

Morabaha Financing

Most of the Islamic banks and financial institutions are using "Murabahah" as an Islamic mode of financing, and most of their financing operations are based on "Murabahah". That is why this term has been taken in the economic circles today as a method of banking operations, while the original concept of "Murabahah" is different from this assumption.

"Murabahah" is, in fact, a term of Islamic Fiqh and it refers to a particular kind of sale having nothing to do with financing in its original sense. If a seller agrees with his purchaser to provide him a specific commodity on a certain profit added to his cost, it is called a "murabahah" transaction. The basic ingredient of "murabahah" is that the seller discloses the actual cost he has incurred in acquiring the commodity, and then adds some profit thereon. This profit may be in lump sum or may be based on a percentage.

The payment in the case of murabahah may be at spot, and may be on a subsequent date agreed upon by the parties. Therefore, murabahah does not necessarily imply the concept of deferred payment, as generally believed by some people who are not acquainted with the Islamic jurisprudence and who have heard about murabahah only in relation with the banking transactions.

Murabahah, in its original Islamic connotation, is simply a sale. The only feature distinguishing it from other kinds of sale is that the seller in murabahah expressly tells the purchaser how much cost he has incurred and how much profit he is going to charge in addition to the cost.

If a person sells a commodity for a lump sum price without any reference to the cost, this is not a murabahah, even though he is earning some profit on his cost because the sale is not based on a "cost-plus" concept. In this case, the sale is called "Musawamah".

This is the actual sense of the term "Murabahah" which is a sale, pure and simple. However, this kind of sale is being used by the Islamic banks and financial institutions by adding some other concepts to it as a mode of financing. But the validity of such transactions depends on some conditions which should be duly observed to make them acceptable in Shari'ah.

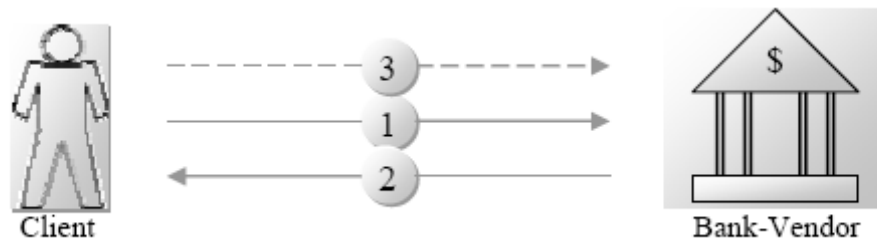
In order to understand these conditions correctly, one should, in the first instance, appreciate that murabahah is a sale with all its implications, and that all the basic ingredients of a valid sale should be present in murabahah also. Therefore, this

discussion will start with some fundamental rules of sale without which a sale cannot be held as valid in Shari'ah. Then, we shall discuss some special rules governing the sale of Murabahah in particular, and in the end the correct procedure for using the murabahah as an acceptable mode of financing will be explained.

An attempt has been made to reduce the detailed principles into concise notes in the shortest possible sentences, so that the basic points of the subject may be grasped at in one glance, and may be preserved for easy reference. agent to receive the goods purchased by the bank.

Mechanism:

The simplest possible structure emerges when the transaction involves two parties only – the client and bank. The bank is also the vendor and sells the commodity to its client on a deferred payment basis. From a Shariah point of view, such a structure is the most ideal one. Its profits are fully justified by the risk it assumes as a vendor and there is no suspicion of riba. This structure is presented below. This structure has recently been used in car financing products as will be discussed later. The bank in this case claims to have its own car show rooms from where its clients may purchase cars on a deferred payment basis. The financing structure comprising several activities may be presented as follows.



1. Client approaches Bank-Vendor and identifies commodity, collects relevant information that includes base price and the mark-up;
2. Bank sells commodity, transfers ownership and possession to Client at marked-up price;
3. Client pays marked-up price in full or in parts over future (known) time period(s).