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Can Islam Save The Economy?

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Governments worldwide are struggling to manage the global financial crisis, with no end to the downturn in sight. But at least so far, one sector has been unscathed: the $1 trillion-and-growing business of Sharia-compliant banking.

That's right, Sharia. The same combination of medieval Islamic law and modern post-colonialism that makes the terrorist clique supposedly so hateful of Western freedoms. Where finance is concerned, most muftis—Islamic religious scholars—agree that God prohibits charging any amount of interest on loans. Trading debt and risky speculation are off-limits too, as is investment in immoral enterprises like gambling, prostitution, and war profiteering. Transactions should be highly transparent and risk, as well as return, should be shared by all parties. You can't trap people into owing more than they can pay. Basically, most everything that caused the current mess isn't allowed. "Given their constraints, they actually don't hold any conventional debt or conventional mortgages," explains Samuel Hayes, emeritus professor of investment banking at Harvard. "They don't have any of these derivatives or outright subprime loans. There's no doubt that they have weathered this better than the conventional banks."

For a world in need of fast, creative solutions to a cascading crisis, might this financial subculture offer a way out? Duke University economist Timur Kuran calls for caution. "I think it's going to be a year or two before we have enough data to really know if it is the case that the banks are doing better and what explains it." One way or another, says Bill Maurer, an anthropologist at U.C., Irvine who studies alternative economies, "this is a really interesting moment for Islamic banking."

Sharia-compliant banks began appearing in the 1970s, but the concept dates to mid-century in South Asia and the Middle East, as Muslims newly independent from European rule sought to create an Islamic identity that would permeate all aspects of life, public and private. The first banks were small partnerships and development initiatives. In 1975, the Islamic Development Bank was founded by 23 Muslim countries (now 56), combining a World Bank-style mission with interest-free loans to member governments. It lent legitimacy and visibility to the approach. That decade's oil boom gave a jump start to a new crop of commercial Islamic banks, particularly in the Persian Gulf states. By the 80s, Pakistan, Sudan, and Iran were making efforts to Islamize their entire economies.

In the last decade, the industry has expanded dramatically. Dow Jones now offers an Islamic index for tracking halal businesses. Networks are growing among the religious scholars who sit on the banks' regulatory boards. The sharia-compliant line of financial instruments continues to grow, each known by its Arabic name: *takaful* insurance and *sukuk* bonds are already feeding the construction boom in the Gulf states. Islamic banks are opening across the Muslim diaspora, in places like London and Pasadena, California. Even big conventional banks are feeling the Islamic fever. Citicorp, Deutsche Bank, and HSBC have all opened Sharia-compliant subsidiaries. Recently, the British government has announced plans to issue *sukuks* of its own.

Meanwhile, governments that fear the power of Islamist movements, such as Egypt and Tunisia, have been reluctant to put their support behind the industry. There are some loose connections to radicalism. Sayyid Qutb, a hero of Osama bin Laden's, was an early advocate. In Iraq, Muhammad Baqir al-Sadr, the father-in-law of Muqtada, made important theoretical contributions on the Shia side of the movement. The fledgling Islamic banks in the United States have come under increasing official scrutiny since 9/11. But aside from the cadre of vigilantes whose sense of purpose depends on seeing a never-ending "Islamofacist" threat, observers agree that there's no credible link between these banks and Al Qaeda-type bad guys. Read the founding theorists of Islamic economics, in fact, and you'll find a decidedly pacifist tone.

A golden age, in theory

From the view of Islamic law, writes Umar Chapra, a leading economist in Saudi Arabia, "while economic growth is essential, it is not sufficient for attaining real human well-being." Rather, we depend on "spiritual health at the core of human consciousness, and justice and fair play at all levels of human interaction." Much more than a business model for specialty banks, he and many others believe that Islamic economics offers a much wider vision. The conventional view of the *homo economicus*—super-rational, selfish utility maximizer—dehumanizes people, denying the divine stamp on our nature. A truly Islamic economic theory, they believe, should restructure consumer preferences, ensuring that basic necessities are plentiful and luxuries come only after everyone is provided for. People should feel motivated to work by knowing that they share equitably in the produce of their labors. Sharia guidelines for inheritance distribute wealth among families in ways that prevents too much accumulation. More than an economics in the usual "dismal science" sense, this is a comprehensive rulebook for playing well with others. It also claims its authority from God.

The theory has something in mind for governments as well. They are responsible for administering the *zakat* tax, one of the Five Pillars of Islam. Though often translated as "almsgiving," it literally means "that which purifies." Though believers are encouraged to give over and above, the classical jurists developed a system of minimum annual requirements for a person's accumulated wealth. The rate of zakat varies depending on the resources one owns; it can range between 2.5% and 20%. These funds should be directed primarily toward redistributive purposes, to soften the market's burden on the poor. However, they can also be used to fund religious causes, a fact which medieval regimes sometimes used to usurp zakat funds for expansionary warfare. But modern Islamic economists, by and large, discourage military spending wherever possible.

The distribution of charitable giving is one of the many high hopes Islamic economists have for government. There is, in the literature, expectation for a kind of elixir effect. "The question of dishonest practices in the case of zakat is quite unexpected," writes the Pakistani economist M.A. Mannan, "because of zakat's religio-economic character." This, at least, is an impression they share with the Taliban and the ayatollahs: if you make the society religious in name and appearance, it automatically becomes religious in character. With corruption so widespread across the Muslim-majority world, it isn't hard to see the appeal of such a pious panacea.

Islam, the theorists believe, offers a distinct alternative to the other big-picture political economic options, capitalism and communism. By incorporating both markets and redistribution, they see it as the best of both worlds. After the two mega-ideologies spent the Cold War fighting over the allegiances of Muslim countries, the Soviet Union collapsed and now global capitalism is grinding to a halt as well. Islamists suspect that the reason Muslim countries remain impoverished is a fundamental incompatibility between these Western economics systems and the values that Muslim cultures hold dear. Now, perhaps, is the time for a third option to have its chance.

At the very least, suggests Boston University anthropologist Robert Hefner in a recent essay, these theories "provide a fascinating point of entry into the thoughts of Muslim leaders on global capitalism."

Are the fundamentals sound?

The most tangible outgrowths of Islamic economic thought, the banks, tend to be rather quiet about the visionaries' grand ambitions. Their spokespeople sound like bankers anywhere: optimistic, practical, and fond of jargon (in this case, specialized Arabic terms mixed in with the English vocabulary of international finance). By peppering business deals with the language of the Qur'an, the transaction seems to take on the endorsement of a higher power. Preachers play the role of advertisers by exhorting their congregations to purify their savings from interest. "Is 'Islam' merely a sort of brand name attached to products for marketing to a Muslim niche?" asks Bill Maurer in his book, *Mutual Life, Limited*.

If it is, the brand has its consequences. "In their investing options and the lack of diversification that they have to live with," Samuel Hayes says, Islamic investors "pay a price, no doubt about it." On a large scale, risk-sharing arrangements mean slower growth and, potentially, less short-run security for individual depositors. In one Muslim country, Jordan, the central bank has been reluctant to approve many new Islamic institutions for fear that they might add an unstable element to the bourgeoning financial industry. The banks that already do exist there have poor reputations. Because of cases like this, most observers doubt that Islamic finance will broaden its appeal beyond the pious. But according to Mohammad Ismaeel, the Director of Global Marketing for HSBC's Islamic arm, this may be changing. He claims that more than half of his bank's customers in the Asian market are non-Muslim Chinese. "They haven't come to us for Islamic reasons," he insists, "but because it is a sound financial product. They've taken it on for those reasons and those reasons only."

In the process of becoming competitive, though, Islamic banks may have lost some of the values they claim to be founded on. The theorists' original hopes for fostering more ethical consumer preferences hasn't taken hold in the banking culture. Bill Maurer, who has studied Islamic banks in South Asia and the United States, says these institutions aren't much different from other banks, despite some conspicuous signs of piety like prayer rooms and conservative clothing. Working at one doesn't mean joining a monastery. "A lot of the time," adds Maurer, "it's the same kind of drudgery and tedium that any old bank employee is dealing with."

Among those in the West who have been following the progress of Islamic finance, Turkish-born Timur Kuran is the most skeptical. "Endeavoring to implement Islamic economics," he writes in his book *Islam and Mammon*, both bankers and governments inevitably "recognize its unrealism." While the earliest experiments depended on genuine partnerships and risk-sharing, the bulk of today's Islamic transactions use instruments that differ only in name from what a conventional bank offers. In one of the most popular and long-practiced of these, *murabaha*, the bank buys an item for the client, who then in turn buys it from the bank, along with a premium that cleaves suspiciously close to the conventional interest rate. Religious scholars agree that the transaction is acceptable, even if the bank owns the item for just a millisecond. Pure in God's eyes, perhaps, but there is nearly no difference in economic terms. Kuran and others have also pointed out that during the medieval period, when the Sharia guidelines for commerce were developed, nothing resembling a modern bank existed. There was no legal provision for such an institution to outlive individual owners, as nowadays a bank of any scale must.

In light of the Islamic sector's competitive disadvantage, and even questionable adherence to its own ideals, Kuran advocates making its target audience more aware of the risks. Potential customers should know, he believes, that "its political importance and symbolic importance is more important than its economic essence." But symbols and politics are never far from the machinations of economy. One need look no farther than the vagaries of investor confidence or the political imperatives that shaped the bailout plan this past fall.

From constraints to creativity

Kuran nevertheless suspects that there is something to learn from the experience of Islamic finance and that the current crisis would be a good time to start. "It may be possible through Islamic banking, or something similar to it," he says, "to reach out to the subprime borrowing population in a safer way, in a way that makes the risks more transparent and allows better risk diversification." With or without the utopian theories, the constraints imposed by interpretations of a bygone religious law have given rise to a laboratory for different ways of doing business. Because of its religiously-obligated client base, Islamic banking remains insulated, in part, from the conformity that competition enforces on the rest of the financial industry.

Maurer agrees, but he doubts that anybody from the Federal Reserve will be calling up the muftis. "What I think will happen," he says, "is that people in the conventional finance world are going to arrive at things that may look more like Islamic banking as it has already been practiced." Advocates of Islamic finance will probably celebrate the change as triumph for their convictions, even if the resemblance is coincidental. "Depending on where you stand, they're right, or not."

Maybe it is time to get the muftis on the phone after all. In the United States, at least, religious leaders and politicians have deferred some of society's most pressing ethical concerns to the wisdom of the market. Calls that the "end of history" lies with neoliberal capitalism are being heard as far as the People's Republic of China. Not without reason, the 20th century's question of *why* free markets has been replaced, especially in the developing world, with *how* to get there. But last year's collapse is one more reminder that the market won't be our brother's or our sister's keeper for us. The shock waves of harm spread through global markets in ways that "love thy neighbor" doesn't seem to equip us for. Now is a good time to tinker with alternatives, and keeping an eye on models that already exist at the fringes of the global economy are a good way to begin. Peculiar conditions give rise to possibilities that couldn't develop on their own in the mainstream. Looking more closely at what Islamic economic thought has to offer, too, opens the door to more of the elusive "dialogue among civilizations" that leaders talk about but rarely do.

"Certainly asking questions about the ethical boundaries of finance is in order," says Ibrahim Warde, a professor of political science at Tufts University. There are any number of ways to think about economy in terms of right and wrong, but the Islamic case is different in an important sense. "Unlike other pockets of ethical finance," he points out, "it does exist in institutions," which are competitive enough to survive and available for study.

Warde makes sure to add, "We should not go overboard, though."

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