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AT THE INSTITUTE FOR POLICY AND INTERNATIONAL STUDIES
IN TEHRAN, IRAN ON 1 DECEMBER 2008**

“Challenges of the Islamic Ummah in Facing Global Financial Crisis”

1. The financial crisis is yet another threat facing the Islamic ummah. Whether we can avoid being dragged down by this crisis or we can minimize the effect will depend much on us. It will also depend on whether the ummah choose to act together or whether each Islamic nation will act individually.
2. In facing any challenge we need to know as much as possible the nature of the challenge and how it will affect us. But more importantly we need to know the causes of the financial crisis itself, and what made it possible.
3. The systems that we see collapsing i.e. the monetary and banking systems have been in place for centuries. Why is it that the collapse is happening now and not before, not when the systems were introduced or shortly after? And why has it happened to the richest and the most powerful countries of the world?
4. The problem with systems and ideas devised by Man is that they always undergo change over time. New ideas would be added to them. The new ideas may not be good for the original system or idea.
5. Thus money began with coins of metal of definite values. But this was replaced with paper money backed by gold. Then gold backing was dispensed with. The value of paper money is vaguely related to the strength of a country's Government or its economy. Finally it was to be determined by the willingness of the market to accept the paper currency notes.
6. At this stage the currency became open to manipulation by market players. Currency traders find they could easily change the value of a currency in terms of exchange rates by massive selling and buying.
7. Besides making huge profits from currency trading, it was found that the countries whose currency has been devalued would experience political, economic and social turmoil. They and their people can become very poor.
8. The Western powers saw in this an opportunity to hegemonise and control the developing countries. The IMF and the World Bank were used for this purpose. By applying conditions to loans by the IMF/ World Bank, the countries in distress can be forced to surrender political and economic control to the Western powers. The impoverisation of these countries also enabled the

Western banks and capitalists to buy up all the businesses of the debtor countries at very cheap prices as they all have been made bankrupt or nearly bankrupt by the devaluation of their currencies.

9. Currency trading is therefore a political weapon to bring all the countries of the world under the control of the Western powers. How far-reaching the control can be is being seen now. The foreign funds which had come in to buy shares and banks during the 1997 – 98 financial crisis in the East are now pulling out, taking their capital with them in order to escape the impending crises. They have done this, this time, in expectation of the world financial crisis affecting the economies of these countries adversely. The withdrawal of their capital will in fact cause the financial crisis to affect these countries sooner and more severely.

10. Currency trading is made possible because of fiat money i.e. money that is not linked to gold or other precious metals.

11. We all use paper money now. Our paper money is also not linked to gold. But we do not indulge in currency trading although we still have to buy foreign currency to pay for imports. To a certain extent the market determines the exchange rate of our money. This causes a certain degree of instability but not sufficient to impoverish us.

12. Still it is best if the exchange rates remained stable. That is why Malaysia decided that Government should fix the exchange rate of the Malaysian Ringgit. All the great experts predicted a collapse of the Malaysian economy because we did not abide by international rules or wisdom. But as you know we recovered faster than the other countries after fixing the exchange rate.

13. Islamic countries should study the possibility of fixing the exchange rates of their currencies as a measure to protect themselves during the current financial crisis.

14. However the fact remains that the monetary system of the world today is open to all kinds of manipulation. The world needs to have a new monetary system that would be less easily manipulated.

15. Perhaps the ummah might push for a return to the gold standard. Another solution could be the use of the gold dinar purely for trade payments. In any case the Islamic ummah can reduce the attacks against them by not using the American Dollars for trade payments, especially for oil.

16. The U.S. Dollar is not backed by reserves as are other currencies. Apart from that the United States is bankrupt as it has a debt of 14 trillion dollars and it can never repay this debt. This huge borrowing by the United States is because for many years it has trade and current account deficits which forces it to borrow 1 ½ billion dollars a day to sustain itself.

17. The only reason why the U.S. Dollar has any value at all is because it is used in trade payments. If the gold dinar or other currencies are used for trading then there would be no demand for U.S. Dollars. It would then become worthless and that would have consequences over the United States' foreign policy.

18. This is something that the Muslim ummah can make use of in protecting themselves from the current financial crisis.

19. The other major cause of the present crisis is the banking system. For most people a bank is a convenient institution for depositing safely their money and withdrawing it when needed. We do not question how banks function. We assume that the money the banks lend us comes from the capital and the deposits with the banks.

20. The present banking system was created some 300 years ago by the Rothschild's. In that system money is actually made out of thin air, out of nothing. No gold or other assets were necessary. Yet the money borrowed from them has accepted values. Each time money is lent it creates money for the banks.

21. In most countries central banks owned by Government produce coins and print money. The money in circulation is therefore under Government control. But money can also take the form of cheques and how much money issued as cheques is not controlled by the Government.

22. The United States Federal Reserve Bank is not owned by the Government. It is owned by twelve privately owned state reserve banks. Yet the Federal Reserve Bank can actually print and issue currency notes, without any backing. Certainly it can lend money to the Government in the form of cheques.

23. Other banks can borrow from the Federal Reserve Bank when short. But these banks can lend much more than the amount of capital and the deposits from its clients. In the American system the banks can lend 90% of the deposits by its clients. But such is the system in use that the banks can actually lend 10 times the amount that it holds in the form of deposits.

24. Whereas ordinary businesses can only sell what they have in stock, banks can apparently deal in ten times the money held by them.

25. The profits made by ordinary business is hardly ever more than 10% of the total value of the stock sold. But since banks earn a fix interest, and the interest comes from 10 times the money it actually holds, the earnings of the banks are far higher than from ordinary business.

26. Since banks can lend more than the money it has, the tendency is to increase the lending as much as possible.

27. The current crisis began with the sub-prime loans, i.e. loans at high interest to risky borrowers. The total amount of loans to such borrowers runs into hundreds of billions of dollars.

28. Housing loans usually require payment over 30 years. Banks calculate their earning from interest and principle over this period, without taking into account bad debts.

29. To avoid risks these loans were bundled up together with the good loans and insured with insurance companies such as AIG. The banks may also allow for a second mortgage to hedge against possible default.

30. Additionally the houses against which the loans were taken would belong to the bank until the total debt has been paid in 30 years time.

31. It seems that the banks would be making good profits even if the loans carry high risks. So would the insurance companies and the mortgage companies.

32. But when the risky loans defaulted by the millions resulting in debts of hundreds of billions which cannot be repaid, the banks were faced with huge numbers of non-performing loans. At the same time the collateralised houses cannot be sold as banks refused to lend money to buyers and the original banks could not recover any of the money lent through sales of the collaterals.

33. The insurance companies were also unable to pay the banks because the premium they received was far too small for the losses sustained by the banks.

34. The mortgage companies also faced the same problem as payments could not be paid by the borrowers.

35. The result is the spectacular collapse of the banks because most of the loans were not from deposit money but the ten times more than the deposits which banks were allowed to lend.

36. When banks lend much more than the money they have they were actually creating money out of nothing. If the loans are repaid then they would stand to gain far more than if they had limited themselves to their subscribed capital and deposits. However if the borrowers defaulted then their losses could exceed their capital and the deposits they had received. They would become bankrupt.

37. The sub-prime fiasco is due to the failure of the huge loans to high risk borrowers, to yield the interest and the principle expected. The banks concerned have lost far more than whatever capital assets or even deposits they had taken. Obviously they would not be able to return the deposits they had taken. They have by definition become bankrupt. When banks go bankrupt a whole lot of other businesses which depend on the banks for their operating capital will also go bankrupt. Hence, the bankruptcies of the three huge automotive companies of America.

38. The hedge funds are also affected as they depend on loans from the banks to leverage their investments.

39. Why did this crisis happen to the United States and not the other countries? Firstly, it is because the privately owned banks actually issue large amounts of money in America. It should be noted that the money issued need not be in the form of printed currency notes. Cheques can be made out in any amount and effectively the cheques are money. The lending and borrowing are no longer constrained by the amount of currency notes in circulation.

40. The second factor is the faith in the market regulating the value of money. Wall Street and the rich capitalists had persuaded the Government that it should not interfere with the market i.e. with banking and finance and the way money is used to make more money.

41. The market is about making money, making profits regardless of the consequence. When the banks created money out of thin air, when they lend this money to people quite incapable of repaying their loans, when the amounts exceed the capacities of the banks to recover in cash after the loans go bad, when the deals become so big as to be far bigger than money in circulation and total trade in goods and services, the Government did nothing. The Government did not even require accounts to be submitted for tax purposes. Though banks are required to submit accounts and pay taxes, this was easily avoided by having offshore subsidiaries in tax havens where they can borrow huge sums from legitimate banks and do anything they like with the money without having to show accounts to any Government agency.

42. The hedge funds took advantage of the lack of Government supervision to borrow as much as twenty times the amount invested in them. Using these loans the hedge funds made huge investments mainly in the money market, guaranteeing return to investors of 30% or more. This was believed to be possible because the returns would be from twenty times the amount invested in the hedge funds. So huge are the hedge funds that Central Banks cannot hope to protect national currencies by buying the currencies dumped into the market by hedge funds.

43. What can the Muslim ummah do to face the worldwide financial crisis? The first thing would be to continue with Government regulations of the banks and the financial institutions. The free market system should not be adopted, at least not in full. Instead, all financial transaction must be made transparent and subjected to proper regulation. The regulation should be judicious as over-regulation can stifle business, and affect economic growth.

44. The idea of a globalised, borderless world has been promoted by the rich countries especially the United States. Conceived by the rich, we can be sure that it was meant to benefit them.

45. Globalisation is something that cannot be avoided as the ease of communication and travel make isolation of countries impossible. Whether we like it or not whatever happens in other parts of the world will effect us. This involves not only finance and the economy but also political and social ideas.

46. There is more than one way to globalise. Muslims must study the manner and the effect of globalisation in order to devise a system of globalisation which will not destroy the Muslims and their religion.

47. In banking and finance, the principal causes of the current financial crises, there is no need to follow all practices coming out of the West.

48. The ummah can have their own banking and financial system. Already we have Islamic banking and Islamic insurance. They have not been abused the way the Western banking systems and insurance have been abused. It is necessary that the Muslim institutions such as these be scrutinied carefully in order to prevent them from causing the same problems.

49. Muslims must be active in proposing new systems, rules and regulations for banking and finance. We should even propose to go back to gold whether it is in the form of gold dinar or any coin or bullion.

50. To save our currency and economy from being affected by western banking practices and the U.S. Dollar, a new trading currency should be proposed to replace the U.S. Dollar. Such a trading currency should be tied to gold and used only in international trade.

51. This will help stabilise the value of national currencies as gold has intrinsic value in all countries. The local currencies can still be used but the value must be pegged to the international trading currency. There will be fluctuation as gold prices do fluctuate. But this would be minimal, much less than paper money.

52. Truly the Muslim ummah are in the best position to initiate and sustain the monetary and financial systems of the world. This is because they are in possession of more money than they can find use for. They are even in a

position to insist that their oil be paid in the local currency or in any currency designated by them. Whatever currency they choose will become strong simply because there will be a demand for it just as today the U.S. Dollar has a value because there is a demand for it in the settlement of trade.

53. What is needed from the ummah is the will to insist on their wishes to be considered. I do not see all the Muslim countries in the world acting together. But it would be enough if a few would coordinate their efforts, would act together and agree to promote the interest of the ummah.
