

Thoughts on Economics

Vol. 20, No. 01

Islamic Economics, Banking and Finance

**in the 21st century: Selected Issues in
Curriculum/Human Capital Development**

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Introduction

Contemporary Islamic Economics can be seen as a 20th Century response by Muslims to present indigenous solutions to the economic problems faced by the ummah. While early works in the late 1960s and 1970s tried to build conceptual and theoretical frameworks for the discipline, the second half of the 1980s saw works on Islamic banking and finance (IBF) dominate and become the main visible feature of Islamic economics. The track record of IBF is indeed impressive and deserves to be acknowledged. From the establishment of the first private commercial bank in 1975 in Dubai, there are now about 300 Islamic Banks and 90 Takaful companies in over 75 countries. One can also witness the high growth in global Shari'ah-compliant assets, estimated at USD1 trillion with a growth rate of 15-20% per annum.² To fulfill the human resource demands of the IBF, many programmes, specializations and elective courses in Islamic economics, banking and finance, and related areas such as fiqh and accounting have been offered in numerous countries all over the world.

Despite the great strides made, there have also been criticisms of Islamic economics, banking and finance (IEBF), both at the conceptual, but mainly at the 'practice' level. In the case of IBF, the main argument goes back to interconnected issues of 'Islamicity' (of products and instruments), preferences of products and instruments (especially between academics and practitioners), qualifications of those involved in the IBF industry, as well as the role and competency of the shari'ah advisory process. While the world is still trying to come to terms with the exact magnitude of the 2008-2009 global financial and economic crisis, it has also given an opportunity for the proponents of Islamic economics, banking and finance to present IBF as an alternative to the dominant capitalist paradigm.

This paper will discuss selected issues in Islamic economics, especially manifested in the IBF industry. It will then try to connect these issues to IEBF education and human capital development. It will try to address some concerns and debates within the conceptual/theoretical discourse as well as those concerning the conceptual/theoretical- practical relationship. While many issues can be discussed, this paper will try to focus on some interconnected issues that have direct concern to the education process as well as content of curriculum that will help take IEBF forward.

2 "Islamic Banking & Finance at the Crossroads of Global Financial Crisis: The Way Forward", Keynote Address by Dato' Mohd Razif Abdul Kadir, Deputy Governore, Bank Negara Malaysia at the soft lauch of the IIUM Institute of Islamic Banking and Finance, 20 March 2009, Kuala Lumpur. For a detailed elaboration on the development of IBF please see Askari, Hossein, Zamir Iqbal and Abbas Mirakhor (2009), *New Issues in Islamic Finance and Economics: Progress and Challenges*, Singapore: John Wiley and Sons, especially Chapter 1.

Tensions in Contemporary IEBF

Islamicity of IEBF: The Tragedy of Separation

A question that increasingly annoys many in the field of IEBF, especially those in the IBF industry, are the constant doubts concerning the Islamicity or authenticity of IEBF. Although primarily aimed at the practice of IBF, academic and scholars involved in Islamic economics, banking and finance are not spared from the critics. A closer analysis of the literature will betray a complex host of issues both in theory and practice.

In the early 1970s, when Islamic economists started writing about Islamic economics, IBF was presented as part of an Islamic economic system. The writings as a whole put forward a very different IBF than what we see today. The picture was one that had a more ‘developmental’ approach and goal. However, by the late 1980s, this approach and those from among the academia who promoted this approach, were overrun by those who were more ‘practitioner-practice friendly’. What happened was a kind of separation between the mother discipline (Islamic economics) and the more highly demanded ‘offspring’ (Islamic banking and finance).

In many programmes/specializations in IBF, one could easily go through the programme without taking courses in Islamic economics. This mistake does not seem to have been realized.

The Shari’ah Scholars-Bankers Alliance

There is no doubt that IBF has made remarkable advances over the last 30 years. Numerous statistics can be quoted weekly to show the progress³. One controversial area regarding the practice of IBF that has come under scrutiny is the issue of the ‘**shari’ah advisory boards**’ and the shari’ah advisory process that govern individual Islamic banks and their views regarding Islamic banking in this modern age. Issues such as ‘Who should sit on these advisory boards’, ‘What their qualifications should be’ and ‘What should the scope of their duties be’ are questions that have gained importance over the years. Increasingly, Islamic economists have been marginalized in the IBF industry as a result of the separation discussed above.

The separation of Islamic banking and finance from Islamic economics, in the view of the current author, poses a ‘foundational error’ that has had serious repercussions. It betrays a serious lack of proper judgement among those involved in the IBF industry and who dominate its decision-making process and set its future direction. We will take this up in later paragraphs.

³ For example, please refer to Islamic Finance News, a weekly on-line magazine that gives up-to date information on the IBF industry globally.

The Direction of IBF: Modifying Instruments or Going For Fundamental Institutional Changes?

A larger issue is whether Islam and the modern economy can be reconciled at all. Is it enough to create banking products that mimic those of traditional finance but also meet the letter of Islamic law? Or must the goals of the financial system itself be reworked fundamentally? (Carla Power, Foreign Policy, January/February 2009)

One major criticism of Islamic banking has been that it is modeled after the interest based (especially commercial) banking system. Hence, the role and function of banks have primarily been retained while focus has been on creating ‘shari’ah compliant instruments (seen by the critics as more expensive duplicates)⁴ to replace the interest based instruments of conventional banks. Critics as early as 1986 like Ziauddin Sardar blame what they saw as ‘patchwork economics’ stemming from the misplaced Islamization of knowledge (IOK) agenda⁵. He argued that since the IOK takes the modern discipline as the reference point and wants to ‘seek the relevance of Islam to it’⁶, this can only result in patchwork and ‘bad imitations’. This criticism could have some truth to it if one was to take the ‘*simplistic and shallow*’ understanding of IOK that seems to have prevailed among some proponents of Islamic banking, and consequently practitioners of Islamic banking and finance.

What we mean by this simplistic and shallow understanding of IOK is emphasis on narrow areas of economics, in this case banking and finance instruments, without giving due emphasis on foundational issues and on economics itself. Failure to give attention to these foundational issues such as philosophy of Islamic economics and finance, as well as to Islamic economic theory, could easily lead writers to accept the banking institution as is, without understanding the history and foundations of modern economics and banking. The result: an overwhelming dominance of debt instruments such as al-murabahah and ba’i bithaman ajil to replace interest (debt in conventional banking). While these debt based alternatives are generally accepted by scholars as being legitimate contracts, Islamic economists initially argued against these debt instruments being given too much prominence by Islamic banks. The main reason put forward was that these instruments had less ‘developmental impact’ compared to equity alternatives such as mudarabah and musharakah. The practice of IBF clearly shows that ‘Islamization’ efforts, *if not inclusive of foundational, methodological and epistemological concerns relevant to economics and finance*, will end up making Islamic economics a branch of western economics and may not live up to the claims that IBF will be the savior of humankind against crises like we are facing now.⁷

4 See the views of Mahmoud El-Gamal in his website/blog.

5 See his *Islamic Futures* (1986), London: Mansell Publishing.

6 This is taken from step 5 in Ismail Faruqi’s *Islamization of Knowledge: Problem, Principles and the Workplan* (1982), Herndon: IIIT.

7 While this is seen as counter-productive by critics like Sardar, some scholars like Kahf (2003) are of the view that Islamic economics becomes a part of the science of economics just as Marxist or capitalist economics. It is to be studied within the area of economic systems but based on the assumptions of Islamic axioms, values and ethics, just as Marxist and

capitalist economics are studied within their own paradigms. While this is not the place to evaluate this position, the present writer may not fully agree with this view as it may be wrong to equate the nature and scope of Islamic economics with its contemporary western secular counterpart. See his 'Islamic Economics: Notes on definition and Methodology', *Review of Islamic Economics*, Volume 13, pp. 23-48.

IBF in Theory vs IBF in Practice

The tensions that existed, continues to exist today between the ideals of IBF initiated by Islamic economists in the 1960s and early 1970s with the practice of IBF spearheaded by bankers, with the support of some jurists and economists, It will continue to be an important area of debate and criticism. As mentioned in previous points, while the early Islamic economists saw IBF as an extension of Islamic economics, and hence, having developmental goals, the practice sees IBF as primarily a commercial enterprise as in modern banking and finance, and hence, replicating its practices. Even if we accept the less preferred options of debt-based instruments (like BBA and bay' al-inah based contracts in Malaysia) the theory-practice divide is further aggravated when *the practice of debt-based IBF does not necessarily follow the requirements of the theory of debt-based IBF*. A recent High Court judgement in Malaysia gave a verdict stating explicitly that the 'BBA as practiced in Malaysia was not a bona-fide sale' and for all practical purposes was more like a loan contract. On appeal (the written judgement is still pending), the presiding judge found that the High court judge had erred in his judgement, since the BBA is a sale contract and not a loan. A simple reading of this decision indicates that both judgements seem to be talking about different things: the appeal court was referring to the theory of BBA, while the High court was referring to the practice of BBA in Malaysia. While the debate is set to continue, one has to ask why there is a departure between theory and practice? Are the practices violating important conditions of contract? If yes, how were the practices 'justified' by the shari'ah boards? If no, how can their justification be made clear to those who oppose it? This has brought into question the whole process of shari'ah advisement and the qualifications of members of these boards.

The IBF Advisement Process: Breaking Free from Equating the Shari'ah with Law

As mentioned earlier, the Islamization of the banking and finance industry has been on one hand, a great success story for showing the world that Islam and the shari'ah can contribute positively to solving modern finance needs. However, there seems to be only one model of 'Islamization' that has dominated over the last 30 years, the model of 'partial Islamization. What may be needed is the introduction of more holistic Islamization of economics/finance' that would present alternatives that question some of the more fundamental institutional structures of the financial system. We have to make some important changes to the ways the IBF industry works if the second option is to be introduced.

In the current practice, most of the banking products are designed by bankers who are mainly trained in conventional finance or some other conventional area, but whose knowledge in Islamic heritage and Islamic economics/finance may be limited or even non-existent. They rely on shari'ah (misread legal/law) scholars trained in fiqh and to a lesser extent in *usul-al-fiqh/jurisprudence* to give verdicts on these sometimes rather complicated financial products. These scholars with due respect to them, are still in 'legal' mode, i.e. focused exclusively on legal reasoning. They are greatly in demand to make *ijtihad* on contemporary economics/finance issues and to produce alternative shari'ah compliant instruments. While their sincerity is not questioned, the 'originality' of the products and their implications for society sometimes are.⁸

Besides the 'duplication' criticism, there is a much deeper soul searching that needs to be done by all involved. Is it possible for us to truly develop genuine Islamic alternatives if we are not trained in both economics/finance as well as the heritage? Is it possible to look at instruments from the purely legal reasoning angle, dealing with contracts, without also knowing the economic and social implications of those instruments?⁹ Can we truly claim that the instruments that are being put forward are genuinely 'serving public interest' if we do not give the required attention to the economic and ethical (and not just legal) implications of the views that we make? Should there not be a preference for more ethically preferred choices in IBF? Should IBF be satisfied with the 'minimum legal requirement' as seemingly practiced now? Can fiqh/law compliance be equated with shari'ah compliance? All these questions beg well thought of answers.

⁸ See Mohd. Daud Bakar, a leading shari'ah consultant for Islamic banking not only in Malaysia but internationally recognized. In an interview in the STAR newspaper (February, 2005), he voiced his concern that Islamic banking products seem to be losing the confidence of customers because they seem to be 'duplicates' of conventional banking products. He calls for greater effort in developing more original instruments.

⁹ In this issue, M.N. Siddiqi pointed out the importance of understanding the 'macro-fiqh' dimensions of IBF on the economy and society as a whole as opposed to the 'micro-fiqh' qualifications of most legal scholars. See his '*Shari'ah, Economics and the Progress of Islamic Finance: The Role of Shari'ah Experts*', *IIUM Journal of Economics and Management*, Vol. 15 No. 1, 2007.

Limiting knowledge of the shari'ah and the 'heritage' to mere fiqh discussions and reasoning, will not do justice to Islamic economics, banking and finance. In the case of economics, banking and finance, we are talking about a social science that tries to understand, analyse and describe human interaction and choices made in areas of allocation of resources, distribution, exchange and finance (among others). In the last category, it will also involve the creation of instruments.

Similarly, if we talk of the methodology that needs to be adopted, the discipline of *usul al-fiqh* (understood as more legal reasoning) has to be distinguished from *usul al-Iqtisad*, the latter being a much broader area of 'the foundations/methodology of Islamic economics'. Rather than only limited to the legal dimension of the heritage and its methodology, *usul al-iqtisad* would include the Islamic worldview, *usul al-'ilm* (sources or foundations of knowledge), *fiqh* and *usul al-fiqh*, *usul al-din*, history, analytical techniques and many other areas of knowledge that would enable holistic decisions to be made, decisions that will enable the 'more preferred choices to prevail and decisions that will take into consideration a wider end-result that represents public interest'¹⁰ Hence the knowledge of the heritage required to develop contemporary Islamic economics banking and finance must be more than just the narrowly 'mis-defined' shari'ah (legal) sciences. One of the greatest maladies to befall the Muslims is this corruption of original 'rich' meanings of terms and concepts in the Islamic worldview to narrow meanings.¹¹

¹⁰ On the discussion of '*usul al-iqtisad*', please see Mohamed Aslam Haneef and Hafas Furqani, *Usul al-Iqtisad: The Missing Dimension in Contemporary Islamic Economics*, *Readings in Islamic Economics and Finance*, Universiti Utara Malaysia, 2007.

¹¹ See Syed Muhammad Naquib al-Attas, *Prolegomena to the Metaphysics of Islam*, Kuala Lumpur: International Institute of Islamic Thought and Civilization, 1995.

Genuine Islamization Requires Major Overhaul of Curriculum

As far as modern economics is concerned, genuine and meaningful Islamization cannot occur without some level of ‘critical’ understanding of the functioning of the modern economy, its system and constituent elements. We state ‘critical’ because the modern system has to be evaluated from an Islamic framework or perspective. Knowledge in this category would include areas such as economic history (both of thought and practice), statistics (including today’s econometrics), theory (both macroeconomics and microeconomics) and economic sociology (which may include other social sciences). One must also be prepared to include elements of sociology, logic, psychology and philosophy in its connection to economics. In the context of developing Islamic economics, it would be necessary for us to ‘master’ these areas of western knowledge, but always with reference to the Islamic perspective. In terms of economics, banking and finance, this would mean understanding contemporary advances in these areas *critically*.

Meaningful Islamization implies that the Islamic economist or the Islamizer of contemporary economics, banking and finance must know what is acceptable, what needs modification (what to be done and how to do it), what is to be rejected (what and why) and to be able to relate these to contemporary realities as well. It is certainly a tall order and one that does not seem possible if we continue to move in the present way contemporary Islamic banking products are being developed. While the products are developed and presented by mainly western trained economists/bankers, shari’ah scholars are asked to evaluate them. The latter are not necessarily familiar with the running of the economics and finance sectors and their knowledge in areas of philosophy/methodology (with reference to *usul al-Iqtisad*) leaves a lot to be desired. If people are questioning present day products, it is not necessarily only for their legal validity but also for their ethical implications. It is a valid question to ask whether the present two parties involved in the creation of Islamic financial instruments (conventional bankers and shari’ah/legal scholars) should be left alone or some other type of boards need to be set up to act as checks to the shari’ah boards!

If one interprets this as a call for the inclusion of Islamic economists, a point of caution is called for. Even among the Islamic economists, we have to be honest about our ability to truly Islamize economics. While many economics/Islamic economics programmes do offer courses in the heritage, these are usually in *fiqh* and to a lesser extent in *usul al-fiqh*. In addition, these courses are taught in ways that are ‘unconnected’ to economics/finance. The level of discourse in methodology and philosophy of science leaves a lot to be desired in these programmes. Islamic economists themselves keep referring to the heritage in terms of *fiqh* and law. This brings us to the issue of the human capital challenges faced.

Genuine IEBF: The Role of Education and Training

Fard Ayn Knowledge in IEBF: Islamic Heritage and Modern Economics/Finance

In line with the Islamization of Knowledge agenda, the present writer views the solution to developing a viable IEBF alternative to be incumbent upon a serious reform of knowledge and education. We must accept the reality that in order to provide viable, legitimate and ‘preferred’ Islamic alternatives, we must integrate Islamic heritage with modern knowledge. The main lesson gained from 30 years of the IEBF is that no creative synthesis between the Islamic heritage and modern economics, banking and finance in the form of textbooks can be produced unless we are able to create a new breed of scholars (and to a lesser extent, practitioners). Right now, despite much progress, the gap is still there. The gap is there not because no one has pointed out what needs to be done. Taking the IBF example, the gap is still there because short-term gains that make IBF ‘seem to be successful’ are taking precedence over a longer term view on what we want IBF to achieve. These longer term goals cannot be seen without an understanding of both the heritage and modern economics and finance *and their philosophical foundations*.

In academia, modern western trained Muslim social scientists are not able to appreciate the philosophical and methodological issues underlying their own disciplines, let alone having any meaningful exposure to the Islamic legacy. Their training has created, in many cases, ‘second class’ western scientists, who some times even fail to grasp the essence of their disciplines, not to mention any ambition of ‘mastering’ their disciplines as demanded by the Islamization of Knowledge agenda

In other cases, their training may have created ‘masters’ of modern disciplines, who have also, maybe unconsciously, become entrapped in the existing frameworks of those disciplines, i.e. they may not see things from genuine Islamic perspectives. It may be pertinent to keep in mind that although many Muslim academics may also have advanced degrees in specific areas of knowledge, their knowledge of Islam, its worldview, of Islamic philosophy and methodology relevant to their disciplines and of IOK, may greatly differ from one academic to another. In extreme cases, the latter may even be non-existent.

This is not surprising since most economics and finance programs in western universities today hardly discuss philosophical and methodological issues in economics. In addition, western methodology and its ‘scientific methods’ are accepted as objective and correct, with an overwhelming attention paid to technical procedures and application of quantitative techniques to solve mathematical equations, without ever questioning the foundations of these methods and techniques and the theories they promote. Critically evaluating these foundations is what genuine Islamization of Knowledge is all about, and it would seem the logical area to allocate resources, both financial and human. If nothing more, we should at least learn from the developments in the west where an increasing number of economists

and philosophers of science are questioning the entire framework on which the dominant paradigm of neoclassical economics rests.¹²

Scholars keen on Islamization of Economics and Finance would certainly benefit from reading the material coming out from scholars and graduate students in western universities, who in many respects are much more advanced and profound in their critique of mainstream neoclassical economics. IBF needs to devote more resources to creating a new type of scholar who will be able to be genuinely innovative, keeping in mind the developmental goals of contemporary Muslim societies. The scope of knowledge that will be required to meet these challenges must be widened, while areas that are concerned to be irrelevant like history and philosophy need to be part of the curriculum that is emphasized.

¹² In the last three decades there has been a growing disenchantment with the dominant paradigm of mainstream economics. Alternative views are being put forward and heterodox views are having a renewed life. See for example www.hetecon.com and www.paecon.net

Curriculum Coverage: Lessons from B.Economics at IIUM

In order to meaningfully develop genuine Islamic Economics, banking and finance, a major rethinking of curriculum content may be needed. The International Islamic University Malaysia (IIUM) was established by the Malaysian government in 1983 as a direct influence of the intellectual movements of the time and conferences promoting Islamic education in the 1970s. The central thrust of these conferences was that to create a new breed of Muslims who not only new their heritage, but were also well versed in modern disciplines. Hence there was a need to critically evaluate modern knowledge from Islamic perspectives. The Kulliyyah of Economics (now Kulliyyah of Economics and Management Sciences) was established together with the inception of the IIUM in 1983. The 'Islamic perspective' and Islamic heritage was to be conveyed to students in three different ways:

University level courses giving students general exposure to Islam and its different dimensions

Kulliyyah and Department level Islamic Economics/Banking, fiqh and usul al-fiqh courses

Kulliyyah and Department level economics/finance courses presented in a comparative/critical manner from Islamic perspectives

The B.Economics programme had very ambitious goals as stated in its 1983 programme book.

- 1- Every course is presented from an Islamic perspective. Western economic theories will be presented and then critically analyzed from an Islamic viewpoint.
- 2- The program generally adopts a comparative approach.
- 3- The program hopes to "devalue" economic concepts from all alien values (and to infuse Islamic values where possible).
- 4- The program has certain core subjects in *aqidah*, *shariah* and *akhlaq*.
- 5- The Arabic language is very central to the objectives of the program.
- 6- After a strong foundation in the Islamic perspective in economics, the fourth-year courses are of more conventional in nature.
- 7- To ensure correct understanding, a limited number of options are offered.

The author would argue that the initial mission and vision of the B.Economics programme had a genuine Islamization of Knowledge agenda in mind. 'Comparative, critical, devalue (dewesternization), holistic Islamic heritage, build Islamic orientation, followed by conventional economics' are all part of genuine Islamization, although this term was not used in 1983.

However as time passed, the above goals gave way to a diluted form of Islamization. In a paper presented in 2005¹³, the following 6 categories of courses were identified and the emphasis seen clearly indicates changes that occurred :

¹³ See Mohamed Aslam Haneef and Ruzita Mohd Amin, 'Teaching Islamic Economics at the Department of Economics, International Islamic University Malaysia', paper presented at the 6th International Conference on Islamic Economics, Banking and Finance, Jakarta, 21-24 November 2005.

- 1- Conventional economics courses (Conv.)-----
-34%
- 2- Courses with some Islamic input/Comparative courses (SI/Comp.)---
-30%
- 3- Islamic economics courses (IE)-----
-14%
- 4- *Fiqh* courses (F)-----
---7%
- 5- *Usul al-Fiqh* courses (UF)-----
---7 %
- 6- Other Islamic courses (OI)-----
---9%

Some Observations

a. Islamic Heritage

What we notice is that there was a ‘narrowing’ down of the heritage to fiqh and usul al-fiqh. In 1983-1987 students were exposed to a much wider scope of the heritage than is the case at present. This seems to be in-line with the way the IBF industry has also developed, where an overly ‘legal’ mode has taken over IBF. This can be seen very clearly if we analyse the various curricula available in universities offering programmes in Islamic economics, but more so in Islamic Banking and Finance.

b. Modern Economics

The modern economics component has always remained strong and has always met international standards for an undergraduate degree in Economics. One issue that probably needs attention is the possibility of introducing other schools of thought in western economics rather than focusing only on the dominant neoclassical paradigm. This is especially relevant if we want to benefit from the western critique of modern neoclassical economics. Again this is manifested in the IBF industry, where Islamic banks are seen by many to be just ‘replicas’ of modern commercial banks.

c. History and Philosophy

Both western economic thought and Islamic economic thought have been less emphasized, while economic history has never been offered in the programme. Logically one would see economic history as being a very important input in trying to understand how Muslim scholars and society developed thought and practice in the past. In addition methodology/philosophy was never given serious attention, even at the graduate level. There is very little sympathy from present day faculty in economics departments for history and philosophy. This would be even less in the IBF areas.

d. Comparative/Critical Component

Although still making up 30% of the curriculum, this figure does not really represent the content and level of critical evaluation, hence depicting a major shortcoming in efforts at Islamization. The core reason for this is the quality and expertise of the academic staff. As mentioned earlier, most staff are trained in economics, hence their ability to master the Islamic heritage is rather weak. This can probably be described as a shortcoming of the IOK agenda as it had not been focused on creating a generation of scholars/lecturers who could carry out the IOK agenda and to produce teaching materials that would be used in the classes.

Conclusion

There is no doubt that contemporary IEBF over the last 30 years has made progress. However, there is still much room for improvement. Alternative models and approaches should be allowed to be presented. This paper has tried to argue that a reform in curriculum and mind-set change is needed to take contemporary IEBF forward. Many pioneers of Islamic economics have observed that IEBF seems to have reached a 'plateau'. There is an urgent need to convince those in decision-making positions and those who hold the purse-strings, to be bold and facilitate these reforms. The paper has argued for adequate attention to be given to the foundations of IEBF. This was the approach taken by our great scholars in our own tradition in the past, as was the approach adopted in western scholarship during the developmental stages of modern western economics, and again over the last 30 years in the west. We will not be able to do justice to the IOK agenda. Islamic economics, banking and finance if we do not channel resources to this task. It is essential to dedicate funds to undertake research in these less commercial, but vital areas. Equally, if not more challenging, will be the task of trying to get young academics to actually do research in these areas. There is a need to make a long-term commitment to knowledge and scholarship now. Only by focusing on the fundamentals would IEBF be able to genuinely take up the challenge of being the alternative to the dominant paradigm.

