

Introduction

Indian banking system has undergone innumerable changes since last six decades. The nationalisation of banks in the 60's and liberalisation in the 90's marked significant impact on Indian financial system.. A well developed banking system is a pre-requisite for smooth and effective functioning of any economy. The basic function of the banking sector has been mobilising savings from the surplus entities and channelising them to deficit entities for productive purposes. These functions are based on the premise of interest rates, interest being given to depositor and interest being charged by the bank for lending. An alternate to this conventional banking system is Islamic banking which prohibits transaction on the basis of interest and operate on profit and loss based on Islamic principles.

Islamic banking refers to a system of banking or banking activity that is consistent with the principles of the Shariah(Islamic rulings)and its practical application through the development of Islamic Economics. The principles which emphasise moral and ethical values in all dealings have wide universal approval. Shariah prohibits the payment and acceptance of interest charges (riba) for the lending and accepting of money, as well as carrying out trade and other activities that provide goods or services considered contrary to its principles. While these principles were used as a basis for a flourishing economy in earlier times ,it is only in the late 20th century that a number of Islamic banks were formed to provide an alternative basis to Muslims although Islamic banking is not restricted to Muslims. Islamic banking has the same purpose as conventional banking except that it operates in accordance with the rules of Shari'ah known as Fiqh al muamalat (islamic rules on transactions)

It is evident that Islamic finance was practiced predominantly in the Muslim world throughout the Middle ages, fostering trade and business activities. In Spain and Mediterranean and Baltic

states, Islamic merchants became indispensable middleman for trading activities. It is claimed that many concepts, techniques and instruments of Islamic finance were later adopted by foreign financiers and businessmen.

Scope of the study

- Banking institutions have emerged as a necessity for everyone poor as well as rich. Saving is important for an economy to develop. It is considered as the base for economic development. Even after 60 years of nationalisation, 60% of the population does not have proper access to formal banking. As per the Sachar Committee report based on 2001 census data, the percentage of Muslim household availing banking facilities is much lower in towns as well as in villages. Due to the religious reasons the banking sector has categorised Muslims and Muslim dominated areas as 'Negative Zones'. Because of the religious believes, Muslims are reluctant to the practice of conventional banking system.

In a state like Kerala where 25% of the population consists of Muslims, an alternative to the conventional banking leads to the accumulation of crores of interest income in suspended accounts.

Consequently, Muslims both rich and poor as well as those employed in the Middle East invest their money in gold and real estate which are not productive investments. Therefore there is a strong case to have an alternative system based on equity instead of debt based banking system. This will cater to support the religious sentiments of Muslims in the country.

The concept of interest free financial institutions in Kerala is in its infancy. But it has been working well in economically advanced Muslim as well as non Muslim countries. So the present study try to analyse the need for interest free financial institutions in Kerala. It also analyses the

saving and investment activities of the Muslim community in the absence of interest free financial institutions.

Objectives of the study

1. To review the concept of Interest free banking.
2. To make a comparative analysis of interest free banking and commercial banking.
3. To identify the effects of banking on the saving habits of the Muslims in Ernakulam.
4. To estimate its effect on the entrepreneurial ability of the Muslims
5. To analyse the attitude of the Islamic community towards interest free financial institutions.

Methodology

This study falls under the purview of Islamic Economics. Since the study attempts to trace the differences between interest free financial institutions and commercial banking and also to analyse how the present system of banking affects the saving and investment pattern of the Muslims, extensive literature review of the theories and principles binding interest free banking, and commercial banking have been made. .

This study was conducted in three different districts of Kerala –Ernakulam, Malappuram and Kozhikode. Both primary and secondary data is used for the analysis. Simple random sampling method was used for data collection. These districts are thickly populated with Muslims. 30 Muslim households are selected as sample for the study from each district. Simple averages and percentages method are used for the analysis.

Relevance of the study

The following factors indicate to the relevance of the study

Potential population-Muslims are the second biggest community in the state.

Leadership-The community is led by very capable political and religious leadership which has paved the way for their prosperity in comparison to their counterparts in other states of India. Several groups run schools and colleges in a systematic and organised manner. Institutions of higher religious learning can provide the intellectual backing required for the research and development of Islamic banking concepts.

Funds-Finally, there is no dearth of funds as Muslims in Kerala are relatively wealthier than other community in the country having higher standard of living. People presently prefer to put their money in gold and real estate that need not always be wise as productive channel of investment. These factors throw light on the study of an alternative system of banking called Islamic banking or interest free banking.

Findings

One of the main selling points of Islamic banking, at least in theory is that unlike conventional banking, it is concerned about the viability of the project and the profitability of the operation but not the size of the collateral. Good projects with lack of finance would be financed by Islamic finance on a profit loss sharing basis. In this way Islamic banking stimulates economic development. These banks are expected to be more enterprising than conventional banks. Islamic banking has been concentrating on short term trade finance which is the least risky. Long term financing requires expertise which is not always available. Another reason is that there is no back up institutional structures such as secondary capital markets for Islamic financial instruments.

From the analysis it is clear that 36.7% of the sample belong to the income group of 20000-30000. 32.2% of them are from the income group 10000-20000. Only 14.4% falls in the income group between 30000-40000 and 6.7% have a monthly income above 40000.

The study results regarding the educational status of the respondents shows that 25.5% of the respondents have education up to higher secondary level. 23.3% have an educational status of matriculation. 20% of them have only high school level education. 15.5% are degree holders and only 8.9% have PG level education. 6.7% of them have technical education.

The employment of the selected sample is very important. It is clear from the table that majority of the respondents are in the business sector i.e. 35.6%, followed by NRI with 27.8%. A large percentage of our migrant labourers are from the Muslim community. Only 15.6% of the sample has government jobs and 21.1% belongs to the private sector.

It is clear from the study that the religious principles regarding finance prohibit Muslims from the acceptance and giving of interest. Because of this they spent a large portion of their income on unproductive purposes. In Kerala an alternative system of finance is not widespread. Therefore they are compelled to go for various financial avenues prevalent in Kerala. The preference of the selected sample for various saving/investment avenues shows that 88% of them prefer gold as a suitable way for investment. 84.4% of the sample has bank accounts, 71.1% prefer chitty, 64.4% prefer LIC/Insurance and 47.8% prefer post office savings. Only 14.4% like to invest in KSE and 4.4% in Mutual funds.

Regarding the purpose of savings the study reveals that 74.4% of the sample saves for the education of their children. 62.2% of them save for the marriage of their children. 51.1% for

home construction and 41.1 for purchasing household items. Only 26.7 % of the people save to earn interest. A major portion of their saving is spent for marriage of their children.

The different factors which affect the saving/investment behaviour of the people include, monthly income, seasonal changes in income, diseases, children's education, debt, precautionary purpose etc. The most important factor which influences the saving habits of the people is their income. Here saving behavior of 90% of the sample is influenced by their income.75.6% of the sample saves to meet unexpected expenditures, 35.6 % saves to pay off their debts. 20% of them save for other purposes which includes the security of their old age

The study reveals that. 43.3% of the people save less than 10% of their income.26% of the people do not have saving at all The main reason for this is that they are reluctant to receive interest rate.13.3% saves 10%-15% of their income. Only 4.4% of the people save 20-25% of their income.3.3% save more than 25% of their income

The frequency of saving of the respondents shows that 57.7% of the respondents have daily saving habit.50%save monthly and 41.1 %save quarterly. The number of respondents who save annually and half yearly are very less, 13.8 and 17.8 respectively.

As the respondents belong to a particular community Muslim they are aware about the various principles followed by their religion. Their religious study helps in understanding it very clearly. The source of information of the respondents regarding various avenues of savings show that 58.9% of them got information from their relatives.40% of them receives information from their friends. Magazines, newspapers and internet etc. are other sources of information.

The study enquired about the awareness of the respondents about Islamic Banking.74.4% of the respondents are aware about the operation of interest free banking and 25.6% are not aware of

Interest free banking. Majority of them got information on the principles of finance from their religious study.

Sources of information about interest free banking shows that 60% of them got idea about Islamic banking from their relatives. 57.8% got information from different magazines on finance. They undergo religious education along with normal education. They got information regarding different Islamic principles and banking through it. 45.6% of them got information from these institutions.

As there is no active banking system as prescribed by the Islamic principles, it is necessary to know the necessity of Islamic banking in Kerala. As they know the religious principles regarding the prohibition of interest, they all respond positively to the materialization of Islamic Banking. About 53.3% of them highly agree with this, 25.6% agree, 11.1% are neutral in their opinion and only less than 10% disagree

Conclusion

Nowadays a broader array of issues are being analysed, including the link between Islamic banking and financial and economic development, the diffusion of Islamic banking, the role of Shariá Supervisory Boards and governance issues, the impact of religious and financial screening on fund performance, and comparisons of Shariá screening with other types of investment filtering – like those for socially responsible or environment friendly investments. Much of the governance work is in its infancy, as is the analysis of Sukuk and related instruments. In the banking area there still needs to be work done on examining systemic risks and seeing how this links to Islamic and conventional banking. Also, (as in the conventional empirical banking literature) more work is needed on the features and links between liquidity and market funding

risks. There is room for more work to be done on pricing too-big to fail and other government safety net subsidies in Islamic banking systems, as well as (hypothetical) stress testing of banks in Muslim countries