Islamic Banking and Finance in India and Sri Lanka

M. Irfan Shah\(^1\)
Dr. Showkat Hussain\(^2\)

Abstract
Having witnessed a series of developmental stages Islamic banking and finance has shown substantial growth since its inception in the corporate sector during 1970s and has turned into a globally recognized, significant and sizeable finance industry operating, throughout East and West. From the academic point of view “Islamic Economics, Banking and Finance” has amply received attention even from the world’s renowned academic institutions/Universities. Whereas the varied and wide-ranging aspects of Islamic Banking and Finance in the business sector of Middle-East and Western countries have been highly deliberated over, there is paucity of the same with regards to Muslim minority countries particularly of South Asian region. This paper, in this direction, is an endeavor to highlight Islamic banking and finance development in the business sector of India and Sri Lanka, as being the countries, in South-Asia, with a considerable size of Muslim populace as minorities.

Indonesia and Sri Lanka Ahead Towards Islamic Banking and Finance:
The application of the theoretical framework of Islamic economics, banking and finance on a significant level was witnessed in the final quarter of the 20th century. This was to gear up the material developments (within the bounds of Islamic canon law), which were manifested mainly in four directions, as given by Khurshid Ahmed (Ahmed, 2000)\(^1\). Firstly professional economists and bankers pondered over the foundations laid down by the Ulama, Fuqaha and intellectuals of early period and managed to put up theoretical framework of Islamic economics. Secondly, establishment of Riba (interest)-free financial investment avenues and institutions were taken into consideration at an academic level. Thirdly universities, research institutes, international professional organizations (including some western institutes)

(Endnotes)
2. Certain Islamic Financial Institutions that came into being to support growth and development of the Islamic financial industry are: Islamic Development Bank Group (IDB Group); Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI); Islamic Financial Services Board (IFSB); International Islamic Financial Market (IIFM); International Islamic Rating Agency (IIRA); International Islamic Centre for Reconciliation and Commercial Arbitration; General Council of Islamic Banks and Financial Institutions (GCIBFI).
came into existence and started academic training and research programs in different areas of Islamic economics, banking and finance, thus broadening the horizons of Riba (interest) – free system. And finally initiatives were taken at state level to switch over from Riba to Riba –free banking and financial system (Ahmed, 2000). The fact thus established is that Islamic economics and finance made its appearance primarily in academia and got successively demonstrated in corporate sector in the form of Islamic banking and financial institutions. Over the last few decades, the Islamic banking and financial industry, which made its ceremonial appearance in the 1970s, has experienced gigantic global growth owing to some reasons which include:

- The relocation of massive Muslim funds from conventional banks and financial institutions to Islamic institutions following September 11 incident.
- The industry’s market niche in Islamic products and services with a captive Muslim market base.
- The inherent risk managing character of many Islamic products and services and lastly;
- The comparative stability of the industry even in times of global financial crisis attributed to its ample liquidity, safe debts, and high-profit margins.

Among various factors responsible for the significant increase in development of Islamic Banking and Finance (IBF) industry, the main factor is the profound and divinely ordained principles (prohibitions and encouragements) that govern the operational setup of the industry. Some of these key principles and features are as follows:

**Key Principles governing Islamic Finance**

The prohibition of Riba and permission of trade as enshrined in the Holy Quran [Allah has allowed (profit from) trade (and) prohibited Riba] (Chapter 2: Verse: 275) drive the financial activities in an Islamic economy towards asset backed business and transaction (Ayoub, 2007). Islamic finance encourages active participation of financial institutions and investors in achieving the goals and objectives of an Islamic economy. Moreover, the currency in perspective of stability is backed by underlying assets, which enable the medium of exchange to be a reliable unit of account (Shanmugam, 2000). The inherent risk managing character of many Islamic products and services are also among the key factors of Islamic finance.

---


4. The first official bank operating interest free banking was established in Egypt in 1963 but was closed in 1967 for political reasons. In 1972, the Egyptian government established Nasr Social Bank as an introduction to Islamic banking. Islamic Development Bank-IDB, Jeddah was founded in 1975 and was a financial institution more than merely an Islamic bank. Pakistan was the first Muslim country to introduce an Islamic banking system in 1979, and was followed by Sudan in 1982 and then Iran in 1984.

5. Ai, Marilyn Ong Siew Corporate Governance In Islamic Banking and financial Institutions: Islamization Trends and Issues, Faculty of Economics and Business, University Malaysia Sarawak-UNIMAS Working Paper Series No.1008, August 2010.
economy and merges the ethical teachings of Islam with finance to encourage socio-economic justice in a society. The Islamic concept of Haram (unlawful), bars any kind of trading through unethical, unjust and immoral ways, including trade of alcoholic beverages, gambling, pork and pornography (Shanmugam and Zahari, 2009).

In view of above descriptions regarding Islamic financial set up, the five key principles that govern Islamic finance are as follows.

Avoiding interest (Riba)

The implications of the verses of the holy Quran like 2:275-279 and relevant Traditions (Ahadith) lead the Islamic jurists (Fuquha) and Shari‘ah scholars (Ulama) to develop the criteria that could serve as fundamental concept of the Islamic theory of economics and finance. The most important feature of that theory is avoiding interest or any extra return derived on a loan/debt (Riba)(Ayoub, 2007) by which Islam seeks to foster an environment based on fairness and justice. Being a sure gain to the lender regardless any possibility of loss as well as a reward in return for no work, Riba innately possesses the exploitative and the unproductive measures. This leads to inflation and unemployment and restrain the social and infrastructural developments of a nation (Shanmugam and Zahari, 2009).

Avoiding Gharrar

Gharrar is frequently translated as “Deception”, “excessive risk” or “excessive uncertainty” (Shanmugam and Zahari, 2009). Gharrar is also involved, if there is a lack of adequate value-relevant information (Jahl) or there is inadequacy and in accuracy of any vital information leading to uncertainty or exploitation of any of the parties. Islamic banks are barred from any such kind of trade activity which involves Gharrar (Mansuri, 2007). Trading in Derivatives (derivative is a contract or security that derives its value from that of an underlying asset (as another security) or from the value

8. Ayoub, op.cit, p-74.
10. Ibid., p-9.
of a rate (as of interest or currency exchange) or index of asset value (as a stock index) involves Gharar and therefore is a very grey area for Islamic financial system (Ayoub, 2007)\textsuperscript{12}. 

**Profit-Loss Sharing (PLS) or Risk-Reward Sharing:** Shari‘ah prohibits Muslims from earning income by charging interest (Riba) but permits income generation through the sharing of Risks and Rewards (PLS-e.g:Mudharabah) between the parties who enter into a partnership rather than a creditor-debtor relationship (Shanmugam and Zahari, 2009)\textsuperscript{13}. The profit and loss sharing concept entails a direct concern with regard to the profitability of the physical investment on the part of creditor (Islamic bank) (Hassan and Lewis, 2007)\textsuperscript{14}.

**Shari‘ah-Advisory board or Shari‘ah-Approval Activities**

To ensure that all products and services are in accordance with Shari‘ah, each Islamic Bank has an independent Shari‘ah Advisory Board or Shari‘ah Supervisory Board mainly comprised of Shari‘ah scholars and experts (Shanmugam and Zahari, 2009)\textsuperscript{15}. Due to the implementation of Shari‘ah Advisory Boards in the Islamic Banks, the wheel of evolution of Islamic legal system has resurrected. These advisory boards enable Shari‘ah scholars to become familiar with the changing market situation and on the other hand through their exercise of Istinbat or Ijihad contributes to the development of Islamic jurisprudence (Usmani, 2010)\textsuperscript{16}.

**Prohibition of Maysir/Qimar (Games of Chance)**

The words Maysir and Qimar are used in Arabic language identically. Maysir refers to get something too easily or getting a profit without working for it (Mansuri, 2007)\textsuperscript{17}. Qimar means the game of chance—means that one gains at the cost of others. A person puts his wealth at the stake wherein the amount of money at risk might bring huge sums of money or might be lost. While the word used in the Holy Quran for prohibition of Gambling and wagering is Maysir—(Chapter: 2, Verse: 219 and 5:90-91):

---

\textsuperscript{12} Ayoub, op.cit, p-75.

\textsuperscript{13} Shanmugam and Zahari, op.cit., p-8.


\textsuperscript{15} Shanmugam and Zahari, op.cit., p-8.

\textsuperscript{16} Usmani, Mohammad Taqi An Introduction to Islamic Finance, Adam Publishers and Distributors, New-Delhi, 2010, p-238.

\textsuperscript{17} Mansuri, Mohammad Tahir Islamic Law of Contracts and Business Transactions, Adam publishers and distributors Delhi, 2007, p-8.
In October 2011 the Central Bank of Sri Lanka granted a full commercial license to material development, determines a set of features intrinsically present in Islamic finance. Takaful was perceived as the Islamic alternative to conventional insurance. Owing to Islamic banking and finance in Corporate Sector: An Overview of India (collusion to bid up prices), Islamic financial set-up denounces every kind of market malpractice. Such philosophy should be of equity and reward sharing and not of a simple debtor-creditor relationship unlike the interest-based venture (Ahmad, 2007).

**Features of Islamic Finance**

It was only post 1970s of the 20th century that the term “interest-free banking” was used to describe an alternative system to the conventional interest-based system. However, more general term is “Islamic Banking”, which not only signifies to avoid interest based transactions but also to avoid Gharar (uncertainty) and other unscrupulous/corrupt practices prohibited in Islamic Shari’ah. It aims to participate in achieving the goals and objectives of Islamic economical framework (Ayoub, 2007). The concern for establishment of socio-economic justice together with the moral and material development, determines a set of features intrinsically present in Islamic economic and financial system. Among its various features of following are some major or distinguishing features pursued by this novel system:-

**Equity- Sharing**

Islamic finance regulates on the basis of Equity-sharing and risk-taking and operates on the principle of variable return, based on actual productivity and the performance of the projects or business ventures, whether specific or general, individual or institutional, private or public. The economic merging may be of variant types, but the philosophy should be of equity and reward sharing and not of a simple debtor-creditor relationship unlike the interest-based venture (Ahmad, 2007).

The, sharing of profit and loss, mechanism in the Islamic finance establishes a close relationship between bank and entrepreneur and thus enhances the economic development (Shanmugam and Zahari, 2009). Some of the world’s renowned scholars, like Hyman Minsky, Henry Simons, Charles Kindle Berger, and Kenneth Maysir, in academia and got successively demonstrated in corporate sector in the form of Islamic Financial Institutions (IFIs) are responsible for mobilizing funds for its promotion. The Sri Lankan economy is considered as one of the emerging hubs in South Asia, with financial sector being its main contributor and fastest growing field. Owing to the nascent business sector with a resilient potential of sustenance even in the severe international financial crisis of 2008, the Islamic economic system, with financial sector at the helm, is expected to be recognized as a mini Islamic hub of Asia. The expected rapid growth is expected to be recognized as a mini Islamic hub of Asia. The expected rapid growth of the Islamic financial system in the early 1990s has been attributed to a considerable size of Muslim populace as minorities.

The above assessment of the Islamic Banking and Finance in Corporate Sector, in two South Asian Muslim Minority regions Sri Lanka is the first to facilitate measures to promote training and career development programs related to this field. It also contributes academically to the field of Islamic banking and finance by offering its clients a varied portfolio of Fiqh funds. Islamic banking had been adopted by 75 countries, including the UK, and India.

**References**


19. Ayoub, op.cit, pp-63-64.


Rogoff (Chapra, 1992), have argued that equity based economy would tend to be much more stable than a debt-based economy (Chapra, 1992). The Islamic financial institutions, as such, act as representatives for individuals who:

a. Invest their money in the Islamic financial institutions/banks as share-holders or investment account holders.
b. Have co-operative partnership or borrowing relations with IFIs (Islamic financial institutions).
c. Are employed by the IFI.
d. Have other contractual relation with the Islamic banks and,
e. Have an implicit social contract with IFI (Faroq, 2007).

**Stability in Money Value and Asset-backed Financing**

Being an asset backed system Islamic economic and banking system considers money only a medium of exchange meaning that each unit of money is 100% equal to another unit of the same denomination. Therefore, there is no room for making profit through the exchange of these units inter-se (between them). Profit is generated when something having intrinsic utility (usufruct) is sold for money or when currencies are exchanged, one for another. The profit earned through dealing in money (of the same currency) or the papers representing them is interest, and is strictly prohibited in Islam (Usmani, 2010).

Moreover, the currency in perspective of stability is backed by underlying assets, which enable the medium of exchange to be a reliable unit of account (Shanmugam and Zahari, 2009), having a degree of stability, otherwise, and the economic fundamentals become disturbed. This instability leads the poor to suffer worst, and this must be rectified. Islamic banking operates within the limits that ensure stability in the value of money and an almost inflation free economy (Ahmad, 2000).

**Capital-Entrepreneur relationship**

Unlike capitalistic theory, which regards capital and entrepreneur as two separate factors of production, (the former is entitled to interest, while the latter gets profit),


27. Ahmed, op.cit, pp-57-82.
Islamic law establishes that in a business enterprise every capital contributing person is susceptible to an equivalent share in the actual profit as well as loss depending upon the business venture fate. This way the profits generated by the commercial activities in the society are equitably distributed to all the partners of the enterprise barring the concentration of wealth in the hands of few (Usmani, 2010). Thus the trustworthiness of a person and the viability and usefulness of the project are of primary importance for achieving distributive justice, equity and through diffusion of resources in the society (Ahmad, 2000).

**Equitable Distribution of Financial Resources**

In the conventional interest-based financial system the inequitable allocation of financial resources is recognized widely as Chapra cites Arne Bigsten: “The distribution of capital is even more unequal than that of land” and “the (conventional) banking system tends to reinforce the unequal distribution” (Chapra, 1992). The reason for this unequal distribution is that the conventional financing heavily relies on collateral and there is less consideration to strengthen the project or ultimate use of the finance.

In contrast to this, Islamic financing (services) tend to serve the less fortunate by promoting the equitable distribution of resources (Shanmugam and Zahari, 2009). This equitable distribution of wealth may enable society to employ the pool of entrepreneurial ability from even the poor and middle-class leading to employment and need fulfillment (Chapra, 1992).

**Concerns for Social and Ethical Development**

Islamic Financial Institutions (IFIs) are responsible for mobilizing funds from lawful sources and investing them in lawful ventures. By this they can significantly affect the conduct of the IFIs stakeholders in terms of the ideal Islamic Investment and allocation process (Farooq, 2007). As per Khursheed Ahmed, the Islamic approach is rooted in an ethical framework and represents not only a shift from a debt-based economy to an equity-based economy but a transformation from a pure pecuniary profit-taking to a gainful economy characterized by ethical norms and social commitments (Ahmad, 2000).

---

30. Chapra, op.cit.  
32. Chapra, op.cit.  
33. Farooq, op.cit, pp-31-45.  
34. Ahmed, op.cit, pp-57-82.
Similarly, through the institution of *Zakat*, the social welfare and development of the poor is enhanced. *Zakat* may also be imposed on the initial capital of an Islamic bank, its reserves and profits- this being the significant manifestation of social solidarity in Islam (Shanmugam and Zahari, 2009)^35^.

**Profit and Loss Sharing (PLS)**

Islamic Financial system operates mainly on the basis of Profit and Loss sharing scheme (PLS) instead of the interest based scheme. Unlike the conventional financial system, the majority of clients in Islamic financial system are not savers but holders of Profit and Loss accounts who are supposed to get a large share of investment–return and are gradually changed from savers to investors. Currently, *Mudarabah* and *Musharakah* are two ways through which Islamic financial institutions carry out their transactions of PLS arrangement (Iqbal, 2009)^36^.

**Enhancement in Rate of Employment**

Unemployment being one of the most intractable problems of the world’s most countries, stood at 9.2% in European union in 1999 as compared to 2.0% in 1973. Decline in speculation and wasteful spending^37^ together with the rise in saving and productive investment could act as a savior, but at the same time giving credit without due regard of its end use would not allow this to happen. Islamic financial framework provides a logical solution to this as, by means of careful lending the unproductive and speculative spending will decline and more resources may become available for productive investment and development, leading to higher growth and rise in employment opportunities (Chapra, 1992)^38^. Also, through *Zakat, Infaq, Sadaqat* (charity) and inheritance laws transfer of sufficient purchasing power to the poor is enabled to keep the effective demand high enough for achieving a full employment equilibrium.

**Resource Optimization**

In the Islamic financial organization, the funding is provided only for projects with most favorable return-for-risk forecasts, in addition to execute the criterion of being

---

^35^ Shanmugam and Zahari, op.cit, pp-1-11.

^36^ Iqbal, Jaquir Islamic Finance Management, Global Vision publishing House, Delhi, 2009, pp: 122-123.

^37^ Speculation and wasteful expenses led to unemployment. Over consumption by both, private and public sector has reduced the rate of saving, which resulted in high interest rates leading to lower rates of investment that ultimately joined hands with other socio-economic factors to reduce growth out-put and employment. Thus the basic cause for this lies with the interest based monetary policy.

^38^ Chapra, op.cit.
It was only post 1970s of the 20th century that the term “interest-free banking” was introduced in 2002 with the entry of ATL, which recently created history in Sri Lanka. Features of Islamic Finance

In the current global economic scenario, and Middle-East and Western countries have been highly deliberated over, there is paucity of the varied and wide-ranging aspects of Islamic Banking and Finance in the business sector of South Asian Muslim Minority Countries, Indian and Sri Lanka, reveals that it is a Islamic banking hub for the South Asian region. Islamic finance has the potential to thrive as a fresh and resilient monetary system and the thriving results it has shown,—Islamic banking and financial system. Such malpractices may include Ihtikar (amassing or hoarding with a view to raise prices), Tanajush (collusion to bid up prices), Tasawum (counter-bidding), efforts to forestall (jump in before or prevent) genuine competition by discouraging the sellers to reach the market and middle-man ship by shrewd people to deprive the sellers of the best price available (Khan, 1999). In short, Islamic financial system aims to prescribe a free market based on supply and demand.

Islamic financial set-up denounces every kind of market malpractice. Such malpractices may include Ihtikar (amassing or hoarding with a view to raise prices), Tanajush (collusion to bid up prices), Tasawum (counter-bidding), efforts to forestall (jump in before or prevent) genuine competition by discouraging the sellers to reach the market and middle-man ship by shrewd people to deprive the sellers of the best price available (Khan, 1999). In short, Islamic financial system aims to prescribe a free market based on supply and demand.

The above mentioned major features of Islamic banking and financial system add to uniqueness of its structure and application. Islamic banks’ ability to withstand the global downturn (recession) has accelerated an expansion of Islamic banking and finance around the world to such an extent that the international banks like City Bank, HSBC Bank, Standard Chartered Bank etc., also have already opened Islamic Banking divisions across the world, especially in several West Asian countries, Europe and USA. This has eventually made it worthwhile to study the reasons for their incredible expansion and progress and in this paper the main theme is to study the development of this emerging industry in the South Asian Muslim minority countries like India and Sri Lanka.

Islamic Banking and Finance in Corporate Sector: An Overview of India

In the Asian region, over the last few decades, the Muslim minority countries like India and Sri Lanka have also shown inclination towards the establishment of Islamic banking and financial divisions or interest free, but profit sharing banking. Owing to around 177 million Muslim community living there as minority it is supposed that they will get benefit on the basis of religious conviction and further, Indian industries will grow by getting lot of foreign funds from Gulf region and can use these funds on win-win basis (Pasha, 2012).

In India the Dallah Al-Baraka Group has been allowed to establish Al-Barakat Finance House in Mumbai in 1990 with an authorized capital of Rs 50 million, paid-up

capital of Rs 30 million with Al-Barakat’s share of 51% and rest in domestic Equity. The Al-Barakat Finance House has been given license to operate as an investment bank with the limits set by the Indian Law (Ausaf, 2006 and Ikhtiyaruddin, 1996).42

Indian banks are regulated by “Indian banking Regulation Act. 1949”, the “Reserve bank of India Act 1935”, “the Negotiable instruments Act and Cooperative societies Act. 1866” and none of these admit the possibility of interest free bank. Owing to such constitutional hindrances no Islamic bank as such exists in India. However due to non-permissibility of interest in Islam, the Indian Muslim community made attempts to establish interest free avenues and their attempts can be observed in the following ways:-

1. Interest free credit association;
2. Interest free financial companies; and
3. Investment Funds.

Interest free financial companies
These are registered companies conducting business on the interest free basis and operate in organized markets. Notable among these are: Al-Ameen Islamic Financial and investing corporation (AIFIC); Al-NajibMilli Mutual Benefits Limited; Barakat Financial Company; and Al-Falah Group of Companies.

Al-Ameen Islamic Financial and investing corporation (AIFIC)
A premier Islamic financial institution in India with headquarters in Bangalore and Karnataka, it is the only financial institution in India that functions under the supervision of Shari’ah supervisory Board. It has the Authorized Capital of Rs. 100 million divided into 10 million shares of Rs 10 each. Out of which 52.39000 equity shares of Rs 10 each have been issued, subscribed and paid-up. It has been registered under the “Indian companies Act 1956” and started its operations in 1986 and now it is recognized by the Reserve Bank of India, as a non-banking financial company(Ausaf, 2006)43.

Taqwaa Advisory and Sharia’h Investment Solutions Pvt.Ltd (TASIS)
Founded by a group of finance and investment professionals in 2006, it is an

42. Ahmed, Ausaf “Relevance of Islamic Banking and Finance to Muslim Minority Countries”, in Nadeem Husnain (Editor), Aspects of Islam and Muslim Societies, Serial Publications, Delhi, 2006, p-86; see also Baghsiraj, M. Ghaus Ikhtiyaruddin Islamic Financial Institutions of India: Progress, Problems and Prospectus, Scientific Publishing Center, King Abdul Aziz University, Saudi, Arabia, 1996.

43. Ahmed, Ausafop.cit, p-86.
organization that provides Shari‘ah advisory and investment solutions in India, while operating within the Indian legal framework. It was founded to fill the void of credible organization that would provide guidance and support to individuals and corporate bodies interested in Islamic finance in the country. In 2009 SEBI-Securities and Exchange Board of India offered permission to India’s first Shari‘ah complaint Mutual Fund, advised by TASIS. Also TASIS has become the India’s first institution to be recognized as the member of Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), an international autonomous not-for-profit corporate body that prepares accounting, auditing, governance, ethics and Shari‘ah standards for Islamic financial institutions and the industry.

Recently in 2010, the Bombay Stock Exchange (BSE) launched India’s first index of companies compliant with Islamic financial laws of Shari‘ah, in order to bring the Muslim population of country into the main stream finance sector and also to attract investment from foreign Shari‘ah abiding subsidiaries. The index, is a conglomerate of several Indian market leaders from different sectors like telecommunication, IT services, construction companies etc with the association of Taqwa Advisory and Shari‘ah Investment Solutions (TASIS). It is the first Shari‘ah-stock index created in India based on the strict guidelines of the local Indian Based Shari‘ah Advisory Board.

About 200 interest free credit societies have been established by the Muslim community in India to mobilize financial resources and provide interest-free loans. Among such institutions some notable ones include, Muslim Fund in Najibabad (U.P India) and Bait-un- Nasr Urban Cooperative Society India.

Islamic banking and financial institutions aim to attain socio-economic well being of the masses and establishment of a welfare based society together with wealth generation activities. For this Islamic banking industry needs to easy access for prolific operations and expansion of its network throughout the length and breadth of the country. Also through establishment of the financial dealings with the Muslim dominated nations and by considerably attracting equity finance from the Gulf countries Indian government can achieve diplomatic advantages for infrastructural development.

This way it is obvious that the Islamic financial institutions in India operate in diverse modes, as: credit societies or associations, Islamic financial companies and investment funds. Islamic banking had been adopted by 75 countries, including the UK, and India

46. Ibid.
could no longer afford to stay away from the $1.5-trillion Islamic financial market, which could even help address the country’s huge fiscal deficit. Due to enormous size of Indian Muslim community (an estimated 177 million Muslims in India, the largest Muslim minority population in the world) together with the successful functioning of the Islamic banks elsewhere, it can be expected that the future prospectus of Islamic banking and finance is promising and is expected to emerge on a large scale in India, provided the Indian banking acts mentioned above would be modified.

Islamic Banking and Finance in Sri Lanka: An Overview of the Corporate Sector

The Democratic Socialist Republic of Sri Lanka is an island state and a Unitary Republic comprising a parliament together with nine Provincial Councils. Since its independence from the British in 1948, the country has experienced several changes to the system of governance. Also the country had to bear up a long bloody civil conflict that was only concluded in 2009. Islamic Finance was first introduced to Sri Lanka as early as 1997. The Sri Lankan economy is considered as one of the emerging hubs in Asia, with financial sector being its main contributor and fastest growing field. Owing to some amendments made to the Banking Act No 30 of 1988 in March 2005, by CBSL-Central Bank of Sri Lanka47, adequate flexibility for conventional banks to establish Islamic banking windows and launch Islamic financial products (based on Musharikah and Murabaha), got recognition in Sri Lanka48. Thus it became one of few Muslim-Minority countries to have legislation for the Islamic banking sector. Still it needs to be admitted that, efforts in strategic marketing communication to promote and raise awareness of these products are passing through the juvenile stage. However, Islamic banking operations to be carried out in licensed commercial banks as a regulated and legal activity have been authorized by the Central Bank of Sri Lanka. The Islamic microfinance institutions in rural areas operate beneficently in this field but with a limited service provided to densely Muslim populated areas. With the significant progress of academic sector, the future prospectus of Islamic banking and finance industry in Sri Lanka is expected to show a prolific growth provided the government organizations, monetary authorities and the private sector show their keen interest in working with Islamic banking institutions as the country has the potential to become an Islamic banking hub for the South Asian region49. Islamic finance has the potential to develop the capital markets of Sri Lanka and assist with the development of

47. The Banking and Finance system in Sri Lanka is regulated by the Central Bank of Sri Lanka-CBSL.


infrastructure along with encouraging foreign investment in Sri Lanka\textsuperscript{50}. Among the South Asian Muslim Minority regions Sri Lanka is the first to facilitate measures to accommodate Islamic finance in the country and further promote Shari'ah compliant methods of financing as an alternative to the interest based financial scheme, there by leading even India in this novel area\textsuperscript{51}.

The estimated market value of IBF ‘Islamic Banking and finance’ industry in Sri Lanka is Rs 70 billion to Rs 100 billion. Currently active Islamic financial services providers include the following\textsuperscript{52}:

The Sri Lankan financial market consists of a number of Islamic financial service providers in the form of investment companies, leasing companies and subsidiaries of finance companies. Notable among them are: Amana Investments Ltd and Amana Bank; Ceylinco Islamic Investment Corporation (CIIC); Muslim Commercial Bank (MCB); National Asset Management Limited (NAMAL); First Global Investments Group; and ABC Investments.

**Amana Investments and Amana Bank**

Established in 1997, Amana Investments has been the torchbearer of Sri Lankan Islamic banking and financial services market. Recognized by Colombo Stock Exchange in late 2006, its subsidiary Amana Takaful Ltd (ATL) began operations in June 1999 and is acknowledged as the market leader for Takaful services (commonly perceived as the Islamic alternative to conventional insurance). Takaful was introduced in 2002 with the entry of ATL, which recently created history in Sri Lanka and the Islamic financial services industry worldwide when it was ranked 203rd in the world’s first comprehensive “Top 500 Islamic Financial Institutions” published by The Banker, the global finance magazine of the Financial Times Group, in its November issue. ATL accounted for US$5.55 million worth of Shari’ah compliant assets\textsuperscript{53}.

In October 2011 the Central Bank of Sri Lanka granted a full commercial license to Amana Investments Ltd. to set up Amana Bank, to be the first Islamic bank in Sri Lanka. Headquartered in Colombo, it consists of least 13 branches in East and West of the country which operate fully on the principles of Islamic banking\textsuperscript{54}.

---


\textsuperscript{52} Farook, op.cit.

\textsuperscript{53} Ibid.

\textsuperscript{54} Islamic Finance Report, KPMG and Research Intelligence Unit-Sri Lanka, Sri Lanka, September-2011, p-37. KPMG is a Swiss entity, globally recognized network of firms. Available at http://www.kpmg.com.
Ceylinco Islamic Investment Corporation (CIIC)

Launched in 2003 it is fully backed by Ceylinco Insurance, one of the leading conventional insurance providers in Sri Lanka. CIIC offers both selected Shariah compliant and Takaful (Islamic Insurance) products. The Takaful concept is steadily gaining acceptance in Sri Lanka, where there are now 13 licensed insurance companies (Farook, 2007).

However the Sri Lankan market, including that for Takaful, faces several challenges and obstacles. One of the primary obstacles is the unconcern of the regulators to make necessary amendments in law to encourage the development of Takaful. Other hurdles that can be brought into consideration are, lack of investment opportunities that are Shariah compliant and acceptable to the insurance regulators, a high capital requirement, severe competition, consumer resistance to a new form of insurance based on religious principles and Muslim representation being only 9% of Sri Lanka’s population. To subdue these impediments is a great challenge for Takaful industry in Sri Lanka, the operators of which need to employ a concerted effort to convince insurance regulators to accept the salient features of Takaful and treat it as a new business model.

Muslim Commercial Bank, MCB Sri Lanka

The Head Office of MCB is located at No.8, York Arcade Building, and Leyden Bastian Road, Colombo. MCB Sri Lanka was established after MCB Bank Ltd Pakistan took over the operations of Middle East Bank Ltd Colombo in 1994. Over the past decades of its operation, while improving service quality and investment in technology and people, the Bank has concentrated on growth, which is further attested by the large deposit base of its ever-expanding branch network. Within just a period of 17 years of operation MCB Bank has managed to accomplish several key milestones of their presence in the Island. MCB Sri Lanka has the credit of being one of the pioneers in introducing a fully-fledged “Shariah Compliant” product range through its Islamic Banking Division (IBD).

National Asset Management Limited (NAMAL)

It is the first fund management company in Sri Lanka licensed to manage unit trusts. Together with Amana Capital (a subsidiary of Amana Investments), it launched the

55. Farook, op.cit.
58. Farook, op.cit.
NAMAL Amana Equity Fund early in December 2007. The objective of the equity fund is to achieve significant growth over the medium to long term by primarily investing in equity securities that are Shari’ah compliant (Farook, 2007). NAMAL is launching “NAMAL Shari’ah Fund”, a Shari’ah compliant Unit Trust, which will offer its clients a varied portfolio of Shari’ahcompliant equities listed on the Colombo Stock Exchange.59

**First Global Investment Group**

Launched on 27 November 2007 in Sri Lanka, it is a public limited finance investment company, which deals with Shari’ahcompliant investments and financing products and services. It also contributes academically to the field of Islamic banking and finance by promoting training and career development programs related to this field.60

**The ABC InvestmentsLtd. (Barakah Islamic Financial Services)**

It is a newly introduced investment company that has established a memorandum of understanding with the Central Bank of Sudan in which the latter’s experts will provide assistance on training and development to ABC — especially in its Takaful segment — and will be working closely with leading Islamic financial countries for the funding in Takaful as they plan to start off with general insurance (Farook, 2007). The ABC Investments Limited (Barakah Islamic Financial Services) ceremonially launched its first Islamic Credit Card in Sri Lanka at Holiday Inn Hotel, Colombo recently. Being the third Islamic Credit Card in the region, this Card is titled ‘ABC Barakah Credit Card.’ The First such card was launched in Malaysia, second in Pakistan and third in Sri Lanka and the first Islamic Credit Card in the World was launched in 2002 by ABC Islamic Bank in Bahrain.62

Sri Lanka is supposed to excel in this lucrative field of Islamic finance and banking as it had recently joined the growing number of countries which are facilitating measures to implement Islamic finance as an alternative method of banking and financing and are expected to be recognized as a mini Islamic hub of Asia.63 The expected rapid growth of the Sri Lankan Islamic Banking and Finance Industry is accredited to the increased awareness of faith based concepts and internalization of the financial markets and the strong demand for Islamic financial products is not only from the


60. Headquartered in Sri Lanka, First Global Group (FFG), is a diversified multi-disciplined institution engaged in providing Shari’ah compliant products and services. FFG has pioneered a number of 'first of its kind' initiatives in the Islamic banking & finance (IB&F) industry and growing into a global business company building strategic alliances in UAE, Qatar, Kuwait, India, Maldives, Bangladesh, Pakistan, Mauritius, Oman, Malaysia and Indonesia.
Muslims but the non-Muslims are also going for it\textsuperscript{64}. Provided its beneficial output of the profound financial products, Islamic Finance is gradually witnessing a shift of the global banking and finance system market towards it, Sri Lankan budding IBF industry being no exception to it.

**Conclusion**

With commencement of the second half of the 20\textsuperscript{th} century the world panorama showed a gradual transition of its geo-political phase towards the geo-economic one and during the mid of 20\textsuperscript{th} century top brass Muslim intellectuals and scholars felt the need of invigorating their religio-political and economic policy to bring the life of Muslim masses in conformity with the Shari'ah on one hand and compatible with the modernizing world on the other. In this backdrop Islamic economics, banking and finance was academically brought under consideration during mid of 20\textsuperscript{th} century and saw its practical implementation in 1975 onwards and has turned into a trillion dollar industry now a days. Recognized as a novel discipline in academics and as an alternative to the conventional economic system throughout the globe, it has shown significant tendency in the Muslim minority regions as well.

The above assessment of the Islamic Banking and Finance in Corporate Sector, in two South Asian Muslim Minority Countries, Indian and Sri Lanka, reveals that it is a nascent business sector with a resilient potential of sustenance even in the severe economic crisis. It shows a gradual growth in corporate sector with a significant rate in these countries. However, owing to some political as well as legal issues that turn out to be the impediments in the course of its development, there is a significant scarcity of large-scale adoption of this sector in the financial markets of these two countries. Keeping in view the religious conviction of the Muslims living as minorities and actively involved in the socio-political and economic affairs, there is an immediate need for large-scale incorporation of Islamic banking and finance tools in the business sector of these two countries. Also the global acceptance of Islamic banking and finance as a fresh and resilient monetary system and the thriving results it has shown over the past few decades brings it home that these developing countries should take a colossal step towards bringing the novel and unique tools of Islamic finance in operation one way or other, so as to get substantial profit out of it like other economies of East and West.

61. Farook, op.cit.
62. Available at Islamicfinanceexpert.wordpress.com.