



ISLAMIC INTERBANK MONEY MARKET
INMALAYSIA: THE ANALYSIS OF THE MODUS
OPERANDI AND THE INSTRUMENTS FROM
SHARIAH PERSPECTIVE

BY

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ABSTRACT

This thesis studies the Islamic Interbank Money market in Malaysia (IIMM) from the *Sharfīlah* and legal point of view. The significance of the research can be viewed from the point of the criticism against the credibility of the market in terms of the *Sharfīlah* compliance requirement. Another problem is the dearth of tradable instruments in the IIMM which culminates in the liquidity mismatch in the liquidity portfolios of the Islamic financial institutions. The scantiness of the instrument also poses challenges to the emerging jurisdictions of the Islamic banking across the globe as regards the best Islamic money market model that is worthy of adopting. The objective of this research is to contribute to the efforts towards the solving of the problems. Thus, as for the issue of the compliance of the Market with the *Sharfīlah* principles, a jurisprudential study of the underlying contracts of the Modus Operandi of the market and that of the instruments was conducted. Therefore, the findings of the study show that there is a need for the *Sharfīlah* adaptation of the underlying contracts of the Modus Operandi of the IIMM. However, as for the underlying contracts of the instruments of the IIMM, it is discovered that they are all *Sharfīlah* compliant, given the fact that all the contracts are rooted in the literatures of Islamic jurisprudence, notwithstanding the divergence of opinions between the scholars of the notable schools of law, on some of the contracts. Moreover, as regards the matter of the inadequacy of tradable instruments, a proposal for the developing of *Bayʿ al-Wafʿ* which is a sale contract under the Islamic commercial law as an instrument of the Islamic Interbank money market is made. Therefore, an instrument which is coined as *Bayʿ al-Wafʿ* Repo (BW Repo-i) is proposed to be introduced into the Islamic Interbank money market. The proposition is the contribution of the current research to the subject of the IIMM. Finally, the study is a qualitative legal and jurisprudential research. It finally concluded that the Malaysian model of the Islamic Interbank money market can be adopted by other jurisdictions as the best practice model. This will be helpful to the existing jurisdictions that are confronted with the problem of Islamic money market and the emerging jurisdiction of Islamic banking and finance, due to its, viability, simplicity, sophistication and the *Sharfīlah* compliant credibility.

ملخص البحث

إن هذه الأطروحة تمثل الدراسة حول "السوق النقدي الاسلامي فيما بين البنوك في ماليزيا (IIMM)"، وذلك، من حيث المنظور الشرعي والقانوني. وتبدو أهمية الدراسة في التحديات التي تواجه هذا السوق من حيث مصداقيتها لتطبيق المبادئ الشرعية. ومن تحدياتها كذلك قلة الأدوات القابلة للتداول فيها والتي من نتيجتها مشاكل السيولة المتواجدة في المؤسسات المالية الاسلامية. وقد انعكست هذه مشكلة في قطاعات أسواق البنوك الاسلامية الناشئة من حيث فقدانها للإطار الأمثل القابلة للتبني والتأسي بها في هذا المجال. وعلاوة على ذلك، فإن هدف هذه الأطروحة تكمن في الإسهام في محاولة إيجاد الحلول لهذه التحديات. وقد قام الباحث بدراسة الفقهية حول طريقة تسيير السوق والأدوات المتداولة فيها، وكانت نتيجة الدراسة، الاكتشاف بأن العقود الكامنة في طريقة سير السوق محتاجة إلى التكييف الفقهي، ولكن العقود التي كرت عليها أدوات السوق فإنها كلها عقود شرعيّة، وذلك بحكم كونها مستمدة من المصادر والمراجع الفقهية، وبغض النظر عن الخلافات الفقهية بين المذاهب الأربعة المعروفة، في بعض تلك العقود. وفيما يتعلق بتحدي قلة الأدوات القابلة للتداول في السوق، فإن الباحث يقترح تنمية "عقد بيع الوفاء" كأداة السوق النقدي سدا لهذه الفجوة، ومن ثمّ تقديم الخطة لأداة السوق النقدية المسمى بـ ("Bay' al-Waf' Repo", "BW Repo-I"). وتمثل هذه المحاولة مساهمة البحث في موضوع السوق النقدي الماليزي. وأخيراً، فإن هذا البحث قد سلك طريقة نوعيّة قانونيّة، وتواصل أخيراً إلى أنّ الإطار العملي للسوق النقدي الماليزي صالحة للتبني لدى القطاعات المالية والمصرفية الاسلامية الناشئة، وأنها قادرة على مساعدة القطاعات الموحدة التي تعاني من التحديات إدارة سيولتها، كما ستفيد القطاعات الناشئة للمصرفية الاسلامية في تنمية سوقها النقدي، وذلك بالحكم ملائمتها وسهولتها وتطورها ومصداقيتها لتطبيق المبادئ الشرعية.

APPROVAL PAGE

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DECLARATION

I hereby declare that this thesis is the result of my own investigation, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degree at IIUM or other institutions.

Abdul Azeez Maruf Olayemi

Signature

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INTERNATIONAL ISLAMIC UNIVERSITY MALAYSIA

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I dedicate this thesis to my father, Abdul Azeez Olasunkanmi Abdul Kareem Akinola Ogunyemi Akingbola for directing me and guiding me toward the path of knowledge and playing an excellent and wonderful parental role in my life, May Allah grant him long life to reap the fruits of his labour, and to my late mother, Safrat Busari Ayoola Ogunyemi Akingbola whom I lost when I was in dire need of her. May Allah grant her Jannah al-Firdaos.

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Skim Perbankan Islam (SPI).
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LIST OF ABBREVIATIONS

AB-i	Accept bill – Islamic
ADIs	Authorized Depository Institutions
AITAB	<i>al-Ijārah Thuma al-Bay'</i> 'Lease Agreement that incorporates the sale of the leased asset at the end of the tenure
AMLA	Anti-Money Laundry Act 2001
BAFIA	Banking and Financial Institutions Act 1989
BAIS	Cagamas <i>Bay' bi-al-Thaman al-Ūjil</i> Islamic Securities
BBA	<i>Bay' bi-al-Thaman al-Ūjil</i> 'Deferred Sale'.
BIDS	Bond Information and Dissemination System
BE	Bill of Exchange'
BNM	Bank Negara Malaysia
BNMN –i	Bank Negara Monetary Notes – i
BNMWP	Bank Negara Malaysia <i>Wad'fīlah</i> Placement
BNNN	Bank Negara Negotiable Note
BW Repo-I	<i>Bay' al-Waf'ē</i> 'Repurchase Agreement
CMB	Cagamas <i>al-Mud'rabah</i> Bond
CMP	Commodity <i>Mur'abahah</i> Program
CPO	Crude Palm oil
DvP	Delivery versus Payment Arrangement
ECM	Exchange Control Notices of Malaysia
EPT	Electronic Trading Platform
Espick	Sistem Penjelasan Informasi Cek Kebangsaan Secara Elektronik
ETC	Exchange Traded Commodities
FA	Facility Agent
FAST	Rules on Fully Automated System for Issuing/Tendering
GII	Government Investment Issues
GP	(<i>Garis Panduan</i>)
GP8-	Guidelines on the Specimen Reports and Financial Statements for Licensed Islamic Banks
GP8-i	Guidelines
GPS 1,	Rate of Return Framework,
GRUNIF	Guaranteed Revolving MUNIF
IAB	Islamic Accepted Bills
IB	Islamic Bond
IBA	Islamic Banking Act 1983
IBs	Islamic banks
ICP	Islamic Commercial Papers
IDS	Islamic Bond (IB) /Islamic Debt Securities
IFSI	Financial Services Institutions
IFTS	Interbank Funds Transfer System
IICCS	Islamic Interbank Cheque Clearing System
IIM	<i>Mud'rabah</i> Interbank Investment
IIMM	Islamic Interbank Money Market

IMF	International Monetary Fund
INID	Islamic Negotiable Instrument of Deposit
IPDS	Islamic Private Debt Securities
IPO	Initial private or public offering
IRUF	Islamic Revolving Underwritten Facility
ITB	Islamic Treasury Bills
KLACH	Kuala Lumpur Automated Clearing House
KLSE	Kuala Lumpur Stock Exchange
L/C	letter of credit
LA	Lead Arranger
LMC	Liquidity Management Centre
LME	London Metal Exchange
MARC	Malaysian Rating Corporation Bhd.
MCC	Foreign Exchange Market
MCD	Middle East and Central Asia Department
MGS	Malaysian Government's Securities
MII	<i>al-MudÉrabah</i> Interbank Investment
MITB	Malaysian Islamic Treasury Bills
MUNIF	<i>MurÉbahah</i> Notes Issuance Facility
MyClear	Malaysian Electronic Clearing Corporation Sdn. Bhd. (MyClear).
NID	Negotiable Instrument of Deposit
NIDC	Negotiable Islamic Debt Certificates
NLC	National Land Code, 1963
NSAC	National <i>SharfÍlah</i> Advisory council
OIC	Organization of Islamic Conference
OMO	Open Market Operations
OTC	Over-the-Counter Market
PA	Payment Agent
PD	Principal Dealers
PDs	Principal dealers
PDS	Private Dept Securities
PG	Municipal Council, Mukah Power, OCBC Sub Debt
PN	Primary Note
PPA	Property Purchase Agreement
PSA	Property Sale Agreement
PTM	Tender Panel Members
RA-I	<i>al-Rahn</i> Agreement-I
RENTAS	Real Time Electronic Transfer of Funds and Securities
RMBS-i	Cagamas Islamic Residential Mortgage Backed Securities
SAC	<i>SharfÍlah</i> Adversary Council
SBBA	Sell and Buy Back Agreement
SBL	Securities borrowing and Lending Programme under RENTS
SBNMI	<i>SukÉk</i> Bank Negara Malaysia <i>al-IjÉrah</i>
SC	Securities Commission
SLC	Sarawak Land Code
SN	Secondary Note
SPI	Islamic Banking Scheme
SPICK	<i>Sistem Penjelasan Imej Cek Kebangsaan</i>

SPV	Special Purpose Vehicle
SSTS	Scripless Securities Trading System
STP	straight-through-processing
TSR	Transferable Subscription Right
WI	When Issue

ARABIC TRANSLITERATIONS

Alphabets

ا	A	ط	Ù
ب	B	ظ	Ú
ت	T	ع	Ñ
ث	Th	غ	Gh
ج	J	ف	F
ح	×	ق	Q
خ	Kh	ك	K
د	D	ل	L
ذ	Dh	م	M
ر	R	ن	N
ز	Z	و	W
س	S	ه	H
ش	Sh	ة	Ah
ص	Ø	ء	ò
ض	Ö	ي	Y

Vowels and Diphthongs

ا	A	آ	Ó
إ	I	إي	0
أ	U	أو	Õ
أو	أو	Aw	
أي	أي	Ay	

CHAPTER 1

INTRODUCTION

1.1 INTRODUCTION

The success of the Central Bank of Malaysian ‘Bank Negara Malaysia,’ in its efforts to ensure the growth of Islamic Banking and finance is crystal clear. However, the prelude to such development is the outcome of the success of the Bank in the developing of a reputable model of Islamic interbank money market (IIMM) in the country. The IIMM has emerged as the leading best practice for the emulation of the emerging *Sharfīlah* compliant money market jurisdiction across the world. Thus, the concept of money market in the broad sense is defined as ‘the business activity in which banks and other financial institutions engage to lend money to each other,¹ on a short term basis for the purpose of their liquidity management. In another word, the market is a financial mechanism for dealing with short term papers such as notes and bill. This is in contrast to the capital market, which provides for medium and long-term financing.² The money market system is available in both the conventional and *Sharfīlah* compliant banking systems.

The instruments of the money markets include Commercial Papers, Bankers Acceptances, Treasury bill, Certificate of Deposits and other short-term securities. It provides liquidity funding for the financial system.³ It is an open secret that the IIMM

¹ *Macmillan English Dictionary for Advanced Learners*, International Student Edition, (UK: Selwood Systems, 2006), at 918.

² Henry Campbell black M. A., *Black Law Dictionary*, 5th Ed., (St. Paul Minn. West Publishing Co., 1979), at 907.

³ *Ibid.*

operates on the same platform with conventional systems,⁴ after the elimination of prohibited acts from it. Thus, the activation of *al-Ijtihād*⁵ is a necessity for the rapid growth of the IIMM,⁶ hence, the adoption of the principle by its jurists (the *Sharfīlah* scholars)⁷ who embarked on the way of *al-Rukhīlah* wherever there is a necessity⁸. That is, based on collective *al-Ijtihād*⁹ and *al-maqāsid-based al-Ijtihād*.¹⁰ As a matter of fact, *al-Rukhīlah* is of a God's gift to mankind which cannot be rejected.¹¹

However, since the money market system under the Islamic financial institution is the Islamic interbank money market, which is a *Sharfīlah* compliant system; the instruments of the Islamic inter-bank money market must conform to the principles of *Sharfīlah*. It is required that all the products that are involved in the sale and buying must be from the ethical activities. The profits gained should not be from prohibited business, such as alcohol production, gambling, pornography, interest-based activities and interest-based debt. Some of the acceptable instruments of the market, under *Sharfīlah* are the profit sharing contract of *Muḥābah* and the trading contract of *Murābahah*, *al-bayʿ bithmanin ḥijil*, *bayʿ al-dayn* and *bayʿ al-ḥnaḥ*¹². The

⁴ Syed Omar Syed Agil Aidit Ghazali, *Reading in the Concept and Methodology of Islamic Economics*, (Kuala Lumpur: CERT Publication, 2007), at 189.

⁵ Hikmatullah Babu Sahib, *Islamic Law and Modernity Conflict and Reconciliation*, in *Contemporary Issues in Islamic Law*, Ed. By Abdul Haseeb Ansari, (New Delhi: Serial Publications, 2011), at 199.

⁶ Ibn ḤAshʿr, *Treatise on Maqasid al-Sharfīlah*, (Kuala Lumpur: Islamic Book Trust and International Institute of Islamic Thought, London, 2006), at 219.

⁶ *Macmillan English Dictionary for Advanced Learners*, International Student Edition, (UK: Selwood Systems, 2006), at 918.

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⁷ ×abʿb Aīmed, *Product Development in Islamic Banks*, (Edinburgh: Edinburg University Press, 1988) at 46.

⁸ YĒsfn Suwaylim ŪĒhĒ, *Hukm al-Islām fī Arbāh Shahādāt al-Isthmār wa Wadā'ī'u Ṣanāādīq al-Idkhār*, (al-Hazhar: 1417) at 13.

⁹ Aznan Hasan, *An Introduction to Collective Ijtihad (Ijtihad Jama'i)*, at 29.

¹⁰ Aīmad al-RaysĒnĒ, *al-Shātibī Theory of the Higher Objectives and Intents of Islamic Law*, (Kuala Lumpur: Islamic Book Trust and International Institute of Islamic Thought, London, 2006), at 336.

¹¹ Nicolas P. Aghindes, *Mohammedan Theories of Finance with and Introduction to Mohammedan Law and a Bibliogra*, (New York: The Faculty of Political Science, Columbia University 1916), at 114.

¹² Financial Sector Talent Enrichment Programme, FSTEP, *Islamic Banking Hand Book*, at 178.