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Perceptions of Selected Representatives towards the Impacts of Interest on the Different Segments of Economy and Society: A Fieldwork Study on Pakistan

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Abstract

Present study examines the perceptions of selected representatives of Pakistani society towards the impact of interest on economical, political, societal and ethical affairs of country. This study contains an opinion survey of 30 representatives, 5 each from Religious scholars, Islamic bank managers, conventional bank managers, modern economists, political & societal representatives, and common peoples. This survey was undertaken as a fieldwork during the months of October/November 2005 and February/March of 2006. Although, all representatives were Muslims yet their opinions regarding effects of interest on economy and society were notably different. Majority of the Islamic scholars and religious leaders were of the opinion that interest has adverse impacts on economy and society. On the other hand, majority of political representatives and modern economists opined that interest has no severe effects on the economy and society. The most notable result of this endeavor is the fact that despite the difference in approach and interpretations there is broad unanimity on the exploitative role of interest in all of our respondents. All of our respondents were agreed that interest has negative effects on the morals attitude and ethical affairs of peoples.

1. Introduction

Present study is one of the series towards the understanding of Islamic Economics, especially Islamic Banking and Finance. This study deals with the dilemma of interest, which is perhaps, the most crucial problem related to the Islamic economics.

Islam is not only a religion to believe in specific aspect only; it is a complete code of life. It

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provides guideline in spiritual as well as worldly affairs of believers. Interest in all its forms is peremptorily prohibited in all divine religions especially in Islam.¹ A Muslim living in an Islamic territory cannot enter into interest-bearing money dealings.

In Pakistan, where religion is a basic element of every day life, the government has implemented legislative measures to eliminate interest from Banking and Financial institutions. These measures could not achieve their ultimate goals due to several reasons.² Present study is designed to evaluate the perceptions of different representatives of Pakistani society about the impacts of interest on the affairs of the individuals and society.

2. Objective of the study

The objectives of this study were threefold. Firstly, we made a comparative analysis of the replies of different representative on the subject to formulate strategic policy/acumen for the elimination of interest from the economy. Secondly, we made an attempt to evaluate the degree of religious (Islam) influence in the daily life of peoples in Pakistani society. Thirdly, we tried to sort out the common agreed points of different representative regarding the impact of interest.

3. Hypothesis of the study

Our hypothesis in this study is “Religion (especially Islam) has great influence on the behavior of peoples both in individual life (private matters) and collective life (society)”.

4. Methodology of the survey

The sample size of the study was limited to a total number of 30 representatives. These representatives include Modern economists, Islamic economists, Managers (or equivalent) at Islamic and conventional banks, Political/societal representatives and common peoples. This survey was undertaken during the month of October/November 2005. However, researcher could not collect all samples in this trip, hence some samples of this survey were obtained in the month of March 2006. The study is based on both filling of pre-designed questionnaire and direct interview of scholars. The opinions obtained were arranged on 3-point liker scales i.e.,

¹ Mehboob ul Hassan, “An Explanation of Rationale Behind the Prohibition of Riba in the Doctrines of three Major Religions: With special Reference to Islam”, OIKONOMIKA Vol. 42 No. 2 Nov. 2005: 73-87

² For detail discussion on this topic, see page151-173 writer’s Ph.D. dissertation submitted to Nagoya City University in 2007.

“disagree”, “neutral” and “agree” for easier understanding.

5. Literature review and previous studies on the topic

After scrutinizing the works on interest we knew that the well-known scholars namely Dr. M. Uzair, M. Umar Chapra, Anwar Iqbal Qureshi and Khurshid Ahmed³ explained the various adverse effects of interest on the economy and society. The representatives we interviewed also had the similar points of views.

Table 1. Statements and replies of the representatives

Statements	Respondents Group	Disagree	Neutral	Agree
1. Interest results in capital and economic growth retardation (detainment)	Islamic Scholars	-	1	4
	Islamic Bank Manager	1	1	3
	Convent. Bank Manager	-	3	2
	Modern Economists	2	3	-
	Societal Representatives	1	1	3
	Common Peoples	-	4	1
2. Interest results in keeping capital Idle (indolent)	Islamic Scholars	-	1	4
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	-	2	3
	Modern Economists	-	1	4
	Societal Representatives	-	-	5
	Common Peoples	-	-	5
3. Interest diverts investments towards unproductive business	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	1	2
	Modern Economists	1	3	1
	Societal Representatives	1	2	2
	Common Peoples	-	4	1
4. Interest retards sanctioning of banking funds	Islamic Scholars	-	1	4
	Islamic Bank Manager	-	2	3
	Convent. Bank Manager	1	1	3
	Modern Economists	2	1	2
	Societal Representatives	2	1	2
	Common Peoples	2	2	1

³ 1978 (2001): 82, 1985: 117, 1991: 166, 1979: 6 respectively

5. The rate of investments in risky business declines because of Interest	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	1	1	3
	Modern Economists	2	-	3
	Societal Representatives	-	5	-
	Common Peoples	1	1	3
6. Interest retards the rate of investment	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	1	2
	Modern Economists	2	1	2
	Societal Representative	-	1	4
	Common Peoples	-	1	4
7. The prices of goods & Commodities increase because of interest	Islamic Scholars	-	1	4
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	2	1
	Modern Economists	3	2	-
	Societal Representative	-	-	5
	Common People	-	1	4
8. Interest results in purchasing power decline	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	2	1
	Modern Economists	3	2	-
	Societal Representative	-	-	5
	Common People	-	-	5
9. Interest compels the producers to destroy their surplus manufacturing	Islamic Scholars	-	3	2
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	3	-
	Modern Economists	3	2	-
	Societal Representative	-	3	2
	Common People	-	-	5
10. Interest enhances the unemployment and reduces the wage rate	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	2	1
	Modern Economists	3	2	-
	Societal Representative	-	3	2
	Common People	-	1	4
11. Interest enhance the economic disparity in the society	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	2	2	1
	Modern Economists	2	3	-
	Societal Representative	-	1	4
	Common People	-	1	4

12. Interest helps creating instability in the society and prolongs the business cycle stagnation.	Islamic Scholars	-	-	5
	Islamic Bank Manager	-	-	5
	Convent. Bank Manager	3	1	1
	Modern Economists	-	3	2
	Societal Representatives	1	1	3
	Common Peoples	2	2	1
13. Interest gives rise to the speculative business	Islamic Scholars	-	-	5
	Islamic Bank Managers	-	1	4
	Convent. Bank Manager	2	2	1
	Modern Economists	2	1	2
	Societal Representatives	-	3	2
	Common Peoples	1	3	1
14. Interest helps destroy moral of the society	Islamic Scholars	-	-	5
	Islamic Bank Managers	-	-	5
	Convent. Bank Manager	2	3	-
	Modern Economists	2	3	-
	Societal Representatives	-	-	5
	Common Peoples	1	2	2
15. Interest is one of the causes of political and social unrest	Islamic Scholars	-	3	2
	Islamic Bank Managers	-	1	4
	Convent. Bank Manager	2	1	2
	Modern Economists	1	2	2
	Societal Representatives	-	-	5
	Common Peoples	-	-	5
16. Interest compels the government to resort to borrow at the time of emergency	Islamic Scholars	-	2	3
	Islamic Bank Managers	-	1	4
	Convent. Bank Managers	-	1	4
	Modern Economists	1	3	1
	Societal Representatives	-	1	4
	Common Peoples	-	-	5
17. Foreign debt increases because of interest	Islamic Scholars	-	-	5
	Islamic Bank Managers	-	-	5
	Convent. Bank Managers	3	2	-
	Modern Economists	4	1	-
	Societal Representatives	-	4	1
	Common Peoples	-	5	-

6. Responses of the statements

Table 1 indicates the responses of each of the 17 statements. It also shows the frequency of responses to the elements of the 3-point scale for each of the questions. It is assumed that

‘Agreed’ are positive opinions to the statements and ‘Disagree’ are negative opinion to the statements, while neutral responses are neither positive nor negative.

1. Interest results in capital and economic growth retardation (detainment)?

The analysis of the table portrays that 80% of the Islamic scholars 60% of the Islamic bankers, 40% of the conventional bank managers, 60% of the societal representatives and 20% of the common citizens expressed that interest results in capital and economic retardation. The total number of positive replies were 13 out of 30 total samples, while, 4 out of 30 samples were in negative response. These outcomes show an obvious result i.e., majority of respondents who have knowledge about Islamic economics or have religious background favored the statement and people without religious backgrounds did not favored this statement as compared to religious or Islamic economist or Islamic bank manager group.

2. Interest results in keeping capital idle (indolent)

80% of Islamic scholars, 100% of Islamic bankers, 60% of conventional bank managers, 80% of modern economists, 100% of societal representatives and 100% of common peoples were of the favor, but rest were against the statement. The results of this statement also favor our hypothesis similar to the previous statement.

3. Interest diverts investments towards unproductive business

100% Islamic scholars and Islamic bank managers, 40% conventional bank managers, 20% modern economists, 40% and 20% of societal representatives and common citizens favored the statement and opined that interest diverts investments towards unproductive businesses. While the responses of rest representatives were in negative sense or did not favored our statement.

4. Interest retards sanctioning of banking funds

Again 80% of Islamic Scholars, 60% of Islamic Bank Managers, 60% of Conventional Bank managers, 40% of modern economists, 40% of societal representative and 20% of common citizens were of the opinion that interest retards sanctioning of banking funds. And the rest were against to this statement.

5. Rate of investments in risky business declines because of Interest

All of Islamic scholars and Islamic bank managers, 60% of Conventional bank mangers, modern economists and common peoples were in favor; while the remaining were against this statement.

6. Rate of investment retard because of interest

All of Islamic Scholars and Islamic Bankers, 40% of Conventional bank managers and modern economists and 80% of the societal representatives and common citizens were of the opinion that interest retards the rate of investment in general. The rest were against the statement.

7. Prices of goods & commodities increase because of interest

80% of Islamic scholars, 100% of Islamic Bank managers, 20% of conventional bank managers, 100% of societal representatives and 80% of common peoples agreed to this statement, hence favored our hypothesis. And the rest were against this statement.

8. Purchasing power of consumers decline due to interest

Again, with the exception of modern economists and 80% of conventional bank managers, all respondents were in favor that interest declines the purchasing power of consumers.

9. Interest compels the producers to destroy their surplus manufacturing

40% of Islamic scholars, 100% of Islamic bank managers and common citizens, and 40% of societal representatives were of the opinion that interest compels the producers to destroy their surplus manufactured goods; while the remaining of conventional bankers and modern economists were not in favor of the statement.

10. Interest enhances the unemployment and reduces the wage rate

The rate of unemployment increase and wages rate decline due to interest, were opined in positive by all of Islamic scholars and bankers, 40% societal representatives and 80% common peoples. The rest were against the statement.

11. Interest enhance the economic disparity in the society

All of Islamic scholars and Islamic bank managers, 20% of conventional bank managers, 80% of common peoples and societal representatives were of the opinion that interest is main cause of increasing disparity in the society.

12. Interest helps creating instability in the society and prolongs the business cycle stagnation.

100% Islamic scholars and Islamic bank managers held the statement that interest helps creating instability in society, followed by 20, 40 and 60% conventional bank manager, societal representatives and common peoples respectively. The remaining respondents were not agreed with this statement.

13. Interest gives rise to the speculative businesses

100% of Islamic scholars, 80% of Islamic bank managers, 20% conventional bank managers and 40 % societal representative and modern economists, positively replied that interest gives rise to the speculative business. While positive replies from common peoples were 20% only.

14. Interest helps destroy moral of the society

Again 100% of Islamic scholars, Islamic bank managers and societal representatives respectively, and 40% of common peoples replied positively that interest helps destroy moral of the society, while 100% of conventional bank managers and modern economists denied the

statement.

15. Interest is one of the causes of political and social unrest

The statement that interest is one the cause of political and social unrest has been answered in positive by all common peoples, 80% Islamic bank managers, and 40% of conventional bank managers, Islamic scholars, and modern economists.

16. Interest compels the government to resort to borrow at the time of emergency

The interest compels the government to resort to loan at the time of emergency was opined in positively by 100% common peoples, 80% societal representatives, Islamic bank managers and conventional bank managers, 20% of modern economists, and 60% of Islamic scholars.

17. Interest is one of cause of foreign debt increase?

Finally, the statement that foreign debt increases because of interest answered in positive by all of Islamic scholars and Islamic bankers, 20% of societal representatives. While the rest of societal representatives, all of conventional bank mangers, and modern economists replied in against the statement.

7. Specific impacts of the interest on the Society and Economy

The opinions of theses representatives can be summarized under following clauses: (A) Economic impacts of interest; (B) Impacts on economic stability and society (C) Impacts on the political affairs of the society.

(A) Economic impacts of interest

Impacts on capital formation and investment

Interest in all its forms may impose reverse impact on the capital formation and investment of the economy in the following ways:

1. Interest not only retards capital formation but also reduces the rate of capital growth. It is the rate of interest, which sets limits to the rate of growth of real capital.
2. Interest encourages keeping capital idle. If there is no interest, the capitalists will be bound to invest their funds for earning profit.
3. Interest reduces the rate of investment especially in risky capital-intensive projects: because there is inverse relationship between rate of interest and rate of such investment. The more the rate of interest the less the rate of investment in capital-intensive investment and vice-versa.
4. Interest leads investments to unproductive speculative sector. This is one of the main reasons of low investment for productive purpose in interest-based economies. The banks

and financial institutions feel encourage to invest their funds more and more in government securities, bonds and bills and other speculative business in order to get fixed, risk-free and certain income. As a result investment in productive sector tends to be reduced due to shortage of required capital.

5. Interest reduces the rate of investment in social welfare projects; since, usually, such type of investment does not lead to attractive profit. And some times even for government, ignoring the rate of interest, it is not possible to make investment in such welfare projects.
6. Interest encourages the idleness among the depositors; since it is obtained without any risk and labor on the part of depositors.
7. Interest tends the capitalists to embraces towards exploitative behavior and attitude. In words of Dr. M. Uzair;

“...the lions’ share of capital of economy remains under the control of capitalists and bankers. They do not at all consider the normal demand and proper necessity of the economy while granting loans”⁴

Impacts of interest on production

Interest may impose adverse impacts on the production system of an economy in the following ways:

- 1) Interest tends to reduce the rate of production since it retards capital formation. In the interest-based economy the major portion of the capital is invested in unproductive sectors of the economy while another portion of the capital is kept idle. As the result, requisite amount of capital is not available for investment in production.
- 2) Interest tends to increase the price of commodities and services. When the manufacturers make investment of loan amount (obtained on interest) in production, they add the interest amount with their production cost. As a result, the cost of production of the commodities increases equal or more to the amount of interest. The manufacturers then fix up the selling price of their commodities on the basis of cost plus profit and interest.
- 3) Interest tends to reduce the purchasing power of the people. This is so because the purchasers are to pay more prices of their commodities because of inclusion of interest amount in the cost price. As a result, the purchasers are to spend extra amount for buying their commodities. This tends to reduce their purchasing power. This reduced or low purchasing power tends to reduce the demand of the commodities because of low purchasing power of the people. The low purchasing power reduces the demand of the commodities.

⁴ Mohammad Uzair, 1978 (2000): 184

(B) Impacts of interest on the economic stability and society

Economic stability is pre-requisite for the development of all countries, but interest imposes adverse impacts on the economic stability of a country mainly in following ways:

1. Interest helps creating inflation in an economy. Interest through increasing the prices of commodities tends to create inflation. High rate of interest on loans and unproductive uses of loan are responsible for inflation. In interest-based banking system the created credit of commercial banks are also responsible for inflation.
2. Interest helps creating business cycles in an economy. In the interest-based economy, interest helps creation of unstable and uncertain condition of economy through loan and depressions in the cyclical order. It is the interest, which is the main cause of revolving economy of a country around loan and depression.⁵
3. Interest tends to create instability in the economy. The rate of interest does not remain fixed; rather it varies very frequently. Whenever there exist boom in the economy, the demand of capital increases and along with this the rate of interest increases. On the other hand, whenever there is depression, the demand of capital decreases associated with the decrease of in the rate of interest. Such unstable rate of interest leads to unstable situations of the whole economy. M. Umar Chapra, an Islamic economist is of the opinion that interest is the main element of economic instability.
4. The rate of interest tends to make the monetary policy of a country ineffective.⁶ The central bank of the country fails to regulate the interest rate if it tries to regulate the money circulation. The bank can control the circulation of money either control the rate of interest or the stock of money; but it is impossible for the bank to regulate both in such a balance manner that inflation is checked without hurting investment.⁷

(C) Impacts of interest on the political affairs of society

Interest may adversely affect the political condition of a country in the following ways:

1. Interest helps creating political unrest in the country.
2. Interest creates obstruction to the government for social welfare development.
3. Interest compels the government to take loans at the time of emergency like wars, floods, cyclones etc., because in the presence of interest-bearing loans nobody will want to lend his/her money without interest at the time of emergency.

⁵ Umar Chapra 1985: 117

⁶ Ibid: 119

⁷ Ibid: 120

8. Conclusion

The principal reason behind the harsh tone of our religious scholars, Islamic bank managers and societal representatives responses is, perhaps, religious background. All divine religions, especially. Islam do not allow the injustice perpetuated to the financier being assured of a predetermined return without sharing in practical business work or sharing in the business risk, while the entrepreneur, on the other hand, in spite of his management and hard work, is not assured of any predetermined return. Islam wishes to establish justice between the money holder and the entrepreneur. The Qur'anic prohibition of Riba aims at eliminating exploitation, oppression, and inequality, and to promote a just economic system based on profit and loss sharing basis.

Due to the religious influence, peoples wish to establish an economic system where all kinds of injustice are eliminated and all forms of exploitation are controlled.

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