

Interest and its Role in Economy and Life (part 8 of 8): The Islamic Solution

Description: An Islamic solution to the interest model, and how economy can still thrive without interest.

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The Islamic Solution

The Islamic solution to the issue of interest rests upon two basic principles:

(1) If an individual wishes to lend money to another in order to help the latter, this act must be based on "brotherly principles" and it is absolutely unacceptable to charge any interest in such a case. It is not helping another individual to put him into a cycle of debt where he has to pay more than what they borrowed. This principle applies as well to Islamic international relations. If this important principle were applied today, countries would truly give "aid" and assistance to other countries, rather than sucking them into a pattern of dependency and debt burden.

(2) If an individual wishes to use his money to make more money, then he must be willing to put his money at risk. In other words, he cannot guarantee for himself a fixed return (whose amount keeps growing over time) regardless of the result of the investment that his money is used for. If he puts his money at risk, he is deserving of some share of the profits. However, this also means that he must accept losses if losses occur. This is a system that is based on justice. It also has numerous benefits to it. The one who invests becomes concerned about the results of his investment and cannot demand his "pound of flesh" regardless of what may occur to the debtor.

This Islamic solution works for individuals as well as for society as a whole. Banks are essentially financial intermediaries. They take money from those who have excess money (savings) and turn it over to those who need money for investment purposes. Interest is not necessary for such a system to work. The bank and its depositors (shareholders) invest, rather than simply loan, their holdings. The money is put at risk and the return to the depositors will be based on the amount of profits made in the respective investments. Under normal circumstances of a growing economy, if the bank is big enough and it diversifies its portfolio, the bank is virtually "guaranteed" a positive return on its total investments. Thus, those who invest their money with the bank will also receive a positive return on their money without it being guaranteed or fixed ahead of time.

Numerous "Islamic" financial institutions have been set up throughout the world today. They have been established on the principle of avoiding interest and some of them have flourished.[\[1\]](#)

Conclusions

For the most part, "modern civilization" has decided to turn its back on Divine Guidance (mostly due to the experience in the West with Christianity) and have attempted to construct their own economic systems, political systems, international laws and so on. When doing so, though, they have to admit that they are attempting something that is beyond their means. The social sciences are very different from the physical sciences. There are no labs in which humans can be entered to determine what may be the best results under different scenarios (and even that would have to assume that humans will always react the same under the same circumstances).

In the realm of economics, the first thing that may come to mind is the collapse of the theories of socialism and communism. One should, though, also take a closer look at capitalism and how far its reality is from what it is supposed to be. The early capitalist theorists envisioned a theory that would lead to "the best of all possible worlds."

However, their theories were based on assumptions that never were and will never be fulfilled. They assumed perfect competition, perfect knowledge, free trade and so forth. Once these assumptions are violated, which they inevitably are, they do not lead to the "best of all possible worlds." Instead, they easily lead to a world of exploitation, wherein the rich get richer and the poor get poorer. One of the driving forces behind this system is the institutionalization of interest.

God has blessed humans with the guidance of the Quran—a book that has been minutely preserved since its revelation. This book contains the guidance that humankind needs to lead a successful life in both this world and the Hereafter. It is therefore no surprise that this book absolutely prohibits and condemns interest in the strongest fashion.

Endnotes:

[1] For more details on the theoretical and practical workings of such institutions, see El-Gousi, pp. 199-247; Frank E. Vogel and Samuel L. Hayes III, *Islamic Law and Finance: Religion, Risk, and Return* (The Hague: Kluwer Law International, 1998), pp. 181-295.

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