Q: Can, in the light of the Injunctions of Islam, any differentiation be made between private and public banking in respect of charging interest on banking facilities or services rendered?

A: Public and private banking institutions are treated at par in respect of the Islamic injunction of prohibition of interest. No interest is allowed on any financial transaction in both public and private banks. However, the banks both in public and private sector can charge service charges to take care of administrative expenses.

(i) Can the capital, according to the Injunctions of Islam, be regarded as an agent of production thus requiring return for its use?

(ii) Does devaluation of the currency affect the payment of loans taken before such devaluation?

(iii) Can inflation causing rise in the cost/ value of gold and consumer goods in terms of currency have any effect on the sum, borrowed?

A: The word capital is used in two meanings: Physical and financial.

-Physical capitol like machinery, building, etc. participating in the production process are allowed to claim their reward in the form of rental.

-Financial capital like money and near-money instruments taking part in the production process through Mudarba or Musharkah arrangement can participate in profit or loss. However, no fixed return is admissible for the use of money capital.

ii) The question is two dimensional. The first relates to the effect of devaluation on the internal loans. In such loans, the same amount of loan will be repayable as before the devaluation. In this case, Imam Istijabi reports the consensus of Fuqahah on the point that, if there is any change in the value of currency, then the same amount of currency units will be repaid as were loaned.'

As far as the payment of the external loans is concerned, the devaluation will involve extra payment proportional to the rate of devaluation on such loans.

iii) The answer here is essentially related to the above answer. A given sum borrowed before inflation will be repaid in the same amount, after the inflation. The inflation tends to reduce the real burden of the loan. From this angle, it tends to favour the borrower against the lender. To protect the lender, the indexation of loan is not allowed because the indexation while protecting lender, hurts the borrowers.

Real answer to the problem of inflation is the introduction of the Islamic Economic System in totality. An important feature of this system in the monetary sector is prevalence of a relatively constant value of money.

Contemporary fatawaa