**Islamic Finance Products**

Islamic financial instruments or Islamic banking products are Shariah-compliant business contracts designed to lend money into assets to earn halal profits. Islamic banking institutions first take ownership of the assets sold or rented. The ownership of the assets is important because, according to a well-known principle of Islamic jurisprudence, “One cannot earn profit from his capital or asset, unless he has have taken risk, or liability of ownership of that capital or asset.” Contrary to that, conventional banks earn interest by lending money. Three main categories of modes of Islamic banking or Islamic finance products exist

**Types of Islamic Finance Products**

The three categories of Islamic financial instruments are:

1. **Debt- or Trade-based products**, such as Murabahah,Musawamah, Salam, and Istisna.

2. **Equity-based products**, such as Musharakah and Mudarabah.

3. **Semi-debt based**; that is Ijarah.

Equity-based products share the profit based on actual earnings.Because of this, they are more risky than the other two categories, so they are most preferred in Islamic Shariah.

**Islamic Banking Products VS Conventional Products**

In the case of conventional banking:

\* For Asset side products, the bank is the lender, and the client is the borrower.

\* For Liability side products, the bank is the borrower, and the client is the lender.

However, the case is different in Islamic banking and financial

system. Both types of Islamic finance products are listed below:

|  |  |
| --- | --- |
| **Liability Side**  **Products** | **Asset Side**  **Products** |
| Murabahah | Mudarabah |
| Musawamah | Musharakah |
| Salam |  |
| Istisna |  |
| Mudarabah |  |
| Ijarah |  |

**Overview of Important Islamic Banking Products**

Below is an overview of some major modes of financing in Islamic banking:

1**. Mudarabah Contract-**Mudarabah contract is an Islamic financial instrument in which one party participates with money and the other with efforts. The profit shall be divided in strict proportion, and no party shall be entitled to a predetermined amount of return. Financial losses shall be borne solely by the investor.

**2. Murabahah Contract-** refers to the sale of goods; the profit margin is

included in the sale price. The subject of sale must exist, be

owned by the seller, and be in his physical or constructive

possession. So, the seller assumes the risks of ownership.

Murabahah requires an offer and acceptance, which must include

Certainty of Price, Place of Delivery, and Date when Price will be

paid.

**3. Ijarah Contract-**Ijarah generally means lease or rent, and it is one of the widely

used Islamic banking products. Ijarah is selling the benefit of use

or service for a fixed price or wage. The bank makes an asset or

equipment available, such as a plant, office automation, or motor

vehicle, for a fixed period and rent. The corpus of the leased

commodity remains in the lessor’s ownership, and only its

usufruct is transferred to the lessee**.**

**4. Musharakah Contract-**Musharakah is a business contract established by partners who agree to share business profits and losses. Profits are distributed

in the proportion mutually agreed upon in the contract. In this type of Islamic banking product, one or more partners choose to become non-working partners, their profit ratio cannot exceed their ratio in capital investment**.**

**5. Salam Contract-**Salam contract is an Islamic mode of financing where the seller undertakes to supply specific goods at a future date, considering a price fully paid in advance at the time of the contract. If the full amount is not paid, it will be tantamount to a sale of debt against debt, Haram.

**6. Istisna Contract-**It is one of the Islamic banking products where a buyer orders to manufacture, assemble, or construct something at an agreed price and to be delivered at a future date. The commodity must be known and specified, including its kind, type, quality, and quantity. The price must also be fixed in absolute and

unambiguous terms and can be paid in a lump sum or

instalments, as mutually agreed.

**7. Diminishing Musharakah**-Diminishing Musharakah is a type of Shirkah where one partner gradually purchases the other partner’s share. According to this

concept: “A financier and his client participate in the joint ownership of a property, or equipment, or in a joint commercial enterprise. The financier’s share is further divided into units, and it is understood that the client will purchase those units

periodically until all the financier’s units are purchased by the client.

**Applications of Islamic Finance Products**

**Murabahah** is used for Islamic Trade Finance Transactions, working Capital Finance, and Fixed Assets Financing.

**Musharakah** is used for Working Capital or Running Financing, Term Finance for Joint ventures, and Equity Participation.

**Diminishing Musharakah** is used to finance assets such as cars, houses, and shops.

Ijarah, or Islamic leasing, is used to finance Autos, Buildings,

Machinery, and Equipment.

Istisna is used to finance manufacturing goods,

constructing buildings, Exporting, and Paying overhead

expenses like salaries and utility bills.

Salam contrat is used for Agriculture or Commodity

financing