

## **Islamic Economics and Finance as an Alternative for the Current Economic System in the Context of Covid-19**

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### **Abstract**

Most of the economists in the world agreed that there will be a significant difference in the current global economic system in the post of COVID-19 pandemic, even they are waiting for an alternative economic system instead of the current one. Since Islamic Sharia provide us an integrated economic system, detailed by financial instruments and economical solutions, so it seems ready to be the alternative of the current system. The aim of this paper is to discuss the role of Islamic economic as a new strategy in overcoming and manage the problem of the global financial crisis that happened in the post of COVID-19 pandemic. Also, to discuss the effects that have impacted on the world economy during the pandemic period. In order to do that, the paper first presents crises due capitalism and its impacts on the world economy. Then, it analyses the role of Islamic finance for economy during the pandemic and it investigates the indicators of Islamic economic to prove its ability in solving financial crises and to be as an alternative economic system.

**Keywords:** Islamic Economics; Islamic Finance; Capitalism; Alternative Economic System; Crises, Covid-19.

### **Introduction**

The countries of the contemporary world knew two economic systems: socialist system and capitalist system. The first of them collapsed because of a defect in its theoretical construction and a deviation in its practicality, similarly capitalist system was exposed to crises and almost collapsed. Moreover, capitalist had experienced crises such as the great depression of 1930s, the crisis of 1970s and the financial crisis in 2008. Even though we are still watching fluctuations, recession, and inflation in the economy.

According to the United Nations (UN) projections, the world is facing the worst economic recession since the Great Depression (Hassan and others 2021). COVID-19 begun as a health crisis then turned into an economic crisis and it is continuing to develop into a humanitarian crisis. It had disrupted the normal life, political and economic life of societies on all levels, especially the poor and it affected small businesses (Jan and others, 2021). Business sectors have seen decline in their gross domestic products and employment due to the reduced demand and cash flow constraints. Furthermore, COVID-19 is having a significant impact on the economies of the MENA region, leading to the fall in oil production, hospitality and tourism are worst affected and decline in GDP per capita income. Further, the affection is harder on countries with low resources and still live war situations and conflict like Iraq, Yemen, Afghanistan, Syria, Lebanon, and Somalia. Thereby, the economy is literally in damaging, and it will take years to heal and recover (Hassan and others 2021).

In the global economic crisis of 2008, while global money market was collapsing because its dependence on dollar not on gold or silver; the countries rushed to reduce interest rates and even cancel it, which is an Islamic economic theory. And then, senior western economists invited to depend Islamic economic system to stand up to global financial crisis (Aydin, 2013). The particular reason for this circumstance is Islamic economics explain in detail what can be traded or not under the principles of Islamic Sharia. This can be used for the people's greatest prosperity with the principles of independence, togetherness, just efficiency, environmental awareness, sustainability and maintaining a balance between national economic unity and progress. So, if the principles of Qur'an and Sharia applied in the right way and direction, it will be the solution to all challenges in society to be a blessing for the entire world (Aydin, 2013).

The pandemic has brought the entire world into a recession without any exceptions. If large countries made small mistakes made either intentionally or unintentionally, this will trigger destructive economic impacts for other countries due to the capitalist economic system. Therefore, all the world leaders are terribly busy looking for a solution to save the economy of their countries (Jan and others, 2021). Thus, in this context, we will present economy crises happened in capitalism period in order to take in consideration capitalism's failure in dealing with crises, to proof our needs for a new alternative economic system.

This paper is an attempt to improve Islamic economics as a new alternative economic system by discussing the effects that had impacted on the world economy during the period of COVID-19 pandemic and presenting the crises due capitalism and its effects on the world economy. In order to do that, we analysed the role of Islamic finance instruments for economy during the pandemic and we investigated the indicators of Islamic economic to prove its ability in solving financial crises and to be as an alternative economic system.

### **Literature Review**

After the fall of socialism, capitalism started in Europe and had become the dominant system in the world. Then the world economy had experienced crises such as the great depression in 1930s, the crisis of 1970s and the financial crisis of 2008. After the last and the biggest crisis, people started to ask questions about the destiny of capitalism and they expected another global financial meltdown shaking the infrastructure of capitalism. In that case, there was a great opportunity to understand and fix a main fault of free market capitalism. If the fixing failed as well as capitalism failing to deliver its promise of paradise in this world then this actively demonstrates that we need a new paradigm (Aydin, 2013).

We can see the economic performance by the capitalist system as a positive fair side because it gives the individuals freedom to compete and perform themselves. On the other hand, capitalist economic system is too pragmatic, individualistic, and selfish. This has been proven by a bad record about the pragmatic economic system in the history after the second world war (Arfah, Olilingo & others, 2020). The governments who have the power of capital, make efforts by increasing the interest rates on their foreign debt loans to borrower countries by making the value of their country's currency rates to grow as well. Therefore, this system will affect the developing countries until the highest rate of

increase is seen. So, they are stuck in economic growth that comes from high-interest rates loans, thus make it difficult to resolve the debts (Arfah, Olilingo & others, 2020).

The capitalist economic theory itself explains that a large amount of money in circulation will trigger inflation then the inflation will trigger a price increase as a result of unbalanced between price and aggregate demand in the markets. In particular reason for that circumstance, it will be difficult for most people to meet their needs; thus, unemployment and economic decline will occur. Even though in 1971, in order to speed and develop the US economy, the US unilaterally decided that the US dollar is not back up or equalized to gold or silver anymore. Since then, the dollar is just a paper with no value and it still printing according to the US need (Arfah, Olilingo & others, 2020).

In Aydin's point of view, he think that the financial crisis in 2008 is essentially "moral crises" with its root going back as far as the Enlightenment (Aydin, 2013). He also considered that "capitalism is a secular religion in this context. Capitalism relies on the magical power of the free market mechanism to fulfill its promise of earthly paradise." (Aydin, 2013). In contrast, Islamic (moral) economic system is a noble way aims to achieve the prosperity of the community by depending Islamic values along the lined of; equality, justice, and the balance that regulates the economic practices (Arfah, Olilingo & others, 2020). However, the main difference between the capitalist economic system and Islamic economic is that secular capitalism gives uncontrolled rights and powers to profit and private ownership, in that way who have the authority in terms of capital will determinant the situation even its limits can always change by humans unlike Islamic economic refer things to Islamic principles (Arfah, Olilingo & others, 2020).

According to all these referring signs of capitalism failure in crises management, it's time to find a new economic paradigm to take a place as an alternative economic. So from many researchers point of view, as mine too, Islamic economic is ready to be the solution for these crises and to be the next economic system. Thereby, in the first place we will discuss the role of Islamic finance during Covid-19 and other crises in order to consider proofs.

### **The role of Islamic finance during Covid-19**

In the history of Islam, Islamic social finance proved its way to go during pandemic and crises. Thereby, Islamic banking and finance had an important positive role on the last economic crises, in particular its role in the development agenda of the MENA region and developing countries (Hassan, Rabbani & Abdulla, 2021). MENA countries faced many economic challenges along the lines of financial inclusion, inequality of income and employment generation, the role of Islamic finance becomes the most suitable solution for these issues (Hassan, Rabbani & Abdulla, 2021).

Investors find Islamic equity investments as safe heaven asset because of its stringent screening and reserving benefits for the investors. Furthermore, they sum up that the excess benefits provided by the Islamic indices are because of the systemic risk, it is actively demonstrating that the hedging benefit comes at an extra cost (Hassan, Rabbani & Abdulla, 2021). As Islamic equities performed well during the crisis of 2008(madi,2014), the same thing happened in the first quarter of 2020, Islamic finance indices have outperformed their conventional counterpart according to empirical analysis on Islamic equity investments indices (Hassan, Rabbani & Abdulla, 2021). Moreover, except the first

three months of Covid-19 pandemic, there was a significantly well performance for Islamic equities and indices. This refer to the high level of screening, this also actively demonstrates that the Islamic principle focusing on wealth creation in order to protect the economy from shocks caused by Covid-19 (Benamraoui, 2021).

As a supporting for Islamic banks costumers during the pandemic, they participate in the offering of the moratorium package to the public. However, there is a group of costumers who benefit the moratorium even if they are not financially affected of Covid-19 pandemic. And then they will be given a financial opportunity to leverage from the deferred instalments. In spite, a well-off debtor who purposely delayed his debt repayment as unacceptable and injustice act to creditor (Shaharuddin, 2020). In addition, Islamic banks are less susceptible to speculation and high leverage, the particular reason for this circumstance is in Islamic finance; banking products that associated with the transactions are directly linked with the real economy. Thereby, it gives Islamic banks flexibility at time when individuals and businesses are not able to meet their debt obligations (Benamraoui, 2021). But this may not forever work because if the real economy starts to decline at a higher rate of uncertainties brought by the pandemic. In that case, Islamic banks need more protection through central bank including plans such as liquidity requirements for the bank and lowering capital (Benamraoui, 2021).

According to Jan's paper "Before the pandemic, the demand for Islamic banking financing, deposits, and assets grew gradually. According to the Islamic Financial Services Industry Stability Report 2019, the cumulative annual growth rate (CAGR) of Islamic banking for the period of 2013–2018 increased by 7.1% for Islamic finance, 7.4% for deposits, and 7.2% for Islamic banking assets. Now, in the context of the imminent global recession, the Islamic banking industry, along with the rest of the world, is looking forward to a long path of recovery and confronting new business challenges" (Jan and others, 2021).

On the other hand, Hassan indicated that " report in June 2020 indicates that the pandemic offers a growth opportunity for the Islamic finance, which is more cohesive, transformative and consistent. Though Islamic finance industry grew at an overwhelming 11.4% in 2019 but the growth is expected to be in single digit during 2020-21" (Hassan, Rabbani & Abdulla, 2021). Consequently, Islamic finance has the power to arise as a new way for the investors in order to serve as a sustainable finance model to various stakeholdersthis can be through suitable coordination between different Islamic finance stakeholder and use of financial technology(Hassan, Rabbani & Abdulla, 2021).

As Benamraoui mentioned experienced ways to recover the economy after the pandemic, the reducing of interest rate increases the consumption and encourages individuals and firms to borrow more, which leads to more investments and providing job opportunities. Likewise, central banks took monetary measures in order to lower interest rates to zero in some countries like Spain and Sweden. This have been experienced under Covid-19 in order to increase lending and help economy to recover (Benamraoui, 2021). Second, profit and loss sharing instruments that adopted from Islamic principles provide better protection to the bank and their clients, such as Musharakah can create stability and lowers their agency costs for the banks (Benamraoui, 2021). From the author point of view, he confirm that the share of losses would avoid further weakening of their balance

sheet and enable banks to protect their net worth. Additionally, as deposits are not fully guaranteed, any potential losses are likely to be better absorbed by the Islamic banks minimizing their overall credit risk (Benamraoui, 2021). Third, it is another experienced way from Faturrohman (Faturrohman, 2021) concluded that Waqf can support the economy by employ Waqf assets for educational and infrastructure development purposes. As evidenced of the development of the Waqf board in Egypt, Kuwait, Malaysia, and Indonesia shows significant positive results in improving people life quality.

In order to proof the ability of Islamic economic system due solving pandemic issues, the next paragraph discuss some ways and solutions.

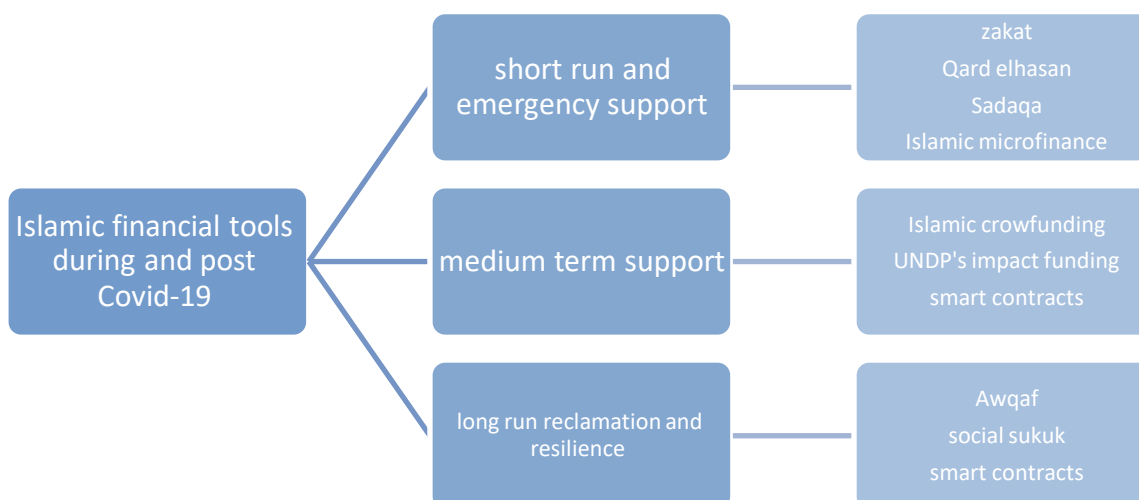
### **Indicators of Islamic economic as an alternative system**

Islamic economics defined as a branch of science in economics that aims to provide human welfare by distribute rare resources according to Islamic principles without limiting individual freedom, learning a sustainable macro, micro-economic and ecological balance. It is also known monetary policy and fiscal policy which are refer to the concepts of justice and equality, leads to to economic growth based on morality (Arfah, Olilingo & others, 2020).

The fundamentals of Islamic economic supported by factors such as; depending the currency on gold and silver to be free from inflation and to provide an open distribution and infrastructure. Therefore, in that way, all people can distribute without any monopoly also workers and the owners of capital are equal in making decision. Additionally, in general Islamic economic values refer to the control of individual assets, business optimization, income distribution, financial transactions, decency, civilization social participation, and transactions of goods and services based on morality, balance and togetherness (Arfah, Olilingo & others, 2020). Moreover, Islamic finance prevent the unfair and unethical trading like *riba*, *gharar*, *maisar* and excessive speculation. In that case, we can consider Islamic finance as a stable financing method can boost financial stability and generate a long term employment (Hassan, Rabbani & Abdulla, 2021).

Islamic finance has instruments can help and support the economy, financial institutions and banks during pandemics like the currently. If these instruments combined with the innovative technologies, it can be very useful to help the society not to negatively effect of Covid-19 implications, in case these instruments suited to each stage of the pandemic (Hassan, Rabbani & Abdulla, 2021). Some of the social instruments as described by (Hassan and others, 2020) are explained as follows:

**Figure 1:** Islamic finance instruments during and post Covid-19.



**Source:** adopted from Hassan and others, 2020.

These tools can be a great solution by combining with the innovative technologies like Fintech for building up the falling businesses and economies because of the foundation on what sharia-based financing is assembled. Haidar Sayed suggested a solution with a model developed by him, he used FinTech with natural language processing (NPL) and artificial intelligence in addition to Islamic finance tools such as Qard alhasan and Zakat ( Haider Syed, 2020). Similarly, Hassan discussed another solution in his research by combining FinTech with Islamic finance instruments like Zakat, Qard alhasan, Social Sukuk and Waqf. Thus under special requires related to interest rate that should be charged at 0% and tax rate to be around 2%. This way can be used to recover from the Covid-19 implications in individuals, small and medium size businesses (Hassan and others, 2020).

If the adoption of FinTech grew by the Islamic financial institutions, this will boost the prospect of international financial institutions quickly recovery from the shock. Furthermore, some Arab countries have the platform for these instruments in order to support the economy during the pandemic. Like the country with largest strength of Islamic financial institutions in the MENA region; Bahrain. In addition, Kuwait and Saudi Arabia are having the largest asset per bank followed by the UAE and Qatar (Hassan, Rabbani & Abdulla, 2021). Moreover, the countries of MENA region have a significant part of the development agenda of Islamic finance and banking (Arfah, Olilingo & others, 2020).

Islamic finance is expected to play a huge role in recovery of the economies during COVID-19 because the rules and principles prescribed by the Sharia, Islamic finance is accepted as ethical moral finance (Hassan, Rabbani & Abdulla, 2021). The ability to take the chances and transform is the key to economic resilience become from the various economic uncertainties, both external and internal. Thereby, many Islamic countries are competing to develop an Islamic economy that grow along with the growth of the world's Muslim countries (Arfah, Olilingo & others, 2020). According to the UN Sustainable Development Goals, in terms of the Islamic finance instruments, that's will lead to lower

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the impacts of Covid-19 on people, community, planet and profit. This is by unlocking the potential of Islamic banking industry for various stakeholders (Jan and others, 2021).

### **Conclusion**

In a conclusion, to sum up everything that has been stated so far, this paper discussed the effects that had impacted on the world economy during the period of COVID-19 pandemic also it discussed the crises due capitalism and its impacts on the world economy. In addition, it discussed the role of Islamic finance for economy during the pandemic also it investigated the indicators of Islamic economic to prove its ability in solving financial crises and to be as an alternative economic system.

Islamic finance and banking; main part of Islamic economy, has proven its ability and flexibility to control the economy situation during financial crises, in order to be stable as possible. The particular reason for this circumstance, is Islamic finance basing on the real economy and prevent the interest-based transactions and investment in bad assets like financial derivatives.

Moreover, Islamic finance has various instruments like, Qardh-Al-Hasan, Zakat, Waqf and Social Sukuk can combined with financial technology to be the most useful tool which is tailor made for the crises and pandemic like COVID-19 conditions and it can fight against the economic consequences.

Overall, we are still at the beginning of our path to exhibit Islamic economics as a ready alternative economic system. There are many missions ahead, like we need to go beyond the existing paradigm and create our own concepts and models whenever it is necessary. And we need to begin from microeconomics.



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