



THE NEGATIVE IMPACT OF RIBA BANKING ON
THE PERFORMANCE OF ISLAMIC BANKING IN A
DUAL BANKING SYSTEM

BY

MUHAMMAD ZAHID ABDUL AZIZ

A dissertation submitted in fulfilment of the requirement
for the degree of Master of Science in
Islamic Banking & Finance

Institute of Islamic Banking & Finance
International Islamic University
Malaysia

MAY 2012

ABSTRACT

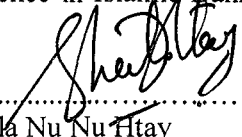
Islamic banking is now an established part of many nations' banking system so much so it is said to be operating in a dual system alongside conventional banking. This duality is particularly emphasised in Malaysia and even recognised by the nation's central banking legislation. However this duality is not such an innocuous situation and is suspected by the researcher to be a principal reason for many of the weaknesses found in Islamic banking today. That Islamic banking is criticised for many deficiencies is a widespread phenomenon these days. These includes it being a mirror image of conventional banking, tenuous in terms of Shariah compliance; fails to meet Maqasid Shariah, do not aid equitable distribution of wealth and manages risk like a money lender. The reasons attributed include it being too focussed on debt financing, weaknesses of Islamic bankers, and impiety of the ummah. No studies have sought to identify the coexistence of conventional banking as a factor directly contributing to these weaknesses of Islamic banking. No studies have examined the environment Islamic banking is expected to be operating in as compared to the environment it found itself in. No studies have examined whether the regulatory measures imposed on conventional banking is correct when imposed on Islamic banking. This study aims to fill that gap. This study articulates that conventional banking is negatively impacting the performance of Islamic banking, in particular on Islamic banking's ability to uphold true compliance with Shariah. It is hoped that this study will trigger similar studies to further prove its findings. It is the unashamed hope of the researcher that one day Muslim nations can bury riba banking and build on its ashes a sole and single Islamic banking system that upholds and embodies the true demands of the Quran and Sunnah.

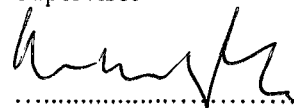
خلاصة البحث

تعتبر المصرفية الإسلامية هي الآن جزءاً أساسياً من النظام المصرفي العديد من الدول، لدرجة يقال أن تكون عاملة في نظام مزدوج جنباً إلى جنب مع المصارف التقليدية. وهذه الثنائية كما في ماليزيا ومعترف بها حتى من قبل التشريع في هذه البلاد من قبل المصارف المركزية. لكن هذه الازدواجية ليست مثل هذه الحالة غير ضارة يعتقد الباحث أن يكون هذا الازدواج السبب الرئيسي لكثير من نقاط الضعف الموجودة في المصرفية الإسلامية اليوم. وتطال المصارف الإسلامية هذه الأيام العديد من الانتقادات حتى أصبحت عادة منتشرة. و منها، أن المصارف الإسلامية صورة طبق الأصل من المصارف التقليدية، ضعيفة من حيث التوافق مع الشريعة، لا تستوفي المقاصد الشرعية، لا تساعد التوزيع العادل للثروة وإدارة المخاطر مثل المال المقرض. و أسباب أخرى تشمل تركيزها أيضاً على تمويل الديون وضعف من المصرفيين الإسلاميين. لم تبحث الدراسات السابقة على التعايش بين المصرفية التقليدية بوصفه عاملاً مساهماً مباشرة إلى نقاط الضعف في الخدمات المصرفية الإسلامية. ولا توجد دراسات فحصت ما إذا كانت التدابير التنظيمية المفروضة على المصارف التقليدية مناسبة في حالة فرضها على الخدمات المصرفية الإسلامية. تهدف هذه الدراسة إلى سد هذه الفجوات و توضيح أن البنوك التقليدية هي التي تؤثر سلباً على أداء المصارف الإسلامية، ولا سيما على قدرة المصارف الإسلامية على الامتثال الصحيح مع أحكام الشريعة الإسلامية. ومن المؤمل أن هذه الدراسة سوف يؤدي دراسات مماثلة لإثبات مزيد من النتائج التي توصل إليها. ويأمل الباحث أن يأتي اليوم الذي تستطيع فيه الأمة الاستغناء عن الربا المصرفي، وبناء النظام المصرفي الإسلامي الذي يحترم ويجسد المطالب الحقيقية للقرآن والسنة.

APPROVAL PAGE

I certify that I have supervised and read this study and that in my opinion; it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Islamic Banking and Finance.

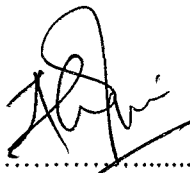

.....
Sheila Nu Nu Htay
Supervisor


.....
Mustapha Hamat
Co Supervisor

I certify that I have read this study and that in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate, in scope and quality, as a dissertation for the degree of Master of Science in Islamic Banking and Finance.

.....
Mohd Azmi Omar
Examiner

This dissertation was submitted to the Institute of Islamic Banking and Finance and is accepted as a fulfilment of the requirement for the degree of Master of Science in Islamic Banking and Finance.


.....
Abdul Rahim Abdul Rahman
Dean, Institute of Islamic
Banking and Finance

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 degrees at IIUM or other institutions.

Muhammad Zahid Abdul Aziz

Signature.....

Date.....*9 May 2012*.....

INTERNATIONAL ISLAMIC UNIVERSITY MALAYSIA

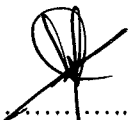
**DECLARATION OF COPYRIGHT AND AFFIRMATION OF
FAIR USE OF UNPUBLISHED RESEARCH**

Copyright © 2012 by International Islamic University Malaysia. All rights reserved.

**THE NEGATIVE IMPACT OF RIBA BANKING ON THE PERFORMANCE
OF ISLAMIC BANKING IN A DUAL BANKING SYSTEM**

I hereby affirm that The International Islamic University Malaysia (IIUM) holds all rights in the copyright of this work and henceforth any reproduction or use in any form or by means whatsoever is prohibited without the written consent of IIUM. No part of this unpublished research may be reproduced, stored in a retrieval system, or transmitted, in any form or by means, electronic, mechanical, photocopying, recording or otherwise without prior written permission of the copyright holder.

Affirmed by Muhammad Zahid Abdul Aziz.


.....
Signature

9 MAY 2012
.....
Date

This Dissertation is dedicated to the workers of the Islamic banking industry in Malaysia, the unsung individuals who fought to create the beachhead for the current progress of Islamic banking and finance. Dedicated and unassuming they seek no reward other than to know that they had served.

ACKNOWLEDGEMENTS

I would like to extend my deepest thanks to my Supervisors Dr Sheila Nu Nu Htay and Mr Mustapha Hamat for their invaluable guidance and patience with me.

My fullest appreciation and gratitude also to the following peers and experts on Islamic Banking who agreed to be interviewed for this Dissertation and henceforth for sharing with me their most invaluable insights.

Dato' Dr Abdul Halim Ismail, Founder Bank Islam Malaysia Berhad and Sharia Committee Member of Securities Commission of Malaysia; Dato' Ahmad Tajuddin Abdul Rahman, Former Managing Director of Bank Islam Malaysia Berhad; Professor Saiful Rosly of INCEIF and Sharia Committee Member of an Islamic Bank; Dr Hikmatullah Babu Sahib of International Islamic University Malaysia (IIUM) Sharia Department and Sharia Committee Member of an Islamic Bank ; Dr Azman Md Nor of IIUM and Sharia Committee Member of an Islamic Bank; Dato' Wan Ismail Wan Yusoh, General Manager of Bank Islam Malaysia Berhad; Wan Abdul Rahim Kamil Ali, Islamic Capital Market Advisor to the Securities Commission of Malaysia and Sharia Committee Member of an Investment Bank; Abdul Rais Majid, Former Head of International Islamic Financial Market, Bahrain and Former General Manager of Bank Muamalat Malaysia Berhad; Mustafa Omar of Islamic Development Bank, Jeddah and formerly of Bank Islam Malaysia Berhad; Yazit Yusof, General Manager of OSK Investment Bank and formerly of Bank Islam Malaysia Bhd. Last but not least two peers and experts who wished not to be named, being a current Chief Executive Officer of an Islamic Financial Institution, and an Academician who writes in International Academic Journals on Islamic Banking & Finance and is a Sharia Committee Member of an Islamic Bank.

Finally, for all the sacrifices they have had to make, a special thank you to my wife Anira, and our dear, three little ones.

TABLE OF CONTENTS

Abstract	ii
Abstract in Arabic	iii
Approval Page	iv
Declaration Page.....	v
Copyright Page	vi
Dedication.....	vii
Acknowledgements	viii
List of Charts	xii
CHAPTER 1: INTRODUCTION	1
1.0 Introduction	1
1.1 Background of the Study	1
1.2 Problem Statement.....	3
1.3 Objective of Study and Research Question	5
1.4 Scope of Study.....	6
1.5 Significance of the Study.....	8
1.6 Limitation of the Research	8
1.7 Organisation of Dissertation	9
CHAPTER 2: LITERATURE REVIEW	11
2.0 Introduction.....	11
2.1 Theoretical Framework Based on Current Literature	11
2.1.1 The Halim Model.....	11
2.1.2 The Chapra Model	16
2.1.3 A comparison of both models.....	18
2.2 Literature in Islamic Banking and Finance.....	20
2.3 Researcher's Theoretical Framework	31
2.3.1 Riba.....	31
2.3.2 Promulgation of the Ayah on Riba	31
2.3.3 Rationale for the Prohibition of Riba.....	33
2.3.4 Structuring of Islamic Banking and Finance in Modern Times...	34
2.3.5 Criticism of Debt Financing	34
2.3.6 Overstretching of the Principle of Trade In Today's Islamic Banking.....	35
2.3.7 Ijtihad to be Based on Maqasid Syariah, Going Beyond Mere Compliance With Legal Rules of Fiqh.....	38
2.3.8 Islamic Economics as a Foundation for Islamic Banking and Finance.....	42
2.4 Conclusion	62

CHAPTER 3: METHODOLOGY OF STUDY	64
3.0 Introduction	64
3.1 Research Design	66
3.1.1 Qualitative Research Method.....	66
3.1.2 Rationale Why Interview Technique Is Suitable for This Research.....	68
3.2 Development Interview Questions.....	69
3.2.1 Research Methodology	69
3.3 Data	81
3.3.1 Primary Data	81
3.3.2 Secondary Data.....	83
3.4 Sample	83
3.5 Statistical Methods.....	85
3.5 Conclusion	86
CHAPTER 4: RESULTS OF STUDY	88
4.0 Introduction.....	88
4.1 Evidence from current literature	88
4.2 Interview of peers and experts of Islamic Banking	90
4.2.1 Response Rate of Interviews.....	90
4.2.2 Tabulation of Results	91
4.2.3 Findings for each Questions	93
4.2.3.1 Findings on question one on whether Islamic banking is disadvantaged in competing for deposits in a dual system.	93
4.2.3.2 Findings on question two on whether riba banking is preventing the extension of mudarabah financing.....	97
4.2.3.3 Findings on question three on whether riba banking is preventing the extension of Parallel Istisna' house financing?	99
4.2.3.4 Findings on question four on whether the Islamic banking sector is being influenced by risks which should be confined only to conventional banking?	100
4.2.3.5 Findings on question five on whether sukuk structures are engineered to deliver conventional demand?	101
4.2.3.6 Findings on question six on whether the Group of experts agree that overall riba banking negatively impact the performance of Islamic Banking in a Dual Financial System like Malaysia	103
4.2.3.7 Findings on question seven on whether the group of experts agree that Islamic Banking will perform well if Riba Banking is banned and the country adopts a single Islamic Banking System	104
4.3 Summary of Results of the Study	105
CHAPTER 5: CONCLUSION	107
5.0 Summary of the Research	107

5.1 Significance of the Research..... 110
5.2 Other Findings of the Research..... 110
5.3 Limitations of the Research and Suggestions for Future Research 118

BIBLIOGRAPHY 120

APPENDIX I: SHORT DESCRIPTION OF PEERS AND EXPERTS..... 126

APPENDIX II: EXPERIENCE OF PEERS AND EXPERTS 128

LIST OF CHARTS/MODELS

<u>Chart No.</u>		<u>Page No.</u>
2.1	Overall Halim Model	12
2.2	The Halim Model	13
2.3	The Chapra Model	16
2.4	Form of Islamic Bank and Islamic Banking and Financial System as determined by Islamic Economics	44
2.5	Implication of Pillars of Economics on Islamic Banks	47
2.6	Islamic Bank is not a Mukallaf	48
2.7	Implication of Principles of Islamic Economics on Islamic Banks	50
2.8	Implications of Three Principal Parameters of Islamic Economics on Islamic Banking	54
2.9	Implications of another Parameter of Islamic Economics – Guarantee of Minimum Standard of Living by the State	55
2.10	Responsibility of Islamic Banks as a unit in the Islamic Economy to help in guaranteeing minimum standard of living	55
2.11	What is Human Welfare Formula?	61
2.12	Implication of Shariah objectives on Property to Islamic Bank	62

CHAPTER 1

INTRODUCTION

1.0 INTRODUCTION

This chapter gives a brief summary of the dissertation. Section 1.1 provides a description of the dual environment of Islamic banking today. Section 1.2 describes the Problem Statement that there are criticisms in the performance of Islamic banking today in particular with respect to strict compliance with Shariah. Section 1.3 describes the research objective and the main and the sub research questions. This will then be followed by a brief discussion on the scope of study in section 1.4, followed by significance of study in section 1.5 and limitations of the research in section 1.6. The chapter ends with organisation of research in section 1.7.

1.1 BACKGROUND OF THE STUDY

According to the Islamic Banking Act of Malaysia 1983 an Islamic bank is defined as “any company carrying on Islamic banking business, which is further defined as banking business whose aims and operations do not involve any element which is not approved by the religion of Islam”. Today there are over 300 Islamic Financial Institutions operating in 75 countries with total assets exceeding USD750 billion and growing at an average annual growth rate of 15% - 20% (Bank Negara Malaysia, 2011). Apart from two countries namely Iran and Sudan, all the Islamic banks in the world today can be said to be operating side by side with conventional banking or in other words in what is referred to as a dual system. In the group of countries operating with the dual system Malaysia is said to be taking the lead with the world’s

first dedicated Islamic banking legislation called the Islamic Banking Act and also the world's first Central Banking Act to specifically acknowledge the existence of a dual banking system, conventional and Islamic. Islamic banking has been in existence in Malaysia since 1983. From basically one bank it grew to what is today. Today there are 17 Islamic banks in Malaysia operating side by side with 25 conventional Commercial banks and 15 Investment banks. Of the 17 Islamic banks, 5 are Islamic banks owned by Islamic banking groups whilst 12 are Islamic banks owned by conventional banking holding companies. At end 2006 Islamic banking assets represent 6.6% of total banking assets. This grew to 16.7% as of end April 2011. In terms of financing it grew from 6.2% to 18.4% whilst for the same period deposits grew from 7.19% to 18.6%. The average growth rate for the Islamic banking industry is estimated at 18% - 20% p.a. (Bank Negara Malaysia, 2011, p.1.).

Islamic banking have made its mark in Malaysia and captured the hearts and imagination of many. Borne of a desire for Muslims to have an alternative access to banking that is not riba in nature, Islamic banking in Malaysia grew into an adolescent ready to enter the adult world of banking. However, in spite of some progress achieved by Islamic bankers and Islamic banking in Malaysia there is an undercurrent of unhappiness with its achievements so far. There is unhappiness with the direction it has taken, unhappiness with the areas it did not cover, unhappiness it took many shortcuts in Shariah interpretations, and most of all unhappiness with the form it has taken which many see as just a mirror image of its conventional counterpart (Wong, 1995; Samad, 1999; Saiful Azhar, 2003; Asyraf & Nurdianawati, 2006; Engku Rabeah, 2006; Asyraf, 2008a & 2008b; Obiyatulla, 2008; Saiful Azhar, 2010). What is important in Islamic banking is for it to achieve its role to replace riba transactions. Many are reluctant to reconnect Islamic banking to its original source as a command

of Allah swt (Saiful Azhar, 2003, p.2, Asyraf, 2008a, 2). Being over circumspect in this matter, has led Islamic banking to be a shallow manifestation of its true potential. Without constant reminder to oneself and others who are the cogs in the Islamic banking machine of the principal reason for doing Islamic banking, the fight is detached and lacks commitment in resolve. Islamic banking should be the platform to begin the removal of riba from our lives (Ahamed Kameel & Larbani, 2006). After discussing the background of the study the next section will explain the Problem Statement.

1.2 PROBLEM STATEMENT

Most studies revolved around the comparison of efficiencies between Islamic banks and conventional banks and many conclude there are deficiencies in Islamic banking. The deficiencies are attributed to various reasons including wrong choice of products used, too much reliance on debt based products, and while complying with fiqh rulings not complying with Maqasid Shariah. This study will attempt to analyse the position of Islamic banking in a different perspective than normally done by previous researchers such as Radiah (1995), Wong (1995, p.2), Samad (1999, p.2), Saiful Azhar & Mohd Afandi (2003, p.2), Asyraf (2008a, 2 & 2008b), Hamim, Naziruddin & Syed M (2008), Sudin & Wan Nursofiza (2008), Taufiq, Shamsar & Bader (2009) and Hutapea and Kasri (2010). This study will look at Islamic banking from the point of view of the negative impacts of riba banking on its performance in a dual system like Malaysia. The definition of performance will not refer to the Islamic bank's profitability as such but more towards the Islamic bank not being able to be its true self or to fully comply with Shariah because of the existence of conventional banking in a dual system with Islamic banking. In other words situations where riba banking

prevents Islamic banking from being its true self or where riba banking forces Islamic banks in order to survive to adopt strategies or actions which are arguable or tenuous in terms of Shariah compliance. Shariah compliance here is defined as the Islamic banks being able to stick to the basic rules of Shariah in their products and operations. For example if in a Musharakah the basic rule says no partner should be given a capital guarantee against business losses then there should not be innovations that allow this. Further if *qabdh* (possession) is to be achieved before a purchaser can sell an asset bought this must be upheld strictly in all *Bai Bithaman Ajil* (BBA) transactions. In a Musharakah where all external risks are lumped only on one partner is also an example of non compliance with Shariah. In this study an act of the Islamic bank or an aspect of its product which seems alien to a natural understanding of basic Shariah principles is taken as breaching Shariah compliance.

The following is a list of the some of the major criticisms of Islamic banking which could be attributable to the negative impacts of riba banking.

- 1) Replication of conventional banking.
- 2) More expensive than conventional banking.
- 3) Not interested in microfinance.
- 4) Give financing mainly to big corporates just like conventional banks.
- 5) Encouraging ummah to take on more debts.
- 6) Over focusing on debt financing rather than equity financing.
- 7) Adopt conventional banking practice of wholesale transfer of risks to customers.
- 8) Islamic banks do not exercise restraint when customers in financial difficulty.
- 9) Financial engineering to turn equity products into debt.
- 10) Legal documents which enhance transfer of all risks to customers.

i) Not a declared objective to achieve Maqasid Shariah.

The explanation of the above problem sets the platform to frame the Objective of Study and the related Research Questions.

1.3 OBJECTIVE OF STUDY AND RESEARCH QUESTION

The main research objective is to examine to what extent riba banking system negatively impacts on the performance of Islamic banking in a dual system like Malaysia. Hence, the main research question is “What are the negative impacts imposed by the riba banking system on the performance of Islamic banking in a dual banking system like Malaysia”.

In order to identify the negative impact of riba banking on the performance of Islamic banking the researcher has identified five sub- research questions where there could be negative impact of riba banking on the performance of Islamic banking as defined above. These five sub-research questions are as follows:

- i) Is the Islamic bank disadvantaged in the competition for deposits with riba banks?
- ii) Is the Islamic bank hindered by riba banking from extending *Mudarabah* and *Musharakah* Financing?
- iii) Is the Islamic bank hindered from extending highly ethical financing products?
- iv) In terms of risk, is the Islamic banking sector influenced by risks which should be confined only to conventional banking?
- v) Are sukuk structures engineered to deliver conventional demands?

After discussing the Research Objective and outlining the Research Question the next section will explain the Scope of Study.

1.4 SCOPE OF STUDY

The study is conducted in a dual banking system like Malaysia. This means although the emphasis is on Malaysia, evidence will also be sought from other jurisdictions operating as a dual system like Malaysia.

The Islamic banking system is taken to include Islamic commercial banking as well as Islamic investment banking. Islamic investment banking will include Islamic capital market activities such as issuance of *Sukuk*. In fact examples from all facets of Islamic banking and finance which operates in a dual environment may be used in this study. The study shall use the term Islamic banking, and Islamic banking and finance, interchangeably, and shall also use the term riba banking and conventional banking, interchangeably.

The researcher will begin the study by describing the characteristics of an Islamic Economics system from available and established literature. Based on the parameters set by Islamic Economics on what an Islamic Financial system should be, such as no riba by legislation, and a *qirad* driven economic system, the researcher will suggest what a true Islamic Financial System will look like from the perspective of Islamic Economics. Once this is done the researcher will then suggest what form the Islamic banks and the Islamic banking system should be. The purpose of this approach is to provide a perspective of the true environment the Islamic banking system should be working in. Environment here is taken to mean whether it is operating singly or alongside another system, whether the nature of the economy it

operates in is based on Islamic principles or otherwise and similarly whether the laws of the nation it operates under is based on Islamic law or otherwise.

In addition the researcher will conduct an interview of peers and experts to see whether they agree the five situations mentioned above represents situations of the negative impacts of riba banking on the performance of Islamic banking. The researcher has made a decision to confine the research to a qualitative one instead of a quantitative due to the time constraint and the complexity and difficulty in operationalizing the concepts and reducing them to numbers that lends itself to a full quantitative study.

It will be apparent now that to answer such questions requires some understanding of the inner workings of Islamic banking and finance. Therefore this research could not open itself to the possibility of surveying the general public at large. The research would require a focused interview of peers in Islamic banking and finance and/or those who understand the workings of an Islamic bank i.e. existing and former Islamic bankers especially pioneers who worked in full-fledged Islamic banks, and academicians and scholars who have studied the subject well.

Although mindful of the fact that existing studies conducted so far do not specifically target the negative impacts of riba banking on the performance of Islamic banking the Researcher will also delve into such studies to find, if any indirect evidences exist of the negative impacts of riba banking on Islamic banks.

The results of the studies will then be analysed to see whether they support the proposition that riba banking is negatively impacting the performance of Islamic banking. With the scope of the study addressed the next section will outline the significance of the study.

1.5 SIGNIFICANCE OF THE STUDY

The study attempts to discover the negative impacts of riba banking on the performance of Islamic banking in a dual system like Malaysia. In particular it seeks to establish whether Riba banking prevents Islamic banking from fully complying with Shariah in its products and operations.

The study will help identify to the regulators the current problems of Islamic banking in a new perspective which will assist them in promoting Islamic banking further. The Islamic bankers will hopefully find in this study a voice that brings to the fore issues which they understand but was never articulated on their behalf before this. The consumers may enjoy the true aspects of Islamic banking which have not been offered to them through the Islamic Banks' preoccupation with competing with conventional banks on uneven terms. The minds of the academicians will be refocused to assist in finding permanent solutions for the woes of the Islamic banking industry now that a new perspective to the environment Islamic banking is working in is highlighted. The next section addresses the limitation of the research.

1.6 LIMITATION OF THE RESEARCH

This study is primarily a qualitative study analysing current literature for evidence supporting the research question and conducting extensive interviews with peers and experts on the subject. The group of peers and experts include some luminaries in Islamic banking in Malaysia generally covering founder, past and present Islamic bankers, experienced Shariah scholars, and well known academicians who write extensively on Islamic banking and finance with works published in International Journals. The researcher was unable to include regulators in the group due to the limited time constraints in conducting the study. The duality of the system is of

course not the only factor negatively impacting the performance of Islamic banking in particular its ability to fully comply with Shariah. It is beyond the scope of this study to quantify the contribution of each factor. The study limits itself to establish whether or not riba banking negatively affect Islamic banking in the manner described. The next section addresses the organization of the Dissertation.

1.7 ORGANISATION OF DISSERTATION.

Chapter 2 is organized in three sections. Section 2.1 deals with the theoretical framework based on current literature. In particular, it will describe the Halim Model and the Chapra Model of Islamic banking. This is followed by the researcher's comparison of both models. Section 2.2 deals with other current literature and focus on the other relevant writings on Islamic banking and finance. Within this section is a brief discussion of the major criticisms of Islamic banking and finance today. Section 2.3 deals with the researcher's own theoretical framework of Islamic banking and finance. Chapter 3 is organized in 4 sections. Section 3.1 deals with the research design explaining why the qualitative and interview method was chosen. Section 3.2 deals with development of the interview questions and outlines the research methodology. Section 3.3 describes the data collection whilst section 3.4 outlines the sample method followed by the chapter conclusion. Chapter 4 will begin with a discussion of evidence from the current literature in respect of the research question in Section 4.1. Section 4.2 deals with interview of peers and experts of Islamic banking. Section 4.2.1 describe the response rate of interviews. Section 4.2.2 tabulates the results of the interview. Section 4.3 discuss the findings for each question posed to the interviewees. Chapter 5 is divided into 4 sections. Section 5.0 discusses the summary of the research. Section 5.1 deals with the importance of the research while Section

5.2 describes other important findings of the research. Section 5.3 outlines the limitations of the research together with suggestions for future research.

CHAPTER 2

LITERATURE REVIEW

2.0 INTRODUCTION

This Chapter is organized in three sections. Section 2.1 deals with the theoretical framework based on current literature. In particular it will describe the Halim Model and the Chapra Model of Islamic banking. This is followed by the researcher's comparison of both models. Section 2.2 deals with other current literature and focus on the other relevant writings on Islamic banking and finance. Within this section is a brief discussion of the major criticisms of Islamic banking and finance today. Section 2.3 deals with the researcher's own theoretical framework of Islamic banking and finance.

2.1 THEORETICAL FRAMEWORK BASED ON CURRENT LITERATURE

2.1.1 The Halim Model

Islamic banking have to be located in the Islamic scheme of things in order to determine the Shariah framework for Islamic banking and finance (Halim, 2008). According to Halim, Islam is basically divided into three main branches, *Aqidah*, *Shariah*, and *Akhlaq*. *Aqidah* relates to all matters of faith in Allah swt, the Creator Muslims worship, His characteristics, our fundamental faith in Him and our belief in His commands. *Akhlaq* deals with the higher behaviour of Muslims, his character as required of him. *Shariah* are the rules Muslims live by coming from two principal sources, the primary and secondary sources. The primary sources will be the textual authority from the Quran and the Sunnah; whilst the secondary sources will be from

ijma', *ijtihad* and *qiyas*. According to the rules of *usul fiqh*, *ijtihad* is further refined into its various categories including, *istihsan*¹, *istishab*², *saddhara'i*³, *maslahah*⁴, and *'urf*⁵.

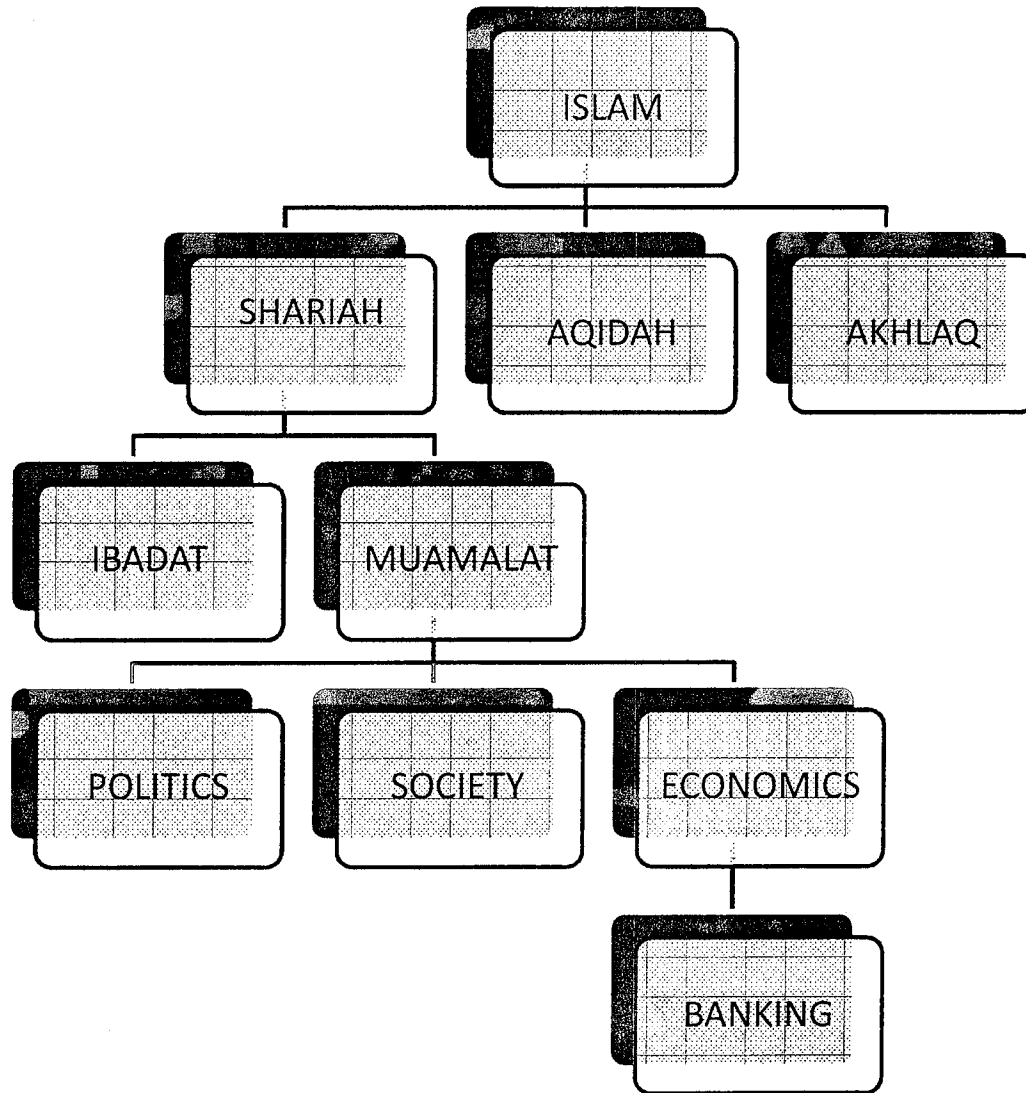


Chart 2.1: The Overall Halim Model

¹ Giving preferences to one of many conceivable solutions to a particular problem in the light of considerations of equity and fairness (Saleem, 2009)

² Presumption of continuity (Saleem, 2009)

³ Blocking the means to an unlawful act (Saleem, 2009)

⁴ Public interest (Saleem, 2009)

⁵ Customary (Saleem, 2009)