

Revisiting the Index to Measure *Maqasid alShariah* Oriented Performance of Islamic Banks: Evidence from Pakistan

Muhammad Mansoor Javed¹

Mohammad Ayaz²

Rukhsana Kalim³

Abstract

In the context of fulfillment of *Maqasid al-Shariah*, Islamic banks' performance has been measured by some researchers by adding many dimensions and elements to the five objectives of *Shariah*, and resultantly many indices have been developed. However, these dimensions and elements are either not comprehensive, or not relevant. The objective of the present study is to provide an improved *Maqasid al-Shariah* oriented performance index that includes all the five objectives of Ghazali's theory of *Maqasid al Shariah*, namely protection of faith, life, intellect, family and wealth. Additionally, the present study proposed more reflective measures to assess *Maqasid* oriented performance including share of financing based on non-controversial modes and percentage of 'value added' that is distributed to various stakeholders. The study applied Sekaran's behavior science method and applied social accounting concept of 'value added statement' and 'service profit chain' as a logic to develop *Maqasid* index which is later on validated through experts' interviews. In addition, the study has also applied the proposed index using eight years' data (2010-2017) from full-fledged Islamic banks of Pakistan to assess their *Maqasid* oriented performance. The findings reveal that only 'protection of intellect' oriented performance of Islamic banks is improving whereas other *Maqasid* oriented performances are deteriorating.

Key Words: *Maqasid al-Shariah*, Social Performance, Index Development

KAUJIE Classification: B4, H47

JEL Classification: C43, G21, Z12

Introduction

Maqasid al-Shariah can be considered as 'rationale for *Shariah* commandments' or 'wisdom behind the *Shariah* rulings' (Dusuki & Abozaid, 2007). The purpose of these *Maqasid* is to pursue the improvement and betterment of humankind under the divine direction and guidance. These *Maqasid* or objectives in a way are broadly related to three categories of human needs namely: "Dharuriyah, Hajiyyah and Tahsiniyah". Dharuriyah refers to basic necessities that cover those benefits which are most important for human life. Hajiyyah refers to complimentary

¹ Muhammad Mansoor Javed is PhD scholar at the Institute of Islamic Banking, University of Management and Technology, Lahore, Pakistan.

² Dr. Mohammad Ayaz, the corresponding author, is Assistant Professor at the Institute of Islamic Banking, University of Management and Technology, Lahore; mohammad.ayaz@umt.edu.pk

³ Dr. Rukhsana Kalim is Professor of Economics at the School of Business and Economics, University of Management and Technology, Lahore.

benefits that are crucial to alleviate hardship from the society. Meanwhile, *tahsiniyah* refers to those benefits which result in perfection or refinement in the behavior of people (Kamali, 2008). Originally, Imam Ghazali introduced five important elements to *Dharuriyah* namely: “protection of faith, protection of life, protection of intellect, protection of posterity and protection of wealth” (Kamali, 2008). However, contemporary scholars have extended this list of five elements by adding some other elements such as human dignity, freedom, orderliness, equality, development in technology, economic reforms and social welfare (Auda, 2008).

Relating *Maqasid al-Shariah* to the Banking Sector

The purpose of *Maqasid al-Shariah* is to pursue the improvement and betterment of humankind under the divine direction and guidance. Thus, *Maqasid al-Shariah* can be considered as instruments which are used for determining the appropriateness and suitability of any reform program in an Islamic economy and their conformity with ideology, doctrines and objectives of Islamic Law (Elahi, 2011). In the context of Islamic banking, as asserted by Mohammad and Shahwan (2013), Islamic banks can achieve the purpose of their existence and can distinguish themselves from their conventional counterparts only by rigorously following the framework of *Maqasid al-Shariah*. This framework requires that Islamic banks should avoid prohibited elements in their transactions, attain welfare, remove exploitation, promote cooperation and brotherhood as well as uphold justice to facilitate equitable distribution of wealth. Hence, Islamic banks should not be merely profit oriented entities; instead they should also promote social welfare and fulfill their responsibilities towards other stakeholders (Asutay & Harningtyas, 2015; Khan, 2013). In other words, socio-economic performance of Islamic banks should be considered at the very least equally important as their financial performance. Hence, it is important to measure the performance of Islamic banks with regard to their social contribution to appraise their role in Pakistan.

Though, measuring social performance of banks is not a novel area for researchers; however, assessing social performance of Islamic banks using conventional indices is not preferable as dimensions and elements used in construction of conventional indices do not cover *Shariah* prohibited elements such as *riba*, *myser* and *gharar*. Hence the conventional indices are not sufficient (Ismail & Muqorobin, 2017). Moreover, theories that are dominant in the discussion of social responsibility are based on the Western perspective and perception. While focusing only on profitability and material performance, they ignore religious obligations of business entities towards other stakeholders (Bakar & Yusof, 2015); do not provide sufficient ethical guidance (Dusuki & Abdullah, 2007); lack in prioritizing social objectives (Darus et al., 2013); reflect secular standards (Darrag & E-Bassiouny, 2013) and ignore the Islamic world view (Ismail & Muqorobin, 2017). Literature, therefore, has suggested framework of *Maqasid al-Shariah* for implementing social performance from the Islamic perspective. (Dusuki & Abdullah, 2007; Darus, 2016; Yusuf & Bahari, 2015).

Rationale of Re-constructing the Index

Currently, Islamic banks are being criticized on grounds of copying conventional products and focusing only on the ‘legal’ form and ignoring the ‘substance’ of transactions (Asutay, 2012; Qoyum, 2018); whereas, the inherent social orientation of Islamic economy, which is based on *Maqasid al-Shariah*, suggests Islamic banking system to satisfy social needs of the society as well (Ibrahim & Momin, 2016; Khaleequzzaman, Mansoori, & Rashid, 2016). Therefore, there is a

need to develop Maqasid based rating scales and indices which can enable various stakeholders to form a justifiable opinion about Islamic banks' adherence to Shariah from the perspective of Maqasid and appraise their social role in an Islamic economy. However, measuring social role or social performance is a challenging task as being qualitative in nature with no consensus on the definition, it is difficult to quantify social performance (Asif & Batool, 2017). Though, some studies have developed Maqasid based indices to measure the social performance of Islamic banks; however, these indices can be criticized on grounds of limited scope, use of irrelevant indicators, partial applicability and based on 'narrated performance' rather than 'actual performance' as discussed below.

Some studies, e.g., by Asutay and Harningtyas (2015), developed Maqasid al-Shariah based performance evaluation models using qualitative information which is narrated in vision and mission statement, director's report, corporate governance report, corporate achievement statement, calendar of events and report on internal controls. However, as argued by Asif and Batool (2017), majority of such reports claim substantial social contribution whereas in reality such 'narrated performance' does not represent 'actual performance'.

Moreover, some of these studies have limited scope as they do not comprehensively cover all the Maqasid al-Shariah. For example, Zaheer and Rasool (2017) ignored the 'protection of family'; whereas Dzuljastri, Omar, and Fauziah (2008) disregarded the 'protection of faith'. Further, some of these indices consist of such indicators which cannot be computed due to unavailability of data. For example, Zaheer and Rasool (2017) could not apply their proposed indicators to measure 'protection of intellect' oriented performance of Islamic banks due to unavailability of relevant data.

Some other studies suggest such dimensions and elements to measure specified Maqasid oriented performance which are irrelevant or do not adequately measure the relevant performance. For example, while measuring 'protection of faith' oriented performance Mohammad, Tarique, and Islam (2015) suggested Muḍarabah and Musharakah modes only and ignored other modes of financing. Although these modes of financing are ideal as they lead to 'participatory society'; nevertheless, other modes of Islamic financing are also Shariah compliant and play an important role in realizing Maqasid (Ayub, 2018); hence should not be ignored. Likewise, to assess 'protection of intellect' oriented performance of Islamic banks Ascarya, Rahmawati, and Sukmana (2016) suggested 'freedom' and 'permissible activities' as dimension and related element respectively; and measured it using data from depositors funds, total financing and fee based income. However, such data has no connection with 'intellect'.

Finally, owing to the contractual nature, as suggested by Asif and Batool (2017), index developed to measure social performance for one region may not be appropriate for another region as social performance has discrete national pattern. For example, Qard-e-Hassan financing is more relevant to poor economies than rich economies. The only study which proposes Maqasid index from the perspective of Pakistan is made by Zaheer and Rasool (2017); however, their index has limited scope and is partially inapplicable as pointed out above.

The above discussion warrants the construction of another index which would be more reflective of Maqasid oriented performance of Islamic banks. The dimensions and elements proposed by the existing indices are either not comprehensive or not relevant as discussed above. Therefore, the objective of the present study is to provide an improved Maqasid al-Shariah oriented performance index that includes all the five dimensions of Imam Ghazali's theory of

Maqasid namely; protection of faith, life, intellect, family and wealth. Additionally, the present study proposed more reflective measures to assess Maqasid oriented performance including share of financing in non-controversial modes and products and percentage value added distributed to various stakeholders such as employees, depositors, shareholders and the State. Additionally, the study also applies the proposed index on full-fledged Islamic banks of Pakistan to explore their Maqasid orientation. The structure of the remaining paper is as follows: section 2 covers literature review, section 3 explains the process of constructing the index, section 4 explores Maqasid orientation of Islamic banks in Pakistan, and finally section 5 concludes the paper.

Literature Review

A vast literature measured social performance of Islamic banks using indices based on general Islamic principles, Islamic world view, ethical theories, Western concept of CSR and guidelines for CSR disclosures from AAOIFI and various regulatory bodies. However, the work of Dzuljastri et al. (2008) can be considered as a pioneer study that developed performance measures based on Maqasid al-Shariah. The study is based on three Maqasid identified by Abu Zaharah's, i.e., "educating the individual, establishing the justice and public interest". By applying behaviour science method, Dzuljastri et al. (2008) identified different dimensions and elements to operationalize these objectives which were later assigned weights through experts' survey. The study also tested the index by taking data from six Islamic banks from six different countries. However, the index has limited scope as it focuses only on three objectives namely educating the individuals, establishing the justice and serving for public interest.

In another similar study, Mohammad et al. (2015) using Ashur (2006)'s reinterpretation of the Al-Ghazali's framework, developed a performance evaluation model to measure Maqasid oriented performance of Islamic banks. The model suggests certain performing ratios that relate to different elements namely: 'freedom of faith, preservation of human dignity and human rights, propagation of scientific thinking, avoidance of brain drain, care for family, wellbeing of society and minimizing income and wealth disparity'. However, some of the ratios suggested by the model to measure these elements are debatable. For example, the model 'and right'; however, this ratio cannot be computed due to unavailability of data.

Using Najjar's concept of Maqasid al-Shariah, Asutay and Harningtyas (2015) also constructed an index to evaluate social performance of Islamic banks. Their study is based on four key objectives namely; "safeguarding the value of human life, safeguarding of human self, safeguarding the society and safeguarding the physical environment". These objectives are operationalized by referring to dimensions and elements used in previous studies such as those of Dzuljastri et al. (2008), Haniffa and Hudaib (2007) and Jaffar and Manarvi (2011). The study also explored the Maqasid orientation of thirteen Islamic banks from six different countries by applying the developed index and identifies the lack of achievement in Maqasid realization. However, the proposed index is significantly based on qualitative data or 'narrated performance' such as "commitments to operate within Shariah principles, commitments to engage in permissible financing and investing activities, directions in serving the needs of Muslim community, employee appreciations, maintenance of effective system of internal control, statement of social policy and statement of environment policy".

Ascarya et al. (2016) also developed 'Islamic bank Maqasid Index' based on five Maqasid or objectives originally proposed by Al-Ghazali. Each objective has 8 dimensions

derived from 42 criteria proposed by Chapra (2008) and are assigned weight using the Analytic Network Process method. However, while applying the index to evaluate the performance of 12 Islamic banks from Indonesia and other countries, Ascarya et al. (2016) had to limit their analysis to four dimensions per objective due to unavailability of observable data for other dimensions. Their study revealed that Islamic banks' performance on 'safeguarding the wealth' and 'safeguarding the intellect' was comparatively better. This study is criticized for using such dimensions which are conceptually intangible and, therefore, cannot be measured properly e.g. dignity, mental peace and freedom.

Zaheer and Rasool (2017) developed 'Maqasid al-Shariah index for Islamic banking institutions covering four objectives from Al-Ghazali's theory namely 'protection of wealth, protection of faith, protection of life and protection of intellect'. For measuring Maqasid oriented performance of Islamic banks they suggest indicators on the basis of financial performance, financial stability, Shariah compliance, service quality, funding structure, interest free lending capacity, interest free financing, research, product development, training, equity financing, Qard financing, SME financing and charitable activities. However, as pointed out by Ayub (2018), the index had a fundamental flaw that protection of wealth was given more weight (50 %) than protection of faith (35 %). Additionally, the index had a limited scope as it ignored 'protection of family' and suggested such indicators for 'protection of intellect' which might not be computed due to unavailability of data.

The above discussion highlights the research gap as there is no index which comprehensively covers all the five dimensions of Imam Al-Ghazali's theory of Maqasid namely; protection of faith, life, intellect, family and wealth especially from the perspective of Pakistan. Additionally, current indices propose less reflective measures to assess Maqasid al-Shariah oriented performances. This warrants the construction of another index to include all the five dimensions of Imam Al-Ghazali's theory of Maqasid and proposes more reflective measures to assess Maqasid oriented performance. Hence, the present study contributes to the existing literature by proposing such index which is more reflective of Maqasid oriented performance of Islamic banks operating in Pakistan. The proposed index can be used in future researches to gauge performance of Islamic banks to know their level of fulfillment of maqasid al shariah.

Methodology Of Constructing The Index

The present study constructs the index to measure the performance of the Islamic banks relating to achievement of the five Maqasid, introduced by Al-Ghazali and reinterpreted by contemporary scholars. Later, by applying Sekaran's Behavioral Science Method, the selected Maqasid are operationalized into observable dimensions and measureable elements which are identified using literature review as well as by applying social accounting concept of 'value added statement' and 'service-profit chain' logic. Afterwards, the identified dimensions and elements are validated through experts' interviews. Lastly, weights have been assigned to the Maqasid and elements using experts' survey.

Operationalization of Maqasid

The five identified objectives are operationalized using Sekaran's behavioral science method. This method is also used by some similar studies (Dzuljastri et al., 2008; Mohammad et al., 2015). Sekaran's technique breaks down concepts into various dimensions which are observable characteristics of behavior. These dimensions are then further divided into measurable elements.

For example, as cited by Sekaran, thirst is a ‘concept’ and the behavior of a thirsty person is to drink a lot of water (which is a dimension); and the degree of thirst can be assessed by the number of glasses drunk (Element) by the thirsty person.

Using Sekaran’s technique, the five Maqasid or dimensions have been translated into measureable dimensions and corresponding elements following review of literature and by applying social accounting concept of ‘value added statement’ and ‘service-profit chain’ logic as discussed below.

Protection of Faith

AAOIFI Governance Standard-7 suggests that Islamic banks should meet their religious responsibility to follow Islamic law in their operations and products. Thus, ‘protection of faith’ oriented performance of Islamic banks can be evaluated by assessing the level of fulfillment of such obligation, or in other words, by assessing the opportunities they create to provide Shariah compliant income for their depositors and Shariah compliant source of financing to their customers. Existing literature suggest equity financing modes such as ‘Mudharabah and Musharakah financing to total financing’ to measure Shariah compliance level of Islamic banks as these modes lead to ‘participatory society’ and, consequently, brings social justice (Asutay & Harningtyas, 2015; Mohammad et al., 2015). However, we argue that other Shariah compliant modes - such as Murabahah, Ijarah, Salam and Istisna - should also be included in such assessment as they can also be validated through Quran and Sunnah and play certain roles in realizing Maqasid (Ayub, 2018).

Accordingly, while measuring ‘protection of faith’ oriented performance, we suggest that only controversial products or modes should be excluded. Ayub (2018) suggested weights to various modes considering their role in Maqasid al-Shariah. We have categorized all those modes which are weighted below 50 as controversial modes. These controversial modes include: Organized Tawarruq, currency Salam, Running Musharakah, Bai-Dayn, Bai al-Inah, Debt based Sukuk and Inah based credit cards. Therefore, to measure ‘protection of faith’ oriented performance of Islamic banks, we suggest two dimensions: ‘Shariah compliant financing’ and ‘Shariah compliant investment’. The former is measured as ‘financing through non-controversial modes to total financing’; and the latter is measured as ‘investment in non-controversial products to total investment’.

Protection of life

Ashur (2006) reinterpreted ‘protection of life’ by re-phrasing it as ‘protection of human dignity and protection of human rights’. Chapra (2008) added that “an essential corollary of human dignity is that need fulfillment must be realized through the individual’s own effort. The jurists have, therefore, emphasized that without fulfilling this obligation of earning a living through his own effort, a Muslim may not even be able to maintain his body and mind in a state of adequate health and efficiency”.

Accordingly, we identified two dimensions to measure ‘protection of life’ oriented performance of Islamic banks. The first dimension is adopted from Chapra (2008) who suggested creation of employment and self-employment opportunities for the enrichment of human self. Empirical studies also found a significant positive relationship between income and health (Carrieri & Jones, 2017). To measure this dimension, we suggest two elements: ‘individual

financing to total financing' and 'charity distributed to total distributable charity' on the assumption that the sooner such funds are distributed, the sooner the needy gets benefits as stated by Zaheer and Rasool (2017). The second dimension is 'investment in health and welfare', to improve quality of life of the people, measured by 'charity distributed for health and welfare purpose to total distributed charity'.

Protection of Intellect

Ashur (2006) re-phrased 'protection of intellect' as 'propagation of scientific thinking and avoidance of brain drain'. Accordingly, to measure 'protection of intellect' oriented performance, we adopted three dimensions from the literature; namely, 'employees' development, creation of awareness of Islamic banking and advancement of knowledge'. The first dimension 'employees' development' can be measured as 'training and development expense to total expense' as suggested by Dzuljastri et al. (2008) and Zaheer and Rasool (2017). However, due to unavailability of relevant data in annual reports of majority of Islamic banks operating in Pakistan, we propose alternative measure i.e., 'investment in technology to investment in total operating fixed assets' as using new technology, which includes both software and hardware, enables employees to learn new things; thus, directly affect the intellect as suggested by Chapra (2008). This notion is also endorsed by Kamali (2008) who added 'development in technology' to the list of Maqasid al-Shariah. Earlier studies also used technology to measure 'protection of intellect' oriented performance of Islamic banks (Ascarya et al., 2016; Mohammad et al., 2015). For the assessment of second dimension, i.e., 'creation of awareness of Islamic banking', we have adopted 'advertisement expense to total expense' from Dzuljastri et al. (2008); whereas for third dimension i.e., 'advancement in knowledge', we have adopted 'charity distributed in education to total charity distributed' from Mohammad et al. (2015).

Protection of Family

Ashur (2006) reinterpreted 'protection of family' as 'care of family'; whereas Mohammad et al. (2015) suggested that stakeholders of Islamic banks can be considered as their family members since Islamic banks, being operated as limited companies, are artificial persons and not real persons. On the other hand, Chapra (2008) added 'need fulfillment' as an important criteria to 'protection of family'. He states, "All these resources are a trust from God and one of the terms of the trust is that they must be utilized in such a responsible manner that the needs of all are satisfied". Accordingly, 'protection of family' oriented performance of Islamic banks can be assessed using such indicators which represents fair dealing with, or protection of rights of, various stakeholders such as shareholders, employees, customers, depositors and government. This notion is supported by the Shariah Enterprise theory which suggests that distribution of wealth should not be restricted to the participants who are associated with or contributed to companies operations; but it should also applies to all mankind (Meutia, 2010).

Accordingly, for 'protection of family' oriented performance, we adopted five dimensions, i.e., fair dealing with employees, fair dealing with depositors, fair dealings with shareholders, fair dealing with government and fair dealing with customers. To measure these dimensions, we apply standard accounting concept of 'statement of value added and distributed', which is prepared satisfying legitimacy theory which argues that "organizations can only exist if the society, in which they are based, perceive the organization to be operating to a value system

which is commensurate with the society's own value system. Legitimacy theory results in voluntary disclosures being made to show that the organization is conforming to the expectations and values of the society within which it functions" (Stainbank, 2009). The 'statement of value added and distributed' demonstrate how value is added and distributed to various stakeholders. The standard practice of computing 'value added', as adopted in annual reports of Meezan bank, is as follows:

$$\begin{aligned}
 \text{Value Added} &= \text{Profit/return on Islamic financing, investments and placements after provision} \\
 &+ \text{Fee, commission and brokerage income} \\
 &+ \text{Dividend income} \\
 &+ \text{Income from dealing in foreign currencies} \\
 &+ \text{Capital gain on sale of securities and other income} \\
 &- \text{Administrative and other expenses excluding staff cost, depreciation,} \\
 &\quad \text{amortization, and workers welfare funds}
 \end{aligned}$$

The above stated 'value added' is distributed among various stakeholders as summarized below.

- i) Employees: Value distributed to employees includes salaries, allowances and other benefits.
- ii) Shareholders: Value distributed to shareholders include dividend paid to them and retained earning added in shareholders' equity.
- iii) Depositors: Value distributed to depositors includes profit or return given to depositors.
- iv) Government: Value distributed to government includes taxes paid to the government.

We suggest 'value distributed' to each stakeholder as a percentage of total valued added' as a possible indicator to measure the level of fulfillment of each stakeholder's need while evaluating 'protection of family' oriented performance of Islamic banks (See Table 1 below). Additionally, since the 'statement of value added and distributed' ignores customers as no value is distributed back to them, we propose market share, measured as 'bank's financing to industry's total financing', as a proxy of customer satisfaction to evaluate 'fair dealing with customers'. This notion is based on widely quoted 'service-profit chain' logic which suggests that improved service quality results in better customer satisfaction and customer loyalty leading towards increased market share (Heskett, Jones, Loveman, Sasser, & Schlesinger, 1994; Stodnick, 2005). Empirical studies also found positive relationship between customer satisfaction and market share (Kamakura, Mittal, De Rosa, & Mazzon, 2002).

Protection of Wealth

Ashur (2006) reinterpreted 'protection of wealth' as 'wellbeing of society' and 'minimizing income and wealth disparity'; Al-Shatibi, as cited by Raysuni (1997), affirms that it is 'the prohibition against injustice, depriving orphan of his property and wastefulness'. Chapra (2008) considers it as 'development and expansion of wealth' while Dusuki and Bouheraoua (2011)

consider it as ‘protection of value’. Consequently, to measure ‘protection of wealth’ oriented performance of Islamic banks, we acknowledged three elements; namely, ‘protection from damage’, ‘growth of wealth’, and ‘protection from depriving someone of his property’.

To measure these elements, we applied CAMEL ratios which comprise a standard test to assess financial health of banks. CAMEL ratios include capital adequacy, asset quality, management quality, earning ability, and liquidity ratios. Accordingly, for assessing ‘protection from damage’, we use asset quality and liquidity ratios. Asset quality ratio, i.e., ‘net financing to gross financing’, measures impairment in assets; whereas liquidity, measured as ‘liquid asset to total deposit’, enables the bank to easily meet its financial obligations and protect its reputation from being damaged. For assessing ‘growth of wealth’, we suggest ‘return on equity’, measured as ‘profit after tax to net assets’. For assessing ‘protection from depriving someone of his property’, we use capital adequacy ratio i.e., ‘available capital to risk weighted assets’. This ratio assesses the degree of protection provided to depositors’ funds by ensuring that the bank has sufficient cushion to absorb losses before it becomes insolvent and, as a result, loses depositor’s funds. Table 1 below show the proposed index.

Table 1
Maqasid Based Performance Index

Maqasid/ Objective	Dimensions	Elements/Indicators	Reference	
O1:Protection of Faith	D1	SC Financing	E1 Financing in Non-controversial modes/Total Financing	Suggested by Authors
	D2	SC Investment	E2 Investment in Non-controversial products/Total Investment	Suggested by Authors
O2:Protection of Life	D3	Employment Opportunities	E3 Individual Financing/Total Financing	Suggested by Authors
			E4 Zakat & Charity distributed/Distributable Zakat & Charity	Zaheer and Rasool (2017)
	D4	Investment in Health & Welfare	E5 Charity distributed for Health & Welfare/Total charity distributed	Suggested by Authors
O3:Protection of Intellect	D5	Employee Development	E6 Investment in Technology/Investment in operating assets	
	D6	Awareness of IB	E7 Publicity & Advertisement Expense/Total Expense	Dzuljastri et al. (2008)
	D7	Advancement of Knowledge	E8 Charity distributed for Education/Total charity distributed	Mohammad et al. (2015)
O4:Protection of Family	D8	Employees	E9 % of value added distributed to employees	Suggested by Authors
	D9	Depositors	E10 % of value added distributed to depositors	Suggested by Authors
	D10	Shareholders	E11 % of value added distributed to shareholders	Suggested by Authors
	D11	Government	E12 % of value added distributed to government	Suggested by Authors
	D12	Customer	E13 Bank’s Financing/Total Financings of IB’s Sector	Suggested by Authors
O5:Protection of Wealth	D13	Protection from damage	E14 Net financing/gross financing	Suggested by Authors
			E15 Liquid asset/total deposit	Zaheer and Rasool (2017)
	D14	Growth in wealth	E16 Profit after tax/Net assets	Zaheer and Rasool (2017)
	D15	Protection from depriving	E17 Available capital to risk weighted assets	Zaheer and Rasool (2017)

Verification of the Proposed Index

The proposed dimensions and elements have been verified through experts’ interviews. Five Shariah scholars associated with Islamic banking industry and five Islamic finance experts from

academia have been interviewed. The following questions were asked during face to face interviews having average duration of 30 minutes.

1. What is the purpose of Islamic banking?
2. Do you think that Islamic banks should be evaluated using the framework of *Maqasid al-Shariah* to appraise their role in an Islamic economy?
3. Do you think that *Maqasid al-Shariah* can be operationalized using ‘proxy variables’; e.g., ‘CSR in education to total CSR’ to measure ‘protection of intellect’ oriented performance?
4. Would you please look at the proposed index and comment on its validity?

Answering the first question, all the experts agreed that the purpose of Islamic banking is to provide Shariah compliant alternatives of conventional products; nevertheless, they are business entities like their counterparts hence they can make profits within the boundaries of Shariah. Responding to the second questions, all the experts had the opinion that the social role of Islamic banks should preferably be assessed using the framework of *Maqasid al-Shariah* as conventional measures for social performance reflect secular standards and ignore the Islamic world view. However, one of the experts added: “Although, in theory, all the *Maqasid* can be related to Islamic banking; nevertheless, in practice, all of them may not be equally relevant. Similarly, contributing towards the development of society is always appreciated; but it should not be considered mandatory for Islamic banks. Therefore, except ‘protection to faith’ oriented performance’, other *Maqasid* oriented performance may not be considered as a benchmark to assess the legitimacy of Islamic banking. However, Islamic banks should not be involved in such activities which contradict any of these *Maqasid al-Shariah*”. As far as the third question is concerned, all the experts were unanimous upon the possibility of operationalization of *Maqasid* using ‘proxy variables’ provided that these ‘proxy indicators’ accurately represent the stated *Maqasid*. Finally, responding to the fourth question, all the experts verified the suitability of the dimensions and elements used in the proposed study after exhaustively discussing the relevant theories, logics and concepts.

Weight allocation to Dimensions and Indicators

We apply experts’ survey method to assign weights to identified elements and objectives. This method is widely used in the literature (Dzuljastri et al., 2008; Zaheer & Rasool, 2017). Accordingly, twenty Shariah experts, associated with the Islamic banking industry, were requested to assign weights to identified elements as well as *Maqasid* according to their significance from the perspective of Islamic banking. The average weights, given by the experts, are shown in Table 2 below.

Table 2

Average Weights Assigned by Experts

Maqasid/Objectives	Average Weight	Elements/Indicators	Average Weight
O1: Protection of Faith	0.30	E1 Financing in Non-controversial modes/Total Financing	0.50
		E2 Investment in Non-controversial products/Total Investment	0.50
		Total	1.00
O2: Protection of Life	0.14	E3 Individual Financing/Total Financing	0.31

		E4	Zakat & Charity distributed/Distributable Zakat & Charity	0.32
		E5	Charity distributed for Health & Welfare/Total charity distributed	0.37
		Total		1.00
O3: Protection of Intellect	0.05	E6	Investment in Technology/Investment in operating assets	0.22
		E7	Publicity & Advertisement Expense/Total Expense	0.24
		E8	Charity distributed for Education/Total Charity distributed	0.54
		Total		1.00
O4: Protection of Family	0.23	E9	% of value added distributed to employees	0.19
		E10	% of value added distributed to depositors	0.27
		E11	% of value added distributed to shareholders	0.26
		E12	% of value added distributed to government	0.08
		E13	Bank's Financing/Total Financings of IB's Sector	0.20
		Total		1.00
O5: Protection of Wealth	0.28	E14	Net financing/gross financing	0.23
		E15	Liquid asset/total deposit	0.20
		E16	Profit after tax/net assets	0.33
		E17	Available capital/risk weighted assets	0.24
Total	1.00	Total		1.00

Using the weights of different Maqasid and elements shown in Table 2, Maqasid based Performance will be assessed using the following equation.

$$MSI = \sum W_i (\sum W_j E_j)_i$$

Where

MSI *Maqasid al-Shariah* Index

W_i Weight of the Object

W_j Weight of the Element

E_j Value of the Element

Maqasid Orientation Of Islamic Banks

The proposed index is applied to assess Maqasid orientation of Islamic banks in Pakistan using eight years data from audited financial statements (2010-2017). The Islamic banking industry in Pakistan consists of 21 Islamic banking institutions including five full-fledged banks and sixteen standalone Islamic banking branches of conventional banks. However, we exclude the Islamic banking branches of conventional banks for having vivid figures. As MIB Islamic bank was established in 2015, we exclude it as well because its annual reports are available for the year 2015 onward. Hence our sample includes four full-fledged Islamic banks of Pakistan; i.e., Meezan Bank, Bank Islami Pakistan, Al Baraka Bank and Dubai Islamic bank, Pakistan. The

average market share of these banks in the overall Islamic banking industry of Pakistan remains approximately 67% in terms of financing⁴ during the observed period (2010-2017).

The index values range between 0 and 1. The design of the proposed index suggests that the higher the index the better would be the performance of the bank. Therefore, reciprocal of administrative expenses to total income is taken to align the results with the design of the proposed index. The average results of the whole sample are shown in Table 3 below:

Table 3
Maqasid Orientation of Sample Banks: Average Results

Elements/Objectives	2010	2011	2012	2013	2014	2015	2016	2017
SC financing	1.0000	0.9971	0.9965	0.9806	0.9494	0.9047	0.8941	0.8223
SC investment	0.9867	0.9932	0.9892	0.9848	0.9852	0.9337	0.8945	0.8671
Protection of faith	0.9934	0.9952	0.9929	0.9827	0.9673	0.9192	0.8943	0.8447
Individual financing	0.1963	0.1802	0.1611	0.1365	0.1339	0.1210	0.1812	0.1775
Charity distributed	0.4461	0.4694	0.2840	0.5960	0.6106	0.5784	0.7342	0.7480
Charity for health	0.8368	0.8696	0.8043	0.6342	0.6610	0.6991	0.7205	0.5850
Protection of life	0.5132	0.5278	0.4384	0.4677	0.4815	0.4813	0.5577	0.5108
Investment in Technology	0.7578	0.7610	0.7975	0.7870	0.7587	0.7549	0.7663	0.8023
Advertisement & Publicity	0.0128	0.0175	0.0167	0.0138	0.0194	0.0156	0.0139	0.0131
Charity for education	0.1632	0.1304	0.1957	0.3658	0.3390	0.3009	0.2776	0.4150
Protection of Intellect	0.2579	0.2420	0.2851	0.3740	0.3546	0.3323	0.3218	0.4038
Value distributed to employees	0.3402	0.1754	0.1923	0.2103	0.2120	0.2542	0.2748	0.2994
Value distributed to depositors	0.9848	0.6325	0.6971	0.6572	0.6215	0.5943	0.5376	0.5156
Value distributed to shareholders	-0.1711	0.1560	0.0901	0.1039	0.1245	0.1097	0.1302	0.1767
Value distributed to government	-0.1537	0.0361	0.0205	0.0285	0.0420	0.0418	0.0575	0.0082
Market Share	0.1580	0.1536	0.1768	0.1806	0.1911	0.1652	0.1672	0.1510
Protection of Family	0.3054	0.2783	0.2852	0.2828	0.2820	0.2737	0.2692	0.2729
Quality of Financing	0.9534	0.9524	0.9517	0.9592	0.9657	0.9628	0.9679	0.9722
Liquidity	0.2382	0.1829	0.1899	0.2113	0.2787	0.3135	0.2531	0.1984
Profit after tax	0.2481	0.1146	0.0692	0.0606	0.1102	0.2167	0.4007	0.1067
CAR	0.1807	0.2038	0.1487	0.1360	0.1498	0.1225	0.1196	0.1278
Protection of wealth	0.6198	0.7079	0.6525	0.6249	0.6513	0.6357	0.6465	0.5617
Overall Maqaid Index	0.6265	0.6468	0.6218	0.6190	0.6226	0.6007	0.6054	0.5652

⁴ Market share is computed by authors using data given in annual reports of stated banks and Islamic banking bulletin December 2017; issued by the State Bank of Pakistan.

The results reveal that ‘protection of faith’ oriented performance of Islamic banks has declined steadily over the period as its index value was 0.99 in 2010 whereas in 2017 the value was decreased to 0.84 due to gradual increase in financing and investment through controversial products. Despite the decline in ‘individual financing’ and ‘charity for health’, the index values of ‘protection of life’ is the same in 2010 and 2017 due to increase in charity distributed. ‘Protection of intellect’ performance is improved over the period from 0.26 in 2010 to 0.40 in 2017 mainly because an increased portion of distributable charity is now allocated to the educational sector. However, still it is far below from the maximum possible value. The ‘protection of family’ oriented performance also slightly decreased from 0.31 in 2010 to 0.27 in 2017; mainly due to lesser distribution of value to the depositors and employees. Similarly, the ‘protection of wealth’ oriented performance also deteriorated from 0.62 in 2010 to 0.56 in 2017; mainly due to decrease in profit after tax and capital adequacy ratio. Finally, overall Maqasid al-Shariah oriented performance also deteriorated from 0.63 in 2010 to 0.57 in 2017. Though, ‘protection of life’ oriented performance of Islamic banks is near to 1, however, index values of ‘protection of life’, ‘protection of wealth’ and overall Maqasid index are about half of the maximum possible value; whereas index values for ‘protection of intellect’ and ‘protection of family’ is less than half of the maximum possible values which indicate poor Maqasid realizations.

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Protection of wealth	0.6198	0.7079	0.6525	0.6249	0.6513	0.6357	0.6465	0.5617
Overall Maqaid Index	0.6265	0.6468	0.6218	0.6190	0.6226	0.6007	0.6054	0.5652

Conclusion

Maqasid al-Shariah can be considered as any factors which are used for determining the appropriateness and suitability of any reform program in an Islamic social sciences paradigm and their conformity with ideology, doctrines and objectives of Islamic Law. In the context of Islamic banking, the framework of Maqasid al-Shariah requires that Islamic banks should avoid prohibited elements in their transactions, attain welfare, remove exploitation, promote cooperation and brotherhood as well as uphold justice to facilitate equitable distribution of wealth. Since Islamic banks are being criticized on grounds of convergence to their conventional counterparts due to copying conventional products while focusing only on the ‘legal’ aspect and ignoring the ‘substance’ of the transaction, it is important to evaluate their Maqasid oriented performance to form a justifiable opinion about their social role in an Islamic economy. To measure such performance, the present study constructs an improved index which is more reflective of Maqasid oriented performance of Islamic banks as existing indices have been criticized on grounds of limited scope, use of irrelevant indicators, partial inapplicability and based on ‘narrated performance’ rather than ‘actual performance’.

The study uses Imam Ghazali’s theory and its reinterpretation made by contemporary scholars, implements Sekaran’s behavioral science method and applies social accounting concept of ‘value added statement’ and ‘service profit chain’ logic to develop Maqasid index which is later validated through exhaustive interviews with the experts. In addition, the present study also explores the Maqasid orientation of Islamic banks operating in Pakistan by applying the proposed index on four full-fledged Islamic banks using eight years’ quantitative data from audited financial statements (2010-2017). On average, the sample banks represent approximately 67% of overall Islamic banking industry of Pakistan in terms of financing over the period 2010-2017. The results revealed that except ‘protection of intellect’ oriented performance, all other Maqasid oriented performances are deteriorating. Similarly, except ‘protection of faith’ oriented performance, all the other performances are far below the maximum possible values indicating poor Maqasid realizations by Islamic banks operating in the country.

Implications

This proposes an improved index which is more reflective of Maqasid orientated performance of Islamic banks as it is based on ‘actual performance’ rather than ‘narrated performance’. It covers all the Maqasid from Ghazali’s theory and uses such data which is both relevant and accessible. By adding more dimensions and elements to the five Maqasid al Shariah, the performance of Islamic banks can be gauged by using the improved index. It might be helpful in creating discipline in Islamic banks to focus on substance of the contracts for achieving the socio-economic objectives of Islamic banking and finance.

Future Research Directions

The proposed index can be used for future empirical studies exploring relationship between Maqasid oriented performance and financial performance of not only the full-fledged Islamic banks but also, the stand-alone Islamic banking system of the conventional banks and other Islamic financial institutions.

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