

## Islamic Banking in India

This has a reference to the news item of Financial Express of March 3, 2006, 'no Islamic bank in India says Govt.' (photocopy of the clipping enclosed).

We need not take the news as heart-breaking one. Islamic Banking is the misnomer of our subject. It should be the 'Islamic Finance.' Islamic Banking is a part of Islamic Finance.

Islamic Finance can, broadly, be divided into two major parts, one Qarde Hasan i.e. interest free debt and the other profit-loss sharing i.e. equity investment.

Acceptance of deposit in the current account is a must for every bank all over the world. To some extent this is an equivalent of Qarde Hasan of Islamic Finance. What makes it unIslamic is the fact that they deploy the float available to the banks in this category of deposit on interest-base lending. Actually this is the social wealth on which the owners do not expect any return. So this should be utilized either in reducing the debt burden of the Government/s or making interest free loans to the needy persons of the society. Therefore, I have suggested in the paper 'Islamic Finance in India'[[1](#)] that these accounts should be run on the pattern of P.P.F. Scheme of the Government through banks. However the banks may earn agency commission on this business also.

Another alternative for accepting interest free deposit from public to be deployed on interest free basis lies in post office, saving bank scheme with minor modification. To avoid the receipt of interest on these deposits the account opening form should contain a standing instruction from the interest averse depositors to the effect that the amount of interest may be transferred to some charitable account of the Government out of which the government should make interest free loan to the needy persons of the society. This will increase the numbers of beneficiaries in the micro finance scheme of the Government. However the Government should assure that the deposits so mobilized shall not be deployed on interest base lending.

As per the recent news a proposal 'to give the status of a bank to the post office' is under consideration of the Government (copy of news clipping closed). If it is done so an opportunity for mobilizing hither to untapped resources and deploying the same for the welfare of the society shall be lost. The idea has not been appreciated, though for different reasons, by the Economic Times also (copy of editorial enclosed).

The second part of the Islamic Finance is 'profit and loss sharing system.' For this purpose a lot of options are available in the existing financial system of India. As is well known the system is 100% equity base. The major hurdle in its way is our taxation system which has a bias in favour of debt as against equity in the formation of capital. Besides being unIslamic it is harmful to our economy also more particularly after its opening to the global competition. Now our companies with meager capital base and high cost debt have to face multi national companies having strong capital base with low cost debt. Our taxation system is largely responsible for reducing competitive strength of Indian companies (a 'proposal for changing present system of taxation to more equitable one' is under preparation).

For further progress of Islamic Finance in India with a view to mobilize hither to untapped local resources as well as to attract FDI to be put in the process of production, distribution and employment of our country we may come out with some concrete suggestions. Focus of our attention shall be the improvement of efficiency of our capital and commodity markets in the larger interest of the society as a whole.

**(Ahsanul Haq)**

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