Editor's Note

The perpetuation of the idea that Islam is a religion that does not incentivize economic productivity is a fundamental misunderstanding of the societal goals of Islam. Often, critics of the progress that Islamic economies have made often base their critique by comparing raw economic results or the wealth generated between Islamic and conventional economies. However, this comparison is an oversimplification of the benefits that fruitful production can provide, and it is one that benefits Western views of economics and productivity. In reality, Islam provides a fundamental motivation for hard work, productivity, and entrepreneurship. Additionally, the faith based characteristics of the Islamic economic system make productivity a mandatory and crucial part of the life of every Muslim, and serving the goals of society is a part of the Islamic economic framework as well.

Islamic teaching does not lack an incentive for productivity. On the contrary, Islam is a religion that promotes and requires Muslims to engage in productive activities. Both the Prophet and the *Qur'an* actively promote the idea that Muslims should engage in business ventures in order to meet their personal and spiritual needs. In one such story in the *Qur'an*, Mary, at the time of giving birth to Jesus, is ordered by Allah to shake a palm tree in order to gain access to the fruit that would fall as a result. However, this story is allegorical, because it would be unlikely that Mary would have physically been able shake the tree hard enough to accomplish this. Nevertheless, she is compelled by God to try. Islamic scholars focus on this story as an example of Allah encouraging hard work, despite the possibility of little personal gain as a result. This teaching implies that all Muslims should behave like Mary by engaging in productive activities.

In fact, the previous story also contends with the idea that Islam is inherently anti-entrepreneurial. In the story, Mary likely had little expectation that she would actually gain for shaking the tree, but her trust in Allah and desire to please him compelled her to do so anyway. Such an activity is not that far removed from the Western definition of entrepreneurship. Westerners would consider risk taking to be a key ingredient to fostering innovation and entrepreneurship. Islamic teaching, however, does not encourage the taking of undue risks. However, the story does illustrate the Islamic belief that entrepreneurial endeavors (like shaking the palm tree) should be undertaken, because faith in God that the activity will succeed yields the benefit of pleasing God through productive effort, even if the physical result does not materialize. In effect, Muslim entrepreneurs can be judged by their efforts in their attempts to be productive and please God and not by whether the activity yields physical results or wealth. In this sense, Muslim economics diverges from its

conventional counterparts, because the lack of religious goals underpinning traditional economics often implies that the only way to judge a project's success is by the physical return it generates.

Another common critique of the Islamic religion and economic system is that it encourages a life of religious extremism. In other words, it is often charged that Muslim adherents are focused so heavily on prayer and the afterlife that they place little value on productive or entrepreneurial activities in this life. However, this viewpoint is also a misunderstanding of most Islamic teachings. On the contrary, Islamic teachings of the Prophet and *Qur'an* place a strong emphasis on striking a balance between fulfilling the obligations of prayer, taking care of one's family, and tending to the needs of society as a whole. One such example the Prophets teachings on moderation describes the interaction of the Prophet with a fellow Muslim at prayer. In this story, the Prophet came across a man at prayer, and he had noted that this man spent a large amount of time praying. The Prophet asked the man how he was able to provide for his family, since he spent so much time at prayer. The man replied that his brother worked to provide for his family. The Prophet replied that the man's brother was the more pious of the two. This story illustrates the idea in Islam that a good Muslim must live a well-balanced life.

Just as Islamic teaching discourages engaging in prayer at the expense of other responsibilities, it also discourages Muslims from pursuing business or personal interests at the expense of religious or societal duties. The goal of Islam is to encourage a combination of religious and business activities that best contributes to society. In addition, this balance in Islamic societies is more easily achieved, because religious principles underpin economic transactions. In this way, Islamic activity itself is designed to inherently instill balance into the economic system. Conventional economic systems incorporate legal principles into their framework, but largely avoid the laying of religious foundations. As a consequence, religious and societal goals are not at the forefront of conventional economic transactions, and individual utility is often seen as the primary motivating factor. In this regards, it can be argued that conventional economics, not Islamic economics, promotes unbalanced activities, because the economic activities are often too focused on agents' personal (often monetary) goals.

Another critique of Islamic culture is that it does not encourage the learning and experimentation that is needed to drive economic growth and often creates the most innovation. However, this claim is also false. Again, words of the Prophet and the *Quar'an* encourage Muslims to learn and pursue knowledge, and knowledge is held in high regard in traditional Islamic society. Many often cite the Renaissance and

Scientific Revolution in Europe as being the great precipitators of economic growth, science, and innovation. However, during the Middle Ages, much of the philosophy underpinning these movements that were developed by the Greeks and Romans were lost to the Dark Ages. Islamic cultures, however, maintained and extended much of this knowledge, and, through later interactions with the West, this knowledge was re-introduced to Europe. Without the focus on knowledge that is a pillar of Islamic society, the great European movements that were the catalyst to their economic expansion would have been unable to take place.

The fact that Islamic tenets permeate the economic transactions of Muslims makes this system substantially different from those of traditional economies. Muslims do not engage in production simply to make profit, but they also serve religious goals and society as well. Thus, the measures of success for Islamic economies are not directly comparable with those of traditional economies, which typically use wealth as the yardstick for economic well-being.

The first paper, by Muhammad Akram Khan, focuses on translating the religious tenants of Islam and the *Qur'an* into a set of economic hypothesis that can be empirically tested in Islamic economies. Islam provides guidance with regards to the function and forms of financial instruments which are acceptable in an Islamic economy, and, unlike in Western countries, these religious tenants are inseparable from the daily economic interactions of devout Muslims. However, the translation of these religious principles into a well-defined theoretical model of an Islamic economy has been slow to develop. A key issue in the development of an Islamic economic model is that, while the holy teachings are seen as pure, their interpretation by clergy and scholars may not be. Hence, there is still work to be done in properly translating the word of Allah into a set of practicable economic activities. This paper attempts to develop the literature along this line by proposing a framework whereby a set of hypotheses are developed based on Islamic principles. These hypotheses can then be tested using empirical data. Of particular interest is testing hypotheses surrounding the key economic concepts in Islamic economics, including *riba*, *infaq*, *shukr*, *tauba* and *taqwa*. The paper helps to develop an empirical framework whereby the theoretical basis of Islamic economics can be developed and empirically tested.

In the second paper, Bijan Bidabad examines the characteristics of the Rent Financial Sharing (RFS) financing mechanism of the Rastin Profit and Loss Sharing (PLS) system. This financing arrangement is an important instrument in Islamic finance. Since Islam prohibits *riba*, or the use of interest, different financing mechanism must be used to fund projects in Islamic economies. Just like in conventional economies, entrepreneurs often have worthy investment projects, but lack the financing to engage

in the ventures. Likewise, depositors have assets, but lack profitable investment projects. Under the Rent Financial Sharing Agreement, the depositors agree to provide funds to the entrepreneur, and the entrepreneur is charged with managing the project. In return, the depositor receives a portion of the profits, proportionate with his investment. In addition, in order to properly align the incentives of the entrepreneur and depositors, the entrepreneur also often mortgages some of his own assets to be held in the venture as well. This type of arrangement is significant in Islamic economies, because it is consistent with Islamic principles banning fixed interest. The paper discusses some of the new innovations taking place with these products such as Rastin digital certificates, whereby depositors/investors can trade claims to Islamic investment opportunities in a marketplace.

In the third paper, Abubakar Garba discusses the issue of Islamic banking and finance in the country of Nigeria, which has faced some controversy in recent years. Nigerians have questioned the spread of Islamic banking in Nigeria, often arguing against the introduction of religious principles into economic transactions, as well as the potential exclusion of non-Muslims from the system. The paper points out that the views often used to criticize Islamic finance stem from a lack of understanding about Islamic banking practices. The paper attempts to enhance the understanding of *Shari'ah* principles and how they translate to banking practices. In addition, the author attempts to enforce the concept that Islamic banking does not attempt to exclude any group from inclusion in banking activities. Lastly, it is stressed the recent Nigerian Constitution guarantees citizen's access to all financial institutions.

In the fourth paper, Aftab Khan examines the degree to which both conventional and Shari'ah stock market indexes can be used to predict real economic activity in Malaysia. The study examines the Malaysian economy from October of 2006 to March of 2012. The author uses industrial production as a proxy for the real productivity of the Malaysian economy, the 3 month Malaysian treasury bill proxies the risk free rate and monetary policy, and the Shariah and conventional indexes serve as measures of stock market activity. A main goal of the study is to ascertain whether the conventional or Shariah stock index better explains real production activities in Malaysia. Methodologies used for testing include cointegration analysis, error correction modeling and variance decomposition. The results show that the Shariah Index is a better indicator of real production in Malaysia. This result has significant implications, because the results imply that changes in the Shariah index should be of concern to policy makers, as it will have a direct impact on economic wellbeing.

The fifth paper, by Sania Ashraf and Malabia De, tests the efficiency of Indian stock market indexes using several statistical methodologies. The empirical analysis uses

data that ranges form 2008 to 2013, and several measures of the Indian stock market are utilized, including the CNX NIFTY, CNX500, etc. Empirical tests along the lines of Brock *et al.* (1996) reject the hypothesis of independent, identical distributions of return variance. Furthermore, a GARCH methodology is used to show that the non-linearity in Indian return volatility is caused primarily by volatility clustering. Such a result implies that the random walk hypothesis is violated and, thus, short-term movement can be predicted. This result has important implications as it indicates a violation of efficiency in the Indian financial markets.

Abduh and Othman examine the quality of service provided by Islamic banks in the United Arab Emirates in the sixth paper. In a number of counties, the financial service industry is comprised of both conventional and Islamic banks. As a result, it is important to determine which firms are able to better service their customers and generate loyalty in an increasingly competitive environment. The analysis examines descriptive statistics from survey data, and the results show that customers prefer the following bank characters: quick approval of financial proposals, quick approval of new account openings, low costs of services and products, and an Islamic working environment. Conversely, customers seemed to be uninterested in the variety of banking products and internet banking. These results can help banks focus resources into areas that can help build a loyal customer base.

In the seventh paper, Mahmoud Bekri and Aaron Kim examine the Islamic financial system in terms of risk-taking behaviors. This paper focuses on the *hifdh almal* principle of investing which promotes safety and the avoidance of risk and uncertainty. Additionally, *amanah* requires that Islamic managers strive to achieve this goal. However, there has been a growing literature that shows heavy tail distributions and volatility clustering in the returns of Islamic investments. These results question whether the Islamic principle of keeping risks low is being followed closely enough. The authors recommend using student's t copula methods to acquire a portfolio based on STARR and Rachev ratios. The results of a simulation show that this methodology significantly improves the performance of Islamic portfolios.

The eighth paper is by Kader, Zakaria, Razali and Abdullah and examines customer preferences in Islamic banking institutions using survey data from the Islamic bank Bank Rakyat. The authors utilize an exploratory factor analysis and find that customers are attracted by high quality services, the returns it is able to provide customers, and its physical image. An additional result shows that both Muslims and non-Muslims are influenced by these characteristics. The results are important, especially in light of increasing competition in the Islamic banking industry.

In the ninth paper, Mahdi Salehi and Arash AriyanPoour examine the issue of Islamic accounting in Iran. The authors utilize a survey of 120 Iranian banking clients and find that the importance of returns is not diminished within Islamic banking institutions. In addition, they find that *zakat* is not a barrier to Islamic accounting. Studies such as this are important, because they can be used by managers to cater better to the needs and demands of the Islamic banking clientele. Also, the results presented show that Islamic banking customers have the same concerns as conventional banking customers and that additional taxes do not serve as a deterrent. These results imply that there is room for the Islamic banking industry to grow by attracting new customers away from conventional banks.

In the tenth and final paper, Syukriah Ali , Rosliza Md Zani , Kartini Kasim examine the factors that drive Islamic investors to invest in a particular *Shari'ah* compliant fund. *Shari'ah* compliant funds are important investment vehicles, and this market has become increasingly competitive. Additionally, the ability of a fund to attract and maintain investors is very important, because fund outflows can cause liquidity problems reduce returns and larger funds can take advantage of economies of scale. The paper focuses on the Islamic unit trust organization in Malaysia. Survey data is used to show that attitude and perceived behavioral control are directly related to investors' decision to invest in the Islamic unit trust fund. The results presented have direct industry applicability, because knowing what motivates investor to select one fund over another can help fund managers attract and maintain investors, thereby improving the return prospects for all investors in the fund.

I hope the readers will enjoy reading this issue of the journal.

Sincerely,
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April 7, 2014
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Reference: Rasem N. Kayed and M. Kabir Hassan, Islamic Entrepreneurship, Routledge Publishing Company, November, 2010. ; ISBN13: 9780415584494, 376 pages, hardback, paperback, Published by Routledge