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## **Content**

Figures.....	5
1. Introduction.....	6
2. Islamic Banking: An introduction .....	7
2.1 Idea of Islamic Banking.....	7
2.2. Islamic Banking in a global economy.....	9
2.3. History .....	11
2.4. Sharia .....	14
2.5. International Organisations.....	15
3. Principles of Islamic Banking .....	18
3.1. Riba .....	18
3.1.1. Interest in Christianity and Judaism .....	21
3.2. Gharar .....	24
3.3. Quimar and Maysir .....	26
3.4. Profit and Loss sharing .....	27
3.5. Support only Halal activities .....	28
3.6. Sharia Board .....	28
4. Financial Instruments .....	31
4.1. Contracts of sale .....	32
4.1.1. Murabahah .....	32
4.1.2. Bay Salam .....	34
4.1.3. Istisnaa.....	35
4.1.4. Bay Inah and Tawarruq.....	36
4.1.5. Qard Hassan .....	36
4.2. Contracts of partnership .....	37
4.2.1. Mudarabah .....	38
4.2.2. Musharakah.....	39
4.2.3. Leasing (Ijara) .....	41
4.2.4. Sukuk .....	43
4.3. Stock investment.....	48
4.4. Deposit accounts .....	51
4.4.1. Current account.....	51
4.4.2. Savings account .....	51

4.4.3. Investment account.....	52
5. Islamic Banking in practice .....	53
6. Islamic Banking in Switzerland and Germany .....	57
6.1. The Islamic market .....	58
6.1.1. The Swiss market.....	58
6.1.2. The German Islamic market .....	65
6.2. Muslim population .....	70
6.2.1. Muslim population in Switzerland.....	70
6.2.2. Muslim population in Germany.....	73
6.3. Other groups that are possibly interested in Islamic Banking .....	78
6.4. Islamic financial instruments and their applicability in Switzerland and Germany .....	79
6.4.1. Applicability of specific Islamic products.....	80
6.4.1.1. Findings of the applicability analysis for financial instruments .....	85
6.5. Comparison of the Swiss and German market.....	86
7. Conclusion .....	94
8. References.....	97

## Figures

Figure 1 Growth of Islamic banking industry .....	9
Figure 2: Categories of riba .....	19
Figure 3 Islamic Financial Instruments. ....	31
Figure 4 Murabahah basic model.....	32
Figure 5 Bay Salam model .....	34
Figure 6 Istisnaa model .....	35
Figure 7 Mudarabah basic model.....	38
Figure 8 Musharakah model.....	39
Figure 9 Ijara model.....	41
Figure 10 Sukuk Issuance .....	47
Figure 11 Investment of the Faisal Private Bank .....	61
Figure 12 Commodity linked investment certificates .....	62
Figure 13 Model of the Saxony-Anhalt Sukuk .....	66
Figure 14 Age distribution of the Muslim population in Switzerland .....	71
Figure 15 Education of the Muslim population in Switzerland based on the census 2000 .....	72
Figure 16 Age Distribution of Turkish Population in Germany in 2006.....	75
Figure 17 Turkish and Bosnian labour force according to net income in 2005.....	76
Figure 18 Turkish and Bosnian labour force according to occupation in 2005 .....	76
Figure 19 Turkish and Bosnian labor force according to level of education in 2005 .....	77
Figure 20 Muslim population in West Europe.....	87
Figure 21 Quantification of the demand for Islamic financial products.....	91

## **1. Introduction**

The intention of this paper is firstly to identify the legal basis of Islamic banking, and secondly to analyse the financial instruments used in Islamic banking. In addition, the market potential of Islamic banking in Switzerland will be explored and evaluated.

In chapters two and three, the legal basics will be highlighted that will provide the necessary basic knowledge for the following parts and chapters. In this section I will address in detail the Sharia, which is the fundamental guideline for every economic activity. Derived from the Sharia, several key principles are established that decisively influence the structure of Islamic banking. By explaining these principles, a basis should be provided for a better understanding of the function of Islamic banking. Furthermore, the most important international organizations will be mentioned. Finally, the composition of a Sharia Board and its role on financial markets will be explained in detail.

Based on these fundamentals, financial instruments and their structure will be introduced in chapter four. The system of these instruments will be presented graphically, the existing standards shown, and the possible areas of application identified. Subsequently, the practice of Islamic banking will be examined in order to clarify whether the presented guidelines are followed in a real economy.

In the last chapter, we will dwell on the question as to whether there is market potential for Islamic banking in the Swiss and the German market. Therefore the Muslim population in Switzerland and Germany, as other potential groups of investors, will also be analysed. Moreover, an inventory of the instruments already offered on the Swiss and German market will be made, followed by an investigation of the applicability of the different Islamic financial products. At last these two markets will be compared.

## **2. Islamic Banking: An introduction**

### **2.1 Idea of Islamic Banking**

There is no universal definition of Islamic Banking, as Warde (2000) points out:

*„No definition of Islamic finance is entirely satisfactory. To every general criterion, a financial institution owned by Muslims, catering to Muslims, supervised by a Sharia Board, belonging to the International Association of Islamic Banks (IAIB) etc., one can find some significant exception“<sup>1</sup>*

However, several authors have tried to give an idea of what Islamic Banking includes, and for what it stands. Among these explanations, the one by the state bank of Pakistan seems to be quite comprehensive:

*„ Islamic Banking has been defined as banking in consonance with the ethos and value system of Islam and governed, in addition to the conventional good governance and risk management rules, by the principles laid down by Islamic Sharia. Interest free banking is a narrow concept denoting a number of banking instruments or operations, which avoid interest. Islamic Banking, the more general term is expected not only to avoid interest-based transactions, prohibited in the Islamic Sharia, but also to avoid unethical practices and participate actively in achieving the goals and objectives of an Islamic economy“<sup>2</sup>*

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<sup>1</sup> Warde I (2000) Islamic finance in the Global Economy. Edinburgh University Press Edinburgh

<sup>2</sup> What is Islamic Banking? State Bank of Pakistan, December 2005  
[www.bankislami.com.pk/JSP/en/faq.jsp](http://www.bankislami.com.pk/JSP/en/faq.jsp)

Islamic Banking indicates a banking system that operates in compliance with the rules of the Sharia, which aims to provide economical and social justice for all members of society. The entire economy is based on these principles. The Islamic financial system is part of the whole concept of society; religion and economy cannot be separated from each other. The main characteristics of Islamic Banking are the prohibition of *riba* (interest), *gharar* (speculation) and *maysir* (gambling). Furthermore all transactions that involve an action forbidden by the Sharia are prohibited.

Piccinelli (1988) divides Islamic Banks into two categories: commercial banks and development banks.<sup>3</sup> Nienhaus (1983) also distinguishes between two different types of Islamic Banks<sup>4</sup>:

- 1) banks that are established by the state and entrusted with special public functions (for example, the Islamic Development Bank)
- 2) Banks that were funded by private investors

The second group is divided further into

- a. banks that focus on rural areas, and whose main concern is to invest profit in order to encourage development
- b. banks in capitals or financial centres that offer alternatives to conventional banking
- c. Islamic investment companies

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<sup>3</sup> Piccinelli GM (1988) Introduzione. I principi e gli istituti finanziari Islamici. Oriente Moderno 1-9, 1-44

<sup>4</sup> Nienhaus V (1983) Islamische Banken. Struktur und Bedeutung. In: Simonis (ed) Entwicklungsländer in der Finanzkrise. Duncker & Humblot, Berlin 159-176



## 2.2. Islamic Banking in a global economy

Islamic financial services are a quite young phenomenon. Although the first Islamic Bank was founded in 1975, the real boom started in the 1990s. The growth ever since is pretty impressive: according to Babai (1995)<sup>5</sup>, the market share of Islamic Banks, in terms of assets under management, increased from 2 percent in the end of the 1970s to 15 percent in the 1990s. According to Standard and Poor's, the Islamic financial industry manages approximately 500 billion US Dollars and increases by roughly 15 percent a year<sup>6</sup>. Siddiqui (2005), director of the Islamic Index Group, qualifies this number by observing: „There is no scientific way to quantify that number. I've been hearing this same figure since about 1997. So if the market was \$150 billion then and growing at 15% per annum, why is it still \$150 billion now? It should be at least \$400 billion by now“.<sup>7</sup>

### *Growth of the Islamic banking industry*

By the end of this year, total volume of Shari'ah compliant assets could reach almost half a trillion USD

Total Volume of Shari'ah Compliant Assets (in BN USD)

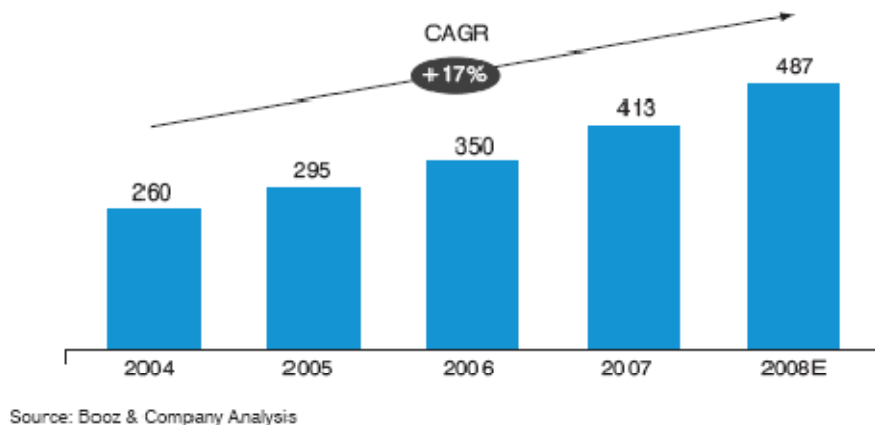


Figure 1 Growth of Islamic banking industry<sup>8</sup>

<sup>5</sup> Babai D (1995) Arab Banker's Association of North America Newsletter

<sup>6</sup> Kubsova J(2007) Allah sei Dank. Financial Times Deutschland.08.03.2007  
[www.ftd.de/boersen\\_maerkte/geldanlage/170509.html](http://www.ftd.de/boersen_maerkte/geldanlage/170509.html)

<sup>7</sup> Dan K (2005) Keeping the Faith. Global Finance, 01.2005 [http://globalf.vwh.net/content/?article\\_id=155](http://globalf.vwh.net/content/?article_id=155)

<sup>8</sup> Vayanos P, Wackerbeck P (2007) Islamic Banking: How do Islamic Banks compete in an increasingly competitive environment. Booz & Company

In a study carried out in 2007 by Vayanos and Wackerberck (2007), both employed at Booz and Company, the estimated value of Sharia compliant assets could reach 487 billion USD.

Rauscher (2006) estimates up to 30 percent growth per year due to the entry of new Islamic banks into the market<sup>9</sup>. The fact is that the true value of funds managed by Islamic financial institutions is very difficult to assess, because information is not freely available. Today more than 350 Islamic financial service providers operate all around the world in over 75 countries – of these, approximately 270 are Islamic Banks that work in compliance with the Sharia. In addition, about 400 international banks offer their clients „Islamic windows“ in divisions that provide Islamic financial instruments.

The fraction of Muslims that carry out their financial transactions in a Sharia-compliant way is still fairly small, but growing. Nearly 1.5 billion Muslims represent an attractive market, and not only for Islamic Banks. New financial institutions and Islamic windows are found constantly, new products develop, and the existing products improve. Not only in Arabic countries, but also in Europe and the US, the market is flourishing. Various European and American banks are expanding into Islamic countries, and are offering Sharia compliant financing there. One example is the UBS subsidiary Noriba, founded in Bahrain in 2002<sup>10</sup>, that works in a 100 percent Sharia compliant way; another is Citibank, which founded a subsidiary, also in Bahrain, as early as 1996.

Different states (Pakistan since 1979, Iran and Sudan since 1983) have changed their whole economic system to a Sharia conforming system; their banks are obliged to follow the rules regarding the principles of Islamic finance. In most other Islamic states, conventional banking operates alongside Islamic banks.

Not only Muslims are investing increasingly in Sharia compliant instruments – non-Muslims are also showing interest in this alternative to conventional banking.

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<sup>9</sup> Rauscher C (2006) Islamic Banking. Internationale Erfolgsgeschichte und dynamischer Wachstumsmarkt. bestbanking, 10:20-24

<sup>10</sup> [www.ubs.com](http://www.ubs.com)

According to Gassner (2007), the main investors in Islamic financial instruments in Malaysia come from the Chinese minority there.<sup>11</sup>

The events of September 11<sup>th</sup> had a strong impact on Islamic banking and finance<sup>12</sup>. Muslims suddenly got a lot of attention from American authorities, who believed that Islamic banks were financing terror groups such as Bin Laden's Al-Qaida, and Islamic finance became a frequently discussed topic. These suspicions became stronger and stronger: in response, Sheikh Saleh Kamel called for Muslims to bring back their money from western countries.<sup>13</sup> These funds were removed from the traditional markets in the US and Great Britain, and placed largely in Sharia conforming investments.<sup>14</sup> In spite of this, compared to all assets under management in the global economy, Islamic financial institutions play a minor role. Most Muslims still invest in conventional banking, mainly because knowledge about Islamic Banking, and the products associated with it, is still not widely disseminated. In order to combat this situation, a vast number of conferences and events have been and continue to be held all over the world.

### 2.3. History

Islamic Banking has its roots in the 1960s. In the last two centuries, most Muslim countries were colonized by western countries that established their own financial and economic systems. After the Second World War, the colonial states gradually backed out from the region: this retreat permitted the discussion about, and the reorientation of an economic system based on the rules of the Sharia. From the 1950s on, a number of bankers and economists thought publicly about organizing alternative financial institutions that would operate within the rules of the Sharia, especially relating to the prohibition of interest.<sup>15</sup> Pakistan, as early as 1956, and

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<sup>11</sup> Gassner M, Wackerbeck P (2007) Islamic Finance. Bank Verlag, Köln, p. 41

<sup>12</sup> See Warde I (2004) Global politics, Islamic Finance and Islamist politics Before and After 11 September 2001. In: Clement (ed) The Politics of Islamic Finance. Edinburgh University Press, Edinburgh, p.37-63

<sup>13</sup> Warde (2004)

<sup>14</sup> Islam Fonds. Deutsche Nachzügler. Der Spiegel 11.12.06, p. 97

<sup>15</sup> For example Quraishi A.(1946) Islam and the theory of interest. Lahore

later Iran, in 1979, enshrined in their constitutions the abolition of a banking system based on interest.<sup>16</sup>

The first Islamic Bank was found in Egypt: at more or less the same time a project, the Pilgrim's Administration and Fund (Tabung Hajji), operated in agreement with the Sharia,<sup>17</sup> started in Malaysia. This fund was opened to cater for pilgrims who wanted to spend money on their pilgrimage that had nothing to do with interest, something not possible with a conventional bank.<sup>18</sup> The Egyptian venture became famous as the first modern experiment in Islamic Banking. In the small town of Mit-Ghamr, Al-Najjar, the future secretary general of the International Association of Islamic Banks, founded in 1963 the first bank to operate in an interest-free way. The system worked in a similar way to the German savings bank system<sup>19</sup> – Al-Najjar was educated in Germany – and it was also mainly German banks that sponsored the project. This first Sharia-compliant bank became resoundingly successful: within a short period approximately 250.000 clients invested their capital with the Mit-Ghamr Savings Bank, which ran nine subsidiaries and managed more than 2 million Egyptian pounds.<sup>20</sup>

Although the project had to be closed in 1967 - according to Grahmmer (1993) and others, because of political rivalry with President Nasser and not because of a liquidity shortage<sup>21</sup> - one major achievement was the integration of the lowest income strata in the financial system that had never before formed part of the saving population. The bank was reopened under a new name - Nasser Social Bank (NSB) - in 1971, and put down in its founding act the principles of Islamic Banking, such as the donation of zakat and interest-free banking. Although the Mit-Ghamr case became crucial for the development of Islamic Banking, it was not linked explicitly to Islamic scholarship or movements or the ideas about an independent banking system

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<sup>16</sup> Amereller F (1996) Hintergründe des Islamic Banking. Rechtliche Problematik des Riba Verbotes in der Sharia und seine Auswirkung auf einzelne Rechtsordnungen arabischer Staaten. Duncker & Humblot, Berlin, p. 40

<sup>17</sup> Henry C, Wilson R (2004) The Politics of Islamic Finance. Edinburgh University Press, Edinburgh, p. 18

<sup>18</sup> Khiyar AK (2005) The rise and development of interest-free banking. Institute of Objective Studies, New Dehli, p.89

<sup>19</sup> Grahmmer (1992) Determinanten und Probleme der Finanzierung und Absicherung von Geschäftsbeziehungen mit den islamischen Ländern des Nahen Ostens und innovative Lösungsansätze im Rahmen des islamischen Bankwesens. Wien, p.187

<sup>20</sup> Gassner (2007) *ibid*, p. 37

<sup>21</sup> Grahmmer (1993) *ibid*, p. 188; Khiyar (2005) *ibid*, p. 88

according to the Sharia – no-one controlled the compliance with the rules of the Sharia.

In the 1970s the Organization of the Islamic Conference (OIC) held a number of meetings. In one of these meetings, in 1972 in Saudi Arabia, the members agreed on the foundation of an Islamic Bank, whose stated aim was to foster the development of a banking system that should be active not only in the public but also in the private sector, by providing funds for development activities and offering financial services and assistance in the member countries. One of the major goals of the Islamic Development Bank (IDB) is still the development of new financial products that comply with the rules of the Sharia.

The bank started its activities officially in 1975, the same year that another Islamic Bank, the Dubai Islamic Bank, started as the first bank founded on private initiative and the first Islamic commercial bank.<sup>22</sup> From this moment on, a large number of Islamic Banks emerged<sup>23</sup>, developing into a feasible alternative to conventional banking by obtaining good results with Islamic products.

First the phenomenon could be observed only in Arabic countries, but it soon spread over the Asiatic region (for example, to the Bank Islam Malaysia) and in the 1990s over Europe as well. According to Hardy (2006)<sup>24</sup>, these first Islamic banks were placed at a disadvantage relative to the existing conventional financial institutions. The real upturn started in the 1990s for various reasons: among them the revolution in Iran, the creation of new Islamic countries, the transformations on the oil market, the rise of the Asian tiger states, the rising influence of Islam in the western hemisphere, and the development of a new Islamic middle class.<sup>25</sup>

One of the first western banks to open an „Islamic window“ by offering Sharia-compliant products was the New York-based Citibank, which established a subsidiary in Bahrain in 1996.<sup>26</sup>

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<sup>22</sup> Khiyar (2005) *ibid*, p. 83

<sup>23</sup> Khiyar (2005) *ibid*, p. 93

<sup>24</sup> Hardy (2006) *Sharia Compliance. Understanding the Contributions of Sharia Boards*. In: Hanstein et al. (eds) *Beiträge zum islamischen Recht V, Leipziger Beiträge zur Orientforschung*, Bd 19. Peter Lang, Frankfurt a. Main, p., p. 202

<sup>25</sup> Warde (2001) *ibid*, p. 5

<sup>26</sup> Warde (2001) *ibid*, p. 5

## 2.4. Sharia

When we discuss the topic of Islamic Banking, we frequently use the terms Sharia, Sharia-compliant products, etc. Sharia is literally translated as „*pathway*“, but could better be interpreted as „*the path in which God wishes men to walk*“.<sup>27</sup> The Sharia is the religious law that affects and regulates not only the religious life of Muslims but also the practical aspects of everyday life. In the Islamic conception, this law is given by God himself, so scholars can only interpret the sources of instruction (Qur'an and Sunnah) in order to deduce from these sources guidelines and rules for various situations in everyday life. These are the rules that Muslims have to follow if they want to be rewarded in the afterlife.

The Sharia is not encoded as a canon of laws like our codes of law, but is a derivation from the main sources - the Qur'an and the Sunnah. The Qur'an is the main religious text, the holy book of Islam, and the basis for all duties a Muslim has to fulfill.<sup>28</sup> In this book the prophet Mohamed (570-632) put down the revelations of the angel Gabriel over nearly 23 years. The words of the Qur'an are perceived to be God's own words, and are therefore considered to be the source of all laws and legal obligations.<sup>29</sup>

The Sunnah, by contrast, was not written down by the prophet Mohammed himself: it was written about a hundred years after his death by followers and scholars who wanted to avoid conflicts about different interpretations. The Sunnah stands for the whole life of Mohammed and his actions, while the Hadith – which form a part of the Sunnah - are the collected sayings of the prophet that were passed down; a compilation of recorded and validated narrations and approvals.

Essential in the Hadith is the traceability back to the prophet himself.<sup>30</sup> The Hadith play an important role in the interpretation of the Qur'an. A large number of the basic obligations of the holy book, like the religious tax zakat (a 2,5% tax on profit) or the

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<sup>27</sup> Khyar (2005) *ibid*, p. 111

<sup>28</sup> Klarmann (2003) *Islamic Project Finance*. Schulthess, Lausanne, p. 17

<sup>29</sup> Ramadan S (1980) *Das Islamische Recht, Theorie und Praxis*. Harrassowitz, Wiesbaden, p. 40

<sup>30</sup> *Encyclopedia of Islam* (1960) Vol. III, London, p. 23

haji (holy pilgrimage to Mecca) would be hard to fulfill if the practical example of the prophet himself did not exist as a model.<sup>31</sup>

Other components of the Sharia are the Ijma (the consensus among scholars), Qiyas (analogies), Itihsan (divergence from a precedence due to legal relevance), Istislah (sentence passed not because of a precedence but in the public interest) and Urf and Adat (local customs).<sup>32</sup> If in a particular case no solution can be found in the above-mentioned texts and customs, the judge has to form an autonomous opinion, Idschtihaad, based on the known legislative sources<sup>33</sup>. His sentence is called the fatwa.

Based on these elements of the Sharia, scholars developed the fiqh, the Islamic jurisprudence, where it is clearly stated – according to the Sharia – what is halal (allowed) and what is haram (forbidden). These laws form a kind of Islamic business or commercial law, which is also taken as the foundation of Islamic finance.

When we speak about Islam, we should not forget that the Islamic World is very heterogeneous: this is reflected in the different interpretations of the Sharia. The main streams within Islam, the Sunnis and the Shiites, each have their own schools of thought. The majority of Sharia rules are interpreted in the same way in all schools, but in some fields there is some diversity of interpretation.

## **2.5. International Organisations**

Quite apart from the religious and legal framework, international organizations play an important role in the development of Islamic banking. To be able to compete with the conventional banking system, permanent development and research is needed to standardize processes and concepts. Several non-governmental as well as government-related organizations exist worldwide to fulfil this role.

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<sup>31</sup> Dutton Y (1999) The origins of Islamic Law. Curzon Press, Richmond, p. 163

<sup>32</sup> Gassner (2007) *ibid*, p. 24

<sup>33</sup> Ramadan (1980) *ibid*, p. 67

- **AAOIFI:** The Accounting and Auditing Organization for Islamic Financial Institutions was founded in 1990 in Algiers, and is today situated in Manama, Bahrain. It is a non-governmental, non-profit organization, whose aims are to standardize accounting, auditing, governance and ethical standards compliance with the rules of the Sharia. In several countries (Saudi Arabia, Jordan, Lebanon, Pakistan, Malaysia, Dubai, Bahrain etc) the standards of the AAOIFI are already obligatory for financial institutions. So far 155 institutional members from 40 different countries have joined the AAOIFI, including central banks and other financial institutions (interestingly, institutions can become members but countries cannot).<sup>34</sup>
- **OIC:** The organisation of Islamic Conference was established in 1969 in Rabat, Morocco by the 30 Foreign ministers of the founder countries: today, with 57 members all over the world, it is the second largest global organization after the UN. It started its work in 1972, and operates internationally with the aim of fostering solidarity and economic cooperation in the Muslim world. One long-term objective is the creation of an Islamic Common Market.<sup>35</sup>
- **IDB:** The Islamic Development Bank was founded in 1973 at a conference in Jeddah, Saudi Arabia by the Finance Ministers of different Muslim countries that belong to the OIC, but started operations officially only in 1975. Its main purpose is the economic development as well as the social progress of Muslim countries, which it achieves by fostering projects, granting loans and providing financial assistance. The IDB is not a commercial bank, but a development bank that consists of 56 members, all belonging to the OIC. Membership at the OIC is a precondition for being accepted as a member at the IDB.<sup>36</sup>
- **IFSB:** The Islamic Financial Services Board was established in 2002 in Kuala Lumpur, where it is still based today, and started its activities in 2003. The IFBS is an organization that fosters the stability and credibility of the Islamic

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<sup>34</sup> [www.aaofii.com](http://www.aaofii.com)

<sup>35</sup> [www.oic-oci.org/oicnew/, p.e\\_detail.asp?p\\_id=52](http://www.oic-oci.org/oicnew/,p.e_detail.asp?p_id=52)

<sup>36</sup> [www.isdb.org/irj/portal/anonymous?NavigationTarget=navurl:/24de0d5f10da906da85e96ac356b7af0](http://www.isdb.org/irj/portal/anonymous?NavigationTarget=navurl:/24de0d5f10da906da85e96ac356b7af0)



financial industry, which it achieves by defining and setting up Sharia-compliant standards that make Islamic financial services more transparent. For this purpose the IFBS works closely with international organizations such as banks and insurance companies, for example the Basel Committee on Banking Supervision, the World Bank, the IMF, and many more. The IFSB attaches great importance to constant research and training – it periodically organizes seminars, workshops, discussions and conferences on the subject of Islamic banking.<sup>37</sup>

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<sup>37</sup> [www.ifsb.org](http://www.ifsb.org)

### 3. Principles of Islamic Banking

#### 3.1. Riba

From a western perspective, the most striking feature of Islamic Finance is probably the prohibition of interest (riba). The Qur'an and the Sunnah forbid the payment of interest explicitly, and state that riba is not only an injustice, but also an economic evil and a threat to the welfare of the whole society. Another source for the ban of riba in Islamic finance are the Hadith. Riba literally means 'increase', and is normally translated into English as usury or interest, but actually has a much broader meaning: „Riba is defined as a monetary advantage without a counter value which has been stipulated in favour of one of the two contracting parties in an exchange of two monetary values“<sup>38</sup>. In the context of the Sharia it „refers to the 'premium' that must be paid by the borrower to the lender with the principal amount as a condition for the loan or for an extension in its maturity“<sup>39</sup>. There are different passages in the Holy Qur'an that deal with riba:

*„Those who devour riba shall only rise again as one whom Satan strikes with his touch, this because they say „selling is like usury“, but Allah has permitted trade and forbidden riba“ (Baqara 2:275-80)*

*„Oh you who believe! Do not gorge yourselves on riba, doubling and redoubling it“ (3:130)*

*„Whatever you give as riba so that it might bring increase through the wealth of other people will bring you no increase with Allah. But what you give as charity, seeking the countenance of Allah (will be blessed) for those are the ones who will truly receive increase.“ (30:38-39)*

The key statement in all these cited passages is quite clear: for a Muslim, riba is prohibited. If a Muslim lends money to another person, which per se is allowed, he

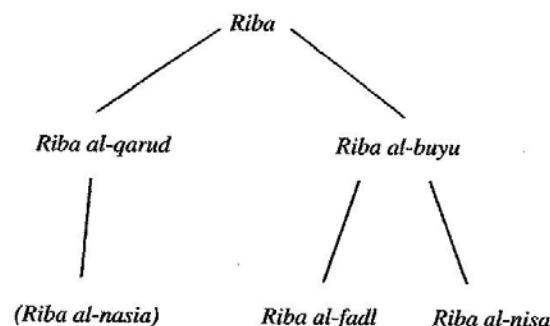
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<sup>38</sup> Schacht J (1964) An introduction to Islamic Law. Oxford University Press, Oxford, p. 145

<sup>39</sup> Chapra U (1985) Towards a Just Monetary System. Islamic Foundation, Leicester, p. 56

only can claim the redemption of the principal, and even has to renounce that if the debtor is unable to fulfil the obligation. Despite this clear prohibition of riba in the Qur'an, discord reigns among the different schools of thought. Umar ibn-al-Khattab (592-644), the second caliph and also a companion of Mohammed, regretted that the Prophet had not clarified in more detail the meaning of riba. Scholars today discuss whether riba stands for interest as a whole or only usury, meaning an exorbitantly high rate of interest: if it were to stand only for usury, most conventional financial transactions would be considered legal.

The modern discussion about riba started with Rahman (1964) who argued that the historical role of riba no longer applies to today's function of banking interest.<sup>40</sup> Even when most scholars agree that riba is a synonym of interest as a whole, and is therefore forbidden, the controversy goes on about the exact definition of riba and how it has to be applied to the various transactions that occur in the financial sector.



Source: El Diwany 2003

Figure 2: Categories of riba

Riba is divided into two categories: Riba al-qarud, which refers to interest related to credits, and riba al-buyu, which refers to interest related to trade, and can be subdivided into riba al-fadl and riba al-nisa.

Riba al-nasia, a subdivision of Riba al-qarud, refers to a loan at interest, and is defined as the increase in the principal sum the creditor charges for having granted a

<sup>4040</sup> Rahman F (2007) Riba and interest, In: Kabir et al. (eds) Islamic Finance. Elgar, Cheltenham, p.22-64

loan to the debtor for a specified time. If this increase is already set at the beginning of the transaction, then the creditor does not take any risk - therefore this increase is forbidden. By contrast, it is not forbidden to give a premium voluntarily, provided that this bonus was not a precondition of the loan.<sup>41</sup>

In the second category of *riba al-buyu*, the first subdivision is *riba al-nisa*, which involves a non-simultaneous exchange of goods with the same quality or quantity. By contrast, the second subdivision of *riba al-buyu*, called *riba al-fadl*, refers to an action in which an unequal quantity or quality of the same goods are exchanged at the same time. *Riba al-fadl* is the category about which scholars disagree. One especially important source for the prohibition of *riba al-fadl* are the Hadith, where the Prophet Mohammed explicitly names, more than once, several items to which the *riba* rules extend:

*„ Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, salt for salt, the same thing for the same thing, like for like, measure for measure, but if these things are different, sell them as you please if it is done only measure for measure<sup>42</sup>.*

The different schools now have differing opinions on which items the prohibition has to be extended to. The Shafi`i, for example, believe that gold and silver stand for precious metals, while the other items represent food as a class. The Hanafis by contrast take up the position that gold and silver represent items that are sold by weight, while the others are sold by measure<sup>43</sup>. However, the important question today is whether the rules for *riba* can be applied by analogy to money and/or currency. Most scholars would answer this question positively, since the cited Hadith lists all categories of goods that were used as means of payment during the Prophet's lifetime. The prohibition of *riba al-fadl* is targeted mainly on the avoidance

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<sup>41</sup> Khalil E (2006) Overview of the Shari`a prohibition of *riba*, In: Abdulkader (ed) Interest in Islamic economics. Routledge, Oxon, p. 59

<sup>42</sup> Khalil (2006) *ibid*, p. 65

<sup>43</sup> For more information on the differences between the different schools: Al-Zuhayli W (2006) The juridical meaning of *riba*. In: Interest in Islamic Economics. Routledge, Oxon, p. 26-54

of profit as a result of dishonesty and injustice. One of the main concerns of the Qur'an and the Sunnah is justice, which makes it a central point in the Sharia – justice being a synonym for ensuring the well-being of all members of a society.

All the different forms of riba have the consequence that credit and other forms of debt only can be exchanged for the original face value if changed for money. This means that the prohibition of riba in Islam prevents debtors from getting caught in a debt spiral, where new debt has to be taken on to repay the interest on old debt.

To determine whether a contract is in agreement with the Sharia, there are certain key elements that have to be taken into consideration:

- A service or product has to be provided
- Both parties need to have the same information (no informational asymmetry), work in an open market, and should not try to hide crucial details from the partner, even if there is no malice aforethought and no intention to defraud
- Both parties have to incur the risk of making a profit or loss, otherwise the profit would be illegal
- The transaction has to be a halal (allowed) action or business
- The foundation of the transaction has to be a clearly-defined written or verbal contract

### 3.1.1. Interest in Christianity and Judaism

Throughout history usury was forbidden not only in Islam, but also in Christianity, Judaism, and Hinduism. In the Christian case, the taking of interest was entirely prohibited for more than 1400 years. The relevant passage on which this prohibition was based can be found in the book of Deuteronomy, where one can find:

*„You must not lend on interest to your brother, whether the loan be of money or food or anything else that may earn interest“ (23:19)<sup>44</sup>.*

Another passage that takes the same line can be found in Exodus:

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<sup>44</sup> Cornell V (2006) In the Shadow of Deuteronomy, Approaches to interest and usury in Judaism and Christianity. In: Abdulkader (ed) Interest in Islamic Economics. Routledge, Oxon

*„If you lend money to any of my people, to any poor among you, you must not play the usurer with him; you must not demand interest from him“ (22:25).*

Although these passages are also binding for Jews, it was common Jewish practice to charge interest (usury). According to Cornell (2006) this fact is due to a unique interpretation by Jewish scholars of the Deuteronomy passage, according to which the prohibition of usury is compulsory for Jews, but not for non-Jewish people - the so-called „Deuteronomic double standard“. <sup>45</sup>

In addition, the violation of this interdiction was not really seen as a crime deserving draconian punishment, but regarded more as a „moral transgression“. This attitude was often the (official) spark for severe persecutions against the Jewish population all over Europe. For example, in England in 1311 the crown fixed the maximum interest Jews were allowed to charge at 20 percent. More than two hundred years later, in 1546, England made the taking of interest legal, with a fixed interest rate that was initially 10 percent: this however reduced steadily through the centuries.<sup>46</sup> From the time that interest became legal by law, the meaning of the word 'usury' changed from interest in general to a rate of interest above the maximum rate approved by law.

In Christianity the prohibition of usury was in the beginning only binding for clergy: later, as commerce in Europe widened and the demand for loans increased, it was widened to include laymen. Rabanus Maurus argued in 856 that the ban of interest, as recorded in the biblical passage of the book of Deuteronomy, only has to be applied to Latin Christians, whilst it can be taken without committing a sin from infidels and criminals.<sup>47</sup> As the prohibition of usury was extended to all Christians, the church discovered the applicability of usury as an economic weapon.

Pope Alexander III (1179) declared that every Christian may take interest from infidels, heretics and all other enemies of the church. By and by the church had to accept that loans, and therefore usury, could not be completely abandoned without severely discriminating against Christians: this led to a number of exceptions, seen as „acceptable loans“. <sup>48</sup> In addition, the church had to protect its members from the

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<sup>45</sup> Cornell (2006) *ibid*, p. 13

<sup>46</sup> Khiyar (2005) *ibid*, p. 59ff

<sup>47</sup> Nelson B (1969) *The idea of usury*. University of Chicago Press, Chicago, p. 4ff

<sup>48</sup> Cornell (2006) *ibid*, p. 20

Jewish moneylenders and Lombards who had achieved a kind of monopoly as providers of capital, charging up to 80 percent interest.<sup>49</sup>

A Christian who infringed upon the prohibition of usury had to face austere sanctions. The sin had to be borne not only by the lender, but also by the borrower and everyone else who had taken part in the transaction. Usury was among the worst sins – usurers became social outcasts, fit only to be hanged, or at any rate exiled, and to have their property confiscated.<sup>50</sup> Furthermore a convicted usurer was excommunicated, which implied exclusion from communion and the denial of a Christian burial. The usurer's family was doomed to a life in misery, since identical sanctions were imposed on them, condemning them to a life of dishonour and disrespect.

In practice, merchants nearly always found a way of getting around the usury ban. One way was to deposit funds with a bank, where the depositor was offered a fraction of the profit by the bank – the mode adopted for example by the Medici. Another way to circumvent the law was to contract a partnership in which both parties shared the profits and losses in accordance with a pre-established ratio. This partnership could be nothing but a legal fiction, designed only to make a profit from the capital invested.

Outstanding personalities arguing against the ban of interest by the church (but for the ban of usury) were Luther (1517), and later Calvin (1545). By their time the usury ban was already ineffective. The ways and means of evading the law were infinite, and the requirements of the market had also changed so fundamentally that the prohibition had become impracticable. Luther and Calvin argued that only unjust interest should be punished. According to Luther, a rate of interest of 4 or 5 percent would be ethical: Calvin went even further, declaring that only the taking of exorbitant interest from the poor would be against the law.

Based on the Protestants' arguments, the prohibition of interest was abrogated in Europe in the 16th century, with England taking the lead. In the 19th century, even

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<sup>49</sup> Montes pietatis (2003) The catholic encyclopedia, Vol X,, [www.newadvent.org/cathen/10534d.htm](http://www.newadvent.org/cathen/10534d.htm)

<sup>50</sup> Nelson (1969) *ibid*, p.4ff

the Catholic Church modified its view, stating that while moderate rates of interest are not counter to Catholic doctrine, excessive interest is still banned and punished.<sup>51</sup>

### 3.2. Gharar

Next to riba, gharar is the most important prohibition in Islam, even though it is not explicitly mentioned in the Holy Qur`an. The best translation for the word „gharar“ would be „risk“, „deception“ or „speculation“, but there is a unanimous notion that gharar includes also cheating and fraud. The Qur`an forbids all transactions where one party is enriching itself at the expense of other parties involved.

In literature one can find different definitions for gharar, but the various schools are once more not in complete agreement on these definitions. According to Al-Zarqa (2006) gharar is

*„the sale of probable items whose existence or characteristics are not certain, the risky nature of which makes the transaction akin to gambling“<sup>52</sup>*

The Hadith deliver evidence on gharar:

*„Do not buy fish in the sea, for it is gharar“*

and

*„Whoever buys foodstuffs, let him not sell them until he has possession of them“*

By definition gharar is not completely forbidden; a certain degree of gharar is accepted. Islam does approve the taking of commercial risk – only excessive risk-taking is prohibited. Some schools permit gharar if there is an urgent necessity for it,

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<sup>51</sup> Nelson (1969) ibid

<sup>52</sup> El-Gamal M (2006) Islamic Finance, Law, Economics and Practice. Cambridge University Press, Cambridge, p. 58



and if it could not be avoided except with major difficulties.<sup>53</sup> El-Gamal (2006) cites one example for such a need: salam, a prepaid forward sale, which would be prohibited according to gharar rules. In this special case it is allowed, since salam is used for example to finance agricultural activities that could not be financed otherwise.<sup>54</sup>

The consequences for trading are extensive:

No transaction can be negotiated without fixing the price in advance. Both parties have to agree on the conditions.

At the moment a contract is negotiated, the principal object must be in existence, and there has to be a real possibility of fulfilling the contract when it is concluded.

As a result of these constraints, no options or futures contracts can be traded in Islamic finance, since there the price is fixed but the compensation is not. Most forward contracts are rendered impossible as well, since they imply uncertainty. Conventional insurance also falls under the prohibition of gharar, since the premium paid for the insurance is prespecified but the insurance payment itself is uncertain. The Islamic answer to conventional insurance is takaful, a charitable accumulation of funds. Members contribute a periodic amount of money which is invested in a Sharia-compliant way. In case of loss, these funds are used to help Muslims with an approved type of gift.<sup>55</sup>

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<sup>53</sup> Saleh N (1992) *Unlawful gain and Legitimate Profit in Islamic Law: Riba, Gharar and Islamic Banking*. Graham & Trotman, London, p. 53

<sup>54</sup> El-Gamal (2006) *ibid*, p. 59

<sup>55</sup> Vogel F, Hayes S (1998) *Islamic Law and Finance, Religion. Risk and Return*. Kluwer Law International, The Hague, Boston

### 3.3. Quimar and Maysir

A further element that plays an important role, especially for insurance companies but also for the whole Islamic finance sector, is the prohibition of maysir (or quimar). Both these terms stand for gambling – in the Qur'an one can find the expression maysir, whereas in the Sunnah the term quimar is used.

*"They will ask thee about intoxicants and games of chance. Say: In both there is great evil as well as some benefit for man; but the evil which they cause is greater than the benefit which they bring." (Qur'an 2: 219)*

*"By means of intoxicants and games of chance Satan seeks only to sow enmity and hatred among you, and to turn you away from the remembrance of God and from prayer. Will you not, then, desist?" (Qur'an 5:90)<sup>56</sup>*

The key element in maysir is found in a game in which two parties are involved with the sole intent to win at the cost of the opposing party. Not only is the profit made in such a game against the law, but the act itself is too. One has to differentiate between trade and gambling: gambling is a zero-sum game. What one side wins, the other loses. Trading in general leads to a win-win situation, where both parties are better off. Scholars mainly agree that investments on stock markets are not affected by the proscription of maysir, whereas short-term trading can be problematic.

Several characteristics have to be fulfilled for a transaction to classify as gambling:

- At least two parties have to be involved in the transaction
- To obtain the other parties' wealth, one compromises his own wealth
- Alternatively, one or other party loses its wealth entirely without receiving anything in return.

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<sup>56</sup> El-Gamal M (2001) An economic Explication of the Prohibition of Gharar in Classical Islamic Jurisprudence,, [www.ruf.rice.edu/~elgamal/files/gharar.pdf](http://www.ruf.rice.edu/~elgamal/files/gharar.pdf)

Mainly affected by the prohibition of maysir are insurance companies, particularly those offering life insurance. In this case maysir is a consequence of gharar. The insurance holder places, more or less, a bet on himself surviving the contract period to then receive the premium. Scholars see this bet on survival as gambling.

### **3.4. Profit and Loss sharing**

The third principle of Islamic Banking is the sharing of profit and loss between two parties involved in a transaction. Instead of borrowing capital at a prespecified rate of interest, a partnership is contracted including the lending bank and the borrower, in which the profits (and therefore the losses as well) are divided at a determined rate. This system is based on the moral and economic beliefs of Islam, since the financial gain for both parties is directly linked to the performance of the venture. Therefore the bank has a vested interest in the long-term success of the project, and not – as in western systems – only until the moment in which the interest and principal are entirely paid back. This caring for long-term performance fosters the whole society's economic and social wellbeing. As a consequence of the cooperation, both sides profit from the deal. The borrower gets the opportunity to implement his business idea, and the lender can profit from a successful activity that brings profit – a profit that is higher than the fixed interest of a conventional bank transaction.

This long-term relationship between the lending bank on the one side, and the borrower on the other, implies higher costs in certain areas - for example, in the performance monitoring of the partner, since in case of failure the investor loses all his invested capital.

### 3.5. Support only Halal activities

According to the Sharia the production and trade of certain prohibited products (Haram) is forbidden, while other products and activities are allowed (Halal). Some examples of Haram products<sup>57</sup>:

- Trade in shares of financial institutions that deal with interest (mainly conventional banks and insurance companies)
- Investments in companies that produce or trade in tobacco and/or alcohol
- Companies that are involved with the production of pork
- Businesses that are concerned with gambling or other similar activities
- Corporations that control nightclubs
- All activities that are connected to pornography or prostitution

The Sharia has enacted regulations about the maximum interest income in a business that is managed in compliance with the Sharia. If a corporation obtains higher earnings out of interest, that is haram, and a Muslim must not invest any more in this company. Furthermore, if a company produces halal goods but invests the profit in activities that return interest, a shareholder should denounce this fact at the annual shareholder meeting. If a part of the gain is made with yield on interest, this share has to be donated for charity purposes at the moment of profit distribution among the shareholders<sup>58</sup>.

### 3.6. Sharia Board

In every Islamic Bank there exists a kind of religious supervisory body – the Sharia Supervisory Board, comparable to a supervisory board in western countries - whose function is to ensure that the bank operates in compliance with the rules of the

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<sup>57</sup> The Encyclopedia of Islam (1960) Vol III, London, p. 173

<sup>58</sup> Altundag P, Haldi N (2005) Handbuch Islamic Banking. Luna Verlag, Zürich, p. 31

Sharia, and to respond to the management's enquiries. Furthermore the Sharia Board plays an important role in the preparation of contracts and the collection and distribution of zakat<sup>59</sup>. This supervisory board plays an important role, since its existence gives credibility to the bank in the eyes of its clients. The appointment of a Sharia Supervisory Board is compulsory under banking laws that have been passed by the United Arab Emirates, Yemen, Jordan, Kuwait and Lebanon, and is a precondition for being admitted into the International Association of Islamic Banks (IAIB).

The Sharia Supervisory Board normally consists of 3-5 members: this is confirmed by the Kuwaiti Islamic Banking Law of 2003, where it is clearly stated, in article 93, that the Board has to be appointed by the general assembly.<sup>60</sup> Their remuneration also has to be fixed by the general assembly. The board members generally have to be men of Islamic Jurisprudence who are qualified by their vocational education to form an autonomous opinion and to issue fatwas. According to the AAOIFI (the Auditing Organisation of Islamic Financial Institutions)<sup>61</sup> only one member of the Board may not be a Jurist, provided he is instead a specialist in Islamic Finance.<sup>62</sup>

Since the qualifications for becoming a member of a Sharia Supervisory Board are various – the candidate has to have profound knowledge of jurisprudence, economy and finance – the number of potential Sharia Board members worldwide is still limited. This problem is well-known in the field: considerable efforts are being undertaken to educate new Sharia Jurists. Current estimates reckon that there are about 50 persons worldwide who meet the standards. This could be the reason for the enormous remuneration of these scholars: extensive investigations can cost 300.000 US –Dollars or more.<sup>63</sup>

One of the tasks of a Sharia Board is to control and approve new financial products before they are offered to clients and used in everyday banking. In fact, the whole financial institution has to be examined before it starts its business activities.

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<sup>59</sup> Lewis M, Algaoud L (2001) Islamic Banking. Elgar, Cheltenham, p. 179ff

<sup>60</sup> El-Gamal (2006) *ibid*, p. 7

<sup>61</sup> The AAOIFI was found in 1991 and provides standards for Islamic Financial institutions. The aim is to harmonize the industry. Until 2007 only 8 countries committed themselves to the standards of the AAOIFI. See: Khalaf Roula 2007

<sup>62</sup> [www.aaofii.com](http://www.aaofii.com)

<sup>63</sup> Hecking (2007) Die Wüste lebt. Rendite trotz Zinsverbot. Financial Times Deutschland 17.09.2007

The members also have to submit an annual statement to the general assembly of the bank, in which they report the extent to which the principles of Islamic Jurisprudence have been met.<sup>64</sup> The independence of the Sharia Board is stipulated clearly in the charter of most financial institutions, as is the fact that the decisions of the Board are binding on the management.

A major problem is the fact that a Sharia Board is not itself supervised. Therefore the establishment of national Sharia Boards, such as the one already operating in Malaysia, is currently being considered. A national or even a supranational Sharia Board would control the different Sharia Boards, so that, for example, contradicting fatwas in different institutions could be avoided.<sup>65</sup>

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<sup>64</sup>Khouildi (1994) La vérification de conformité islamique des opérations bancaires. In: Piccinelli (ed) Banche islamiche in contesto non islamico. Istituto per l'oriente, Roma, p. 81

<sup>65</sup> Gassner (2007) *ibid*, p. 37

## **4. Financial Instruments**

As discussed in the preceding chapters, Islamic Banks have to operate according to the rules of the Sharia, particularly in relation to the prohibition of interest. This has created a need for alternative financial instruments, which permit Islamic banks not only to cover their costs but also to make a profit, despite the prohibition of interest-taking. On the one side, contract forms are used that have been developed by Islamic scholars, and on the other side the forms of financing of conventional banks are modified to prevent an infringement of the Sharia.<sup>66</sup> Islamic finance provides capital in different forms: by equity participation as well as through debt financing. In the case of equity participation, the bank acquires a share (which is at least nominal) of the organization, and shares the profit and loss at the end of the period (PLS, profit and loss sharing). Debt financing is provided for in the form, for example, of a sale contract, where one party (the bank) buys something and sells it later at a higher price (the mark-up).

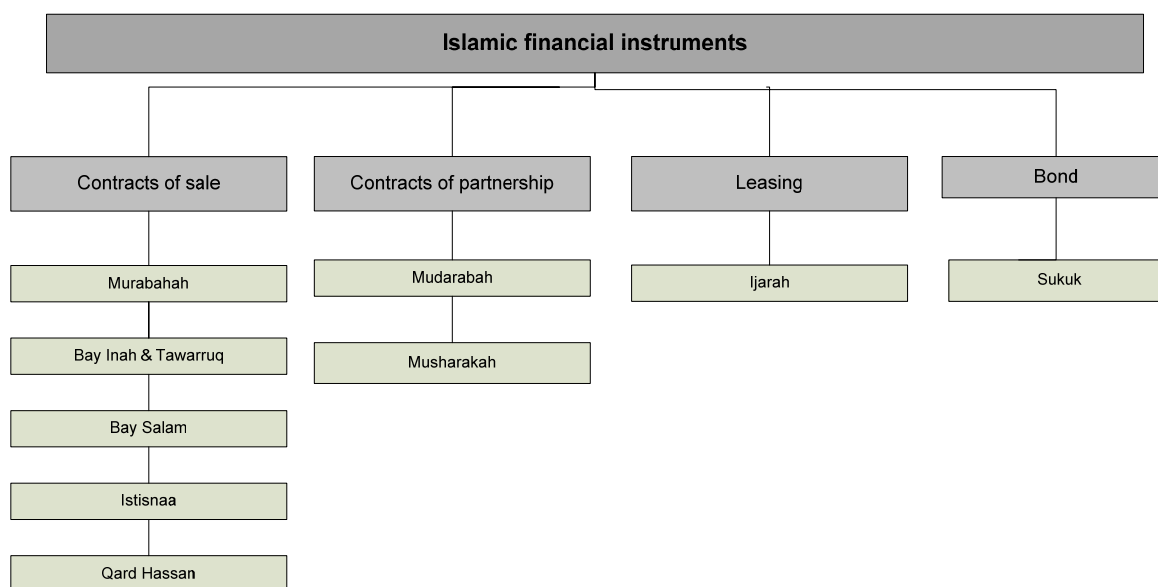


Figure 3 Islamic Financial Instruments.

<sup>66</sup> Piccinelli (1988) *ibid*, p. 4

## 4.1. Contracts of sale

Contracts of sale can be seen as debt instruments. Since it is impossible under Sharia law, as already pointed out, to give out credits that yield interest, credits are granted normally on a mark-up (or cost plus sale) basis, whereby at maturity not only the credit amount becomes due, but also a pre-specified mark-up, payable at once or by installments. Contracts of sale are based on Islamic commercial law and follow certain rules, as already mentioned, such as the ban on selling goods that are not halal, the avoidance of gharar, and the requirement that the object must exist at the moment the contract is closed. But in everyday economic life this is not always possible: for example, a contract regarding the construction of a building would by this definition be illicit. So new forms needed to be developed, such as Istisnaa and Bay Salam.

### 4.1.1. Murabahah

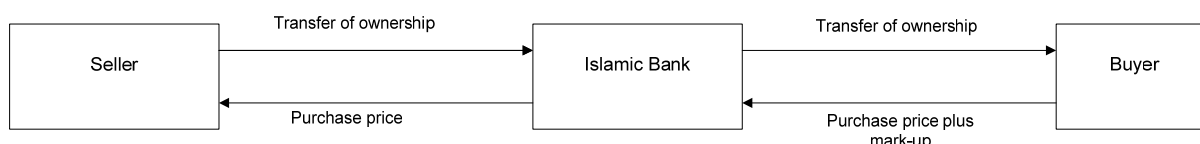


Figure 4 Murabahah basic model

Murabahah is one of the most frequently offered and most frequently demanded financial instruments in Islamic Banking, and means nothing more than a “mark-up sale”<sup>67</sup>. In the literature Murabahah is called either “cost plus financing” or “mark-up sale”<sup>68</sup>. In this case a bank buys a product for a client on the client's instructions, and then sells it to the client later with a mark-up. When the bank sells the product to the initiator, it is delivered immediately: the redemption normally takes place at a later date, as per the redemption contract.

<sup>67</sup> Kabir H, Lewis M (2007) Handbook of Islamic Banking. Elgar, Cheltenham, p. 174

<sup>68</sup> Bälz K (2005) Islamic Finance: Finanziert mit Gottes Hilfe. Zenith Business 3, p. 35-38



The bank acts not only as a financial intermediary, but also as a commercial intermediary. Several points have to be taken into consideration:

- The product must exist at the time of the conclusion of the contract
- The vendor has to be the owner of the product to be sold at the time of the conclusion of the contract
- The product has to be in the physical possession of the vendor
- The sale has to be carried out immediately
- The sale must not be against Sharia law
- The price and the mark-up have to be defined in advance
- The maturity of the redemption has to be fixed in advance
- Even in case of delayed payment, the bank is not allowed to charge interest for default – the price for the product that was sold remains unchanged. In some cases both parties agree on a contribution for charity purposes in case of delayed payment.<sup>69</sup> This contribution becomes due only in the event that the buyer is not able to pay due to financial distress.

According to Warde (2000), 80-90% of financing of transactions undertaken by Islamic Banks take place in the form of Murabahah, mostly in the industry and trade sectors.<sup>70</sup> In this transaction, the bank bears the risk that the buyer does not take delivery, because at the moment the bank buys the product, it becomes the legitimate owner. If the product is damaged, or the buyer finds some severe quality defect, the bank is liable. If the product does not meet its specification, the buyer has the right to refuse delivery.<sup>71</sup> Therefore the bank acts only after its client has entered a binding commitment to subsequently buy the goods. One aspect of this is often criticized in the literature: banks normally base their mark-up calculations on the LIBOR.<sup>72</sup>

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<sup>69</sup> [www.bma.gov.bh/cms/index.jsp?action=article&ID=133](http://www.bma.gov.bh/cms/index.jsp?action=article&ID=133), p. 25

<sup>70</sup> Warde (2000) *ibid*, p. 133

<sup>71</sup> Alkazaz A, Gälli A (1986) *Der arabische Bankensektor*. Band 1. Weltforum Verlag, München, p. 214

<sup>72</sup> Usmani MT (2002) *An Introduction to Islamic Finance*. Kluwer Law International, London, New York, p. 48

#### 4.1.2. Bay Salam

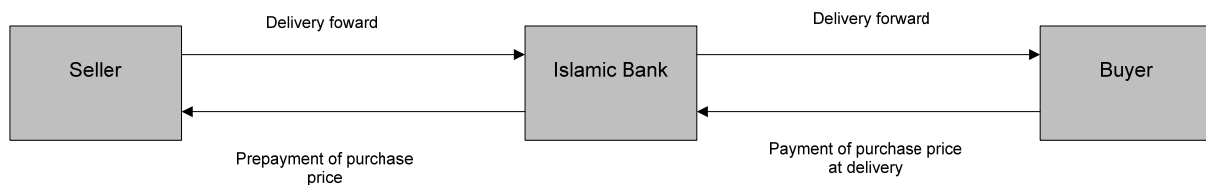


Figure 5 Bay Salam model

The Bay Salam contract could be compared to a forward contract, and is defined as “a sale with advance payment and future delivery”<sup>73</sup>. A basic rule of debt-financed contracts prohibits the sale of a product that does not exist at the time of the conclusion of the contract. The Salam contract is an exception to this rule. Here a product is sold forward; quality and quantity have to be defined in detail in advance. The complete price of this product has to be paid at the time of the conclusion of the contract. This form of financing is used mostly for short-term loans in the agricultural and manufacturing sectors, particularly to small producers and artisans.<sup>74</sup>

The contract is binding, so if the seller is not able to deliver the subject of the contract, he has to purchase it on the market. The profit margin for the bank results in the difference between the price the customer pays and the price the bank pays on the market. In order to assure that no gharar is involved in the transaction, it is important that the product involved is freely available and tradable on the market. Raw materials, commodities and other fungible goods may be traded under a Salam contract: real estate and custom machinery, for example, cannot.<sup>75</sup>

<sup>73</sup> Saleh (1992) *ibid*, p. 89

<sup>74</sup> Piccinelli GM (1994) Contratti bancari islamici per il credito e l'investimento. In: Piccinelli (ed) *Banche islamiche in contest non islamico*. Istituto per L'oriente, Rome, p. 122

<sup>75</sup> Gassner (2007) *ibid*, p. 58

#### 4.1.3. Istisnaa

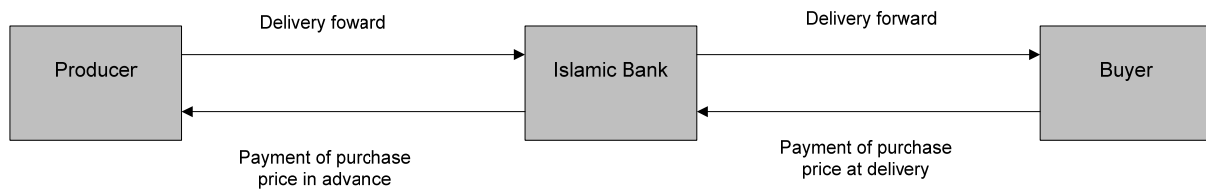


Figure 6 Istisnaa model

The Istisnaa contract is used to finance specially-commissioned products, and is often seen as a special version of the Salam contract: it is also similar to a forward contract. The customer approaches the bank because he needs a special product to be manufactured, and is not able to pay the purchase price himself.

After closing a contract on the transaction, the bank commissions a manufacturer to produce the desired product to the specification of the customer. As well as an initial down payment, the bank makes part payments during the manufacturing process, the last payment being made when the process is completed. The manufactured product is delivered to the bank, which then forwards it to the buyer. The buyer pays the purchase price, with a mark-up, to the bank at the time of delivery, either in a single payment or by installments. This mark-up is the profit margin of the bank. The bank bears the risk that the manufactured product does not meet the buyer's specification, so normally a contractual penalty is agreed that is paid if the producer does not deliver at the agreed time, or delivers a product that does not otherwise comply with the contract. Often Islamic banks also authorize their customers to supervise the production process as their agents, so that they can control this process themselves, and intervene if necessary.<sup>76</sup>

Even though the Istisnaa contract is similar to the Salam contract, there are some differences that should be emphasized. In the case of the Istisnaa contract, the price is not paid at the moment of the conclusion of the contract: in the Salam contract, the purchase price has to be paid in advance. Furthermore, the constitutional idea behind the Istisnaa contract is the manufacturing of a product that does not exist: the

<sup>76</sup> Gassner (2007) *ibid*, p. 61

object of a Salam contract may also need to be manufactured, but should already exist conceptually as part of an established product range.<sup>77</sup>

The Istisnaa contract is used primarily for the production of airplanes, ships and buildings, but the only school that accepts Istisnaa contracts is the Hanafi school<sup>78</sup>.

#### 4.1.4. Bay Inah and Tawarruq

Bay Inah and Tawarruq are two financial instruments that reproduce conventional loans. Any difference with a conventional loan is principally theoretical. In the Bay Inah model, a customer buys raw materials (for example precious metals) and resells them to the vendor immediately on spot. In the Tawarruq contract there is a third party involved: the raw materials are not sold back to the vendor, but to a third party. In practice, these transactions are often settled at the London Metal Exchange<sup>79</sup>.

The only school that allows Bay Inah is the Shafi'i school: the others reject it as not conforming with the Sharia<sup>80</sup>. Tawarruq is also not necessarily allowed: Sharia Boards have to adjudicate on each individual case as it arises. Reasons that are accepted by the Sharia Board as justification include marriage, medical attendance (if there is no better way to finance it), and the transfer of conventional liabilities to an Islamic Bank.<sup>81</sup>

#### 4.1.5. Qard Hassan

Qard Hassan literally means "*good loan*". It is a form of financing without the intention to make a profit – a non-profit loan. This form is found particularly in private life, where members of a family or clan provide funds for other family members in need.<sup>82</sup> Islamic Banks offer this service to entrepreneurs in financial distress, who thus get a

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<sup>77</sup> Altundg/Haldi (2005) , p. 61

<sup>78</sup> Vogel/Hayes (1998) *ibid*, p. 146

<sup>79</sup> Gassner (2007) *ibid*, p. 56

<sup>80</sup> El-Gamal (2006) *ibid*, p. 71

<sup>81</sup> Gassner (2007) *ibid*, p. 57

<sup>82</sup> Gassner (2007) *ibid*, p. 62

loan without having to pay a mark-up.<sup>83</sup> A bank can also use the proceeds from the zakat tax for this kind of charitable loan. The Islamic Development Bank offers this service to member countries, and to countries that belong to the OIC, for the purpose of financing development projects in these countries.<sup>84</sup>

## **4.2. Contracts of partnership**

Contracts of partnership are equivalent to equity participation, where one partner provides at least part of the capital while the other provides the know-how. The profit, but also any possible loss, is divided among both parties according to a previously-specified ratio: therefore this system is also known as profit and loss sharing (PLS). Both parties to the contract bear the risk. In this form of contract, the financial institution acts as an intermediary between the entrepreneur who conducts the business, and the depositor who provides the capital: it does not shift the risk to the depositor.<sup>85</sup> The obligations, liabilities, but also the rights of the two partners depend on the chosen form of financing. The profit for the financial institution is composed of the spread between the part of the gain it gets from the entrepreneur and the amount it returns to the depositor.<sup>86</sup> According to Gassner (2007), only 5% of the financing of Islamic Banks is based on contracts of partnership or equity participation.<sup>87</sup>

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<sup>83</sup> Pichler (2007) *ibid*, p. 45

<sup>84</sup> Piccinelli (1994) *ibid*, p. 126

<sup>85</sup> Vogel/Hayes (1998) *ibid*, p. 130

<sup>86</sup> Saleh (1992) *ibid*, p. 126

<sup>87</sup> Gassner (2007) *ibid*, p. 67

#### 4.2.1. Mudarabah

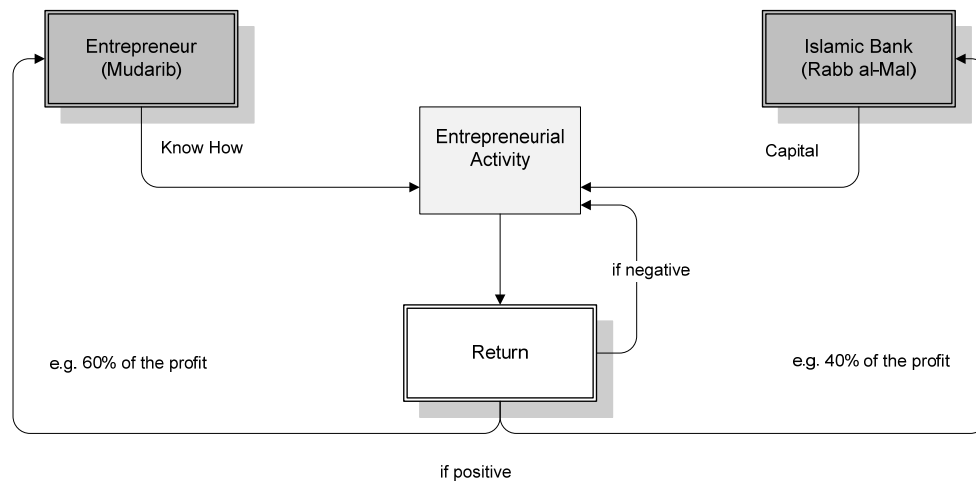


Figure 7 Mudarabah basic model

Saleh's (1992) definition of Mudarabah is this:

*"A contract between at least two parties whereby one party, called the investor, entrusts money to the other party, called the agent manager, who is to trade with it in an agreed manner, and then return to the investor the principal and pre-agreed share of the profits, and keep for himself what remains of such profits."*<sup>88</sup>

In a Mudarabah contract, the bank plays the role of the investor, and the entrepreneur is the agent manager. As mentioned, the profit is shared according to a pre-specified ratio among the two parties, while the investor bears any loss alone - since the agent manager has not put any money into the business. If the losses exceed the contributed capital, the financial institution does not have to answer for it – it can only lose the paid up capital. The bank's risk is quite high, since the agent manager is not allowed to provide any collateral: that would be against the fiduciary nature of this form of financing, since more than just the mere effort of the entrepreneur would be at stake if a capital guarantee were to be given in the form of

<sup>88</sup> Saleh (1992) *ibid*, p. 128

collateral. It is also possible that the entrepreneur provides part of the capital as well, in addition to his labour.<sup>89</sup> Only in the event that the agent manager does not behave according to the contract, or commits verifiably gross negligence, or acts with malicious intent, is he liable for a potential loss.<sup>90</sup>

There exist two different forms of Mudarabah: limited and unlimited. In the limited form, the customer is bound to certain requirements regarding the investment alternatives provided by the investor, although excessive restrictions do not have to be followed by the agent manager<sup>91</sup>. In the unlimited form, the entrepreneur is free to act as he wishes, and to invest in whatever manner he decides, of course only in compliance with the Sharia. Unlimited Mudarabah contracts are rather unusual.

Udovitch (1970) speaks of a “hybrid status”, since in this special form of financing we find a combination of partnership and loan, with the advantages of both.<sup>92</sup> Today Mudarabah is applied in various sectors, such as agriculture, industry and the service sector.

#### 4.2.2. Musharakah

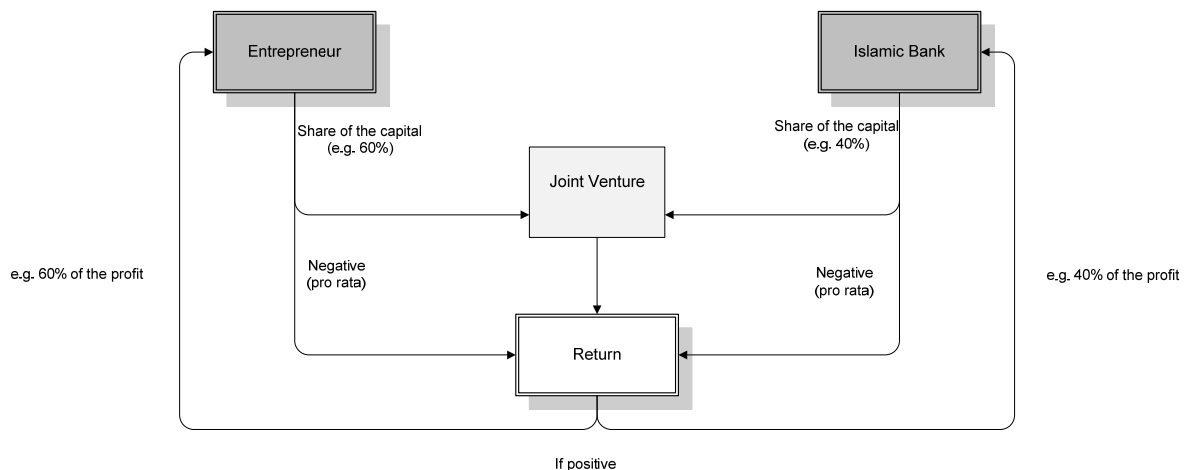


Figure 8 Musharakah model

<sup>89</sup> Kabir/Mervyn (2007) *ibid*, p. 179

<sup>90</sup> Gassner (2007) *ibid*, p. 63

<sup>91</sup> Ray N (1995) *Arab Islamic Banking and Renewal of Islamic Law*. Graham & Trotman, London, p. 71

<sup>92</sup> Udovitch A (1970) *Partnership and Profit in Medieval Islamic Law*. Princeton University Press, Princeton, p.171

Musharakah, which literally means “partnership”, is a longer-term equity based arrangement, quite similar to Mudarabah. In this form of financing, too, the bank provides capital for a project an entrepreneur wants to undertake: the main difference with Mudarabah is that both parties contribute to the financing of the business, and have equal management rights. Therefore we could call a classical Musharakah an Islamic Joint Venture.<sup>93</sup> It does not have to be a new project - it can be an already existing one. Sometimes not only the provision of money is shared among the partners, but the financial institution can also participate in the management of the business. If the bank does not exert its management rights and only follows the development periodically, the entrepreneur is compensated for his services as a manager.<sup>94</sup>

The profit that arises from the project is divided among the partners when the partnership is over, but not necessarily in the ratio in which the parties provided the capital. The share of the profit each partner receives at the conclusion of the contract has to be pre-specified in advance. Possible losses have to be borne by all partners according to the amount of capital provided.

The liability is unlimited, since all partners have equal management rights - even when the bank does not exert this right.<sup>95</sup>

We know of two forms of Musharakah: permanent and diminishing. The permanent Musharakah constitutes a form a financing with unlimited contract duration: it is seldom found today.<sup>96</sup> The partnership continues up to the moment that the contract is dissolved: in this case the financial institution receives annually a share of the profit, according to a pre-determined ratio.<sup>97</sup> The capital is fixed for a lengthy time period.

In the diminishing Musharakah, the financial involvement of the bank reduces with time. The shares held by the financial institution are sold back to the entrepreneur, until he owns 100%. The entrepreneur pays a higher price than the original value of

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<sup>93</sup> Warde (2000) *ibid*, p. 136

<sup>94</sup> Alkazaz/Gälli (1986) *ibid*, p. 209

<sup>95</sup> Gassner (2007) *ibid*, p. 65

<sup>96</sup> Klarmann (2003) *ibid*, p. 147

<sup>97</sup> Khiyar(2005) *ibid*, p. 174



the shares: as a result, the bank makes a capital gain. This form of Musharakah is used for short term financing, mostly in the real estate sector.

#### 4.2.3. Leasing (Ijara)

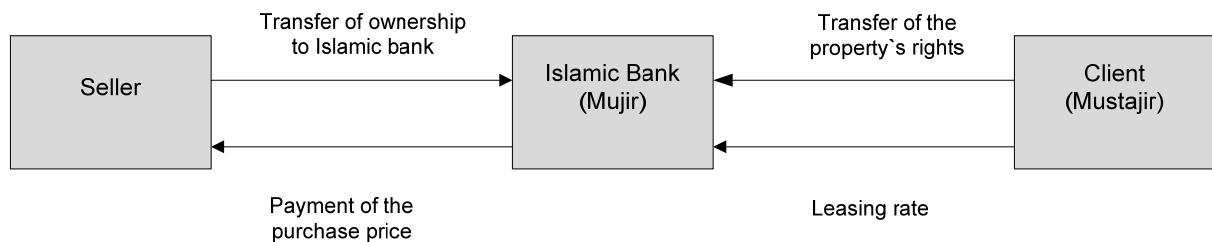


Figure 9 Ijara model

Saleh (1992) defines Ijara as

*„A contract where the subject matter is the lawful and defined use (manfa<sup>c</sup>a) of a lawful and determined corporeal object (ʿayn) for a specific period of time. It is also a contract for providing a defined work for a fixed price”<sup>98</sup>*

Ijara describes a hire purchase, or a lease. It is the equivalent to the western system of leasing, and takes the form of medium- or long-term contracts. The bank acquires an asset and leases it to the client. The right of use of the object involved is granted to the lessee, while the bank remains the owner. The installments to be paid, normally a fixed percentage of the purchase price, and the period for which these installments must be paid by the lessee are both fixed in advance. Therefore a unilateral increase of the installments by the lessor is forbidden. On the other hand, the contract may contain a clause that defines a determined annual percentage

<sup>98</sup> Saleh (1992) ibid, p. 12

increase in the installments, or stipulate a link to a particular market index, because in this case the up-rating is fixed in advance.<sup>99</sup>

Several conditions have to be fulfilled for a leasing contract to be legal according to the Sharia:

- The ownership remains with the bank, which also has to take care of the maintenance (therefore objects that are consumed by usage, like oil, cannot be the object of such a contract)
- The lessee has to be able to dispose of the object without any hindrance
- The contract remains intact if the object is damaged during the leasing period. The lessee is only liable for any damage caused by misuse or negligence: if the object is otherwise destroyed, or heavily damaged, the lessee has no obligation either to replace the object or to pay further rent. The loss is borne by the lessor: for this reason, the object of a leasing contract is normally insured against these risks.
- The right of use of the object is transferred to the lessee for a specified time period and a pre-determined rent
- The costs that result from the usage of the object have to be borne by the lessee (e.g. if the object is a house, the lessee has to pay for the consumption of water, electricity and gas - but the lessor, as the owner, has to pay any taxes on it)
- The Ijara starts on the day on which the object is handed over to the lessee
- In case of delayed payment by the lessee, it is forbidden to levy default interest. It is however possible to stipulate in the contract that the lessee has to donate a pre-determined amount of money for charitable purposes.<sup>100</sup>

Two different forms of Ijara are known and used in Islamic Banking: pure Ijara, and Ijarah wa Iqtina. In the case of a pure Ijara, the object has to be returned to the lessor at the end of the leasing period in the state in which the lessee initially received it.

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<sup>99</sup> Klarman (2003) *ibid*, p. 254

<sup>100</sup> Altundag/Haldi (2005) *ibid*, p. 57

Parallels to the Murabahah can be drawn, but whereas the rents in the case of Murabahah transaction are fixed and cannot be changed after the contract is agreed, it is possible in an Ijara transaction - if both parties agree – to vary the installment payments during the leasing period. Another difference lies in the fact that the rents paid by the lessee do not fully cover the purchase price of the object: the bank has either to find a new lessee, or to sell the object after the expiration of the Ijara contract.

A special form of the Ijara contract is the Ijara wa Iqtina, which can be seen as a lease-purchase transaction, whereby the lessee has the option to purchase the object at the end of the leasing period.<sup>101</sup> According to Vogel and Hayes (1998)<sup>102</sup>, the pure form of Ijara is the one mostly used in modern Islamic Banking. In my view the Ijara wa Iqtina is of greater significance, since it allows a bank to sell capital and cost intensive projects at contract expiry, removing the risk of losing capital by remaining the owner.

#### 4.2.4. Sukuk

Sukuk, also known as Islamic bonds, is one of the fastest developing fields in Islamic Banking. In the last few years it has attracted a lot of attention on the international financial markets. Conventional bonds yield interest, therefore until a few years ago the purchase of bonds was forbidden under the Sharia. This prohibition led scholars to search for alternatives to conventional bonds. The Sukuk was developed in Malaysia (which holds today nearly 60 percent of the total Sukuk market<sup>103</sup>) as a type of investment very similar to conventional bonds, but without the payment of interest. Sukuk is the plural of Sakk, meaning certificate<sup>104</sup>: the word cheque is derived from Sakk. Sukuk are similar to “pass-through certificates” or “investment certificates”.<sup>105</sup> A major difference with conventional bonds is the fact that the volume of the issue is

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<sup>101</sup> Khouildi A (1994) Un contrat “islamique”: le leasing. In: Piccinelli (ed) Banche islamique in contest non islamico. Istituto per L’oriente, Roma

<sup>102</sup> Vogel/Hayes (1998) *ibid*, p. 190

<sup>103</sup> Von Hardenberg C (2006) Wachsen nach den Regeln des Koran. Financial Times Deutschland 22.12.2006

<sup>104</sup> Gassner (2007) *ibid*, p. 95

<sup>105</sup> Wilson R (2004) Overview of the sukuk market. In: Abdulkader et al. (eds) Islamic Bonds Your Guide to Issuing, Structuring and Investing in Sukuk, London, p. 3

limited by the value of the underlying asset. Therefore a Sukuk is less flexible than a conventional bond. Furthermore, tax treatments, which differ from country to country, have to be considered.

The AAOIFI defines investment Sukuk as follows:

*“Investment Sukuk are certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activity, however, this is true after the receipt of the value of the Sukuk, the closing of the subscription and employment of funds received for the purpose for which the Sukuk was issued.”<sup>106</sup>*

Different assets (e.g. real estate) are bundled and brought into a special purpose vehicle (SPV). Then the bond is issued on the capital market, where investors can purchase shares of the SPV. The Sukuk owners do not receive interest payments but a compensation fee like rental income or leasing rates.<sup>107</sup> The structure is very closely related to the well-known asset backed securities, but with the difference that in the case of a Sukuk the underlying security can be either an asset or a leasing contract. The mere bundling of cash flows (like credits) is not allowed. Another difference is that conventional bondholders can be seen as lenders to the issuing company, where the bond is a debt obligation, whereas a Sukuk holder actually owns a share of the asset or SPV.

There are different forms of Sukuk (14 have been registered by the AAOIFI) such as the Sukuk-al-Ijara, Sukuk-al-Mudarabah, Sukuk-al-Musharakah, hybrid or pooled Sukuk, zero-coupon non-tradable Sukuk, embedded Sukuk, and many more.<sup>108</sup> Two major classes can be defined: Sukuk that earn a pre-specified profit (like the Sukuk-al-Ijara), and Sukuk that entitle the bearer to a share of the profit, and even the loss

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<sup>106</sup> [www.aaofii.com/aaofii\\_sb\\_sukuk\\_Feb2008\\_Eng.pdf](http://www.aaofii.com/aaofii_sb_sukuk_Feb2008_Eng.pdf)

<sup>107</sup> Hecking (2007) *ibid*

<sup>108</sup> Tariq AA (2004) Managing financial risks of sukuk structures. Loughborough University, Loughborough

(for example, the Sukuk-al-Mudarabah and the Sukuk-al-Musharakah). The most-used form is the Sukuk-al-Ijara, where the investor earns a pre-determined profit.

#### Mudarabah Sukuk:

This Sukuk is based on a Mudarabah contract. The issuer of the Sukuk is the seller, the clients buy the shares and become thereby the owners of the goods traded in the Mudarabah contract. The owners have the right to resell their shares on the market. The profit is shared according to the percentage of ownership. This type of Sukuk is employed in order to encourage public participation in important projects. The Shamil Bank of Bahrain, for example, issued a Sukuk worth 360 million Saudi Riyal for a real estate investment project in Saudi Arabia through the Al Ehsa Special Realty Mudarabah.<sup>109</sup>

#### Musharakah Sukuk:

This form is based on a Musharakah contract and is very similar to a Mudarabah Sukuk - also in this case the buyers become owners by acquiring a share of the Musharakah equity, which is brought into a SPV, and are entitled to trade the Sukuk on the financial market. The issuer of the Sukuk is the party that starts the partnership in a specific project. 550 million USD were raised in a Musharakah Sukuk for the development of a new engineering centre at the airport of Dubai, which was then leased to Emirate Airlines. The owners of the Sukuk were compensated with the rental income paid by Emirate Airlines. Another example is Sitara Chemical Industries Ltd, which raised 360 million Riyal in 2002.<sup>110</sup>

#### Sukuk-al-Ijara:

This form is based on an Ijara contract. The issuer sells the right of use of an asset, therefore the subscribed capital represents the price of this right. The buyers become

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<sup>109</sup> Nisar S (2007) Islamic Bonds (Sukuk). It's Introduction and Application.  
[www.financeinislam.com/article/8/1/546](http://www.financeinislam.com/article/8/1/546)

<sup>110</sup> Nisar (2007) ibid

the owners of the right of use. The Sukuk-al-Ijara is mostly applied to real estate, in which case the rental is paid to the owners of the Sukuk. In practice, this form is widely used. In 2000 Guthrie Berhad raised 400 million USD with a Sukuk-al-Ijara (Al-Muntahiyah Bit-Tamik) to acquire an oil plantation in Indonesia. This Sukuk was conceded by a consortium of banks, who also acted as subscribers to the Sukuk<sup>111</sup>.

#### Murabahah Sukuk:

This form is based on a Murabahah contract. The issuer of the Sukuk is the seller of the asset in the Murabahah contract, whereas the subscribers represent the buyers of the asset and become its owners. The shares are not tradable. An example of a Murabahah Sukuk is the multi-currency Sukuk issued by Hypo-Vereinsbank AG, Standard Bank Plc and WestLB AG: it had a volume of 155 million USD plus Euro 46 million, and was entrusted by a Bahrain company (Arcapita Bank).<sup>112</sup>

#### Salam Sukuk:

This form is based on a Salam contract. The issuer of the Sukuk is the seller, while the subscribers are the buyers and become owners of the asset. In this case the Sukuk is not tradable, since Sharia dictates that the asset can not be resold before it comes to the real possession of the owner. Therefore an investor will purchase a Salam Sukuk only if he expects the value of the underlying to rise until maturity. The Bahrain government issued a Salam Sukuk based on aluminium.<sup>113</sup>

#### Istisnaa Sukuk:

This Sukuk is based on an Istisnaa contract. The issuer of the Sukuk is the producer or manufacturer of the product, whereas the subscribers are the buyers. The subscribed capital represents the price of the product. Istisnaa Sukuk are often used for infrastructure projects, as in the case of the Durrat Sukuk, which is financing the

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<sup>111</sup> Nisar (2007) ibid

<sup>112</sup> Nisar (2007) ibid

<sup>113</sup> Nisar (2007) ibid

infrastructure development of the artificial island project called Durrat-al-Bahrain.<sup>114</sup>  
The Istisnaa Sukuk is not tradable on the secondary market.

### Sukuk Issuance (US\$ million)

Year	2000	2001	2002	2003	2004	2005	2006
<b>Corporate Sukuk</b>	336.3	530	179.9	4537.06	5731.19	11358.89	24526.32
<b>Sovereign Sukuk</b>	0	250	800	1180	1479.35	706.5	2271.6
<b>Total Sukuk issuance</b>	336.3	780	979.9	5717.06	7210.54	12065.39	26797.92
<b>Percentage Growth</b>		131.94	25.63	483.43	26.12	67.33	122.11

Figure 10 Sukuk Issuance<sup>115</sup>

One motivation for the expansion of Sukuk all over the world is the composition of portfolios of Islamic investors. Because before the emergence of Sukuk no bond-like financial instrument existed that complied entirely with the Sharia, most portfolios were composed of 60-70% real estate, designed to provide fixed income<sup>116</sup>. By comparison, non-Islamic portfolios typically include about 30% real estate, because they reflect the additional requirement that assets should be liquid. Most forms of Sukuk are tradable, and therefore also provide liquidity - at least in theory.

According to Taqi Usmani (2007), the chairman of the AAOIFI board, nearly 85% percent of Sukuk all around the world do not comply with Sharia<sup>117</sup>. Most Islamic bonds have been sold with the promise to pay back the face value at maturity.

<sup>114</sup> Nisar (2007) ibid

<sup>115</sup> Nisar (2007) ibid

<sup>116</sup> Gassner (2007) ibid, p. 96

<sup>117</sup> Abdulkader T, Becic M(2007) Are Sukuk Islamic? The Sukuk market: December 2007 Report  
<http://islamicfinancepro.files.wordpress.com/2008/01/are-sukuk-islamic-the-sukuk-market-december-2007-report.pdf>

Taqi Usmani (2007) criticizes this promise, saying that it is contradictory to the ideas of risk, profit and loss sharing. But according to a director of Deutsche Bank in Dubai, if the AAOIFI were to tighten regulations "the Sukuk would become more of a profit sharing instrument ... from a debt-like instrument to equity, and that's a fundamental change of mindset for investors and issuers".<sup>118</sup> The profit would depend on the development of the underlying asset, and therefore become riskier.

The fact that most Sukuk are not Sharia compliant could lead to serious problems. To date there is no real secondary market for Sukuk, mostly because of the lack of critical mass. For example: if investors had wanted to sell their shares on the financial markets in the middle of the 2008 credit crisis, no other investor would have been keen to buy them - only (mainly Islamic) banks would have been left as buyers. However, these banks are not allowed to purchase Sukuk that are not Sharia compliant, because the transaction has to be approved by the Sharia Board.

Nevertheless, Sukuks are issued not only by Islamic institutions, but with greater frequency also by non-Islamic companies such as UBS and Deutsche Bank AG,<sup>119</sup> who see them as a way to access capital from rich Islamic countries - mainly the Gulf States. Great Britain was one of the first countries to pave the way for a Sukuk market in Europe: Brown announced in 2007 that issuers of Sukuk would be granted tax advantages equal to those bestowed upon other, equivalent financial instruments.<sup>120</sup>

### **4.3. Stock investment**

Investment in stocks is a very important field of Islamic finance. Since bonds that bear interest are forbidden, most investors that want to make Sharia compliant investments put capital into the stock market. According to scholars, the investment in shares is desirable, because capital is provided directly for productive purposes. Unlike bondholders, shareholders participate actively in the risk of the company – which conforms with the ideas of Islamic banking.

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<sup>118</sup> [www.arabianbusiness.com/504577-most-sukuk-not-islamic-say-scholars](http://www.arabianbusiness.com/504577-most-sukuk-not-islamic-say-scholars)

<sup>119</sup> Bälz (2005) *ibid*, p. 38

<sup>120</sup> [www.islamicfinancenews.com/pdf/Legal07.pdf](http://www.islamicfinancenews.com/pdf/Legal07.pdf)



Institutions all over the world have reacted to the increased demand from Islamic countries and created several indices: examples are the Dow Jones Islamic Market Index (Dow Jones was the first to open a Islamic Index in 2000, and today offers more than 80 different indices)<sup>121</sup>, Standard & Poor's S&P Sharia Index (which followed Dow Jones in 2006)<sup>122</sup>, and the FTSE Islamic Index<sup>123</sup>.

There is no real difference between Islamic and conventional shares. The difference lies in the constraints that are dictated by the Sharia. As already discussed in chapter 2.5, various activities are forbidden as haram: investors must not invest in companies that produce or deal with alcohol, weapons, pork related products and tobacco. Furthermore, investing in conventional financial institutions (banks) and companies that operate in the entertainment sector (casinos, gambling, cinema, music, pornography) and in the advertising and media sectors (newspapers are an exception) is also forbidden. Hotels and airline companies are also not allowed, because they serve their clients alcoholic drinks.<sup>124</sup> If a company has passed this test, its financial ratios are examined in detail. For the Dow Jones these financial ratios are as follows:

- The debt-equity ratio must be less than 33 percent.
- Accounts receivables divided by the 12-month average market capitalization must be less than 33 percent
- Cash plus interest-bearing securities divided by the trailing 12-month average market capitalization must be less than 33 percent.<sup>125</sup>

The S&P Sharia index varies in certain points:

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<sup>121</sup> [www.djindexes.com/mdsidx/?event=showIslamic](http://www.djindexes.com/mdsidx/?event=showIslamic)

<sup>122</sup> [www2.standardandpoors.com/spf/pdf/index/Shariah\\_Methodology.pdf](http://www2.standardandpoors.com/spf/pdf/index/Shariah_Methodology.pdf)

<sup>123</sup> [www.ftse.com/japanese/Indices/FTSE\\_Global\\_Islamic\\_Index\\_Series/index.jsp](http://www.ftse.com/japanese/Indices/FTSE_Global_Islamic_Index_Series/index.jsp)

<sup>124</sup> [www.qantara.de/webcom/show\\_article.php/\\_c-468/\\_nr-711/i.html?PHPSESSID=.](http://www.qantara.de/webcom/show_article.php/_c-468/_nr-711/i.html?PHPSESSID=)

<sup>125</sup> [www.djindexes.com/mdsidx/index.cfm?event=showIslamicMethod](http://www.djindexes.com/mdsidx/index.cfm?event=showIslamicMethod)

- Cash plus interest-bearing securities divided by the trailing 12-month average market capitalization must be less than 49 percent
- In certain cases, companies are admitted into the S&P Sharia universe even if they earn profits from haram activities, provided that the income from haram activities is less than 5 percent of the total.<sup>126</sup>

These measures have protected investors from serious losses in several cases, such as Parmalat and WorldCom<sup>127</sup> - an independent Sharia Board supervises the compliance with the rules. The stock exchanges in Islamic countries are normally not subject to the rules of the Sharia. Stock exchanges are obliged to follow these rules only in Sudan and Iran, where the whole economy has been changed to an Islamic system. The Dubai Financial Market has also voluntarily opted for operating in compliance with Sharia rules.<sup>128</sup>

It is worth mentioning the increasing number of Islamic funds, into which potential investors put their capital with the aim of obtaining a Sharia compliant profit. Today more than 250 Islamic funds exist all over the world.<sup>129</sup> The AAOIFI has approved these funds under certain conditions.<sup>130</sup> Two of the key conditions that have to be considered in the context of Islamic funds are as follows:

- The fund capital must only be invested in halal activities
- No fixed interest is paid, but the profit is divided on a pro-rata basis. The investor only receives payments if the fund earns a profit: if it makes a loss, the investor has to bear his part of that loss.

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<sup>126</sup> [http://www2.standardandpoors.com/spf/pdf/index/Shariah\\_Methodology.pdf](http://www2.standardandpoors.com/spf/pdf/index/Shariah_Methodology.pdf), p. 6ff

<sup>127</sup> [www.qantara.de/webcom/show\\_article.php/\\_c-468/\\_nr-711/i.html?PHPSESSID=](http://www.qantara.de/webcom/show_article.php/_c-468/_nr-711/i.html?PHPSESSID=)

<sup>128</sup> Gassner M (2006) Exchanges and Islamic Finance. In: Handbook of World Stock, Derivative & Commodity Exchanges, p. 1

<sup>129</sup> Gassner (2007) *ibid*, p. 136

<sup>130</sup> [www.aaoifi.com](http://www.aaoifi.com)

## 4.4. Deposit accounts

Deposit accounts are accounts that contain a client's savings. Conventional interest-bearing accounts are not compliant with Sharia rules: Islamic banks offer three principal types of deposit accounts.

### 4.4.1. Current account

This type of account is comparable to the conventional current account. The redemption of the capital is guaranteed by the bank, and the client has the right to withdraw money at any time. The bank can invest the capital, but only according to the rules of the Sharia. As a consequence, if the account is not offered by an Islamic bank, but by a conventional financial institution that offers Islamic products through an Islamic window, the bank has to provide an assurance that the capital is genuinely used only for halal activities. Of course, the account does not bear interest due to the prohibition of *riba*, and in contrast to a conventional current account no overdraft facilities exist. If the account is in debit, the bank must not levy overdraft interest, but it is allowed - as it is the case with some banks in Great Britain - to charge a fixed amount as a surcharge.<sup>131</sup> Normally the bank also offers financial services with an account, such as credit and check cards, online and telephone banking. This type of account is used for regular monetary transactions.

### 4.4.2. Savings account

The savings account represents a short or middle term investment possibility, since this type of account produces a yield. The bank invests in relatively risk-free short or middle term projects, deducts costs and a fee from the proceeds and distributes the rest to the client. The share of the bank's profit depends on the amount of capital invested by the client, and sometimes on the period of cancellation<sup>132</sup>. Two different forms of savings accounts are used: the first one is based on the *Wadiah* model, where the redemption of the capital invested is guaranteed by the bank. According to

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<sup>131</sup> Gassner (2007) *ibid*, p. 78

<sup>132</sup> Gälli/Alkazaz (1986) *ibid*, p. 202

the Sharia the proceeds disbursed by the bank have to be seen as a gift to the investor: in reality, banks align themselves with the interest paid out by conventional banks.<sup>133</sup>

The second type of savings account is based on the Mudarabah model, in which the redemption of the capital is not guaranteed by the bank. The two parties engage in a partnership, where the profit is shared according to a pre-determined ratio.

#### 4.4.3. Investment account

This type of account is targeted on earning proceeds with a pre-specified duration or period of cancellation. The account works on a profit-and-loss-sharing basis, which is the ideal form according to Islamic scholars. The bank operates with the invested capital, the redemption is not guaranteed, but the client has to bear possible losses. The proceeds are distributed between the bank and the client according to a pre-specified ratio.<sup>134</sup> Withdrawing money is only possible if the client accepts a discount. Two different types of investment accounts are used: the General Investment Deposit, where the client allows the bank to choose which project to invest in, and the Special Investment Deposit<sup>135</sup>, where the client himself decides how the capital is invested.

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<sup>133</sup> Gassner (2007) *ibid*, p. 79

<sup>134</sup> [www.islamicbanking.nl/chap4.html#\\_Toc3149105](http://www.islamicbanking.nl/chap4.html#_Toc3149105)

<sup>135</sup> Gassner (2007) *ibid*, p. 80

## **5. Islamic Banking in practice**

Theoretically, according to the requirements of the Sharia, the Islamic Banking system relies on PLS (profit and loss sharing). Many studies accentuate the superiority of this system in comparison to conventional banking: the main reasons given are centred on the sharing of equity risk.<sup>136</sup> Another argument in favour of Islamic Banking is that long-term financing fosters growth in the countries involved.<sup>137</sup> However, according to scholars Islamic Banks have not always met the requirements for Sharia compliant banking in reality. A study by Aggarwal and Yousef (2000) revealed that most financing offered by Islamic Banks was not compliant with the principles of PLS, but instead very much the same as conventional debt instruments.<sup>138</sup> According to this study, the maturity of contracts offered by Islamic Banks is normally between one and two and a half years.<sup>139</sup> Different explanations can be found for this phenomenon.

Firstly, PLS contracts are susceptible to adverse selection as well as agency and moral hazard problems<sup>140</sup>. In capitalistic systems, only the owners of the means of production, the entrepreneurs, are entitled to claim the profit. On the other hand, the productivity of capital is of crucial importance to capitalists, and therefore the willingness to share losses accrued during the production process is very limited. In PLS contracts, amoral entrepreneurs have an incentive to hide profits so that their own profit increases. Thanks to their knowledge of these agency and moral hazard problems, capitalists are reluctant to invest into PLS products. In conventional banking, one way to prevent the situation in which one party does not fulfil the contract is to pledge the collateral against the liability in case of default – a solution that cannot be applied to Islamic Banking.

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<sup>136</sup> For example: Ebrahim M, Safadi A (1995) Behavioural Norms in the Islamic Doctrine of Economics. A comment. *Journal of Economic Behaviour and Organization* 27:151-157

<sup>137</sup> For example: Chapra U (1998) *Islam and the Economic Challenge*. Islamic Foundation, Leicester

<sup>138</sup> Aggarwal R, Yousef T (2000) Islamic banks and investment financing. *Journal of Money, Credit and Banking* 32:93-120

<sup>139</sup> Aggarwal Y (2000) see also: Pourian H (1995) The experience of Iran's Islamic Financial system and Its Prospect for Development In: *Development of Financial Markets in the Arab Countries, Iran and Turkey*. Cairo

<sup>140</sup> Iqbal M, Llewellyn D (2002) *Islamic Banking and Finance. New Perspectives on Profit Sharing and Risk*. Elgar, Cheltenham, p. 40-57

A second reason could be the lack of clearly defined property rights, which is the basic prerequisite for a PLS contract to work efficiently in a large number of Muslim countries. Another explanation would be the almost non-existence of secondary markets for PLS instruments. Choudhury (1998) mentions another possible point in the discussion. He claims that PLS contracts are not contracts in a real sense, since although the involved parties share financial resources, the investors are not involved in the decision making process. Another important point is the unequal tax treatment of PLS and interest. Interest is not fully taxed, since it is seen as a cost item, while profit is usually taxed in its entirety.

Also important in the choice of PLS as a financing instrument is the high degree of risk, which makes it hard to use PLS as a short-term financial resource for projects. Islamic Banks therefore rely on other methods, like mark-ups, to assure a certain degree of liquidity. According to Iqbal (1998) approximately 70% of investments financed by Islamic Banks are financed on this basis.<sup>141</sup> In contrast, most banks in Switzerland and Iran do not rely on mark-ups, but instead use the PLS system.<sup>142</sup> Also of major importance is the fact that rules for control and monitoring were designed for conventional banking, and do not work properly for Islamic Banks. Debt financing requires much less monitoring and control than a PLS system - generally speaking, Islamic Banking requires special skills not yet available in a large number of commercial banks.

For many investors, a crucial factor in deciding against PLS is the need to fix the costs of funding in advance. The availability of Sharia conforming capital on the market is bigger than the demand, so Islamic Banks have had to adjust (for example, by using mark-ups) to the needs of their clients.

Another point that has to be considered is the non-participatory nature of these contracts (Choudhury 1998). The investor provides capital without receiving the right to participate in the decision making process, which allows a sleeping partnership.

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<sup>141</sup> Iqbal M (2006) Challenges facing Islamic Banking, Paper presented on the 6th Orientation Course in Islamic Economics, Banking and Finance, The Islamic Foundation, UK, 21-27 September

<sup>142</sup> Dar H, Presley J (2003) Islamic Banking, In: Mullineux et al (eds) Handbook of International Banking. Elgar, Cheltenham, p. 191-206

Bälz (2006) finds an interesting answer to the question as to whether there is a difference between Islamic and conventional products. In his opinion, the answer depends on whether one bases one's point of view on an economic or on a legal perception of the problem. According to the economic point of view there is little difference, since Islamic banks also take fees for their services, even though they don't call it interest. The term 'interest' is much narrower in the Sharia, therefore services by an Islamic institution are structured in a different way, so that interest is not taken openly.<sup>143</sup>

Another problem for Islamic financial institutions is the interpretation of the prohibition of riba. There is no universal interpretation of riba, or of the Sharia itself. Every Islamic financial institution engages its own scholars, in the Sharia Board, who have the job of determining whether a product is Sharia compliant or not. This fact causes massive discrepancies between different banks: a product can be accepted as Sharia compliant by one Sharia Board, and rejected by another. One way to avoid such inconsistencies would be to adopt the standards of the AAOIFI, or of other related organizations: another would be to create a centrally-managed institution that controls the individual Sharia Boards, as has happened already in Malaysia.<sup>144</sup> This process of harmonization is one of the most urgent challenges for the Islamic Banking sector, since the absence of standardization leads to a lack of confidence among investors.

Another challenge is the financial reporting and accounting of Islamic banks. Most of these banks are located in countries where they have to present their annual balance sheets according to international standards, like IRFS, as well as Islamic guidelines. The problem is that no consistent standards exist for reporting. The AAOIFI has presented 25 accounting standards, but they are not compulsory in most countries.<sup>145</sup> Quite apart from accounting and reporting, taxation also plays an important role. Interest is not fully taxed since it is seen as a cost item, while profit is fully taxed. Some Islamic financial constructions therefore suffer from tax disadvantages: one example is the Musharakah contract for financing a real estate purchase. The real

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<sup>143</sup> Bälz K (2006) Islamische Finanzierungen in Deutschland? In: Schneider Irene (ed) Beiträge zum islamischen Recht V. Suhrkamp, Frankfurt a.Main, p. 228

<sup>144</sup> Gassner (2007) *ibid*, p. 160

<sup>145</sup> [www.aaoifi.com/keypublications.html](http://www.aaoifi.com/keypublications.html)

estate tax has to be paid twice: once when the bank acquires the property, and again when the property is assigned to the client.<sup>146</sup> This unequal tax treatment represents a severe drawback for Islamic banks.

A debate has arisen over the last few years about the role of risk management in Islamic financial institutions<sup>147</sup>. Conventional banks already have to operate according to strict rules (e.g. Basel II). Most of these rules are not transferable to Islamic banking, since Islamic financial institutions have to accept either higher risk, or the lower proceeds associated with lower risk. Islamic banks are therefore exposed to risk in a way that conventional banks are not. For example: if a customer does not pay the installments on a loan, an Islamic bank is not allowed to charge interest on the resulting overdraft – something a conventional bank would always do. The degree of risk a bank carries depends on the structure of the financial instrument. The IFSB has developed several standards for risk management that are based on the Basel II guidelines.

Islamic banking is developing, at a faster and faster rate, from a niche player into a global industry. The challenges for Islamic banking are manifold, but they will have to be resolved if Islamic banking is to gain the ability to compete effectively with conventional banking. Several steps have already been taken, but there is still a long way to go.

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<sup>146</sup> Gassner (2007) *ibid*, p. 163

<sup>147</sup> Habib A (2007) Risk management in Islamic banking. In: Kabir et al (eds) *Handbook of Islamic Banking*. Elgar, Cheltenham, p. 144-158



## **6. Islamic Banking in Switzerland and Germany**

Islamic banking is developing from a niche player to a global industry. More than 1,5 billion people all around the world are Muslims, and are therefore potential investors. In Europe alone there are 53 million Muslims, 14 million of them in the European Union. Germany and France hold the largest number, with 5,5 and 3,5 million Muslims respectively.<sup>148</sup> Potential clients are not only institutional investors, but also private individuals and small investors. The need for Sharia compliant investments is rising, not only because of increasing capital transfer to European countries (for example, after September 11 Islamic investors withdrew immense amounts of capital from the US<sup>149</sup>) but also because of a strengthening of Islam in combination with the search for a specifically Islamic identity: banks all over Europe respond to these needs.

Germany as a country with a huge Muslim population, situated in the centre of Europe, is predestined to play an important role in global Islamic finance. It is an important business and trading partner of the GCC region and one of the major economies worldwide. Despite this preferred position, Islamic banking and finance is more or less non existent on the German market apart from some transactions in the real estate sector. Only in November 2008 the first Islamic finance conference was organized in Germany.

Switzerland is by any measure a country with a high reputation in global financial markets. International prestige and excellent business contacts are among the reasons for Switzerland's attraction in the financial world. Due to its neutrality, Switzerland is even preferred by Arabic capital to financial markets like London.<sup>150</sup> Most of the summit conferences and meetings held on the topic of Islamic finance in Europe take place in London, Geneva or Zurich.

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<sup>148</sup> [www.instituteforislamicbanking.de/euromuslims/euromuslims.php](http://www.instituteforislamicbanking.de/euromuslims/euromuslims.php)

<sup>149</sup> Kubsova (2007) *ibid*

<sup>150</sup> Wilson (2004) *ibid*, p. 276

## **6.1. The Islamic market**

### **6.1.1. The Swiss market**

Various banks offer Islamic products in Switzerland. It should be emphasised that Arabic banks are not automatically Islamic banks too. Several Arabic banks run agencies or offices in western countries that may not operate in a Sharia compliant way. These Arabic banks may offer Islamic products in “Islamic windows”, as many conventional western banks do in both Islamic and non-Islamic countries. If they do not offer such products, the bank must be considered to be a conventional bank.

To identify Islamic products in the Swiss market is not an easy task. In practice, it is possible to invest in any fund in any part of the world, thanks to globalisation and the world-wide networking between financial institutions. Most Swiss banks offer funds from competitors as an alternative to their own products. UBS, for example, sells funds to its clients from all over the world, including the US and the Middle East<sup>151</sup>. In the following list, only products are included provided by Swiss banks, or by the branches of international financial institutions that operate in the Swiss market.

#### **Pictet & Cie**

Pictet & Cie, established in 1905 in Geneva, is one of the last genuinely private banks in Switzerland. It is an asset management company with EUR 260 billion in assets under management. In 1988 Pictet founded the investment company Al Dar Islamic Fund, located in Luxembourg.<sup>152</sup> Via this investment company, three Islamic stock funds have been launched: Al Dar-European Equities, Al Dar-Eastern Equities, and Al Dar-World Equities, which invest in Sharia compliant shares in different parts of the world.

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<sup>151</sup> [www.ubs.com](http://www.ubs.com)

<sup>152</sup> [www.pictet.com](http://www.pictet.com)

All three funds were blocked in 2001 when the Luxembourg authorities suspected the funds of being involved in financing terror organizations<sup>153</sup>. Two funds were not re-opened, but the Al Dar-World Equities, accepted by Swiss law as a foreign investment fund under the national law of March 1994<sup>154</sup>, is still on the market today. Earnings from this fund that are a result of interest income are donated to charity organizations once a year.

The three funds were launched following a request from an investor, and are not actively marketed. Islamic banking plays a minor role at Pictet & Cie.

### **Citi Islamic Investment Bank E.C.**

Citi Islamic Investment Bank (CIIB), established in 1996 in Bahrain, is a 100 percent subsidiary company of Citigroup<sup>155</sup>. The CIIB offers three investment funds: the first is the Citi Private Investment Mudarabah (CPIM), which invests in short-term Islamic products in OECD countries based on low risk commodity Murabahah contracts. The second fund is Citi Emerging Market Mudarabah (CEMM), which invests in emerging markets on the basis of Mudarabah or Ijarah transactions. Last but not least is the Citi Islamic Portfolio, which is subdivided into Global Equity A and Global Equity B (both launched in 1997), both actively managed and open ended<sup>156</sup>.

### **EnergyMixx AG**

EnergyMixx AG is a Swiss Holding Company located in Zug: it plans, operates and invests in power plants via its 100 percent subsidiary companies (e.g. EnergyMixx Europe SA in Luxembourg). Its main focus is on renewable energy, using sun, wind,

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<sup>153</sup> Hall W: Private bank hit by Luxembourg probe into funds, 2001  
[specials.ft.com/attackonterrorism/FT3LOO1QCVC.html](http://specials.ft.com/attackonterrorism/FT3LOO1QCVC.html)

<sup>154</sup> [fuw.ch/fundfile.html?objects.isin=LU0085416633&objects.type=AnnualReport](http://fuw.ch/fundfile.html?objects.isin=LU0085416633&objects.type=AnnualReport)

<sup>155</sup> [www.citiislamic.com](http://www.citiislamic.com)

<sup>156</sup> [www.zawya.com/cm/profile.cfm/cid1003794](http://www.zawya.com/cm/profile.cfm/cid1003794)

water and biomass. Since 2007 EnergyMixx has been listed at the Frankfurt stock exchange: it operates subsidiaries in Albania, France, Italy, Poland, Rumania, Luxemburg, Sweden, UAE and the United Kingdom. In 2007 EnergyMixx launched a Sukuk, listed at the Frankfurt stock exchange and supported by the Faisal Bank, that was intended to enlarge its portfolio on the Italian market. It was the first time that a Sukuk has been used to finance a Europe-centered project in the renewable energy sector.<sup>157</sup>

### **Faisal Private Bank SA**

In 1982 the royal house of Saudi Arabia encouraged the establishment of Shari'A Investment Services SA, later named Faisal Private Bank (Switzerland) SA, in Geneva. The bank was re-named in honour of the late Saudi king Faisal ibn Abd al-Aziz. In October 2006, it was registered with the SFBC (Swiss Federal Banking Commission) and became a bank under Swiss law<sup>158</sup>. It was the first Swiss bank to operate completely in compliance with the Sharia. Its Sharia Board is consistent with the Sharia Board that is in charge of the Dow Jones Islamic Index.<sup>159</sup> Its main stockholder is the Ithmaar Bank B.S.C., a major manager and provider of Islamic investment products in the Middle East. With its headquarters in Bahrain, Ithmaar Bank B.S.C. holds 79 percent of Faisal Bank SA. Faisal Bank's main aim is to provide products in the wealth management and private investment sectors for its clients. It offers nearly the full range of Islamic financial structures – Mudarabah, Musharakah, Ijarah, Sukuk etc.<sup>160</sup>

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<sup>157</sup> [www.energymixx.ch](http://www.energymixx.ch)

<sup>158</sup> [www.faisalfinance.com](http://www.faisalfinance.com)

<sup>159</sup> [www.finanznachrichten.de/nachrichten-2007-07/artikel-8628135.asp](http://www.finanznachrichten.de/nachrichten-2007-07/artikel-8628135.asp)

<sup>160</sup> [www.faisalprivatebank.com/la\\_banque/3rd\\_instruments/fin\\_couts\\_en.aspx](http://www.faisalprivatebank.com/la_banque/3rd_instruments/fin_couts_en.aspx)

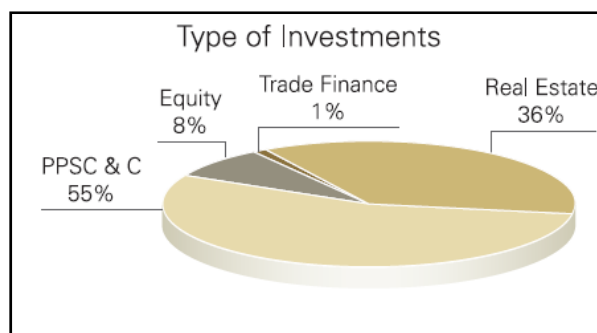


Figure 11 Investment of the Faisal Private Bank<sup>161</sup>

As can be seen, about 55 percent of the assets are invested in short-term projects (parallel purchase and sale of currencies and commodities), while 36 percent of funds under management are invested in real estate (1,1 billion CHF). The products are designed according to the needs of the bank's customers - wealthy private clients as well as institutional investors. This is all that can be said about Faisal's products with any certainty, because published information about them is scarce.

## UBS

UBS AG is a Swiss bank with subsidiaries all over the world. It operates in the wealth management, investment banking and asset management sectors, and has a long history of active involvement in Islamic Banking. Noriba Bank, a 100 percent subsidiary, was established in the kingdom of Bahrain in 2002. This subsidiary has offered Islamic bonds, private equity, real estate projects, Murabahah contracts and many other Sharia compliant products. Because of increasing demand for Islamic products, Noriba Bank was integrated into UBS in 2006 as a part of the restructuring of the UBS business units.<sup>162</sup> Today UBS provides a wide range of Islamic products.

In the asset management sector UBS offers a fund, issued by Noriba in Luxemburg in 2000, called UBS (Lux) Islamic Fund - Global Equities (formerly the Noriba Global Equity Fund). This is an open-ended fund that invests in companies around the globe

<sup>161</sup> [www.faisalprivatebank.com/pdf/annual\\_report06.pdf](http://www.faisalprivatebank.com/pdf/annual_report06.pdf)

<sup>162</sup> [www.ubs.com/1/e/investors/releases?newsId=93737](http://www.ubs.com/1/e/investors/releases?newsId=93737)

that are Sharia compliant and are part of the Dow Jones Islamic Market 100 Titan IndexSM. The individual companies are weighted within the fund according to their strategic orientation, market position, management, profitability, growth potential, and improvement of shareholder value.<sup>163</sup> The fund attracts mainly investors who are looking for long-term value enhancement and broad investment diversification.

In the commodity sector, UBS offers two different types of structures: bespoke indices, and commodity-linked investment certificates. An example of a bespoke index is the UBS Oilfield Strategy Index, which invests in oil allocations for future exploitation. It is a long-term product, unlike conventional oil contracts that are geared to short-term contracts, and is therefore highly volatile. The goal of the index is to replicate a physical oilfield. Commodity-linked investment certificates give the investor the ability to choose freely between different levels of participation and protection, between a wide range of commodities, and between different maturities. The interest yielded by the underlying asset is retained; therefore the product is still Sharia compliant.

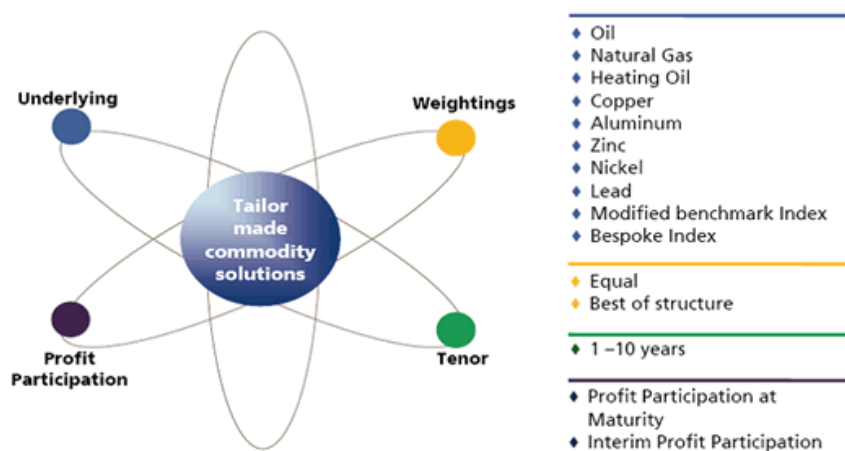


Figure 12 Commodity linked investment certificates<sup>164</sup>

In the equity sector, UBS offers its customers the UBS Sharia-compliant GOAL (Geld oder Aktien Lieferung - cash or share delivery)<sup>165</sup> - structured products based either on a Sharia index or a product that is approved by the Sharia Board.

<sup>163</sup> [www.finanzen.net/fonds/UBS\\_Lux\\_Islamic\\_Fund\\_Global\\_Equities\\_USD](http://www.finanzen.net/fonds/UBS_Lux_Islamic_Fund_Global_Equities_USD)

<sup>164</sup> [www.ibb.ubs.com/mc/islamicfinance/commodities-linked-investment-certificates.shtml](http://www.ibb.ubs.com/mc/islamicfinance/commodities-linked-investment-certificates.shtml)

Its goal is to maximize profits in sideways-moving markets. UBS provides tailor-made products with a maturity of between 6 and 24 months. At maturity the investor receives the share, or the profit up to the strike price (cap). In the first case the share was bought for less than the market price, and in the second case the investor realizes an attractive profit. These products can be traded on the secondary market.

UBS also provides long-term Sharia compliant products<sup>166</sup>, for example, the UBS Sharia-Compliant Deposit, based on a commodity Murabahah, which can't be cashed in before maturity. Another long-term product is the UBS Sharia compliant FX BLOC, which operates exactly like the UBS Sharia-Compliant Deposit except that at maturity the bank also has the right to convert the invested capital into another currency. UBS also offers the UBS Range Murabahah investment, also based on a commodity Murabahah. This product offers full capital protection, but the profit is limited by a cap (Profit Rate Payment).

Further products offered by UBS are different forms of Sukuk – for example, Musharakah Sukuk, Ijarah Sukuk and Murabahah Sukuk. All these products are designed for both private and institutional investors. The Islamic Banking sector is becoming more and more important to UBS.

## **Credit Suisse**

Credit Suisse is a globally active financial services company with its headquarters in Zurich. It offers a wide range of products in the private banking, wealth management and investment banking sectors. Since 2006 Credit Suisse has also provided Islamic financial products. A team has been built up with Islamic financial experts in both Zurich and London. At the moment, the products are aimed mainly at institutional investors, but private customers are expected to be addressed soon. The current fund that Credit Suisse is offering is the CS SICAV One (Lux) Equity Al-Buraq, issued in May 2007 and operated in compliance with Sharia. At least two thirds of the total

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<sup>165</sup> [www.ibb.ubs.com/mc/islamicfinance/equities.shtml](http://www.ibb.ubs.com/mc/islamicfinance/equities.shtml)

<sup>166</sup> [www.ibb.ubs.com/mc/islamicfinance/longer\\_term\\_products.shtml](http://www.ibb.ubs.com/mc/islamicfinance/longer_term_products.shtml)

capital is invested in shares. If profit is earned that is not compliant with Sharia, it is donated to charity organizations.<sup>167</sup>

## **Da Vinci Investment**

In the end of 2008, a new environmental and Sharia compliant Fund was launched – the Green Falcon Fund by Da Vinci Investment. Da Vinci Investment is a Zug based (but incorporated in the UK) asset management company with currently 28 million Euro assets under management. This Fund invests into carbon markets for short-term and forestry for long-term.

From the list above it can clearly be seen that there is still potential for the development of Islamic products in the Swiss market. Every year more and more banks discover the Islamic financial business: however, the Swiss market is quite small, therefore Islamic Banking has until now played quite a minor role.

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<sup>167</sup> [www.fundinfo.com/storage/company/csg/262786.pdf](http://www.fundinfo.com/storage/company/csg/262786.pdf), p.e 21



### **6.1.2. The German Islamic market**

In comparison to the Swiss market the German Islamic market is more than moderate. Different financial institutions offer products to foreign investors outside of Europe.

#### **Saxony-Anhalt Sukuk**

In 2004, the federal state of Saxony –Anhalt was the first European issuer of a 100 million Euro asset backed Sukuk, structured as a Sukuk al Ijarah, which is listed on the Luxembourg Stock Exchange. The debts of Saxony-Anhalt are guaranteed by the German State. The whole Sukuk is based on the Ijarah construction, a sale and lease-back transaction: The German State, represented by the Ministry of Finance, sells a number of buildings to a special purpose vehicle (SPV) and then leases them back. The subscribers of the SPV receive a variable rent over the whole period. This rent is aligned to the EURIBOR, which was chosen as benchmark. This special purpose vehicle is based in the Netherlands due to tax reasons. After 5 years Saxony-Anhalt repurchases the real estate objects and pays back the price paid in 2004, which goes directly to the shareholders of the SPV. This payment will become due in 2009.

Since the returns realized by the investors were financed by the rental income from Saxony-Anhalt, the whole construction was compliant to the rules of the Sharia. Several reasons played a decisive role when deciding for a Sukuk as the financing model for Saxony-Anhalt: first, the enlargement of the investor basis and thereby ensuring the long-term access to capital markets. Second, the issuance of the Sukuk was seen as a marketing instrument for international investors, especially from the Middle East. The Sukuk was rated AA by Standard and Poor's and AAA by Fitch.

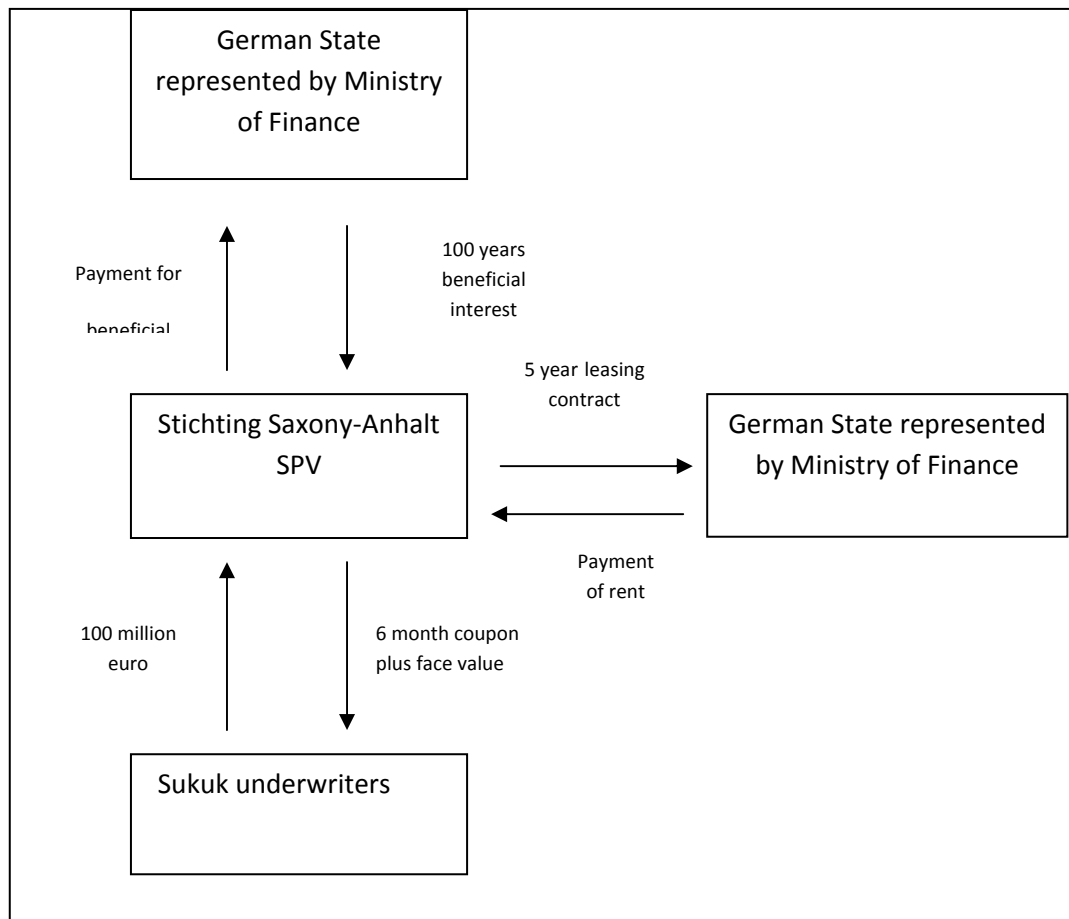


Figure 13 Model of the Saxony-Anhalt Sukuk<sup>168</sup>

## Deutsche Bank

Deutsche Bank AG was founded in 1870 in Germany and is today Germany's largest financial institution in terms of total assets. For the last three decades Deutsche Bank AG was active on Arabic markets, with major focus on Islamic Banking and Sharia compliant products. Deutsche bank was therefore awarded two times special awards: in 2007, the "Most Innovative Custodian Bank – First Islamic Custodian Bank" and "The Biggest and Most Active Custodian Bank for Islamic Funds" in 2008.<sup>169</sup>

Deutsche Bank always engaged in cooperation with local banks, like the joint venture with Abraaj Capital of Dubai and Ithmaar Bank of Bahrain for the launch of a financial fund that is run according to the rules of the Sharia.

<sup>168</sup> Gassner (2004) *ibid*, p. 104

<sup>169</sup> [www.db.com/en/content/company/headlines\\_9222.htm](http://www.db.com/en/content/company/headlines_9222.htm)

Until 2008, the Islamic Finance Team of the Deutsche Bank was situated in London, but moved in August to Dubai.<sup>170</sup> Part of Deutsche Bank's Asset Management Division is DWS, a global mutual fund company, with 269 000 billion Euro assets under management. A range of Sharia compliant funds is offered by the DWS in Africa and the Middle East: "DWS Noor Islamic Funds", which consist of five different funds<sup>171</sup>:

- DWS Noor Precious Metals Securities Fund, which was launched in 2007 and invests in securities (no preferred shares, bonds, convertible bonds, warrants) of companies that deal with precious metals as gold, platinum or silver – from mining to production.
- DWS Noor Global Select Equity Fund, which was launched in 2006 and invests into a number of selected equity or equity related stocks all over the world.
- DWS Noor China Equity Fund, launched in 2006, which invests in equity securities of companies that are listed on the Chinese stock exchange or are related to China.
- DWS Noor Japan Equity Fund, launched in 2006, which invests into the Japanese equity market or into companies that are related to Japan.
- DWS Noor Asia Pacific Equity Fund Class A, which was launched also in 2006 and invests into companies on the Asia Pacific market.

All these funds require a minimum investment amount of 10.000 USD for private and 25.000 USD for institutional clients and deal only with securities, which are compliant with Islamic law. The initial plan was to market these funds after a starting period also in Europe – but until today the funds are only available in the Middle East, Asia and North Africa.

On the German market Deutsche Bank AG offers a special concept to the Turkish community, called Bankamiz. In 55 subsidiaries all over Germany financial services

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<sup>170</sup> Islamische Finanzprodukte: Zwischenbilanz der vor einigen Monaten vom Zentralrat der Muslime ins Leben gerufenen Kam, p.ne. 24.8.2008. [islam.de/10677](http://islam.de/10677)

<sup>171</sup> [www.dws.com](http://www.dws.com)

are supplied to Turkish people in their mother language. The focal point is laid on cultural differences regarding the language and the distribution channel. Even though this concept targets Muslims on the German market, Bankamiz can not be seen as part of Islamic finance, but belongs to the group of ethno-marketing (segmentation of a market according to cultural criteria). After all, Deutsche Bank AG does not provide any financial services compliant with the Sharia on the German market.

## **Commerzbank**

Commerzbank is one of the largest German banks, with its headquarters in Frankfurt am Main<sup>172</sup>. Its subsidiary company Commerz International Capital Management (CICM) launched the AISukoor European Equity Fund in 1999: this Fund is invested in 100 percent European (mostly blue chip) shares, and is marketed by Commerzbank's Swiss affiliates. This fund was initially designed only for institutional investors from the Middle East, but became open for private investors in 2000<sup>173</sup>. CICM looked for partners that would help with the design and the sale of the fund – and found the Al-Tawfeek group, a subsidiary company of Dallah Albaraka, one of the world's biggest banking groups. The AISukoor European Equity Fund was established following the request of a Commerzbank investor.

A Sharia Board ensures that its operations were Sharia compliant: for example, the Board denied approval when the fund managers wanted to buy Lufthansa shares, because the airline serves alcoholic drinks<sup>174</sup>. Unfortunately the fund had to be closed in 2005, since at this point in time the assets under management amounted only to 4 million Euro. Experts identified various causes for the failure of the AISukoor European Equity Fund: it was not marketed actively among the target group in Germany. In the GCC region, where the Fund was promoted actively, the real estate hype was the dominant subject to investment at this time and not equity investment. Furthermore, after September 11<sup>th</sup> stock markets were adjusting downwards. For these reasons no success was granted to the AISukoor European Equity Fund.

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<sup>172</sup> [www.commerzbank.de](http://www.commerzbank.de)

<sup>173</sup> Geyer (2002) *ibid*, p. 263

<sup>174</sup> Geyer (2002) *ibid*, p. 264

The Islamic banking sector plays a minor role at Commerzbank. The AISukoor European Equity Fund was the only Islamic product that was offered to its German clients. According to Commerzbank, Islamic banking is not one of its core divisions.

## **Others**

Two major insurance companies, Hannover Re Group and Allianz, offer Sharia compliant products to their customers. Both of them serve only clients outside of Germany, mainly in Indonesia, the Gulf States and Malaysia. Allianz, one of the biggest global providers of insurance, banking and asset management services, opened a branch in Indonesia in 2006, which is specialised in Sharia compliant products.<sup>175</sup> Hannover Re Group, one of the major reinsurance groups worldwide, offers Takaful insurances to companies that operate according to the Sharia.<sup>176</sup> In 2006, the 660 million Euro Gulf German Residence Fund was issued by Abu Dhabi Investment House, which invests in real estate properties all over Germany.<sup>177</sup> Another real estate Fund investing in Germany, the German AIL Fund 1, was launched in 2007 by Arab Investment Ltd.

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<sup>175</sup> „Allianz Sharia Insurance in Indonesia – a very successful start in 2006“

<sup>176</sup> [www.hannover-re.com](http://www.hannover-re.com)

<sup>177</sup> [Aibim.com/content/view/624/79/](http://Aibim.com/content/view/624/79/)

## 6.2. Muslim population

### 6.2.1. Muslim population in Switzerland

All the data used for this analysis was provided by the BFS (Bundesamt für Statistik)<sup>178</sup> for this study, and is based on the population census of the year 2000. The next census will take place in 2010.

According to the BFS, 310.807 people in Switzerland were Muslims in 2000: 4.3 percent of the total Swiss population. Other sources speak of more than 440.000 in 2007, or 5.8 percent of the Swiss population<sup>179</sup>. Of the 4.3 percent, only 0.6 percent (or 36.481 people) are part of a religious community. Muslims comprise a relatively high proportion of all the foreigners in the country: 18.3 percent.

Looking at the change in the Muslim population since the previous census in 1990, we find a strong increase. In 1990 there were 152.217 Muslims registered in Switzerland – so the Muslim population had more than doubled in only ten years. Islam therefore represents, after the Roman Catholic and Protestant churches, the third largest religious community in Switzerland. The high increase in the Muslim population in the last decade of the 20<sup>th</sup> century can be attributed, inter alia, to immigration from the former Yugoslavia (Bosnia, Serbia, Macedonia and Kosovo) as well as from the Arabic and sub-Saharan countries of Africa.<sup>180</sup>

The age distribution of the Muslim population according to the census in 2000 is shown in the table below. The bulk of the population is under fifty years old: from fifty upwards, the numbers fall continuously. Only 2.5 percent are older than 60. The affiliation to a church or religious community is normally transferred from parents to children. The demographic structure of a religious community has an important influence on population development. In Muslim families, the number of children is normally high compared to Christian families: with the bulk of the Muslim community

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<sup>178</sup> [www.statistik.admin.ch](http://www.statistik.admin.ch)

<sup>179</sup> Ackerl I: Die Staaten der Erde - Europa und Asien, 2007, p. 97

<sup>180</sup> Gianni M: Muslime in der Schweiz. 2005, p. 14. [www.islamresearch.net/muslime\\_in\\_der\\_schweiz.pdf](http://www.islamresearch.net/muslime_in_der_schweiz.pdf)

below the age of fifty, the Islamic population in Switzerland has huge growth potential.<sup>181</sup>

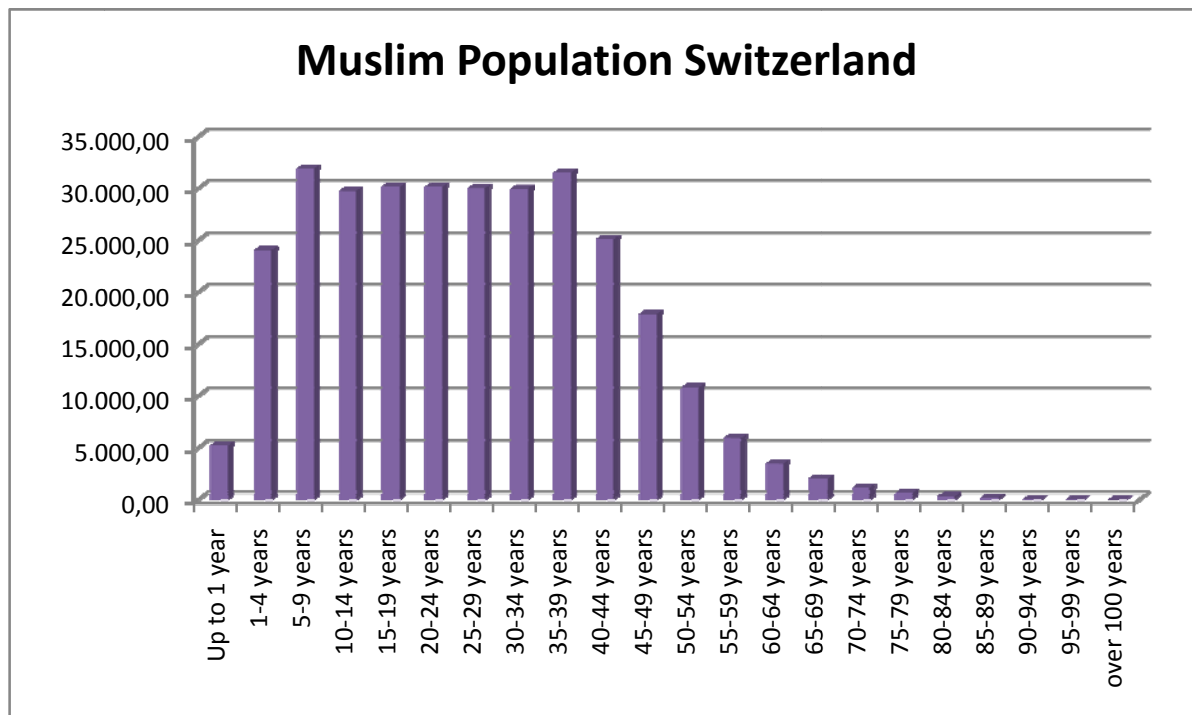


Figure 14 Age distribution of the Muslim population in Switzerland<sup>182</sup>

Another important point to be considered is the occupation and income structure of the Islamic community, which is of course a function of educational attainment. Unfortunately for our analysis, the BFS has not collected data about income, but the distribution of educational levels / occupations is as follows:

<sup>181</sup>Schweizer Religionslandschaft im Umbruch 2003 [http://www.jesus.ch/index.php/D/article/23-Gesellschaft/6252-Schweizer\\_Religionslandschaft\\_im\\_Umbruch/](http://www.jesus.ch/index.php/D/article/23-Gesellschaft/6252-Schweizer_Religionslandschaft_im_Umbruch/)

<sup>182</sup> Based on data from [www.islamresearch.net/statistics.html](http://www.islamresearch.net/statistics.html)

Education	Number of people
University	4.997
Higher professional education	609
College of higher education	2.943
A-Levels	5.069
Without completed professional education	14.806
Completed professional education	37.489
Housework / Volunteer	8.941
Retired	20.722
Unemployed	37.660
In education above 15	14.720
Children under 15	91.948
Not reported	70.017

Figure 15 Education of the Muslim population in Switzerland based on the census 2000<sup>183</sup>

In the year 2000, about one fifth of the Muslim population were employed in the labour market. In reality this number may be higher: some of 70.017 unreported individuals (ref. Figure 3 above) were probably also employed. The high 'not reported' number can be attributed to illegal employment, intentional false statements due to fear of further investigation, and last but not least to people whose knowledge of the language is too poor to fill in the questionnaire.

The category “without completed professional education” contains various sub-categories. A large part of this group is made up of unskilled workers who work in the construction sector or on an assembly line. Another part comprises doctors and lawyers who did not get a work permit to follow their profession in Switzerland, and therefore have to engage in other occupations.

<sup>183</sup> See Altundag, Halidi (2005) *ibid*,



Children under 15 (91.948) and students over 15 (14.720) make up more than a third of the Muslim community. Because of the Swiss school system, most of these future workers receive a good education - leading to qualified jobs in the employment market. This segment of the Muslim population has the greatest influence in the development of the Islamic population. As these young people advance in their careers they will also start their own families: the proportion of Muslims in Switzerland will grow even further, because Muslim families have on average have more children than their Swiss counterparts. Marriage to non-Muslims will reinforce this trend, because most non-Muslim partners convert to Islam.

Of course, not all Muslims growing up in Switzerland follow the religion of their parents. Growing up in a liberal country like Switzerland includes coming into contact with many religions and ideologies that challenge the Muslim world view. However, most Muslims can be expected to keep their traditions and religious views.

The expected increase of the Muslim population in Switzerland will certainly create the demand for Islamic and Sharia compliant products on the Swiss market. Most of these new citizens will also demand conventional current or savings accounts, credits and loans: the wealthiest among them will meet the minimum capital requirements for wealth management.

### **6.2.2. Muslim population in Germany**

For Germany it is much harder to find concrete numbers regarding the Muslim population. The last macrocensus was carried out in 1981 in the former DDR and in 1987 in West Germany. After the 1980s only microcensuses- organized by the Statistisches Bundesamt (DESTATIS) - were realized, in which 1 percent of Germany`s households are randomly interviewed in respect of economical and social situation, occupation, labour market and education. Germany and Sweden were the only countries not to take part in the 2000/01 census that was carried out in whole Europe. In 2010 however, Germany will participate in the europeanwide macrocensus, which will be based mainly on administrative registers. The last

German microcensus was carried out in 2005. All data for this analysis was provided by DESTATIS and REMID.<sup>184</sup>

According to REMID (Religionswissenschaftlicher Medien- und Informationsdienst e.V.) there are 3.5 million Muslims in Germany. 950.276 of them possess a German passport and 14.352 are of German origin.<sup>185</sup> They belong to different religious groups: 2.64 million Sunnis, 400.000 Alevis, 225.500 Irani Imamits or Turkish Shiites, 50.000 Ahmadiyyas, 10.000 Sufis and finally 1.900 Ismailites<sup>186</sup>. This makes Islam the second largest religion in Germany, right after the Catholic Church.

Subsequent to this separation according to religious affiliation a classification in matters of national provenance can be made. Of 3.5 million Muslims 1.8 million are Turkish (2.8 million including nationalized persons), 160.000 Bosnians, 75.000 Iraqis, 70.000 Moroccans, 60.000 Iranis, 55.000 Afghans and 4.000 Lebanese.<sup>187</sup> Gassner (2007) reports a much higher number for Turkish people living in Germany: 2.6 million<sup>188</sup>.

In the German census no data is collected regarding religious affiliation. Therefore it is difficult to make statements about the numbers of Muslims in Germany based on the data from DESTATIS. One can only investigate the data as for national provenance. Since the largest Muslim group in Germany is the Turks, we will focus mainly on the two largest groups: Turks and Bosnians. According to interviews, 95 % of the Turkish population declare themselves of being professing Muslims.

The age distribution of the Turkish population is shown in the table below. The bulk of the population is between 25-45 years. In Muslim families, the number of children is normally high: in the German case we find a deviation from this rule.

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<sup>184</sup> [www.ec.destatis.de](http://www.ec.destatis.de)

<sup>185</sup> Ashrati M (2008) Islamic Banking, Frankfurt School Verlag GmbH, Frankfurt / Main, p. 109

<sup>186</sup> [www.remid.de/remid\\_info\\_zahlen.htm](http://www.remid.de/remid_info_zahlen.htm)

<sup>187</sup> Chaboune J, El-Mogadeddi Z (2008) Islamic banking – das Marktpotenzial in Deutschland. Kreditwesen 15/2008, p. 33

<sup>188</sup> Gassner (2004) *ibid*, p. 11

### Turkish Population in Germany in 2006

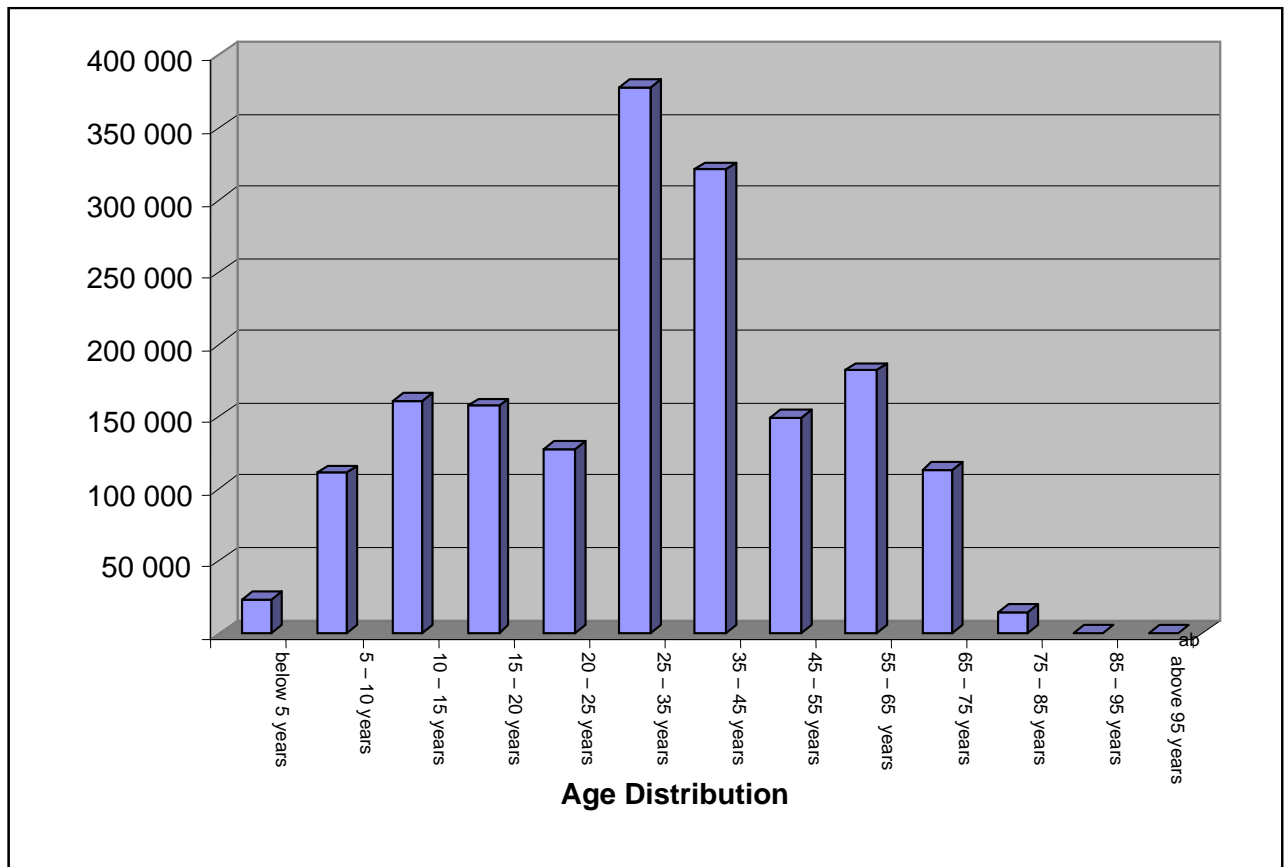


Figure 16 Age Distribution of Turkish Population in Germany in 2006<sup>189</sup>

The distribution of Turkish people shows one fact clearly: the majority of the Turkish population is at an age, where financial products are consumed frequently – e.g. financing of a business idea, insurances. 77 percent of Turks living in Germany are between 14 and 49 years old. Ashrati (2008) speaks about an average need of financial products of 371 EUR a month for Turkish households.<sup>190</sup>

<sup>189</sup> Bevölkerung mit Migrationshintergrund, Ergebnisse des Mikrozensus 2005 [www-ec.destatis.de/shop/sfg/bpm.html.cms.cBroker.cls?cmspath=struktur,vollanzeige.csp?ID=1020312](http://www-ec.destatis.de/shop/sfg/bpm.html.cms.cBroker.cls?cmspath=struktur,vollanzeige.csp?ID=1020312)

<sup>190</sup> Ashrati (2008) *ibid*, p. 110

### Turkish and Bosnian labour force according to net income in 2005 (in 1000)

Nationality	Monthly net income in Euro									not reported
	below 300	300 - 500	500 - 700	700 - 900	900 - 1100	1100 - 1300	1300 - 1500	1500 - 2000	more than 2000	
Turkish	41	76	45	44	62	62	64	136	78	30
Bosnian	6	18	9	9	15	16	13	24	9	5

Figure 17 Turkish and Bosnian labour force according to net income in 2005

El-Mogadeddi (2009) speaks of 720.000 Turkish households in Germany with an average net income of 1.917 EUR monthly (average net income of Germans households: 2.596 EUR).<sup>191</sup> According to Chahboune and El-Mogadeddi (2008) the average savings ration of Turkish households (21% or 228 EUR monthly) doubles the savings ration of German households (10%)<sup>192</sup>. Due to the original intention of returning to Turkey after a few years of gainful employment, the propensity to save fractions of the permanent income was high. In the last years several Turkish families have decided to remain in Germany, whereby huge savings deposits have accumulated. Experts assess the value up to 25 billion EUR. Money transfers to Turkey have regressed significantly over the last years. In addition, Turkish households spend on average 143 EUR a month for insurances<sup>193</sup>.

### Turkish and Bosnian labour force according to occupation in 2005 (in 1000)

Nationality	Total	Labor force	Employed	Self-employed	Employee	Worker	Assisting family member	In education	Without occupation
Turkish	1 887	840	637	43	145	440	8	31	30
Bosnian	265	149	124	-	40	78	/	/	5

Figure 18 Turkish and Bosnian labour force according to occupation in 2005

<sup>191</sup> El-Mogadeddi Z (2009) Islamic Banking. Statistik eines Megatrends.  
[www.banklounge.de/index.php?id=15&no\\_cache=1&tx\\_ttnews%5Btt\\_news%5D=35352](http://www.banklounge.de/index.php?id=15&no_cache=1&tx_ttnews%5Btt_news%5D=35352)

<sup>192</sup> Chahboune. El-Mogadeddi (2008) ibid, p. 33

<sup>193</sup> Ashrati (2008) ibid, p. 110

In the year 2005, about one fourth of the Turkish population and nearly 50% of the Bosnian population were employed in the labour market. In reality this number may be higher, which can be attributed to illegal employment or intentional false statements due to fear of further investigation. Ashrati (2008) puts the demand potential for financial products at 2,7 billion EUR, based on 553.000 employed people. In 2005 already 637.000 Turks were employed on the labour market.

**Turkish and Bosnian labour force according to their level of education in 2005 (in 1000)**

Nationality	Total with terminated education	Internships	Apprenticeship	Vocational qualifications	Craftsman & engineer	College of higher education	University	Without terminated professional education	
								In education	Without graduation
Turkish	529	45	383	19	24	11	37	660	1'305
Bosnian	121	6	86	/	6	/	/	70	122

Figure 19 Turkish and Bosnian labor force according to level of education in 2005

The total annual purchasing power of the Turkish community is estimated to amount up to 25 billion EUR, which are spent nearly entirely in Germany. Turkish companies generate about 50 billion EUR a year for the time being – a number which is predicted to double until 2010.<sup>194</sup>

On the basis of these numbers there is definitely a demand for Islamic and Sharia compliant products on the German market. Most of these new citizens will also demand conventional current or savings accounts, credits and loans: the wealthiest among them will meet the minimum capital requirements for wealth management.

<sup>194</sup> EL-Mogadeddi (2009) ibid

### **6.3. Other groups that are possibly interested in Islamic Banking**

There are other groups, apart from the Muslim community, that might be interested in Islamic financial products. One is the emerging ethical investment sector: this group of investors denounces profit seeking at all costs, preferring ethical investments that transcend purely materialistic considerations. These investors are committed to ecological products, and demand responsible methods of production from companies in industrialized countries. This part of the population could easily identify with the principles of Islamic banking. Of course, not all ethical investors are potential clients of an Islamic bank - but some will doubtless feel comfortable with an Islamic bank that operates according to Sharia principles.

Investors that suffered a lot from the crisis in 2007/2008 could also be interested in Islamic products. The Sharia does forbid all forms of speculation, as well as investments in bank stocks and shares from companies with high debt-equity ratio. Furthermore, all securitization of credits is prohibited. All these themes were discussed widely during the last year.

Another group that could be interested in Islamic banking are SMEs (small and medium sized enterprises). With the availability of conventional loans becoming more and more restricted, some small companies are unable to finance further new projects. It is getting more and more expensive to take out a conventional loan. Sometimes this situation leads to the abandonment of a company that could be profitable. These SMEs constitute a potential customer group for Islamic products. Through cooperation between bank and company, the management of the SME can be improved, and a profitable company created. Both parties can benefit from the situation, and a long-term customer relationship can be built up.

## 6.4. Islamic financial instruments and their applicability in Switzerland and Germany

In the following section we examine the applicability of individual Islamic financial instruments to the Swiss and German market, highlighting any possible difficulties and particularities.

One important consideration is the compatibility of these instruments with the law of the respective country. Firstly, it must be pointed out that according to Swiss law (Bankenverordnung, Bankengesetz and Auslandsbankenverordnung<sup>195</sup>), foreign banks must be treated in exactly the same way as Swiss banks. There is no legal impediment to the establishment of a bank in Switzerland that operates according to Sharia rules, or to the opening of a subsidiary of a foreign Islamic bank. The Swiss banking commission (Eidgenössische Bankenkommission, EBK) examines only whether the bank itself comes into conflict with the law: it does not control every single product that it offers on the Swiss market. From the moment the financial institution receives authorization from the EBK, all the products that it distributes are automatically allowed on the market. The only exceptions are investment funds, which the EBK controls separately. However, no distinction is made between conventional investment funds and Sharia compliant funds. Therefore it can be stated that in principle Swiss law allows all Islamic products: the EBK controls only the banks that offer them.

The same principles hold for German law. According to the KWG (Kredit-Wesen-Gesetz) a financial institution has to apply for admission with the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) before operating on the German market. A discrimination of foreign banks is forbidden. As long as the foreign institution does not have its headquarters in Germany, it is only allowed to open a local branch. Once approved by the BaFin, the offered products are not subject to control procedures. Also in Germany, the exceptions are investment funds, which are controlled separately by the BaFin.

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<sup>195</sup> [www.admin.ch/ch/d/sr/9/952.0.de.pdf](http://www.admin.ch/ch/d/sr/9/952.0.de.pdf) and [www.admin.ch/ch/d/sr/9/952.111.de.pdf](http://www.admin.ch/ch/d/sr/9/952.111.de.pdf) and [www.admin.ch/ch/d/sr/9/952.02.de.pdf](http://www.admin.ch/ch/d/sr/9/952.02.de.pdf)

However, neither in Germany nor in Switzerland, no distinction is made between conventional investment funds and Sharia compliant funds. Therefore it can be stated that in principle both countries allow all Islamic products: the EBK, respectively BaFin, controls only the banks that offer them.

#### **6.4.1. Applicability of specific Islamic products**

##### **Murabahah**

There is no equivalent to a Murabahah contract under Swiss or German law. For a bank, the handling of a Murabahah transaction is quite simple: the bank's duty is to identify the object of the contract, and to control if it is halal. The control is mostly outsourced to a trusted partner, because the bank's resources would otherwise be excessively strained. One big advantage of a Murabahah contract is the limited risk of loss – the maximum loss is limited to the purchase price of the product.

One particularity has to be considered: no default interest can be charged. The bank must develop a strategy to ensure that the customer pays in time. One possibility is to include a clause in the contract that obliges the client to donate a certain amount to a charitable organization in the case of default or delayed payment – which does not cover the costs of the bank. Since the price and the profit from the Murabahah product is fixed in advance, the financial institution must calculate the selling price under all contingencies: if there is any miscalculation, the contract can't be modified later. Murabahah contracts include some other risk for the financial institution: Islamic banks could risk becoming the first port of call for bad debtors, and would therefore have to scrutinize their customers closely.

Murabahah is the most common type of contract in Islamic banking. This type of contract is particularly suitable for financing assets and raw materials, but can also be used for bridging a period of liquidity shortage. Self-employed Muslims and SMEs are potential customers. For the second group, Islamic banking represents a true



alternative to conventional banking, for reasons previously mentioned: this kind of credit could be a lifeline to many SMEs.

## **Bay Salam**

According to the Bay Salam contract, the bank is responsible for the pre-financing of the Bay Salam object. This form of financing is a classic forward transaction, as practiced by conventional banks. In contrast with conventional banking, however, speculation is eliminated under the Bay Salam construct - only the financing of an actual business transaction is allowed. Apart from this, Bay Salam corresponds to a large extent with a conventional forward transaction. However, the Bay Salam contract is tied to several conditions. The contractual object has to be examined in detail before the transaction takes place and the characteristics of the purchased product have to be accurately defined in advance. The strict compliance with these rules constitutes an administrative expense that should not be underestimated by a financial institution offering Islamic products.

Risks to the bank can emerge from the seller side – who, for example, might not deliver in time – and from the buyer side, who could be insolvent at the date of payment.

## **Istisnaa**

The principles of the Istisnaa contract are very similar to the Bay Salam contract: it also has some features of a conventional forward transaction. The most important difference with the Bay Salam contract lies in the principle that the contractual object has to be produced at some time in the future. This form of financing is mainly appropriate for companies that construct buildings, ships or aircraft. With the Istisnaa contract, too, the financial institution runs the risk that the producer can't deliver, or

that the buyer is insolvent. A financial institution needs to include both of these contingencies in its cost estimates.

## **Mudarabah**

The Mudarabah contract is a form of equity financing. The complexity is however kept within limits, because the financial institution only acts as a provider of capital. In this form of financing the bank has to bear two particularities in mind: firstly, the bank has to bear possible losses from the investment project itself. This particularity is a feature of Islamic Banking that does not exist in conventional banking. The bank bears any losses, for whatever time they may last.

The second particularity is the possibility of moral hazard – the Mudarib does not have sufficient interest in the development of the business or project. In case of profit he participates as stated in the contract, but a possible loss does not bother him, because the bank takes the responsibility. Furthermore, the bank providing the finance has no voice in the project. A financial institution will hardly commit itself to mobilize capital without the ability to control, or at least to exert some influence.

It is conceivable that a bank might assume the financing if the prospect of profit is believed to be certain. However, to achieve this level of confidence is not an easy task – it requires detailed information and a deep, on-going examination of the investment, which needs not only capital but also experts in the sector involved. A profound understanding of the Mudarib is also a prerequisite. If the Mudarib causes losses by his case of negligence, he has to bear at least a part of these losses: the difficulty lies in proving his negligence.

## **Musharakah**

Like the Mudarabah contract, the Musharakah transaction is a form of equity financing, but much more complicated. The Islamic Bank is granted a voice in the

management of the joint venture. On the one side, this can be seen as positive, since the financing institution can influence the strategic alignment of the Musharakah project, and is therefore more likely to provide the capital needed. On the other side, its involvement in the business ties up personnel resources, which are limited only by the intended extent of the cooperation

The main characteristics of the Musharakah contract are twofold. Firstly, the liability for possible losses is unlimited, which is also the danger of this form of financing. Secondly, the contract can be terminated at any time – it therefore includes a high level of uncertainty. Because of these peculiarities, a solid partnership with the Islamic bank is required that will facilitate the planning of a medium-term strategy.

As already mentioned, we should differentiate between the permanent Musharakah and the diminishing Musharakah. In the case of the permanent Musharakah, the duration of the contract is open-ended. The financial institution has to develop different exit scenarios and should define in advance how long the partnership should continue, since the partnership will continue only for a limited time period. In the case of the diminishing Musharakah, the exit is arranged in advance in the contract. It is advantageous to stipulate that the repayment of the invested capital is to be made by installments: this ensures that if the partner becomes insolvent, the bank is not left empty-handed.

## **Ijara**

The Ijara contract corresponds in large part to the conventional leasing contract, why it could be easily introduced into the respective markets. The only identifiable difference lies in the prohibition of taking interest in the event of late payment.

There are two major drawbacks for an Islamic bank offering Ijara products. The quantity of funds tied up is usually high, since Ijara is mostly used to finance capital intensive projects like aircraft, buildings and ships. A small bank can easily reach its financial limits. In addition, the bank bears the risk that it is left with the expensive project deliverables: this could happen if the lessee were to become insolvent, and

could lead to a liquidity shortage at the bank. Since conventional leasing products have become an accepted form of credit financing and the market for leasing products is already over-crowded and hotly contested I would not recommend Ijara as a product for Germany or Switzerland.

## **Sukuk**

Sukuk, like conventional obligations, are issued when a company (or the state) needs a large amount of capital, like it was the case of Saxony-Anhalt. Theoretically, companies could issue Sukuk - but companies run by western managers tend to use conventional obligations as a form of credit financing. Furthermore, conventional obligations are seen as a secure source of income, while Sukuk are by definition unsecured. There is however a potential for the sale of Sukuk issued by third parties. An Islamic Bank could, for a commission, sell Sukuk from other banks or companies.

Based on the situation in Switzerland, the issuance of Sukuk there would not make sense. SMEs are too small to issue Sukuk, and the number of companies with the required size is limited. In Germany the Saxony-Anhalt structure remained the only Sukuk issued. Among disappointed experts lack of understanding reigns why it remained the only one and why no corporation or company followed the successful subscription.

The creation of an investment fund company is straightforward, and also quite inexpensive. The creation of a fund is a possibility for every financial institution - even for small banks. Even though the creation is easy, large amounts of capital are needed to be able to operate in a cost-effective and profit-making way. The demand for Islamic funds in the Swiss market could be too small, and the number of potential investors limited. In Germany however, there should be enough potential due to 3.5 million Muslims living in the country. However, the sale and procurement of funds issued by a third party should be included in the portfolio of services provided by a Islamic financial institution operating in Switzerland or Germany. A large number of

these funds are available on the international financial market, as can also be seen on the homepage of Failaka International.<sup>196</sup>

## **Deposit accounts**

Deposit accounts are one of the standard, basic products that a bank offers to its clients. They are the bedrock of every transaction. Client capital, needed for every form of financing, is accumulated in these deposits. The current account is indispensable for regular monetary transactions, and is also used for the execution of credit transactions. The savings account is used to invest capital that is not required in the short-term, and the investment account is employed for long-term investments. In an investment account, the investor hopes for a higher income than from the other two types of deposit accounts. To date, no bank in the Swiss market, other than Faisal Private Bank SA, provides Islamic deposit accounts and none on the German market.

### **6.4.1.1. Findings of the applicability analysis for financial instruments**

In general, it can be anticipated that most of the Sharia compliant financial products would be demanded by the Muslim population in both countries, apart from Ijara. However, in Switzerland it would not make sense for an Islamic bank to introduce own asset or fund management instruments targeted at the Swiss population. The explanation is simple: most of these instruments are aimed at very wealthy people interested in Sharia compliant investments. In Switzerland there are not enough investors in that category: the demand is simply too small. As an alternative to its own products, banks can provide third party products, including Sukuk, to interested clients.

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<sup>196</sup> [www.failaka.com](http://www.failaka.com)

The situation in Germany is somewhat different. The Muslim population has reached the critical mass where it would make sense to offer asset or fund management instruments targeted at the Muslim population. But on the German market not one bank offers even the most basic Islamic financial instruments to their clients.

It should be clear that this evaluation of Islamic financial products is somewhat tentative, particularly because detailed information from the single Islamic bank operating on the Swiss and German market was not forthcoming. For final clarification and review of the options available, it would be necessary to consult Islamic scholars and experts. Further detailed market research is also needed to measure the needs of the potential clientele.

## **6.5. Comparison of the Swiss and German market**

In this chapter I will compare the Swiss and the German market in different aspects. Germany, due to its exposed and geographically optimal location in the heart of Europe, has already a competitive advantage over possible business rivals. For many years now, the German economy had very close business relations with the Middle East and the GCC region. In addition, Germany plays an important economic role due to its position as one of the most important members of the Euro block. The number of German Muslims amounts up to 3.5 million, which is the perfect prerequisite for Germany's financial institutions to become a global player in Islamic Banking. Not only as a provider of Sharia compliant products on the German market, but also in a leading position for whole Europe and also for investors of the GCC region

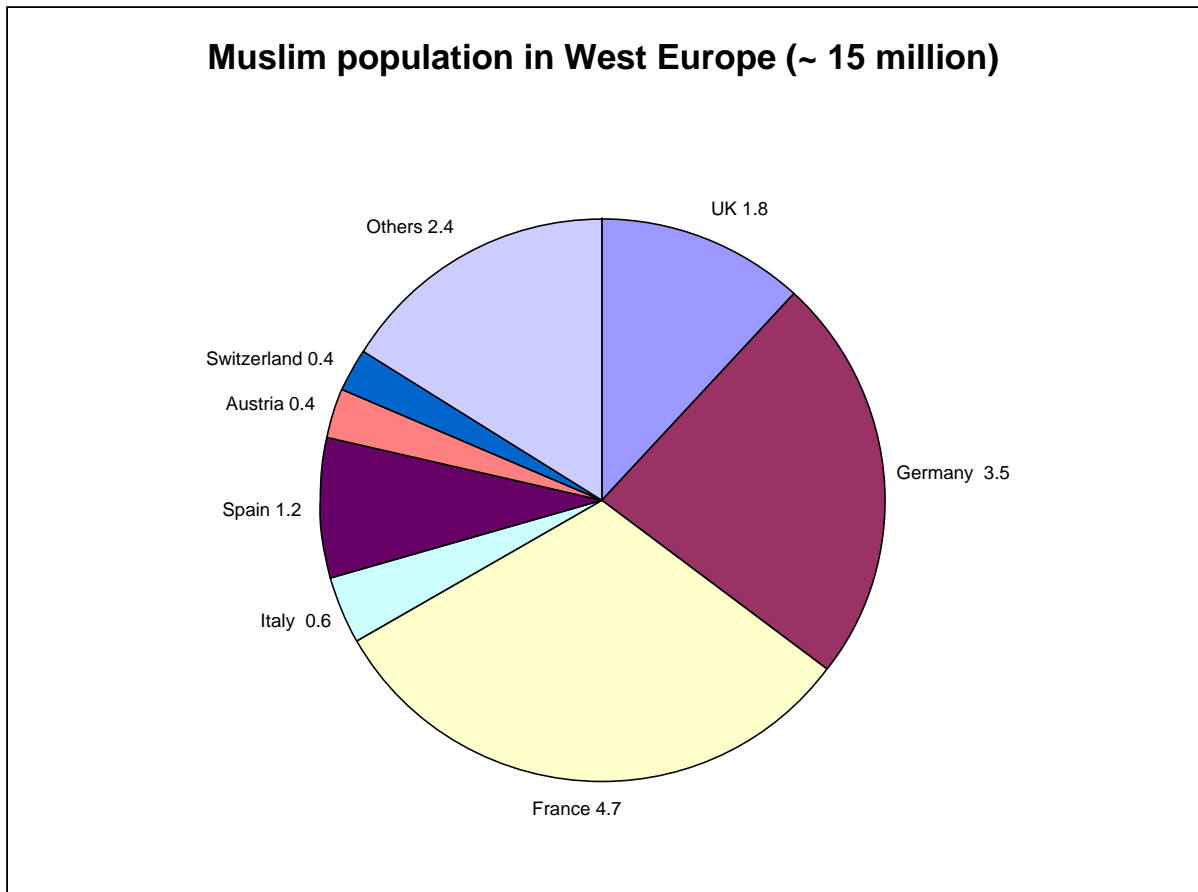


Figure 20 Muslim population in West Europe<sup>197</sup>

Despite this optimal initial position, Islamic Banking is actually not existent at all on the German market. Some years ago the market seemed to develop, when the Saxony-Anhalt sukuk was issued (the first European sovereign sukuk), but it remained just an exception. Nowadays, not even one Sharia compliant financial product can be found on the market that would have been designed explicitly for German clientele – actually there are no products at all available (apart from some funds that can be purchased internationally). Even though both Commerzbank and Deutsche Bank run so called „Islamic windows“, they do not gear towards the German market or German investors respectively, but concentrate a 100 percent on Arabic countries.

Possible potential provider of Sharia compliant financial products on the German market would be the Frankfurter Sparkasse as well as the Islamic Bank of Britain –

<sup>197</sup> Islamic Finance (2008) Booz & Company

next to Deutsche Bank and Commerzbank, which are already active in this sector and have therefore experience in the matter<sup>198</sup>. According to the study conducted by Ashrati (2008), the Frankfurter Sparkasse holds a market share of 35.5 percent of Germany's retail banking. Among this number there is of course a proportion of Muslims. Thus, market penetration is already quite high, which is an excellent initial position for opening an Islamic window.

In contrast, the Islamic Bank of Britain is a financial institution which concentrates only on Sharia compliant investments. The bank was founded in 2004 in the UK, authorized by the FSA (Financial Services Authority) and is the European leader regarding Islamic Finance. On the homepage interested investors are told that a plan exists to expand onto the German and French market, since these two countries are the ones with the largest Muslim population<sup>199</sup>. The success of its concept is easily made clear by looking at the companies key numbers: in 2007 the Islamic Bank of Britain operated 8 branches that serviced 42.000 clients who owned more than 64.000 bank accounts with deposits over 135 million GBP<sup>200</sup>. Considering that the British market consists of 1.8 million Muslims, „only“ these figures are even more impressive. As can be seen, the Islamic Bank of Britain should not be underestimated as potential rival on the German market.

The situation on the Swiss market presents itself somewhat different. Even though Switzerland is situated as well in the heart of Europe, it is much smaller regarding the surface than Germany. Still, Switzerland is an international financial centre, well-known across its border. The Swiss market regarding Islamic finance is much better developed than the German market, although the number of Muslims living in Switzerland is much smaller (according to the census in 2000 about 310.000 Muslims lived in Switzerland – according to Ackerl the number amount up to 440.000 in 2007). Different financial institutions and companies offer products in accordance with the Sharia in their product range: Citi Islamic Investment Bank, UBS, Da Vinci Investment to name only a few. Furthermore, there is a Bank, exclusively dedicated to financial services in accordance with the rules Islamic finance. Faisal Private Bank SA serves private clients on- and offshore and offers the whole range of Islamic financing.

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<sup>198</sup> Ashrati (2008) *ibid*, p. 118 ff

<sup>199</sup> [www.islamic-bank.com](http://www.islamic-bank.com)

<sup>200</sup> [www.islamic-bank.com](http://www.islamic-bank.com)



Therefore one can state that there are enough providers on the Swiss market, which can satisfy the demand of interested investors.

Switzerland has been aware of its locational advantages and makes use of them. Swiss Islamic banking is successful due to a combination of several characteristics, which are attributed to Switzerland as a financial centre and the implementation of financial products in accordance with the rules of the Sharia. Among these characteristics the most outstanding are good reputation, stability of the Swiss banking sector, high service and consulting quality, high quality of products offered, customer proximity and last but not least the perceived competence regarding asset and wealth management. Despite these facts, the Swiss market is no core business for local banks, since the potential is too limited.

If one compares the population of the two countries, the number of German Muslims (3.5 million) exceeds by far the number of Swiss Muslims (440.000). The Muslim population has more than doubled in the years between 1990 and 2000 – the same holds for the German population. From 1987 (when the last census took place in Germany) until 1995 the number of Muslims mounted from 1.65 million to 2.6 million<sup>201</sup>. In Switzerland, the age distribution shows that the major part of the Muslim population is younger than 50. As can be seen in the figure in chapter 6.2., the fraction of Muslims under 30 is very high. In contrast, looking at the German chart one can see that the lion's share of the Muslim population is at an age between 25 and 45 – the birth rate is obviously declining. Blume (2007) finds an explanation for this phenomenon. The birth rate of Muslim women living in Germany declines due to the existing structures, which are according to Blume economically liberal but at the same time hostile towards family life. The more integrated, the more reproductive behaviour adapts to the new environment<sup>202</sup>.

In Germany as well as in Switzerland Muslims receive a better and better education. Thereby not only income increases but also the disposable funds. No exact data is available for the Swiss market. For the German market expert report 1.917 EUR monthly net income and about 25 billion EUR annual purchasing power for Turkish households. The situation in Switzerland should be similar – adapted of course to the

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<sup>201</sup> [www.islamarchiv.de/akver/demografie.html](http://www.islamarchiv.de/akver/demografie.html)

<sup>202</sup> Blume M (2007) haben Muslime mehr Kinder? Zur Demographie des Islam in Deutschland. <http://religionswissenschaft.twoday.net/stories/4520939>

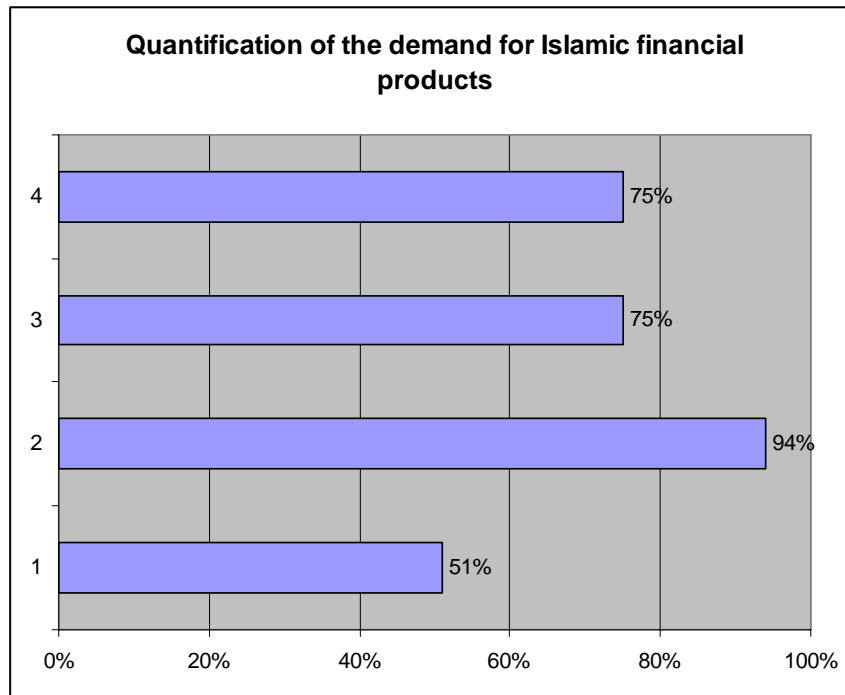
Swiss Muslim population. In addition, the annual number of money transfers from German and also Swiss Muslims to their home countries reduces gradually. This fact implies that the major part of the income (in Germany it is said to be about 95%) remains within the country.

These numbers clarify that there is a lot of potential for Islamic Finance on the German market, and less potential on the Swiss market. But due to the fast-growing Muslim population in Switzerland, and the favourable demographic structure of this population, one can be confident about the potential development of Islamic banking in the future. In a study conducted by Booz & Hamilton the potential for the Swiss Islamic retail market was raised. The estimated number of Muslim retail banking clients accounts for ca. 300.000, with an estimated total volume of 273 million CHF. Thereof, ca.136.000 million CHF account for construction financing, 37 million for consumer credits and 100 million for financial investments (investment funds and Islamic deposits)<sup>203</sup>. Faisal Private Bank SA offers all the mentioned products on the Swiss market, but does not market them actively. It proves to be more than difficult to gain access to information concerning products and conditions of Faisal Private Banks SA. Hence, a big part of the population is more or less completely unaware of this products being on the market. An improved marketing concept would be desirable.

To determine the potential on the German market is much more complicated. In the micro censuses of the last years the religious affiliation was not surveyed. 95 percent of the Turkish community in Germany describe themselves as affiliated Muslims. It is obvious that there is a huge potential on the German market due to above cited numbers (purchasing power, average income...). Ashrati (2008) tried to calculate in his study, which was carried out nationally, the demand for Islamic financial products on the German market:

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<sup>203</sup> Islamic Finance (2008) Booz & Company



1 = Awareness level of Islamic financial products

2 = Usage of conventional financial products

3 = Request that Sharia compliant products should be certificated by a Sharia Board

4 = Interest for an Islamic way of construction financing

**Figure 21 Quantification of the demand for Islamic financial products**

Ashrati (2008) attributes the high percentage of Muslims calling on conventional forms of investment to the lack of supply as well as the lack of awareness regarding the provided possibilities. Furthermore, the majority of the interrogated people stated explicitly that they would prefer a bank operating in accordance with the principles of the Sharia to a conventional bank.

Globally seen it has to be said that in the course of the financial crisis Islamic banking has real development possibilities. Investors feel disappointed and look for alternatives. Investments that are compliant with the Sharia could be such an alternative. Securitization of credits, short selling, and investment with companies above a certain degree of debt to equity ratio – all these risks are forbidden. Furthermore, one of the main principles in Islamic Finance is the sharing of risk between the determined partners. In such battered times everyone calls for stricter

rules for the financial system. Since Islamic finance is by definition rather conservative, it would easily integrate into a highly regulated environment.

Another point favouring Islamic banking at the moment is the increasing need for financial expenditure for big governmental projects in Europe, but above all in the GCC countries (especially for the expansion in the infrastructural, water and energy supply and real estate sector). Particularly in the GCC countries there is a lot of pressure to finance these projects in accordance with the principles of the Sharia.

In Switzerland as well as in Germany the implementation of products compliant with the Sharia is no problem in general. In Germany bureaucratic hurdles have to be overcome in order to make Islamic financing solutions competitive. One example is the financing of a real estate project via diminishing musharaka or murabaha. In this case the tax on acquisition of real estate is due twice, since the property changes twice the owner within the transaction. This double taxation discriminates this form of financing against conventional financing. In the UK a bill was put through that releases the first change in ownership from paying the tax.

Moreover, for Islamic banking a basis has to be established, like the creation of Sharia Supervisory Boards, which are in charge of the certification of Islamic financial products. The challenge today is to find qualified people – the talent pool is very small. Years of education, experience and practice necessary – not only as a scholar in Islamic law, but also in an economic sector. In Switzerland all institutions offering Sharia compliant products engage Sharia Supervisory Boards, which are situated in other countries (mainly London or the GCC countries). In Germany in contrast, since June 2008 the Zentralrat der Muslime in Deutschland (ZMD) certifies Islamic financial products.<sup>204</sup>

Further prerequisites to build up a successful Islamic finance sector in Germany and Switzerland would be: personnel that is specially trained and knows the Sharia into detail; concepts that are tailored to the target audience and above all appropriate products (home loan financing, funds...). Another important point is to market financial solutions actively. Most funds issued by Swiss banks were issued due to requests from private investors and are not marketed at all. It is a principle that the

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<sup>204</sup> <http://islam.de/10677.php>

better potential clients are informed about offers on a market the higher the demand for the product. Therefore, an often heard argument that Muslims would be already embedded into the market and completely satisfied with conventional products and that therefore the demand on the German market would be too small to make Islamic finance an interesting field is inefficient. This was also showed by a huge scandal some years ago. In the end of the 1990s Turkish associations and companies (Kombassan, Yimpas and some more) were promoting Sharia compliant investments in mosques and cultural aggregations. By doing so they collected about 5 billion EUR – which were peculated by these companies<sup>205</sup>.

All these facts can be regarded as evidence for the potential on the German market. An enlarged product range would not only increase the awareness among the population for Islamic financial products but would also have another positive effect: the more competition among different financial institutions, the more product innovations in order to remain competitive. Furthermore, the more competition, the lower the prices for the services offered by the competitors, which would make the market even more attractive for investors.

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<sup>205</sup> Middendorf S (2008) Halal statt Haram. In: Die Zeit, 01.05.2008. Nr. 19

## **7. Conclusion**

As shown in the last chapters Islamic banking is a booming market with an impressive annual growth rate. Even if last year's crisis did as well affect this market, one possible outcome are new chances that arise – for some investors Islamic banking may have become even more attractive due to the risk sensitive approach.

Islamic banking did concentrate so far on the GCC region, the European market, however, is becoming more and more interesting due to the increasing number of Muslims living in Europe – also the number of interested investors rises continuously. New products are developed; new providers enter the market as an alternative to providers of conventional banking. Even if Islamic Banking is still suffering from teething troubles (huge discrepancies between the individual interpretations of riba due to the lack of international standards, no centralized Sharia Board which could act as supreme authority to clarify controversial questions, no consistent standards for reporting and accounting) – the market has a promising future and should not be disregarded.

Anyone having a keen interest in Islamic banking has first and foremost to deal with the basics. Islam is a lot more than mere religion – it extends into every sector of a Muslims every day life. It is a political and legal system of values and norms, written down and fixed in the Sharia, the God-given basic of legislation in all Islamic countries. Further principles like the prohibition of riba, gharar and maysir, the restriction to halal activities and above all the principle of profit and loss sharing are of crucial importance for the understanding of Islamic banking. On the basis of these principles several financial instruments have been developed in the last years, designed according to the parameters of the Sharia. Islamic banks also have to make profit like every other economic entity, even if they do not make it through the conventional vehicle of interest. Thus, different forms have emerged – among them various contracts of sale, which are a form of debt financing with a mark-up sale, contracts of partnership, which are a form of equity participation and therefore direct profit and loss sharing, and leasing. Another possibility to invest capital in a Sharia

compliant way are Islamic bonds (Sukuk) and normal shares, which have to fulfil certain constraints dictated by the Sharia.

As a practical European example the German and the Swiss market for Islamic banking are examined and then compared. The findings of this comparison are as follows:

1. Both countries are well positioned, not only in terms of geographical location, but also in matters of economical strength. Both are situated in the heart of Europe, easily reachable and with a stable legal framework. Switzerland has the advantage of an excellent reputation as an international financial centre; Germany the advantage of long-time outstanding business relations with many Arabic countries.
2. Regarding the development of the markets for Sharia compliant products the two countries could not be more different: The Swiss market is well developed; various providers of Islamic financial products operate on the market – there is even a bank that works completely in accordance with the rules of the Sharia. By contrast, the German market is unknown territory. There are hardly any providers of Islamic financial products on the German market.
3. In Germany as well as in Switzerland Islamic banking does not belong to the core business of the banks offering Sharia compliant products – but due to different reasons. Both big players on the German market that are engaged in the Islamic financial sector (Deutsche Bank and Commerzbank) declare unanimously that they would not be interested at all in the German market. Swiss financial institutions see their growth opportunities in consequence of the limited potential on the Swiss market rather in the GCC region.
4. A crucial difference lies in the number of Muslims living in the respective countries. While in Switzerland about 440.000 Muslims are registered, in Germany there live about 3.5 million. In both countries the Muslim population more than doubled in the last 10 years. The savings ratio of Muslim households is very high in both countries compared to native households; the number of money transfers to home countries reduces annually; good

education and high income create prerequisites for a strong demand.

Interestingly, the age distribution is not distributed evenly. In Switzerland the bulk of the Muslim population is younger than 30, while in Germany the lion's share is between 25 and 45.

5. The applicability of products compliant with the principles of the Sharia should not be a problem neither in Germany nor in Switzerland – even if some products are more suitable for the German or Swiss market than others. The creation of a legal framework that does not discriminate Islamic finance would be necessary.
6. In my opinion the key difference between Germany and Switzerland consists in the existing growth potential and the use of this potential. On the Swiss market new customers could be attracted by marketing the existing products more intensely and thereby extending the demand a bit further. But generally speaking, the demand is satisfied. The case of Germany is completely different. The German potential is not tapped at all. Big growth opportunities wait for institutions that are able to market products actively and arouse the interest of the Muslim population.



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## **Abstract**

In the here present paper the German and the Swiss market for Islamic banking is investigated and afterwards compared. Therefore, in a first step and for a better understanding of the subject the development of Islamic banking and the integration in a global context is highlighted. Furthermore, the basics and principles that every market participant has to follow are discussed, since without knowlegde of these principles one could not understand Islamic banking. Moreover, this description is necessary in order to differentiate Islamic banking from conventional banking and show the differences between these two concepts. In the subsequent chapter individual financial instruments and possible applications in a real economic environment are explained.

In the main part the German and Swiss market are described more into detail. Market participants are identified that are present on the two national markets and that offer Islamic products there. In order to be able to compare the market potential of the two countries, the muslim population is examined by taking into account the demographic and social situation. Thereafter, several financial instruments are tested regarding their applicability. In the last chapter a comparison is drawn between the German and Swiss market related to the offer of financial instruments, market development, market potential and growth potential for new providers.

## **Zusammenfassung**

In der vorliegenden Arbeit wird der Schweizer und der Deutsche Markt für Islamic Banking näher untersucht und sodann verglichen. Hierfür wird zum bessern Verständnis in einem ersten Schritt die Entstehung und Geschichte des Islamic Banking und die Einbettung in einen heutigen globalen Kontext beleuchtet. Desweiteren werden die Grundlagen und Prinzipien, an welche sich sämtliche Marktteilnehmer zu halten haben, erörtert, ohne deren Kenntnis Islamic Banking nicht erklärbar wäre. Diese Darstellung ist notwendig um Islamic Banking vom konventionellen Bankwesen abzugrenzen und die Unterschiede dazu aufzuzeigen. In dem darauffolgenden Kapitel werden die einzelnen Finanzinstrumente erklärt und mögliche Anwendungen im realen wirtschaftlichen Umfeld angeschnitten.

Im Hauptteil werden dann der Deutsche und der Schweizer Markt im Detail beschrieben. Es werden Marktteilnehmer identifiziert, die auf den nationalen Märkten präsent sind und islamische Produkte anbieten. Um das Marktpotential in den Ländern darstellen und vergleichen zu können, wird die muslimische Bevölkerung in den beiden Ländern untersucht, unter Einbeziehung der demografischen und sozialen Situation dieser Bevölkerungsgruppe. Daraufhin werden die einzelnen Finanzinstrumente auf ihre Anwendbarkeit getestet. In dem letzten Kapitel werden Vergleiche zwischen dem Deutschen und der Schweizer Markt angestellt in Bezug auf Angebot an Finanzprodukten, Markterschließung, Marktpotential und vor allem auch Wachstumschancen für neue Anbieter.

## Curriculum vitae

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### Ausbildung

1990-91 Auslandsjahr (1. Klasse Gymnasium) in einem Internat im Piemonte (Italien)

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10/99 Beginn des Studiums in Wien (Geschichte, Theaterwissenschaft, Germanistik)

2004 Beginn Internationale BWL

2003-2004 Erasmus-Aufenthalt in Granada (Spanien)

07/05 Magistra der Philosophie (mit Auszeichnung)

### Jobs

2005 – 2008 Geschäftsführerin von „Dolce Terra Aichbichler Novotny OEG“ (Import von italienischen Spezialitäten für die Hochgastronomie)

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