

Islamic Finance and Business Ethics

Ralph Huenemann

(Notes for faculty seminar on 5 March 2012)

My Approach to the Topic: As the Chinese expression says, we make progress by “crossing the river by feeling our way from one stone to the next” (摸石头过河). Here are some of the stepping stones along my personal intellectual and experiential path to my current interest in Islamic finance and business ethics, about which I will make a few comments as an introduction to my seminar:

- *Memorizing the Heidelberg Catechism:*
- *Grappling with Psychopathy:*
- *Studying Marxism and Leninism:*
- *Meeting Naz Rayani:*

Islam in Historical Context: Islam can be viewed in the historical sequence of monotheistic, creationist, sacred text religions (my list may be incomplete):

- Judaism: Moses (ca. 1391-1271 BCE): Old Testament (Ten Commandments)
- Christianity: Jesus (ca. 7-2 BCE to 30-36 AD): Old and New Testaments (Beatitudes)
- Islam: Mohammed (570-632 AD): Quran (or Koran), dictated by Allah
- Mormonism: Joseph Smith, Jr. (1805-1844 AD): Bible + Book of Mormon
- Taiping Rebellion: Hong Xiuquan (1814-1864 AD): Bible + lost texts?
- Bahá'í: Bahá'u'lláh (1817-1892): varied writings, especially The Most Holy Book and The Book of Certitude
- Christian Science: Mary Baker Eddy (1821-1910): Bible + Science and Health with Key to the Scriptures

Each of these seven religions claims to know the fundamental Truth as given by Jehovah/God/Allah. The other six religions are sometimes characterized as less valid though not necessarily entirely wrong, and sometimes dismissed as heretical. But in each case the Truth was communicated through various human scribes/spokespersons. How do we deal with the question of human fallibility?

I can see at least five possible interpretations of this history:

- God exists, holds humans in special status (as compared to swine or earthworms), and keeps trying to give guidance to humans, with partial success.
- God exists, some of the scribes got closer to the Truth than others, and there are deep human disagreements about which scribes got it right. This has led to mixed results amongst the humans: some ecumenical tolerance, but some Holy Wars between religions (and deep schisms within).

- God exists, but doesn't interact with humans (an idea explored by Spinoza, Diderot, Thomas Jefferson, Einstein, etc.) I have found the following books useful:
 - Antonio Damasio, *Looking for Spinoza: Joy, Sorrow, and the Feeling Brain*, 2003;
 - Matthew Stewart, *The Courtier and the Heretic: Leibniz, Spinoza, and the Fate of God in the Modern World*, 2006;
 - Charlie Huenemann, ed., *Interpreting Spinoza: Critical Essays*, 2008; and
 - Philipp Blom, *A Wicked Company: The Forgotten Radicalism of the European Enlightenment*, 2010).
- God doesn't exist, but the various scriptures nevertheless contain useful insights on ethical behavior, to the extent that the scribes/prophets were wise people in their own right.
- God doesn't exist; therefore we have little basis for accepting any of the teachings, since all are based on human mythology/hallucination. Any valid ethical teachings must therefore be grounded in secular philosophy.

Islamic Finance in this Context: A fundamental aspect of Islamic finance is that the Quran forbids any interest on debt. [Is this the same as the Biblical critique of “usury”?] Islamic finance attempts to construct a complex, modern financial system without interest, debt, bonds, mortgages, etc. as normally understood.

Possible outcomes:

- Islamic finance will fail to deal satisfactorily with all the complexities needed for a modern economy.
- Islamic finance will provide for all the complexities, by developing new instruments that provide all the needs of a modern economy.
 - The new instruments are genuinely different from the conventional finance instruments, and therefore (because usury is avoided) Islamic finance is morally superior, as asserted explicitly by at least some of the Islamic scholars.
 - The “new” instruments are different in name only (“old wine in new bottles”), and therefore Islamic finance is neither superior nor inferior.

My sources on Islamic finance (so far):

- Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice*, 2007;
- Masudul Alam Choudhury, *The Universal Paradigm and the Islamic World-System: Economy, Society, Ethics and Science*, 2007;
- Hossein Askari, Zamir Iqbal and Abbas Mirakhor, *Globalization and Islamic Finance: Convergence, Prospects and Challenges*, 2010;
- Thorsten Beck, Asli Demirgüç-Kunt, and Ouarda Merrouche, “Islamic vs. Conventional Banking: Business Model, Efficiency and Stability,” World Bank WPS5446, 2010;
- Hennie van Greuning and Zamir Iqbal, *Risk Analysis for Islamic Banks*, 2008;

- Murat Çizakça, *Islamic Capitalism and Finance: Origins, Evolution and the Future*, 2011; and
- John A. Rees, *Religion in International Politics and Development: The World Bank and Faith Institutions*, 2011.

I welcome further suggestions.

Islamic Finance and Speculation: Basma Majerbi has shared with me two interesting marketing pamphlets for bachelor-level programs in “Islamic Banking and Finance” and “Islamic Financial Planning,” both offered by a new university in Kuala Lumpur, Universiti Tun Abdul Razak (est. 1998). It has AACSB and EFMD accreditation. The first pamphlet says: “The heart of Islamic finance lies in two defining principles, the prohibition of *Riba* (interest) and the sharing of profit and loss. These principles help to insure that funds are being channeled into real business activities as opposed to speculative activities.” (p. 4). On the next page the pamphlet describes the International Centre for Education in Islamic Finance (ICEIF), which “was set up by the central bank of Malaysia, Bank Negara Malaysia (BNM), to produce professionals for the global Islamic financial services industry.” (p. 5)

Interesting paradox: Bank Negara Malaysia carried out massive speculative activities in the early 1990s, leading to “mammoth foreign exchange losses” and the forced resignation of the Bank’s governor, Jaffar bin Hussein. See Laurent L. Jacque, *Global Derivative Debacles: From Theory to Practice*, 2010, pp. 41-45. I guess that, even in the Islamic context, one person’s immoral speculation is another person’s professional financial engineering!

The World Bank Dilemma: The World Bank borrows by means of interest-paying bonds sold to wealthy coupon-clippers (Swiss pension funds, etc.), and the Bank on-lends to Third World governments to finance development projects (again, interest is paid). How does a devout Muslim like Zamir Iqbal work for the World Bank?

The AACSB Dilemma: AACSB insists that to be accredited as a first-rate school, a business school’s curriculum must include—and demonstrate success in teaching—lessons in business ethics. But AACSB in fact accredits programs that are based on various conflicting religious foundations (including, for China, the secular religion of Marxism-Leninism-Maoism-Dengism). If one law school teaches the principle “innocent until proven guilty” and another law school teaches “guilty if the Monarch/Party/Leader says you’re guilty,” would a law school accreditation agency be equally happy with both, as long as both schools paid their membership fees? What if one science department teaches Creation and another teaches Evolution? Are both curricula equally legitimate? Is teaching the same is preaching, or is there an important difference between them? Does excellent teaching mean “teaching the Truth,” or does it mean “teaching whichever perceived truth is authorized on your campus,” or does it mean “helping students think for themselves”? How does AACSB answer these questions? Or does it skirt the issue, perhaps out of fear of losing lucrative fees from one subset of potential members or another?

The Gustavson School Dilemma: We already teach finance, and ethics, among other topics. And we meet the AACSB standards. But, in my judgment, the AACSB standards set the bar much too low. And, in AACSB terms, “assurance of learning” in ethics is mostly form, very little function. How can we do better for our students? Specifically, how do we help our students deal with the assertion that Islamic finance is morally superior to conventional finance?

P.S. I have found the following items extremely helpful in exploring the current status of ethics in economics and finance:

- Daniel Kahneman, *Thinking, Fast and Slow*, 2011.
- Robert R. Locke, “Reform of Finance Education in US Business Schools: An Historian’s View,” *Real-World Economics Review*, No. 58 (2011), 95-112.
- Peter Radford, “Ethics in Economics—Where Is It?,” *Real-World Economics Review*, No. 58 (2011), 2-8.