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CONTRIBUTIONS TO BOOKS

- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

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- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

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- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

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- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, Kurukshetra University, Kurukshetra.

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ISLAMIC BANKING IN INDIA: DEVELOPMENTS, PROSPECTS AND CHALLENGES

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ABSTRACT

Indian financial system has witnessed lot of changes in recent past. The most important of them all are deregulation of Indian banking sector and the opening of new banks. Islamic bank is a new global phenomenon, which India should recognize in developing Indian financial system. This study is carried out to evaluate the developments and to measure the prospects as well as the challenges faced by the movement of Islamic banking in India. This paper reveals that Islamic banking in India has real potential to grow along with the conventional banking system. Our aim is to draw the attention of Indian regulators, Islamic finance scholars and business activists to think over the measures to be adopted in developing Islamic banking in India. It also provides necessary measures to allow conventional banks to carry on Islamic banking business using the existing financial infrastructure.

KEYWORDS
Islamic Banking, Developments, Prospects, Challenges, India.

1. INTRODUCTION

Islamic Banking is a system of banking based on Islamic law (known as Shariah). Shariah forbids the payment or acceptance of interest (known as *riba* or usury) for the well being of the society. Interest from the conventional bank and economic arguments can lead to the divide between the rich and poor, and inflation which can create financial and economic instabilities. Islamic banking has grown out from the conventional banking only in the year 1971. However, still at infancy stage, its growth has been tremendous and impressive. Now, not only Muslim countries but also Western countries have adopted Islamic banking. Despite the growth and confidence towards Islamic banking, there are still few countries which have not implemented Islamic banking in their economies, including India. This paper, hence, is aimed to discuss Islamic banking in India.

2. GLOBAL OUTLOOK ON ISLAMIC BANKING

Islamic Banking is a value based system that principally aims at ensuring moral and material well being of the individual and society as a whole (Ahmad, 1994; Naqvi, 1981; Zarqa, 1983). Islamic banks were almost non-existent 40 years ago. However, it started to grow in mid 1980s; the first financial company in recent history based on Shariah was the Mit Ghamr savings project in Egypt. The Mit Ghamr co-operative society allowed depositors to borrow for fruitful reasons. In addition, the project attracted funds to invest in projects on a profit-sharing basis. In 1971, the project was incorporated in Nasser Social Bank. From a handful of banks in the late 1970s, including the Islamic Development Bank and Dubai Islamic Bank, there has been significant growth in Islamic banking industry (Warde, 2000).

Since the late 1990s the industry has been growing at an annual rate of 10–15%. The number of banks offering Islamic financial services is growing and is no longer limited to small niche banks. Nowadays, conventional banks jointly contribute to the growth of Islamic finance via Islamic Window (Schoon, 2008). Islamic banking has become a worldwide inclination. There are over 500 Islamic banking institutions operating all over the world from Africa and Europe to Asia and Australia. According to International Islamic Finance Forum, the total assets under management world over in Islamic Banking and Finance are predicted to increase to $1 trillion by 2013 (Shamshad, 2011). The Asian Development Bank projected Islamic Banks' annual growth at more than 50% over the next 5-10 years. Highly Potential global market of 2 billion Muslims is drawing tremendous attention from players all over the world (Khan et al., 2012).

To support the growth and development of Islamic banking and finance in Singapore**,** the Monetary Authority of Singapore has set the development of Islamic finance as one of its priority and has accordingly aligned tax policies. Even, China has opted for Islamic banking to pool Islamic Investment Funds. Malaysia has proven itself as pioneer of Islamic banking and finance. There are 16 Islamic banks and 5 International Islamic banks in Malaysia (Bank Negara Malaysia, 2011). More than 40% of the investors and 60% borrowers in Malaysian Islamic banks are non-Muslims. One-fifth customers of Islamic banks of Britain are non-Muslims. Therefore, it can be said that Islamic banking is not just for Muslims but it's a mechanism for financing business to all without charging interest. Segrado (2005) has observed that Islamic banking is growing at an average rate of 15% a year, which makes it the fastest growing sector in the financial markets of the modern-day world. The Asia-Pacific region accounts for 60% of the global Islamic banking market and this proves the potential of Islamic banks (Platt, 2009). According to Zaher and Hassan (2001), Islamic banking is making waves in all corners of the world from Malaysia, through the Middle East and Africa, to Europe and America.

3. DEVELOPMENT OF ISLAMIC BANKING IN INDIA

3.1 HISTORICAL DEVELOPMENTS

The work on Islamic finance in India has started in the beginning of the 20th century. According to Shariq Nisar, it can be classified as literary and practical. The literature available was primarily in Urdu, the rest being either in English or in Arabic. The first book published in English on the Islamic finance was *Islam and the Theory of Interest* in 1946 written by Professor Anwar Iqbal Qureshi of Usmania University Hyderabad. On the practical side, *Anjuman Mowudul Ikhwan* a welfare association, established in 1890 by a famous *alim* of Hyderabad. This was later managed by his son Syed Mohammad Badshah Husaini. The society collected donations and skins of sacrificed animals from the public and provided interest free loans to weaker section (Nisar, 2002).

In north India, the Muslim Fund Tanda Bavli, Rampur was established in 1941. Unfortunately, the fund was closed due to partition of India. After about fifteen years since partition, the Muslim Fund Deoband (MFD) was established in the year 1961, and is still operating. Muslim Fund Najibabad (MFN) was established on the model of MFD in 1971. In 1990, MFN floated a subsidiary, Al-Najib Milli Mutual Benefits Ltd. (Bagsiraj, 2002a).

In western India, the Patni Co-operative Credit Society, Surat (Gujarat) was established in 1938 and is still in operation to provide interest free loans to its members without any collateral security or service charges. This region showed great efforts to establish a co-operative credit society. The result of the efforts was recognized in the form of establishment of the Modern Education Social and Cultural Organization (MESCO) by a few college students of Bombay (now

Mumbai) in the year 1968. MESCO led to the establishment of Baitun-Nasr Urban co-operative credit society (BUN), commenced functioning in the year 1973. Restriction on the operation of the society beyond the geographical boundary of Bombay and certain other restrictions leads to the formation of Barkat Investment Group (BIG) in the year 1983 (Nisar, 2002). BIG and Tata Mutual Fund came together in 1996 to launch a mutual fund scheme especially designed for Muslims in view of their inhibitions about interest, though it has never being regarded as Shariah compliant fund as no Shariah advisor involved for screening of the fund. The scheme named Tata Core Sector Equity Fund. But, the fund name was changed four times due to various reasons in past and presently known as Tata Ethical Fund (Adajania, 2011).

3.2 RECENT DEVELOPMENTS

Over the last decade, a number of significant changes have occurred in the Indian banking sector with a view to raise the efficiency and productivity of banks as a whole.

3.2.1 ANAND SINHA COMMITTEE

With an objective to reach the banking system to more people in India, Reserve Bank of India (RBI) had constituted a committee in June 2005 to examine financial instruments used in Islamic banking headed by Mr. Anand Sinha, deputy director of RBI. Two observations were made by the committee; First, appropriate modification should be made in banking regulation act 1949 along with separate rules and regulations. Secondly, taxation proposition have to be examined. But, the idea of Islamic banking was rejected by RBI saying that it is not feasible for Indian banks to undertake Islamic banking or to allow their branches to carry out Islamic banking operations abroad without amendments in current related banking and other laws.

3.2.2 RAGHURAM RAJAN COMMITTEE

In 2008, the Planning Commission of India appointed a committee, headed by International Monetary Fund (IMF) former chief economist, Raghuram Rajan, to recommend various ways to take the country's financial sector reforms forward. Raghuram Rajan committee has made two major recommendations. These recommendations have given a boost to the demand of Islamic banking in India. First, committee recommended that measures should be taken to permit the delivery of interest free finance on a larger scale, through the banking system and this is in accordance with the objectives of inclusion and growth through innovation. The committee affirms that interest free banking is currently provided in a limited manner through Non Banking Financial Companies (NBFC) and cooperatives. Second, the committee believed that it would be possible only through appropriate measures to create a framework for such products without any adverse systemic risk impact.

3.2.3 PARLIAMENTARY COMMITTEE

Apart from the two important committees, there was another important development which has provided strength to the demand of Islamic banking and finance in India. It was revealed from the report of the Parliamentary committee set up by Prime Minister, headed by Mr.Rahman Khan, Ex-deputy chairman Rajya Sabha has recommended to create a Hajj pilgrimage fund based on Shariah principles. Lack of Shariah compliant investment opportunities in India has discouraged Muslims to invest, not only through banks but also through stock market. The Securities and Exchange Board of India (SEBI) has given approval for India's first official Shariah compliant mutual fund scheme "Taurus ethical fund" in 2009. The Taurus Mutual Funds and Parsoli corp. had applied the fund's offer document in October 2007, initially SEBI had some reservations on the fund, as it targeted a particular community (Islamic Finance News, 2009).

3.2.4 KERALA GOVERNMENT INITIATIVE

In 2010, Kerala State Industrial Development Corporation (KSIDC), a wholly owned Kerala state government company, got into an agreement with Al Barakah group to offer Shariah compliant finance to the Muslim community. In the proposed Islamic financial institution, KSIDC holds 11% stake. However, The government order was challenged by Janata Party leader Subramanian Swamy in the Kerala High Court arguing that association of government agencies in setting up Islamic investment company goes against secular principles preserved in Indian constitution and was stayed on grounds of violation of Article 14, 25, and 27. In February 2011, Kerala High court has dismissed the petition filed by Subramanian Swamy and maintained setting up of an Islamic investment company.

3.2.5 PRESENT SCENARIO

In June 2012, Chairman of national commission for minorities has proposed to Ministry of Finance (MoF) to take a fresh account of the matter after RBI has again rejected the possibility of Islamic banking in India. Consequently, MoF has asked the RBI to examine the possibility of Islamic banking model a part of Indian banking system. In October 2012, RBI governor confirmed their discussion with MoF on amendments in existing laws to accommodate Islamic banking in India (Unnikrishnan, 2012). This positive move of RBI certainly paves a path and gives an insight of the future of Islamic banking in India.

India has strong ability to emerge as a potential market for Islamic banking, provided there is supportive political environment and increased awareness among people in India as a whole. Presently, there is no Islamic bank in India except few Shariah compliant funds and several other Islamic financial institutions and credit cooperative societies. India is in prime need of an Islamic bank because as per Sachar committee report, about 80% Indian Muslims are financially excluded due to interest based deposit and credit from conventional banks. In addition to that, RBI reports that Muslims have a Credit Deposit Ratio (CDR) of 47% against the national average of 74% (Majumdar, 2008). It is to note that CDR is a monetary tool which maximizes the credit flow and ensures better deployment of credit. As per the RBI, if the CDR is low, the weaker sections will be the most affected along with other borrowers. Hence, the lesser credit flow from banks to Muslims would widen the gap between the weaker sections and economically sound sections.

4. PROSPECTS AND BENEFITS OF ISLAMIC BANKING IN INDIA

The prospects of Islamic banking in India are bright; with reference to demographic structures and the benefit of Islamic banking in itself.

4.1 DEMOGRAPHIC ADVANTAGE

India is at an advantage due to its Muslim population. Islamic banking has been augmented in Asia-Pacific region, now account for 60% of the global Islamic banking market. Despite its rise in the rest of the region, the adaptation in India of the same has been low. It is very surprising mainly because according to Pew Research Center, India is the 3rd largest Muslim populated country after Indonesia and Pakistan, having approximately 177 million Muslims, which is 14.6% of total Indian population (Grim and Karim, 2011). According to India census 2001, Muslim population enumerates at over 138 million.

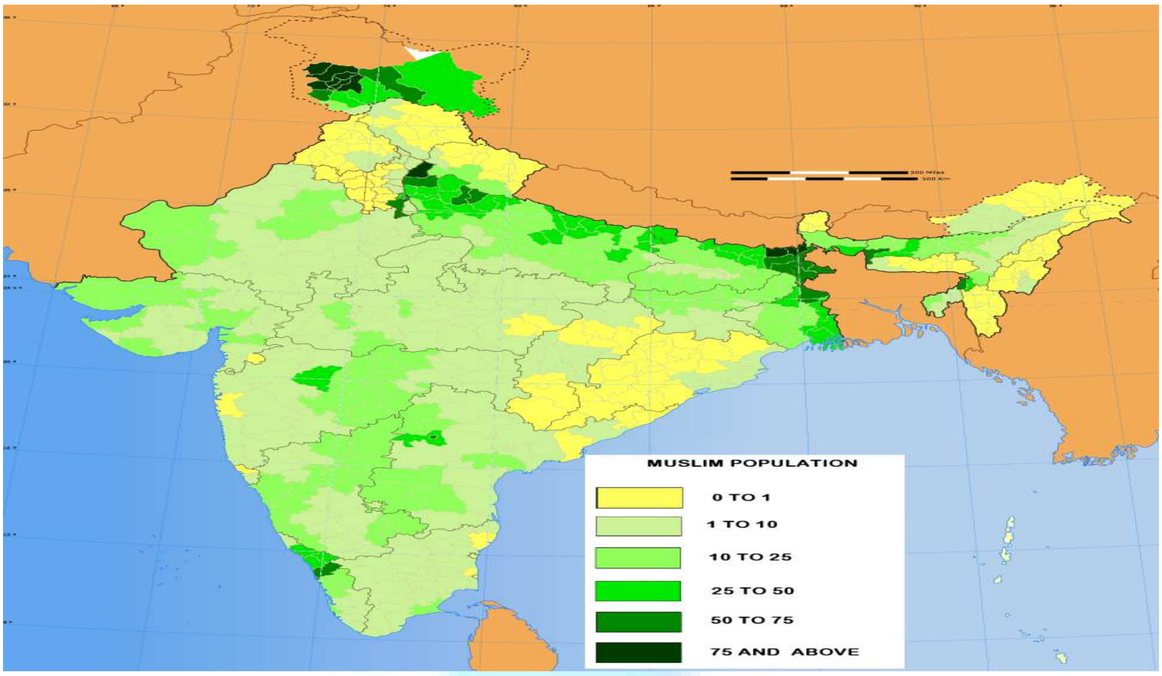
In terms of the state wise distribution, the majority of the Muslims in India are based mainly in four states Uttar Pradesh, Bihar, West Bengal and Maharashtra with at least 10 million Muslims each. Uttar Pradesh has the largest Muslim population in India with around 30 million Indian Muslims living, as shown by the census 2001. The other states with a considerable Muslim population are Kerala, Andhra Pradesh, Assam, Jammu and Kashmir and Karnataka with a population of between 5 to 10 million Muslims each. Rajasthan, Gujarat, Madhya Pradesh, Jharkhand and Tamil Nadu have Muslim population of between 3 to 5 million each. Delhi, Haryana and Uttaranchal have 1 to 2 million each.

TABLE 1: NUMBER OF DISTRICTS BY MUSLIM POPULATION SIZE AND CONCENTRATION, CENSUS 2001

Percentage of Muslims in the total population of the district	Number of districts
75 or more	9
50 or more but less than 75	11
25 or more but less than 50	38
10 or more but less than 25	182
1 or more but less than 10	276
Less than 1	77
Total	593

A report on social, economic and educational status of the Muslim community of India (Sachar, 2006).

FIGURE A: MAP OF INDIA SHOWING MUSLIM POPULATION ON DISTRICT BASIS.



A report on social, economic and educational status of the Muslim community of India (Sachar, 2006).

According to district wise distribution, Committee reports that out of 593 districts in India, 20 have Muslim majority. Nine have over 75% Muslim population; these include Lakshadweep and eight districts in Jammu and Kashmir as shown in table 1. The other 11 districts have between 50 to 75% Muslim population. These are extended in following states: 6 districts of Assam, 2 districts of Jammu and Kashmir, as well as 1 district each for West Bengal, Bihar and Kerala. Nearly 18 Million people lived in these districts, making about 13% of India's Muslim population as shown in table 1 (Sachar, 2006).

A further 38 districts have a noteworthy Muslim population of between 25 to 50%. These are scattered in a number of states as follows. Uttar Pradesh 12 districts, West Bengal 5 districts, Kerala 5 districts, Assam 4 districts, Bihar 3 districts, Jharkhand 2 districts, Delhi 2 districts and 1 district each in Andhra Pradesh, Haryana, Jammu and Kashmir, Uttaranchal and Pondicherry. These districts accounts for around 30 Million people, about 22% of the Muslim population.

182 districts have a significant Muslim population between 10 to 25%. These districts accounted for nearly 47% of the Muslim population, around 65 Million people. In about 276 districts Muslim population is between 1 to 10% of the population. For the remaining 77 districts Muslim population is between 0 to 1% and these 353 districts have nearly 25 Million people, about 18% of India's Muslim population.

The demand for Islamic banking by Muslims in India is supported by a survey conducted by Bagsiraj (2002b) which revealed that 80% urban Muslims in India are all set to deposit or invest on Profit Loss Sharing (PLS) basis and 67% urban Muslims are willing to borrow from Islamic financial institutions.

4.2 SIGNIFICANT FLOW OF FUNDS

The absence of Islamic banking is an obstacle to the flow of substantial funds into the market. According to Shariq Nisar, Director, TASIS, there is approximately INR 50 billion unclaimed interest in Kerala state alone. People generally choose to invest their money in gold or jewellery, which is regarded as worst kind of investment. There are at least 300 Islamic societies which accept deposits and lend money, but can't make a business of it because of the Shariah prohibition of interest. And these Islamic societies cannot convert themselves into bank because the regulation restricts interest free banking. Some of these societies have collected more than INR 2 billion in interest-free deposits, but they do not have any opportunity to invest the fund (Sampath, 2008).

4.3 EVADING PETRO-DOLLAR LOSS

Islamic banking is expected to benefit Indian government through diplomatic rewards in financial dealings with Muslim dominated nations. Particularly, trillion dollars finance from Gulf Cooperation Council (GCC) countries can be attracted. The GCC countries interest in venture capitalism and real estate financing can help in infrastructure development in India. In 11th five year plan the expected total investment in infrastructure is to be INR 2,056,150 crores (1 crore = 10 million). Out of which INR 1,436,559 crores are expected to be met from public investment and Rs.619,591 crores from private investments (Planning Commission of India, 2008). Due to absence of Islamic banking, India is losing millions of petro-dollars which are now moving to countries like UK, China, Singapore, Malaysia and Japan.

4.4 LARGE NUMBER OF SHARIAH COMPLIANT COMPANIES

According to Ashraf Mohamedy, MD, Idafa investments, there are almost 80% of the Indian companies are Shariah compliant to the extent their business in India is concern. In the year 2009, SEBI has given licenses for Shariah compliant portfolio products. In 2011, National Stock Exchange (NSE) with Ratings Intelligence Partners (a London/Kuwait-based global Islamic consulting company) has launched NSE Shariah Index *S&P CNX 500 Shariah.* Whereas, in the same year Bombay Stock Exchange (BSE) with Taqwaa Advisory and Shariah Investment Solutions (TASIS) has launched a Shariah Index known as *BSE TASIS Shariah 50*. According to Shariq Nisar, the Director of TASIS, BSE has the highest number of Shariah compliant companies across the globe.

4.5 PROJECT FINANCING FOR ECONOMIC GROWTH

The financing in Islamic banking concerns more with the viability of projects instead of credit worthiness of borrowers. In other words, Islamic banking is financing projects which link to the economic growth. According to Siddiqi and Khan (2003) interest based loans give advantage to credit-worthy individuals and do not necessarily finance profitable projects. Conventional banking system priorities credit worthiness of the client rather than expected profitability of the project. At times promising projects might fail to receive finance if it comes from one who does not have a guarantee to support the project. The emphasis on equity and profit sharing which is the key aspect to determine whether a project is worth financing is a valuable asset of implementing the Islamic banking in India.

Furthermore, the inadequate capital investment in unorganized sector can receive a boost through equity finance promoted by Islamic banking. This sector normally lacks collateral, hence are not eligible for debt financing. Islamic banking can overcome this situation and thus can lead to the next revolution in agriculture and unorganized sector.

4.6 SAFEGUARD AGAINST ECONOMIC DECLINE

As per the global downturn scenario, Islamic banks are a solution to the economic decline. One of the important factor which leads to international financial crisis are innovative financial products, transactions and short selling. Islamic banks are shielded from interest based transactions because Shariah prohibits interest as well as short selling.

4.7 INCOME DISPARITY REDUCTION

According to United Nations Development Programme (UNDP) human development report, India needs to draw attention towards increasing income disparity as they reported it to be 36.8, quite close to worlds average and with a rising trend (UNDP, 2011). This wide income disparity in its severe ravenous from has lea to widen the divide in society. Muslims who follow Shariah do not avail credits and remain isolated. Hence, Islamic banking would assist in the upliftment and the disparity reduction.

4.8 INCREASED PARTICIPATION IN STOCK MARKET

It is expected that the introduction of Islamic banking and development of Islamic funds would lead to addition of new stock trading accounts, thereby giving a rise in the stock market. In line with Dow Jones' Islamic index, similar Indian Islamic indexes like *BSE TASIS Shariah 50* and *S&P CNX 500 Shariah* will attract funds from Muslims wishing for Shariah compliant investments.

4.9 ISLAMIC WINDOW FOR BUSINESS DIVERSITY

A growing number of commercial banks around the globe are considering the prospects of offering Islamic financial products. Banks are not only planning to offer services to a growing Muslim population, but also motivated to tap the growing global investors attracted to Shariah-compliant products. Considering the idea, Indian banks may want to explore the potential of this market, and hence may be interested in launching a pilot project.

There have been arguments that banking based on religion has limitations to spread in a secular country like India; which is not true. Britain, with less than 2 million Muslims population, already has 6 Islamic banks, of which 3 were set up in 2008. According to Ali Ravalia, associate, UK Financial Services Authority, people have started to realize that Islamic banks are not a threat but an opportunity for economic growth. In addition to the large and available Muslim population, Islamic banking is currently beginning to catch the attention of non-Muslim customers, who are interested in alternative way of banking. Indeed, a growing number of non-Muslims are turning towards Islamic banking; as customers are frightened by chaos in the western banking system. Secondly, this sector is considered safer and well connected to the real economy. According to Fiorina (2008) Islamic banking will be benefited from the new customer's interest and grow even more quickly than it recently did. In addition, corporate giants like Tesco (UK) and Toyota (Japan) have used Islamic financial instruments to fulfil capital requirements (DiVanna and Sreih, 2009). This proves that not only individuals, but also corporate giants have showed confidence in Shariah compliant financial instruments.

5. CHALLENGES OF ISLAMIC BANKING IN INDIA

Despite the prospects and benefits of Islamic banking in India, various challenges and obstacles for introducing Islamic banking prevails. India is a secular country and its banking system is fully based on conventional banking. India has 88 scheduled commercial banks (SCBs), 26 are nationalize banks (Government of India holding a stake), 21 are private banks and remaining 41 are foreign banks. These SCBs have a combined network of over 69,160 branches and 60,153 ATMs. Although, several institutions are operating on the Shariah principles but they are treated as NBFCs which functions like a bank. However, NBFC does not accept demand deposits and cannot issue cheques. Following are the major challenges to be faced by Islamic bank in India.

5.1 ADVERSE REGULATORY FRAMEWORK

One of the major challenges is the regulatory framework governing banks in India. The lack in accounting, auditing, and credit analysis standards for Islamic banks exist until now. Significant amendments in regulations are to be done, such as stamp duty, banking regulations act, corporate and other tax regulations to evolve a different system of regulation and control. None of these laws provide a room for the possibility of an Islamic banking system in India. Countries such as France, Germany, Switzerland, Singapore, Japan, Malaysia and the UK have adopted Islamic banking and amended the regulatory framework to be favourable to Islamic banking. The Indian government can choose and apply any model which is reasonable to the Indian scenario.

The RBI appointed Anand Sinha committee to elucidate if Islamic banking can be introduced in India. The committee evaluated options and concluded that Islamic banking cannot be offered by Indian banks as well as the overseas branches of local banks under the present legal framework. Except for a basic current account, almost no other banking product in India can be modified to meet the Islamic banking requirement. Few Indian banking laws extracted from Indian banking regulation act 1949 are the barriers in the ways to Islamic banking are listed as below:

Al Wadiah (for saving bank account): Section 21 requires payment of interest on such deposit.

Mudarabah (for term deposit or investment): Section 21 disallows such products where the bank can invest the money in equity funds.

Mudarabah and Musharakah (for project finance and SME credit): Sections 5 and 6 indicate the forms of business a banking company can undertake, and does not allow any kind of profit-sharing and partnership contract.

Ijarah (for leasing): As against Islamic banking where the banks owns the asset and hold the title, Section 9 prevents the bank from any sort of immovable property other than private use.

Istisna (for home finance): Besides the usual curbs on acquiring immovable property, offering Islamic banking products may not be bankable due to stamp duty, central sales tax and state tax laws that will apply depending on the nature of the transfer.

5.2 INTERPRETATIONS OF SHARIAH PRINCIPLES

The second major challenge in introducing Islamic banking in India involved the varying interpretations of Shariah principles across regions, countries and even within the same country. Shariah council, an independent bank appointed panel of scholars determines the Islamic practice and its interpretation. Therefore, based on the interpretation of what is considered Islamic in Bahrain may not be accepted in India. This absence of uniform standards might affect the bank's ability to duplicate and apply Islamic banks and products across geographies and its expansion to other states.

5.3 INVESTOR'S ASSURANCE

The third challenge is captivating investor's assurance. The conventional banks have the facility of deposit insurance and credit guarantee which develops sense of security and confidence among investors. The investors may demand for the same from Islamic banks.

5.4 LOW LITERACY RATE

The fourth challenge in introducing Islamic banking can be examined from demographic characteristics of Muslims in India. One of it involved the education status of the Muslims in India. For instance, census 2001 shows that the literacy rate among Muslims is 59.1% which is below the national average i.e. 65.1%. It has also been observed 26% of those aged 17 years and above has completed high school but again this percentage below national average accounted 17% of Muslims. While 7% of those aged 20 years and above are graduates, this percentage is less than 4% amongst Muslims. Illiteracy prevails among Indian Muslims which is the major cause of ignorance towards religious regulations and aspects.

5.5 NON-AVAILABILITY OF BANKING FACILITIES

In addition to low literacy rate, the Sachar committee report shows that the access of bank credit to Muslims is low and inadequate (Sachar, 2006). The average size of credit is also meagre and low compared with other Socio-Religious Categories (SRCs) both in Public Sector Banks and Private Sector Banks. The situation is same with respect to finance from specialized institutions such as Small Industries Development Bank of India (SIDBI) and National Bank for Agriculture and Rural Development (NABARD). The data from census 2001 reveals that the percentage of households availing banking facilities is much lower in villages where the share of Muslim population is high. One of the reasons for such an outcome could be non-availability of banking facilities in these villages. The report concluded that the financial exclusion of Muslims has far reaching implications for their socio-economic and educational upliftment. It was suggested that to empower Muslims economically, it is necessary to support self-employed persons as it is the main source of income to Muslims. This can be done through ensuring flows of credits to the Muslims in India. The committee observes that some banks use the practice of identifying 'negative geographical zones' on the basis of certain criteria where bank credit and other facilities are not easily provided. Such practice is referred to as 'red lining' in the United States. It is possible that in some of these areas the share of Muslim population is high and yet the community is not able to benefit fully from the banking facilities.

6. SUGGESTION

Indian government should allow conventional banks to open an Islamic banking window for early development of Islamic banking system. Islamic window is a facility within a conventional bank through which customers can make use of Shariah compliant products (Kamaruddin et al., 2008). The concept of Islamic banking window has been successful in Malaysia, Pakistan and Hong Kong. Currently, India has strong setup with 88 SCB and these banks have a joint network of over 69,160 branches. According to Khan and Ahmad (2003) to function in globalised economy, banks have to meet international standards. Islamic banks have to learn a lot from conventional banks, especially on their managerial skills, financing tools and transparency standards. The conventional banks will not only provide infrastructure to Islamic banking window but will also provide the initial experience needed to establish the same. Considering large network of conventional banks in India, India is suggested to start Islamic banking by opening Islamic window to reach the prospective customers.

Opening an Islamic window will require the bank to establish the suitable measures to avoid the mixing of Islamic and conventional funds. Once a conventional bank has run an Islamic window and gathered a substantial clientele base for its Shariah compliant products, it may choose to launch a full-fledged Islamic bank.

Indian government may consider Malaysian Islamic window as a role model. The first Malaysian Islamic bank was Bank Islam Malaysia Berhad established in 1983 did not get anticipated success. Therefore, in 1993 the government allowed conventional banks to offer Islamic banking services through Islamic window assuming it will be more effective and efficient in increasing the number of Islamic financial institutions and lowering cost within short span. The effectiveness of Islamic window is proven as it has leaded to an improved performance and enhanced efficiency of banking industry (Mokhtar et al., 2006).

In addition to that, for the growth of the Islamic banking in India, proper amendments in the different acts and regulations should be made to accommodate Islamic banking. This is to ensure that Islamic window division can work according to Shariah principles within the existing setup. So that, funds at the disposal of such mixed banks cannot be pulled from Shariah prohibited earnings.

7. CONCLUSION

India has a huge market potential for Islamic banking. The growth of Islamic banking in Southeast Asian countries like Malaysia and Singapore shows it as a viable option for India. The entry of Islamic banks is positive in terms of growth, product innovations and financial inclusion and may encourage the adoption of best practices among the present banks as:

- Islamic banking can help in eradicating poverty by lowering down the economic disparities as there is no interest obligation on the part of the unfortunate borrowers.
- It can induce the habit of savings among people and create the financial insertion required in India. Islamic banking draws finances from both Muslims and non-Muslims alike.
- Islamic banks offer financial instruments that are not only profitable but also reasonable and are ethically fair.
- Islamic banks would give advantage to entrepreneurs who have profitable proposals but lack collateral.

For these, Indian government should look for the opportunities and take a stand in introducing Islamic banking. However, there are challenges to be faced to introduce Islamic banking in India:

- The Indian banking regulation acts are desired to be duly modified to launch Islamic banking in India.
- New standard accounting practice has to be developed.
- Lack of experts in the field of Islamic finance, differences in interpretation and compliance with Shariah makes the situation more challenging.
- The main challenge is a favourable political environment, presently which goes against growth of Islamic Banking in India.

In conclusion, the initiatives in establishing Islamic banking in a secular nation of India may face various political, legal and societal constraints. However, the support of the government in implementing Islamic banking would bring various benefits to India.

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