

## ISLAMIC BANKING AND FINANCE: A TOOL TO ENHANCE FINANCIAL PRESENCE AND SUSTAINABLE DEVELOPMENT IN CONTEMPORARY NIGERIA

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### Abstract

This study intends to bring in to limelight the roles of Islamic Bank and Finance to Sustainable Development in Nigeria. In doing so, the paper dwells on the features of Islamic Banking and financial system, traces its origin, discusses its benefits, enumerates its challenges, highlights its expected contributions to sustainable development in Nigeria and provides recommendations towards its challenges. Generally, expository methodology was used for the study while historical approach was resorted to where necessary. The paper revealed that, Islamic banking and finance is of related purpose to other forms of banking except that it operates using *Shar'ia* rules. One basis principle of Islamic banking and Finance is the sharing of profit and loss and the prohibition of the rate of interest. It also revealed that, the literature of Islamic Banking and Finance is replete with several benefits of adopting the Islamic banking and Finance model as a viable alternative to conventional finance. The paper also noted that, there are common misconceptions about Islamic Bank and Finance such which can hindering is rapid development such as: is only for Muslims, is a camouflage for terrorism financing, is only charitable Islamic Banking and finance and is Islam's World domination– Islamization plan. It is also provided possible suggestions to its expected challenges such as: low Western patronage, inefficient support from Central Bank, equity capital/cash requirements and orientation challenge, societal belief and socio-political environment, manpower and awareness. It finally exhibited how it can contribute to sustainable development in Nigeria.

**Key Words:** *Islamic Banking and finance, sustainable development, Shar'ia, awareness, contributions*

### Introduction

Islamic banking and finance is increasing its valuable market in the global finance industry, day by day. So much interest has been generated in Islamic banking and finance on a global scale because of its phenomenal growth within a relatively short span of time, and more especially, as an aftermath of the recent financial crisis. On a regional and sub-regional plane several countries are struggling to become the hub of Islamic banking and finance in African continent or in the West African Sub-region or at least to become pioneers in the field. Globally, Islamic banking and finance assets are expected to skyrocket to, with issuance of Islamic finance continuing to increase sharply across a widening geographic footprint. Today, over 300 Islamic banks and financial organizations are successfully running their business from Dubai, Los Angeles, London, Karachi, Jakarta, Cairo, Riyadh, and many other cities in the world<sup>1</sup>. Even, America has a history of quickly adopting and exploiting new financial systems, and it is appropriate and timely for the USA's financial sector to embrace IFS<sup>2</sup>. Hong Kong, UK, Luxembourg and South Africa are among a growing list of non-Muslim markets that have Islamic banking and finance, amending their legal, regulatory and taxation frameworks to accommodate Islamic banking and finance structures. As Islamic banking and finance is growing at 10 to 15% per year, and there is no sign that this trend is going to slow down in the near future and as such it is the fast growing segment of global finance in the world<sup>3</sup>.

So far, the World Economy today has exhibited weaknesses in recent times and led to a re-evaluation of economic and financial models. Islamic banking and finance Institutions therefore has:

- i. demonstrated resilience in the face of the global financial crisis relative to their conventional counterparts

- ii. considered a viable alternative to the conventional interest-based system
- iii. no longer considered a Muslim only alternative
- iv. becoming the fastest growing financial sector in the world (15% per annum)-IMF<sup>4</sup>

The purpose of this paper therefore, is to raise the awareness and knowledge of the roles of Islamic banking and finance to Sustainable Development in Nigeria in today's global financial market.

### **Islamic Banking and Finance**

Islamic banking and finance is banking or financing system that based on the principles of Islamic law and its practical application through the development of Islamic economics. It is can also be defined as a financial institution that abides by *shari'ah* principles in all of its activities through its role as a financial intermediary between savers and investors and it is also provides financial services within the framework of legitimate contracts and achieves a balance between economic and social return<sup>5</sup>. This type of banking differs from the Western form of banking. However Islamic banking is of related purpose to other forms of banking except that it operates using *Shar'ia* rules.

Two basic principles behind Islamic banking and finance are the sharing of profit and loss and, significantly, the prohibition of the collection and payment of interest by lenders and investors. Collecting interest or "*riba*" is not permitted under Islamic law. The principles deal with universal appeal and lay emphasis on moral and ethical values in all dealings of human transactions. In particular, Islamic ruling (*shari'ah*) prohibits the collection and payment of interest charge called *Riba*. Islamic jurisdiction prohibits investing in businesses that are considered unlawful or known as *haram* and are contrary to Islamic values<sup>6</sup>. More also, contracts where ownership of a good depends on the occurrence of a predetermined, uncertain or put in the future (chance) and speculative transactions are transaction that are prohibited by Islamic law because all involve excessive risk and are supposed to foster uncertainty and fraudulent behaviour<sup>7</sup>.

Since this system of banking and finance is grounded in Islamic principles, all the undertakings of the banking and finance follow Islamic morals. Therefore, it could be said that financial transactions within Islamic banking and finance are a culturally distinct form of ethical investing. For example, investments involving alcohol, gambling, pork, etc. are prohibited<sup>8</sup>. Therefore, the objectives of Islamic Banking and finance are:

- To operate in accordance with the *shari'ah* (Islamic law) and they have different objectives to foster and improve the well being of an individual and the economy at large.
- To promote, foster and develop the application of Islamic principles, law and tradition to the transaction of financial and related business affairs.
- To promote investment campaigns, enterprise and concerns which are they engaged in lawful business activities.
- Investors getting their return from profit and business sharing (PLS) investment<sup>9</sup>.

Some notable modes of Islamic banking/finance are:

**Musharakah (Joint venture):** This financial technique is one in which the capital owner provides finances investments in the business of another party<sup>10</sup>. Extra finance is provided to the party which may be an individual or group that already has some funds for investment. The provider of the finance makes additional funds available with a condition of sharing profits realized in the business. The ratio of sharing between the provider of the finance and the party receiving additional fund is fixed and pre-determined and this is made known to all concerned. There is also sharing of loss according to the proportion of the capital invested<sup>11</sup>.

**Mudharabah (Profit sharing):** This financing technique is the one in which the owner of the capital makes funds available to the capital user for some productive activity on the condition that the generated profits will be shared between them<sup>12</sup>. Here, the capital owner bears the loss incurred in the normal process of the business and due to misconduct or neglect by the capital user. Both parties know the predetermined and fixed ratios for the sharing of profit. This technique is similar to *Musharakah* since there is both sharing of profits in both and the provider bears the losses of the investments. Islamic banks have a norm which is to assess the profitability of a project, back projects with higher profit rates and this is taken to be safest and most beneficial for the society<sup>13</sup>.

**Ijarah (Leasing):** This is a financial technique in which an individual who is short of funds may approach another with a surplus who is referred to as the financier in order to fund the purchase for the productive asset involved<sup>14</sup>. The financier can do this by renting or buying it out to the one who needs the asset. This enables the investor to overcome the financial difficulties that has to do with

purchasing the required asset. He does not incur the capital investment involved in the purchase of the asset.

**Ijarah wa Iqtina (Higher Purchase):** This has to do with a higher purchase agreement between the clients and its banks<sup>15</sup>. In this case, the bank agrees to rent or buy a building, equipment or other facility for the client in union with the undertaking that is signed by the client to make incremental payments into an account. Profits are added to the paid installments at the end of the year in order to purchase the facility or equipment. The owner of the financed equipment becomes the client and that is the end of the contract<sup>16</sup>.

**Bai 'al Mu'ajjal (Deferred Payment):** There is immediate delivery of goods, inputs or implements while the agreed price is paid by the purchaser at a particular date in the future<sup>17</sup>. The component of the price includes the cost, plus the reasonable margin that covers the administrative costs. Example is that if a farmer sells inputs to farmers on a deferred basis, then the transaction is seen as a sale and not a loan. There is provision for the sale of goods for cash or credit on the condition that the price upon the agreement between the parties at the time of the bargain is not changed even if payment is not made when due.

### **The Origin of Islamic Banking and Finance**

The origin of Islamic banking and finance dates back to the very beginning of Islam in the seventh century. The Prophet Muhammad's first wife, Khadija, was a merchant and he acted as an agent for her business, using many of the same principles used in contemporary Islamic banking and finance<sup>18</sup>. Information has it that, the origin of Islamic finance dates back to the dawn of Islam 1,400 year's ago<sup>19</sup>. The boom in the internal and external trades in the dawn of Islam led to the creation of Islamic financial tools such as deposits, money transfers, checks, bills of exchange, and so forth to cope with these commercial developments<sup>20</sup>. For instance, history has it that, In its wider sense, date back to the rise of the Islamic Empire<sup>21</sup>. There were bankers called *sarraffeen* or *sayarifah* (singular *sarraf*) or *jahabidhah* (banks called *dawawin al- jahabidhah*) in the Islamic Empire.

Also, during the Abbasid-Khalif period (from the 8th century) the term *sarraffeen* was used to refer to financial clerks, experts in matters of coins, skilled money examiners, treasury receivers, government cashiers, money changers, or collectors to designate the well-known, licensed merchant bankers in those times. In addition, the first check in history was drawn by a *sarraf* in Baghdad in the 4th century AH (10th century AD), and it was cashed by the prince of Aleppo, Saif Al-Dawla Al-Hamadani<sup>22</sup>. Indeed, the historical records indicate that there were banks in those days. Muslims contributed greatly to the development of banking practices because, during the Islamic empire, there was

1. a legislative system, which included firm rules and regulations to govern all transactions;
2. a strong judicial system, which was capable of enforcing all legitimate contracts;
3. different kinds of commercial papers and banknotes that were widely accepted, such as promissory notes (*reqaah al-sayarifah*), bills of exchange (*suftaja*), and goods *sukuk*; and
4. licensed bankers, who had offices or agencies in different parts of the Islamic Empire and accepted deposits, assigned debt (*hawalah*), exchanged money, issued banknotes, and performed many other services<sup>23</sup>.

Information has it that, by the Middle Ages, trade and business activity in the Muslim world relied on Islamic banking and finance principles, and these ideas spread throughout Spain, the Mediterranean and the Baltic States<sup>24</sup>. Beginning with the decline of the Islamic Empire from about the 12th Century BC, the rule of the *sarraffeen* began to weaken. Islamic financial practices therefore, gradually withered due to the weakening of the Islamic empire. Their loss of power within society can be attributed to several internal and external factors<sup>25</sup>. Such as:

1. gradual but continuous deviations from Islam and Islamic *Shari'ah* especially in the political sphere.
2. extravagance and lavish expenditure of the courts.
3. lack of organisation and the inflated bureaucracy.
4. political breakdown, involving the loss of authority of the central government in the remote provinces and the emergence of petty dynasties and quasi-independent governors resulting in the degradation of the caliphs to the status of mere puppets of their ministers and military commanders.
5. rise and development of different and antagonistic sects, all claiming to be the only real Muslims such as the Sufis, the Shi'ites, the Ismaelites, the Druzes, etc..

6. prolonged warfare with the crusaders, Mongols and Tartars, which caused much destruction in Iraq and Syria.

7. Turco-Persian wars, which dragged on for nearly three centuries and which impeded the economic recovery of Iraq<sup>26</sup>.

Later, the Europeans adopted these Muslim practices and continued to evolve them until modern days. This allowed Western influence to increase throughout Islamic countries, especially through colonization. Under European influence, many Islamic countries began to adopt a Western banking model in the 19th century<sup>27</sup>. This started by opening branches of foreign banks or by establishing banks within countries. This trend continued in all Islamic countries until the middle of the 20th century, precisely, between 1960s to the 1970s when the calls to establish Islamic Banking and finance resurfaced in the modern world<sup>28</sup>.

### **Benefits of Islamic Banking and Finance**

Islamic Banking and Finance is replete with several benefits which could be beneficial to banks, customers, the economy and society at large:

**1 Economic system stability:** Major International Institutions like the IMF and the World Bank find that Islamic Banking and finance system is more stable compared to their conventional counterparts. It is also argued that the system does not create new money and therefore not inflationary as their conventional counterparts<sup>29</sup>. Furthermore, Islamic Economists argue that profit sharing model of Islamic Banking and finance will ensure a stable economy especially with respect to financial markets<sup>30</sup>. To a large extent, such a model resonates with a world experience a financial turmoil. This explains why the spotlight has fallen on Islamic Banking and finance, especially in the post financial crisis era where there is greater concern for ethical financial practices<sup>31</sup>.

**2 Efficiency:** Islamic Banks and finances are more efficient. This is because they are not subject to the volatile principle. Since Islamic Banking and finance prohibit interest rates, they eliminate all speculative activities that relate to interest rate expectations<sup>32</sup>. Again, proponents of the Islamic Banking and finance model advance that Islamic Banking and finance have greater market discipline as they are technically expected to do better screening of credit risks and be honest in their financial reporting<sup>33</sup>.

**3 Reduction of Moral Hazard and Adverse Selection Problems:** since Islamic Banks and finances are able to provide both debt and equity capital simultaneous they are able to reduce the risk of moral hazards and adverse selection. In addition, it could influence firms as they have representation on boards. They will be able to monitor and reduce moral hazards<sup>34</sup>. Also conventional systems allocate capital to credit worthy units and not productive ventures as Islamic Banking and finance model would through the PLS scheme.

**4 Pro-poor system of banking:** In a conventional system, funds are usually directed to those who have guarantees and collaterals and demonstrate better capacity to repay loans. On the other hand, funds in Islamic Banks and finances system are based on sharing of profit and loss and therefore one can access funds whether rich or poor, to the extent that one has ideas to undertake a venture<sup>36</sup>. The provision of interest free charitable loans (known as *Qard al-Hassan*), are also geared towards making life better for the poor<sup>37</sup>.

**5 Wide scopes of financial products:** Islamic Banking and finance will increase product variety and ranges and also improve quality of institutions in the financial sector<sup>38</sup>. Also Islamic Banking and finance offers the opportunity to deliver competitive, flexible and diversified tools in finance. In addition, there are three major benefits of the Islamic Banking and finance model which are described as its “developmental characteristics”. They are: productive characteristic, ethical and moral characteristic and relational characteristic<sup>39</sup>.

**6 Productive characteristic:** The Islamic Banking and finance model has a unique link with the real economy. Contracts such as *Musharakah* and *Mudarabah* are available for firms engaged in real production and contribute real-life businesses. The firm should be profitable so that such profits can be distributed between the entrepreneur and the bank. Other financing contracts such as the *Murabaha* and other sale related contracts are also linked to real assets or provision of some service. In this direction all forms of Islamic Banks and finances are interlinked with production or exchange of real goods and services<sup>40</sup>. Again, in relation to this, it is seen that the Islamic Banking and finance Model is detached from purely monetary activities such as debt rescheduling and derivatives trading (such as swaps etc.) which usually form part of the operations in conventional banks<sup>41</sup>. Also, the strongest argument put forward in favour of Banking and finance is its unique mechanism of integrating the

financial sector with the real economy. To this extent, it could be argued that, all other things being equal economies with high level of Banking and finance activity will experience real growth over time.

**7 The ethical and moral characteristic:** The uniqueness of the Banking and finance model also lies in its ethical and moral dimension. The Islamic Banking and finance model fully incorporates moral and ethical issues such that funds are not made available for production of goods that are harmful like alcohol and tobacco or services such as casino and production of pornographic material. Although such products and activities may be profitable, they are perceived to have negative long term effects on the economy and society<sup>42</sup>.

On another level, the Islamic Banking and finance is seen to be committed to giving interest free credit to the poor and needy usually from social funds. These are usually funded by yearly *Zakah* funds paid by Muslims, interest money accumulated from deposits in conventional banks and transactions deemed suspicious by *Shari'ah* boards. In some cases, Islamic Banking and finance maintain charitable funds. A typical fund is the "*Waqf*" account maintained in the Islamic Development Bank in Jeddah, Saudi Arabia purposely spent on research, developmental study, disaster relief services etc.

**8 Relational characteristic:** Islamic Banking and finance have unique relationships with customers and workers<sup>43</sup>. For instance, Financial contracts like *Musharaka* which takes the form of a joint venture agreement or venture capital-style financing for a project and mutually shares profits and losses allows for ongoing interaction and stronger partnerships and relationship with customers<sup>44</sup>. These special relationships are a source of competition among Islamic Banks and finances. In order to keep pace with competition, Islamic Banks and finances offer "*culturisation programmes*" to orientate their staff on the religious perspectives of the banking activity. Their knowledge of *Shari'ah* strengthens their competitive completion<sup>45</sup>.

**9 Reduction on Bank Exploitation by Charging Interest:** Exploitation by banks due to charging of interest is reduced since Islamic Banking and finance uses the non-interest banking technique<sup>46</sup>. The charging of interest by conventional banks has been noted as exploitative and the Islamic Banking and finance system is seen as a better option.

**10 Attraction of idle money:** A lot of Muslims do not see saving money in conventional banks as a worthwhile option, but now that there is Islamic Banking and finance, they will now be encouraged to utilize idle money into meaningful ventures<sup>47</sup>.

**11 Promotion of employment:** This happens due to its mode of operation giving the investors more chance to get access to direct financial opportunity. This to an extent promotes employment. It provides better opportunities to businessmen<sup>48</sup>.

**12 Promotion of Economy through Non-interest Banking:** A lot of economic proposals to better the economy have encouraged Islamic Banks and finances methods as an instrument to promote the economy. Non-interest banking will deepen the financial market. This allows a large portion of people to engage to actively participate in economic development owing to its nature and ability to offer an array of products that can take care of the financing needs of the public<sup>49</sup>.

**13 Adoption of Asset-backed Finance:** This method has to with the transfer of funds and this is not based on making money from money alone as obtainable from interest-driven transactions. *Ijarah* (Leasing) and *Musharakah* (Joint venture) are examples<sup>50</sup>.

Other features include are: reduction on bank exploitation by charging interest, attraction of idle money, promotion of employment, promotion of economy through non-interest banking and adoption of asset-backed finance.

### **Common Misconceptions about Islamic Finance**

There are many misconceptions about Islamic Finance among them are:

**Islamic Finance is only for Muslims:** Islamic Banking and finance system is an alternative means of making money through wealth creation and distribution and it is available to both Muslims and non-Muslims. There is nothing prohibiting a non-Muslim from using Islamic Banking and financial services or owning an Islamic Banking and financial institution. Although Islamic Banking and finance is based on the principles of Islamic law, its features grant social justice to mankind, which actually appeals to both Muslims and non-Muslims<sup>51</sup>. It is worthy to note that among the largest institutions offering Islamic Banking and finance services are conventional banking groups such as Citigroup, HSBC, Standard Chartered, and BNP Paribas. This is to prove that the values of Islamic Banking and finance are not exclusive to Muslims. This is also evidenced by the staggering

percentage of non-Muslim investors benefiting from Islamic Banking and finance services through these banks mainly because of its competitive returns. In Malaysia, for instance about 40% of the customers in its Islamic Banks are non-Muslims.

**Islamic Finance is a Camouflage for Terrorism Financing:**

An Islamic Banking and financial institution is strictly prohibited by the Shari'ah from knowingly assisting, let alone actively participating, in terror-related activities. This is because the Shari'ah does not condone violence against innocent victims and hence categorically condemns terrorism<sup>52</sup>. Quite unfortunately, the effect of the 9/11 attack on the United States and other similar activities in other parts of the world (and recently in Africa) has skewed the general perception of Islam, thereby raising undue fear and skepticism to anything branded "Islamic" or "Shari'ah". Hence, the misconception that Islamic Finance is a front for terrorism financing. However, the reality is, Islamic Banking and finance does not operate in a vacuum and is no different from other financial institutions which are subject to and bound by the strict laws and regulations within its jurisdiction of operation. For instance, there are provisions of the law on anti-terrorism and anti-money laundering and there is no financial institution that is immune to these laws<sup>53</sup>. Therefore, regardless of whether an institution is providing Islamic Banking and finance or not, if it is proven to be involved in or is supporting terrorist activities, it would be held accountable and face the consequences.

**Islamic Banking and Finance is only Charitable:**

Islamic Banking and finance is about wealth creation and just like any other business, is profit oriented. Islamic Banking and financial Institutions are accountable to their shareholders and investors who have invested their funds in the business with the aim of making reasonable returns on their investment which the institution is to ensure that it delivers in line with the principles of the *Shari'ah*. However, as is already evident above, Islamic Banking and finance is not a capitalist driven system of finance. There are inherent mechanisms to encourage Islamic Banking and financial Institutions to undertake corporate social responsibility in Islam such as the mandatory *Zakat* (alms giving) and voluntary *Sadaqah* (donations) which can be used to contribute to societal development<sup>54</sup>.

**Islamic Banking and Finance and Islam's World Domination-Islamization**

Islamic Banking and finance accounts for less than 1% of the global financial system. Furthermore there are more than 1.5 billion Muslims spread around the world and therefore are too heterogenous to have such a common agenda<sup>55</sup>. Muslims around the world belong to different races and are of diverse cultures. It is almost improbable that such diversity can create a single government with a common goal to dominate the world. As historical evidence has illustrated, Islamic Banking and finance should be viewed in the same vein as *halal* foods which has been around for centuries and is available everywhere around the world including non-Muslim countries and consumed by both Muslims and non-Muslims. In view of the fact that the presence of *halal* food has not resulted in the demise of non-*halal* foods or instigated world domination, Islamic Banking and finance should not be viewed differently<sup>56</sup>.

**Expected Challenges of Islamic Banking and Finance System in Nigeria**

**Awareness:** There is apparently low awareness of the Islamic Banking and finance concept. Hence, for interest free banking system to work efficiently in Nigeria, there is a great need for sensitization of all the stake holders (government/public, government and individuals) by Islamic professional scholars and Muslim economists. This is borne out of the fact that Nigeria is a secular state. Hence, government should not be seen as trying to Islamize the country's financial/banking system. This means that the tendency of the non-Muslims to mis-construe the ideology because of its religious colouration calls for nation-wide awareness.

**Manpower:** It is worthy to note that for Nigeria to institutionalize Islamic Banking and finance system, there is need to incorporate this concept into Nigeria University curriculum to prepare a good foundation and human resources for the operationalization of Islamic Banking and finance system. In other words, Scholarship can be awarded to students to travel abroad for practical training from those countries that have succeeded in the implementation of the Islamic banking. E.g. Malaysia, Bahrain, Saudi-Arabia. Etc. Requisite legal framework Central bank of Nigeria being the supervisor and regulator of the banking industry is expected to come up with details of regulations governing the operation of Islamic Banking and finance in Nigeria (legal frame work) that conforms to the principles of Qur'an and *ahadith* of the holy prophet Muhammed (SAW). However, the policy framework should be such that the Islamic Banks and finances will be competitive with conventional

banks. More importantly, the justification for the existence of an alternative is to quench the thirst of Muslim faithful for banking facilities that will be in total adherence to the law of Islam.

**Societal Belief and Socio-Political Environment:** There is no gain saying that the society's belief on the interest-based banking services would take a bit longer time to be eradicated. For instance, most of 'money bags' in the society often constitute the major shareholders in the banking capitalization. Hence, to remove such interest from what they have been enjoying might turn out to be a blow on their prosperity and an attack on their sources of wealth. But if the government is really sincere about this course as instructed by Almighty Allah then, the concerned authority could enact law that will lay the foundation for the establishment of Islamic Banking and finance system in Nigeria.

**Equity Capital/Cash Requirements and Orientation Challenge:** Due to risk involved in putting huge sums of money for take-off of Islamic Banking and finance, people will tend to be reluctant to invest. Hence, one would hardly see businessmen/money lender putting a lot of money on uncertainties, just in the name of Qur'an and *Ahadith* of the holy prophet (SAW).

**Inefficient Support from Central Bank:** The Islamic Banking and finance system in Nigeria may not receive effective support from the Central Bank of Nigeria. This will actually reduced the impact of this banking system on the Nigerian economy

**Low Western Patronage:** Banks like the World Bank are not yet given proper assistance to the Islamic Banking and finance system as they give to conventional banks. This will also have advert effect on the Islamic Banking and finance in Nigeria.

### **Islamic Banking and Finance and Sustainable Development in Nigeria**

The expected contributions of Islamic Banking and Finance to sustainable development in Nigeria are: Muslims all over the world are clamouring for Islamic Banking and finance. For instance, in Bangladesh, about 80% of the conventional banks recently opened separate Islamic banking and finance windows. Islamic Bank of Bangladesh Limited has 132 branches in the country and five hundred applications are pending with Islamic Bank Bangladesh Limited for opening of new branches. The situation may not be the same across countries<sup>57</sup>. But if Islamic Banking and finance succeeds in any country, the position may be similar in every Muslim-populated country. This means, that the Islamic Bank and finances in Nigeria should be well managed and successful so that people would have confidence in the system. Nigeria should enter into working relationships with countries with established Islamic Banks and finances to lend competent officials to assist in setting up Islamic Banks and finances in the country. However, the following points outline the benefits and opportunities for the establishment of an Islamic banks and finances in Nigeria:

The population of the Muslims in Nigeria which was put at about 50 percent is a veritable source of patronage more so as the bank will cater for not only Muslims but also indigent non-Muslims who would also tap the opportunity to build small and medium scale enterprises with little fear for their sustainability due to high interest rates. The establishment of the Islamic banking and financial system will help in furthering trade and businesses among the most vulnerable portion of the populace leading to an increase in the development and growth of the real sector of the economy. It should however be noted that when a business succeeds, it opens the door of employment opportunities, human capacity development as well as productivity and ultimately a positive effect on the gross domestic product (GDP).

An interest free investment climate will naturally attract investors who would want to benefit from the support of the interest free financial system. Investment can only thrive successfully in an environment where there is no stringent conditions attached to getting funds to finance investment. This means that Islamic banking and finance system has the wherewithal to facilitate and speed up the development of infrastructures which the country has been yearning for<sup>58</sup>. There is no doubt that the Islamic banks and finances would foster equality in the distribution of wealth in the society. This will facilitate the transformation of the Nigeria society into a more balanced state with reduced rate of poverty. A sense of belonging would also be created through financing of the business of customers based on Islamic financing procedures. In recent times, many Banks has come out with the list of bank executives that have engaged in un-secured loan lending resulting to the insolvency of most so-called reputable conventional banks. This action could be traced to the fact that they were not guided by the principle of the Qur'an and the *Ahadith*. Islamic banks and finances are based on trust and there are dire consequences, spiritual and physical, for contravening the rules guiding the entrenchment of such trust.

Financial stability, financial inclusion and shared prosperity can be instrumental in the successful implementation of policies on ending poverty, achieving food security, ensuring healthy lives, achieving gender equality, and promoting peaceful and inclusive society. Additionally, innovative Islamic Bank and financial instruments especially for infrastructure development such as *Sukuk* can be used to mobilize resources to finance water and sanitation projects, sustainable and affordable energy, build resilient infrastructure and shelter. In today's world, the global financial order needs to adopt a new banking and finance paradigm, one that is built on the principles of justice, risk sharing and direct linkages with real economy and avoidance of excessive speculation. This is necessary so that the world economy, in general, and the financial services sector in particular will achieve greater stability and sustainable growth trajectory<sup>59</sup>. Islamic Bank and finance has strong potential in promoting financial stability, financial inclusion and shared prosperity, and infrastructure development which will set an enabling environment for sustainable Development. Renewed efforts in the wake of the current global financial crisis in search of a more resilient and robust financial system based on stronger links between credit and the real economy have brought attention to Islamic Bank and finance<sup>60</sup>.

The principles of Islamic Bank and finance can minimize the severity and frequency of financial crises by introducing greater discipline into the financial system and requiring the financier to bear or share in the risk of the underlying economic activity. Islamic Bank and finance also requires the creditor to bear the risk of default by prohibiting the sale of debt, thereby creating a proper and sound due diligence by those who extend credit. Islamic Bank and finance emphasizes the full integration of finance with the real economy. Debt creation must be contractually linked with trade and production. Islamic Bank and financial instruments, (e.g. sale with a deferred price) make debt inseparable from real transactions. Accordingly, debt cannot grow beyond real resources. This is vital for sustainable development as uncontrolled debt is not sustainable and can be a heavy burden on natural resources and the environment<sup>61</sup>.

The de-linking of profit-making from the real economy is a major cause of excessive lending. It is important to underline the imperative of risk-bearing that Islamic Bank and finance encourages through its emphasis on real economic activities, including equity and partnership, sales-based and lease-based financing instruments. While debt is allowed in Islamic Bank and finance, it is not allowed to grow on its own. It can grow only in step with the growth of the real sector. Thus by integrating debt creation with wealth creation, finance is properly positioned as a means for promoting productive activities and cannot be used for speculation or be an end in itself. This prevents the creation of an inverted debt pyramid and, thereby, largely mitigates financial instability.

Islamic principles require an annual donation (*Zakat*) to the poor and the needy as an essential obligation of all Muslims who possess a minimum level of wealth. In addition, it strongly encourages establishing endowments (*Awqaf*) the return on which is dedicated to social objectives. These two institutions have historically played a major role in serving the social needs of Muslim communities. When fully utilized, they can be of great value in fighting poverty and achieving sustainable Development.

The small and medium enterprises (SMEs) are source of job creation and economic growth. The partnership financing, the core element of Islamic finance, provides an important source of funding for SMEs that might not be able to take on debt financing<sup>62</sup>.

Despite its relatively small size, the Islamic microfinance industry has shown a significant growth. The elements of just, ethical and pro-real sector development have interested many parties around the world in seeking to promote financial inclusion to support socio-economic development. Furthermore, Islamic Bank and Finance can create cross border trade and investments as foreign investors seeking to invest in Islamic products and services will find investment outlets to meet their needs thereby creating access to foreign exchange and positioning Nigeria on the map as an international financial centre. Customers (Institutional Investors and foreign investors) with an investment appetite can also benefit from *Shari'ah*-compliant funds as well as *Sukuks*, which are increasingly becoming common in global markets as a result of their impressive growth rates. Islamic Finance will undoubtedly create job opportunities as a lot of specialised skills will be needed to develop the industry and expand its growth thereby contributing significantly to the reduction of unemployment rate in the country<sup>63</sup>.

The innovation brought about by the structuring of Islamic products will also contribute to the creation of a new asset class which will be available to customers of all faiths. The introduction of

Islamic Bank and Finance models such as the *Mudarabah*, *Murabaha*, *Sukuk*, and *Istisna'a* which have been tried and tested in other countries will further strengthen the financial system and create risk diversification against future financial crisis. Furthermore, the introduction of a new asset class will create competition within the financial system and competition will drive the market and the economy<sup>64</sup>.

Islamic Bank and Finance will also contribute significantly to financial stability. This is because the principle of Islamic Finance negates all the factors which led to the global financial meltdown. Some of its inherent features identified by the IDB-IFSB (Islamic Development Bank-Islamic Finance Services Board) Task Force on Islamic Finance and Global Financial Stability provide key potentials in contributing to the global financial and economic stability: The fact that investments or financing can only be extended to real assets such as projects, trade, economic and commercial transactions ensures that there is growth in real economic activities which reduces the possibility of excessive leveraging.

The principle of ownership being very pertinent makes it impossible to sell what you don't have, which also restricts the possibility of unhealthy and excessive speculation as found in derivatives instruments used in conventional finance<sup>65</sup>. Participation of risks provides a strong incentive for Islamic Bank and financial institutions to ensure the success of the projects and activities that they finance. Its emphasis on certainty and transparency ensures that there is full disclosure and documentation of contracts which avoids unpredictable and unanticipated circumstances resulting in one party's undue advantage over the other<sup>66</sup>. Finally, stability and sustainable development have become the watchword in global business and governance and Nigeria as a developing country stands to gain immensely from this alternative means of financial management, not only for its foundation in religious principles but for its potential to contribute to the development of the country's economy and the society at large<sup>67</sup>.

### **Conclusion**

This study brought in to limelight the roles of Islamic Bank and Finance to Sustainable Development in Nigeria. It dwelled on the features of Islamic Banking and financial system, traced its origin, discussed its benefits, enumerated its challenges, highlighted its expected contributions to sustainable development in Nigeria and provided recommendations towards its challenges. The paper revealed that, Islamic banking and finance is of related purpose to other forms of banking except that it operates using *Shar'ia* rules. One basis principle of Islamic banking and finance is the sharing of profit and loss and the prohibition of the rate of interest. It also revealed that, the literature of Islamic Banking and Finance is replete with several benefits of adopting the Islamic banking and finance model as a viable alternative to conventional finance. Such as: adoption of asset-backed finance, promotion of economy through non-interest banking, promotion of employment, attraction of idle money, reduction on bank exploitation by charging interest, economic system stability and reduction of moral hazard and adverse selection problems. The paper also argued that, there are common misconceptions about Islamic Bank and Finance such which can hindering is rapid development in Nigeria like other country in a secular nation such as: is only for Muslims, is a camouflage for terrorism financing, is only charitable Islamic banking and finance and is Islam's World domination-Islamization plan. It is also provided possible suggestions to its expected challenges such as: low Western patronage, inefficient support from Central Bank, equity capital/cash requirements and orientation challenge, societal belief and socio-political environment, manpower and awareness. It finally exhibited how it can contribute to sustainable development in Nigeria.

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