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# Social History of Islamic Banking and First Example: Bank-I Awqāf

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**Abstract**

*The cash waqf was a unique category of Islamic endowment that played a significant role in the economic and financial history of the Ottoman Empire. It can be considered an important Islamic financial institution that facilitated the flow of funds from those who could save to those who needed capital, primarily entrepreneurs and the general public. This institution is regarded as one of the most notable contributions of the Ottoman Empire to Islamic civilization. Ottoman scholars have been discussing Islamic banking since the era of Suleiman the Magnificent (1574). In the Ottoman state, Islamic banking was referred to as Mu'amalah al-Shar'iyyah, commonly known as murâbahah. The Ottoman state established the "Awariḍ Akcasi Sandiklari," meaning "The Box of Waqf Money." Scholars preferred practices such as mudaraba, murâbahah, and qarḍ. This tradition continued with the establishment of the Awqaf Bank in 1914. On 3 Jamaziyalawwal 1332 (1914), the Ottoman Ministry of Awqaf decided to establish the first Islamic bank, Bank-i Ewqaf, with its central branch in Istanbul and potential new branches across all provinces. The bank operated entirely under Mu'amalah al-Shar'iyyah, or simply murâbahah, and was authorized to issue bonds, certificates, and facilitate money transfers, among other activities.*
Keywords: *Bank-i Ewqaf, Cash Waqf, Islamic Banking, Murâbahah, Ottoman Empire*

## INTRODUCTION

The cash *waqf* constituted a special category of Islamic endowments and played a major role in Ottoman economic/financial history (Akgunduz, A. (Ed.). 2009). As such, it can be considered to be an important Islamic financial institution that facilitated the flow of funds from those who were able to save to those who needed capital, i.e., primarily entrepreneurs as well as the general public. This institution is also considered to be one of the most significant Ottoman contributions to Islamic civilization.

The cash *waqf* was basically the establishment of a trust with cash whose return could be utilized to serve humankind in the name of God (Ab Rahman, M. F., Abdullah Thaidi, H. A., Mohamad Suhaimi, F., & Ab Rahim, S. F. 2024). These endowments were approved by the Ottoman courts as early as the beginning of the 15th century and, by the end of the 16th, had become extremely popular all over Anatolia and the European provinces of the empire. Yet they found little, if any, application in the Arab provinces. In a society where health, education and welfare

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were financed entirely by gifts and endowments the cash *waqfs* carried serious implications for the very survival of the Ottoman social structure. Moreover, they were also instrumental in the emergence of a legally sanctioned and well-developed money market.

Archival documents support the view that *murâbahah* was used as a general expression meaning profitability. Accordingly, a cash *waqf* was founded with a capital of 5000 akchas. The *murâbahah* of the *waqf* was stated as 2000 akchas, thus indicating a return rate of 40%. Clearly, such a high rate of return could have been earned only through profit sharing. Here, therefore, we have more evidence that *murâbahah* was used as a general expression meaning profitability and could refer to other financial instruments such as *mudarabah* or *musharakah.*

Ottoman scholars have been discussing Islamic Banking since Suleiman the Magnificent (1574) (Islahi, A. A. 2018). Islamic Banking was known in the Ottoman state as *Mu'amalah al-Shar'iyyah*, which we can simply call *murâbahah*. The Ottoman state established the "Avariz Akcasi Sandiklari," which means "The Box of *Waqf* Money." Ottoman scholars preferred *mudaraba* and, *murâbahah* or Q*ardh*. This practice continued with the Awqaf Bank in 1914.

Early scholarly work on this subject in the modern period appeared from the 1940s through the 1960s in Urdu, Arabic and English. The focus was not banking and finance in the narrow sense but the economic system as a whole. The writer would, generally speaking, criticize capitalism and socialism and then proceed to outline a system based on Islamic injunctions relating to moderation in consumption, helping the poor, encouragement of economic enterprises, avoidance of waste, justice and fairness, etc. The poor tax, *zakat*, and prohibition against interest would be emphasized in this context, and it would be argued that Muslims should not adopt the conventional system of money, banking and finance blindly. They must purge it of the prohibited interest and modify it to suit the just and poor-friendly economic system of Islam. Some of these writers went beyond generalities and suggested that the early Islamic contracts provided sound bases for restructuring banking so that it would be free of interest and serve the goals of Islam. The youngest Islamic country, Pakistan, made the commitment to abolish *ribâ* part of its constitution.

Professional Muslim economists as well as *sharî'a* scholars made significant contributions to the subject so that, by the end of 1960s, some kind of a blueprint of Islamic banking was available. Bankers and businessmen had also joined the task of evolving a workable model since efforts were being made in several Muslim countries to put the idea into practice. The political conditions in Arab countries were not favorable for any initiative at the state level, but private practical initiatives had a greater chance of mobilizing the monies needed for such a venture in these countries, as we shall see when tracing the history of the practice of Islamic banking.

The earliest theoretical model was based on the two-tier *mudaraba*, profit sharing replacing interest in bank-depositor as well as bank-borrower relationships. Islamic banks would be financial intermediaries, like conventional commercial banks, except that interest would be purged from all their operations and they would rely on partnerships and profit sharing instead. They could operate demand deposits like their conventional counterparts and offer other services for fees like other banks. Banks doing business directly with and entering the real estate market to make profit for their depositors and shareholders (partners) were not part of this model.

The rumors that Islam's prohibition of interest was violated through some monetary endowments and Islamic banking experience in the ottoman state

Among the Islamic schools, with the exception of the Hanafi school, the Maliki school has an absolutely reliable view about monetary endowments. The Shafiis and Hanbalis accept it as valid but there are conflicts among their scholars. Nonetheless, we know that there happen to be different opinions in the Hanafi school regarding movable endowments and that cash endowments were usually included in the group of "the movables the endowments whereof are accepted conventionally.

The issue of cash endowments, which is mentioned as a minute issue in *fiqh* (Islamic jurisprudence) in books on this subject, gained importance in the Ottoman application because of the following facts. For a long time the Ottoman jurists and Shaikhulislams disputed the permissibility of cash endowments, and the system of *Mu'amalah al-Shar'iyyah* (*Sharî'a* Transactions), a method for the management of endowments' money and a practice of Islamic banking, was closely related to the issue of "interest" that had been banned by Islam. For these and similar reasons, this issue of cash endowments became one of the most important issues of the Endowments' Legislation.

Unfortunately, research on this subject was carried out during the Republican period, and only one side of the issue – its relation to interest – has been studied. Furthermore, certain interpretations – which might be regarded as incorrect – have been made due to the incognizance of cash endowments in Islamic Law. These factors, however, have actually increased the importance of research in this field. Although how endowments' money was managed was not uniquely a matter of *Mu'amalah al-Shar'iyyah*, in Ottoman practice and in the opinions of those Hanafi jurists who viewed it as permissible, the other methods were neglected and – we do not know why – this single view has never been elaborated upon.

As far as we can understand from major references, it was likely to profit from the endowments' money in three ways: first, by establishing a company of *mudarabah*, whereby the profit to be gained could be given away as charity; second, it could be given to the poor and to those to whom it was allocated as trade capital, viz. given as credit; third, profit was gained in the way known as *Mu'amalah al-Shar'iyyah* in the Ottoman application (*istirbah*), whereby the profit and the income to be gained was distributed to the needy. Research has focused solely on the above-mentioned third method and posited a strange allegation that the Ottoman state deemed interest permissible in its entirety. Although the exploitation of a *sharî'a* aspect and the acceptance that there were certain – though few – abuses and defects in application, as was stated by the imam of Birgivi, support the aforementioned allegations, it is out of the question that the Ottoman state applied interest.

*Mu'amalah al-Shar'iyyah* (*Sharî'a* Transaction) was the most noteworthy of those methods of managing endowments' money observed in the Ottoman application. The income gained that way was called *ribh* (profit), *nama* (income); giving money to earn an income *istirbah* (giving money for management to gain a profit) and *istighlal* (earning income) and the method of management *Mu'amalah al-Shar'iyyah* (*Sharî'a* Transaction) and *Murabaha al-Mar'iyya*h or merely *Mu'amalah* (Transaction) and *Murâbaha*.

The legal basis of the management system of the endowments' money, which was called *Mu'amalah al-Shar'iyyah*, was a sort of sale contract known as *Bai'al-Inah* in Islamic law. Let us first explore that sale contract and its decree. In the *Bai' al-Inah* system, after a commodity had been sold by installments and delivered to the purchaser, it was repurchased from him but at a lower price. For example, if a commodity was sold to **A** for TL (Turkish lira) 5,000,000,000 on credit and repurchased from **A** for TL 4,000,000,000 TL before he paid for it, that would be *Bai' al-Inah***.** There could be various forms of that method of selling. The important thing here is that a commodity is purchased on credit and sold in cash with the objective of finding a loan and thus earning the capital holder some extra money. What really matters to us is the legality of such a sale contract; further information on the varieties of this will be given below.

While the legists of the Shafii school opined that that kind of contract is permissible, those of the Maliki school, the majority of the Hanafi, and those of the Hanbali schools, decided that it was not. *Bai' al-Inah* was adopted by Ottoman jurists – owing to the current economic requirements, the pressures of the public customs and traditions as well as with a view to not closing the gates of charity – as a system for managing the endowments' money in the above-mentioned manner. Since it had been adopted and applied in the form that had been brought into conformity with

*Shar'-i Sharif* by the other legists even before Abussuud, it was called *Mu'amalah al-Shar'iyyah* (*Sharî'a* Transaction). In effect, that transaction had always been known as a legal remedy for avoiding interest since the Prophet Muhammad and had actually been adopted by the Shafiis in its entirety. Not every *hilah al-Shar'iyyah* (canonical device for including an apparently illegal purpose) necessarily entails a trick or ruse. Moreover, *hilah al-Shar'iyyah* should not be confused with "legal tricks" either. While it is possible to share the opinion that the transaction had been abused, it would be absolutely wrong to claim that it was completely a form of interest, leaving aside interpreting *ribh* (profit) as interest or *istirbah* (lending money) as giving for the sake of interest.

The allegations of some researchers that interest was allowed and applied in the Ottoman state have been refuted through specific decrees in the Ottoman legal codes, e.g. the decree in the general legislation of Sultan Selim the Excellent, who was given the title of *Adil* (the Just) by virtue of his just character, is a manifest proof of this. Yet presenting *Bai' al-Inah* or *Muamalah al-Shar'iyyah* as it was called in the Ottoman legal codes and was regarded as permissible by certain Islamic jurists as interest would entail ignorance of the subject. An article for Yawuz Sultan Salem Legal Code: **"**It is not allowed for *Mu'amala-i Shar'iyyah* if the rate of benefit does not exceed 10% and it must not be allowed for the sake of interest (*Ribâ*) via *Mu'a-mala-i Shar'iyyah."*

## RESULTS AND DISCUSSION

### The History of Islamic Banking 1960-1979

Applications and practices in finance based on Islamic principles began in Egypt and Malaysia. The landmark events include the rise and fall of the *Mitghamr* (Egypt) Saving Associations during the 1961–1964 period and the establishment of Malaysia's *Tabung Haji* in 1962 (Khoshroo, S. 2018). *Tabung Haji* has since flourished and has become the oldest Islamic financial institution in modern times. Operational mechanisms for institutions offering Islamic financial services (IIFS) began to be proposed and a number of books on Islamic banking based on profit and loss sharing and leasing were published.

The first modern experiment with Islamic banking was undertaken in Egypt in a covert way without projecting an Islamic image – for fear of being seen as a manifestation of the Islamic fundamentalism that was anathema to the political regime. The pioneering effort, led by Ahmad El Najjar, took the form of a savings bank based on profit sharing in the Egyptian town of Mit Ghamr in 1963 (Orhan, Z. H., & Kavakcı, S. 2024). This experiment lasted until 1967, at which time there were nine such banks in the country.

Islamic banks emerged with the establishment in 1975 of the Dubai Islamic Bank and the Islamic Development Bank (IDB). *Fiqhi* objections to conventional insurance also became pronounced in 1975, laying the groundwork for an alternative structure. Financial *murâbahah* was developed as the core mechanism for the investment of Islamic banks' funds. Academic activities were launched with the first International Conference on Islamic Economics, held in Makkah in 1976. The first specialized research institution – the Centre for Research in Islamic Economics – was established by the King Abdul Aziz University in Jeddah in 1978. The first *takaful* company was established in 1979.

**History of Islamic Banking 1980-1999: Islamic Banking at the State Level**

During the 1980s, the subject of Islamic banking and finance received wide academic and professional attention. A number of Muslim countries began considering the implementation of the idea officially and appointed expert bodies to work out the details. Several universities started teaching the subject and encouraged research, resulting in hundreds of Ph.D. dissertations, some of them in universities in Europe and America. Numerous seminars and conferences drew attention to the subject in places as diverse as Kuala Lumpur, Dhaka, Islamabad, Bahrain, Jeddah, Cairo, Khartoum, Sokoto (Nigeria), Tunis, Geneva, London and New York. A number of research centers made Islamic economics their field, paying special attention to money and banking. Some of these launched academic journals providing forums for the exchange of views and dissemination of information on a worldwide scale.

More Islamic banks and academic institutions emerged in several countries. Pakistan, Iran and Sudan announced their intention to make their general financial systems comply with *sharî'a* rules and principles (Jeeva, S. 2020). The governors of central banks and the monetary authorities of the Organization of Islamic Conference (OIC) member countries, in their fourth meeting held in Khartoum on 7–8 March 1981, called jointly for the first time for strengthened regulation and supervision of IIFS. The Islamic Research and Training Institute (IRTI) was established by the IDB in 1981. In 1980, Pakistan passed legislation to establish *mudarabah* companies. Other countries such as Malaysia, Turkey and Bahrain initiated Islamic banking within the framework of the existing system. The International Monetary Fund (IMF) published working papers and articles on Islamic banking, while Ph.D. dissertations and other publications on Islamic banking were on the rise in the West.

The OIC *Fiqh* Academy and other *Fiqh* boards of IIFS engaged in discussions and review of financial transactions. Islamic mutual funds and other non-banking financial institutions emerged towards the middle of the 1980s.

Local Islamic banks formed in the 1970s in Muslim countries like Malaysia, Pakistan and Dubai were originally emphasized as joint venture structures akin to private equity (Hanieh, A. 2020). These quickly evolved to provide short-term credit facilities by using the *murâbahah* structure. In 1983 a new law was passed in Turkey on interest-free banking and two institutions were established: Faisal Bank and Al-Barakah.

Public policy interest in the Islamic financial system grew in several countries. The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) was established and its first standards were issued (Mohammed, N. F., Mohd Fahmi, F., & Ahmad, A. E. (2019). The development of Islamic banking products intensified. Interest in Islamic finance increased in Western academic circles, and the Harvard Islamic Finance Forum was established. Large international conventional banks started operating Islamic windows (Henry, C. (Ed.). 2019). The Dow Jones and Financial Times Islamic indexes were launched. Systemic concerns and regulation, supervision and risk management issues gathered momentum. Several countries introduced legislation to facilitate Islamic banking and its regulation and supervision. Commercial event organizers discovered Islamic banking and finance activities as a source of lucrative business.

With increases in scale, Islamic banks began to branch out to more complex financing schemes, including: retail banking, including accepting deposits and consumer lending, bonds (*sukûk*), medium- and long-term leases *(ijâra)* (Arabi, A. (2008) (Arabi, A. 2008).

**The History of Islamic Banking 2000-2007**

Islamic banks and academic institutions emerged between 2000 and 2007 in several countries. Pakistan, Iran and Sudan announced their intention to make their general financial systems comply with *sharî'a* rules and principles. From 2000 to 2006 sovereign and corporate *sukûk* as alternatives to conventional bonds emerged and increased rapidly in volume. Bahrain issued financial trust laws.

The perception of a hostile climate in many Western jurisdictions, in particular, the United States, led to the repatriation of dollars by Arab investors to Middle Eastern banks.

Islamic banks, along with conventional banks in the region, benefited from this reverse flight of capital. The increase in oil prices led to a dramatic increase in liquidity in the Gulf (El-Beblawi, H. (2019).

International Islamic financial infrastructure institutions such as the Islamic Financial Services Board (IFSB), International Islamic Financial Market (IIFM), (General) Council for Islamic Banks and Financial Institutions (CIBAFI) and the

Arbitration and Reconciliation Centre for Islamic Financial Institutions (ARCIFI), as well as other commercial support institutions such as the International Islamic Rating Agency (IIRA) and the Liquidity Management Centre (LMC), were established. The systemic importance of Islamic banks and financial institutions has been recognized in several jurisdictions. The governments of the United Kingdom and Singapore extended tax neutrality to Islamic financial services (PY Lai, K., & Samers, M. (2017). Conventional Banks Open "Islamic Windows": Conventional banks began to respond to requests from Muslim clients to offer products that complied with Islamic law; As the size of the potential market became clear, conventional banks responded with the creation of divisions dedicated to Islamic banking

Almost all regional banks have followed international banks in creating "Islamic" windows and some have converted or are in the process of converting to the Islamic banking model.

**The Islamic Development Bank**

The Organization of Islamic Conference (OIC) took several steps culminating in the establishment of a bank of Islamic countries that would serve the entire Muslim *ummah* (community of the faithful). Share capital, initially fixed at two billion dollars US was supplied by member countries, the largest amount coming from Saudi Arabia, Kuwait, Libya, the United Arab Emirates and Iran. It started operations in 1975 with its headquarters in Jeddah, Saudi Arabia. Clause One of its charter states that it was "*to foster economic development and social progress of member countries and Muslim communities individually as well as jointly in accordance with the principles of shari'ah*." (Marboe, I. 2013, Muhammadin, F., & Sholihah, F. 2016).

By the year 2000 the Islamic Development Bank (IDB) had financed inter-Islamic trade to the tune of over 8 billion USD, primarily using the markup technique. It also gives loans, charging only for services in accordance with actual administrative expenditures. But it does try to promote sharing-based methods of financing. It also manages an investment portfolio in which individual Islamic banks place their surplus liquidity. Even though it cannot, and does not aspire to serving as a lender of last resort for all Islamic banks, it is trying to help them solve their liquidity problems. It fosters technical cooperation between member countries and has established or sponsored a number of institutions for this purpose. The Islamic Chamber of Commerce and the Islamic Foundation for Science, Technology and Development are two of these (Saad, N. M., Kassim, S., & Hamid, Z. (2016). Cunha, J. A. C. D., Souza, L. J. D., Macau, F. R., & Alssabak, N. A. M. (2016). It also distributes scholarships for higher learning and technical education to Muslim students in countries in which Muslims are in a minority.

In order to fulfill its mission, the IDB has established the Islamic Research and Training Institute (IRTI). It conducts in-house research, sponsors external research, publishes a research journal, conducts training courses, organizes seminars and conferences and maintains a database on Islamic countries' economies, etc.

The Islamic Development Bank interacts with all regional and international financial institutions like the International Monetary Fund (IMF), the World Bank, the Asian Development Bank, etc.

## CONCLUSION

Islamic and conventional finance are converging rapidly around the world. As conventional investors become more comfortable with Islamic structures, the cost differential between Islamic and conventional products has almost disappeared. As a result, Islamic products may be more practical because they appeal to both Islamic and conventional investors. It is not too late for Dutch banks to compete for Islamic finance business. To do so successfully, they need to establish a presence in the region, as their competitors have done, and they should produce some Islamic finance products. There are about 20 million Muslims living as citizens in European countries. They have a real need for Islamic products, even from conventional banks.

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