

ORIGINAL CONTRIBUTION

## Islamic Banking and Finance: A New Paradigm in International Relations

Abdul Qayyum Khan <sup>1\*</sup>, Arshad Ali Bhatti <sup>2</sup>

<sup>1</sup> Ph.D scholar, International Institute of Islamic Economics (IIIE), International Islamic University, Islamabad, Pakistan and Assistant Professor, Government College, Mallot, Bagh, Azad Kashmir

<sup>2</sup> Assistant Professor, School of Economics, IIIE, International Islamic University, Islamabad, Pakistan

### Keywords

Islamic Banking  
Religion  
International Relations  
Harmony among Nations  
Radicalism

**Abstract.** This paper aims to explore whether Islamic banking and finance could be a means of developing new international relations among Muslim as well as non-Muslim countries. It uses self-administered survey data and employs descriptive and logistic regression for analysis. The key findings show that Islamic banking and finance is indeed a means of building up on new international relations by its integration with the conventional financial system. It does this by promoting education and research, and bringing peace and harmony in and among States by controlling radical elements. Also, it is a means to win friends with cooperation among Muslim nations and others through interfaith dialogue. This is the first empirical study of its kind on the matter in question.

**Received:** 28 December 2017

**Accepted:** 12 March 2018

**KAUJIE Classification:** I3, J0, J4, L0, V12

**JEL Classification:** C01, C83, F50, F65, G20, G21, N40

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### INTRODUCTION

Tracing back the history of Islamic finance, the Holy Prophet (PBUH) personally carried it out on the basis of Qur'ānic revelations in the seventh century. Muslims practiced *mudārabah*, *mushārahah*, *bai' al-salam* and *qard al-ḥasan* during his time (Kahf & Khan, 1992). With the expansion of the Islamic state, the Islamic financial system reached Central Asia, India, China, Africa, Morocco, as well as Spain in four centuries. Poverty, famine, and financial and economic crises were not there in the long history of 1000 years (Khan, 2009). The Islamic financial system continued in the Muslim world till the beginning of the 19th Century (Warde, 2000). The ending episodes of Islamic finance can be linked to the colonial rule in Muslim countries, when the Muslim institutions were replaced by secular system and institutions. Later on, Muslims began the revival of their identities and lost values in all aspects of life, especially economic systems (Iqbal & Mirakhor, 2011).

The key factors in the emergence of contemporary Islamic banking are the rise of Pan-Islamism, writings of Islamic scholars, political awareness, establishment of the Organization of Islamic Countries (hereafter OIC), establishment of the Islamic Development Bank

\*Corresponding author: Abdul Qayyum Khan

†Email: [aqayyum63@gmail.com](mailto:aqayyum63@gmail.com)

(hereafter IDB), the oil boom of 1970s, and Saudi Arabia's support for the establishment of universities and institutions in the Muslim states. Furthermore, the establishment of certain infrastructure institutions such as the Bahrain based Accounting and Auditing Organization for Islamic Financial Institutions (hereafter AAOIFI), International Islamic Financial Market (hereafter IIFM), the Malaysia-based Islamic Financial Services Board (hereafter IFSB), and the Islamic Research and Training Institute (hereafter IRTI) paved the way for the worldwide evolution of the Islamic banking industry. Something important is that the fall of communism and the crisis of capitalism created a gap in the world that demanded an alternative system for the benefit of mankind. Consequently, the Islamic economic system emerged as an alternative mainly in the form of Islamic banking and finance (Chapra, 2009; Ibrahim, 2007).

The salient features of Islamic finance are risk-sharing, promotion of entrepreneurship, sanctity of contracts and non-speculative behavior. It prevents the use of debt-based instruments as interest and a fixed rate of return without bearing ownership related business risk are prohibited in Islam. Islamic Sharī'ah governs the economic, social, political, cultural and financial aspects of Islamic societies (Iqbal, 1997). On the other hand, *ribā*-based conventional systems cannot achieve the goals of Islamic Sharī'ah such as justice, fairness and general welfare of the humanity. *Ribā* is against the human interests, promotes an unfair financial system and increases income inequalities within and among the nations (Siddiqi, 2006).

The proponents and opponents of Islamic Banking and Finance (IBF) are worth mentioning here. For example, Ilias (2009) refers to the opponents of Islamic finance who tend to link it with the finance of terrorists. Another similar observation is made by Alexiev (2007) who equates Islamic finance with Nazism and Communism, that aimed at destroying the Western civilization. According to this view, IBF is a key instrument of the militant Islamist movement in its struggle against the West. However, the proponents of IBF consider it an alternative tool for economic development. Terrell (2007) argues that religiousness and oil wealth are the base of IBF development. IBF has no ties to terrorism, in fact it counteracts as a means of moderation and enfranchisement. Abraham (2008), asserts that Islamic finance challenges the conventional finance; it addresses religious identity and explores the relationship between religion, politics and economy.

It is worth mentioning that the modern Western society is afflicted with the social evils of race realization and alcohol and '*fawāḥish*' (shameful deeds), while the moral achievement of Islam is the elimination of race consciousness among Muslims. Racial intolerance can be eliminated by the propagation of the moral values of Islam. The spirit of Islam can convert this issue to peace and tolerance around the world (Toynbee, 1946). Hence, IBF can be used as a means to achieve peace, tolerance, and harmony among the nations.

### EMERGING THEMES

Keeping in view our topic of research, we thematically divided this section into five subsections. Section 1 explains the revival of Islam in the world. Section 2 examines IBF as a means of cooperation among the nations. In section 3, we explore IBF as a means of

foreign direct investment among the Muslim world. Section 4 highlights the need of IBF as an alternative paradigm. Section 5 explores IBF as a means to incorporate Muslim voices and role of religion in world affairs.

### **Revival of Islam in the World**

The revival of Islam is an appeal to Muslim masses for the restoration of religious beliefs, cultural refinement and adoption of pure Islamic teachings in every walk of life. It demands to reconsider their Islamic institutions, such as economic, social, political and education systems. It is a move to change the behaviors of Muslim masses by adopting Islamic values and divine guidance (Shuriye, 2011). Whereas, it is also considered as a transnational concept and is growing in every Muslim state and becoming an active movement having multidimensional impacts by providing social services (Esposito, 1999).

The modern history of Islamic finance can be linked to the independence movement against colonial rule in the Muslim countries. Few examples include the opposition against the interest-based Barclays Bank of Egypt for raising funds to construct the Suez Canal, development of a formal Islamic banking system by a group of scholars in India (1953), an effort to develop an interest free financial system to assist Muslims performing the Pilgrimage in Malaysia (1960s) and the need of the Arab world for IBF due to oil wealth of 1970s (Iqbal & Mirakhor, 2011). The end of colonial rule brought chances for the Muslim leaders to implement domestic policies and Arab's defeat of 1967 created a big opportunity to revive Islamic financial institutions (El Ashker & Wilson, 2006; Lubeck, 1999).

The growing influence of Islamic NGOs, apparently apolitical, refers to an institutionalized attempt to counter the Western values and the practices hostile to Islam. Their activities for socio-economic provisions become political when they challenge other cultural codes and institutions by abstaining direct confrontation with the state or participating in the formal politics (Wiktorowicz & Farouki, 2000). The emergence of a new business minded middle-class in Muslim societies, prominently in Iran, Pakistan, Malaysia, Indonesia, Turkey, and Dubai, implies a struggle for social transformation and replacement of radical elements (Nasr, 2009). On the other side, the Muslim masses have money to invest and their demand for Islamic financial system is growing over time. Bayat (2005) considers the emerging religious power and strength as a shift from Islamism to socio-economic development.

### **IBF: A Means of Cooperation among the Nations**

IBF is a means of cooperation among different cultures of the world. An interesting glimpse is the coins discovered from Sweden, the Baltic States, Ukraine, China and Zimbabwe which show how the Byzantine and Sassanian coins were used to substitute with Islamic coins in 695 A.D. Arab traders were the pioneers to develop the adequate infrastructure of international banking by extending the model of the ancient Persian system to foster the world trade and the same was adopted by Europeans till the order was destroyed by Philip IV of France in 1307 (Skeen, 2008). A similar evidence of banking activities, in Islamic history

around 1200 years ago was reported in well-known Muslim cities (Kahf, Ahmed, & Houmoud, 1998).

Taking a thread from the past, the mechanism and spirit of IBF are to cooperate with other cultures and civilizations of the world. It can be used to promote interfaith dialogue among nations to win friends by cooperation rather than confronting them (Siddiqi, 2006). Likely, Islamic financial institutions are becoming partners with Western market players to promote Islamic banking in European markets. These developments have given the IBF industry an opportunity to become a truly competitive and integrated part of international financial markets (Khan and Bhatti, 2006). Similarly, a surplus of funds of many Islamic Financial Institutions (IFIs) can be invested in non-Muslim countries by working together the risk-desire of conventional financial institutions and risk-return characteristics of IFIs (Lee & Ullah, 2007).

Moreover, the concept of geo-educational dynamics of Islamic finance is going to provide an additional network to international relations. A rivalry prevails between Britain and Malaysia to become an educational hub for Islamic finance (Belouafi, Belabes, & Daoudi, 2012). In order to support the idea, Said (1983) presents the traveling theory, which says that like people, institutions, ideas and theories travel from person to person, situation to situation and from one period to the other. He identifies four stages for theories to travel. The first stage is the development and explanation of a theory. In the second stage, it travels through people, publications and electronic media to different parts of the world. In the third stage its acceptance, rejection or modification is done in a new time and place. The last and fourth stage reflects its uses as a new theory (Mandaville, 2003).

El Ashker & Wilson (2006) document that Islamic organizations and OIC supported the teachings of Islam among the Muslim states which provided intellectual development and establishment of infrastructure institutions in the Muslim world. The establishment of the IDB in mid-1970s created an everlasting effect on the socio-economic development of the Muslim *ummah* (Montgomery, 2010). Similarly, Saudi Arabia provided financial support to Muslim regimes for the establishment of Islamic universities and research institutions that facilitated the worldwide IBF activities (Garas & Manama, 2007).

### **IBF: A Means of Foreign Direct Investment (FDI) among the Muslim World**

Political links supported with economic factors are considered as a major driving force for the emergence of a contemporary IBF. As indicated in the introduction, political-economic developments of Pan-Islamism and oil price shocks of 1970s resulted in the creation of modern Islamic banking and finance (Warde, 2000). Moreover, the idea of Islamic brotherhood was incorporated in the OIC. It became an international political body of 58 Muslim states advocating their rights. In addition, it is aimed at promoting monetary cooperation and unity among the Islamic states (Sheikh, 2003). Furthermore, the foreign ministers of Islamic states approved the articles of an inter-governmental financial agency in 1973 and consequently the IDB was formally established in 1974. Egypt and Pakistan had an active role in the creation of IDB and provided motivation for formal cooperation among Islamic

states. Saudi Arabia provided 25 per cent of the paid-up capital, while Libya and the United Arab Emirates paid 16 and 14 per cent respectively (Roy, 1991).

The above background highlights the importance of Islamic banks as compared to conventional banks in countries like Saudi Arabia, Kuwait, Jordan and Turkey on the basis of openness and globalization. The most significant outlook of Islamic finance's future may be the large multinationals that have opened Islamic windows for receiving deposits. Islamic finance is becoming respectable in international business circles. It is in the Western world's interest to encourage a more benevolent sort of globalization, whereby Islamic financial instruments are integrated into international finance (Soliman, 2004). However, Wilson (2004) advised to devise a mechanism of IBF to protect capital flight from the Muslim countries.

Tajgardoon, Noormohamadi, and Behname (2012) empirically analyzed the impact of Foreign Direct Investment (FDI) on Islamic banking for nine OIC states and concluded that both FDI and Islamic banking reinforce each other. Hence, Islamic banking is a mechanism to bring FDI while FDI in turn reinforces Islamic banking among OIC states. Similarly, another empirical analysis between Islamic banks' financing and economic growth is done by Tabash & Dhankar (2014) for Qatar that shows favorable results for its economy.

### **Need of IBF as an Alternative Paradigm**

Humanity is in search of a new economic system which could resolve the instability problems created by the capitalism in the recent past. A new economic system based on religion, traditions, culture and Islamic civilization is emerging in the world (Rosser, Barkley Rosser Jr, & Kramer Jr, 1999). In a similar fashion Chapra (2009) argues that the capitalism is subject to economic recessions and has resulted in the failure of conventional banking system. The emergence of Islamic banking, free from interest, as an alternative model is based on justice and equity. Moreover, Zaman (2006), emphasizes on an alternative paradigm, as the main principles of modern economies are empirically false, and ignore ethical values and care for the poor.

The post-colonial way of adopting western policies by Muslim regimes aggravated the situation in Muslim states. The economists are of the view that these policies would not solve their problems and that they should develop their own discipline to cater to their needs (Tahir & Haque, 1995; Yousri, 2005; Zaman, 2009). Thus, the main reason for Islamic underdevelopment can be linked to the dependency theory (Wallerstein, 1991). The international economy is divided into a dominant center and a periphery of dependent poor countries. The center, holding dominancy in terms of wealth, capital and technological advancement, is developed at the cost of periphery countries which are deliberately kept underdeveloped. Islamic states being periphery got victims of underdevelopment and Islamic decay by the colonial powers. The colonial masters exploited resources of Islamic states for maximization of their profits (Mehmet, 2002).

Moreover, development models of 1980s are challenged by cultural, economic, technological and geopolitical changes in the world and ultimately sovereignty of nation-states is threatened. The social transformation studies have been proposed to incorporate social, economic, political and cultural changes for development models (Castles, 2001). To prove

the assertion that Western development models are means of exploitation for Islamic world, John (2004) discusses how poor countries are trapped on the name of growth in the form of loans to develop infrastructure projects by the loaning country. The development projects in the form of loans are a means to conquer the poor countries of the world. Initially, the poor countries are motivated and influenced to accept development loans. When the borrowing countries default on loan and are at the mercy of its creditors, the creditor country then demands from indebted nations for favors, like a U.N. vote, a military base abroad or even energy resources. In this perspective, the solution of economic problems faced by Muslim regimes lies in the adoption of IBF paradigm. It may solve their present day's problems of economic instability, currency run-off, investment needs, political subservience, inequity and poverty. This reconstruction would increase the political stability and organization for the spread and practice of Islamic transformation (Choudhry, 2003).

### **IBF: A Means to Incorporate Muslim Voices and Role of Religion in World Affairs**

Muslims are one fourth of the world population and Islam spreads from Asia to the west of Africa and onward to South America. It is logical to incorporate their voices, experiences, civilization and value system in the discipline of International Relations (I.R) to understand the contemporary world affairs. Western scholars remained biased while discussing the achievements of Islamic civilization in the field of social sciences during the medieval period (Khan, 2009). Likely, the growth of Islamic finance is linked to Islam which remains the fastest growing religion in the world. (Zaher & Hassan, 2001).

Current wave of research in international relations stresses on a need to develop I.R. theories by incorporating norms and practices of non-western world as the discipline remained dominated by western perspectives (Acharya, 2011). Neuman (1998) argues that I.R. theories exhibit major gaps in explaining the political, economic and security relationships in the non-western world. Hurd (2004) blames western social scientists for neglecting religion and this trend is strongest in I.R. discipline. Moreover, the current financial crisis has threatened the regimes in the west and I.R. has failed to develop any solution (Ozkan, 2012). Contemporary I.R. is based on enlightenment, western experience of the world and ignoring the role of religion. Major theories of I.R. and their empirical methods exclude religion, whereas, lot of world population believe religious values (Fox & Sandler, 2004). The world is recognizing the role of religion which has been ignored by I.R. theories. The awareness of incorporating religion to solve issues of the contemporary world is evident. The integration of religion to I.R. theories is imperative to understand and solve the issues at a global level (Wallerstein, 2005). Religion is emerging at the state level and in international affairs of contemporary global politics (Shuriye, 2011).

### **EMPIRICAL ANALYSIS**

The attributes on the basis of a thematic review of the above sections are empirically tested in this section. We use positivist methodology of research for which survey method is used to collect data from the respondents through a self-administered questionnaire. After pre-

testing, the questionnaire was posted on a designated website and the response of 1008 respondents was recorded.

We describe our data using graphical and numerical tools. For example, a descriptive analysis of each stakeholder group is explained in the light of frequency tables which are constructed out of the collected data and then histograms are designed followed by explanations and citations from the literature. Further, we provide logistic regression analysis to examine the factors that may affect the probability of occurrence of certain attributes, particularly the adoption of IBF in Pakistan. Finally, we synthesize our results obtained from different methods of analysis.

### **Targeted Population and Sample Frame**

The target population of this study is the whole of Pakistan; however, our sample frame consists of those respondents who use the internet, such as religious scholars, officers at the State Bank of Pakistan (SBP) and officers at the Ministry of Finance. We use cluster sampling for officers and convenient sampling for religious scholars. Cluster sampling is used when target population is located in a particular geographical area like Ministries, Headquarters, Universities, Industrial Areas and Organizations. Our sample size is 1008 respondents from various stakeholders of IBF in Pakistan, which is consistent with most of the empirical literature (Bartlett, Kotrlik, & Higgins, 2001; Comrey & Lee, 1992).

### **Unit of Analysis**

The following key stakeholders are identified to be the units of analysis of our empirical analysis.

- a) *The Religious scholars*: They are the experts of Islamic Shari'ah and closely connected with the masses. Their appeal can convert IBF into a mass movement. These are the *imāms*, *khateeb*s, or teachers of the religious schools (*madāris*) of Pakistan, being very influential in society. Usually, they issue verdicts over the legitimacy and authenticity, or otherwise, of IBF.
- b) *Officers, SBP*: Officers who are responsible for overseeing matters related to licensing, regulation and supervision of Islamic banks in Pakistan. They are responsible for the supervision of Islamic banking by all means, conducting R&D and taking care of training of employees at Islamic banks.
- c) *Officers, Ministry of Finance*: They are responsible to identify the mechanism for converting the whole conventional banking into IBF along with Islamization of the economy by providing funds through budget allocations. Moreover, they design and implement the fiscal policy of the country.

### **Construction of Questionnaire and Pre-Testing**

We constructed our questionnaire in the light of attributes collected from a group discussion of key stake holders, such as customers (corporate & non corporate), general masses, religious scholars, Islamic political parties, employees of Islamic banks, officers from SBP and officers from Ministry of Finance. The amended questionnaire was then pre-tested on

various groups of concerned stakeholders. Finally, the revised questionnaire was posted on a designated website to collect primary data in year 2013-14. The questionnaire contained close-ended as well as open-ended questions.

### **Data Collection Procedure and Response Rate**

We used a mixed mode, a combination of mobile, surface mail, e-mail, the internet, and personal meetings to generate the primary data through structured questionnaire. This method is most effective to include the maximum respondents in the area of research. Those who do not respond by one means are included by the other. We developed a website through which the questionnaire was posted. The targeted groups were approached to fill in the questionnaire through social media and e-mails. Repeated advertisements were made for the responses through social media by highlighting the importance and need of the survey and its relevance for IBF in Pakistan. Personal references were used for online responses from the citizens of Pakistan as well as overseas Pakistanis from America, England, Australia, Middle East, Malaysia and China. Personal visits were also made by the researcher to the approachable target groups. Sometimes the target groups were approached and reminded twice or thrice for compliance. It took about two months to get the online responses from officers at the Ministry of Finance. We spent 10 days in Karachi to get the online response from officers at the State Bank of Pakistan. We fixed a target of 1050 respondents out of which 1008 responded to our questionnaire. So the response rate is 96 percent.

## **DESCRIPTIVE ANALYSIS**

This section covers results of the attributes of religious scholars, officers at SBP and officers at the Ministry of Finance to prove the assertion that IBF is a means of new I.R. in the Muslim world.

### **IBF is a Platform to Convert the Religious Strength into a Political Force**

It is important to analyze whether IBF converts the scattered religious strength into a political force by making political alliances, involving the radical elements, opening new avenues of cooperation among the OIC countries and by conducting education/research to harvest political benefits domestically and internationally. Most of the respondents from religious scholars (81.64 percent) believe that IBF is a means to convert the religious strength into a political force by making political alliances (see Figure 1). This finding is consistent with Rana (2011). Similarly, most of the respondents (76.53 percent) favor that IBF is a means to convert the religious strength into a political force by involving the radical elements into nation building. The above result strengthens the view of Atzori (2012). Moreover, most of the respondents (above 90 percent) from religious scholars endorse that IBF is a means to convert religious strength into a political force by opening new avenues of cooperation among the Muslim world, conducting education/research of IBF, and constituting dialogue with other nations. It proves our hypothesis of Islamic banking being a means of new I.R. among the Muslim countries.

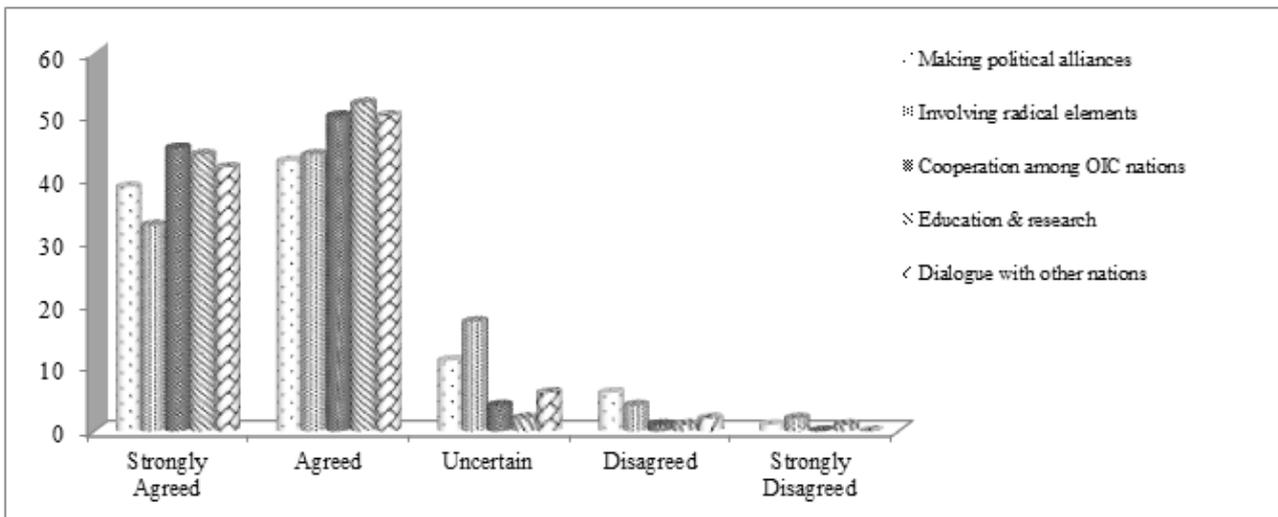


FIGURE 1. IBF, a means to convert religious strength into a political force by

**Motivations for the SBP to Launch Islamic Banking in 2001**

The analysis of data reflects that majority of the respondents (53 to 66 percent) from SBP confirm that the reasons for policy shift in 2001 are motivation by Muslim countries’ institutions and investors (see Figure 2). These results endorse our hypothesis of ‘IBF as a means of new paradigm in I.R. among the Muslim world’. IBF as a foreign policy tool can be utilized for awareness, popularity and promotion, education and training among the hostile Muslim countries. Credit must be given to international Islamic financial institutions for eliminating resistance to IBF and increasing its acceptance, awareness and capacity building in the OIC countries. IBF is a means to revive Islamism, to counter radical Islam, to build civil societies, having no ties to terrorism and could be leveraged as a means of moderation, and to bridge gap among different segments of the society. These results are consistent with Henry (2001), Kahf (2004), Keyman & Koyuncu (2005) and Lubeck (1999).

Further, most of the respondents (95 percent) appreciate the SBP’s initiative of organizing training courses and research seminars for the employees of Islamic banks in collaboration with OIC institutions (IRTI, AAOIFI, IDB and IFSB). This result is consistent with the opinion of many scholars (Siddiqi, 2006; El Ashker & Wilson, 2006; Garas & Manama, 2007; Montgomery, 2010).

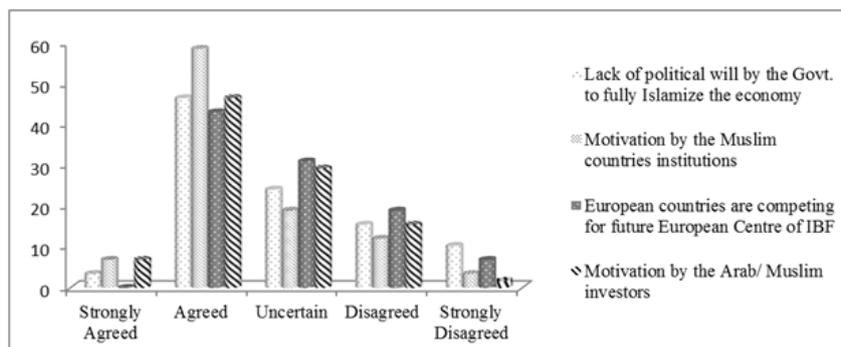


FIGURE 2. Reasons for policy shift of SBP in 2001

### Reasons to Institutionalize IBF in Pakistan

According to our survey, most of respondents (86 to 92 percent) from officers in the Ministry of Finance support the reasons to institutionalize IBF in the country. They think that in the face of current world economic crisis, Pakistan can become a hub of Islamic banking in the region and it would open new avenues of I.R. among the Muslim countries. While even non-Muslim countries are promoting IBF, why not Pakistan. IBF can attract investors from the Muslim world, especially the Middle East (see Figure 3). Further, the Western financial markets have become more favorable for IBF practice that have given the IBF industry an opportunity to become truly competitive and an integral part of international financial markets (Dilawar, 2012; Lee & Ullah, 2007; Khan & Bhatti., 2006; Siddiqi, 2006).

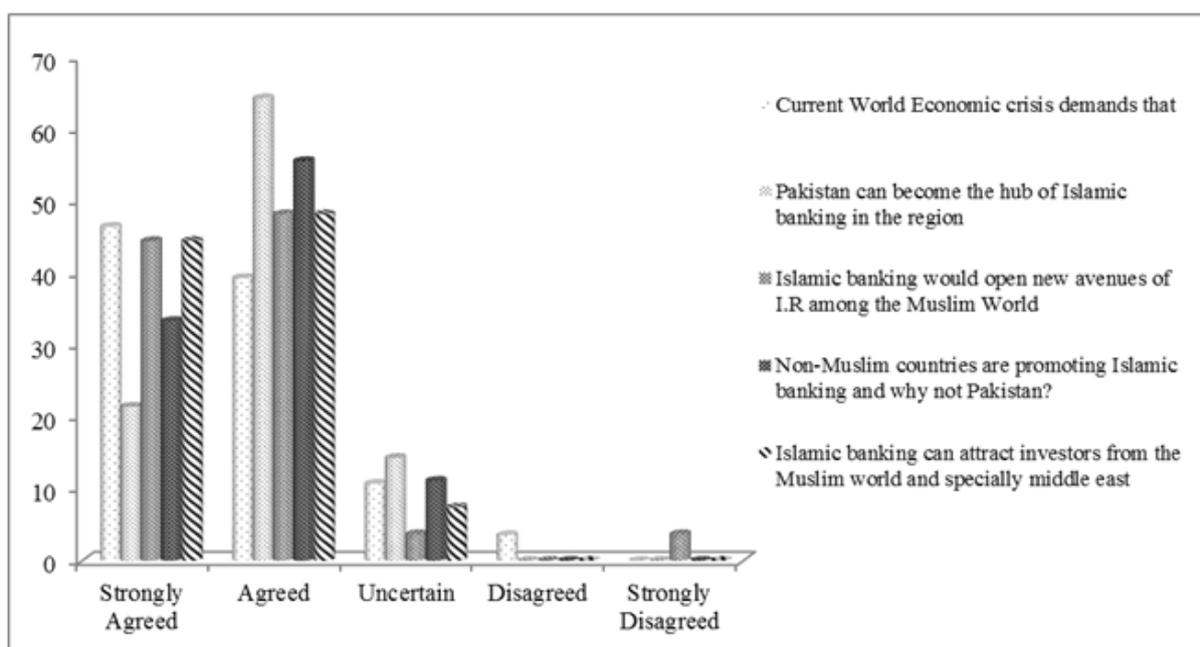


FIGURE 3. Reasons to institutionalize the IBF in Pakistan

### Coordination of Finance Ministry with OIC Institutions for Promoting IBF

Our results show that most of the respondents (65 to 70 percent) are in favor of various actions taken by the Ministry of Finance in Pakistan to coordinate with OIC institutions. These actions are sending delegations of government officials, sending delegations of Sharī‘ah scholars to various institutions, organizing training for the employees of Islamic banks with the collaboration of international financial institutions of the Muslim world, sending government officials for higher studies in the Muslim world, sending Sharī‘ah scholars for higher studies in the Muslim world, granting scholarship to the students of Muslim countries and granting scholarship to the Muslim students of Muslim minority countries (see Figure 4). These observations are also consistent with Garas & Manama (2007), El Ashker & Wilson (2006) and Siddiqi (2006).

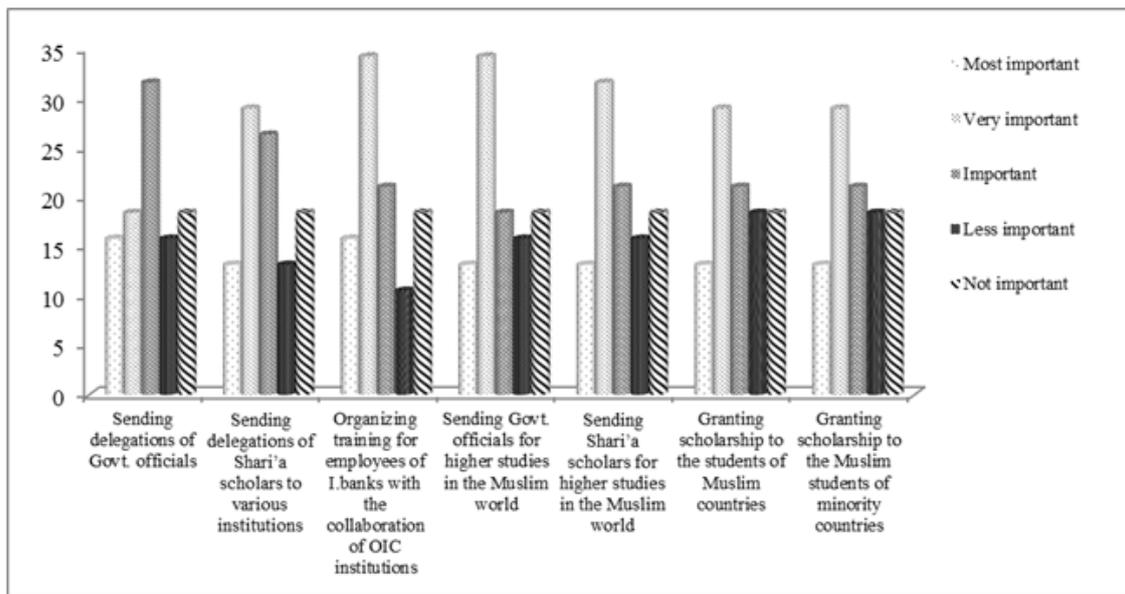


FIGURE 4. Finance Ministry coordinates with OIC institutions for IBF through

Overall, our descriptive analysis confirms our hypothesis that ‘IBF is a new means of I.R. among the Muslim world’.

**Logistic Regression Analysis**

We use ordered logistic regression to analyze the impact of various attributes that may affect the choice of IBF as a new means of I.R. among Muslim World (IBFNIR). As our dependent variable, IBFNIR is ordered in nature, we use 1 for strongly agreed, 2 for agreed; 3 for uncertain; 4 for disagreed and 5 for strongly disagreed. Likely, the independent variables are measured on 5-point Likert scale. Our ordered logistic regression of IBFNIR is given as follows:

$$\ln\left(\frac{P_{ci}}{1-P_{ci}}\right)_{IBFNIR} = \alpha_c + \beta_1(IBMOCM)i + \beta_2(SRNDU)i + \beta_3(SRNDRC)i + \beta_4(SRNDCE)i + \beta_5(SRNDIFB)i + \beta_6(BCIIB)i + \beta_7(EFSCIB)i + \beta_8(EIUIB)i + \beta_9(EIEPOR)i + \beta_{10}(SCCEIE)i + \beta_{11}(IPLSACB)i + \beta_{12}(IMC)i + \beta_{13}(ETFMFEI)i + \beta_{14}(ETFMLLM)i + U_i$$

where,  $P_{ci}$  is the probability of IBFNIR for categories (c) ranging from 1 to 5 given the information on regressors;  $\alpha_c$  is thresholds or cutpoints in increasing order ( $\alpha_1 < \alpha_2 < \dots < \alpha_{c-1}$ ). The independent variables, measured on 5-point Likert scale, are given as follows: IBMOCB is ‘interest based products offered by conventional banks’, SRNDU is ‘successive regimes neglected development of universities’, SRNDRC is ‘successive regimes neglected development of research centers’, SRNDCE is ‘successive regimes neglected development of center of excellences’, SRNDIFB is ‘successive regimes neglected development of Islamic financial boards’, ECIIB is ‘establishment of the Council of Islamic Ideology for Islamic banking’, EFSCIB is ‘establishment of the Federal Shari‘ah Court for Islamic banking’, EIUIB is ‘establishment of the International Islamic university for Islamic banking’, EIEPOR is ‘elimination of interest from economy is the part of *Objective Resolution*’, SCCEIE is ‘special clause of constitution to eliminate interest from the economy’, IPLSACB is ‘introduction of profit-loss-sharing (PLS) accounts in commercial banks’, IMC is ‘introduction of *muḍārabah* companies’, ETFMFEI is ‘establishment of task force in Ministry

of Finance for elimination of interest’, and ETFMLLM is ‘establishment of task force in Ministry of Law for legal measures’ and  $U_i$  is error term.

We estimated the above general model, which is then reduced to a parsimonious model given in Table 1 by dropping insignificant variables, sequentially, following the general to specific approach.

Our results in Table 1 show that IBFNIR is positively affected by ‘successive regimes neglected development of research centers’, ‘elimination of interest from economy is the part of *Objective Resolution*’, and ‘introduction of *muḍārabah* companies’. Any improvement in the above measures and institutions has potential to enhance the chances of IBF as a new means of I.R. among the Muslim world. These results suggest that the development of research centers for IBF can promote education, research and interfaith dialogue among the nations. Likely, *Objective Resolution* is an ideological base for the constitutional development of Pakistan that can be used to strengthen the thesis of IBFNIR. Moreover, *muḍārabah* companies in Pakistan can be a leverage to achieve financial self-reliance of the country by attracting FDI from the Muslim world. However, the attributes such as ‘special clause of constitution to eliminate interest from the economy’, and ‘establishment of task force in the Ministry of Finance for elimination of interest’ are negatively related with the dependent variable, the latter being insignificant. Therefore, these attributes might not play any important role in the promotion of IBF in Pakistan because of their dormant characteristic. Thus, the government of Pakistan may pay particular attention to activate their role for the elimination of interest from economy. Finally, our chi square estimate shows that overall model is significant.

**TABLE 1**  
**Logistic Regression: IBF as a New Means of I.R among Muslim World (IBFNIR)**

IBFNIR	Coefficient	Robust S.E.	Z	$P >  z $
SRNDRC	1.0715***	0.2488	4.31	0.000
EIEPOR	0.9930**	0.4160	2.39	0.017
SCCEIE	-1.1548***	0.3909	-2.95	0.000
IMC	0.8459*	0.4420	1.91	0.056
ETFMFEI	-0.7658	0.4699	-1.63	0.103
Obs.	57	57	57	57
Wald Chi Sq.	22.81			
(p- Value)	(0.0004)			

Notes: \*\*\*, \*\*, \* represent significance at 1%, 5% and 10% level respectively.

Our dependent variable is ‘Islamic banking is a new means of I.R. among Muslim world (IBFNIR)’. The independent variables are ‘successive regimes neglected development of research centers (SRNDRC)’, ‘elimination of interest from economy is the part of *Objective Resolution* (EIEPOR)’, ‘special clause of constitution to eliminate interest from the economy (SCCEIE)’, ‘introduction of *muḍārabah* companies (IMC)’, and ‘establishment of task force in Ministry of Finance for elimination of interest (ETFMFEI)’.

In Table 2, we also estimate the probabilities for various categories of IBFNIR given the mean values of regressors. It shows that the probabilities of ‘strongly agreed’ and ‘agreed’ are 36% and 41.5% respectively that are significantly higher than the ‘disagreed’ and ‘strongly disagreed’ options. These results further confirm our hypothesis that IBF can be used as a means of new paradigm in international relations.

**TABLE 2**  
**Average Predictions for various categories of IBFNIR**

IBFNIR (Categories)	Strongly Agreed	Agreed	Uncertain	Disagreed	Strongly Disagreed
Pr(IBFNIRbase)	0.360	0.415	0.115	0.076	0.033

## CONCLUSION

This paper investigates the role of IBF as a new paradigm in international relations. Our findings depict that IBF can be a means to convert the religious strength into a political force by making political alliances, involving the radical elements in nation building, opening new avenues of cooperation among the Muslim world through conducting education/research of IBF and arranging dialogue with other nations. Further, the reasons behind the afresh launch of IBF in Pakistan, side by side with the conventional banking, are not merely domestic, rather other Muslim countries, international institutions and investors motivated the Government of Pakistan to take a policy shift and launch IBF in 2001 with policy different from the overall transformation policy adopted in 1980s.

We note that the arranging training by NIBAF, the training arm of the SBP and joint research and awareness seminars for IBF with the collaboration of OIC institutions leave positive and significant impact on IBF to be a new means of I.R. among Muslim countries. Also, delegations of government officials and Shari‘ah scholars to various International institutions, organizing training for the employees of Islamic banks with the collaboration of International financial institutions of the Muslim world, sending Government officials and Shari‘ah scholars for higher studies in the Muslim world, and granting scholarship to the students of Muslim countries and Muslim students of the minority countries could be important means of coordination among OIC institutions for the promotion of IBF.

Our findings stress upon the development of research centers in order to cater the need of creating awareness about IBF, educating and training people, and generating effective research to face the global challenges for IBF. Furthermore, there is a dire need to empower the Council of Islamic Ideology for Islamic banking, but our findings show no significant role for this; that is why we dropped it from our final model; and similarly establishment of task force in the ministry of finance is extremely important, but finding show that it is insignificant. Consequently, these measures may enhance the image of IBF as a new means of I.R. in the Muslim world. Our empirical results strengthen the thesis that IBF is a means of new international relations among the Muslim countries.

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