

**SPEECH BY THE HON TUN DR MAHATHIR BIN MOHAMAD AT THE UAE UNIVERSITY  
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“The Role of Islamic Financial Institutions in Developing the Economy”**

I would like to thank the UAE University in Dubai for this invitation to speak on “The Role of Islamic Financial Institutions in Developing the Economy”. You must know that I am not a financier or even an economist. My brush with finance came from having to manage my country’s financial affairs when I was Prime Minister and Minister of Finance ad interim. For this I relied on my experience of my own personal finances – which is based on the very simple dictum, “neither a borrower nor a lender be”. I just did not want my country to borrow. If it must borrow, then borrow what it can pay. If not it must live within its means. I had read and seen too many countries overspending, getting into debt and placed under the power of the lenders. I did not wish that to happen to Malaysia while I was its Prime Minister.

Malaysia is not a big oil producer with an inexhaustible reserve. It is a trading nation, dependent on the world market. And the world market can never be stable. It must therefore always be prepared for a rainy day as the saying goes. In Dubai a rainy day is probably not such a catastrophe. Being prepared means having sufficient savings or reserves, to be used when needed. And now I will try to talk about Islamic finance, or what little I know about it. There is hardly anything written about Islamic finances in the period of the glorious Islamic civilisation. What we do know however is that before Islam there were debt slaves, the borrowers of money who, unable to pay back their loans, became slaves of the lenders. And they lived miserable lives.

This was because before Islam usury was common, the lenders living on the business of lending money on fixed return, i.e. on interest. The rates, usually calculated on a monthly basis were very high, often one-fifth of the amount lent. At such high rates of 20% per month, or 240% per year most borrowers would not be able to pay. They would end up being debt-slaves of the lenders, for whom they had to work for the rest of their natural lives, trying to earn enough to repay in order to discharge themselves. Large numbers of people would be made debt slaves because of this system. Their misery and that of their families can well be imagined.

To appreciate the cruelty of these money-lenders we have to read Shakespeare’s, “Merchant of Venice” in the absence of any literature written by Muslims regarding this usurious practice. In the play the borrower had agreed to pay with a pound of his flesh if he failed to settle his debt. When he failed, Shylock, the money-lender wanted to cut out the man’s heart as the pound of flesh that was due to him. That the man would die as a result did not seem to bother Shylock. Such was the perception of usurious money-lenders among Europeans during the time of Shakespeare.

It was this perception of money-lenders that resulted in the persecution of the Jews in Europe throughout the ages. But the ethnic Europeans soon learnt what a lucrative business money-lending was. They then started their own banks and they refined usury, introducing what they called new products, which may have made banking more respectable. Despite this and the lowering of interest rates, many people and many countries still suffer because of the inability to repay and so remaining debtor forever. To protect the lenders, the banks, from losses from non-payment of debts, in place of slavery, most countries provided laws for bankrupting the borrower. Once bankrupted the borrower would be forced to work and earn money which, apart from a small sum needed for basic sustenance for himself, would be used to pay off his debt. If his earnings are small he may have to spend the rest of his life a bankrupt, hardly able to keep body and soul together. Even though he may not be owned like a slave by his lenders, he is no better than a slave.

It is the same with Governments which borrow money for whatever purpose. If the Government fails to pay up or to service the loans, then the management of its finances and its economy would pass to its creditors or the powerful institutions like the IMF and World Bank. A big portion of the country's earning would go towards paying the interest and the principal. Some debtor countries use as much as 85% of Government revenue to pay the loans. To ensure payments international agencies such as the IMF would literally take over the management of the country's economy. Effectively the country has lost its independence. Effectively it is a colony of the lenders.

This used to happen to the Malay states in the past. Because of the profligate ways of the rulers of the states debts were incurred with neighbouring countries like Siam. Unable to repay, the Malay states had to accept financial advisers appointed by the Siamese Government. From that stage to becoming a vassal of Siam was a short step. To release themselves from their Siamese overlord, the Malay states, including my home state of Kedah, had to accept British protection. Effectively this meant becoming British colonies.

Thinking Malaysians cannot forget this. Borrowing beyond our capacity to repay can result in our being debt-slaves to other nations, becoming in fact colonies of other nations. To remain free we have to manage our finances well. We have to live within our means. If we want to live well then we must work hard and create enough wealth for us to spend. This is not always possible. As with individuals, Government will one day find a need to borrow.

But despite good financial management we can still be made impecunious and have to borrow. When the rogue currency traders devalued our currency, our debts suddenly ballooned. Where we had to find Ringgit 2.5 to pay a debt of 1 USD, at the height of the financial crisis we had to find 5 Ringgit, i.e. twice the amount of local currency in order to pay a debt of 1 USD. Suddenly we became very poor and ran the risk of becoming debt-slaves of our lenders despite our careful management of our finances.

Countries, like people, need to borrow. Even the richest countries need to borrow. If you are a world power like the US then you can go on spending borrowed money forever. You don't have to pay because your lenders dare not bankrupt you. We know if a man cannot pay his debt of 1 million dollars, he would be in trouble. If he owes 1 billion dollars and he cannot pay then his bank would be in trouble. The US is not in trouble despite owing the world 8 trillion dollars. If it is bankrupted, it and the lenders would lose all their money. Even today they have already lost a third of value of the money they lent the US.

But even when the currency is not devalued, borrowing foreign funds exposes the country and the individuals to great risk. One of the things that contributed to the Asian financial crisis was the borrowing of large amounts of foreign currencies by private business in the developing countries. The currency traders predicting that the borrowers would not be able to repay the loan, declared that the economy is unsound. They then claim that the value of the local currency is much lower than the current value. To make sure that what they say is right, they short sell large amounts of the currency and so depreciate it. They can then buy the depreciated currency to deliver to the buyers they sold to earlier and make large profits. With their currencies depreciated the Government and the private businesses of the target country would have difficulty paying foreign currency debts or paying for imports.

During the Asian Currency crisis the debtor countries had to borrow from the IMF to repay loans and finance imports on condition they submit to supervision by the IMF, an extension of the US. This means that the country would lose some of its independence. But we cannot just abolish interest? Would anyone lend money without expecting to make some profit from it? Some probably would. Rich devout Muslims have been known to keep money with commercial institutions and refuse to collect interest. But the institution, even if it has no need to give interest or any return would still incur a cost when keeping the money. It would have to make use of the

money kept with it. And usually it lends out the money charging a fix interest. The depositor would be helping un-Islamic loans. If the lender cannot charge interest and the borrower defaulted or failed in his business or whatever, then the lender would suffer. Islam does not intend that those who abide by its injunctions would suffer.

Some have tried to get around this injunction by imposing a small service charge. If it is truly a service charge, i.e. it is the exact amount that the lending institution has to expend to manage the loan, and then there would be no profit at all for the institution. This could actually result in a loss. If the loan turns bad then the institution would lose the amount lent completely or partially. Since it is not making anything from the service charge, it follows that over time the funds of the lender must diminish as non-performing loans increase.

If we also take into account inflation, the funds held by the lending institution would, in purchasing power terms, diminish further overtime. Money lending without interest, even if there is a service charge will simply not be viable. In which case, no one would want to be in the money-lending or banking business. Yet we must remember that borrowing money under certain circumstances is an absolute necessity.

Realising this, it is imperative that Muslims devise a way of lending which would not hurt either the borrower or the lender. This can be done if both borrower and lender share the risks. How risk is to be shared will of course be based on certain principles which should include the degree of risks the lender is exposed to. For high risks cases the lender may take a bigger proportion of the returns from the enterprise, but where the risks are minimal or absent the borrower should have a bigger proportion of the returns.

In a majority of the cases the cost of money would be higher than the cost due to interest rates. But then the borrower would be less subject to the kind of punishment meted out to bankrupts. He certainly would not be made to spend the rest of his life working for the lender. In the case of Governments borrowing under Islamic banking, the same thing would apply. The country would not be bankrupted but the lender would get some return if the terms of the loans are prudently negotiated. Today Islamic banking has developed new instruments in order to compete with usurious banking and to provide better alternatives. As a result Islamic banking has become more attractive. Since its introduction Islamic banking has grown considerably and the systems have become more standardised.

Today the Muslim world is flushed with money. There is enough for them to provide loan facilities which would be competitive. Islam teaches us that apart from "fardhu ain", the compulsory observances which each one of us must perform for our own salvation; there is "fardhu kifayah" which a community must provide for the salvation of all the members of the community. Failure to perform "fardhu kifayah" will, as we all know result in every member of the community being guilty of committing a sin. If our community suffers because we fail to provide for the shariah compliant financial needs of the community then we cannot claim to have fulfilled our obligations according to the teachings of Islam. We would be sinning more because we have so much capacity now to provide for the financial needs of the community.

Where possible we should share our wealth with the poor and the needy, whether individuals or countries through acts of charity. If we consider that we are all members of the ummah, the community of Muslims in the world, then it is imperative that we do this. But if we cannot donate money as charity we must provide for Islamic loans to take care of the needs of the Muslim ummah and to protect them from having to resort to usurious borrowing.

The means and the systems are there. It is for us to decide whether we should apply our wealth, bestowed upon us by Allah s.w.t. in accordance with our religion or not.

And so what is the role of Islamic Financial Institutions in Developing the Economy. The main role is to provide an alternative source of loans to that provided by the usurious banks. If there is no choice, if there are no Islamic banks or other financial institutions, then Muslims will have to borrow from the fixed interest banks. But today there should be no reason why there is no Islamic bank anywhere. If there isn't, it is because the authorities in an Islamic country or a non-Islamic country do not allow for Islamic banks or institutions to be set up. I will not pass judgement on anyone if such facilities are not available in Islamic countries. As usual interpretations regarding the teachings of Islam differ from place to place and between different sects of Muslims. So there must be a reason why Islamic banking is not available in some Islamic countries.

For the development of an economy it is possible to depend on legitimate revenue collected by a Government. There is no doubt that countries endowed with rich resources can do without borrowing. But for most countries, Muslim or non-Muslim loans are needed to finance development. As has been pointed out borrowing from usurious foreign sources may end up with the country becoming a kind of debt slave to the lenders. If Islamic sources practising Islamic injunctions against riba are available, Islamic countries wishing to develop should depend on these sources.

What if there is little or no expectations that the loan would be repaid. The best thing is not to go ahead with whatever economic development project that the loan is supposed to finance. If Muslims who are rich believe in charity, then they should provide funds for such non-viable needs, e.g. to pay for food for starving people, of which so may are Muslims. But if the borrowing is for some viable project which will give a return over a short or long period, then Muslim banks must undertake to finance the project if the project would stimulate the economy and give higher revenue for the Government which can slowly repay the loan taken. The Muslim banks can share ownership of the facility if it can earn an income sufficient to repay the loans.

The share of the Islamic institution can be fractional, or any percentage up to 100%. The Islamic bank should help with the project management or should manage the facility by itself if it has majority share or total ownership. If there is no Islamic bank in the Muslim country then it must be prepared to allow a Muslim bank from another country to finance and manage the facility until it becomes viable and is able to defray the loans. This is no different from borrowing from any foreign banks or institutions. If for example an airport is needed in order to increase revenue from tourism, then an Islamic loan can be used with the lender taking up various percentages of the cost of the airport and where necessary undertake to manage the airport.

By itself the airport even if it is a basic utilitarian facility, may not be able to earn enough to repay the loan. But the Government may earn more from tourism. The Government can then pay for the facilities to support earnings from airport operations, to repay the loans and to eventually own it. There are various permutations of Islamic loans which can be applied. The rich Muslim countries should consider it their duty to the ummah to provide Islamic banking facilities to save Muslims from any form of debt-slavery that can be the result of borrowing from usurious financial sources.

Truly there is no reason now why Muslims and Muslim countries cannot have access to Islamic finance for whatever needs. The skills in the management of Islamic banking have already been developed. And so are the skills in project management and in the management of facilities in order to get maximum return. All that is needed is the will, the political will, and the honest belief and commitment to the teachings of Islam. No Muslim country need to be poor and undeveloped today if we think of ourselves as the community of Muslim, the Muslim ummah and not as nation states concerned only with the state and nationals of the state. Insha'Allah if we help the ummah to prosper, we all will prosper. In Islam we are our brother's keepers. And Muslims are brothers of each other.