

Customer's Awareness and Attitude Towards Interest Under Islamic Law and Shari'ah-Case of People's of Zanzibar

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Abstract: The main aim of this study was to determine the influence of consumers' awareness and attitude toward interest under Islamic law and Shari'ah. The study used a target population of peoples of Zanzibar which was a majority Muslim by 99 percent. A descriptive design was adopted in this study for data collection. The descriptive design allows the description of the state of affairs as it exists and draws respondents' opinions and views on the influence of the consumer awareness toward prohibited of interest in Islam. The study found out that 68.9 percent of the respondents were aware the interest is one of the dangerous weapons to exploit and extort the poor and needy. We recommended that in order achieve certain economic and social goals, central banks have intervened in the determination of the rate of interest and establish of an interest free banking system because the most important portion of the wealth of a country is captured by a few rich peoples through interest.

Keywords: Islamic banking, Islamic financial Institutions, Interest rate, Customer awareness, Conventional banking, and Microfinancial Institutions

INTRODUCTION

Banking industry is one of the major service sectors in Tanzania that engage in the use of ICT facilities in its operations. According to the Bank of Tanzania up to 7th November 2014, the banking industry in Tanzania consists of 34 banks, 2 development banks and 20 non-bank financial institutions [6]. Out of the 34 banks, three (3) were in existence prior to the liberalization and the remaining banks emerged after trade liberalization in 1986, and especially after the formal financial sector reforms started effectively in 1991 when the Banking and Financial Institution Act was endorsed by the legislature. Banks and other financial intermediaries are gaining additional advantage in modern micro finance programmes so that the greatest contribution of profit oriented institutions in the micro finance market may have both constructive effects, in terms of effectiveness and sustainability, and negative effects, in terms of ethically. Thus, the role of banks and financial intermediaries in modern micro finance must tie in with the aim of maximizing the positive effects, while minimizing the negative ones. In this situation, those micro finance programmes supporting single projects, investing in the share capital of MFIs/bank. In addition, they are able to carry out the credit decision-making process and in particular, the assessment of the beneficiaries' credit worthiness. Their capability in this field would assist to achieve a higher economy of scale,

particularly for those programmes that aim to benefit a large number of clientele.

Islamic finance is growing rapidly, with growth rates reported at least twice as high as those recorded on global conventional financial markets¹. Much of the focus of activity had been in the Middle East and South and South-East Asia, where Islamic finance had gained currency rapidly to meet the growing interest in domestic market there. More recently, there has also been considerable growth of Islamic finance in the regions beyond its historical boundaries and increasing cross-border Islamic activity². In addition to that, Islamic banks now have significant market capitalization both globally and in their domestic markets³. Islamic banking activity in international financial centres is growing, with new full-fledged Islamic banks having been established in London and Singapore in the last few years. Now a day's Islamic banking attracts sovereigns, financial institutions, multinational, corporate entities and customers across the retail spectrum who seek to take advantage of Islamic liquidity for financing, spanning

¹ Moody's (April 2008), "Islamic Banks and Sukuk (Islamic Debt Securities): Growing Fast, but Still Fragmented", Moody's Investors Service.

² Standard and poor's (23 April 2007), "Chief Driver behind Islamic Finance's Global Expansion", *Islamic Finance Outlook 2008*.

³ McKinsey (2007-08), World Islamic Banking Competitiveness Report 2007-08.

the spectrum of corporate, retail, acquisition, development, project financing, and international capital market offerings [17]. The Islamic banking is guided by Shari'ah⁴ principles and has the same principles as conventional banking such as, to make money intended for the banking institute by means of lending out capital, faithfulness to Islamic law as well as ensuring the central part of Islamic banking. The elementary law of Islamic financial institutions is founded under scheduled prospect allotment which is a constituent of trade toward an assured coverage further than threat transmit within the conservative banks. Islamic financial institutions such as banks called earning's allotment (*Mudharabah*), protection (*Wadiah*), joint venture (*Musharakah*), cost added to (*Murabahah*), and rental (*Ijar*) [9].

Under Islamic law mortgage contract, as a replacement for lending the buyer money to procure the thing, a bank might procure the thing itself from the vendor, and re-sell it to the consumer at a profit, at the same time allowing the consumer to reimburse the bank in instalments. The asset is recorded with the person's name (customer) at the beginning of commencement of the contract. This agreement is called *Murabahah*. Another alternative is *Eljara WA Elqtina*, which is comparable to valid land leasing [1]. *Musharakah al-Mutanaqisa* is the modern arrangement where certain banking uses the habitat loan to accept a buoyant fee in the structure of leasing. The bank and customer form a joint venture creature; both provided that capital as an agreed percentage to acquire the possessions. The joint venture unit at that time rents away the possessions to defaulter and takes rental fee. The financial institution and the defaulter resolve subsequently contribute to the profits from this rent based on the present equity share of the joint venture. At the similar time, the borrower in the joint venture unit if they fail to pay, both the bank and the borrower take rescue of the percentage of the profits from the sale of the possessions based on every party's current equity [7]. There are a number of other approaches used by business transactions. Islamic banks give somebody the loan of their money in the direction of issuing floating rate. The floating charge of absorption is the way the company's personage charge of return. As a result, the bank's turnover on the credit is the same to a definite proportion of the company's returns, once the credit is disbursed. This situation is called *Musharakah*. Another aspect is *Mudharabah* which is venture capital financial support of an industrialist who provides labour at the same time as financing is provided through the bank as a result that both profit and risk are shared [9]. The arrangements between capital and labour under Islamic views reflect that the borrower should not require abiding all the risk/cost of a failure, the important at this point are

disinterested sharing of revenue. In addition to that, the borrower is allowed to dominate the financial system. Under Islamic law, all financial institutions which operate under the umbrella of Islamic system, it is prohibited for them to accept any transactions which involve in any kind of interest, speculation, or gambling also its prohibited to any investment sectors deals on (alcohol, armaments, financial services, pork, pornography and tobacco) e.t.c, any investment instrument e.g. (no forward transactions, limited option use, short selling, no derivative, credit and dept product are not encouraged). The main reasons are to keep in simply decent investing, and ethical purchase. In presumption, Islamic banking is an instance of overflowing requirement of financial institutions, especially banks; accomplish a 100% diffidence relative amount. Conversely, in a normal situation it's difficult to exit a financial institution like a bank which has 100% reserve [7].

LITERATURE REVIEW

Principle of Riba (Usury or Interest)

Interest is already known to be the main issue discussed in comparing operations of an Islamic Bank and Conventional Bank. Profits of conventional banks are generated from the different interests on loans and interest on deposits which clearly involve riba. Wealth from Islamic perspective should be created through commerce and trading within the framework outlined in the Quran. Profit maximization of conventional banks is not limited to any means; it uses public funds to maximize revenue. Thus, a conventional bank could be involved in a business that optimizes the wealth of the bank despite causing ill effects to the public [17]. Islamic banks take into consideration the social implications that may be brought about by any decision or action taken by the bank. They are responsible for holding customer savings while trying to achieve the socioeconomic prosperity of the Ummah. On the other hand, interest applied by a conventional bank is identified as the fountain-head of economic evil and is largely responsible for the concentration of wealth in a few hands; furthermore, the attainment of profit at any cost is not one of the Islamic banking performance criteria. Islamic banks need to match the material and social objectives that will serve the interests of the community as a whole and help achieve the development of the society. Among the social responsibilities which distinguish Islamic banking from conventional banks are as follows:-

- Islamic banks encourage savings, particularly among those who are not willing to deal with the conventional banks, irrespective of their income. So savings can be channelled for the interest of the community, instead of being diverted from economic and social causes within the community, and try in their level best to restrict the dominance of the few, by providing the opportunity for many producers to get financing using techniques which are permitted by Shari'ah; hence in this way, the

⁴ Shari'ah: It is used to refer both to the Islamic system of law and the totality of the Islamic way of life. (<http://www.religioustolerance.org>, 2014).

banks may succeed in bringing social justice to all the parties concerned.

- Another important feature of Islamic banks is to give priority to investments- whether in the form of full ownership or joint ventures- in the field that would help solve the problems of the community. A distinguishing characteristic of Islamic banking system called *zakkat* (alms duty), and the bank promotes its resources and the distribution of *zakkat* as prescribed by Allah (God) and the Sunnah of the Prophet (pbuh). Meanwhile, the Islamic banks also provide *qardh al-Hassan* (benevolent loans) (as discussed later), to restore life to the Islamic concept of social justice and cooperation. These loans are free of interest and any other burden [17].

The main purpose of establishing an Islamic banking system is to avoid *riba* and to apply Shari'ah principles in their cooperation. Moreover, the fundamental principles of Islamic banking rest on the doctrine of *riba*. Literally the word *riba* means an increase or excess (*ziyyadah*). According to the more concise Encyclopedia of Islamic, *riba* literally means increase. In technical terms, it is known as usury or interest. In general, it is any unjustified increase of capital for which no compensation is given. Another issue concerning *riba* which is also prescribed in the Islamic Holy constitution is the condition of exchange- either in commodities or money. Each commodity has to be exchanged by the same amount if it is of the same type, for instance gold has to be exactly exchanged with gold in the same weight and measure, and any surplus is *riba*. Islamic law and Shari'ah strictly prohibits and condemns any predetermined, fixed increase or charge earned as a result of allowing the use of one's money by another. Thus, it is clearly stated that interest is harmful and repeated in the Quran verses (30:39, 4:160~161, 3:130~131), and also in the hadith of Ubadah Ibn al says "*Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, salt for salt exactly equivalent for equivalent, hand-to-hand*". You are free to trade objects as long as they are differing and are traded hand-to-hand [14].

Conventional Micro Finance

Under conventional Micro Financial Institutions within the present dominant economic system, there are a number of serious market failures that cannot be resolved without external intervention. One such failure is the inability of the prevailing credit system to satisfy loan demands from segments of the population that cannot access formal credit channels or do not have sufficient collateral against which they can borrow [2]. These assemblages universally known as "non depository" not only include the poor, but also would be entrepreneurs with projects or ideas with potentially high rates of return. A solution to this market failure comes in the form of Grameen Bank (GB), which comprises and endures an exceptional

achievement from the time of its establishment in the mid-1970s. Information economics, developed by Joseph Stieglitz, explains that informational problems underlie many failures of the market system. In particular, the credit market failures are due to the fact that the information collection as well as analysis is an important outlay, designed for the Financial Intermediaries (FI) such as (banks), making it expensive to collect and analyze the necessary information and to decide whether to extend a loan, and then examine the performance of the customer-borrower on the way to guarantee fulfillment through loan's terms and conditions as well as its repayment [2]. Conditions in succession expenses besides individual elevated, financial intermediaries extend loans only to those clients who keep a good credit record and/or high valued collateral to make defaults costly. Essentially this is the concept of asymmetric in sequence, so as the borrower may have information regarding the project's purpose and chance of success that the lender lacks. This, in turn, leads to problems of adverse selection (the banker-lenders may perhaps make a decision in the direction of expanding mortgage toward precarious borrowers-customers excited to reimburse higher significant charge) or ethical risk problems (the borrower will use the proceeds for purposes other than stated or with the intention of defaulting) [12].

Micro finance bank deal with these problems by resorting to group lending, in its original conception (Grameen Bank 1), no collateral is required and only the poor can borrow, but each client has to be an affiliate of a five individual assembly with the purpose of revolving, belongs to eight groups (a total of 40) "centre" within a village. While the loans could be granted to individuals within the groups for their own independent project, failure to repay the loan could lead to combine retribution that the whole five affiliate assembly loses its membership in the bank. While there is rejection of unambiguous obligation intended for the assemblage toward a loan defaulted by one of its members, implicitly there is a strong intention of the group to do so if it wants to regain its membership. MF banks' interest rates have been in the range of 20% to 30%. This approach of lending to close-knit group of borrowers resolves both informational problems of adverse selection and moral hazard by shifting the cost of *ex ante* selection of the right borrowers (those with low probability of default) and the responsibility for monitoring the borrower's behaviour of the group. Despite the fact that Grameen 2 adapted various facial appearances of Grameen I, the essential constitution of the previous adaptation of Micro finance bank is retained in that reliance is still placed on the reputation of borrowers with group familiarity with each client, interest rates is still as high as 30%, and the ultimate of this establishment is toward development into flourishing profitable depositories. Under Islamic solution- *qard-ul-hassan* to credit market failure to

serve the target groups is substantially different from the prevailing Micro Finance bank approach [5].

The Islamic Solution (Qardh-Ul-Hassan)

Qard-ul-hassan (QH) is a voluntary loan without the lenders' expectation of any payback principal. Furthermore, at the same time the borrower has an obligation to return the principal, the lender is urged, according to a number of the sayings of the Prophet (pbuh), not to press the debtor if he/she is unable to repay at the specified deadline. For example, verses (2:245, 5:12, 11:57 18:57, 17:64 and 20:73) in the Quran explain in detail about those issues [5].

The term *Qard-ul-hassan* (QH) means "beautiful loan" because the *Qur'an* asserts that these loans are made to (God)-Allah (swt) rather than to the borrower, intending to ease the pain of "tearing away" part of one's wealth and parting with it to lend to someone in need. Hassan and Ihsan belong to the constellation of the same root. There is an illustrious proverb of the Prophet (pbuh) that when asked what Ihsan means, "to adore Allah (swt) the same as stipulation you perceive Him and be acquainted with so as to (still) stipulation you perform, He sees you". Perhaps the word Hassan, understood in the context of Ihsan, is meant to imply that only when a person assembly a mortgage in the way an important person demand, devoid of expecting something during return and only in order to please Allah (swt) will transaction is possible. The difference between QH and *sadaqah* (charity) - another way Islamic law takes steps of separation through one's prosperity toward lending a hand to the deprived, even though merely the borrower indicates the instant of compensation, although *sadaqah* is uncontaminated charitable trust [12].

(i) Prohibition of interest in the Holy Qur'an

If we explore the Holy Qur'an, we find a number of places where Allah has categorically mentioned the consequences of interest [4]. Allah says in the Holy Qur'an:

- O you who believe! Devour not interest doubled and multiplied; but fear Allah, that you may prosper. Fear the Fire, which is prepared for the disbelievers (3:130-131).
- That which you lend on interest for increase through the property of people, will have no increase with Allah: but that which you give for charity, seeking the countenance of Allah, it is these who will get recompense multiplied (30:39).
- O you who believe! Fear Allah and give up what remains of your demand for interest if you are indeed believers. If you do not, take notice of war from Allah and his Messenger: but if you repent, you shall have your capital sum: deal not unjustly, and you shall not be dealt with unjustly (2:278-279).
- Those who devour interest will not stand except as stands one whom the Satan by his touch has driven

to madness. That is because they say: "trade is like interest", but Allah has permitted trade and has forbidden interest ... Allah will deprive interest of all blessing, but will give increases of charity: for He does not love any ungrateful sinner (2:275-276).

- That they took interest, though they were forbidden; and they devoured people's wealth wrongfully: We have prepared for those amongst them who reject faith a grievous punishment (4:161).

In the above Qur'an verses, Allah has evidently declared that the earnings based on interest are absolutely against the law and liable to be punished by God. Make a note of that any kind of interest such as simple interest, compound interest, periodic interest, commercial interest, money interest, interest al-nasiah, interest al-fadl and so on, all are prohibited in Islam [3]. In his clarification on the Holy Qur'an mentioned that interest is condemned and forbidden in the strongest possible conditions. Consequently, there can be no question about the prohibition. Due to the fact that interest occupies a central position in modern economic life, and has been considered as the life blood of the accessible financial institutions, a number of Muslim countries have also been tending to construe it in a way which is totally a different form the sympathetic of Muslim scholars throughout the last fourteen centuries and is also penetratingly in conflict with the traditions of the Prophet (pbuh) [13].

(ii) Prohibition of interest in the Hadith of the Prophet (pbuh),

In addition to the above verses of the Holy Qur'an, the Prophet also made many decisive statements about interest. For example, the following statements obviously reveal the significance of this action [14].

- The second Khalif of Islam Hazrat Umar bin Al-Khattab reported: the last of what was revealed in the Holy Qur'an was the verse of interest. The Messenger of Allah was taken to Him and he could not explain it to us. So, we should give up interest and doubt (Ibn Majah, Darimi)
- A time will certainly come over the people when none will remain who will not devour interest. If he does not devour it, its vapor will overtake him (Ahmad, Abu Dawood, Nasai, and Ibn Majah)
- Avoid the seven destructive sins: associating partners with Allah, sorcery, killing a soul which Allah has forbidden- except through due course of the law, devouring interest, devouring the wealth of orphans, fleeing when the armies meet, and slandering chaste, believing and innocent women (Bukhari and Muslim).
- The interest adopter, the interest giver, the interest accountant, and the witness of interest dealing, all

are cursed and equally defaulter (Muslim, Abu Dawood, Ibn Majah, Nasai, Ahmad).

- I came across some people in the night in which I was taken to the heavens. Their stomachs were like houses wherein there were serpents, which could be seen from the front of their stomachs. I asked: O Jibril! Who are these people? He replied, these are those who devoured interest (Ahmad, Ibn Majah)
- One coin of interest that is knowingly consumed by a person is worse to Allah than 36 acts of illegal sexual intercourse (Ahmad, Darequtni, Al-Tabarani and Al-Hakim).

(iii) Prohibition of interest in Christianity and Judaism

[8]. Islam, of course, is not the only religion that has barred interest and measured it as a dreadful practice. The ruling out of interest has also been regarded as an illegitimate and punishable practice in both Christianity and Judaism. For example, we observe the following verses from the Bible:-

- But love ye your enemies, and do well, and lend, hoping for nothing again; and your reward shall be great, and ye shall be the children of the Highest: for he is kind unto the unthankful and to the evil (Luke, 6:35).
- If you lend money to one of my people among you who is needy, do not be like a money lender; charge him no interest (Exodus 22:25)
- Do not charge your brother interest, whether on money or food or anything else that may earn interest (Deuteronomy 23:19).
- Hath given forth upon interest, and hath taken increase: shall he then live? He shall not live: he hath done all these abominations; he shall surely die; his blood shall be upon him (Ezekiel 18:13).
- Do not take interest of any kind from him, but fear you're Allah, so that your countryman may continue to live among you (Leviticus 25:36).

On the other hand, the Torah and Talmud, encourage the granting of loans but without interest. Charging interest has been considered as worst sins and has prohibited according to Jewish law. The Talmud dwells particularly on Ezekiel's disapproval of interest, where Ezekiel criticizes it as an abomination, and symbolically reveals usurers as people who have shed blood. Similarly, the untimely Christian Church associated to the New Testament, confirmed that any kind of interest was against divine law, preventing pious and outwardly religious. Christians from using capital for commercial purposes in 1179, Pope Alexander III excommunicated usurers which in that period were seen as an enormously harsh punishment [13].

RESEARCH METHODOLOGY

Study Area

Zanzibar is situated south of the Equator between latitude 5⁰ and 7⁰, in the Indian Ocean, off the coast of Mainland Tanzania. Zanzibar is located on the East African Coast, consists of two islands, Unguja and Pemba and 14 other small and isolated islets, the biggest being Tumbatu on the North–West of Unguja. Unguja is situated some 72 km North–East of Dar-es-Salaam which is the industrial and commercial capital of the United Republic of Tanzania. The Island of Pemba lies about 40 km North East of Unguja Island [11]. The total area of Zanzibar islands is 2,332sqkm, with Unguja and Pemba Island having an area of 1,464 sq km and 868 sq km respectively. The topography of Zanzibar Islands is variable. Unguja is mainly flat with a ridge the highest point 120m crossing the North-South of the Island. Pemba consists of an undulating hilly terrain. Historically, the two islands are very famous chiefly from their characterization by unpopular central role-played in the East Africa slave trade. Toward the middle of the 18th century, the islands were ruled by the Sultan of Oman, Sayyid Said bin Sultan⁵, who also made Zanzibar his commercial and financial centre. The Sultan also controlled a large part of the Eastern African coastal strip including both Kenya and the then Tanganyika. These lands were later on lost to the Germans and the British forces. In 1890, Zanzibar became a British Protectorate though the Sultan continued to control the internal affairs of the Islands [11].

The rise of nationalism in Zanzibar brought with it strong difference along racial lines. These racial differences are also reflected in the income distribution of the society. Thus, the rich class consisted of the minority Arabs, Asians and Europeans, while the majority Africans and Shirazes were poor. After a series of unrepresentative elections, on December 10, 1963 independence was finally granted to a government formed by the coalition of two political parties Zanzibar National Party (ZNP) and Zanzibar and Pemba People's Party (ZPPP). The Sultan remained as a constitutional monarch thereafter. The majority of the voters, however, were not satisfied with the manipulated elections outcome. As a result, on January 12, 1964, they overthrew the government and established a revolutionary government that was led by Honorable Abeid A. Karume [15]. On 26 April 1964, only three months after the revolution, Zanzibar united with Tanganyika to form the present United Republic of Tanzania. Administratively, Zanzibar has five regions, each of which has two districts. Each district is also sub-divided into several smaller administrative units

⁵ Sultan means a secular ruler usually in an Arab country. Zanzibar was under Sultanate system from 1832 to 1964 when Sayyid Said from Al Busaid family started to rule Zanzibar.

known as *Shehia*⁶. A Shehia can be demarcated area in urban areas, a village or collection of few villages in rural areas, with an average population of around 4,000 inhabitants [10].

Research Design

The purpose of this section is to explain what is involved in planning and conducting research projects. This will be done against the descriptions that will be given on the main approaches used by researchers. A descriptive design was adopted in this study in order to find out the extent to which the awareness and attitude of consumer's toward interest under Islamic law and Shari'ah. The descriptive design allows the description of the state of affairs as it exists and draws respondents' opinions and views on the influence of the consumer awareness toward prohibited of interest in Islamic law and Shari'ah. The research method was a case study of which the majority of peoples of Zanzibar were Muslim by 99%. The aim of adopting the case study method was to gather comprehensive, systematic and in-depth information about the lack of awareness and attitude toward interest under Islamic law and Shari'ah [18]. Argues that "the case study aims to understand the case in-depth, and in its natural setting, recognizing its complexity and its context". The intention of this research was concerned with 400 respondents of which 200 from each Island i.e. (Unguja and Pemba). These techniques are definitely used to facilitate accurate along with trustworthy information to be achieved because of appropriate information from respondents [16]. The knowledge gained from the sample is representative of the total population under study. Also, a large sample increases variation and strength of the revealed information and reliability of test's results.

RESEARCH FINDINGS AND DISCUSSION

The study sought to find out the extent to which the awareness and attitude of consumer's toward interest under Islamic law and Shari'ah. According to analysis made the overall response rates for questionnaires and interview was as high as 88.5% i.e. 354 out of 400 clients and non clients who are respondents from different MFI's were covered during data collection process, while among them another 33 respondents out of 50 were interviews which is equivalent to 66% of the respondents. From the above data, it is observed that 350 copies of questionnaires were distributed to respondents and only 321 copies were returned, which is equivalent to 91.7% while 29, copies remained in the field which is equivalent to 8.3%. The researcher could not for several times meet the respondents due to the time frame for collecting data have elapsed.

Effect of Interest Rates on Loan Performance

The economy of Tanzania meets the unfolding challenges from globalization and abject poverty among its population. These challenges require speedy transformation, including diversification of the economy with the objective of attaining high sustainable and broad based growth. Without attracting huge investments from both foreign and local sources into the economy, it would be almost impossible to meet those challenges, which are clearly stated in the Zanzibar Development Vision 2020. In order to attract repayment of the loan for those SMEs, Tanzania has undertaken a focused promotional strategy and a substantial change of the MFI policy and operational framework for small businesses in line with worldwide "best practice" standards.

The analysis show that 73 percent of clients claimed that loans were received to them without any Islamic knowledge of prohibited of interest. This implies that there are clients receiving loans without knowing any of the policies of the MFIs. One of the clients claimed that, "*she was told the procedures for obtaining and repaying the loan by her group members*". She further obtained information about MFIs' policies and procedures during the fifteen minutes through questions asked during the loan appraisal session. This shows that sometimes Credit Officers grant loans to clients just because the group members were satisfied. This has a negative impact on loan repayment. When asked about the scenario during interview, MFI staffs argued that the loan appraisal process is not detailed enough to provide sufficient information to avail credit worthiness of the loan applicants, sometimes they are overloaded with customers, short period of time to meet with customers and the level of education of their customers, that it may take the whole day to make a single client understand borrowing rules and regulations.

Effect of the Interest Rate and Supply and Demand for Loanable Funds

When taking into account the banking system and its monetary transactions, the researcher reveal that there is a higher percentage 76.4% of the respondents who argue strongly dissatisfied, while only 18.2% dissatisfied so the amount of dissatisfied is higher when compared to the satisfactions as a result the rate of interest on money at present was not depended on supply and demand for loanable funds, and thus is not the equilibrium factor. According to that we observe that in some countries, like Tanzania, Iran etc, the rate of interest is determined by the central bank. Not only that, it is mostly influenced through the open market and discount rate method. And still in others, it is influenced for pursuing other economic and social goals such as stabilization of the general price level, creating over employment, and short-term flow of resources. In many countries preferential interest rate system (i.e.

⁶ *Shehia* means ward in Tanzania Mainland. *Shehia* is governed by *Sheha* appointed by Regional Commissioner.

multiple rates) is used intend to increase investment in different sectors. But also, when you consider the positive slope of the saving curve against the rate of interest, while accepting the functional relationship of saving and national income, becomes uncertain, this means that any rise in the rate of interest causes the investment to decline and finally it turns to reduce the national income which decreases saving, and vice versa. Furthermore, there are serious doubts against interest rate and other economic objectives. For instance, the use of the interest rate for scheming inflation is no more satisfactory, for the reason that inflation regularly takes place with stagnation. The inflation happening in times of depression cannot be simply adjusted through interest rate variations, meanwhile in cases of low elasticity of demand, the excess burden of interest rate will simply fall on the final consumer. In such circumstances, the interest rate change itself into an inflationary variable. In conclusion of that in the long run, via decline in investment and production, increase in interest rate turn out to be more inflationary.

Effect of the Interest Rate and the Flow of Financial Resources

The analysis reveal that 60% of the respondent agree that the effect of the rate of interest on the flow of short-term financial has, to a large extent, been overstated. Although it is probable to influence the flow of international resources by raising the rate of interest, we should note down that, in the first stage, such a flow has a small range of performance. For example, the rise in the rate of interest, in many countries, has not engrossed more finances. Moreover, the cumulative debts have gone beyond the debt capacity of many countries.

In other side 43% of respondent argue that we know the interest is prohibited under Islamic law but we don't have other choice for taking loan to run our business because we observed the several challenges and prospects of Islamic banks operating such as:

“Lack of adequate banking law for Islamic banking; existence of unproductive money; lack of awareness; lack of operational difference between Islamic and conventional banks; Islamic banking lacks the ability to channel deposits into long-term investment; lack of experience in Islamic Shari’ah; excessive short-term financial instrument; inability to make use of Mudharabah and Musharakah financial institutions; inferior technical resources and technology; Islamic banks are compelled to recruit staff trained in traditional banking; inability to differentiate ownership from management; and lack of financial innovations”.

Another interviewees commented that:

“There is a big challenge in a bank which operate under the Islamic law such as “ financial instability, inability of the government to restore law and order in the country, resistance from the banking community, inadequate infrastructure for information

dissemination, inconsistency in policy making and implementation of the fiscal and monetary authorities, Central bank control and supervision of Islamic banking with unqualified persons in Islamic finance, absence of Islamic inter bank, misperception, current political and economic situation, and default culture”.

CONCLUSION AND RECOMMENDATIONS

From this eye-opening research, it was revealed that even the elite's consumers were not entirely aware of interest and what Islamic banking was up to. Where almost 40% of respondent did not know that Islamic banks are not operated by Muslims only, there is need for enlightenment. If the People's of Zanzibar wants to bridge the gap between the poor and the rich it must believe the architecture of Islamic financial institutions is advantageous to every economy because it enhances equitable distribute of income, operate interest free transactions, and invest in only lawful investments and in real sector of the economy. In Islamic banking system, time deposit account is divided into two such as general investment account and specific investment account. Under the general investment account, the bank will invest investors' fund in any investment sector they see fit provided it is in procession with the Islamic law and Shari'ah. Whereas the specific investment account, the customer's will identify the financial sector for which their money should be invested by the financial institutions. And in this case, the bank will not digress from the customer's choice of investment.

Finally, the Central Bank of Tanzania is supposed to launch new amendable framework for Islamic banking because it cannot segregate itself from the global transformation in the financial system brought about by Islamic finance. In addition to that, there is a large market for Islamic banking institutions in terms of large number of Muslims in country who are ready to invest and benefited from Islamic banking services. The study recommended that: In order to achieve certain economic and social goals, central banks have intervened in the determination of the rate of interest and establish of an interest free banking system in order to exploit and extort the poor and needy. The most important portion of the wealth of a country is captured by a few rich peoples through interest. The poor become more poor and the rich more rich as a result; civilization in the society is divided into different classes, and hence envies, jealousy, murder, etc. For this reason, Almighty Allah has declared for the human kind in His Holy Qur'an, “Allah has allowed trade and has prohibited interest” (2:275).

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