

## **Eradicating Poverty through *Salam* and *Istisn'a'* Strategy for Poverty Reduction in Rural Pakistan**

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### **ABSTRACT**

*The share of microfinance in the Islamic financial industry is very low and, therefore the industry contributes very little to the poverty reduction. This study proposes a microfinance model based on Salam and Istisn'a'. The proposed model is based on cooperative structure in which the MFI places production order against finance, and arranges marketing by itself. In this way, the producer does not need to be engaged in marketing which is not his specialty. In this way, the producer devotes all his energy for production, the efficiency of producer increase. This paper also proposes mechanism for vulnerable financing on the same concepts.*

**Keywords:** Islamic Micro Finance, Salam, Istisn'a, MFI, Microfinance Intermediary.

### **Introduction:**

The importance that Islam gives to helping the poor and needy can hardly be overstated. Islamic *Shari'ah* has declared a well-defined share of a poor in the wealth of every Muslim in the form of *Zakat* and *Ushar*. Islam has made arrangement the arrangements so that poor can enjoy every celebration and it is made obligatory for the well-off people to help poor on the two annual celebrations i.e. Eid-ul-fitr and Eid-ul-Adha. Besides these obligatory sources of helping the poor's, Islam emphasizes much on voluntary donations in form of charity and alms. Even the Holy Prophet has said that a person cannot be a good Muslims if his neighbor spends the night in hunger.

However, despite this level of stress on the charity and alms, the Islamic financial system that emerged during last 50 years has no space for helping the poor. The charity and micro financing that provides basis for helping the poor constitute only negligible part of the overall Islamic finance. According to Islamic Microfinance Network website, the total volume of Islamic financial industry is over 1.3 trillion \$ whereas the volume microfinance is only 1 billion million dollar which forms only 0.1% of the industry. To keep the Islamic financial industry consistent with its spirit, there is need of taking initiative to improve the role of Islamic financial institution in the poverty reduction.

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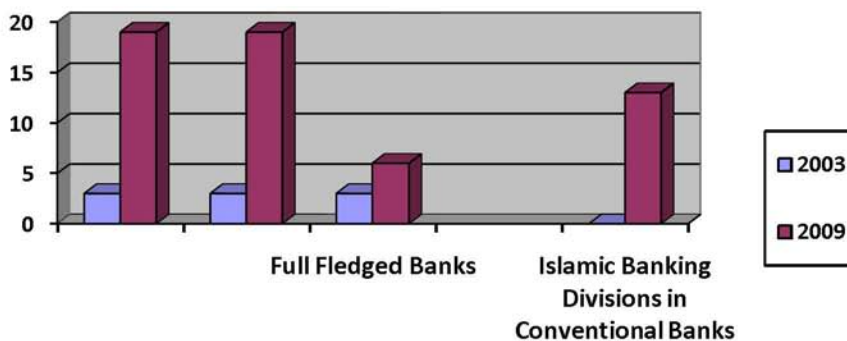


Figure 4: Increase Number of Islamic Banking Institutions

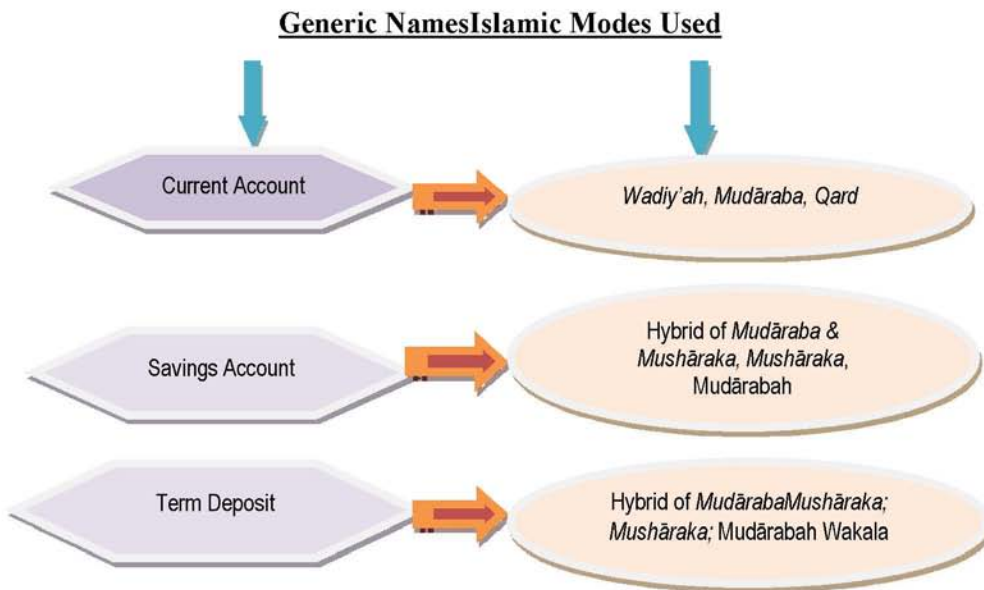
Such growth is obstructed by many challenges that need to be addressed in an adequate manner (Haron & Shanmugan, 1997). State Bank of Pakistan emphasized on strenuous efforts in terms of research capacity building, policies, audit, risk management and conformity to *sharī'ah* for Islamic Banking Industry. This indicates the importance of tools employed for *sharī'ah* compliance and all the formulated trading systems, financial engineering are tailored as per Islamic injunctions to meet the standards of fulfilment of *maqāsid al Sharī'ah* in pursuit of welfare of Islamic state and its citizens. The real impact of Islamic banking is the economic aspect of moral impact which can be seen significant in not only Pakistan but overall. It is said that the conventional global banking system has adopted many tools of Islamic banking system to strengthen their system (Toutourchian, 2009).

## References

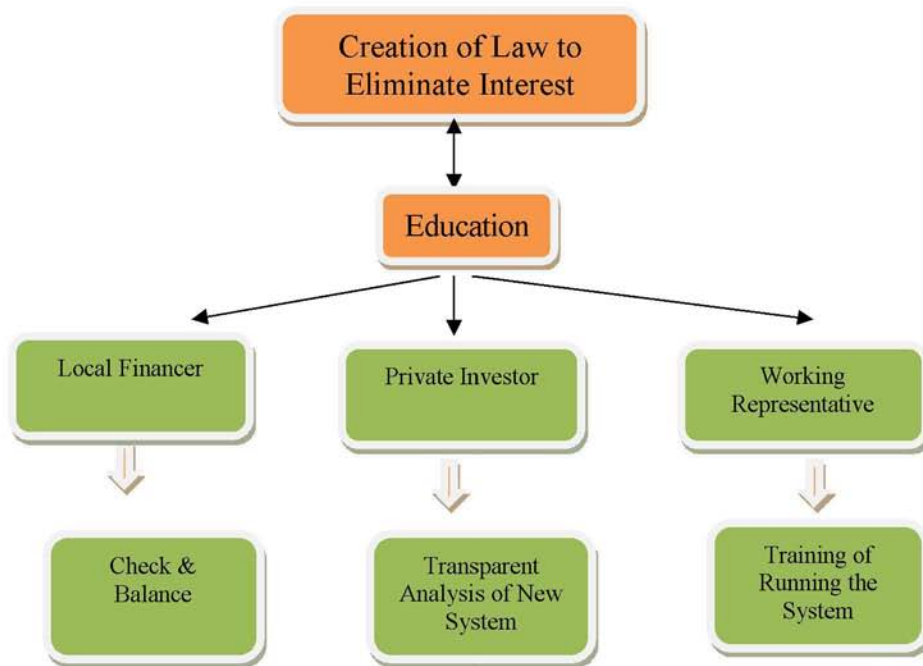
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Although Islamic *Sharī'ah* frame provides a number of practical and useful modes of trade, business and finance like *Murābaha*, *Ijārah*, *Salam*, *Hiba* etc.

These are currently used to be used as an alternative to recurrent conventional banking offerings. A representation of conventional modes and their Islamic alternatives are shown in the figure 3 below:



All these steps are found remarkable in uplifting the poor and the elimination of poverty in Pakistan. But still there are some serious complications and hurdles from local and foreign bodies to achieve the goal of complete Islamic Economic System in the way of Pakistan (Khan & Mirakhor, 2010). Elimination of *ribā* was one of the bold steps taken in 1980s, in an effort for implementation of *Sharī'ah* compliant interest free banking. In 2001, an Islamic Banking division was established at State Bank of Pakistan keeping in view the experiences of Bahrain, Malaysia, and Saudi Arabia. The growth of Islamic finance is globally very fast, i.e. 15-20 % as estimated by Islamic Development Bank, and it's a wide spread phenomena in Pakistan too. Islamic finance is successfully running commercialized banking, *Takāful*, as well as funds management. That's the reason the number of Islamic banks increased as shown in the figure:



Raja Zafar ul Haq Commission Report specified three business groups in the banking system, private domestic group, the Government and the foreign financier. The commission suggested the settlement of government liabilities as mobilization of the resources for the retiring governmental debt and future fiscal operation clarity. The Commission of Transformation of Financial System (CTFS) was formed in the State Bank of Pakistan in 2000. The commission in its two interim reports felt that:

1. There is a lack of education and awareness about the Islamic System and the system introduced by the government bodies.
2. A legal infrastructure for running the system is needed

This commission in its serious and consistent efforts worked to construct the system of Islamic banking and finance in Pakistan.

Other serious measures taken by the government of Pakistan were:

1. Task Force of Ministry of Law
2. Finance Minister's Delegation to study the banking systems of other Islamic countries (Egypt, Saudi Arabia and Malaysia)

The task force after completing its work suggested that Malaysia would be the best role-model for Pakistan in this regard. Moreover, the task force in its final report concluded that it will not be beneficial for Pakistan to adopt a completely new and different system of banking and finance as one-step. It will be harmful for the financial data of the government

(<http://sbp.org.pk/departments/pdf/StrategicPlanPDF/AppendixD%20Summary%20of%20Reports.pdf>; [www.sbp.org.pk/ibd/Islamic-Bkg-Review-03-07.pdf](http://www.sbp.org.pk/ibd/Islamic-Bkg-Review-03-07.pdf)).

sharī'ah demands. In the constitution making the basic structure of state as Islamic frame, it was felt important to change the economic system of the state. In this context, since 1973, many suggestions, recommendations, laws and ordinances were made, passed and implemented in Pakistan.

a) **Property Rights** Private property rights are protected in Pakistani law under the sharī'ah concept of individual's property ownership. It entertains the economic development on individual level. The position of Pakistan is 30th in the Asian index of property right.

b) **Zakāt and Usher Ordinance**In the history of Islamization of economic structure of Pakistan, the *zakāt* and *usher* ordinance is a successful contribution by the government sector. The departments of *zakāt* and *usher* in Pakistan has successfully practice the politics of Islamic economics in fulfilling many sharī'ah obligations of the State. It is playing a positive role in the elimination of poverty and up lifting of the poor by supporting them in education, social problems and investment (<http://www.Zakat.gop.pk>).

c) **Islamization of Banking and Finance System**

Banking and finance system bears a general structure of a country's economic system. In Pakistan the improvement in this system is made on the basis of elimination of usury/*ribā*. The sequence of the 1973 constitution, the elimination of usury/*ribā* was responsibility of the state of Pakistan. In the struggle of Islamization of economic system, many governmental and non-governmental institutions have made their contributions. In 1979, Islamic Ideology Council prepared a report which suggested two *ribā* free business techniques, Profit-lose sharing and *Qarz e Hasanah*. There were few other practical techniques also which were adopted by the private investors and financiers, leasing, hire Purchase, *Bai' Mu'jjal* and investment Auctioning etc. All above suggested modes were to be practiced on three main objectives, normal rate of return, actual operating adjustment and no back door usage for interest.

In 1991, Federal Sharī'ah Court made a decision in the case of the elimination of interest/*ribā*/usury from the economic system of Pakistan; the concerned government departments immediately adopt concrete steps for this purpose. So, in the achievement of the interest free banking and finance system the Hanafi Commission (made by State Bank of Pakistan) Report contributed many solid and concrete steps two of which are *Mushārah* and *Mudārah* (Rasul, 2010). The commission recommended for all the participants of banking system an action plan which can be shown in Figure 2 as follows:

### **h) Property Rights**

*Allāh* has created a lot of preserves in this universe and guarantees these preserves to everyone and everyone have their own possession on preserve but with utilizing of these resources deal with individuals and betterment of community by making tax and take risks and also prohibited the hoarding of recourses and concentration of wealth (Hamza, 2011).

### **i) Income Distribution**

In matter of income distribution, distribution is economic process in which the state is responsible to collect all taxes from the people and from productive land; it improves income and wealth distribution. That is why; individuals are highly encouraged for the contribution to the needy neighbors and anticipate to be rewarded by *Allāh* on the day of resurrection (Siddiqi, 1983). *Zakāt* is a widespread wealth tax obligatory on all income earning property counting the possession of animals, gold, and silver, articles of trade, and the manufacture of the land. It is collected by the government to make sure proper distribution among the poor and needy in order to improve income/wealth distribution. *Usher* is a property tax on creative land when and only when it produces harvest. The tax rate depends on the quality of the land: 5% on irrigated land and 10% on rain-fed land. *Kharaj* is tax on income from the land. It can be fixed or proportional. *Interest and Usury* The taking of interest on money lending is prohibited. Usury is utilization of one person by another and therefore sinful for three reasons: It increases the consideration of economic wealth; it involves a riskless economic business enterprise; it is a self-absorbed attempt to exploit the money's rate of arrival without labor activity and hard work. Concentration of wealth must be based on personal effort and labor and capital investment. In an Islamic banking system, depositors are partners who share the profit or loss of the activity and pay a small transaction cost (Warde, 2000). *Rent* Like interest, rent on virgin land or uncreative resources are forbidden. However, rent can be levied (only in cash, not in kind) on enhanced land and possessions which necessitate labor or capital deal. Rent is theme to property tax to restructure income. *Inheritance* The inter-generational alter of wealth is based upon the following principles: the deceased can transfer up to 1/3 of his/her property as wanted; women are free to divide in inheritance, but only 1/2 of men's share; the inheritors are members of the direct family, but other relatives increase share of distribution if desired by the departed; the state comes into the land of a person with no legal inheritors; the offspring's must pay property taxes to the state. So in economic policy presented above rules, regulations, principles must be following.

### **Implementation of Islamic Economic System the Experience of Pakistan**

In Pakistan the creation and implementation of Islamic economic regulations has remained as the outstanding effort done by the authorities as well as the Muslim scholars. There are two areas covered in the implementation of Islamic economic system in the country, elimination of shari'ah prohibition and the compliance of

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to show it in deeds of charity; be good citizen, support social organisations; and be firm and unshakable in all circumstances (Ayub, 2007).

This average of judgment delivers the centre around which the whole moral conduct should turn round Before placing down any moral commands Islam seeks to firmly implant in man's heart the pledge that his transactions are with God who sees him at all times and in all places; that he cannot hide from Him, cannot betray Him nor can he run away from God. Thus, by setting God's pleasure as the objective of man's life, Islam has well-appointed the highest possible standard of morality.

#### **f) Equitable Distribution of Wealth and Income**

A few decades ago, freedom from interest was unknown to the West and the world banking community as an improved option to an interest-based economic system. *Zakāt* is also an important part of Islamic economic system (Qureshi, 1999). The *Qur'ān* itself explains the economic position of *Zakāt*. The order to pay *Zakāt* is mentioned more than 100 times, usually in harmony with *Salah*, as two means of purification. *Allāh* commands Muslims to pay *Zakāt* on their total wealth according to *nisab*, (minimum wealth) to the poor for benefit of the society's social and economic welfare. Qur'ānic verses, underline that all resources belong to *Allāh* and that these resources are thus a trust that must be used to satisfy the basic needs of all those who cannot afford the basic supplies of life in a humane and distinguished manner. In 6:141 *Allāh* Almighty gives a beautiful simile of blessings in the form of fruits which yields and there is a share in the form of *Zakāt* in the harvest for those who are needy. *Allāh* enjoin the believers to take what the messenger gives you and refrain from what he forbids in order to avoid *Allāh*'s punishment (59:7). According to *Qur'ān* monetary justice and providing general well-being for all members of the society needs a focus on three essential economic factors: earning halal income; ensuring equitable circulation of wealth; and creating economic safety to assure need fulfilment of those who can't afford basic provisions of life. By paying *Zakāt*, a person fulfils religious obligation, whereas a taxpayer pays taxes to enable the state to perform its duty competently.

#### **g) Family and Social Solidarity**

Meanings of harmony are unity, agreement, consistency, and unity. Thus solidarity also gives the true meaning of Islamic norms and ethics in a complete way(Ahmed & Eijaz, 2011). In *Surah al-Imran*, verse 103, an excellent example is given stressing the believers to hold fast to the rope of *Allāh* and do not divide into groups. *Allāh* Always favours by saving the believers from falling into pit of Fire by sending clear signs in the form of ayahs. Islamic harmony does not only talk about for the oneness of Muslims but it also wishes to hold other peoples of the world together. Islam supports unity of all mankind, fairness, and equal opportunity Islam integrates humanity instead of dividing (Jafari, 2014).

depression and destruction individual as well as community (Muslim, 1996). The prophet (ﷺ) associated justice with darkness on the day of resurrection because people has created black darkness in this world through the prevailing of injustice and end of the result it becomes the depression social conflict and displeasure and become the reason of clash and decline. Therefore injustice and Islam both cooperate with each other in matter of life and result comes in the shape of displaced and weakness of human being. Injustice has widespread meanings like all forms of inequity, injustice, misuse and use of misbehave through this a person hurts others and deprive them from all evil deeds (Chapra, 1985).

**d) Security of life, property and honour**

The Islamic views and its morals discourse the third terrible need of the human personality which is security of life, property and honour. Security of life is emphasized repeatedly in different verses of the Holy *Qur'ān* to the extent that killing an innocent life is like killing humanity and saving one is saving all mankind (5:32). This is natural because the Islamic call for the admiration of life and the brotherhood of mankind would be worthless if the life of even-non-Muslim were not considered to be as sacred as that of Muslims. The Prophet (S.A.W) address which he provided during his departure pilgrimage stated that the believer's life, property and honour are sacred for each other; just as the sacred day of Hajj and pilgrimage. Since the *hajj* enjoys utmost degree of purity in Islam, the life, property and honour of every individual also enjoy the same degree of purity (Chapra, 2007).

**e) Social and Moral Uplift**

Spiritual raise may be separate in rebirth as well as achievement, but moral raise suggests one's behaviour and conduct in relations with other beings, and animal. Man is a social being, and hardly any of his actions, by thought. Word or deed, is without its direct or indirect effect on the society he is a fellow of. In fact, even mystical improvement is well nigh unbearable without the farming of natural and suitable moral values. Religion in practice is, therefore, nothing but a strong-minded and normal effort to lead a pious, virtuous and moral life (Jain, 1975).

Islam has laid down collective important rights for humanity as a whole, which are to be practical and esteemed under all situations. To achieve these rights Islam delivers not only legal protections but also a very actual moral system. Thus whatsoever leads to the welfare of the individual or the society is morally good in Islam and whatever is harmful is morally had. Islam assigns so much importance to the love of God it warns against too much of formalism( Ayub, 2007). Righteousness is described in the Holy *Qur'ān* (2:177) it encompass beliefs including faith in Oneness of *Allāh*, His books, angels, Last day; as well as helping poor, orphans, travellers, slaves and charity and patience. For a virtuous and God-fearing man one should fix his stare on the love of God and the love of his fellow-men in the given four heads: faith should be true and sincere;



**a) Dignity and Self Respect**

The word 'Dignity' comes from the Latin noun *decus* means development, individuality honour and majesty. But literally dignity means someone is unlimited to respect (Lebech, 2014). According to 1996 international human rights agreement " *these rights drive from the inherent dignity of the human person.* " (ICESCR, Preamble; ICCPR, Article 10). Islam explains the dignity as a very good manner it is stated that *Allāh* has made the *Fitrāh* of human being and un-doubted *Allāh* is good. The distinctive nature of human beings is also good (5:4) as long as they do not corrupt it (30:30). That's why *Allāh* Almighty made the human being as a *khalifah* on earth, all Muslims are equal in the status of *khalifah* with each other. Our lives are just like a trust one day we will give it back to the *Allāh* Almighty therefore one should to observe mutual harmony and have non violent relationship and use those sources in the way of *Allāh* for the benefit of human beings (17:70). This honour has been conferred being the *khalifahs* or vicegerents of God on earth (2:30).

Likewise human being is not sinner by birth but he become sinner due to changing in environment and his acceptance of those changes without any hesitation, *Qur'ān* defines different occasion related to the conflict of sin and it also highlights the its punishment depended (57:7) the good or bad deeds of his/her. *Allāh* has a lot of qualities in such two qualities are *Al Rahmān* (merciful) and *Al Rahim* (mercy upon) (6:164; 15:35) if a person do bad deeds but in his lifetime he returns to the *Allāh* for seeking his forgiveness (Chapra, 2007). But human being has no limits he has no boundary he can use the resources with free will. And *Allāh* is merciful upon everyone. It would be impossible for Him to do so given that He is a Loving (*Wudood*) and forgiving God and has all the good attributes that can be conceived (7:180).

**b) Social Equality and Justice**

The second need of the human personality is justice and equality not only individual level but also on the state of community. The main purpose of human dignity, brotherhood, self respect, social equality and well-being of all would remain empty ideas having totally no soul if they are not propping by socio-economic justice (Chapra, 2007).

**c) The Essence of Justice**

Literally Justice is fairness in giving rights and in enduring by responsibilities without judgments for any reason, either for religion, race, colour, etc (Lahsasna, 2013). *Qur'ān* also gives a lot of stress upon the justice of humanity or it is placed in *Qur'ān* that "justice is nearest to piety" (5:8). In positions of its importance in the Islamic faith, piety is surely the most necessary because it helps as a substance for all rightful actions, including justice. So it is proof that *Allāh*'s major aim to protecting the people from injustice and provide justice for this purpose he sends his messengers (57:10).The *Qur'ān* has clearly stated that there can be no peace without justice by saying that the lack of justice lead to

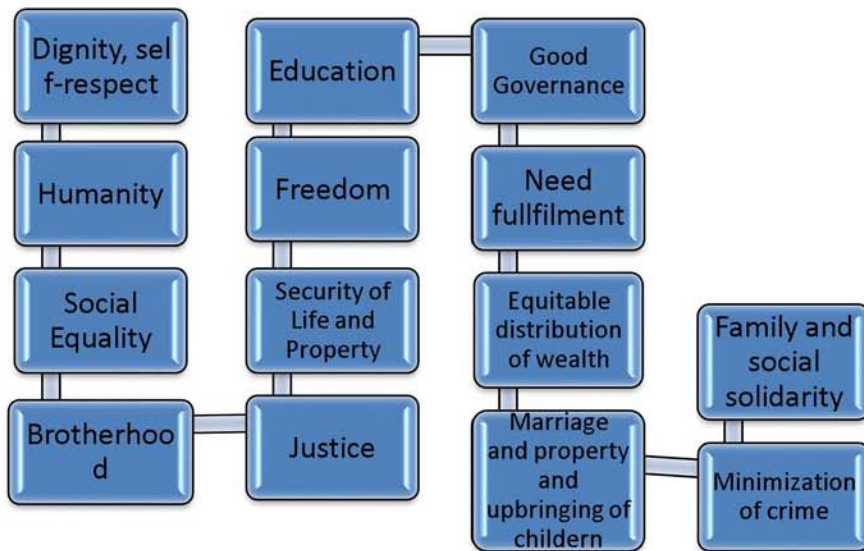
### Elimination of Wastage of Resources

The important aim of Islamic economics is to stop elimination of surplus resources of Islamic economics. *Allāh* Almighty creates all these resources to fulfil the need of all men and therefore made all things useful in the universe, as bounties and blessings which provided for the human being. *Allāh* created these resources for the human being and wastage of these resources is not acceptable and will punish in this life and hereafter (Elsefy, 2007).

### Implication of *Maqāsid Al Sharī'ah* Social Policy

The aim of social policy is to help, improve and protect the lives of needy. The main purpose of *maqāsid al Sharī'ah* is to protect the individuals by protecting the situation, currency, and human rights of society and provide them welfare and betterment. *Imam Al-Ghazāli* used the word 'safeguard' to make sure the continued growth, development and wellbeing of a society (Laldin, 2008). A person can get wellbeing, development and improvement till a social policy is working with the implication of *Maqāsid Al Sharī'ah* and as per the needs specified by classical *Fuqahāas* shown in the figure:

Figure 1: *Maqāsid al Sharī'ah*: Human Well Being to Be Realized By Ensuring Enrichment of Following:



Islamic theme of some terminologies of social policy is presented here: