

## **ANALYSIS OF THE BASIC PRINCIPLES OF ISLAMIC ECONOMIC BANKING SYSTEM IN NIGERIA**

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### **ABSTRACT**

*The study examines basic principles of Islamic economic banking system, the work is to bring into focus viable methods by which an interest free banking will mobilize savings and idle funds of an economy and make them available for use without engaging into “riba” or (interest). The study put emphasis on the need to correct the impression not only throwing light on the alternative mode of carrying out banking system without interest, but also to analyze other aims and objectives of an Islamic economics and banking as an instrument of monetary policy in an Islamic economy, the study cover areas or an Islamic economics system which include its distinction from other ideologies (for instance, communism, capitalism) as well as the role of Islamic banking in an Islamic economic set tip.*

### **1.1 INTRODUCTION**

Having realized the fact that the so called “modern civilization” that rejects the guidance and directive of Allah in the social, political and economic life of the people is a direct challenge to the purpose of creation of man by the creator (which is to submit to Allah in all embankments) However, the work will concentrate on the sources of fund and method of loaning under Islamic banking system with all the efforts and the progress being made by some Islamic banks in Nigeria as well as some financial co-operations established for security of funds and the investment of businesses shall be looked into. Muslims today wish to quench their thirst for political and social orders through the original sources of Islamic ideologies which are, the Quran, the Sunnah of the last messenger Prophet Mohammed (SAW) and upon the historical experiences of the early Muslims. Efforts are being made in almost every area of individual and social life viz a viz literary, educational, political, socio-cultural, economic and technological to assess relevance of Islam and to find out ways and means of transforming this consciousness into socio-economic reality. The social discipline of Islamic economics which

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banking is one of branches represents one such creative response from Muslim economists and “ulama”<sup>1</sup>

The Shariah laid down a general principle learning the terms and conditions of a business contract or a commercial organ, so long as any contract of exchange does not outstrip, it is perfectly legal and valid. There is unanimity among the Muslim jurists that all forms of business contracts or bargains which any of the unlawful elements like “interest” (riba)<sup>2</sup> gambling etc are illegal and invalid.

The real issue, now is to analyze the modern banking system and it under the magnifying lens of Islamic principles to confirm its legality or otherwise. Looking at the modern banking system which is (interest) base, there is no doubt about the fact that its operations is un-Islamic, but the truth lies in the fact that banking plays a major role in development of an economy and of course there could be viable active mode of operation. Therefore, it is important to discover an interest free-based banking system that will comply with Islamic principles.

## **1.2 BASIC PRINCIPLES OF AN ISLAMIC ECONOMIC.**

The first basis principles of Islamic economics is that it does not see as in materialistic economic “live hood” as the fundamental problem of man and economic developments as the Ultimate and of human life.

As far as Islam is concerned, live hood and economic development are not more than just stages on man’s journey and his final destination lies beyond their destination and is the sublimity of character and conduct, consequently, the felicity of the other world.

Islamic does not deny the essentials of these two things (live hood and economic development), which are necessary for man’s worldly life. But as soon as they are seen as final destination, the very same means of live hood turn into an “allurement” or delusion into a trial and into a veritable foe.<sup>3</sup>

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<sup>1</sup> Afzalur Rahman, *Economic doctrines of Islamic Banking and Insurance*, the Muslim School Trust, London U.K. 1400H (1979) Pg. 16.

<sup>2</sup> Ibid

<sup>3</sup> A A Yusuf, *The translation of the Holy Quran*(Eliassi Family Book Service, India Rev Edition (2000) Q8 V28.

“Seek the other world by means of what Allah has bestowed upon you”

Another fundamental principles which has great importance with regard to the problem of the distribution of wealth is that according to elucidation of tile Holy Quran “wealth” in all its possible forms is a things created by Allah, and is in principles, His “properly”. The Tight of property over a thing, which accrues to man, is delegated to him by Allah. Quran says

“Give to them from the property of Allah which He has bestowed upon you”<sup>4</sup>

This is because all what man can do is to invest his labour into process of production, but Allah alone, arid no one else can course this endeavor to be fruitful and actually productive.<sup>5</sup>

“Have you considered what you fill? Is it you yourself who make it grow or we who make it grow” “Have they not seen that along the things made by Quran Hands we have created cattle for them and thus they acquired the right of property over them”<sup>6</sup> these verses throw ample light on the fundamental point that “wealth” no matter what its form is in principles “the property” of Allah (SWT) and it is He who has bestowed upon man the right to exploit it.<sup>7</sup>

Therefore, Allah has the right to demand that man should subordinate his exploitation of his wealth to the commandments of Allah. Thus, man has the “right of property” over the things lie exploit, but this right is not absolute or arbitrary or boundless it carries along with it certain limitation and restrictions which have been imposed by the real owner of the “wealth”. We must spend where He has commanded it to be spent and refrain from spending where He has forbidden us.<sup>8</sup> It is clear from the above that whereas in the conventional economics, problem of choice is greatly dependent on the things of individuals, they may not taken into consideration (lie requirements of society. But in Islamic economics the Muslims are not allowed to distribute their resources in any way they like. There is a serious moral limitations imposed by the Quran and the Sunnah on the powers of the individuals in this respect, for example, A Muslim is not allowed to invest in haram (Forbidden things) e.g. Brewery Company, Piggery forming, therefore in Islamic economics, not only the social individuals is study but also man with religious bent of man. Islamic economics is guided by the basic values

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<sup>4</sup> Q 24:33.

<sup>5</sup> Q 36:77

<sup>6</sup> Q 36:71

<sup>7</sup> Abu Dawud, Sunan Abu Dawud translated by Ahmad Hassan vol.3 (Labore Sh. Muhammad Ashraf, 1984) No.3585 of 1019.

<sup>8</sup> Q28:77

of Islam, while (the modern economy is based on capitalistic socio-economic framework greatly controlled by the whims of the individuals).

Again in modern economics the individual welfare is regarded as an increasing function of the commodities and services while he, according to his scale of values like to have and as a decreasing function of orts and sacrifice which he will have to make for their attainment. But in Islamic economics the individual must take into accounts the injunctions of the Holy Quran and the Sunnah in pursuing his daily pursuit or activities. In Islam social welfare is maximized the economic resources are so allocated that it is impossible to make any individual better off by any re-agreement without making any one or some others worse off within the network of the Quran and the Sunnah. In this way Islam harmonizes the money earning and money spending activities in such a way that they may promote welfare of the people. Thus, in one sense, Islamic economic is more restricted and in the other sense it is more comprehensive than modern economics. It is restricted because it is concerned only with those people who have faith in the oneness of Allah and His moral teaching as reflected in the Quran and the Sunnah.<sup>9</sup> It is also restricted because an Islamic state cannot encourage any and every economic, the activities which cannot promote human welfare and cannot be encouraged in an Islamic state, for instance, gambling and production of alcohol.

Islamic economic is comprehensive in the sense that it takes into cognizance of non economic factors like political, social ethical and moral. In essence it is like an applied economics, which also takes into cognizance the non economics factors. Here, we could distinguish between Islamic principles and capitalism which is theoretically and materialistic and gives man the unconditional and absolute right of property over his wealth, and allows him to employ it as he likes or deems fit. But the glorious Quran has adopted an attitude of disapprobation towards this theory of property quoting, the words of the community of the Prophet Shuaib (AS) they use to say “Does your way of salat command that we should forsake what our fore fathers worshiped or leave off doing what we like with our own property”.<sup>10</sup> These people used to consider their property as really theirs and hence the claim of “doing what we like” was the necessary conclusion of their position.

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<sup>9</sup> Abdal Al Ati, H. *The family Structure in Islam*, India. American Trust Publication, (1977) p.64.

<sup>10</sup> Q11:87.

But the Quran has in Suratul Nur, substituted “the property of Allah with the expression “Our possessions”<sup>11</sup> and has thus struck a blow at the very root of the capitalistic way of thinking, but at the same time, by adding the qualification “what Allah has bestowed upon you” it has cut the roots of socialism as well, which starts by denying man’s right to private property over them, similarly, thus they acquired the right of property, a verse in Suratul Yasin explicitly affirms the right to private property as a from Allah (SWA).<sup>12</sup> We can deduce from the above that Islamic economic principles is not per with capitalism which affirms an absolute and unconditional right to private property nor is it in support of socialism that totally denied the right to private property, rather it lies between these two extremes that is: Islam admits the right to property but does not consider it to be an absolute and unconditional right which is right bound to cause disorder, furthermore, one of the most important characteristics of an Islamic economy is the absences of interest bared transactions and the presence of a property functioning Zakkah system.<sup>13</sup> “The Zakkah system according to Islamic economics is regarded as a fundamental component of the Islamic economic order and the most important element of the social security system. On the issue of interest it has been explicitly stated in the Quran that trading is permitted but usury is prohibited or forbidden.<sup>14</sup> This principle is aimed at the betterment of mankind in all economic and spheres of life, from the above one can conclude that the modem economic system because of the fact that it fails to recognize or take cognizance the Holy Quran and the Sunnah injunction in particular that of riba (interest). Therefore, those who strongly believe in Islamic Ideology must search for an alternative free interest banking that will be in harmony with Quran and Sunnah injunctions, the objective of the Shariah is to promote the welfare of the people, which lies in safe guarding their faith, life, their intellect, their property and their prosperity. Whatever ensures the regard of these five (5) serves public interest and is desirable.<sup>15</sup>

Therefore, the aim of an Islamic economic system is to provide for an environment with a further realization of Islamic spiritual values in the visual, as well as in society, to provide for an adequate fulfillment of all its needs of life. In view of the statement made above and the goal of an Islamic monetary policy are:-

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<sup>11</sup> Al-Hilali, M.T. and Khan, M.M, Interpretation of the meaning of the Noble Quran (Saudi Arabia: Darul Islam, 1996) Q7:189

<sup>12</sup> Q 36:47

<sup>13</sup> Ismail R. Al-Faruq and Abdallah Umar Naseef. (Editors) Social and Natural Sciences the Islamic Perspective, King Abdul Aziz, University, Jeddah (1981)

<sup>14</sup> Q3:130

<sup>15</sup> Inquiry magazine, 1988—TopValley London. P. 13

i). Broad based economic well being with full employment and optimum economic growth.

ii) Socio-economic justice and equitable distribution of income and wealth.

iii) Stability in the value of money to enable the medium of exchange to be reliable unit of account a just standard of differed payments and a stable store of value.

iv) Mobilization and investment of saving for economic development in an equitable manner such that a just return is ensured to all parties concerned.

(v) Effective rendering of all service normally expected from the banking system.

## **2.1 ECONOMIC WELL BEING WITH FULL EMPLOYMENT AND OPTIMUM OF ECONOMIC GROWTH**

With the view of the Islamic Jurists to the fact that welfare of people and relief of their hardship is the basic objective of Shariah, this view would in the economic field, necessitate economic well-being through satisfaction of all human needs removal of all major sources of hardship, discomfort and improvement in the quality of life morally as well as materially.

Hence full and efficient employment of human resources would be an indispensable goal of the Islamic system because it would help realize not only the objective of broad based economic well-being, but also impart to human beings the dignity demanded by their status as Allah's vice gerents. Likewise, in the full and efficient employment of material resources which according to Islam are meant to be tapped from all resources in the heaven, and the earth for human welfare. (It is He who hath created for you all things on earth)<sup>16</sup> but while full employment and material well being are essential in an Islamic content, a high rate of growth is only essential to [lie extent that it contributed to full employment and broad based economic well being beyond this, its importance would have to be weighted against all its other moral and socio-economic implications. This is because the requirement to attain material property within the framework of Islamic values requires that it should not be attained through the production of in—essential or morally questionable goods and services not widen the social

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<sup>16</sup> Research Journal in Islamic Economics Banking System Vol.3 No. 1. King Abdul Aziz University Jeddah (1985). P42.

gap between the rich and the poor, and it should not have present or future generations by degenerating their moral or physical environment.

## **2.2 SOCIO ECONOMIC JUSTICE AND EQUITABLE DISTRIBUTION OF INCOME AND WEALTH:**

The equality of mankind in the sight of Allah does not need to be stressed here, for it abide in the Quran and Sunnah of the Prophet (SAW) when it has been mentioned that mankind is one from the same source and as such, their creator (Allah) only loves most, the one with *taqwa* (consciousness of Allah).<sup>17</sup>

Therefore, Islamic economic policy would see to achieve a just dealing between the employer and the employee as well as between supplier and the consumer.

## **2.3 STABILITY IN THE VALUE OF MONEY**

Stability in the real value of money is vitally important not only for the continued long-term growth of an economy but also for social justice and economic welfare<sup>18</sup> money being a measure of value, any continuous and significant erosion in its real value may be interpreted in the light of the Quran to be tantamount to corrupting the world because of the adverse effect. This erosion has on social justice and general welfare, which are among the central goals of the Islamic system. Therefore, any activity of individual or group or institutions, which significantly erodes the value of money, should be considered to be a national issue. But an exception to the strictness of it is that if there is an unavoidable conflict between the realization of these goals and a compromise becomes inevitable, then the goal of real value for money may be somewhat relaxed provided that the damage done by such relaxing is more than offset by the realization of oilier indispensable national goals. Hence it may be considered obligatory for the Islamic state to resort to healthy monetary fiscal and incomes policies and appropriate direct controls when necessary, including wage price controls to minimize erosion in the value of money, thus preventing one group of society from knowingly short changing others and violating the Islamic norms and values of justice in measures.

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<sup>17</sup> Ibid. p.34

<sup>18</sup> Q22:183

## **2.4 MOBILIZATION AND INVESTMENT OF SAVINGS**

Islam condemns hoarding of savings and demands their productive use for the realization of the socio-economic goals of Islam.

But it is not possible for each individual to employ his savings productively, therefore, it would be in the interest of the society in fulfilling Islamic teachings if efficiently organized financial institutions, “Should be properly equipped to be generally able to meet the genuine, noninflationary financing needs of both the public and private sectors for the realization of the economy’s goals”.<sup>19</sup> Moreover, since such institutions would not operate on the basis of *riba* (interest) but would be participating in profit or loss, they would need to be organized in such an efficient and diversified way that they are able to generate a positive net return for distribution for their depositors and shareholders.

## **2.5 RENDERING ALL SERVICES NORMALLY EXPECTED FROM THE BANKING SYSTEM**

An Islamic banking system had to develop a primary, and a secondary, money market, render all banking services to the public at least as efficiently as the conventional banking institutions and fulfill the non inflationary financial needs of the government. Because of the difference in the nature of the customer bank relationship between the Islamic banking system and the interest based banks, most of the services rendered by Islamic banks may have to evolve some different lines.<sup>20</sup> The development of both a primary and secondary market is essential for efficient mobilization of financial resources while the existence of primary markets is needed for providing finance resources to those who can employ them productively, the existence of secondary markets is essential to help savers and investors ‘liquify’ their investment wherever they feel the need to do so. The existence of an efficient secondary market in an equity based Islamic economy will be particularly important because its absence would induce savers to hold longer balances for precautionary motives, thus increasing hoarding and reducing the rate of economic growth by preventing savings from performing their natural role.

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<sup>19</sup> Afzahurrahman. Ibid p.32.

<sup>20</sup> Afzahurrahman, Ibid p.37

## **2.6 INSTRUMENTS OF MONETARY POLICY IN AN ISLAMIC ECONOMIC SYSTEM**

As pointed out earlier, while discussing the difference between an Islamic economy and the conventional economy, here in this case no policy can materialize in the mode which Islam laid down except the community allows Islamic ideology to penetrate both its private and public affairs. In other words, day-to-day activities of the society as well as that of the individual must be merged, and be controlled by Islamic ethics. Islam has provided the mode in which it expects the affairs of man either social, political or economic to be coordinated, this has to form the basis of organizing the Islamic policy.<sup>21</sup> Again, the state has to play a major role in watching the business activities in the society, making sure that it conforms with Islamic ideals, departing from the capitalist state when every thing is left to the control of market forces the Islamic state will come in to protect both the consumer and the producer where need be in order to make sure that they do not engage in anything that will be against the interest of individual or the state both morally and spiritually, either in the long run or in the short run. One of the most important instruments for the achievement of the objective of Islamic economic policy is the interest less based banking system.

## **3.0 ISLAMIC BANKING: A KEY TO THE ACHIEVEMENT OF MONETARY POLICY IN ISLAMIC ECONOMIC SYSTEM**

The central feature of an Islamic financial system is the absolute prohibition of the payment and receipt of interest. Thus, to bring economic system into closer accordance with the rules prescribed by Islamic law, banking system has to be restricted to conform with the restrictions on interest based financial transactions. As Islamic law, while rejecting the concept of a predetermined interest rate, permits an uncertain rate of return based on trade and profits, banks on an Islamic economy can strictly operate only on some type of profit and loss sharing basis, an Islamic banking system is essentially an equity based system in which depositors are treated as if they were shareholders of the bank.<sup>22</sup> Consequently, depositors are not guaranteed the nominal value, or a predetermined rate of return on their deposits; if the bank makes profits,

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<sup>21</sup> Research Journal in Islamic Economics Banking System. Ibid. p. 9

<sup>22</sup> Dr. Siddiqi M.N. paper presented at the economic Conference held in kano, (2018) Op.Cit. P.8.

then the shareholders (depositors) is entitled to receive a certain proportion of these profits. On the other hand, if the bank incurs losses the depositors are expected to share in these as well, and receive a negative rate of return. Thus, from the deposits perspective an Islamic commercial bank is in most respects identical to a mutual fund or investment trust. Furthermore, to remain consistent with religious structure, the bank cannot charge interest in its lending operations, but has to use special modes of investment and financing that are also based on the concept of profit and loss sharing.<sup>23</sup>

Consequently, profit sharing and equity participation are the principles, on which Islamic banks have to operate. In the Islamic system savings are mobilized through direct participation of savers in entrepreneurial activities, including banking, and surplus funds are loaned out in various forms of (religiously) approved transactions.<sup>24</sup> From the above it is very clear that the interest free banking can help not only in mobilization and investment of savings, but also in eradication of interest, by not accepting deposits for a fixed rate of return not lending out money on interest free, there by acting as a source of removing inflation and injustice being promoted by banking system based on interest. This will go a long way in reducing the risk of the entrepreneur that borrowed from Islamic bank will only need to add profit margin, unlike in the interest-based bank that has to force the entrepreneur to add profit margin as well as interest margin.

#### **4.0 ACHIEVEMENT OF MONETARY POLICY IN ISLAMIC ECONOMIC SYSTEM IN NIGERIA (JAIZ BANK PLC)**

A lot of achievements of monetary policy in Islamic economic system in Nigeria were recorded by bringing Jaiz bank plc in to board. Jaiz bank plc is a commercial bank licensed by the central bank to operate across the country.<sup>25</sup> The bank is in business of financial intermedium as other conventional banks, the only exception is that the modus operandi of the bank differs in how it mobilizes deposits and creates risk assets.<sup>26</sup> However, jaiz bank plc strategic business focus is mainly on retail banking, having due regards to a report published by Jaiz Annual General Report (JAGR) in 2006 which estimated the market for retail banking

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<sup>23</sup> Dr. Siddiqi M.N. Op.Cit. P.9

<sup>24</sup> M.Umar.Towards Monetary System, Islamic Foundation, Leicester, UK 1405H (19850). P. 46.

<sup>25</sup> Jaiz Operation Manual, p.8&9

<sup>26</sup> Jaiz Operation Manual, Ibid p.12

in Nigeria at thirty billion US dollars to some extent.<sup>27</sup> The bank is being positioned to be a national bank offering its services to all regardless of religious beliefs.<sup>28</sup>

Furthermore, jaiz bank plc is a bank in Nigeria operating under Islamic banking principles and is a non interest bank, it is the first non interest bank established and is headquartered in Abuja the capital city of the country,<sup>29</sup> as at 2012 the bank was a medium sized, financial services provider in Nigeria with a vision and values to be Nigeria premier wholly interest free bank providing efficient and innovative services to its customers, creating values for its shareholders and making a lasting positive contribution to society with a mission to strengthened co-ordination and partnership working in a whole system approach and is making life better through ethical finance, thus the need to create the opportunity for individuals and communities to take to take control of their own lives and towards a vision where all people are enabled and supported in achieving their full potential.<sup>30</sup> Finally, the aims are not more than to achieve better life and well-being for everyone and reduce inequalities.

## **5.0 CONCLUSION**

Banking being one of the most important financial institutions in any country plays an important role in collecting idle funds from individuals and institutions and loaning the same to the needy individuals as well as institutions, it is an institution that any progressive society cannot but encourage its development. Islamic community being an ideological nation where no room is allowed for anything that contradict the principles of the ideology (that is Shariah) is faced with the problem of finding alternative to the conventional banking which the operational system is based on riba (Interest) forbidden by both the Quran and the Sunnah.

Therefore, this work is a contribution to the basic principles Islamic Economic Banking system in Nigeria without going against the Islamic injunctions, it is also discusses the distinction between an Islamic economy and the conventional economy while the latter is based on secularism ideology the former takes its roots from the belief in the creator (Allah SWA) with an obligation to follow His commandments in all undertakings, in the same vein, the

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<sup>27</sup> Jaiz Annual General Report (JAGR), (2012), p.5

<sup>28</sup> Seminar Paper Presented by Mohammad Bin Ayyub in Jaiz National Conference Abuja, (2017), 7.

<sup>29</sup> Mohammed Bin Ayyub, Ibid p.12

<sup>30</sup> Mohammed Bin Ayyub, Ibid p.14

explanation on the aims and objectives of Islamic economy and how the banking system plays a vital role in achieving these aims and objectives and the objectives includes providing.

It is also clear that, due to prohibition of 'Riba' (Interest) by shariah in any form, the Islamic banking system is to be operated, on no other basis than profit sharing and equity for an environment for a further realization of Islamic spiritual values in the individual life as well as in the communal life; to provide for an adequate fulfillment of all basic needs of life participation. As such the operation of the bank shall involve investment activities rather than loaning with fixed return interest, in this instance the profits and risk arising from the money given out by (lie bank on investment shall be shared in an agreed rates; also the depositors will have no fixed rate of return on their deposits rather it will also involve profit and risk sharing where the deposit is intended for profit makings, because of the fact that most people cannot understand how the Islamic bank can be able to mobilize funds without engaging in interest.