

A note on money and islam - a medium of exchange and a unit of account versus mon...

[Economics](#), [Currency](#)



These Short Essays are partial fulfillment of Paper IE1001 of Part 1 of Certified Islamic Finance Professional (CIFP) [DRAFT V0. 5] INCEIF Student Name: Mustafa Aydemir Student ID: 1200279 IE1001 Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc - 1- Bismillahirrahmanirrahim Essay No. (3) Money and Islam - A Medium of Exchange and a Unit of Account versus Money as a Commodity Everybody is using money. Most of us want it; we work for it and think how to get more of it. Therefore, it is vital to ask what money is, where it comes from, and what money is worth. Economics is an academic discipline that tries to answer those questions. It would be too long and lengthy to discuss about money creation and growth from A-Z but in the following paragraphs the subject matter is elaborated from the conventional as well as the Islamic worldviews. Money in the conventional sense is a commodity people use in exchange for goods and services. Before money was used as a medium of exchange, barter trade was practiced whereby people trade goods and services in exchange for other goods and services. However, barter trade was considered not so practical as weighing, transporting and dividing goods was difficult. It was the lack of transferability and inefficiencies that created the need for better ways of exchange. The concept of money was born. There are different types of money that developed over time, which should be presented briefly. Commodity money is defined as valuable goods, which were used as an underlying for a currency, such as gold, silver, coffee or even tobacco. The biggest advantage of this kind of currency was its portability and easy storage. Another example of commodity money is the U.

S. currency before 1971, which was backed by gold (Investopia). Fiat money is the paper money currently circulating in our world that is not convertible in any other type of money. It is used in our daily life where we buy and sell goods and services. Fiat money is basically not backed by any commodity but by a government that guarantees its value and creates a perception and faith in people that it is worth it. It is simply needed because gold is IE1001 Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc -2- rare on this planet. The perception created is, that the stronger the economy, the stronger is the value of its money. It is important to understand, that money is valuable because we want it, but we want it only because it can get us a desired product or service. Money is generated by a kind of an uninterrupted collaboration between physical things, our elusive desire for them, and our theoretical trust in what has value. That is why printing fresh money will not enrich a nation. Another type of money is named credit money. Investopia defines credit money as " Any future monetary claim against an individual that can be used to buy goods and services". There are many forms of credit money, such as IOUs, bonds and money market accounts. Virtually any form of financial instrument that cannot be repaid immediately is considered credit money. Economists measure money in M1, M2 and M3 defined as follows. M1 money includes all coins and currency that is physically available, travellers checks, demand deposits, checking accounts that is used to make payments. M2 money is all the money in M1 plus saving accounts, timelinked deposits and non-institutional money-market funds. M3 money is all the money in M2 plus all

large time-deposits, liquid assets, institutional money-market funds, and short-term repurchase agreements. $M1+M2+M3$ together is the total supply of money in an economy, the "broad money". Money fulfills the three main functions. It is used as a medium of exchange. Furthermore, money is a unit of account that is a numerical unit of measurement for transactions, goods and services. IE1001 Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc -3- Lastly, money is used to store value that can be retrieved and used again. In Islam money is not a commodity, which makes all the difference. It is not considered as a commodity that should be used for a price, but rather as a medium of exchange in business transactions. Money as a commodity concept is prohibited, because it contradicts Islamic principles that does not recognize money as a tool to make profit. "Money is only a medium of exchange, a way of defining the value of a thing; it has no value in itself, and therefore should not be allowed to give rise to more money, via fixed interest payments, simply by being put in a bank or lent to someone else." (INCEIF Lecture Notes p. 81). Money used as a commodity would presumably divide the society into the poor and the rich, even countries into categories rich and poor economies neglecting their national debt levels. People or nations in need for cash, deficit units, borrow money from people or nations with additional cash, surplus units. They are required to pay a fixed interest payment for their loans. This is *riba* and is clearly illegal according to Shariah law because it enriches surplus units without any contribution to the real economy. Consequently, people in need for money would take a high risk of

becoming even poorer. Compound interest is the big problem that creates money out of thin air. Moreover, the so-called fractional banking system that creates 100. 000 USD out of a 10. 000 USD deposit, 90. 000 USD can be considered fictional money. 1 Title: Concept of Money from Islamic Perspective; Class: Islamic Economics [IE1001]; Prof: Dr. Magda Ismail Abdel Mohsin; Institution: INCEIF; Date: 8/16/2006 # Of Pages: 44 IE1001

Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc -4- The rich is getting richer relatively faster than involvement into the real economy, because money creates more money without work required and Many countries fall into the trap of borrowing money from the International Monetary Funds, in particular Muslim states. The weaknesses of money as a commodity, hit those countries with all its evil as borrowed money doubles, multiplies and compounds. Consequently future generations are affected. The current generation is living in exaggerated prosperity on the cost of many future generations. Money is Islam should not be hoarded and kept in the bank savings account. Instead, money is required to circulate within the economy freely to benefit frequently, continuously, proactively and directly the society at large. This leads to the basic principle of interest prohibition and replaces this Riba system with that of Al-Bay. A system that is very different from Riba. The principle paradigm is risk sharing to allow borrowers and lenders to share rewards. The process of wealth accumulation and distribution in the economy is fair and just and fits the spending (infaq) criteria of Al-Bay suggested by the following verses. “ Those who eat Riba (usury) will not

stand on the Day of Resurrection except like the standing of a person beaten by Satan leading him to insanity. That is because they say: " Al-Bay is only like Riba," whereas Allah has permitted Al-Bay' and forbidden Riba. So whosoever receives an admonition from his Lord and stops eating Riba shall not be punished for the past; his case is for Allah (to judge); but whoever returns [to Riba], such are the dwellers of the Fire - they will abide therein. "

(2-275) The verse (2-261) states the incentive of spending in the way of Allah swt by counting the great reward and the blessing that an individual get from one single transaction: Then the following verse (2-262) puts the conditions for infaq to be accepted, and that is for Infaq not to be followed

IE1001 Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc -5- by Riya (show-off) or by harming anyone or harming the society as a whole. Even if the spending is based on charitable purposes mentioned in verse (2-263), no reminding of it and no harm should be resulted from spending process. Indeed, a kind speech and asking for forgiveness would have better impact. So infaq has to be fully for the sake of Allah swt. (2-264). The consequences of Infaq being not for the sake of Allah are serious as there would be neither Baraka nor growth. Verse (2-265) shapes the objective of spending and is to be for the sake of Allah and his reward so the profile of gain and loss in Infaq is different from the ordinary thinking. In conclusion, the definition of money and the way wealth is accumulated and spend draw a fine line in the distinction of both the conventional versus the Islamic economic system. As money is a medium of exchange, savings does not yield interest income but instead require

business transactions. Al-Bay as the system of exchange that is based on the concept of spending (Infaq) and risk sharing for any single transaction between parties of exchange. It is notable that Tijarah and Bay are of two different meanings. Tijarah is for the individuals that are setting up the business that has the aspect of long term. It becomes clear that lots of efforts have to be spending in education, elucidation and clarification of the consequences by a simple definition of money. 2 2 This meaning can be clarified by looking verse: (2-282) " And do not be too weary to write it, whether it is small or large, for its specified term. That is more just in the sight of Allah and stronger as evidence and more likely to prevent doubt between you, except when it is a Tijarah which you conduct among yourselves. "So we can understand from this verse that Tijarah is among some people that the conduct it among themselves. (61-10) " O you who have believed, shall I guide you to a Tijarah that will save you from a painful punishment? " So, we can sense the longterm involvement in this transaction as Allah swt stated that for in the following 3 verses 11, 12 &13. 11 " It is that you believe in Allah and His Messenger and strive in the cause of Allah with your wealth and your lives. That is best for you, if you should know. "12 " He will forgive for you your sins and admit you to gardens beneath which rivers flow and pleasant dwellings in gardens of perpetual residence. That is the great attainment. " 13 " And you will obtain another favor that you love - victory from Allah and an imminent conquest; and give good tidings to the believers. " IE1001 Assignment in Islamic Economics - Short Essay No 3 by Mustafa Aydemir - DRAFT Version 0. 5. doc -6-