to go through various objections raised against insurance, and to the extent there may be some weight in any of these objections, they must be analysed and replied by counter acguments.

(a) Insurance and Gambling

Some scholars find an element of gambling in all kinds of insurance as a matter of principle. Thus, according to their opinion, irrespective of how insurance is organized it can not be freed from gambling.

Treating insurance as a kind of gambling stems from failure to make a proper distinction between the hvo with respect to the type of risk involved in and motivation behind each of these activities and their implications on income and wealth distribution in the society.

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(i) The risk involved in gambling is an optional risk in the sense that, the risk of financial loss incurred by the gambler could have been avoided had he decided not to gamble. The gambler, motivated by the hope of gaining, becomes exposed to the risk of financial loss as a result of his voluntary choice. Such risks involve both loss and gain. On the other hand; there are other risks in daily life whose occurance do not depend on a particular voluntary choice. Such risks, called pure risk, involve only chance of loss without any chance of gain.Insurance entails "pure risk" in the sense that the occurance of, say, an accident against which the individual (the insured) seeks financial protection does not in any way depend on whether he has taken any measure against it or not (e.g. whether he is insured against it or not). Insurance risk is a measurable risk in that the probability of incidence of a particular insurance risk can be measured (estimated) fairly accurately with a certain margin of error, based on the Law of Large Numbers and the Law of Averages.

Thus; as different from gambling which involves optional risk (the risk arising from voluntary choice), insurance involves pure risk the incidence of which does not depend on any voluntary choice of the individual.

(ii) Motivations behind gambling and insurance are also fundementally different. The financial motivation for becoming insured is to have protection against the financial loss to be suffered in the event of occurance of an apprehended peril. The insured, by paying a certain (agreed) premium, becomes entitled to receive compensation for the financial loss in case of occurance of the risk. Thus, the stipulated payment of compensation (claim money) to be received by the insured must be regarded as a relief from the burden of loss incurred, rather than a profit as this payment is not an enhancement to his wealth. On the other hand; in case of non-occurance of the apprehended peril, he does not receive any payment of compensation against the premiums he has paid. Should this be considered as a kind of net loss to the insured? Premiums paid by the insured must be viewed as a price paid for receiving a socially useful service (or "an investment towards security"), and not as a loss in any sense.

In the case of gambling, the motivation behind the gambler's taking risk is the hope of gain in order to enhance his wealth. In case of winning, the money won is an addition to his wealth, whilst losing is an absolute loss.

(iii) Gambling and insurance have different implications on wealth and income distribution. Financial losses resultant from incidence of insurance risk are disrupt'ive to income and wealth distribution as they are net losses to the individual incurring the peri¥. Insurance provides compensation for such losses, thus restoring income and wealth distribotion approximately to its previous (pre-inciden-

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ce) condition. On the contrary, in gambling there is a redistribution of social wealth from the loser to the winner, and this redistribution does not stem from need-based rights of the winner, nor from any productive labour and contribution or competence on the part of the winner, but from pure luck. Gambling not only disrupts wealth distribution based on labour, competence etc., but also discourages productive human activities.

(b) Insurance and Uncertainty

An Islamically acceptable contract or transaction must avoid elements of uncertainty as to the rights and obligations of each party, which are likely to lead to disagreement and dispute in future. Except in certain cases where uncertainty (GHARAR) can not be removed entirely by nature of the transaction, uncertainty is not permitted to be present under the Islamic Jurisprudence.

It is argued that insurance contract contains a great deal of uncertainty in that (i) it is uncertain whether or not the insured would receive any compensation against his premium payment (as he becomes entitled to receive it only in the case of occurance of the apprehended peril), and, (ii) if and when such peril ever occurs, the amount of compensation is not certain.

Firstly; whilst according to Islamic Jurispruclence, element of uncertainty should not exist in a permissible contract or transaction, in certain cases transactions fulnlling genuine needs (where there exist no other ways of fulfilling such needs) are permitted to contain some tolerable level of uncertsinty if such uncertainty can not at all be removed by nUture of the transaction. Thus; permissibility of uncertainty becomes rather a matter of degree than of quality. None-the-less, there exists a diference of opinion as to the permissible level of uncertainty amongst the Muslim Jurists.

Secondly; in insurance there exists uncertaintu at the individual level as the incidence of a particular risk (against which insurance is taken) can not be determined at the individual level. But uncertainties are determined fairly accurately at the collective level (by virtue of the Latv of Large Numbers and the Law of Averages), which is the-very essence of insurance. In other words, occurance of a risk is known and certain at the collective level, whilst unknown and uncertain at the individual level. Bearing in mind the collective nature of insurance, it is quite inappropriate and incorrect to reject insurance on the ground that it contains element of uncertainty at the-individual level.

Thirdly; in insurance contracts, as long as the rights and obligations of both parties are defined clearly and unambigiously, there would not be any future disputes between the parties. Even if the insured party does not receive any return

on his premium (investment), he is well aware of the fact that, he is insured against the possibillty of a future peril which may or may not at all occur.

(c) Insurance and Interest (Riba)

Another objection raised against insurance is that insurance entails interest, explicitly and implicitly. The question to be raised aaainst this objection is whether interest relates to the essence of insurance, or it exists in insurance contracts only as a result of a particular organization of insurance business. In other words, is the relationship between insurance and interest a theoratical or a practical issue?

Funds accumulated in the hands of insurance companies are generally invested in short-term, liquid interest-bearing assets, lor practical as well as legal reasons, in order to secure constant growth of such iunds at minimum possible risk of loss. But investment of available funds in interest-bearing assets has nothing to do with the basic principles of insurance. It is possible to invest such funds in other assets (i.e. non-interest bearing assets), thus removing the element of interest from insurance transactions.

II. CO-OPERATIVE INSURANCE IN PRACTICE

Majority of Islamic Jurisprudents agree that the basic principles of insurance are not contradictory to Islamic values. The question is, how to organize insurance in the modern society without any necessary involvement in practices disapproved by the Islamic Jurisprudence.

It is argued that the existing (commercial) insurance system considers insurance as trade whereas Islamically acceptabfe insurance (cooperative or mutual insurance) is essentially a form of cooperation on the basis of charity and piety. But how to achieve an insurance system based on solidarity and cooperation?

It is Clear that achieving cooperative insurance is far easier and more readily managable in a group of limited number of people exposed to the same or similar type of risks. These limited number of people can easily manage their insurance activity on voluntary basis without too much need for a professional management. However, any activity through voluntary contributions becomes quite difficult to carry on in the Iong-run, and almost impossible to manage in an efficient and effective manner as the number of people in the group increases substantially. Thus, as the scale of activity increases and becomes more complex, a professionai contribution becomes indispensible to organize insurance activity of the group members on full time basis, efficiently and through sophisticeted methods. This professional contribution can possibly be provided by a company (insuran-

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ce company) rnanaged by professionals with experience and expertise in insurance business.

Now the question is: if insurance is not to be considered as trade (as in the case of commercial insurance system), how to incorporate a profit-seeking (professional) company into the Cramework of cooperative insurance. Stated differently; how to reconcife the profit-making objective of a company offerifig insurance service, with an insurance activity essentially based on solidarity and cooperation, and not on profit-making.

An acceptable insurance model must therefore critically look at the nature of the relationship between the insurance company and the insured. The relationship between the insurance company and the insured must be substantially different than that between the existing commercial insurance company and the policy-holders.

In what follows, a cooperative insurance model is outlined, which is broadly practiced by some Islamic insurance companies in some Islamic countries.

Cooperative Insurance Model

1) A company is established with a certain paid-up capital, whose business objective is to carry out insurance activities on co-operative basis. The company employs personnel with sufficient expertise and experience in insurance business.

2) The company employs the most modern scientific methods adopted in the field of insurance, for (a) securing the statistical data for insurance, plannins and controlling purposes; (b) estimating premiums (contributions value) for the different insurance funds according to the type and nature of the risk and the probability of its occurance and other technical aspects, and (c) expediting payment of indemnity to those whose properties were effected by damage, immediately after occorance.

3) The company provides all insurance services, such as insurance, reinsurance and offers technical insurance consultations in all insurance clesses. Accordinglyl, aseperate fund is established for each insurance class (marine, transport, aviation, rnotors, fire, engineering risks, miscellanous accidents, medical expenses, workmen compensatian etc..)

4) Persons/companies who wish to subscribe to a particular insurance funds make a stipulated contribution (pay premium) to the respective insurance fund.

5) Contrary to commercial insurance companies which invest most of their funds in liquid, interestrbearing assets, the company invests policyholders' funds (and its own equity funds) in interest-free assets. Thus the element of interest is removed from the insurance activity.

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A certain proportion (say 20 %) of profitsgenerated from investment of policy-holders' funds is taken out by the company as its "management share" (a fee for providing insurance service to participants of the insurance fund), the remaining balance is augmented to the insurance fund.

6) The company's income consists of return on investment of its own equity funds plus its management share. Gross company profit is obtained after deducting company expenses. Note that, as different from commercial insurance system, the company's income do not in any way relate to insurance activity itself. In the case of a commercial insurance company, gross profit of the company is roughly premiums collected plus return on available funds invested minus compensations paid and expenses incurred; in other words the company's profit performance is directly related to insurance activity.

7) Available insurance funds consists of collected and due contributions (premiums) plus policyholders' share of profit earned from investment of available funds. Certain items are deducted from available insurance funds in order to arrive at "insurance surpfus" if any. "insurance surplus" is the end result of insurance activity. These items are :

(i) the net of paid and due contributions

(ie the company's share in compensations after dedocting the share of co-insurers and re-insurers of compensations),

(ii) the insurance direct costs

(costs of insurance contributions and cost of reinsurance with the companies Participating in the insurance coverages,

(iii) premium reserves

(reserve against continuing risks). It is the portion of contributions collected during the year and which pertain to next years.

(iv) the share of insurance fund of the company's administrative expenses.

These expenses are distributed among the different insurance funds in a suitable method proportional with the relative importance of the insurance fund. Such expenses represent the insurance funds's responsibility for the administrativ expenses as regards the supervision, contracts etc..

Distribution of insurance surplus, if any, to the insured. There exist alternative approaches with regard to distribution of insurance surplus to the policy holders. They are follows:

(i) distribute the insurance surplus to every policy-holder (according to his respective share in the fund), irrespective of whether or not he has received any compensation during the year.

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(ii) do not distribute any insurancesurplus to those policy holders who have received compensation during the year; distribute the entire insurance surplus to those policy holders who have not received any compensation.

ii) If the policy holder has received any compensation, deduct the compensation amount from insurance surplus due to his share, and pay the positive difference, if any.

Distribution of insurance surplus (reflecting the profitability of the policy holders' fund from insurance activity) is consistent with the cooperative nature of insurance. What would under commercial insurance system becorne profits of an insurance company now goes to those who have come together to cooperate for a common purpose, i.e., reducing the financial burden of risks to which they are commonly exposed, through cooperation and solidarity. Thus insurance becomes not a trade out of which a particular group makes subtantial profits, but a socially useful activity at minimum possible cost.

3. CONCLUSION

A vast majority of Muslim scholars recognize that insurance is a genuine need and a socially useful service, and its basic principles are not in any way contradictory to Islamic values. It appears that the objections raised against insurance largely stems from viewing the existing (commercial) insurance system as the one and the only possible form of insurance, as well as from various conceptual confusions about insurance.

Based on the opinions of Muslim scholars approving insurance subject to certainlimitations and qualificationsl a number of (Islamic) insurance companies have been established in various Islamic countries, providing insurance services to the community on co-operative principles. Despite that an insurance system based on co-operative principles is stills at its infant stage, these companies have shown considerable success in terms of increase of business volume as well as diversification of products provided. However; whilst these companies have shown success as far as insurance business is concerned, they still depend almost entirely on conventional insurance companies for re-insurance of their risks. Their dependence on the conventional insurance system may however be expeded to decline in future as the number and business volume of companies working on cooperative insurance principles rise in the future.

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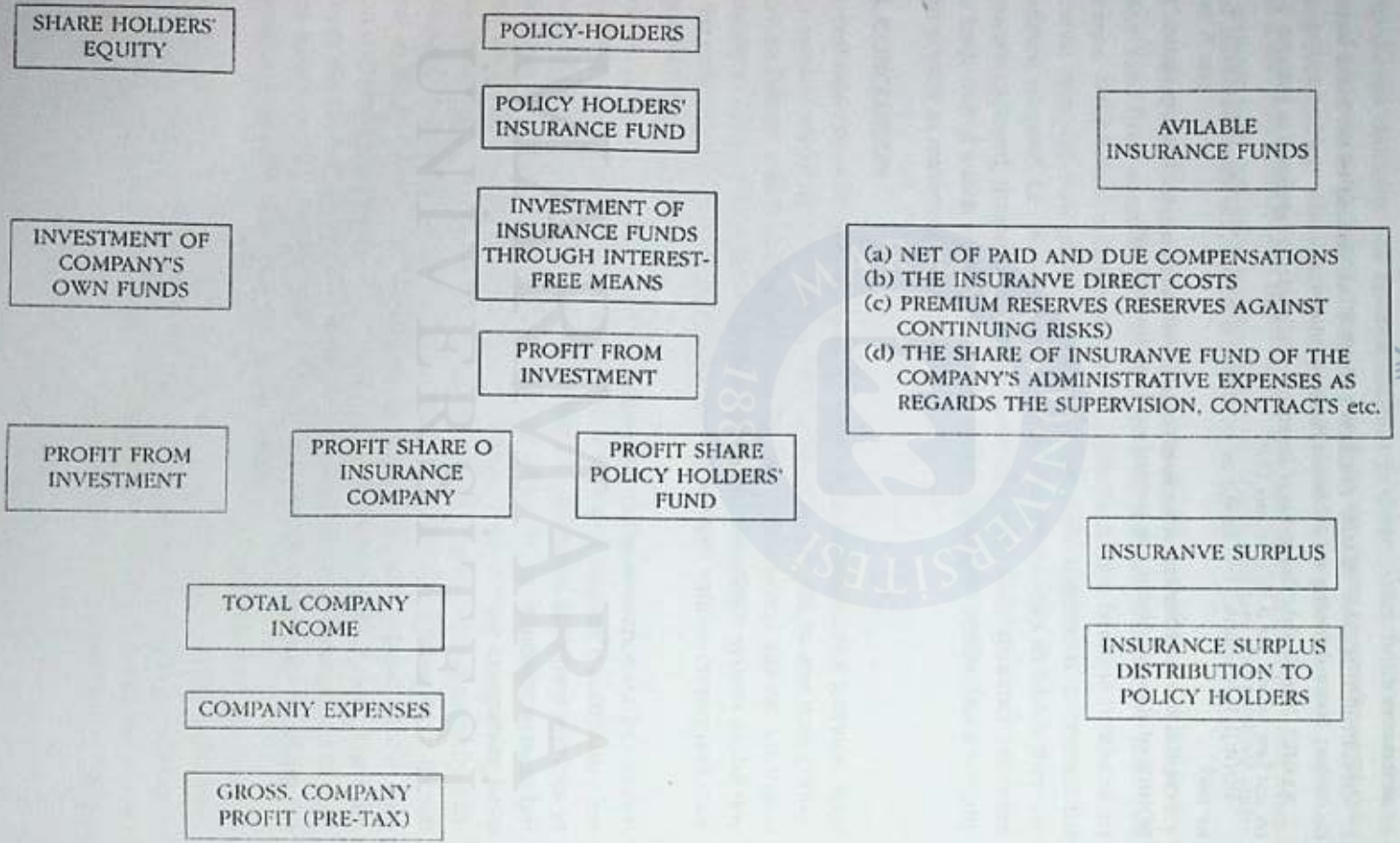
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CO-OPERATIVE INSURANCE



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ECONOMIC GROWTH AND STABILITY IN ISLAMIC FRAMEWORK

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The description of a complete Islamic economic framework and analysis of the stability and growth aspects of an economy within this framework is not a simple task. At this stage only the following question is being addressed to:

If interest is eliminated from the economy (because it has been categorical forbidden in Islam) and is replaced by an Islamic alternative then what will possibly be the implications on growth and stability of an economy?

Of course, elimination of interest is not the sole factor that would Islamize an economy but it is still important to study the impact of this elimination only as most of the conventional economic analysis and discussion on growth and stability centres around interest rate. Once the effect of elimination of interest has been crystallized, the introduction of other elements of Islamic economic system will be simple from the point of view of studying their impact on growth and stability.

Even with this simplification there still remains a big question and that is, what Islamic alternatives we can introduce as a replacement of interest. One very simplest view based on the practice of existing Islamic banks can be that we can take the mark up based financial system as an alternative to interest. Islamic economists, however, are critical of this approach on the ground that this will not reflect the true spirit of Islamic economic system and would simply be an instrument to bring the interest from back door and hence nothing will change in the economy. Islamic economists believe that a true Islamic alternative to interest would be the introduction of profit-loss sharing based financial system in the banking system in which any loan will always be free of interest and any financing will

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have to be based on the concept of Profit-Loss Sharing. This paper will, therefore, only be considering the growth and stability effects of introducing Profit-Loss based sharing system in place of interest based financial system.

The growth and stability analysis of an economy requires the development of an appropriate macro-economic model which too is not a simple task. This paper will attempt to present only a simple macro economic model to point out the growth and stability effects of introducing Profit-Loss sharing based system.

Before discussing the growth and stability effects in the framework of an Islamic macro- economic model, let us have an over-view of the broad features of profit-loss sharing system from the point of view of growth and stability.

Growth

Growth in economy will fundamentally come from growth in the endowment of the factors of production i.e. land, labour, capital and enterpreneurship and or from their improved productivity. Assuming that changing the financial system will not have a direct and immediate implication on the labour supply and the land available in the economy, we will, therefore, restrict our analysis to the effect of introduction of Profit-Loss Sharing (PLS) based system on the two factors; namely capital and entrepreneurship only. As regards capital, the basic question that needs to be asked, would be whether introduction of PLS system will increase or decrease investment activities in the economy. The contemporary literature on this have discussed two types of arguments. One line of argument is that since there is no interest in the economy, therefore, investment can be made until marginal productivity of interest becomes zero whereas in the interest based system the investment will have to be stopped where marginal productivity of investment becomes equal to interest rate. Hence, the investment level in Islamic economy will be higher than in the interest based system. The other line of argument is that investment level under the PLS System will decline because Profit-Loss Sharing system will involve an extra-cost for the owner of capital because of the asymmetry of information with respect to the productivity of enterprises. Capital owner will have to incur extra cost in order to monitor and acquire information about the profitability of enterprise where they have invested their capital and this extra cost being a deadweight loss will imply reduced investment activities.

Both the arguments are in fact incorrect. This is not correct to assume that in the absence of interest, investment can be made until the marginal productivity of investment becomes zero. No economy has abundance of capital. Capital is always scarce and there will always be an opportunity cost for capital and investment will be made only to the level where the marginal productivity of invest-

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ment becomes equal to this opportunity cost. Whether opportunity cost of capital at a particular point of time was equal or not to the interest is an empirical question and the answer will determine whether not investment level be same, higher or lower if PLS is introduced at that particular point.

Similarly, it is also not correct to say that the PLS system involves extra information cost which is a deadweight loss. Extra information cost will be incurred to identify the efficient and profitable and reliable projects which in turn will result into a higher rate of return for capital owners because he will be getting the return on the basis of share in the profit. The fact that capital owner will be monitoring the efficiency, profitability and reliability of the enterprise which will be contributing to the efficiency of the entrepreneur means that the information cost cannot be simply a deadweight loss. It will be rather a positive contribution to the economy and hence will have a positive impact on investment.

After the introduction of PLS in the financial system the Islamic Banks will be obtaining a share in profit of their clients on their asset side. They will not be taking fixed rate of interest from their clients. Everybody knows that profits are higher than the rate of interest because they include a premium for risk also, therefore sharing the profit may end up giving the banks a higher return. Since the banks have to share their profits with the depositors according to pre-agreed ratio and the bank's profit are likely to be higher than the rate of interest, the depositors will also end up getting a higher return on their deposits. That is what is in the theory. What will be in actual practice that depends on how efficiently the Islamic banks operate or what is the actual situation. In theory, however, we have reasons to believe that the rate of return on deposits given to the depositors may be higher than the interest rate. If that is the case then, of course, the supply of investible funds would be higher than as compared to what it would be under the interest based system. On the demand side, since the banks would be providing financing on the basis of the profit and loss sharing, the fact that the banks are willing to share the losses will motivate several potential investors to come forward. Previously when they were supposed to pay only a fixed rate of interest, many potential investors fearing that they may not be able to make profit higher than rate of interest would not come to the Bank. They will just stay away. Many potential investors who were shy in the interest based system to go to the banks will now be motivated because of the profit loss sharing phenomena. Hence there will be higher demand for investment.

The conclusion is, there will be higher demand for investment, there will be a higher supply for investment and the equilibrium level is likely to occur at a rate of return higher than the interest rate.

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This was with respect to the effect on introducing PLS system on the capital formation in the economy. What about the other factor involved in growth i.e. entrepreneur. How does elimination of interest affect this factor? Entrepreneurs are the human beings who organize the other factors of production to make more production and bear risk in this process. This risk bearing aspect is what makes one an entrepreneur. The entrepreneurs can not organize production out of nothing. They need some capital to hire different factors of production. When they use the capital they of course take risk because this capital may be lost in the process. Entrepreneurs who do not have their own capital will have to find out capital from someone else to take this risk. But if this capital is available on the condition that he will have to return it in full plus a fixed interest on it, many of the entrepreneurs would like to shy away because they do not have means to guarantee the repayment of capital with interest. Many people despite having potential would like to be away from entrepreneurial activities and would rather like to look for a wage paid job. If the capital becomes available to the people only on the basis of profit & loss sharing, then several people who were potentially very good entrepreneurs but did not have the capacity to bear the risk will now be willing to come forward and take up entrepreneurial jobs. The new entrepreneurs will emerge. The role of entrepreneurship in the economy will increase and we will have a solid reason to believe that the supply and demand of the fourth factor of production, i.e. entrepreneur, will definitely be at a higher level in an Islamic economy than what it will be in an un-Islamic economy or in interest based economy. This possibility of increase in a factor of production which is an important factor for growth, of course, gives a lot of hope for growth in an Islamic economy.

Stability

Regarding stability in the economy, again we ask the question that when we eliminate interest rate and instead introduce profit-loss sharing system, what do we lose that will affect the stability? What was there in the interest based system that will not be available now to us and will cause instability in the economy? The argument that is given in this respective is the following:

In a system with fixed interest rate, investors know what is the cost of capital and hence they can take appropriate investment decisions. When we eliminate the interest then investment decisions will have to be made on the basis of uncertain profit and this will lead investors to make wrong decisions. The fluctuation in rates of return will change costs of capital. The people who invested on the basis of an expectation will realize their mistakes when they see the actual return and will come back and withdraw their investment and this will create instability.

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Such an argument certainly does not have a sound basis. When people invest, they don't invest on the basis of interest. Interest does not lead people to decide how much to invest. If I have a lot of money and if I want to invest, it is not interest that I will look at it, the first thing that I will look at is the project that is available to me. How much rate of return it has. Interest can only lead me not to invest, but it can not force me to invest. Investment will always be on the basis of the rate of return that I am seeing in a certain project. Even in the interest based system investment decision are always made on the basis of expected rates of return. Absence of interest will hardly make any difference with respect to stability in investment. On the contrary it is the presence of interest that creates instability in the investment as discussed at length in economic literature.

A second argument in an interest-based system is that the policy makers have interest rate as a policy variable in their control to keep the economy stable. They can always manipulate this policy varitable if there are any shocks in the economy, in order to bring back the economy to the equilibrium path. Government, for example can increase the bank rate to deduce the investment demand and vice versa. With the elimination of interest it is apprehended that Goverment will lose this policy variable. This is not the case with the replacement of interest rate by profit-loss sharing based financial system. The profit sharing ratio of the banks with the depositors and the profit sharing ratios of the banks with their clients on assets side have been shown to serve as an effective policy variable. It has been shown rigorously that this policy variable is more effective than the interest rate.

An interesting argument made in the literature in favour of the stability aspect of Islamic Banking is the following:

On its liability side, a bank is obliged to guarantee principal as well as a certain fixed rate of interest. On the other hand, Bank is vulnerable on its asset side. Any shock on the asset side e.g. failure of the businesses where bank has invested, puts the bank in critical situation. Its liabilities do not much the assets. Any effort to stop paying depositors or delaying the payment to the depositors on such an account will make the depositors panicky which will further add to the troubles of the banks. Several hundreds of banks are reported to have collapsed on this ground. It was pointed out in the literature that this failure of the banks is because their liabilities are fixed but their assets are not. In order to remedy the situation, a scheme of deposit insurance was introduced. But recent failures of several banks indicates that even this did not contribute much towards stability of a bank. A paper on this subject was published in the IMF Journal showing that Islamic system maintains through the profit-loss sharing mechanism a balance bet-

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ween the liabilities and assets of the banks. If the assets of the bank decline the liabilities to the depositors also decline to the same extent because Bank is committed to share the profit-loss with the depositors. This makes the banking system more stable.

Coming to another aspect of stability i.e. inflation we again ask the same question, what element of the profit-loss sharing system will make the economy more inflationary compared to the interest based system. We cannot find any argument that the profit & loss sharing system will create inflation, and interest based system willnot. On the contrary we can give several arguments which will prove that profit and loss sharing system will reduce inflation. One basic argument is that under profit-loss sharing system there will be no loans but investments only. This will discourage consumption and promote investment. Banks will be discouraged to give loans for consumption purposes because banks will not be able to share the profit with them. There is no profit calculation in consumption and hence, they will either depend on mark-up based financing which gives low return and which also requires them to be involved in trading or they will have to depend on leasing which will be costly business for the bank because they have to own and maintain the asset. The general consumption loans are expected to decline. When general consumption loans decline, and investments increase instead, then of course this has a negative effect on inflation. In the profit-loss sharing system most often financing from the banks will be taken for productive purposes because banks have to share the profit. The bank financing will mostly create production which will lead to an increase in supply of goods and services which in turn will absorb the demand rather than create any inflationary pressures. Hence there are reasons to believe that introduction of profit-loss sharing system will have a dampening effect on inflation, but there is no reason to say that introduction of PLS system, profit-loss sharing system will increase the inflationary pressure in the economy.

With this general discussion on growth and stability aspects of introducing profit-loss sharing system, we can turn to a more rigorous analysis of these aspects in the framework of a macro economic model for the economy as whole.

Several attempts have been made to develop macro economic models for an Islamic economy. These models usually, being income determination models, have been developed primarily to study the stability aspect of an Islamic economy like any macro economic model developed in the secular framework. No attempt has been made so far to describe the macro economic framework of an Islamic economy in the context of growth and development. In the secular framework, we do find macro models related with growth through the concept of full emp-

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loyment equilibrium suggesting that manipulation of aggregate demand may improve fuller utilization of productive capacity and hence generate growth in the economy. Also, Leif Johansen discussed the macro economic framework in relation to growth in the economy by explaining the price impact in the model and hence showing that casual demand encourages growth by increasing the profitability implicit in the rise in price level. Such an attempt for economic development in general for an Islamic economy in particular , though very much needed, has not yet been made.

The secular attempts referred to above related macro economic models to growth through manipulation of aggregated demand. I feel that an Islamic economy will potentially have a macro model where development can be manipulated through supply side.

In one of my earlier papers relating to Development Strategy in an Islamic framework (7) it was emphasized that growth in Islamic economy can be manipulated through supply side by mobilizing human resources through the peculiar nature of Islamic financial system. No formal macro model, however was presented in this respect. In the present paper I want to develop a macro model to show that the Islamic Financial System generates an implicit macro framework that leads the economy to full employment and then continues it towards further growth and development. The paper will utilize the conventional ISLM Framework to link a simple income determination model to growth in the economy. The ISLM Framework will be developed under the assumptions of Islamic economy. The ISLM framework will particularly highlight the investment function in Islamic economy and money demand functions and then will link this framework to the process of economic development in the economy.

The Model

We assume an economy with unemployed resources so that supply of output is perfectly or almost perfectly elastic and all prices remain constant. The aggregate supply curve for output is horizontal and so is the labor supply curve (at least a very big chunk of the total labor stock).

We assume an Arthur Lewis type economy.[1] There is surplus labor available with an almost infinitely elastic supply at a constant wage,[2] say W.

An economically active population can be divided into two categories, (a) those who work as what we may call entrepreneurs (working for themselves to earn a profit and not earning a wage or salary), and (b) those who work as what we call labor (working for someone else). We thus write Human Resource equation as:

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Where

H = E+L

H = is stock of economically active human resources,

E = is that part of human resource that is active as entrepreneurs,[4] i.e. working for (uncertain) profits,

L = includes all those who are either working for someone else for wages in a modern sector or are disguised unemployed in the subsistence sector.

L has two types of labor (a) those employed in the modern sector (call this labor as L_1) and (b) those employed in subsistence or traditional sector (call this labor as L_2). Bulk of L_2 is disguised unemployed in the sense that their removal form the traditional sector is possible without affecting the output of the traditional sector.

The output that L_2 shares in the traditional sector is sort of average product in the sector. This average product determines a floor for the minimum wage that L_1 will demand in the modern sector.[4] We may call this W which is assumed to remain constant as long as there is a surplus stock of labor in the traditional sector.

The employment of labor in the modern sector (L_1) is generated by the demand for labor from the entrepreneurs (E) which, in turn, depends on the following:

i) Marginal productivity of labor

ii) Reservation wage W referred to above

The employment of human resources (H) into E depends on the following:

a) Opportunities for the human resources to avail to work for themselves;

b) Expected profits (P) from entrepreneurial activities;

c) Availability of the capital requirement for the activity;

d) Willingness and ability of human resources to avail of an entrepreneurial opportunity yielding a certain expected return (P) by beating certain risks.

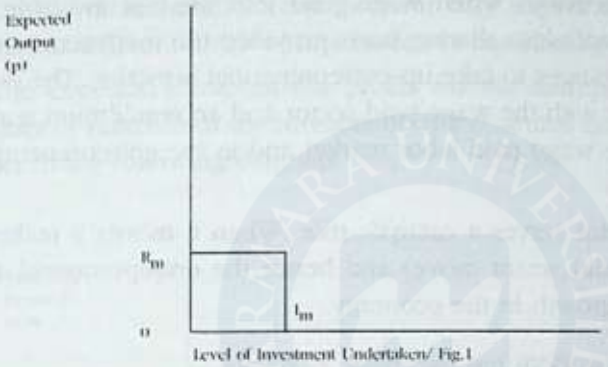
Since W is assured in the subsistence sector to all the population, the human resources will take up entrepreneurial work only if it ensures a certain minimum expected profit (P) for them. The reservation for expected profits is a function of W.

$$P = F(W) \qquad (2)$$

Expected profits (P) from possible entrepreneurial opportunities motivate resources to organize profitable enterprise. Such enterprises once initiated may also generate demand for labor (L).

There may also be a minimum capital requirement to generate a minimum reservation of expected P desired by the entrepreneurs. However, the more capital is available to an entrepreneur, the more profits (P) he expects to make.

A typical entrepreneur may perceive a potential entrepreneurial activity as below:



R_m = Minimum expected output that may motivate a typical human resource to take up an entrepreneurial activity.

I^m = Minimum level of investment required to generate R profit in the activity.

The curve implies diminishing marginal output on investments as more and more funds are used by the same entrepreneur.

We further assume the following:

a) Savers and entrepreneurs are different agents. Savers are owners and Suppliers of investible funds and entrepreneurs are users of these funds.

b) There is no cost charged or profits made by institutions for financial intermediation. (This is only for simplifying the analysis. The assumption can be withdrawn without affecting conclusions).

c) There are no funds available on an interest-basis.

d) Owners of funds can supply funds to the entrepreneurial human resources only on a profit/loss sharing basis. Under this arrangement owners of funds agree to share the actual profits according to a pre-agreed ratio and to share the losses (if any) in the proportion of their funds in the total investment of the enterprise. If the entrepreneur has no investment of his own, all losses will have to be borne by the supplier of the funds).

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e) There is a tax (Z) on the ownership of money balances or all such assets that are susceptible for investment or are susceptible to growth or generating income. The tax is exempted in initial stages of development if it is given as a loan to a potential or a low income earning entrepreneur. (As an economy grows even the loans to entrepreneurs may become taxable).

f) Growth in GNP comes by mobilizing human resources by motivating them to take entrepreneurial activities when wage paid jobs are not available. The supply of finance on a profit-loss sharing basis provided the motivation and incentive to the human resources to take up entrepreneurial activities. The entrepreneurial sector competes with the wage paid sector and an equilibrium is simultaneously achieved in the wage paid labor market and in the entrepreneurial labor market.

g) Entrepreneurial sector serves a catalytic role. When it moves it makes the other sector (the wage paid sector move) and hence the entrepreneurial sector plays a catalytic role for growth in the economy.

This model of growth in GNP has two basic elements:

- There is no interest in the economy.
- All finances/investments are available on profit-loss sharing system.

What type of macro framework will result in the economy if the above strategy is to be implemented and what implications will such a framework have for growth to be discussed in the rest of the paper?

The above mentioned elements are primarily expected to affect investment demand and money demand. The reformulation of macro framework, therefore, concentrates on reformulation of these two sectors only.

Investment Demand

Determination of Profit-Sharing Ratio and Demand for Funds at Micro Level.

An entrepreneur, intending to avail himself of a particular entrepreneurial opportunity, generates demand for investible funds. The effective demand of the entrepreneur for investment funds depends on expected profits (P) that the entrepreneur can earn from the potential entrepreneurial activity. This P, in turn, depends on:

- Total profits (R) expected from the entrepreneurial activity.
- Share in the profits claimed by the owner of funds.

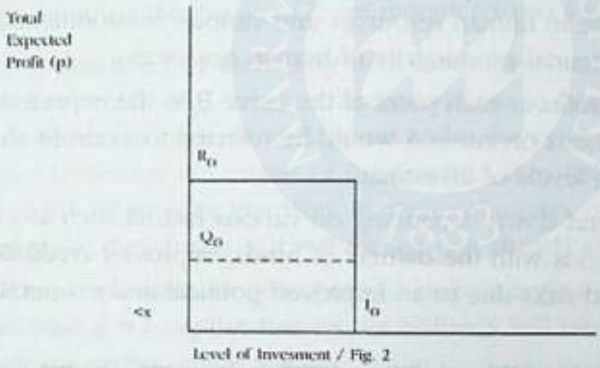
The profits that the supplier of funds will expect to receive on his investment may increase at a constant rate implying a constant expected rate of return on his

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funds or it may increase at an increasing rate because the risk may increase for the supplier of funds as he supplies more and more funds to the same entrepreneur. There may be a limit beyond which the supplier of funds may not be willing to supply the funds irrespective of the expected profits. This limit may depend on various factors including the human capital of the entrepreneur seeking the funds.[5]

On the other hand, an entrepreneur may expect certain profits from his enterprise at different levels of investment as has already been shown in Figure (1).

The expectations about the profits for the entrepreneur, as well as for the supplier of funds from the investment in a potential enterprise, can be shown together in the following diagram:



Curve A shows the total expected profits that the entrepreneur expects to make from his enterprise with different levels of investment.

Curve B shows the expected profits that supplier of funds wants to claim for his investment in the enterprise.

The entrepreneur will effectively demand that amount of investment funds which leaves him the maximum expected profit after paying the share of the supplier of funds. In the above diagram the effective demand would be I_0. At this level of investment, the enterprise is expected to make a total profit P_0 out of which supplier of funds expects to claim Q_0. The ratio of Q_0 to R_0 at I_0 os a_0. This is an optimum point for both the parties and becomes a basis for entering into a mutual contract. The contract between the parties will then be made to include the following:

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1. Supplier of funds will supply an amount of I_0 to the entrepreneur to invest.

2. Supplier of funds shares in the actual profits. Share of the supplier of funds in the actual profits of the enterprise will be determined according to the pre-agreed ratio a_0.

3. If entrepreneur has made no investment of his own, all losses will be adjusted against the investment made by the supplier of funds.

Investment Demand Function at Micro Level

The 'a' - value is agreed upon ex-ante and determines the planned level of investment. The changes in 'a' will affect the effective demand of investment funds from the entrepreneur. The changes in 'a' may occur as a result of shifts in A or B or both.

Curve A may shift up or down depending on the shifts in the level of human capital, technology available to human resources and various environmental factors affecting the entrepreneurial productivity of human resources.

The ratio of expected profits at each point of the curve B to the expected profits at the corresponding points on curve A would be referred to as profit-sharing ratio for the corresponding levels of investment.

Curve B may shift up and down depending on various factors such as availability of more investible funds with the owners of funds, improved credibility of the users of funds, reduced risks due to an improved political and economic climate etc.

An upward shift in Curve A (other things remaining the same) means reduction in 'a' as the ratio to Q_0/R_0 goes down at all levels of investment. This may lead to an increase in the entrepreneurs effective demand for investment funds.

An upward shift in Curve B, on the other hand, means an increase in 'a' at all levels of investment and hence may lead the entrepreneur to reduce its effective demand for investment. It should be noted that Curve A and Curve B are determined independently of each other.

The equilibrium point for an entrepreneur to enter into a contract with the owner of the funds will occur when the marginal productivity of investment in the enterprise becomes equal to incremental increase in the expected profits claimed by the owner of the funds. (For further elaboration see Appendix).

We thus draw the conclusion that the entrepreneurial demand for investible funds will be negatively related to the profit-sharing ratio 'a'. This relationship, we may express as:

$$I = F(a) \qquad Fa < 0 \qquad (3)$$

This will be referred to as investment demand function.

'a' varies between 0 and 1. It is possible for 'a' to become zero.

When 'a' = 0 implies hat the owner of funds supplies his funds to the entrepreneur with no share in profit. This also implies that he will also not share or bear any losses and the entrepreneur is obliged to return the full amount at sometime in future. The possibility that the owner of funds may supply their funds at a = 0 may occur due to several reasons.

1. Expected profits are too low and risk of loss is considered too high to be compensated by the share in the expected profits.

2. The action of helping a poor entrepreneur and allowing him to keep all the profits till his enterprise is developed to the extent that it can afford paying a share in the profit.

3. Avoiding the penalty (Z) on money balances as already mentioned.

It is possible that there may be a lower limit on 'a' which we may refer to as 'a' below which 'a_m' may not decline except to become zero. This will happen when optimum value of 'a' happens to be the value that generates such low expected return for the owner of funds which they find not worth accepting because of the larger risks involved. In such a situation, owners of funds rather prefer to advance their funds at a = 0 for reasons already explained.

It is not possible for 'a' to become unity though it may approach to unity. This is because a = I implies that owner of funds will take all the profits that the entrepreneur makes which will not be a rational situation from the entrepreneur's point of view and hence he may cease to effectively demand any amount of investible funds. 'a' may be approaching to unity if R is very large and/or supply of investible funds is very scarce.

Investment Funds Market: Macro Perspective

At this state, it is important to recognize that the economy may have projects of varying degrees of risk. On the other hand, economy may also have fund owners with varying degrees of risk aversion. In other words, there will be 'n' sets of projects having different levels of riskiness ∂_i, ∂_2 ..... ∂_n. The demand for these sets of projects and supply of funds available for each set of project determines respective equilibrium level of 'a' for each set of project. In the economy thus, there will be 'n' sets of 'a'. To keep the analysis simple, we assume homogeneity with respect to the riskiness and hence we get rid of the third dimension to reflect ∂_i.

We assume large number of entrepreneurs and large number of suppliers of

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funds. An entrepreneur chooses a supplier whose return-risk preferences (Curve B) enable him to agree upon an optimum value of 'a' yielding him maximum expected profit (P).

In this process of search, it is possible to enter into a contract jointly with more than one suppliers, in order to arrive at optimum investment-profit-sharing-ratio package. We will, therefore, refer to the supply of investible funds in terms of units of investment funds (rather than owner of investment funds) available at different levels of 'a'. At macro level, curve B thus is replaced by an upward supply curve as shown below:

On the other hand, the available investment funds look for more productive



Supply of Units of Investment Funds / Şekil 5

entrepreneurs so that they are able to claim more profit. The most productive entrepreneur believed to be generating the highest return (R) at all levels of investment would be chosen first. At this stage, we may not distinguish between entrepreneur and enterprise. In the presence of surplus stock of human resources, we assume that each entrepreneur represents a single enterprise. Nence, we need not distinguish between profitability of an enterprise and productivity of an entrepreneur. Competitive conditions can be assumed to ensure that profitability of enterprises is equalized over all enterprises in the economy. The investment funds market, thus, will determine three things:

i) Profitability of marginal enterprise in the economy (R);

ii) Investment level in the economy (I);

iii) Profit-sharing ratio (a) for the owner of the investment funds.

Because of the assumption of large numbers of enterprises/entrepreneurs in the economy, we can also assume that the profitability (R) of the enterprises in

the economy at the margin will not be affected by the changes in the level of investment (I) and profit-sharing ratio (a).

Hence at macro level, while the investment will continue to be negatively related to the 'a'-value, as shown in equation (3) the (total) profits per enterprise (R) will remain fixed in the background in a short run perspective.

Goods Market Equilibrium

Let us take the simplest model of goods market:

$Y = C+I+G$ (4)

C = Private Consumption

I = Investment Demand

G = Government Expenditure

Y = Aggregate Demand (Equal to Aggregate Supply)

$C = b_0 + b(1-t)Y$ (5)

$I = i_0 - ia$

G = G (Exogenously given) (6)

$Y = A_0 - A_1 a$ (7)

Where $A_0 = b_0 + i_0 + G/1-6(1-t)$

$A_1 = i/1-b(1-t)$

Equation (7) shows a negative relationship between 'a' and Y. This is an IS curve in our framework with positive slope.

Money Demand

Money Demand Function

Demand for real money balances will depend on the level of real income and the expected return on financial assets.

It depends on the level of real income because individuals hold money to finance their expenditures which in turn depend on their income.

$L = by$ (8A)

The demand for money depends also on the expected return on financial assets. The higher the expected return on the financial assets the less worthy it is to hold money.

This part of the demand for money may not be directed at speculative demand for money. This part of demand for money, in an Islamic environment has the following elements.

Besides the transaction demand for money, there is a demand for meeting the

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short term borrowing needs of others. With the importance attached to Qard-ul-Hasan and with the embarrassment attached with not helping a brother in need, the Islamic environment would require every one to keep some cash for meeting the short-term borrowing needs of others. The money necessary for such situation, however, will depend on cost of holding money which of course is the expected rate of return on investment. The lower the rate of return the higher the demand for this purpose. The demand for money motivated by altruistic considerations in fact, will be a function of both income (Y) and rate of return (Q). While it will be positively related to Y, it will be negatively related to Q. This part of the demand for money for some cash for altruistic purposes can be written as:

$$A = a_2 Y - hQ \qquad (8B)$$

The equations (8A) and (8B) can be combined to write:

$$LA = ky - hQ \qquad (8)$$

As far as speculative demand for money is concerned, theoretically it can exist on the same based economy. The expected rate of return will be more volatile than the fixed interest rate and hence increase the urge to speculate. Though speculation will always be on an expected rate of return but it can always be translated into the profit-sharing ratio prevailing in the market. Thus, the higher the profit-sharing ratio the lower will be the speculative demand for money and vice versa.

There is generally an impression given by Islamic economists that speculative demand for money cannot exist in an Islamic economy because of the prohibition on gambling.

Since there will be a natural urge to hold money in periods of low expected returns in order to be able to invest in periods of high expected returns and since such an urge cannot be institutionally controllable, some speculative demand for money is inevitable. It can, however, be said that the speculative demand for money will be shadowed by the altruistic demand for money. In periods of low expected return on investment the urge to hold money for altruistic purposes will be more than in periods of high expected return. There is some institutional control on speculative demand for money in the form of zakah. That will only reinforce the altruistic motive for holding money. The speculative motive will, therefore, still keep the form of demand function the same as shown in equation (8).

Hence, the demand for real money balances increases with the level of real income and decreases with the expected rate of return on financial assets. We can write demand for money function as:

$$LA = KY - hQ,\ k > o;\ h > o \qquad (8)$$

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L = Demand for money

Q = Expected profits on financial assets for the owner of the asset

But we know that Q = aR.

Since R is exogenously given to money holders as far as money demand is concerned, we can write equation (8) as:

$$LA = kY\text{-}haR$$

$$\text{or } LA = kY - h'a \qquad (9)$$

where $h' = hR$

Money Market Equilibrium

Assuming a fixed money supply (M) and a constant price level (P) implying fixed real money balances M/P we write money market equilibrium as:

$$kY - h'a - M/P \qquad (10)$$

This gives a relationship between a and Y as below:

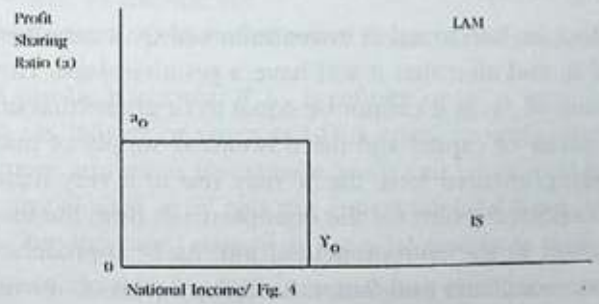
$$a - 1/h' (ky - M/P) \qquad (11)$$

This is the equation which will be referred to LAM curve in order to distinguish it from the LM curve that represents interest-based speculative demand for liquidity. LAM curve is based on the demand for liquidity that is motivated by profit-cum-altruistic considerations.

Income Determination - 'ISLAM' Framework

IS and LAM curves determine equilibrium level of income as usual except that we have profit-sharing ratio (a) instead of interest as shown below:

Slope of LAM Curve



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LAM curve is represented by the equation.

LAM - I/h' (kY - M/P) (12)

Is there a vertical section in the LM curve?

The answer depends on whether 'h' can be zero i.e. whether demand for money can be insensitive to changes in 'a'. (Equation for money demand being M = kY - h'a). 'a' may cease to have any effect on demand for money when Q (the expected rate of return for the owners of the financial assets) is very low. At very low Q, the owners of financial assets may not prefer to invest at positive 'a' as a matter of risk aversion. Positive 'a' means also the responsibility to bear the losses. The low Q may not tempt the financial assets owner to bear the responsibility of loss implied in this Q. On the other hand there is a cost in holding money. The holders pay Z on the amount held. In such a situation where holders of money do not like to invest on a profit/loss sharing basis and also want to avoid the penalty Z, they may prefer to lend the money to those who need it. Money lent, in our framework, does not share any profit and is liable to be returned in full at some future date. This may also be referred to as investment with a = O (i.e. neither earning any profits nor bearing any losses).

The money demanded will remain insensitive to 'a' until Q reaches a certain level (Q) beyond which owners of financial assets become responsive to changes in 'a'. With R (expected total return on investment) as given, this implies, that there is a corresponding 'a' as well below which h'a is zero. Hence it is possible to have a vertical section below a certain a. There may not be any vertical section, if R is not low.

Is there a horizontal section in LAM curve? The answer depends on whether it is possible for money demand and financial assets to be perfect substitutes of each other. In terms of lower Q, we have already discussed that it is not possible that any addition to money supply may add to the money demand because of the existence of a cost (Z) of holding money.

Thus, the LAM curve cannot be horizontal at lower values of Q. It may be vertical up to a certain level of' a' and after that it will have a positive slope. However, there is a limit to the value of ,'a' as it cannot be equal to or greaterthat unity. If R is very high, there is scarcity of capital and there is excess supply of human resources willing to take entrepreneurial jobs, the 'a' may rise to a very high level, still leaving enough P (expected return for the entrepreneurs from the investment) to induce him to remain in the entrepreneurial job. As b' approaches to unity, the LAM curve will become flatter and flatter. At higher levels of 'a' with R being very high, Q will also become very high which enables the entrepreneur to

demand more money as they can afford to pay Z on their money balances out of the Q earned on the finances already invested. Hence the bulk of any addition to the money supply at this stage may simply add up to the money demand. The horizontal section of LAM curve is possible at very high (close to unity) level of 'a' values. Such a horizontal section may not occur at a very low level of R may mean P to be less than P_m (a thousand point of entrepreneurial human resources to remain in entrepreneurial jobs).

Thus, we may observe two extreme positions as below:

1. When Q is very low due to lower values of R, LAM curve may be vertical below a certain level of 'a'.

2. When Q is high because of higher R, LAM curve will be horizontal as 'a' approaches to unity.

In between these two extreme situations, the slope of LAM curve will depend on the slope of money functions which is an empirical question.

In this framework, it is important to recognize that the slope of LAM curve will be different at different stages of economic development. Whereas the vertical LM curve will occur at initial stages of development, the horizontal section of the curve may occur at advanced stages of economic development.

Slope of the IS Curve

Can the IS curve have any horizontal section?
To see this we reconsider the IS equation viz:

$$Y = A_0 - A, a \qquad (12)$$

or $$a = A - A' Y \qquad (13)$$

where $$A' - 1 - b (1-t) / i \qquad (14)$$

b = Marginal propensity to consume
t = Rate of income tax
i = Responsiveness of effective demand of investment funds to the profit ratio

IS can be horizontal if A_1 is infinity or 'A' is zero. This can be possible either when i is infinity or when b(1-t) is equal to unity. For i to be infinite, it implies that more and more investment funds can be offered by the owner of funds without any change in 'a' and the entrepreneurial human resources are available to utilize the increased supply of financial resources without a change in 'i'.

For b(1-t) to be equal to unity implies that there are no taxes on income and the marginal propensity to consume is equal to unity. Let us consider under what

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circumstances any of these two conditions may hold good.

It may be convenient to start by considering investment demand as a function of Q (the expected return on investment to be paid by the entrepreneur to the owner of the funds). We ask the question: Is there any level of Q at which investment may continue to be done without decline in Q? In our framework this can occur as below:

i) For a given R on investment for an entrepreneur there will be a level Q which leaves just that amount of P which is threshold point for human resources to stay in an entrepreneurial job.

ii) There is surplus stock of human resources, which implies an infinitely elastic supply curve of entrepreneurs at P. This surplus stock cannot compete to raise Q because that would mean a return to them below P.

iii) Any additional supply of financial assets in this situation does not have to offer a lower Q to get themselves deployed with an entrepreneur.

iv) Hence investment can continue to take place at Q because of the surplus supply of human resources. It is not necessary that new entrepreneurs always have to come from the surplus stock in the subsistence sector. Labor already employed in the modern sector can take entrepreneurial jobs vacating wage-paid jobs in the modern sector to be filled by the surplus labor in the subsistence sector. The investment function, thus, may have a horizontal section.

Infinitely elastic portion in the investment curve may occur without the presence of the surplus stock of labor. This may occur in a situation where R and P are such that they leave Q which is not acceptable to the owner of funds. Accepting Q (expected return for owners) also means responsibility of bearing the loss, if it should arise. The risks may be too high to be compensated by Q. But owner of investible funds cannot keep the funds idle in view of the existence of the tax Z. An easy alternative to them would be to give their financial resources temporarily to an entrepreneur with 'a' = O which would mean neither sharing the profit nor bearing the losses. Besides avoiding tax Z, the various considerations may also complement the motivation of advancing one's resources on 'a' = O when R, P and Q are too low. These considerations have already been elaborated in section 3.2.

In this case a horizontal section in the investment curve will occur at 'a' = O as shown below:

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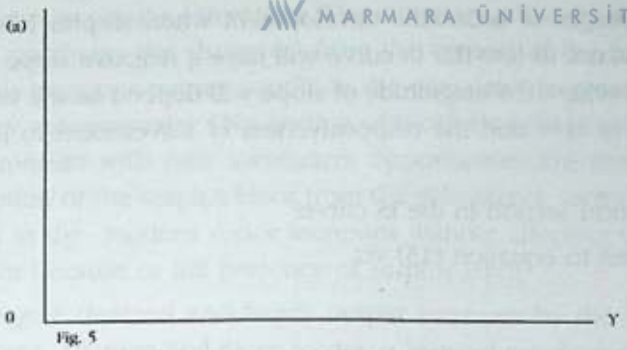
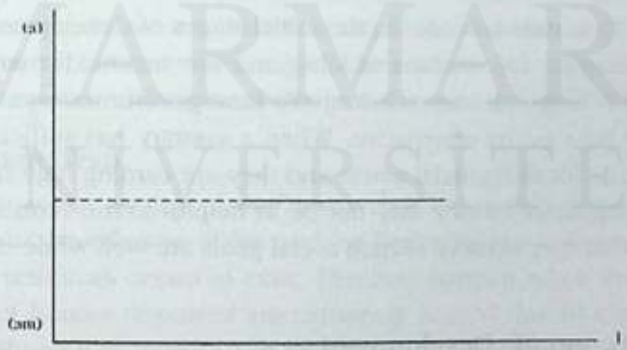


Fig. 5

Now we come to consider the conditions when [1-b (1-l)] may approach to zero and hence may cause IS curve to have a horizontal section. The expression [1-b (1-t)] can approach to zero only if b approaches to unity and t approaches to zero. This can occur, generally, at very low levels of personal income. We can safely say that in the initial stages of development when R is very low [1-b (1-t)] may approach to zero. This is because when R is low, P and Q will also be low and P will not be low if W is not low. Hence low P, Q and W imply low personal incomes in the economy which in turn may make 1-b (1-t) approaching to zero.

The conclusion of all above is that slope of IS curve may be horizontal at some low level of R if the economy is in the initial stages of development.

Since R is given per entrepreneur, the investment function expressed in (a, I) space will be as below:



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This is turn implies that there can be a horizontal section in the IS curve in the initial stages of development when there is surplus stock of human resources and the return on investment is quite low.

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At advanced stages of economic development when surplus labor has been absorbed and R is not to low the IS curve will have a negative slope as shown in the equation (13) where the magnitude of slope will depend on the values of marginal propensity to save and the responsiveness of insvestment to the values of 'a'.

Is there a vertical section in the IS curve?

We again revert to equation (13) viz.

$a = A'Y$

Economic Development and the Macro Framework

Efficacy of Monetary Policy vis-a-vis Fiscal Policy

LAM has been shown to be vertical for having a steep slope when 'a' is wery low and of return (Q and P) are also lower. In such cases, fiscal policy will be ineffective whereas monetary policy will have full impacts on GNP. When returns (Q and P) are higher and 'a' is also closer to unity, the LAM curve has been shown to be flatter. The monetary policy, in this case, will cease to be very effective and government spending (preferably to help improve the productivity of human resources) will produce more effective results on growth and employement.

It means in our framework, the government will have to rely more on monetary policy when the economy is in the initial stages of development. But as the economy grows, goverment may use both policies. Ultimately when the country has sufficiently developed, government may have to rely only on fiscal policy.

This appeals to common sense. In the initial stages of development, (meaning low incomes of capital, low income of labor and low income for entrepreneurs), the lack of taxable capacity may substantially limit government spending. Monetary policy may be a better alternative. When a country has sufficiently developed, people own a lot of financial assets and they are earning high rates of return on them, pumping more money may not be as helpful to the economy as goverment spending that may achieve certain social goals are well while expanding the GNP.

Process of Economic Development

We start with the following situation. The economy is at a very low stage of development. There is a stock of surplus labor. R is very low nd so is W, P and Q. This implies a horizontal IS curve.

Government has to rely on monetary policy. Hence, government decides to increase the money supply. It instructs the monetary authority to purchase go-

vernment shares in private enterprises. The monetary authority selects suitable enterprise and purchases the shares (a) from the owners of the funds of these enterprises. This increases money supply in the economy. Increased money supply looks for new entrepreneurs. (No portion of it can be held because of the tax Z). New entrepreneurs with new investment opportunities are generated, implying some absorption of the surplus labor from the subsistence sector. The output and employment in the modern sector increases without affecting the output of traditional sector because of the presence of surplus labor.

The aggregate demand and hence output increases by the full effect of the new investment. As more and more money is injected not does only employment and output increase but the entrepreneurial productivity improves through learning by doing and through the competition that newly entered entrepreneurs pose to the existing entrepreneurs. In the process R improves. This is in turn raises Q as well as P. This means demand for money goes down. The IS curve becomes horizontal at a higher level of 'a'. The above process continues with IS curve shifting in horizontal jumps till all surplus labor is absorbed. Now R is at a higher level than that from we started and there is no surplus so that 'a' has to be reduced to attract human resources to employ additional supply of investible resources. But reduced h' will also affect money demand. A choice has to be made between monetary policy and fiscal policy depending on which of the two will be more powerful given various parameters. R keeps on improving till we reach a stage where IS curve becomes vertical. Monetary policy loses its significance. Fiscal policy becomes important. Now it is time for government to take up big development projects of its own. This will further increase R forcing 'a' to come down and once again, we are on a downward sloping IS and an upward sloping LAM. The proces continues till a stage comes where the government's role ends up in the economy and self sustaining growth may take place.

Low Income Trap

In the horizontal section of the IS curve, it is possible that even the money supply may not be effective if demand for investible funds from the entrepreneurial human resources ceases to exist. This may happen when the entrepreneurial liabilities of human resources are extremely limited due to extremely bad infrastructure (absence of road etc) or extreme political instability etc.

In such a case, mere injection of money supply may not be enough. It will have to be supplemented by measures conducive to generate entrepreneurial demand for investible resources.

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Footnotes

1. See Arthur Lewis [3]

2. This may be a subsistence wage as assumed Arthur or a Market-cum-reservation wage of labor suplus economy as in Khan's framework (1)

3. This includes self-employed.

4. For further elaboration of this hypothesis see Fahim Khan [1]. The theory basically is that of Arthur Lewis (3)

5. For more discussion, see Khan (2).

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APPENDIX

Demand For Profit Sharing Capital

Consider an entrepreneur demanding capital for an enterprise. With Y as output/ income, K as capital and L as Labor, we write production function as:

$$Y = F(K,L) \qquad (1)$$

Since labor and capital are sharing the income of the project and hence do not impose fixed costs, this production function also represents net income function for the project.

Assuming that the entrepreneur is the only labor in the project and hence the labor component is faked we can write the production function as:

$$Y = F(K) \qquad (2)$$

As a typical production function we assume that this production function has a declining marginal productivity of capital, i. e. $F'(k) > O$, $F''(k) < 0$.

The function, in otther words, has the following form:

On the other hand the provider of capital expects to receive a certain return his capital. The expectted return, of course, will be directly related with the total amount he invests. In the very simplest form, his relationship can be linear relationship of type:

$$C = rK \qquad (3)$$

Where C is total return that the provider of capital expects to earn on his capital K whereas 'r' is based on his own utility function.

In the interest-based framework, the provider of capital demands 'r' from the user of his capital. In the Islamic framework, the provider of capital cannot demand 'r'. It can only fix a share in the income or profit of the project.

Let this share be called 'a'. Since income, i.e. 'y' is not fixed and varies at different levels of K, therefore, the profit-sharing ratio becomes a function of the amount of capital.

Using equation (3) and (2) we can write:

$$a - C/Y - rk / F(K) \qquad (4)$$

This equation shows, that profit-sharing ratio will vary as more capital is invested because C is increasing at a constant rate and Y is increasing at a declining rate.

This fact can be more clearly seen in the following diagram:

The curve A is the production function representing equation (2). The line B

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shows the total return expected by the capital owner at different amounts of capital to be provided by him. This is a straight line representing equation (3).

Two things are clear from Fig (2).

Firstly, the income sharing ratio (a) is different at different levels of (K). The value of (a) can be observed at any level of K as a ratio of the corresponding value at line B to the ratio of the corresponding value at curve A.

It can be noted that beyond a certain level of K, the income sharing ratio starts increasing until it reaches a level equal to I.O. This will occur at KO.

Secondly, it will not be in the interest of the entrepreneur to demand any amount of capital from the capital owner. A profit maximizing entrepreneur will demand only that much capital from the capital owner that will allow him to retain maximum profit. In terms of Figure (2), he would demand that much amount of capital against which the distance between curve A and line B is maximum. (The distance between curve A and Line B measures the income to entrepreneur after paying the share of capital owner from the income of the enterprise).

Hence, the assertion[1] September 11, 1931 that under the profit-sharing system



Fig. 1

there will be infinite demand for capital is not valid per se.

The argument can be taken a step further.

Under a profit-sharing arrangement, the supply schedule for capital funds may not be a linear function as shown by equation (3). Since capital owner bears all losses of an enterprise, a capital owner would not like to give as much capital demanded by the entrepreneur at a constant rate of return 't'. Giving all his money to one entrepreneur would mean putting all his eggs in one basket. He would like to spread his investment among different enterprises unless an entrepreneur is willing to offer a higher than t' return - higher enough to compensate the risk of putting more capital in one enterprise.

Thus a higher supply of capital for the same entrepreneur would mean a higher income- sharing ratio with the same entrepreneur. In other words, we will have to rewrite equation (3) as:

$$C = g(K) \qquad (4)$$

with $g'(K) > O$

$g''(K) > O$

The profit maximizing entrepreneur then faces the following profit function:

$R = Y\text{-}C$

$R = F(K) - g(K)$

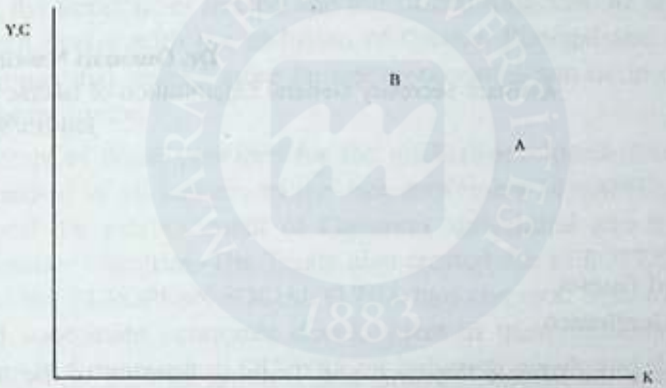


Fig. 2

Optimum demand for capital by entrepreneur will be for that level of K where,

$F'(K) = g'(K)$

1 Several scholars make the assertion that profit-sharing system would mean infinitely elastic demand for investment.

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ISLAMIC COMMON MARKET

Dr. Ousman Nassiru Othman
Assistant Secretary General Organization of Islamic Conferance
Jeddah/Saudi Arabia

Excellencies,
Distinguished Guests,
Ladies and Gentlemen,

I wish to thank the Islamic Research and Training Institute of the Islamic Development Bank as well as the authorities of the Marmara University in Istanbul, for having so kindly invited me as a Guest Speaker during the International Seminar on "Orientation in Islamic Economics"

I have been requested to make a presentation on the theme "Islamic Common Market" and I shall attempt, during this lecture, to address this issue not from a purely academic point of view but from the perspective of the Organization of the Islamic Conference which groups 51 Islamic States to promote and strengthen Islamic solidarity and to consolidate cooperation among Member States in the economic, social, cultural, scientific and other vital field of activities so as to ensure the socio-economic welfare of the more than 1.2 billion Muslims that we now have in the World.

I shall try to be as simple and practical as possible and deal with questions like "what do we mean by an Islamic Common Market, When was an OIC policy on Islamic Common Market formulated, Why is there the desire for an Islamic Common Market, How do we intend to achieve the goal of an Islamic Common Market, What are the constraints and what are the prospects?

WHAT DO WE MEAN BY AN ISLAMIC COMMON MARKET?

Well a "Common Market" can very simply be defined as an area, usually combining a number of countries, in wich all can trade on equal terms. Such a system requires the establishment of a CUSTOMS UNION with a COMMON EXTERNAL TARIFF, the free movement of FACTORS OF PRODUCTION as well as of goods and services and a considerable harmonization of tax and other policies.

Perhaps the best example of a Common Market could be seen in the European Economic Community (now European Union) which was formally established in 1957 by the Treaty of Rome agreed to by the Governments of Belgium, France, the (then) Federal Republic of Germany, Italy, Luxembourg and the Netherlands. By 1973 the number of countries had increased to nine with the joining by Denmark, the Republic of Ireland and the United Kingdom. As of today the number is about twelve with the inclusion of Greece, Portugal and Spain and there are indications that several more European countries will be in the group in the not-too-distant future.

The Treaty of Rome provided for the gradual development of a full Customs Union, removal of all barriers to the free movement of CAPITAL, LABOUR and services and the establishment of Common agricultural and transport policies among Member countries. The Treaty also created the EUROPEAN INVESTMENT BANK and the EUROPEAN SOCIAL FUND, two common institutions designed to assist and coordinate economic development in the community. By 1961, the Community had removed all QUOTAS on industrial goods and the removal of all INTERNAL TARIFFS and the adoption of a COMMON EXTERNAL TARIFF resulted in the establishment of a full CUSTOMS UNION in 1968.

I have cited the case of the European Economic Community to provide an insight as to what we should do or strive to achieve in order to create an Islamic Common Market. If we go by the definition and example I have cited above, an Islamic Common Market will seek to group all Islamic countries, from Africa to the Arab States, to Asia and Central Asia to form an area in which all can trade on equal terms. To do this Islamic countries will have to, at one point, establish a CUSTOM'S UNION to allow free movement of factors of production (that is CAPITAL and MANPOWER) as well as of goods and services and proceed with the harmonization of tax and other policies. This is, in a nutshell, what one will generally have in mind when one talks of an Islamic Common Market.

But is an Islamic Common Market feasible taking into account the geopolitical and socio-cultural difficulties that obtain within the Islamic Community? Before we answer this question we must first look at the formulation of an OIC policy on Islamic Common Market and the reasons which have motivated Islamic leaders in the OIC to "dream" of an Islamic Common Market.

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WHEN WAS AN OIC POLICY ON ISLAMIC COMMON MARKET FORMULATED?

May I remind at this juncture, that the idea of an Islamic Common Market was first mooted in Islamic circles in the early seventies but it was not until 1991 that it became an official OIC policy. In December of that year, during the OIC 6th Summit held in Dakar, Senegal, the Kings and Heads of State and Government of the Organization of the Islamic Conference examined the issue and in their Final Declaration stated and I quote:

"We shall endeavour to reduce or progressively eliminate all kinds of obstacles to the development of Intra-Islamic Trade and to encourage in the future the implementation of the principle of the Most Favoured Nation Clause.

In this regard we shall take appropriate measures to reduce, at all levels tariffs and other barriers and study such other measures which are required to promote intra-Islamic economic and commercial cooperation including the prospects of promoting all forms of economic integration between Member States both at the regional or sub-regional levels leading to the setting-up of an Islamic Common Market"

The Islamic leaders also passed an important RESOLUTION during the SUMMIT in which, inter-alia, they I Ouote "Request the COMCEC (that is the OIC Standing Committee for Economic and Commercial Cooperation) to consider within the framework of its forthcoming review of the strategies and of the Plan of Action on economic cooperation among Member States to study ways and means for the promotion of inter-regional cooperation and progressive economic integration leading to the setting up of an Islamic Common Market taking due account of the existing regional integration groupings working in the same fields" Unquote.

This was the first OIC RESOLUTION calling for the setting up of an Islamic Common Market and has since constituted the main OIC policy decision on this matter.

The Summit resolution was strongly re-echoed by the succeeding Islamic Conference of Foreign Ministers (the 21st ICFM) which was held in Karachi in 1993. In their resolution on the Economic Problems facing the Islamic the Foreign Ministers reiterated "the need for integration among the OIC Member countries with the ultimate objective of establishing an Islamic Common Market and requested the Member States to examine the technical studies already prepared in order to formulate policies towards this end. In this context (the Foreign Ministers) requested Member States to encourage and advance the initiatieves taken by some of them at setting up joint-economic groups at sub-regional level."

These two RESOLUTIONS from the highest organs of the OIC provide guidelines which continue to preoccupy the attention of all the other organs and institutions of the Organization working in the economic field.

WHY AN ISLAMIC COMMON MARKET?

The reason for the clarion call for an Islamic Common Market are contained in the preambular paragraphs of the Resolutions I have just quoted. In the main they centre around the recent changes that have taken place globally and their impacts on developing countries to which category all Islamic countries belong.

As we all know, the overall international economic relations are characterized by inequities which continue to aggravate socio-economic inequalities between developed and developing countries as well as impede all the efforts of the latter for development. Furthermore, the system of global economic relations is undergoing significant changes marked by the continuing recession in the major economies, the process of economic and monetary integration of the European Union, NAFTA and others, the turmoil created by the changes in central and Eastern Europe and the assistance needed by these countries to implement their transformations to market economies, the major trade imbalances, the uncertainties for the developing world of the recently concluded Uruguay Round on Global Trade Liberalization as well as the emerging trends of rising protectionist barriers and greater sub-regional economic cooperation.

The problems of the developing countries including Islamic countries continue to be compounded by a staggering external debt, decline in their terms of trade, the falling prices of commodities and the declining levels of Official Development Assistance (ODA).

In the political field, the global situation is characterized by a strategic cooperation and partnership between the East and the West. In fact our world today, hitherto governed by a bipolar force is leading towards unipolarity. What used to be known as the Soviet Union has disintegrated and disappeared. Ethnic and nationalist sentiments are intensifying, thus exposing the fragility of certain frontiers drawn up in the after-math of the two world wars and at the end of the colonial period. Trends towards political plurality, towards democratic reforms and towards market economy are in evidence.

This state of affairs coupled with the technological revolution which has ushered in tremendous advances in micro-electronics, in biotechnology and renewable energy and which is having a profound effect on international economic relations, is now creating an awareness that most of the developing countries are too small to be able to create modern, viable industrial structures within their national

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frameworks, The high cost of modern industrial establishments cannot be justified where markets are too small.

The state of affairs has also prompted a fundamental examination in many developing countries themselves, of their place individually and collectively in the framework of the emerging configuration of international political and economic power structure.

It is because of this state of affairs, the rapid changes and developments in the international economic arena, that developing countries see the dire need to pool their resources and coordinate their development efforts in a movement toward regional solidarity. It is because of this state of affairs that Islamic countries feel the strong need for an Islamic Common Market.

WHAT ARE OIC's EFFORTS AT ECONOMIC COOPERATION OR RATHER TOWARDS THE ESTABLISHMENT OF AN ISLAMIC COMMON MAKRET?

The multifarious efforts at attaining economic integration among OIC Member countries can be grouped under two main headings, namely:

(a) The Strengthening of Economic Cooperation;

(b) Encouragement of the creation of sub-regional economic groupings.

(a) The Strengthening of Economic Cooperation:

When the Organization of the Islamic Conference was founded in 1969, it was mainly conceived as a political organization whose main objective was to strengthen Islamic solidarity. But even in the early days of its existence, the member countries began to feel the strong need for the establishment, promotion and expansion of economic cooperation among themselves.

In fact, the Charter of the Organization, approved in February 1972 underlined the necessity of cooperation for community-wide economic progress and the need to help the individual Member States develop their productive capacities at an accelerated pace. In this way the stage was set for the OIC to embark on a serious consideration of the economic and social issues facing the OIC member countries.

The objective of such a move was to discover possible areas of cooperation that would bring member states closer together and strengthen them not only in the pursuit of their original and immediate political objectives but also in paving the way for an ultimate economic integration.

Conscious of the fact that multilateral economic cooperation would not only benefit individual member countries but would also go a long way in supporting

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and consolidating the joint political action originally envisaged, Member States of the OIC undertook quick and determined steps to work out the organisational and institutional framework necessary for an intensive form of economic cooperation. Specialized meetings were organized at the experts, senior officials and eventually at Ministerial levels to formulate detailed cooperation ideas and to discuss ways and means of implementing them.

The outcome of all these efforts culminated in an OIC initiative to participate in the world development process in a co-ordinated manner. This initiative consisted in the formulation of a document entitled "Plan of Action to Strengthen Economic Cooperation Among the OIC Member States", The Plan of Action was adopted by the Third Islamic Summit Conference held in Makkah Al-Mukarramah/Taif in January 1981. It is important to observe here that it was during this Conference that the OIC blue-print known as the "Declaration of Makkah Al-Mukarramah" was adopted. The Declaration was built around the basic concept of JOINT ISLAMIC ACTION.

The 1981 PLAN OF ACTION aspiring to consolidate all the OIC economic work to date into an integrated whole, identified TEN MAIN SECTORS for economic cooperation. These were:

- Agricultural Development and Food Security.
- Trade.
- Industrial Development.
- Transport.
- Communications and Tourism.
- Energy.
- Science and Technology.
- Labour and Social Security.
- Health and Population.
- Technical Cooperation.

Later on, during the Fourth Islamic Summit Conference held in Casablanca in January 1984, Six Sectors, among the ten enumerated above, were adopted as PRIORITY AREAS OF COOPERATION. The six sectors were:

- Agricultural Development and Food security;
- Industry.
- Science and Technology.
- Trade.
- Transport and Communications.
- Energy.

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In order to ensure an efficient handling of economic cooperation and an effective coordination and implementation of THE PLAN OF ACTION, two STANDING COMMITTEES were also created by the Third Islamic Summit. They are:

- **The Standing Committee for Economic and Commercial Cooperation (COMCEC),** chaired by the President of the Republic of Turkey.

- **The Standing Committee on Scientific and Technological Cooperation (COMSTECH),** chaired by the the President of Islamic Republic of Pakistan.

These two Standing Committees are being assisted, as implementation agents, by the General Secretariat of the OIC, the Subsidiary Organs (like the Statistical, Economic and Social Research and Training Centre for Islamic Countries - SESRTCIC, the Islamic Centre for Development of Trade ICDT, the Islamic Foundation for Science, Technology and Development (IFSTAD), and the Islamic Centre for Technical and Vocational Training and Research (ICTVTR).

They are also assisted by OIC specialised institutions like the Islamic Development Bank (IDB) and the Islamic Educational, Scientific and Cultural organization (ISESCO). Affiliated institutions like the Islamic Shipowners Association, the Islamic Chamber of Commerce, Industry and Commodity Exchange (ICCICE) and the International Association of Islamic Banks (IAIB) contribute to the implementation process of the Plan of Action.

Together, these Standing Committees and institutions have been making precious contributions towards the implementation of the programmes outlined in the areas of cooperation, especially in the six priority areas of the Plan of Action.

Within the framework of COMCEC, intensive efforts covering various fields of commercial and economic cooperation have been undertaken. In this regard, sectoral meetings at both experts and Ministerial levels have been organised. These meetings dealt with vital common concerns such as food security and agricultural development, industry, transport, communications, energy and trade.

Activities of the COMCEC have given rise to the among Member States, of a number of multilateral agreements to create the necessary legal and institutional framework to help promote and strengthen economic and commercial relations among the Member countries. We have in place, for example, the Agreement on Promotion, Protection and Guarantee of Investments, the General Agreement for Economic, Technical and Commercial Cooperation among Member States and the Framework Agreement on Trade Preferential System among Member States of the OIC. Also, certain schemes designed to promote trade, such as the Longer Term Trade Financing Scheme, the Export Credit Insurance and Guarantee of Invest-

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ment Scheme and the Multilateral Clearing Union have been established or are in the pipeline.

Significant progress has also been made towards the establishment of an Islamic Telecommunications Union, an Islamic Civil Aviation Council, the OIC Information Network (OICISNET) and for the harmonization of standards in Member countries.

At this juncture, special mention should be made of the Islamic Development Bank (The IDB) which has been playing a catalytic role in the reinforcement of economic cooperation and development of Member States.

The IDB which was established in 1975 has as its main objective to contribute to the economic and social cooperation among them. It was the first international development financing institution to operate according to Islamic principles and banking.

The Bank very quickly became one of the pillars of the cooperative spirit and joint action within the OIC with its multi-faceted financing and technical assistance activities at the service of the Islamic community. Different modes of financing used by the Bank has been providing much needed support for the development efforts of the Member countres. IDB's Foreign Trade Financing Facility has been of special importance to many OIC countries. In this connection IDB's contributions have also been substantial for the implementation of several projects on the agenda of the COMCEC, for example, the establishment and activation of the Lonter-term Trade Financing Facility within the Bank and the preparation of the draft articles of agreement establishing the Islamic corparation for the Insurance of Investment and Guarantee.

In concluding this chapter on OIC's efforts to promote economic cooperation and integration. Three observations are to be highlighted.

First of all, Member States are today more than ever before determined to intensify and strengthen economic cooperation among themselves. It is because of this, that in 1991 during the Sixth Summit the Kings and heads of State and Government gave specific directives for the formulation of new strategies for the updating of the 1981 PLAN OF ACTION which has been and is still is the OIC print for economic cooperation. Serious work has been undertaken within the auspices of the COMCEC to update the PLAN. The final draft of the updated PLAN OF ACTION comprising a set of overall long-term objectives together with a number of basic principles and modalities for implementation and follow-up, is now ready for the consideration and approval of the COMCEC authorities. One interesting feature of the new Plan is the introduction of new areas of cooperation like in human resources development, the environment and the emphasis on the PRIVATE

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SECTOR in the economic activities of the OIC.

Secondly, throughout their initiatives at economic cooperation, Member States have always been convinced that one of the best ways of ensuring meaningful co-operation is through TRADE. It is for this reason that in addition to the schemes that have been designed to inter-Islamic trade, a lot of emphasis is put on the organisation of ISLAMIC TRADE FAIRS, on the organisation of BUSINESS FORA and on the implementation of the Agreement on Trade Preferences.

Thirdly and finally, the various OIC activities geared towards economic cooperation which have just been outlined go to show that the Organisation of the Islamic Conference has made serious efforts over a period of some fifteen to twenty years to provide a framework within which the Islamic World could cooperate extensively, initiate and carry out joint economic action in stages in a World that is fast moving towards globalisation through regional cooperation and integration.

(b) The Encouragement of Sub-regional Economic Groupings:

The process of economic integration which is a long and complex initiative could only be achieved in phases and the promotion and reinforcement of cooperation at the sub-regional level is an essential first step in this direction. It is for this reason that the OIC has been encouraging the establishment of economic co-operation at the sub-resional level and has greatly appreciated the initiatives undertaken by many Member States to create economic cooperation groupings at the sub-regional level.

Even before the 6th Summit adopted its Resolution on the creation of Islamic Common Market on a step by step basis and through OIC economic groupings at the sub-regional level, several economic groupings had existed within the Islamic Ummah.

Faced with chronic setbacks in terms of actual national economic performances and growingly aware of the fact that economic integration would enable the participating countries to attain together higher rates of growth and development, a large number of OIC countries embarked and participated in a considerable number of regional and sub-regional schemes that, within differing horizons, aim in one form or the other at economic integration either among themselves or with other developing countries.

One can make a list of all such groups, which have been in place for a long time. The list could be long but for the purposes of this lecture one would limit one self to highlighting just a few of them and selecting those which are currently active in the three regions of the OIC.

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The OIC has been encouraging and monitoring with a large measure of interest the activities and achievements of the following sub-regional groupings:

(i) The Gulf Cooperation Council - The GCC.

This organization was established in 1981 and groups Bahrain, Kuwait, Oman, Saudi Arabia and the UAE.

The GCC is actively involved, inter-alia, in unifying trade and industrial legislation as a common uniform customs tariff, liberalisation of inter-trade of industrial goods, policy coordination in petrolium industry, coordination of financial and monetary policies, introduction of common currency as well as technical and scientific cooperation.

(ii) Arab Maghreb Union (AMU).

Came into being in 1987 grouping Algeria, Libyan Arab Jamahiriya, Mauaritania and Morocco and Tunisia.

The Union has completed the institutional framework and broad guidelines for integration in food security, economy and finance, infrastructure and human resources development. It is planned to have joint services and service infrastructure and an AMU industry, energy resources, finance, tourism and crafts are operative.

(iii) Arab Cooperation Council (ACC).

The Council groups Egypt, Iraq, Jordan and Yemen and plans to coordinate and harmonize the major economic policies of member countries especially in finance, customs, industry, trade and agriculture with an ultimate aim of creating a common market.

(iv) Economic Cooperation Organization (ECO).

Created in 1985 and grouping ten Islamic countries Iran, Pakistan, Turkey, Afghanistan and the six central Asian Republics of Kazakhstan, Kyrgyzstan, Turkmenistan, Uzbekestan, Azerbaijan, and Tajikistan.

At the moment, programs and projects are being developed in various technical committees to promote technical cooperation in trade, industry, agriculture, energy, infrastructure and several other fields. A protocol on exchange of trade preferences has already been signed.

(v) Association of South-East Asian Nations (ASEAN).

Established in 1967 and groups Brunei, Indonesia and Malaysia together with three other non-OIC countries. The Association has realised Intra-Asian trade liberalisation through the Basic Agreement on Preferential Arrangements of 1977.

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Various sectoral agreements and arrangements have been put into effect and common projects in diverse economic and social fields planned.

(vi) South Asian Association for Regional Cooperation (SAARC).

Groups together Bangladesh, Pakistan, Maldives plus four other non-OIC countries (India, Nepal, Bhutan and Sri Lanka) for cooperation activities which were expanded in 1988 to cover trade, manufactures, services and education.

(vii) Economic community of the West African States (ECOWAS).

It was established in 1975 and groups Benin, Burkina Faso, Gambia, Guinea, Guinea-Bissau, Mali, Niger, Nigeria, Mauritania, Senegal, Sierra Leone together with five other non-OIC countries.

The ultimate aim is to create a Common Market with trade liberalisation through consolidation of customs duties, charges and non-tariff barriers. It is aimed to gradually harmonize all major sectors including monetary and financial matters.

(viii) Preferential Area for Eastern and Southern Africa (ESAPTA).

This preferential area comprises Comoros, Djibouti, Somalia, Sudan, Uganda plus 13 non-OIC countries.

It endeavours to create a common market eventually by gradual elimination of trade barriers internally and adopting a common external tariff, a clearing facility and payments arrangements. Some joint projects in industry, energy, agriculture and infrastructure have been initiated.

There are several more sub-regional groupings involving both purely OIC countries and OIC countries plus non-OIC countries. In fact, more than two-thirds of the OIC Member Countries are associated with regional and sub-regional economic cooperation and integration schemes. This should be considered as a very useful asset for OIC as a whole as it makes possible community-wide action to promote and expand cooperation. And although very few of these grouping have managed to progress as planned, their continued creation and existence are being encouraged by the OIC as they represent the step-by step approach being advocated for the creation of an Islamic Common Market.

WHAT ARE THE PROSPECTS FOR THE CREATION OF AN ISLAMIC COMMON MARKET?

Now that we have had some insight into the attempts being made by Islamic countries to work towards Islamic Common Market, we have seen from the initiatives being undertaken by Islamic countries that a lot is being done towards this end.

We have taken a policy-decision at the highest levels to work towards the creation of an Islamic Common Market. We have in place a solid framework within which one can work towards this goal. We have the necessary institutional structures, we have the legal instruments that should help with our ambition. We have strong institutions which are in place and which can help in achieving our objectives. We have a stronger Organization from 46 Members upto 1991, we are now 51 in the OIC -, most if not all of our Member countries are involved in one way or the other in economic integration at the sub-regional level. With all this, where do we stand? Is an Islamic Common Market a dream or could it be a reality? In short what are the prospects for an Islamic Common Market?

In my opinion and in fact from the perspective of the Organisation of the Islamic Conference, an Islamic Common Market could best be conceived as the ultimate goal of the cooperation activities of the Organization of the Islamic Conference.

For if go by the definition I gave at the beginning and the example of the EEC, an Islamic Common Market could only be a long term objective as such an advanced mode of economic integration is full of national, commercial and international limitations and constraints.

Historical experience of the various integration schemes among developing countries in general and the OIC countries in particular has shown that the conceptual and practical difficulties that these countries have faced with integration projects are considerable. They arise in fields as diverse as the transport and communication systems inherited from the colonial period (quite unsuitable for inter-regional trade), the competitive structures of the industries and natural resources of countries potentially interested in joining regional groups, the existence of vested interests unwillingly to give up the protection they now enjoy, unrealistic exchange rates and even the shortage of basic statistical data which often rules out any reliable assessment of the probable repercussions of the integration process.

Further difficulties could be found in the effective coordination of investment throughout the region, the need to compensate countries which may suffer losses in the early stages and the step by step surrender by Member States of powers to take economic and social decisions at the national level.

In the face of these obstacles or difficulties, OIC authorities are advocating more modest objectives rather the complete integration of the economies. It is by beginning with cooperation in concrete investment projects together with the step by step expansion of trade between OIC countries that the climate of mutual trust and solidarity, which is an essential prerequisite for the realization of ultimate integration, can best be created.

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Hence in view of the rapidly changing world-scene, where the South is going to be faced with a more integrated North than before, and taking into consideration the problems mentioned above, the approaches to OIC cooperation need to be remodeled to attain two goals simultaneously:

(i) To create powerful economic entities capable of facing the challenges emanating from the emergence of huge economic blocks;

(ii) Structural transformation of OIC countries economies to attain economic efficiency and social welfare.

From all these, it is quite clear that an Islamic Common Market should be a long term ideal which could and should be approached carefully and in stages. This is the idea the higher authorities of the OIC had in mind when they passed their resolutions, quoted earlier, calling for a step-by-step approach. Though far from reaching an advanced stage, some important initiatives so far have been taken in a multitude of economic cooperation fields comprising trade-preferences, joint-ventures, coordination and harmonization of various sets of economic policies, regional schemes of monetary and financial cooperation. Once these modalities are made to work more thoroughly, establishment of regional integration schemes could be considered seriously, linked to one another with special preferential arrangements. This could then constitute the concrete foundation of an overall Islamic Common Market Framework made up of regional components.

The OIC countries basically constituting the Islamic World now number 51; they represent around 20% of the World's population, produce 50% of the World's oil and 40% of the World's export of raw materials, as well as other resources. They therefore have the potential not only to make their collective weight felt as active participants on the global scene but also to further strengthen cooperation among themselves with the ultimate goal of establishing an Islamic Common Market resources.

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