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11 July 2019

Online at <https://mpra.ub.uni-muenchen.de/95006/>
MPRA Paper No. 95006, posted 13 Jul 2019 08:27 UTC

Criticism of the Interest System in Conventional Banking and Islamic Monetary Solutions

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Abstract. The purpose of this study is to review some of the criticisms of the Bank's interest system. Issues related to whether bank interest including usury or not usury has been debated and is still being discussed to date by Islamic economists. But now there has been criticism from Western or Conventional Economists of the negative impact of the Bank's interest in the economy. The method used is a qualitative method using descriptive analysis and literature review. From these experiences, the Islamic Monetary System which is free from interest can be a solution to realize prosperity and guarantee economic justice. This system is expected not only to increase the money in circulation but how to be able to improve the performance of the real sector in accordance with Islamic sharia. Because basically in the Islamic monetary system, it is not only aimed at material welfare but aims at moral well-being. There are at least five values of Islamic economic instruments that can be integrated into the economic system, namely zakat, waqf, social security, the justice system in resolving economic disputes and sharia financial institutions

Keyword : criticism, interest system, Islamic monetary.

JEL : A10, E03, E42, P43, P51

I. INTRODUCTION

Speaking of banking, the existing banking system in Indonesia has followed a conventional system and some have followed the sharia system. But basically, all banking systems are inseparable from bank interest. Issues related to whether bank interest including usury or not usury has been debated and is still being discussed to date. There are several opinions that state the pros and cons even among the scholars themselves.

There are three opinions that are discussed related to whether bank interest is the same as usury, the first is bank interest including usury and because it is considered unlawful. Second, allowing interest because it is considered not the same as usury which is forbidden by the Islamic Shari'a. Third, bank interest is forbidden but because there is no way out for it, it is permissible. Whereas in the view of Islam, interest (usury) is a system that is prohibited in the Koran and hadith. Therefore, through the literature study method, the author will examine in depth the criticism of bank interest, including usury or not, and examine how the Islamic monetary system.

As for the Islamic monetary system, this system is expected not only to increase the money in circulation but how to be able to improve the performance of the real sector in accordance with Islamic Sharia. Because basically the Islamic monetary system is not only aimed at material welfare, but aims at moral well-being. Islamic monetary system will be discussed in this discussion as a comparison and solution to the problem of bank interest.

II. RESEARCH METHODS

The interest-based banking economic system research method used in this research topic is in the form of studies or literature studies obtained from various sources of books, journals, and other sources that are very relevant to the topic of this research

III. LITERATURE REVIEW

3.1. Bank Interest System (Conventional Banking System)

Bank interest is a remuneration provided by the bank based on conventional principles to customers who carry out savings or loan transactions with the bank. Interest can also be interpreted as the price to be paid to the customer (who has savings) with what the customer has to pay to the bank (the customer who gets the loan).¹

Bank Interest Criteria:

1. The determination of interest is made at the time of the contract with the assumption that it must always be profitable.
2. The percentage is based on the amount of money (capital) that is lent.
3. Fixed interest payments as promised without growth whether the project carried out by the customer is profit or loss.
4. The amount of interest payments does not increase even if the number of profits multiplies or the economic situation is "booming".
5. The existence of interest is doubtful (if not criticized) by all religions, including Islam.²

Based on the method there are two kinds of interest given by the bank to its customers, the two types of bank interest are as follows:³

- Bank interest in the form of deposit interest, namely interest given by the bank to the customer as a reward for customers who save their money in the bank.
- Bank interest in the form of loan interest is the interest given to borrowers to the bank because of borrowing.

From the various definitions above, it is very clear that bank interest is an addition due to the existence of deposits and loans between the customer and the bank from the principal and loan principal carried out or transacted. Savings and loan systems that generate bank interest are among the targets and instruments in conventional monetary system policies.

3.2. Criticism of the Bank's Flower System

1. Criticism based on the opinions of experts

¹ Abdul Haris, "Sistem Ekonomi Perbankan Berlandaskan Bunga (Analisis Perdebatan Bunga Bank Termasuk Riba Atau Tidak)," *AKutansi Dan Pajak* 13 No 1 (n.d.), <https://jurnal.stie-aas.ac.id>.

² Syafi'i Antonio, *Bank Syariah : Dari Teori Ke Praktik* (Jakarta: Gema Insani Press, 2001).

³ Syafi'i Antonio.

Muslim scholars and scholars still have differences of opinion about bank interest law. Some of them are Abu Zahrah, Abu al-Maududi, Abdullah al-Arabi, and Yusuf Qardhawi, saying that conventional bank interest is included in the *riba nasiah* class which is prohibited by Islam. So that Muslims are prohibited from conducting transactions with banks that use the interest system in various transactions carried out, except when this happens in an emergency so that there is a settlement or relief.⁴

Yusuf Qardhawi said that bank interest is usury and expressly forbids the existence of transactions with conventional banks. In his view, he did not know the term emergency, so there was no such thing as *rukhsah* (relief). Furthermore, the opinion of Al-Syirbashi, according to him, that conventional bank interest obtained by someone who held money in the bank was usury without seeing much interest earned. Strict Islam whose name is haram even though the interest is still a bit unclean. But those who are forced, the religion allows borrowing money at the bank with interest.⁵

According to Yusuf Qardhawi unlawful bank interest based on *ijma* results conducted by three well-known scientific institutions, namely the Islamic center of Al Azhar in Egypt, the Rabithah Alam Al Islami Islamic Institute in Makah, and the Islamic Fiqh institution in Makah, and the OIC in Jeddah. The *ijma* results cannot be canceled except with other equivalent *ijma*.

The opinion of Shaykh Sholih bin Ghonim As Sadlan, where a Saudi Arabian Mufti named Syaikh Muhammad ibn Ibrahim rahimahullah suggests that loans given by banks with certain interests are both called usury. Because the interest of the bank itself is an advantage of lending and borrowing transactions. Therefore, what is called bank interest is taken from borrowing or saving, it is usury because it is obtained from the addition (in accounts payable)⁶

According to the Ulama in the Middle East who are supported by several economic experts in secular countries, they argue that usury is not the same as bank interest, so bank interest is permissible or not. Like the Egyptian Mufti, Dr. Sayid Thantawi said that he was allowed to issue a bond certificate issued by the Egyptian National Bank, which in total was still using the interest system.⁷

Other experts like Dr. Ibrahim Abdullah anNashir said, "The right words are that there is no power of Islam without being supported by the power of the economy, and there is no economic power without being supported by banks, while there is no banking without usury. He also said, "The banking system of the banking industry has clear differences with the religious charities which are prohibited by the Holy Qur'an. Because bank interest is a new thing, the law is not subject to definite texts contained in the Qur'an about the prohibition of usury".⁸

Mr. Kasman Singodimedjo argues that the modern banking system is permissible because it does not contain the elements of exploitation that are illegal, therefore there is no need to establish a bank without interest. A. Hasan Bangil, the leader of Islamic Unity (PERSIS), expressly stated that bank interest is lawful because there is no multiplier element.⁹

⁴ Haris, "Sistem Ekonomi Perbankan Berlandaskan Bunga (Analisis Perdebatan Bunga Bank Termasuk Riba Atau Tidak)."

⁵ Haris.

⁶ Haris.

⁷ Haris.

⁸ Haris.

⁹ Haris.

Another argument that states that the interest given by financial institutions today is not the same as usury practiced in the era of ignorance. But this argument, unable to shake the opinions of the jurists and the majority of modern Muslim economists who upheld the historical consensus on usury, which received much support.¹⁰ Their opinion, the term usury means an interest in all its manifestations without distinguishing between consumptive and productive loans, between personal and commercial loans, or whether the borrower is a government, private individual or company and does not distinguish between low and high-interest rates. This is clearly summarized in Q.S. Al-Baqarah [2]: 275-279.¹¹

2. Criticism of the interest system because of its impact on the economy

From an economic perspective, the prohibition of usury is at least due to four factors,¹² namely: first, the conventional economic system causes injustice. Because capital owners will definitely get profits without considering the results of the business carried out by the borrower. If the borrower does not get a profit or bankrupt his business, he still pays back the borrowed capital plus interest. In conditions like this, the borrower has gone bankrupt as if he has been hit by a ladder again and not infrequently the application of interest instead of helping the creditor's business, actually adds to his problems. This is where injustice arises.

Second, the conventional economic system is the main reason for the imbalance between investors and borrowers. The large profits obtained by borrowers which usually consist of giant industrial groups (conglomerates) are only required to pay capital loans plus interest in a relatively small amount compared to the profits they earn. While for savers in commercial banks consisting of middle to lower class people do not get a balanced profit from the funds they save in the bank.

Third, the conventional economic system will hinder investment because the higher the interest rate, the smaller the tendency of people to invest in the real sector. People are more likely to save their money in banks because of the greater profits due to the high-interest rates.

Fourth, interest is considered as an additional production cost. High production costs will cause an increase in the price of goods (products). Rising prices, in turn, will invite inflation as a result of weak public purchasing power.

A real example is a monetary crisis that occurred in 1997-1998 and the global crisis in 2008. At a time when Indonesia was hit by the monetary and banking crisis in 1997-1998, at that time bank interest rates soared to a high of 60%. With such high-interest rates, it can be said that almost no one dares to borrow from a bank for investment. Thus, the violation of usury in Islam, the investment flow becomes optimal and channeled to the productive sector. Meanwhile, in the conventional system, the interest system makes investment flows not optimal and not smooth because some are hampered.

Meanwhile, criticism of the western economy has been raised by many western economists themselves such as: Schumpeter in 1940 who said that the economy entered a period of crisis, Daniel Bell and Irving Kristol in the 1950s in their book *The Crisis in Economic Theory*,

¹⁰ M. Umer Chapra, *The Future of Economics: An Islamic Perspectives Islamic Foudation* (leicester: Islamic Foudation, 2000).

¹¹ Ummi Kalsum, "Riba Dan Bunga Bank Dalam Islam (Analisis Hukum Dan Dampaknya Terhadap Perekonomian Umat)," *AL Adl* 7 no 2 (n.d.), <http://ejournal.iainkendari.ac.id/al-adl/article/view/220>.

¹² A.M. Sadeq, "Factor Pricing and Income Distribution from an Islamic Perspective," *Journal of Islamic Economics*, 1989.

Gunnar Myrdal 1960s who was the architect of Pakistan's development economy¹³ with his book Institutional Economics, Hyla Mint in his book Economic Theory and underdeveloped countries.

Another criticism is the criticism of Mahbulul Haq (1970), Amitai Etzioni (1988), Crito-Van Barque (1993), Paul Emerald (1994), Fritjof Chapra (1999), Stiglitz (2004), Naomi Klein (2007). And Hendri Tanjung (2009).

From these experiences, sharia economic systems that are free of interest/usury can be a solution to realize prosperity and guarantee economic justice. As said economist Umer Chapra in his book entitled The future of economics: an Islamic Perspective. In the book, it is said that the solution to the problems of the world economy is based on Islamic economics.¹⁴

However, what should be discussed further is how to apply the Islamic economy into the existing economy, or what strategy can be implemented to 'Islamicise' the existing economy?

3.3. Islamic Monetary System

According to M. Umer Chapra, Islamic monetary system policy is different from conventional monetary policy in the selection of targets and instruments. One fundamental difference is that it does not allow for guarantees of nominal or interest rates. Therefore, the target of implementing Islam-based policies does not establish tribes

Then the next difference in conventional systems is that there is a fractional reserve banking system where banks are only required to store reserves in a certain percentage of deposits collected. With this system, banks have the ability to create other types of fiat money, namely bank money (demand deposits, including electronic money). This also happens when banks give loans. Thus the benefits for banks through this system are given the power to create new money. Whereas in the Islamic economic system there is a hundred percent reserve banking system, where this system does not provide an opportunity for banks to create new money because all reserves must be deposited with the central bank. The maximum bank can only channel financing up to the initial deposit. This causes no new purchasing power to be created, thus does not contain elements of usury and no party is harmed.

Islamic Monetary Policy Strategy

The Islamic monetary strategy is the abolition of interest rates and the obligation to pay taxes on idle productive costs, thus eliminating the initiative of people to hold idle money so as to encourage people to do:¹⁵

- a. *Qard* (lend assets to others).
- b. Sales (*Muajjal*)
- c. *Muḍārabah*.

The fund owners will invest their funds in activities that provide the greatest return (actual return), so the higher the demand for money for investment in the real sector or the greater the need for a stock of funds for investment, the expected profit rate will decrease. Because the magnitude of the actual return level does not fluctuate like interest rates, it will make the demand for money more stable.

The monetary policy strategy must be implemented at a technical level, in this case, Islamic monetary instruments, as well as Islamic monetary strategies that prohibit the use of interest, then Islamic monetary instruments are also the same. Explanation of monetary

¹³ Hendri Tanjung, "Kritik Ekonomi Konvensional Dan Solusi Ekonomi Islam. Universitas Ibn Khaldun," 2015, <http://oaji.net/articles/2015/1163-1425031554.pdf>.

¹⁴ Tanjung.

¹⁵ Adiwarmman Azwar Karim, *Ekonomi Makro Islami*, 3rd ed. (Jakarta: Rajagrafindo Persada, 2007).

instruments in Islam will be explained based on three schools, namely the *Iqtiṣādunā* school, the mainstream school and alternative schools. the differences between the three schools can be caused by different periods of times, while the instruments used from the three schools are:¹⁶

- **Mazhab *Iqtiṣāduna***

In the early days of Islam, it could be said that there was no need for a monetary policy due to the almost absence of a banking system and the minimum use of money. So there is almost no reason to change the money supply and demand because credit at that time only applies between traders. The monetary instrument used is Promissory Notes or Bill Of Exchange, this letter can be used as a loan to get fresh funds, but the letter cannot be used for credit purposes. Creditors can sell the letter but the debtor cannot sell the letter. That is why there is no market for buying and selling negotiable instruments, speculation and the use of the money market becomes non-existent. So the credit system does not create money.¹⁷

- **Mazhab Mainstream**

The purpose of monetary policy is to maximize existing resources so that they can be allocated to productive economic activities. Therefore this school designs policy instruments aimed at influencing the size of the demand for money (Md) so that it can be allocated to increasing the productivity of the economy. Therefore in the Islamic economy, there is no demand for money (Md) for speculation.¹⁸

The motive for money demand (Md) in Islam is twofold, the motive of the transaction (transaction motive) and the precautionary motive, the more money is idle, the greater the demand for money (Mdprec). While the higher the tax imposed on money is idle, inversely proportional to the demand for money just in case. Dues Of Idle Fund is a policy instrument that is imposed on all productive assets that are idle.

If the demand for money increases (Mdprec) increases, the effort that can be made by the monetary authority to return to the equilibrium point is by increasing the dues of idle funds. The higher the dues of idle funds imposed on idle money, will cause people to be reluctant to save the idle money. So that people will prefer to allocate idle money to productive economic sectors.¹⁹

- **Mazhab Alternatif**

The monetary system recommended by this third school is the Syuratiq Process, which is where a policy taken by the monetary authority is based on previous deliberations with the real sector. So the policy adopted in the monetary instrument is integration and adjustment between the monetary sector and the real sector. This school says that the balance that occurs in the monetary sector is the derivation of the balance that occurs in the real sector. This means that if there is an increase in activities in the real sector, with the increase of Aggregate Demand (AD), the monetary authority must also increase the money supply (Money Supply / MS).²⁰

In other words, the monetary sector should not leave the real sector, there must be harmonization between the two sectors, what happens when the monetary sector leaves the real sector (a situation in which the money supply in society far exceeds the need for economic activity) is nothing but inflation . If inflation occurs especially high, then there will be

¹⁶ Aan Nasrullah, "Sistem Moneter Islam: Menuju Kesejahteraan Hakiki," *Sekolah Tinggi Agama Islam Miftahul 'Ula (Staim) Nganjuk*, n.d., <http://oaji.net/Articles/2017/1163-1502161295.Pdf>.

¹⁷ Karim, *Ekonomi Makro Islami*.

¹⁸ Karim.

¹⁹ Karim.

²⁰ Karim.

disadvantaged parties, for consumers whose income is fixed, if inflation occurs it will certainly reduce purchasing power (Purchasing Power Parity), then at the macro level there will be a decrease in Aggregate Demand (AD), this broad impact on the sluggish economy and national income will also be affected negatively. And in the end, people's welfare will also be further away from the achievement.²¹

From the information above, we can see that the Islamic monetary system which was broken down to monetary instruments showed consistency in improving the welfare of the community in general, was not discriminatory or one party was benefited. In monetary Islam, money is expected to revolve in all walks of life. The aim is none other than so that all groups can carry out economic activities so that public welfare can be achieved.

Islamic Economic Instruments

There are at least 5 values of Islamic economic instruments that can be integrated into the economic system, namely zakat, waqf, social security, the justice system in resolving economic disputes and Islamic financial institutions²². Next is his presentation:

Zakat

Integration of zakat into taxes, we all need to struggle. We all hope that zakat can be done as a tax deduction, not as a deduction from the tax object. If zakat can be applied as a tax deduction, then the source of state revenues will be extraordinarily powerful

Waqf

The integration of waqf into the Indonesian economy has begun with the establishment of the Indonesian Waqf Agency (BWI). It is expected that BWI can manage waqf assets which are of such great potential for the welfare of the ummah.

Social Security

According to the author, there is an urgent matter carried out by the government related to social security, namely the urgency of implementing farmer insurance. The government must be able to protect farmers from crop failure. This, besides motivating farmers, is also a strategy to achieve food self-sufficiency.

Judicial System in resolving economic disputes

The integration of sharia economic systems into existing legal systems can occur in the court world. Disputes involving sharia financial institutions are settled in religious courts.

Islamic Financial Institutions (LKS)

In an effort to develop Islamic financial institutions, the Indonesian Ulema Council (MUI) has a strong enough contribution. As a commitment to maintain the economic values of sharia financial institutions, the MUI forms a National Sharia Council (DSN).

Syariah banking

In its operations, the Islamic banking system collects public funds in the form of wadiah demand deposits, mudharabah deposits, and mudharabah savings deposits. The product of channeling funds to the public can be done with 6 things: financing mudharabah, murabahah, Bai 'Bithsaman a'jil, qardhul Hasan, ijarah and musyarakah participation.

²¹ Karim.

²² Tanjung, "Kritik Ekonomi Konvensional Dan Solusi Ekonomi Islam. Universitas Ibn Khaldun."

Sharia Insurance

If conventional insurance contains elements of Gharar, maisir, and Riba, then Islamic insurance is clean of such elements. The principle of sharia insurance is Qs Yusuf, 12: verses 43-49. There are 10 principles of sharia insurance, namely: the principle of tauhid, justice, help, cooperation, trust, mutual pleasure, avoiding usury, avoidance, avoid gharar and avoid risywah.

Islamic Pawnshop

Sharia pawnshops began operating in Indonesia in 2003. Before it was established, a comparative study was held in Malaysia. Data in 2008, there were 3.7% of sharia pawnshops customers out of 19 million total pawnshops. The community's responsiveness to sharia pawnshops is good, including the rapid process, only 10-15 minutes.²³

IV. Conclusion

After conducting the discussion above it can be concluded that the law of usury in Alqur'an and hadith is expressly stated as haram. As for the interest of the bank based on the opinions of the leaders, it was shown that the majority of Muslim scholars and scholars stated that bank interest was the same as usury, so bank interest law was illegitimate. But there are also those who consider that bank interest is different from usury interest, so bank interest is okay, according to several Middle Eastern scholars supported by secular economic experts.

As for the impact of interest or usury on the economy, among them will cause uneven income, hamper the economy, economic inequality between the rich and the poor, and even other impacts can cause a monetary crisis.

From the presentation of the Islamic monetary system, some conclusions can be drawn as follows: First, the objectives of the Islamic monetary system include: full employment opportunities and optimal economic growth rates, socio-economic justice and equitable distribution of wealth and income, stability of currency exchange rates, mobilizing investment and savings for economic development and providing all forms of effective services normally expected from the banking system.

Second, the goal - Islamic monetary strategy is to abolish interest rates and obligation to pay taxes on idle productive costs, so that it will eliminate people's initiative to hold idle money so as to encourage people to do: Qard (lending assets to others), Muajjal Sales, and Muḍārabah.

Third, the instrument of Islamic monetary policy is divided into three schools based on the times and needs of the people at that time. The instrument introduced by the iqtisāduna school is Promissory Notes or Bill Of Exchange, a kind of letter to get fresh funds. The second school is the mainstream school instrument used is the Dues of Idle Fund, a policy instrument imposed on all productive assets that are idle. The third school of the alternative monetary system advocated by this third school is the Syuratiq Process which is where a policy taken by the monetary authority is based on previous deliberations with the real sector.

The main characteristic of the Islamic monetary system is that in its policy instruments it does not abandon Islamic economic ideology and does not abandon the need for economic returns for economic actors, namely profit sharing. Which is then expected to meet human needs for material and immateriality, so that ultimate welfare can be achieved.

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