



## A study of “Islamic Banking” as an ethical alternative to conventional banking system with special reference to its prospects in Patna

• Anam Fatima • Vaishnavi Bharti • Sonali Anand  
• Soofia Fatima

Received : November 2013  
Accepted : March 2014  
Corresponding Author : Soofia Fatima

**Abstract :** India with a 13% Muslim population, the highest in a Non Islamic Country and second highest in the world, is still a financially neglected lot ([www.academia.edu](http://www.academia.edu), 19<sup>th</sup> Sept., 2013). The size for Islamic Bank will be very large as the Indian population is above 100 crores and Muslim population itself is about 15 crores and on the name of religious faith, they are looking for interest free banking and finance system. Islamic Banking is a banking system which is based on the principles of Islamic law with three main objectives - abstinence from interest, profit and loss sharing and ethical investment. This banking system is running successfully around the globe in

many countries with proper amendments in their respective laws.

In India, Islamic Banking system will serve, as a powerful effective tool to address the problem of poverty and unemployment. It will act as an ethical alternative to the conventional banking system. Small traders and petty entrepreneurs who could not avail credit facilities from commercial banks due to burden of heavy interest rates, can enjoy the facilities of interest free banking and open up to new ventures. It will be a boon for a state like Bihar which is financially less developed. Islamic Bank is open for all, whether a Muslim or not. It is evident from the fact that 40% of the clients of Islamic Banks are Non Muslims in Malaysia ([www.dnaindia.com](http://www.dnaindia.com), 30<sup>th</sup> March, 2012). Out of the 110 respondents surveyed in Patna region, as high as 64% strongly feel that Islamic banking will be a boon for our nation and will foster economic development. It will also lead to large inflow of funds and help in income disparity reduction. As per the present RBI guidelines, however Islamic banks cannot fit into our financial framework until and unless proper amendments are made in Banking Regulation Act 1949.

**Key words:** Islamic Banking, Interest Free Banking, Ethical Investment.

### Anam Fatima

B.Com. III year, Session: 2011-2014,  
Patna Women's College, Patna University, Patna,  
Bihar, India

### Vaishnavi Bharti

B.Com. III year, Session: 2011-2014,  
Patna Women's College, Patna University, Patna,  
Bihar, India

### Sonali Anand

B.Com. III year, Session: 2011-2014,  
Patna Women's College, Patna University, Patna,  
Bihar, India

### Soofia Fatima

Head, Department of Commerce,  
Patna Women's College, Bailey Road,  
Patna – 800 001, Bihar, India  
E-mail : [soofia.fatima@gmail.com](mailto:soofia.fatima@gmail.com)

## Introduction :

A study of “Islamic Banking” as an ethical alternative to conventional banking system with special reference to its prospects in Patna is a study to explore the potentials of Islamic Banking sector as an ethical alternative to conventional banking system.

Islamic banking refers to a system of banking that is consistent with the principles of the Shariah (Islamic rulings) and its practical application through the development of Islamic economics (en.m.wikipedia.org, 2<sup>nd</sup> Oct., 2012). The principles which emphasize moral and ethical values in all dealings have wide universal appeal. Shariah prohibits the payment or acceptance of interest charges (riba) for the lending and accepting of money, as well as carrying out trade and other activities that provide goods or services considered contrary to its principles. While these principles were used as the basis for a flourishing economy in earlier times, it is only in the late 20<sup>th</sup> century that a number of Islamic banks were formed to provide an alternative basis to Muslims, although Islamic Banking is not restricted to Muslims (www.theislamicbanker.com, 13<sup>th</sup> Aug., 2013). Islamic Banks over the years, have developed a number of financial instruments for their functioning. These financial instruments broadly fall under two groups: Profit and Loss Sharing Arrangement and Non Profit and Loss Sharing Arrangement. The profit and loss sharing arrangement includes MUDARABA, a form of investment partnership between a bank and a business that shares the risk and profits between both parties at pre-agreed levels, MUSHARAKA is a partnership, normally of limited duration, formed to carry out a specific project, MUQARADA, investors who buy muqarada bonds take a share of the profits being financed, but also share the risk of unexpectedly low profits, or even losses. The Non Profit And Loss Arrangement includes MURABAHA, a form of cost-plus or mark-up

financing where an asset is acquired by the bank and sold to the customer, IJARAH, leasing involving the rights over the use of an asset under which the bank buys the asset then leases it to the customer over a fixed period in return for a pre-agreed monthly price, SALAAM, a kind of forward sales contract which requires the buyer to pay in advance for that are to be supplied later (www.qib.com, 9<sup>th</sup> Sept., 2013).

Islamic banking has the same purpose as conventional banking, except that it operates in accordance with the rules of Shariah known as Fiqh-al-Muamalat (Islamic rules on transactions).

Our research study aims to ascertain the level of people’s awareness regarding the fundamental understanding of Islamic Banking in India, with special reference to Patna, and to ascertain its impact on the socio-economic conditions of the Muslims, especially low and middle income group entrepreneurs, who have not yet been given any credit assistance from commercial banks.

## Objectives :

The pivotal objectives of our research are enumerated below-

- (1) To develop fundamental understanding of Islamic Banking.
- (2) To study the prospects of Islamic Banking in our Economy.
- (3) To study its impact on the socio-economic condition of the marginalized section of the society.
- (4) To study as to how Islamic Banks can help tackle Financial Exclusion.

## Hypotheses :

The hypotheses of our research are-

- (1) Islamic banking will serve as a boon to the financially excluded class.
- (2) It will attract the muslim investors who generally abstain from investing due to religious bindings of interest (riba).

- (3) Islamic Banking will emerge as an ethical alternative for conventional banking system.

### Methodology:

In our project, we collected the data using two sources, namely primary sources and the secondary sources.

*Primary source include :*

- (i) Survey based on structured questionnaire
- (ii) Personal Interview conducted from the people of Patna
- (iii) Interview of the officials of Sahulat Micro Financing Society, Ali Nagar, Patna

*Secondary source include :*

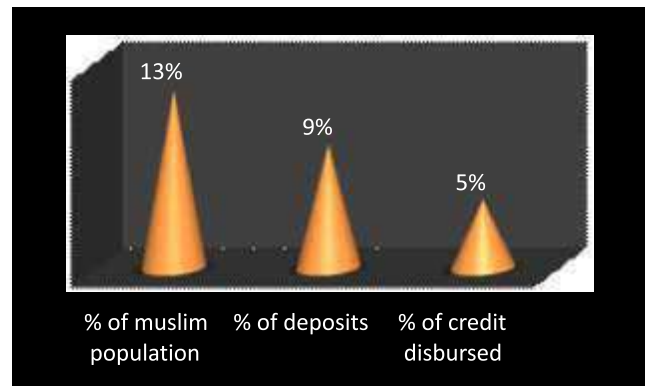
- (i) Books
- (ii) Journals
- (iii) Newspapers
- (iv) Magazines
- (v) Internet Websites

We conducted our study among 74 Muslim and Non Muslim Investors and 36 Entrepreneurs in Patna region. The research instrument used by us was Snow Ball Random Sampling method.

### Findings:

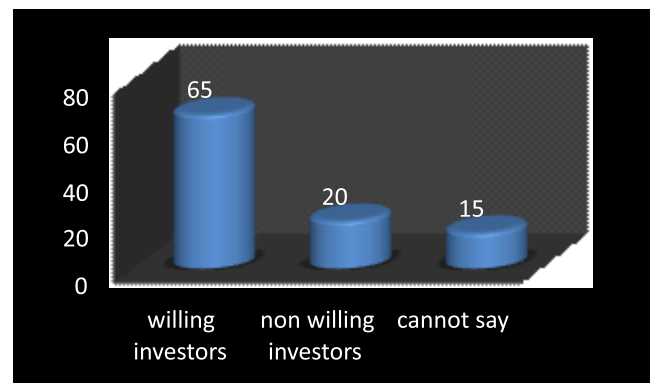
India has 13% Muslim population out of its total population and a maximum proportion of it falls under financially excluded class due to many reasons. The primary among them are lack of credit facility and abstinence from interest based banking. RBI has estimated that only 9% of the Muslims have bank accounts while credit disbursement is as low as 5% of the Indian Muslims.

We see that if Islamic banking is introduced in India it will serve as a boon to financially excluded class.



In our survey conducted at Patna region, out of the total 110 respondents, 65% are willing to invest with Islamic Banks if introduced in Patna (fig 2).

As the religious bindings of interest (riba) abstain muslims from investing, the survey proves that people are willing to channelise their savings with the help of Islamic Banks which will induce flow of money into the Indian market.



Questions	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Will Islamic Banking help in alleviating poverty? (fig 3)	51	27	6	9	7
Can Islamic Banking promote sustainable development? (fig 4)	14	25	27	24	10
Will Islamic Banking provide employment opportunities? (fig 5)	44	39	2	8	7

Small traders and petty entrepreneurs who could not avail credit facilities from commercial banks due to burden of heavy interest rates, can enjoy the facilities of interest free banking and open

up to new ventures. It proves that Islamic banking will provide credit facility to low income muslim entrepreneurs as the primary aim of Islamic Bank is to help the needy. Thus the last hypothesis finds its way here that Islamic banking will emerge as an ethical alternative to conventional banking system.

The findings of the research study clearly depict all the three hypotheses have been proved.

### Conclusion :

While concluding our project, we came to know that Islamic Banking System can be proved highly advantageous to the Indian economy; but the authorities need to evaluate its prospective importance and then recommend a proposal to the Union Government for making necessary amendments in relevant sections of Banking Regulation Act 1949 to ease its establishment and allow its functioning under effective and continued surveillance for protecting national interest too.

### Suggestions:

- The functioning of Existing Islamic windows and NBFC can be checked and their suitability and profitability can be evaluated for the Indian Market. Then the Government with proper amendment in the Banking Regulation Act 1949, can establish full fledged Islamic Banking System.
- India needs to follow the UK example and introduce new laws to govern the Islamic Banking business (www.alislam.org, 13<sup>th</sup> Aug., 2013).
- More effort is required in the area of training and education; the State can play a pivotal role in promoting this subject by including it in the curriculum of professional courses.
- The myth that Islamic Banking is only for Muslims must be dispelled, and awareness of Islamic Banking as an ethical alternative form of banking should be created. Public seminars and discussions are a good way to do this.

### References :

#### Books and Journals :

'Microfinance' ; By Sahulat Microfinancing Society, Ali Nagar, Patna.

Islamic Finance on Economics (Islamic Magazines, Periodicals and Journals, 21<sup>st</sup> March, 2010).

#### Newspapers & Magazines :

Ramavarman T., "Kerala's Islamic NBFC to launch venture capital fund," *The Times of India*, 18.12.2013.

*Economic Times*, 5<sup>th</sup> February, 2008 on 8<sup>th</sup> Oct., 2013.

Kumud Das, "Raghuram rajan report advocates introduction of islamic banking.", *Financial Express*, 4<sup>th</sup> September, 2008 on 13<sup>th</sup> Aug., 2013)

#### Websites :

[http://www.academia.edu/5132939/islamic\\_Banking\\_in\\_India\\_What\\_more\\_Needed](http://www.academia.edu/5132939/islamic_Banking_in_India_What_more_Needed) (19<sup>th</sup> July, 2013).

[http://en.m.wikipedia.org/wiki/islamic\\_banking](http://en.m.wikipedia.org/wiki/islamic_banking) / (2<sup>nd</sup> Oct., 2013).

[http://www.dnaindia.com>Analysis/\(March 30, 2012\)\(8<sup>th</sup> Oct., 2013\).](http://www.dnaindia.com>Analysis/(March_30,2012)(8thOct.,2013))

[http://www.qib.com.qa/en/footer/islamic\\_banking/islamic-banking-tools.aspx](http://www.qib.com.qa/en/footer/islamic_banking/islamic-banking-tools.aspx)(9<sup>th</sup> Sept., 2013).

[http://www.alislam.org/library/articles/islamic\\_Banking\\_in\\_the\\_UK.pdf](http://www.alislam.org/library/articles/islamic_Banking_in_the_UK.pdf)(13<sup>th</sup> Aug., 2013)