

## **CHAPTER 2 : HISTORY AND DEVELOPMENT OF ISLAMIC BANKING AND FINANCE AROUND THE WORLD**

### **KEY CONCEPTS AND SKILLS**

- Business and Financial Activities during the Time of the Prophet
- Early establishment of Islamic Banking and Finance: 1950-1970s
- Commercialization of IBF: 1980s-1990s
- Rapid Growth of IBF: 2000 and beyond
- Development of IBF: Country-specific Experience

Business and Financial Activities during the Time of the Prophet

- **History of Islamic Banking and Finance**

Early Establishment of Islamic Banking and Finance: 1950-1970s

- **History of Islamic Banking and Finance**

The first attempt to establish IB was in the 1950's – in the rural area of Pakistan

- Pious landowners deposit their funds without interest rewards
- Credit was advanced to other poorer landowners for agricultural improvements
- Although there was no shortage of borrowers, for the depositors, it was a once and for all effort
- Depositors took considerable interest on how the money was loaned out
- **History of Islamic Banking and Finance**

25<sup>th</sup> July 1963 – February 1967: Mit ghamr Islamic Savings Bank started in Egypt by El-Naggar:

- Based on German saving bank
- Purpose to mobilize idle savings of the majority of Muslim within the Syariah and to provide halal returns on their saving
- El-Naggar was an academic himself
- Managed the staff

### **The role of the bank (El-Naggar, 1974)**

- a) An efficient intermediary between the supply and demand of capital
  - b) Act as one educational center for economic efficiency, saving education and banking habit
  - c) Set a dynamic factor in mobilizing the idle capital for investment, reducing hoarding and reduce problem of capital formation
- History of Islamic Financial Institutions- Overview
  - History of Islamic Financial Institutions- Overview (3) : Asia and Western Countries

- 3. Internationalization of IBF: 1980s-1990s

### **Internationalization of Islamic Banking and Finance**

**Numerous countries in this region have begun development of Islamic banking and finance**

- Indonesia: set up first Islamic bank in 1992
- Brunei: established Islamic Bank of Brunei in 1993
- Singapore: recently announced that it envisions to be regional hub for Islamic financial services
- Thailand: approved draft bill for the establishment of an Islamic bank in 2001

Rapid Growth of IBF: 2000 and beyond

### **VITAL STATISTICS OF IBF INDUSTRY**

- Islamic Banking and Finance Today- (1)
- Islamic scholars have **profound influence** on the practice of Islamic banking and finance
  - No equivalence in other religions
- Muslim governments' approach in relation to IBF differs
  - Transformation of the entire internal financial system to Islamic
    - Iran, Pakistan, Sudan
- Islamic Banking and Finance Today- (2)
  - Embrace Islamic banking as a national policy concurrently with conventional banking and finance (dual track banking)
    - Bahrain, Brunei, Indonesia, Kuwait, Malaysia, Turkey, UAE
  - Neither support nor oppose Islamic banking
    - Egypt, Yemen
  - Actively discourage separate Islamic banking presence
    - Saudi Arabia, Oman

Development of IBF: Case of Malaysia and other Countries

- **Islamic Banks in Malaysia**
- [BNM List of Licensed Banking Institutions in Malaysia: Senarai Institusi Perbankan Berlesen di Malaysia](#)
- Local vs. Foreign
- **Participation by Non - Muslim banks**

- Big players in Islamic financial landscape today are Western-based, majority non - Muslim owned banks who participate via their Islamic subsidiaries
  - Citigroup’s Citi Islamic (Bahrain) has deposits exceeding USD6 billion compared to largest local Al-Baraka whose deposit amounted to a little over half a million
- What is the motivation or rationale behind apparent “embracing” of IBF by non-Muslims?
  - Muslims act on faith and adherence to religious injunctions
- Participation by non-Muslim banks
  - Some possible explanations for non-Muslims
    - **Appreciation and concurrence with wisdom behind prohibition of *riba***
      - The negative repercussions of interest-based lending on the economy and society
      - Benefits associated with profit-sharing arrangements including better realization of distributive justice
    - **Pure commercial incentives**
      - Islamic banking perceived as a market segment, rather than a distinctively separate offering
      - Ignoring this marketing niche will be at the expense of lost profit opportunities
    - **Conventional banking stakeholders view Islamic banking as a threat**
      - If Islamic banking is implemented as envisioned by the *Shari’ah*, inferiority of conventional banking will be self-evident
      - In an attempt to pre-empt such a possibility, conventional banking stakeholders participate in Islamic banking in order to steer it towards convergence with conventional banking