

Islam and Debt

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Overview of debt crisis

The 'debt' of world's poorest countries is estimated to currently stand at \$2.7 trillion¹. Since 1996, the world's poorest 66 countries have paid a total of more than \$230 billion between them to service their foreign debt - this amount far exceeds any aid they have received in return². Indeed, indebted countries are paying approximately \$118 million every day in interest and principal payments to rich countries - although payments far greater than the original loan amount have already been made. Indonesia, for example, has already 'overpaid' in the region of US\$151 billion in payments - twice the level of the country's recorded debt. This means that Indonesia has made a cumulative net transfer to the rich countries of US\$138 billion to date - or 90 per cent of Indonesia's GDP³.

Debt is in one of the principal causes of poverty; it has hampered the economic development of indebted countries and has prevented them from investing in essential services such as healthcare and education. For example, Ecuador spends 47% of its government income on servicing debt and only 12% on education and just 7% on healthcare⁴. The reality is, therefore, that many poor countries are spending more on debt repayments than on providing the most basic needs for their own people.

Much of this debt is 'unjust'. It has arisen from loans knowingly granted to dictators or oppressive regimes, provided by lenders who knew that funds would be misappropriated through corruption, or used for projects that would fail because of poor advice or incompetence by the lenders. The unjust debt is, therefore, largely a consequence of reckless, negligent and self-interested lending by the governments of rich countries and international financial institutions. Not only are successor governments burdened with paying off the debts of their predecessors, but also because the loans were not used productively, there are insufficient means to repay. Poor countries are often forced into taking out new loans just to service the old ones. They are trapped in a vicious circle of debt – indeed 'lending money to a starving woman to buy food when she has no capacity to repay does not create a legitimate debt'⁵.

From an ethical and moral perspective there are, therefore, clear reasons why the unpayable and unjust debts of the world's poorest countries should immediately be cancelled in full by fair and transparent means. Cancelling these debts would release funds that poor countries could invest in social welfare resulting in, for example, millions of children being able to attend school; reducing the incidence and impact of HIV/AIDS, malaria and other infectious diseases; increasing the provision of safe drinking water and sanitation facilities; and reversing the loss of environmental resources.

Are there any additional insights that can be gained through analysing the debt crisis from an Islamic perspective? Are there any specific Islamic teachings and guidance that Muslims can refer to when considering solutions? This paper examines briefly Islamic teachings on debt and, with references from the Qur'an and ahadith (narrations attributed to the Prophet Muhammad, peace be upon him), argues that for Muslims there are indeed strong and clear faith-based reasons for advocating debt cancellation.

Islam and social justice

The present crisis should not be examined within the relatively narrow confines of debt; rather, it is fundamentally a question of social justice, a concept that is paramount in Islam. Social justice includes three aspects, namely a fair and equitable distribution of wealth; the provision of basic necessities of life to the poor and the needy; and protection of the weak against economic

exploitation by the strong. The debt burden, however, is increasing inequality between rich and poor countries and is tantamount to exploitation. It also means that poor countries are often unable to provide the most basic services for their citizens.

The Qur'an commands Muslims to stand firm for justice at all costs:

“O ye who believe! Stand out firmly for justice, as witnesses to Allah, even as against yourselves, or your parents, or your kin, and whether it be (against) rich or poor: for Allah can best protect both.” (4:35)

The importance of justice as a human value is emphasised in the following verse:

“Be just, that is closest to Godliness”. (5:8)

Striving for social justice involves the struggle against poverty and inequality. The Prophet Muhammad (peace be upon him) said, “He who sleeps on a full stomach whilst his neighbour goes hungry is not one of us” (reported by Bukhari and Muslim). It is through good deeds and praiseworthy initiatives that Muslims can earn the good favour of Allah. The Qur'an says:

“Let there arise from among you a band of people who invite to righteousness, and enjoin good and forbid evil.” (3:104)

Hence, Islam stands firmly against inequality and encourages Muslims to be involved with initiatives that aim to eradicate poverty and challenge the root causes of inequality such as campaigns against unjust debt repayments and the pernicious causes of debt.

Islam enjoins Muslims to advocate on behalf of the poor

It is the moral duty of Muslims to continuously and fervently work for a more just and humane society. There are several verses in the Qur'an that encourage believers to also be the *voice* for the poor and marginalised:

“This was he that would not believe in Allah most high, and would not encourage the feeding of the indigent” (69:33-34)

“But ye honour not the orphans! Nor do ye encourage one another to feed the poor” (89:17-18)

The Prophet Muhammad (peace be upon him) said: “Whoever relieves his brother of a trial or a difficulty in this life; Allah will relieve him of a trial in the next life” (reported by Bukhari and Muslim).

Such commands go beyond asking believers to feed the poor and provide charity and clearly exhort the true believer to encourage each other to help the poor. Islam compels Muslims to speak out on matters of justice for the sake of the community. This can be understood as advocacy on behalf of the poor that is speaking for those who have no voice and working for the greater good of communities and the state.

Islam advocates wealth sharing

So important is the concept of social justice in Islam that *zakah*, meaning to purify or cleanse in Arabic, is one of the five pillars of Islam. The purpose of *zakah* (almsgivings) is to promote equality by redistributing wealth from the rich to the poor as well as keeping wealth clear of greed and selfishness. In addition to the compulsory payment of *zakah*, Muslims are encouraged to make voluntary contributions, or *sadaqah*, to help the poor and needy, and for other social welfare purposes.

The payment of *zakah* helps to prevent wealth from being accumulated and circulated only among the rich, while depriving others of the means to earning a livelihood. The Qur'an warns:

“Wealth should not only circulate between the rich amongst you” (59:7)

According to Islamic teachings, if creditors fail to alleviate the burden of debt, then debtors are eligible for *zakah*. Through *zakah*, Muslims are exhorted to assist the poor and the *indebted*, as well as other potentially vulnerable groups such as orphans and travellers. The Qur'an states:

The alms are only for the poor and the needy, and those who collect them, and those whose hearts are to be reconciled, to free captives and the debtors in need, and for the cause of Allah and the needy travellers. (9:60)

Islam prohibits interest

The huge debt that currently burdens poor countries has arisen from loans that have charged interest and have not shared risk between the lender and the borrower and have, therefore, contravened the two most fundamental principles of Islamic finance. Islamic commands to refrain from charging interest and to share financial risk seek to avoid the concentration of wealth and the economic exploitation of the weak and thereby prevent situations such as the current debt crisis from arising in the first place.

The core belief in Islamic finance is that money should not in itself be an earning asset; therefore Islam prohibits any and all forms of interest. There are several passages in the Qur'an which clearly condemn the practice of interest (referred to in Arabic as *riba*):

“Those who devour interest will not stand except as he stands who has been driven to madness by the touch of Satan ... Allah has permitted trade and forbidden interest ... Allah will deprive interest of all blessing” (2:275-6)

“O ye who believe! Fear Allah, and give up what remains of your demand for interest, if you are indeed believers. If you do not, take notice of war from Allah and his Messenger. But if ye turn back, ye shall have your capital sums: deal not unjustly and ye shall not be dealt with unjustly” (2:278-279)

Interest is considered an unjust and exploitative instrument of financing since the lender is assured a return without doing any work or sharing in the risk, while the borrower in spite of hard work, is not assured of a positive return. Furthermore, if the borrower's investment is unsuccessful through no fault of his or her own, it is unfair for the lender to demand repayment. The prohibition of interest is therefore a mechanism to establish justice between the lender and borrower⁶.

Of particular relevance are situations when debt becomes unpayable and the debtor's misery is aggravated by interest charges:

“O believers! Do not live on usury that is compounded over and over again. Have fear of Allah so that ye may prosper” (3:130)

Undoubtedly, the interest rates and penalties imposed by rich countries and international financial institutions have contributed to creating the current debt crisis. Thus, while Africa received \$540 billion in loans between 1970 and 2002, and paid back \$550 billion, because of imposed arrears, accumulated interest and penalties, in 2002 the continent still owed \$295 billion⁷. Although Nigeria only borrowed \$13.5 billion from Paris Club⁸ creditors between 1965 and 2003, it paid back \$42 billion because of accrued penalties and interest and yet still incredibly had a debt of \$25 billion to the group in 2004⁹

Islam advocates risk sharing

Islam encourages legitimate commerce, trade and wealth creation but only on the basis of equitable risk sharing. Importantly, Islam does not allow gain from an economic activity unless the financial capital is also exposed to the risk of potential loss. Therefore, Islamic finance promotes investment on the basis of profit and loss sharing between the lender and the borrower¹⁰. Financing methods that share risk encourage more responsible lending since both parties share in the reward or failure of the investment and have, therefore, an interest in ensuring that funds are invested wisely and productively. Since the loans provided to poor countries have not been on the basis of risk sharing, lenders have given loans irresponsibly to governments they knew would be unable to repay.

Furthermore, risk sharing between lender and borrower also assumes a certain degree of equality between the two parties. However, in all negotiations relating to debt cancellation and re-scheduling payments, poor countries have always been at a distinct disadvantage. While rich countries have joined together to bargain as one unified entity known as ‘the Paris Club’, poor countries have been barred from acting similarly, creating an unjust and unequal relationship.

Islam discourages heavy debt

Islam permits and even encourages assuming debt within affordable limits. If debts are incurred responsibly then prompt and full repayment is important. The Prophet Muhammad (peace upon him) said, “the best among you are those best in paying off debt” (reported by Muslim) and “procrastination (delay) in repaying debts by a wealthy person is injustice” (reported by Bukhari). Another hadith states “Whoever contracts a debt intending to repay it, Allah will repay it on his behalf, and whoever contracts a debt intending to waste it, Allah will bring him to ruin” (reported by Bukhari). This hadith emphasises that those contracting debt with the intention to repay will be granted the means to do so. However, at the same time it warns against acquiring debt that one does not have the means or intention to repay.

Islam discourages heavy debt as much as possible – indeed it is something that is considered to have a serious and direct effect on a Muslim's belief or conviction because it can lead to harmful consequences. The Prophet Muhammad (peace be upon him) used to regularly supplicate “Allah, I seek refuge with You from sin and heavy debt”. When someone remarked, “how often you seek refuge from heavy debt”, he replied, “when a man gets into debt, he speaks and tells lies, and he makes a promise and breaks it” (reported by Bukhari and Muslim). The Prophet Muhammad (Peace

be upon him) also said, “Whoever dies free from three things – arrogance, cheating and debt – will enter Paradise” (reported by Tirmidhi), and “The soul of a believer is held hostage by his debt in his grave until it is paid off” (reported by Tirmidhi). Clearly, from an Islamic point of view, accruing debt is a serious matter and should not be undertaken except in cases of real necessity. Importantly, it is incumbent upon those providing finance to do so in a responsible manner and to not overburden borrowers.

It is worth emphasising that incurring debt to fund luxury and extravagance is contrary to core Islamic values that condemn excess and waste. The Qur’an has in very strong words condemned and prohibited extravagance and prodigality:

"Eat and drink, but waste not by excess, for God loveth not the prodigals". (7:31)

"Squander not wastefully, surely the squanderers are the devil's brethren." (17:26-27)

Much of the huge debt that currently burdens poor countries has clearly contravened these principles and indeed has been termed ‘odious’¹¹ since it has been recklessly given by the governments of rich countries and international financial institutions and irresponsibly borrowed and frequently misspent or stolen by corrupt or dictatorial regimes. For example, President Daniel Arap Moi stole an estimated \$4 billion from the Kenyan Treasury between 1978 and 2002, while when Nelson Mandela was elected president of South Africa in 1994 he inherited debts of around \$20 billion from the oppressive apartheid government¹². Such practices have left the inhabitants of poor countries, who benefited little if at all from the loans and many of whom had not even been born at the time the debt was incurred, with the responsibility for payment.

Islam encourages debt forgiveness

Most importantly, there is clear and unequivocal support in both the Qur’an and ahadith for a policy of debt cancellation for those who are genuinely unable to meet debt payments. In the first instance, Islam encourages lenders to wait until such time as the loan can be repaid (with no penalties for late payment), or re-schedule the loan repayments. However, for those unable to repay it favours simply forgiving the remainder of the loan - indeed this is considered a virtuous action. The Qur’an clearly states:

"If the debtor is in difficulty, grant him time till it is easy for him to repay. But if ye remit it by way of charity, that is best for you if ye only knew" (2:280)

Similarly, the Prophet Muhammad (peace be upon him) said, “If anyone would like Allah to save him from the hardships of the Day of Resurrection, he should give more time to his debtor who is short of money, or remit his debt altogether.” (reported by Muslim)

An Islamic perspective on debt

Islam enjoins Muslims to strive for social justice. This requires a fair and equitable distribution of wealth, the provision of basic necessities of life to the poor and the needy as well the protection of the weak against economic exploitation by the strong. It is also the duty of Muslims to continuously and fervently work for a more just society, indeed Muslims are urged to advocate on behalf of the poor and marginalised. The debt that currently burdens many poor countries has arisen through loans that were given irresponsibly by rich countries and frequently misspent by corrupt and dictatorial regimes in poor countries. It is unjust to force their successor governments to repay. Furthermore,

the loans that were given contravened many aspects of Islamic financing; they were not given on the basis of risk sharing, they charge interest, and they have burdened poor countries with heavy and unpayable debts. In addition, for those genuinely unable to meet their debt repayments, Islam encourages the debt to be forgiven. Therefore, there is clear support in Islam for those movements that advocate for justice on behalf of the poor and marginalised and that argue in favour of debt cancellation.

Notes

¹ www.jubileedebtcampaign.org.uk

² Glennie, J (2007) *Enough is Enough: The debt repudiation option*, London: Christian Aid

³ Mandel, S (2006) *Odious Lending: Debt relief as if morals mattered*, London: New Economics Foundation

⁴ Glennie (ibid)

⁵ Hanlon, J (2002) Defining Illegitimate Debt and Linking its Cancellation to Economic Justice, Open University (available at www.globalfairtrade.ca/Illegitimatedebt.pdf)

⁶ Christian and Jewish theologies also maintained traditions against usury. In the Old Testament, for example, it says: “If thou lend money to any of my people that is poor by thee, thou shalt not be to him as an usurer, neither shalt thou lay upon him usury. If thou at all take thy neighbour’s raiment to pledge, thou shalt deliver it unto him by that the sun goeth down” Exodus (22: 25-26). In other words, not only is one not supposed to charge interest, but also if the collateral for a loan is in the form of a necessity like a coat, one must make sure that the borrower can still make use of it when it is needed. Anti-interest sentiment in the West existed as far back as Aristotle and was reinforced by the great Roman Catholic theologians, such as Augustine and Thomas Aquinas. There are further references against interest in Leviticus (25:35-37) and Deuteronomy (23:20). However, modern Christian and Jewish scholars have reinterpreted the term from its original meaning of “all” interest to “excessive” interest.

⁷ UNCTAD (2004) *Economic Development in Africa: Debt Sustainability: Oasis or Mirage?* United Nations: New York

⁸ The Paris Club is an informal group of financial officials from 19 of the world’s richest countries, which provides financial services such as debt restructuring, debt relief, and debt cancellation to indebted countries and their creditors. The permanent member-nations of the club are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Ireland, Italy, Japan, the Netherlands, Norway, Russia, Spain, Sweden, Switzerland, the United Kingdom, and the United States.

⁹ Glennie (ibid)

¹⁰ There are a range of Islamic, or more correctly *shariah* compliant, financing techniques. The most prominent profit and loss sharing techniques include *mudaraba* financing in which the lender provides all the money and an entrepreneur who uses his or her skill to invest funds in an attractive business. The resulting profits are shared between the two parties according to a pre-determined ratio. In the case of a loss, providing it has incurred in the normal process of business and not due to neglect or misconduct by the entrepreneur, the financier loses all his or her money, while the entrepreneur merely loses his or her time and effort. In a *musharaka* contract both parties contribute with capital or in kind investment and share profits according to their contributions. *Musharaka* can perhaps best be described as equity participatory financing. For a full discussion of the practical application of these and other Islamic financing techniques see, for example, Iqbal, Z and A. Mirakhor (eds) (2006) *Introduction to Islamic Finance: Theory and Practice*. Singapore: John Wiley & Sons.

¹¹ Odious debts is a doctrine that was developed by Russian legal scholar Alexander Nahum Sack in 1927 and is used to describe debts that have arisen when creditors have knowingly lent vast sums to oppressive and corrupt regimes, without the consent of people of the country, and knowing that the funds would be stolen or misspent. Successor governments are still expected to service the debt while creditors deny any responsibility. Mandel (ibid) has argued that the term ‘odious lending’ would be a more accurate description.

¹² Hanlon (ibid)