IKAM Reports 13 | Country Reports 7

Country Reports

April 2020

A RETROSPECTIVE LOOK AT THE ISLAMIC BANKING AND FINANCE IN IRAN

Zahra Afshari

ikam
RESEARCH CENTER FOR ISLAMIC ECONOMICS

ikam.org.tr/en

IKAM Reports 13 | Country Reports 7

A RETROSPECTIVE LOOK AT THE ISLAMIC BANKING AND FINANCE IN IRAN

Zahra Afshari

ABSTRACT

In this paper, we have tried to trace the evolution and performance of Islamic banking in Iran by reviewing the past literature. For this purpose, different phases of the Islamization of the banking industry in Iran after the ratification of the *Riba*-Free Banking Act in 1983 were studied. Furthermore, the steps that were taken in the last four decades to fully implement this act and its regulations throughout the whole banking system were assessed. Spreading the rules and principles of *Shari'ah* across the entire industry and unifying the whole banking community based on the *riba*-free practice started with the commercial banks and was later adopted by the Central Bank of Iran. Therefore, this report sheds light on the practice of monetary policy in the context of *riba*-free banking. It follows the growth of the Islamic banking system in the context of Iran's economic development and attempts to highlight the role of monetary policy in Iran's economic development process. More specifically, the work critically reviewed regulatory products offered by Islamic banks in Iran, government support, and performance of Islamic banking institutions as well as monetary policy performance in Iran.

Keywords: Islamic Banking, Iran, Monetary Policy, *Riba*-free

JEL Classification: E42, E5, G21

Reference: Afshari, Z. (2020). *A Retrospective Look at the Islamic Banking and Finance in Iran* (Report No. 13). Istanbul: Research Center for Islamic Economics (IKAM).

ABOUT AUTHOR

Zahra Afshari is an Iranian economist. She received her Ph.D. in Economics from Indiana University in Bloomington, Indiana, U.S.A. in 1983. She is a full professor of economics at the Faculty of Social Sciences, Economics Department in Alzahra University. She has authored several books and articles in the field of monetary economics and economic development. She is currently teaching advanced Macroeconomics and advanced Monetary Economics to postgraduate courses.

Acknowledgement

This work has been edited and proofread by Ahsan Shafiq while Research Center for Islamic Economics (IKAM) has sponsored this research.

ikam

RESEARCH CENTER FOR ISLAMIC ECONOMICS

Halk cad. Türbe Kapısı sok. No:13 Üsküdar İstanbul

ikam.org.tr/en info@ikam.org.tr ikamorgtr ikamorgtr

Research Center for Islamic Economics (IKAM) which was established within ILKE Association for Science, Culture and Education in 2016, aims at promoting a new perspective in economic theorizing and its application enabling. IKAM, which organizes theoretical and empirical research, publications and , education and training activities, aims at supporting researchers, business world and policymakers with its research initiatives. Thus, IKAM hosts many activities in the field of Islamic Economics to introduce and increase acceptability of the field in public. In this context, IKAM reports; a serial publication, is an attempt to share the research results in the field of Islamic economics.

Introduction

After the 1979 Islamic Revolution, The government of Iran played a primary role in converting conventional banking into Islamic banking (CBI, 1980). In the 1980s, there were three countries in the world that announced the full conversion of their banking and economic system to an Islamic system – Pakistan, Iran, and Sudan. From amongst these three, Pakistan and Sudan have already gone back to dual banking systems. If we exclude Iranian Islamic banks and financial institutions from the global list of Islamic financial institutions, the total size of the Islamic financial industry drops significantly. Iran's banking assets account for almost 40% of the global Islamic banking industry, making it the largest Islamic financial system in the world (Global Islamic Finance Report, 2017).

This report aims to review Iran's experience in conducting interest-free banking for more than three decades and introduces the challenges and visions ahead. It elaborates on how the Islamic Revolution of 1979 gradually transferred the conventional practice of the financial sector into an integrated framework aimed at a mission within which all operations are required to be *Shari'ah*-compliant. This was a very challenging task in a widespread banking system that had been in place for more than eight decades. The aim seemed more achievable for the capital market, which was considerably younger and more flexible, and was spread across a limited network. The financial sector in Iran is heavily bank-based. The extent of equity financing in Iran outside the banking industry through the primary market consists of a tiny portion, whereas the major share belongs to the banks. The system is designed for ease of access to banking resources rather than architecture or depth of the market.

This report presents the process of Islamization of the banking system in Iran through three phases, in which the ratification of the *Riba*-Free Banking Act in 1983 was a turning point. It explains the steps that were taken in the last three decades to fully implement this act and its regulations throughout the whole banking system. The rules and principles of *Shari'ah* across the entire industry and unifying the whole banking community based on the *riba*-free practice began with the commercial banks and proceeded to the Central Bank of Iran. This report sheds some light on the practice and performance of monetary policy in the context of *riba*-free banking.

Islamic banking development and performance should be considered in the light of several external and internal factors that Iran confronted with including freezing of foreign assets, Iran Iraq war, the toughest world economic sanctions and a drastic reduction in oil revenue.

The rest of the paper is classified as follows: In part two, a short overview of the process of Islamization of the Iranian economy after the revolution; from the evolution of the Islamic economy in 1979 to the current economic position will be discussed. Part three discusses the evolution of Islamic banking in Iran. The three stages of banking system development in Iran i.e., Prior to the introduction of modern banks in Iran, modernization, and Islamization, are presented. Then the process of Islamization of the banking system through three phases, i.e. widespread nationalization, nationwide Islamization, and governmental influences is presented. In part four, the structure of the financial system in Iran in the context of the Banking system and Non-bank institutions is discussed. The complex institutional setup of Islamic banks, i.e. heavy state dominance, ownership structure, shadow banks, Non-Bank institutions, and weak internal controls are also discussed. Part five is devoted to the explanation of Riba-Free Banking Act (RFBA), the evolution of Islamic Banking in Iran in the context of its goal, resource mobilization, performance, and monetary policy. Part six evalutes the macroeconomic performance of Iran in more than three decades of implementing Islamic Banking. Section 6.2 and 6.3 are devoted to the discussion of the Instability of the Banking system and inefficiency of monetary policy respectively. In section 6.4 the shortcomings of Islamic banking in the country will be discussed critically. Finally, in part seven, we conclude the discussion by recommending a series of reforms that should be taken to improve the performance and overcome the shortcomings of Islamic banking in Iran.

Islamization of the Iranian Economy

After the Islamic revolution in February 1979, the theocratic Islamic state launched a comprehensive program known as "Islamization". In its economic dimension, the objective of the program was to lay the foundations for an Islamic economic system in Iran. Two divergent approaches regarding the principles of an Islamic economic system have clearly emerged from the writings of the proponents of such a system.

The first is the mainstream, liberal view-sometimes called the "laissez-faire" approach. The lassez-faire approach represents a continuity of Islamic tradition and thought on economic matters. Islam is viewed as a religion that looks favorably towards economic and worldly matters, hence encourages commercial activities, sanctions the right to private property, and emphasizes an individual's freedom in her/his pursuit of self-interest in economic activities. Islam is further regarded as a religion that furnishes sophisticated forms of contracts to help smooth the flow of credit and business activities. Liberal Islam allows a certain level of economic intervention by the state. Although this role is larger than the role of the state in a competitive capitalist structure, it does not go beyond that of a modem welfare capitalist state. This group finds its support among the conservative high-ranking clerical titles (Behdad, 1989; Valibeigi, 1993). The second approach to the Islamic economic system is in light of the radical interpretations of the Islamic economic laws that emerged mainly due to the failure of the capitalistic development policies in the Muslim countries. The anti-capitalist and anti-imperialist political philosophies of the proponents of the populist approach have influenced the populist interpretation of the Islamic teachings to the extent of public ownership and the role of the public sector in the economy. In essence, the advocates of this view subordinate the domain of individual rights to the domain of public interest. They envisage an Islamic community in which the state takes the leading role as an economic agent. In this view, public ownership is the primary form of ownership, and the state is significantly involved in economic activities directly. A significant portion of the national product is produced under the state sector, and the private sector is mainly involved in the downstream activities of the public and cooperative sectors (Behdad, 1989; Valibeigi, 1993).

With the start of the Islamization drive, there appeared a considerable disagreement among the advocates of the populist and liberal approaches. The 1979-80 was politically dominated by the populists. The 1981-88 period is therefore characterized by intense ideological battles between the radical and liberal advocates of Islamic economic principles. By mid-1987, the extent of this doctrinal conflict reached a point at which the legislative process and long-term economic policy formation were effectively brought to a standstill. The conflicting views of the liberal and radical Muslim fundamentalists on the limits of private property and the economic role of the state in an Islamic economy undermined the formation of coherent economic policies in post-revolutionary Iran. Such inconsistencies were particularly notable in the areas of land reforms and foreign trade, as well as in Islamic banking (Behdad, 1989; Valibeigi, 1993).

Land Reform Program: According to Islam, uncultivated agricultural land and all-natural resources belong to the public. Consequently, on September 16, 1979, the revolutionary council introduced a land redistribution program that made the following lands eligible for redistribution:

1. Confiscated or unclaimed lands that had become public land after the revolution.
2. Public lands that were in the possession of private or public agencies.
3. Uncultivated lands.
4. Scattered wooded lands and pastures that were surrounded by cultivated lands (Razzaghi, 1988, p. 345).

This rather conservative land reform law was changed with political conditions and the radical land reform program in April 1980. The program was known as "Reza Esfahani's Land-reform" after its architect. The new law provided for extensive land redistribution. It limited the land ownership for small-scale farmers to three times the acreage sufficient to support a peasant family. Absentee owners with no other source of income could hold twice this amount. The law also provided that mechanized farms be kept intact and be transferred to cooperative farms. Following the ratification of "Esfahani's land reform" law, the seven-member committees started distributing land among the villagers. On November 12, 1980, under mounting criticism by the liberal grand ayatollahs that "the denial of ownership and the violation of property rights of the people is not in accordance with any of the principles of Islam", and landlords, the supreme leader ordered the suspension of those articles of the law. The final version of the agricultural land reform law was ratified by the Islamic Assembly on December 1, 1982. Again, even this conservative legislation was rejected by the Council of Guardians in January 1983. Since then, land reform legislation has been put on the shelves, and the pre-revolutionary patterns of land ownership, which favored large-scale landlords and the clerical landholding establishments, prevail.

Waqf Properties: Waqf is one of the Islamic avenues instituted for the transfer of private wealth into public use (Cizakca, 2000). In the post-Islamic era, the scope of Waqf activities was extended to more than social protection purposes, such as the establishment of schools, libraries and education financing (Kabesee, 1975). Almost a hundred years ago, the first Waqf law was passed by the Iranian parliament. Since then, the law has been amended several times as the social and economic conditions of the country demanded. During the monarchy regime, when the agricultural land reform law was passed and implemented, unfortunately, some endowed lands were sold out and subsequently, public trust in the preservation and security of endowed properties was diminished (Auqaf, 2002). After the Islamic revolution, Ayatullah Khomeini issued a fatwa that all previous endowed properties that had been privatized should resume their original status. Consequently, the first bill for the revival of endowed estates was approved by the Revolution Council in 1979 in the first year of the establishment of the new Islamic state. The new law specifies, not only the property rights of the endowed properties but in addition the type of organizations that should manage or supervise them. The trustee is obliged to maintain the income-generating properties most efficiently and allocate the revenues to avenues that the benefactor has specified. The income generated by the endowed properties shall be used for research, propagation, and publication of Islamic teachings if the categories of expenditures are not specified in the deed or are for general public benefit. The compensation of the trustee, being a specified person by the deed or by the Auqaf and Charity Organization (ACO), will be paid up according to the deed. In case it is insufficient, the ACO will pay up the difference. Article 33 determines the compensation for the trustee and the supervisor. If it is not specified by the deed, it would be ten and five percent of the endowment's net income, respectively. When this remuneration is not adequate or is excessive, it will be adjusted by the consent of the ACO supervisor.

Articles 24 and 25 of the Codes of Procedure specify that trustees should prepare a balance sheet showing the revenues and expenditures of the endowments. The funds should be deposited in a bank account, different from that of the trustee. The inspectors of ACO should audit the account every year. Article 26 makes it incumbent upon the trustee to manage the corpus such that the generated revenues will significantly increase, at least, every five years.

There are three major types of Waqf organizations in Iran; the public, autonomous and private. The administration setup of each organization is examined in order to find out how they are performing and what policies and initiatives they are adopting to rehabilitate the unproductive estates and develop further the revenue-generating properties. The first public organization is the ACO which takes care of all endowed properties that have missed or have no trustee. It is noticeable that almost half of Waqf properties that are managed by the ACO are "benefit" and the other half are "usage" Waqfs, i.e. mosques or religious places. Many of the endowments are family Waqfs. About one-tenth of the endowments are run by independent trustees and are supervised by the ACO; the rest are managed (89%) by the latter. A small proportion however is under their joint management. The small share of the private sector in the management of endowed properties is an important concern which may imply that private trusteeship is not sustainable. Interestingly, 99 percent of the endowments are devoted to local citizens and very few are for the whole nation. The second Waqf administration is that of holy shrines of the Prophet's progeny members. The first article of the new law states that those endowments which are devoted to the progeny of the Prophet (SAAS) are also exempted from ACO supervision and are under the auspices of the leader unless the benefactor has specified and appointed a trustee. Examples of such endowments include the sacred shrine of Imam Reza (AS) in Mashhad and associated endowments, such as that of Hazrat Fatemeh Masumeh in Qum. The mosques, seminaries, and refuge places are exempted from the coverage of this law.

Astan Quds Razavi (AQR) is an autonomous charitable foundation in Iran. It is a complex which contains Imam Reza (AS) Shrine, and various educational, cultural, medical, and economic institutes. The main resources of the AQR are endowments, many of which were overtaken by private interests and were underutilized prior to the Islamic revolution of Iran. After the revolution, with the change in trustee and efforts to take back the confiscated properties and enhance the productivity of commercial and agricultural endowed properties, both the generated income and the value of the corpus increased significantly. The corpus value is estimated to be worth $15 billion. Subsequently, AQR grew from a "modest concern" into a conglomerate employing 19000 people and running universities, hospitals, commercial and agricultural businesses, auto plants, financial units and many other enterprises (Astan Quds, 2013). Thirteen cultural, academic, and research institutions are active in the fields of higher education, art, research, consultation, publication, and library services.

Hazrat Masoumeh (AS) Endowments: The endowed properties include cultural, agricultural and commercial estates. The total farm area operated and managed by this corporation is 3000 hectares. The commercial and residential units are rented out with and without a down payment. Endowments of the Prophet's (SAAS) progeny members in Shiraz based on the annual statistical publication of the Fars province in Iran in 2011, include 160 pious foundations in the province, 49 of which belong to grandsons of the Prophet's (SAAS). At present, 33 villages are endowments in which 765 farms are established and five government organizations are stationed (Fars province, 2011). The income generated from the endowed properties is allocated to teaching of the Holy Qur'an, giving religious lessons to students, holding public lectures and ceremonies in the month of Ramadan and Moharram and on the occasions of the Prophet and his progeny members' birthdays and martyrdom anniversaries. Distribution of food on these occasions and maintenance of the shrines are other categories of expenditure.

The third type of administration is that of private trustees or joint private-public custodians. Two conspicuous examples of this sort are Namazi Hospital Foundation and Afshar Cultural Foundation. Both were founded by scholars who devoted their wealth for the provision of piped refined water and medical services as well as cultural studies. The trustees of both foundations are groups composed of private individuals and public authorities. The sustained and robust services of both foundations might be attributed to the mix of trustees and supervisors (Sadr and Souri, 2010)

***Takaful* (Islamic insurance):** It is a form of cooperative insurance involving the allocation and spreading. Theoretically, *Takaful* is perceived as cooperative or mutual insurance, where members contribute a certain sum of money to a common pool. Iran represents 44% of the total global *Takaful* premiums (according to the Dubai Center for Islamic Banking and Finance (DCIBF)), which could increase if Iran alleviates its internal and external challenges with foreign investment and cooperation with other Islamic economies. The annual growth rate in Iran in 2001-2011 periods was 29.9 % (DCIBF). This could be due to Iran being the only country to maintain a fully Islamized financial system; thereby establishing a domain in which *Takaful* may thrive by making Sharia compliance a legal requirement for the domestic insurance industry. Comparative sources often omit Iran from their findings, despite its market size. This is despite their similarities in fundamental underlying values of mutuality – upon which even Sunni Islamic economies are divided. Significantly, information regarding Iran's *Takaful* model and its differences compared to other Islamic economies is sporadic and limited. This theme is recurring for Iranian companies across other industries and may complicate comparisons with other *Takaful* industries. Iran's Shia Islamic-based legal system significantly differentiates Iranian *Takaful* from other *Takaful* models. Unlike other Islamic economies, it is noted that insurers in Iran do not require a Sharia council and do not operate as traditional *Takaful* operators because the Iranian government does not maintain a 'strict' division from conventional insurance. The meaning of *Takaful* is ambiguous in the Iranian context as the scantily existing research on Iran does not clearly differentiate between them. This is perhaps due to the Iranian financial system being entirely based on Shia Islam, meaning its insurance industry is grouped under the umbrella of Sharia compliance instead of just covering part of a dual system, which is commonly seen among the predominately Sunni Islamic economies. As a result, Iranian insurers across the industry predominately have conventional operational structures with a prevalent use of subordinate *Takaful* 'windows'. What is known is that *Takaful* and Iranian insurers are not differentiated unlike other Islamic economies because in-house Sharia councils are not required. Health, third-party motor and social insurance are compulsory in Iran, and Iran's Establishment Act stipulates that life and non-life business from insurers will be partially ceded to the central Insurance of Iran, the insurance regulatory authority and official reinsurer. Out of 305 *Takaful* operators and windows, 107 are licensed for general takaful and 57 for family *takaful*, while 116 hold composite licenses, and 25 are re*takaful* operators. Iran's *Takaful* sector will be heavily affected by the lifting of sanctions, based on how it has established itself as a leading market despite considerable economic restrictions. Central Insurance of Iran is in charge of regulating the insurance sector in Iran. 27 insurance firms dominate the sector, 26 of which are active in commercial insurance. The leading player is the Iran Insurance Company, followed by the Asia Insurance Company, the Alborz Insurance Company and then the Dana Insurance Company. Twenty two other private insurance companies are also offering service through agents and brokers. Export and Investment Insurance on the other hand deals with foreign trade.

Nationalization of Foreign Trade: The hostage crises, the outbreak of war, and acute crises of foreign exchange earnings gave rise to further intensification of inflationary pressures, which, in tum, furnished a noble excuse for the radicals to push for complete nationalization of foreign trade. Section 44 of the Constitution of the Islamic Republic requires the government to carry out the "foreign trade". The first step towards the enactment of this section of the constitution was taken on May 10, 1980, according to which nine centres were to be established for the import and distribution of basic imported goods by the commerce department (Behdad, 1989).

After a decade of debate and controversies among the liberals and the radicals, and failing to set long-term objectives for economic policy, the final version of a plan that was developed in 1982 was eventually approved by the Islamic Assembly in January 1990. Although the original broad objectives of the 1982 plan have been reinstated in Rafsanjani's plan, the focus has been shifted from agricultural development to economic growth through increased industrial production. In this plan, state enterprises have been given more autonomy, a more liberal approach has been taken toward foreign trade, the significance of private investment has been emphasized, and, perhaps most importantly, for the first time, provision for foreign finance ($27 billion dollars over five years) has been made. This latter issue has become the most recent subject of conflict between the radicals and the liberals, led by President Rafsanjani. One may well argue that this kind of political maneuver by the pragmatic, government of President Rafsanjani has been one of the main reasons for his success. At the same time, such pragmatic solutions have undoubtedly undermined the very fundamental original principles upon which the Islamic economic system of Iran was supposed to be established. In this report, we mainly focus on Islamic banking and finance as we know that attempts to apply the principles of Islamic economic teachings to the economy are not new to the Islamic world.

The Evolution of Islamic Banking in Iran

Prior to the introduction of modern banks in Iran, operations had been carried out by famous merchants in the traditional form. In addition, a number of money dealers lent money, mostly at 24-36 percent per annum. Before the advent of the Achaemenid Dynasty, banking operations had been carried out by temples and princes. During the Parthian and Sassanids eras, both Iranian and foreign coins were used in trade in the country. However, with the emergence of Islam in Iran, money changing and the use of banknotes and coins in trade faced stagnation because Islam prohibits interest. (Issawi, 1972, pp. 42-48).

Modern banking in Iran was introduced by foreign banks in the late 1920s. The British-owned New Oriental Bank was the first modern bank to start operations in Iran. It was shortly afterwards replaced by Bank Shahanshahi (Imperial Bank) in 1889, which remained as a major financial institution in the country for more than six decades (Curzon, 1892, p. 474). In 1856, a Russian national had established Bank Esteqrazi for 75 years. The bank continued its activities under the name of Bank Iran until 1933 when it was incorporated into the Agriculture Bank. The foreign banks, by replacing Iran's traditional banker-merchants tended to limit the growth of the urban private sector. Despite their early contribution to introducing financial innovations, they were not able to bring up indigenous economic development.

In 1925, the first bank (Bank Sepah) was established with Iranian capital under the name of Bank Pahlavi, in order to manage the financial affairs of the military personnel and set up their retirement fund. In April 1927, the law of the establishment of Bank Melli (national) of Iran was approved by the Iranian Parliament. The Central Bank of Iran was established in 1928 with the aim to control the quantity of money and credit, preserve the value of the national currency, implement monetary policy, and supervise the banking system (Idem, 1982).

With the establishment of state-owned banks, the banking system provided a growing source of funds for the development expenditures. However, with the establishment of private indigenous and joint-venture banks in the 1950s, the banking sector helped to absorb the growing private savings and provide the needed financial capital for the private as well as the public sector. Furthermore, the rental price of capital and the interest rates charged to the private entrepreneurs were kept low in real terms. The availability and the low cost of borrowing on the one hand and the rising national income on the other tended to encourage the private sector in Iran.

In the 1960s and 1970s, the government increasingly utilized the banking system to expand private capital formation. The banking system was being fed by the vital flows of oil revenues and played a crucial role in accelerating economic growth. The rate of transformation and financial expansion was especially accelerated after 1973. These expansions mostly relied on unstable oil revenues (CBI, 1978).

The revolution put an end to the nine decades of Western-oriented banking expansion. In June 1979, all banks along with a number of other financial and industrial establishments were nationalized and banking regulations changed with the approval of the Islamic banking law.

Islamic banking in Iran is rooted partly in the pre-revolutionary oil-dependent economic structure and partly in its difficult political development. The Iranian economy is highly dependent on oil revenues. The industrial sector was organized without sufficient attention to efficiency and comparative advantage and in light of the poor agricultural performance after 1960. After the revolution, Iran was confronted with many internal and external shocks including, freezing of the foreign assets, economic sanctions, Iran Iraq war, and a drastic reduction in oil revenues. As a result, the Interest-Free Banking Law contains several features that are specific to the Iranian circumstances. Iran utilized the banking system to achieve the economic goals of the revolution. Three distinct phases of this progress have been identified.

In the first phase (1979-82), in order to remove the weakness of the inherited system, the Iranian government nationalized and merged the banking system (Banks Nationalization Act, 1979). Out of 37 banks emerged 6 commercial banks (Refah, Melli, Saderat, Tejarat, Mellat, and Sepah) and three specialized banks i.e. Agriculture, Housing, and, Industry and Mining (Law for the Administration of Banks, 1979). However, internal and external developments in this phase did not allow the policymakers to build an adequate plan for the Islamization of the banking system (CBI, 1984).

The second phase began in 1982 and lasted until 1986. The public demand for elimination of *riba* (usury) from the banking system made the academics, experts, and fiqh scholars come together to prepare a draft bill for *riba*-free banking. In this environment, the law of usury-free banking (i.e. no interest) was passed by the Islamic Parliament of Iran in 1983 and went into effect on March 20, 1984 (Hassani, 2010). The Law required the banks to convert their deposits in line with the sharia within one year, and their total operations within three years, from the date of the passage of the Law, and specified the types of transactions that must constitute the basis for asset and liability acquisition by banks (Iqbal and Mirakhor, 1987). The law described 14 types of operations applicable to assets and liabilities (CBI, 1983). The banks were allowed to buy debt instruments, supported by real assets, for a period of one year. The Central Bank was implicitly envisioned as a quasi-independent economic institution similar to that of most western central banks, and revealed extensive control over the operation of the banking system (Khan and Mirakhor, 1990). All banks and credit institutions in Iran adopted Islamic rules and were required to act as *Shari'ah*-compliant businesses.

In the third phase which began in 1986, the banking system is being rapidly integrated with the rest of the government. Thus, the banking system is perceived not only as the major source of financial resources to finance the government's fiscal deficits but also as an effective tool for processing economic objectives, such shifting in the patterns of consumption, investment, and production behavior in the economy as well as restructuring of the economy and income redistribution. Finally, a highly activist rule is defined for the Central government for allocating funds and restructuring of the economy. Therefore, the interventionist posture of the government in the economy was legitimized (Khan and Mirakhor, 1990).

The Structure of the Banking System in Iran

Understanding the roots of Iran's banking system's shortcomings and the financial instability requires a sense of its particular institutional setup. The banking system of Iran is a complex sector with heavy state dominance, an ownership structure that involves significant interconnections with various public or semi-public institutions, shadow banks, corporations, and finally has considerable shortcomings in supervisory regulations and implementation.

The Law of Establishment of Non-Government Banks was passed about two decades after the revolution to reform and restructure the economy. Partial privatization of the banking system led to significant financial deepening (IMF, 2011a). New private banks were set up and several public sector banks were privatized. In accordance with article 44 of the constitution, all public banks except four were privatized, and their ownership, management, structure, and administration status were transformed. Private banks also played a significant role in the circulation of funds by using electronic instruments. Public banks have pushed to follow the same direction.

Iran's financial system has undergone a major transformation with privatization. The banking system was previously dominated by state-owned banks including commercial banks, private banks, and specialized banks or *qard hasan* banks, which jointly hold about 85% of the Iranian banking sector. However, following the privatization of the large public commercial banks in 2008-09, private bank assets have become the largest in the system. Despite efforts to encourage private banking, state-owned and specialized banks hold about 35 percent of the banking sector's assets - but about 70 percent if one includes privatized banks whose assets are effectively under government control. Private banks' assets grew from 13% in 2007 to 65% in 2016 due to the licensing of private banks. In 2016, the assets of Commercial banks, Specialized banks, and Private Banks & Non-Credit Institutions were 3554.8, 4243.9, and 14,341.3 (Trillion rials) respectively. In year 2016, 20 banks were listed on the Tehran Stock Exchange.

Currently, there are four categories of banks in Iran: public commercial; public specialized; privatized; and private. In addition, a large number of unlicensed (and unregulated) financial institutions (shadow banks), which are connected to public sector entities, the armed forces, and charities, included 2,489 credit cooperatives and 3,525 religious charity funds (IPRC, 2018). They have competed aggressively with regulated banks over deposits by offering interest rates considerably higher than those offered by the regulated banks many of which are now inactive or facing closure. Now, 32 banks and financial/credit institutions are operating in Iran including 10 state-owned banks, 20 private banks, and 2 other financial institutions. All of these banks are governed by the central bank (Global Islamic Finance Report, 2017).

The ownership structure of private banks is complex, with a network of cross-ownership between banks and nonfinancial corporations. The privatized banks are de facto controlled by the government or public sector entities. This cross-ownership structure, nontransparent and unsupervised, has been highly vulnerable to connected lending, rent-seeking, and corruption (Mazarei, 2019). Although Iran was cut off from the global banking sector due to sanctions imposed, the domestic banking sector in Iran has overcompensated and is effectively overbanked.

There are also some 7,000 registered nonbank credit institutions, of which 5,000 are active (3,500 microfinance entities; 1,500 credit unions). The total assets of Non-Bank Institutions had an increasing pattern as shown in figure 1. It accounts for more than 15 percent of the GDP. For many years the sector was neither licensed nor supervised by the CBI.

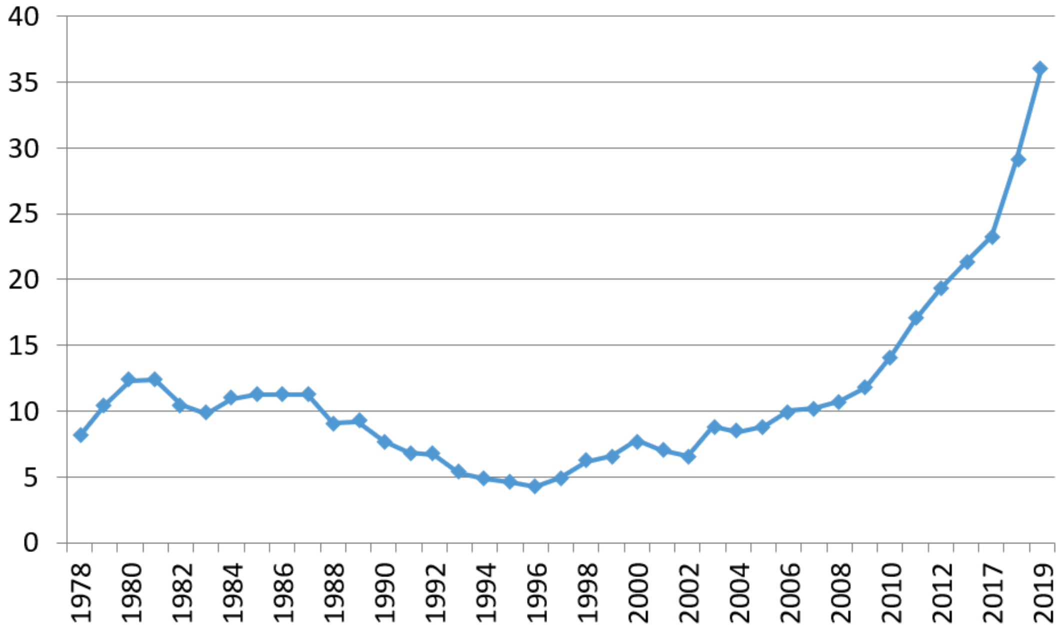


Figure 1. The value of assets of non-bank institutions.

Source: C.B.I

Microfinance Charities with six entities account for 90 percent of the sector's assets of $40 billion. The entities' funding consists of charitable donations supplemented by non-remunerated deposits that the public entrusts to them given that the funds are lent interest-free to borrowers.

Credit Unions: Ninety percent of the sector's total assets of $20 billion are also accounted for by six entities. Credit unions were licensed by the Ministry of Cooperatives, but was not supervised effectively. While the vast majority of institutions provided banking services purely to their members, some progressively engaged in regular banking in violation of the license.

The 5th FYDP of 2010 (article 96) makes the CBI solely responsible for licensing and supervising of nonbank credit institutions. Since then, 900 credit unions have applied for a CBI bank license and many small and medium-sized ones will operate under the umbrella of a new Cooperative Bank of Iran. The CBI closed 50 credit unions and merged the remainder into six new entities. The consolidation is therefore expected to result in 12 new banks and the Cooperative Bank of Iran. Other non-bank financial institutions consist of 2 investment banks, 110 brokerages, and 48 investment companies regulated by the Security and Exchange Organization. Hundred active leasing companies are regulated by the CBI as well as 1,000-1,500 money transfer operations (Guillaume & Sensenbrenner, 2011).

The *Riba*-Free Banking Act (RFBA)

The *Riba*-Free Banking Act (RFBA) consists of four sections: goals, mobilization of financial resources, allocation of funds, and central banking and monetary policy.

Goals

According to Article 1 of the RFBA, "the goal of Islamic banking can be summarized as follows: Monetary and credit mechanisms to engage in activities conducive to the attainment of the economic goals, policies, and plans of the government. Creation of the necessary facilities for the extension of cooperation and *qard hasan* among the general public through the attraction and absorption of surplus funds, reserves, and savings and deposits, and their mobilization to provide conditions and opportunities for gainful employment and investments. Maintenance of the currency value and equilibrium in the balance of payments and commercial transactions. Facilitation of payments and receipts, exchanges, transactions, and other services to be performed by banks, as well as other duties that have been determined by law".

Therefore, the RFBA has obligated the banking system to perform all tasks and duties that are being practiced by central as well as commercial banks in other countries. The banking sector has been used as an instrument for restructuring the economy as well as an instrument for income distribution through the provision of *qard hasan* loans for the needy, financing the building of housing for low-income groups, and provision of financing for small agro-businesses and industrial cooperatives. The Central Bank provided the required finance in the form of venture capital for innovative industrial projects in the cooperative sector. Finally, the banking system, in partnership with government, finances industrial projection and invests in overhead social capitals (Mirakhor and Zaidi, 1988). In addition, the banking system finances government deficits, which have distributive effects. With respect to these situations, the performance of Islamic Banking was smooth (Thiagaraja, Morgan, and Tebbutt, 2014, p. 11).

Mobilization of Financial Resources

According to Article 3, "Banks are authorized to accept the following types of deposits: (1) *qard hasan* deposits, for current and saving accounts, and (2) term investment deposits, which may be used in joint ventures, *mudarabah*, hire-purchase, installment transaction, muzaraah, musaqat, direct investment, forward dealings, and joalah modes of finance. The bank works as an agent, or attorney, for the utilization of term investment deposits." Based on this article, contrary to the practice in other Muslim countries, the only contract used for fund mobilization of non-qard hasan deposits is wakalah. In addition, Banks are obliged to repay the principal of qard hasan deposits and may undertake and/or insure the principal of term investment deposits (Article 4).

Deposits

In an economy with Islamic banking, commercial banks are allowed to accept demand deposits same as the conventional banks do. There are various methods of absorbing deposits in the Iranian banking system. According to the law of usury-free banking in Iran, liabilities incurred by the banks are basically of two kinds: *qard hasan* (benevolent loan) current and savings deposits. These are similar to the conventional banks except that they cannot earn any return. Current *qard hasan* deposits are like demand deposits or current account in conventional banks. This account is simply a means of making transactions and payments. The other type of *qard hasan* is the saving account. In order to attract and mobilize deposits, banks may, through promotional methods, give the following rewards to the depositors: Non fixed bonuses in cash or in-kind to *qard hasan* deposits. Exempting the depositors from, or granting discounts to them, in payment of commissions and/or fees. Most Iranian banks and credit institutions consider awards for *qard hasan* deposits, although such a process is not binding (Article 6). *Qard hasan* deposits are the main sources of *qard hasan* loans. (Parveen et al., 2015).

Term Investment Deposits (Wakalah Accounts)

The relationship between the bank and the depositor is such that the bank is appointed as a representative to undertake transactions on the behalf of the depositor. Investment deposits which banks are authorized to acquire are of two kinds: short term and long-term investment deposits. These deposits differ with respect to time. The minimum time limit for short term deposits is three months and for long term deposits, 1, 2, 3, 4 and five years (Parveen et al., 2015)

Banks invest the funds in contracts such as joint ventures, *mudarabah*, hire-purchase, installment transactions, *muzaraah*, *musaqat*, direct investment, forward dealings, and *joalah* transactions. Repayment of the principal is secured, and profits gained through investments are distributed among the depositors based on the original contract, the amount of the deposit, and the duration of the deposit after the deduction of bank fees and commission. Legally, in the beginning, the exact amount of profit is not clear, but the diversity of transactions and their vastness guarantees substantial profits. Currently, Iranian banks pay an initial profit based on a bank's expected profit. This primary profit is paid on a monthly basis, and the final profit is determined after completion of the accounting and auditing processes at the end of the financial year. If the final profit is less than the initial on-account profit payment, the bank accepts the loss does not impose it on the depositors. Otherwise, the difference is paid to the depositors. The Iranian banking system uses wakalah in the mobilization of resources, which include term investment deposits. Most Islamic countries use contracts such as *mudarabah* and *wadiah* instead (Parveen et al., 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011).

Allocation of Funds

Allocation of Funds by Banks

Article 7 to 17 of the RFBA deals with the allocation of funds through Sharia compliant contracts and transactions, in which avoidance of *riba* is the main feature. The only cash loan utilized by banks is *qard hasan*. Figure 2. shows the share of facilities extended by the banking system to the non-public sector in the form of different Islamic contracts after the establishment of Islamic banking in Iran. The *qard hasan* and various contracts for other types of transactions are described next.

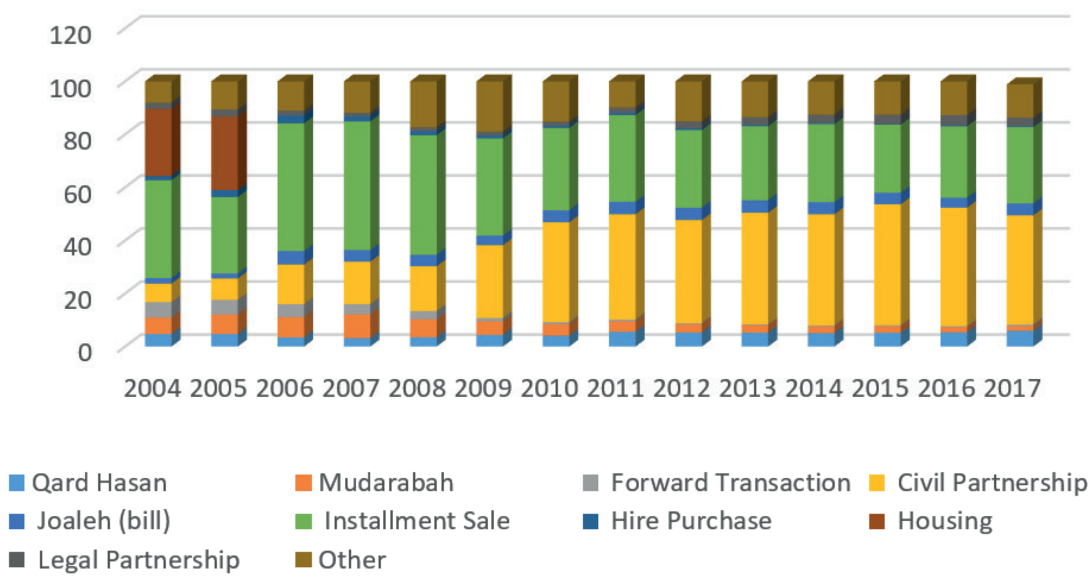


Figure 2. Facilities extended by banks and credit institutions in percent (by Islamic Contracts).

Source: On the basis of C.B.I

Qard hasan (benevolent loan) is a non-commercial facility without any expectation of profit. *Qard hasan* loans are usually made to small producers, farmers, small-scale businesses and the people who are unable to find financial sources for their personal needs such as weddings, medical needs, etc. The ability of banks to grant this loan depends on the *qard hasan* saving deposits. Banks are authorized to lend a certain amount of funds to individuals or companies. The recipient commits to return the same amount at a specified time. Banks receive collateral to secure the repayment of loans. Banks are allowed to recover expenses associated with granting *qard hasan* finance. Moreover, they charge the borrower up to 4 percent as administrative fee. There is an annual 1.5 percent handling fee charged for "industrial" or 1 percent handling fee charged for personal *qard hasan*. The maximum tenure for institutions is usually five years and for individuals three years (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011).

In 2017, 5.1% of Outstanding Facilities Extended by Banking System to Non-public Sector were in form of *qard hasan* (Figure 2). According to figure 2, before 2009, commercial banks had a dominant role in extending *qard hasan* to the non-public sector (above 80%), but afterwards non-public banks took on aa leading role. The share of specialized banks remains almost the same.

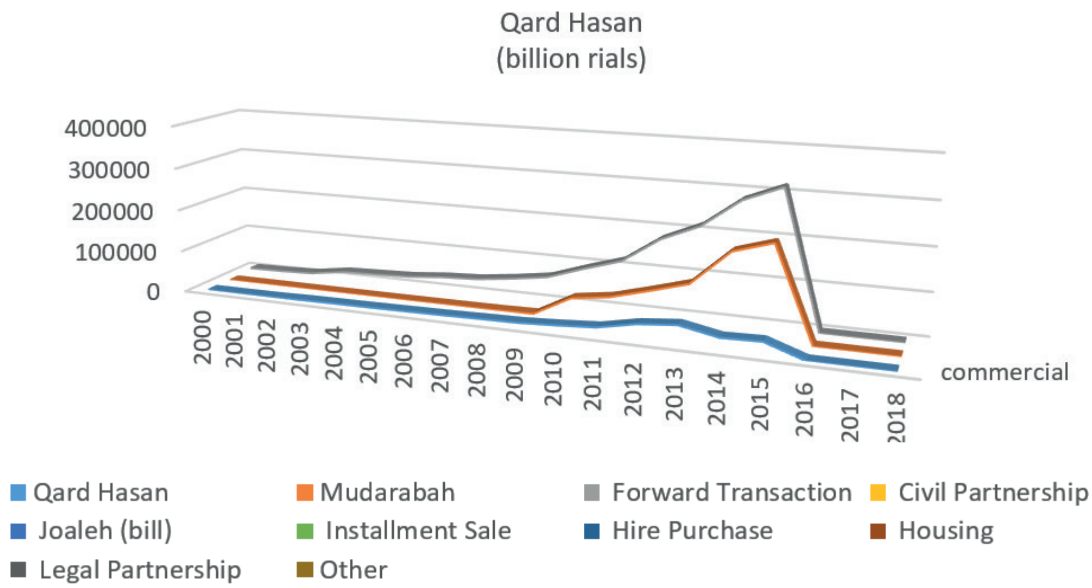


Figure 3. The amount of Qard Hasan extended by banking system to non-public sector.

Source: On the basis of C.B.I

Mudarabah or Qirad (Profit Sharing): Banks provide initial capital to the commercial sector, both individuals and traders who engage in trade and business. Profits generated are shared between the two parties according to a previously agreed-upon ratio. The maximum period for *mudarabah* is one year. The customer (an individual or a company) is required to provide the bank with information about identity, subject of the contract, required capital, estimated costs, duration, and proposed shares of profits. After reviewing the information, banks may accept the request and get involved in a *mudarabah* contract. By previous agreement, the profit from the undertaking is divided at the end of the contract. According to imamiah jurisprudence, *mudarabah* is limited to the buying and selling of commodities. It is noticeable that other countries do not follow this restriction. (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, 1.8% 0f Outstanding Facilities Extended by Banking System to Non-public Sector were in form of *Mudarabah* (Figure 2).

Musharakah (Partnership): The law recognizes two different forms of partnership, namely civil and legal partnership. A civil partnership is a project-specific partnership for short and medium terms. It is defined as the joining of capital from a bank with the capital from a partner or partners (in cash or kind) on a joint ownership basis for performing a specific job (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). During the period 2009-2016, non-public banks had a dominant role in extending facilities in the form of civil partnership (Figure 3). In 2017, 42.3% of outstanding facilities extended by banks to non-public were in the form of civil partnership (Figure 2).

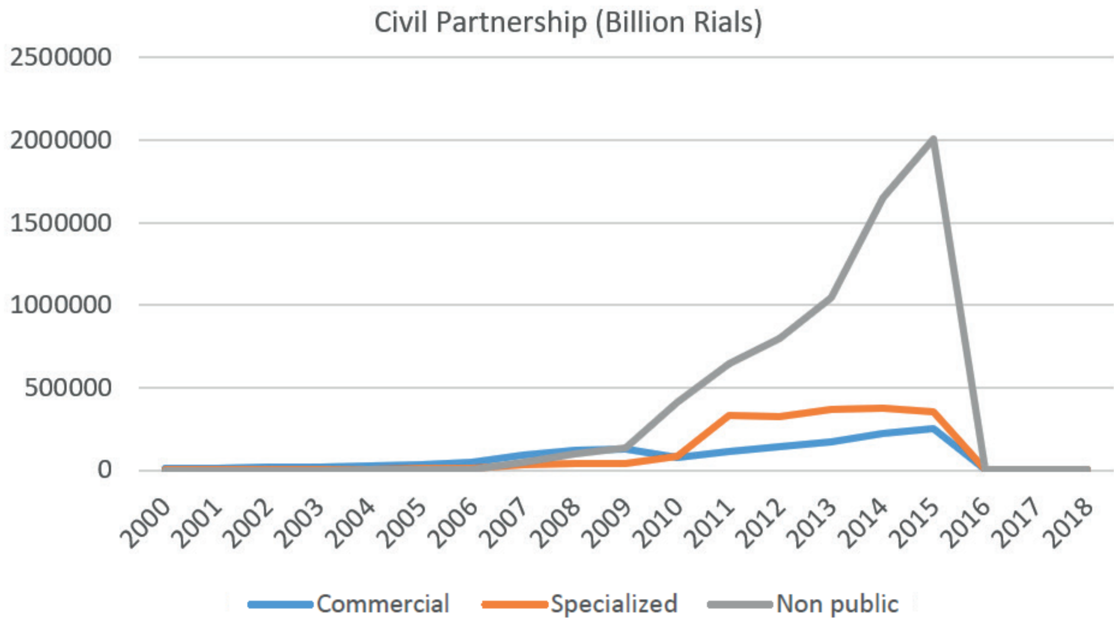


Figure 4. Outstanding facilities extended by banking system to non-public sector in form of civil partnership.

Source: On the basis of C.B.I

The legal partnership is a joint venture for a long duration. In a legal partnership contract, the bank finances part of the capital for a start-up or purchases corporate shares in order to compensate for a shortage of capital in joint-stock firms. The bank receives a dividend at the end of each fiscal term. This kind of deal aims at the long-term provision of resources for productive, commercial, and service companies. Legal partnerships help start new businesses, develop existing plants, and increase the supply of goods and services (CBI, 1997). Currently, the rates are 6 percent for agricultural projects; 8 percent for mining and industrial projects; 10 percent for housing and construction; and 12 percent for commerce and services. Besides the minimum required profit rates that can be manipulated by the Central Bank for policy purposes (setting the country's priorities), the maximum amount of the bank's share in a project can also be used as a policy variable. Currently, the maximum share for a bank entering into a civil Musharakah agreement in agriculture is; 90 % in mining, 85 % in housing and commerce, and 80% in the services. Even though the bank is providing a given share of the capital, this does not necessarily mean that the profits are to be shared in the same proportions. That is, the ability to manipulate how the profits are to be shared is another tool available to the policymakers for setting the economic priorities of the country. The maximum amounts that a bank can invest in a *Musharakah* agreement are set by the Central Bank of Iran (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, 3.6 % of outstanding facilities extended by banking system to non-public sector were in form of legal partnership. As figure 5 Shows, although till 2009, commercial banks had a dominant role in extending facilities in the form of legal partnership, the share of specialized banks had a dominate role afterwards. The share of non-public banks dominated that of the commercial banks after 2010.

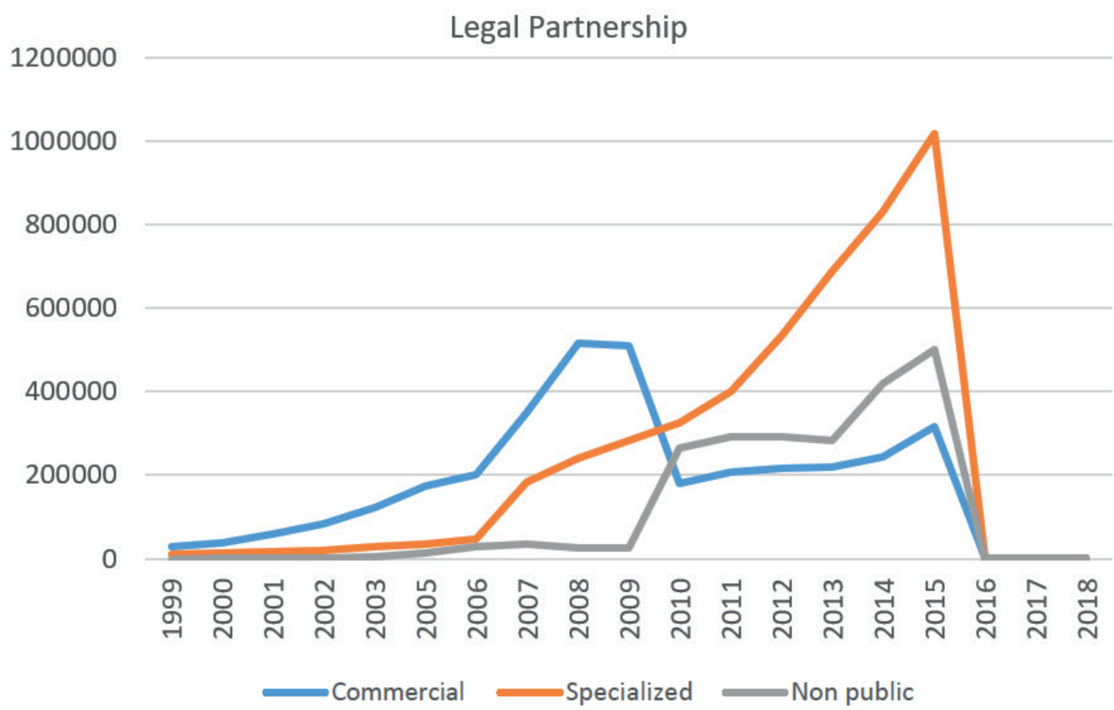


Figure 5. Outstanding facilities extended by banking system to non-public sector in form of legal partnership

Source: On the basis of C.B.I

The Muzara'a is a financing method in agriculture in which the bank may provide a piece of land for a specified period of time to a farmer for agricultural purposes and share the profit earned. In addition, the bank may provide seeds, fertilizers, water, pesticides, transportation, etc. Currently, banks have the authority to set the terms of Muzara'a contracts, which usually last for one year. The crops are then divided based on a previously agreed-upon ratio. The bank normally authorizes the client to sell the crops on its behalf (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011).

Musaqat is a contract in which the owner of an orchard assigns another party to take care of the trees, and eventually, the products are divided proportionately. This contract is used when a bank or some of its branches own an orchard with fruit trees. The recipient of the facilities is normally authorized to sell the products. The bank may provide an orchard to a farmer for a period of time (one year or until its fruits are harvested) for a share of the profits (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011).

Direct Investment: Banks can invest directly in any economic activity that is not considered a luxury, for a long period. The possibilities for direct investments by banks only exist in the public sector through the creation of companies where the legal partnership is not possible. It must also consider the priorities of the country's economic development. The bank provides, in part or entirely, the required capital for productive, commercial, or service projects upon an accurate assessment of their profitability (Article 8 of the RFBA) (Parveen et al., 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, 0.9 % of outstanding facilities extended by banking system to non-public sector were in the form of Direct Investment. As figure 6 shows, although till 2011, commercial banks had a dominant role in extending facilities in the form of direct investment, the share of non-public banks dominated after that, and the share of specialized banks was less than 5%.

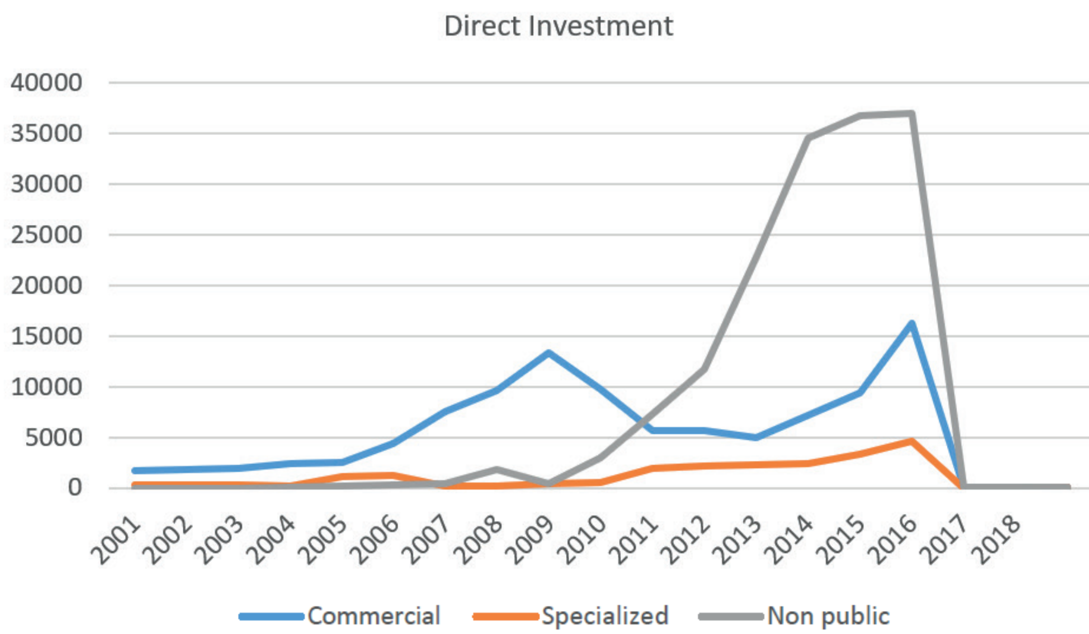


Figure 6. Outstanding facilities extended by banking system to non-public sector in form of direct investment

Source: On the basis of C.B.I

Salaf (Forward Transaction): Banks can purchase agricultural, industrial, or mining products at a certain price from productive enterprises in order to provide them with working capital. Thus, instead of lending money, the bank buys part of the products in future at an agreed price which must not exceed the market price of the product at the time of the contract. The applicant is required to provide the bank with information about the specifications of the firm, the amount of the sale, the specifications of the product, the price of the product at the time of signing the contract, the predicted price at delivery, the place and time of delivery, and the proposed collateral. As the dealer, the bank sells the product after delivery and gains a profit. In most cases, the client commits to sell the product on behalf of the bank (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, only 0.3% of outstanding facilities extended by banking system to non-public sector was in form of *Salaf*. As figure 7 shows, although till 2009, commercial banks had a dominant role in extending facilities in the form of Forward Transaction, the share of non-public banks has increased since then. The share of specialized banks kept variating during the whole period.

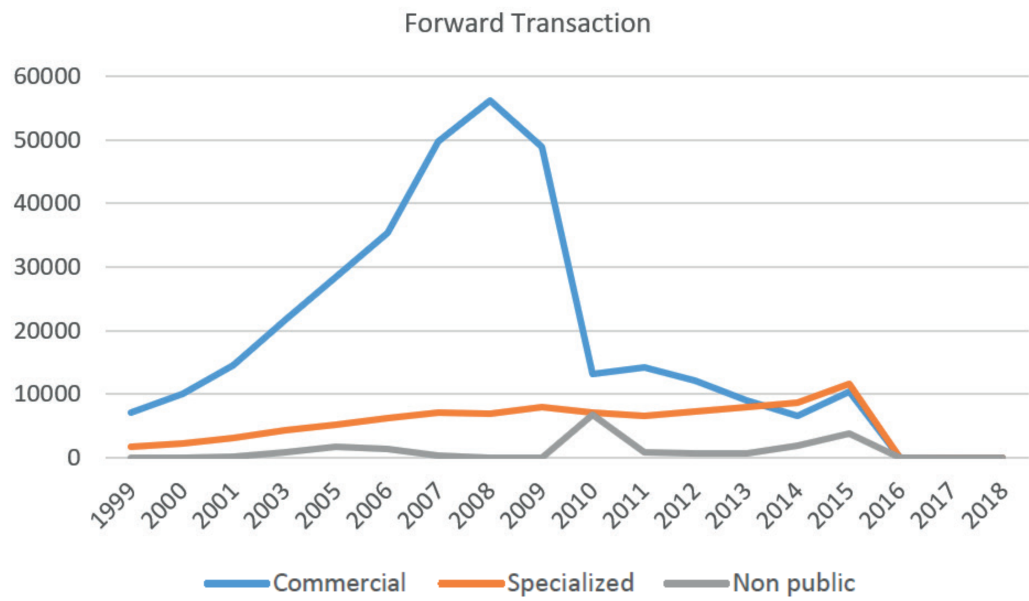


Figure 7. Outstanding facilities extended by banking system to non-public sector in the form of Forward Transaction

Source: On the basis of C.B.I

Jo'aleh is a short term contract according to which one party (*Ja'el*) purchases another party's (*Amel* or contractor) services for a specified commission (*Jo'al*). The bank may function as either *Jo'aleh* or *Amel* depending on the situation and the need of the customer. The service to be performed and the fee to be charged must be determined at the time of the contract. In this way, the customer receives the service needed while the bank receives its costs and profit.

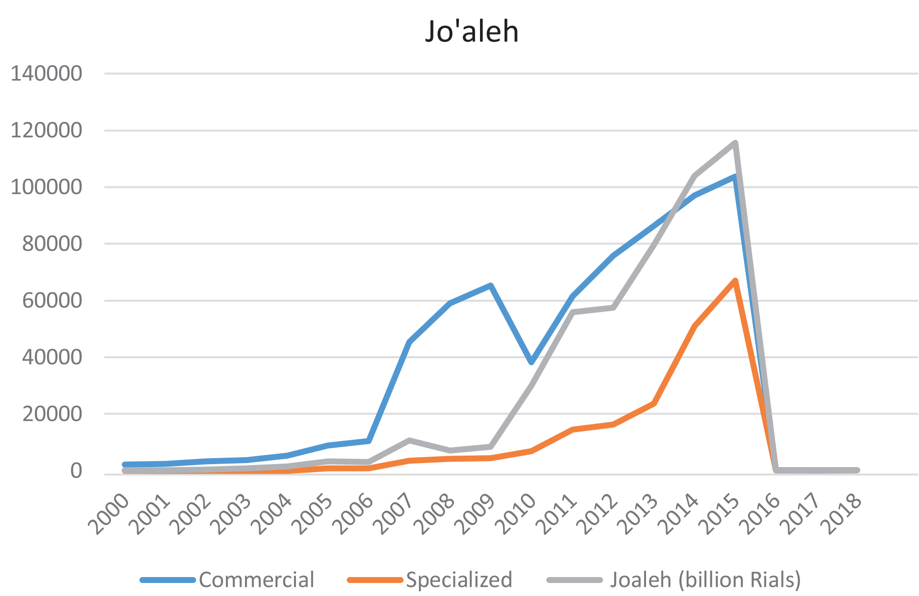


Figure 8. Outstanding facilities extended by banking system to non-public sector in form of *Jo'aleh.*

Source: On the basis of C.B.I

In installments paid by the customer (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011) in 2017, only 3.6 % of the outstanding facilities extended by banking system to non-public sector were in form of *Jo'aleh*. As figure 8 shows, the facilities in the form of *Jo'aleh* had an increasing pattern till 2015, but after that they sharply decreased for all types of banks. Although till 2013, commercial banks had a dominant role in extending facilities in the form of *Jo'aleh*, however the share of non-public banks increased afterwards.

Murabaha (A debt-purchase) occurs when a bank buys a real debt (i.e., a promissory note) created through a contract of deferred payment of sale of goods or services. Based on the guidelines approved by the Money and Credit Council, the bank provides the customer with a credit line. The customer may purchase some items and give the seller a promissory note that can be discounted by the bank. This kind of contract was recognized as *Shari'ah*-compliant by the Guardian Council of Iran in 1982. According to the related guidelines, the banks must be assured of the accuracy of the transaction and the indebtedness of the client. The discount rate is specified by the Money and Credit Council. Debt purchase, which is not common in other Islamic countries except Malaysia, is permitted in the Iranian *riba*-free banking system (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, 5.3 % of outstanding facilities extended by banking system to non-public sector was in form of *Murabaha*. As figure 9 shows, although, till 2009, commercial banks had a dominant role in extending facilities in the form of *Mudarabah*, by that time the share of non-public banks had increased. The share of specialized banks kept variating during the whole period.

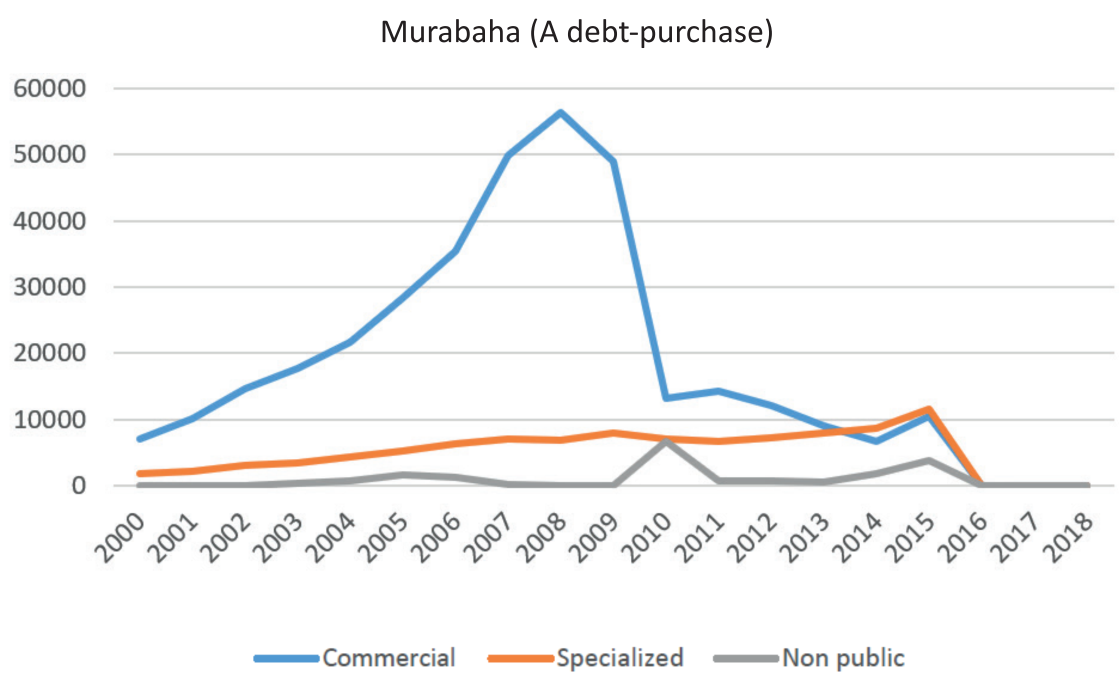


Figure 9. Outstanding facilities extended by banking system to non-public sector in form of Murabaha (A debt-purchase).

Source: On the basis of C.B.I

Installment Sale: In order to provide facilities for production and service companies, banks may purchase basic materials and spare parts, movable assets such as machinery and equipment, and houses, and sell them to the clients in installments. Currently, banks are not allowed to finance durable consumer goods on installments. Based on the related guideline, the client may request the bank to purchase a certain item and then commit to buy it back from the bank. The bank considers the request and purchases the requested item to be sold in installments with terms and profits as agreed in the contract. The Money and Credit Council determines the minimum and maximum bank profit in such contracts. The sale price of the goods sold on an installment basis will be based on a cost-plus scheme. In the case of raw materials and spare parts, the sale price must be paid back in one year. In special cases, the repayment period can be postponed for an additional year. In the case of machinery, the repayment period cannot be more than the useful life of the machine. The bank may require a down payment from a corporation (Parveen, et al., 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, 25.6% of Outstanding Facilities Extended by Banking System to Non-public Sector were in form of Installment Sale. As figure 10 shows, the commercial banks had a dominant role in extending facilities in the form of Installment Sale and the share of non-public banks had an increasing pattern.

Figure 10. Outstanding facilities extended by banking system to non-public sector in form of Installment Sale.

Source: On the basis of C.B.I

Ijarah (Lease Purchase or Hire Purchase): In this mode of financing, banks buy buildings, machinery, and equipment to buy real property or other assets needed by enterprises or individuals and lease the assets to them. The price of the asset is determined on a cost-plus basis. The ownership of the property is transferred to the lessee at the end of the contract. The contract delineates the total sum, number, and amount of installments and the duration of the agreement. At the end of the lease period, the lessor (the bank) transfers the property (movable or immovable property) to the lessee. Since the item belongs to the bank, the lessee is obliged to observe conditions such as proper application, maintenance, and repair. The total sum is calculated based on the price of the item plus the bank's expected profit (Parveen et al. 2015; Nili, 2014; Ashraf and Alizadeh Giashi, 2011). In 2017, only 0.3% of outstanding facilities extended by banking system to non-public sector were in form of *Ijarah*. Figure 11 shows that the commercial banks played a dominant role in extending facilities in the form of Lease-Purchase, whereas the lowest share belongs to the non-public banks.

Figure 11. Outstanding facilities extended by banking system to non-public sector in form of Hire Purchase.

Source: C.B.I

Facilities Extended to the Public by Non-Bank Institutions

Figure 12 summarized the facilities extended by non-bank institutions in Iran. As the table shows, the share of non-bank institutions has reflected an increasing pattern in Iran. The share of non-public and credit institutions, and special non-bank institutions increased following year 2010. The credit institutions had a dominant role in extending facilities to the public since 2010.

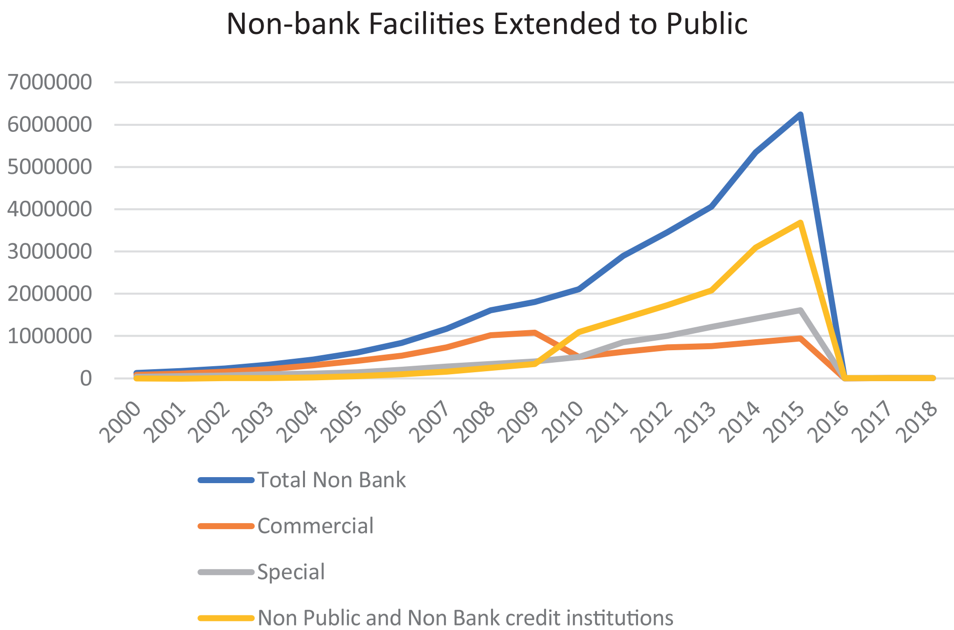


Figure 12. Outstanding facilities extended by non-bank institutions.

Source: C.B.I

Microfinance Charities: Their license allows them to charge a 4 percent commission on lending. However, unless a minimum scale is reached, 4 percent is not sufficient to cover operating costs in times of high inflation. As a result, sub-optimal entities started to take on credit risk by granting non-interest, free facilities. Losses led to a run on a microfinance charity in Isfahan in 2003. The panic brought to light the risk posed to social stability by chronically loss-making microfinance institutions that also collect deposits. The 2007 "law on the regulation of Non-Bank money markets" imposed limits on charities' operations: deposits became subject to CBI reserve requirement; lending was restricted to interest-free loans.

Credit Unions: The vast majority of Credit unions progressively engaged themselves in regular banking in violation of the license. To attract deposits away from established banks, some institutions promised to remunerate term deposits much above THE CBI-regulated rates offered by banks. Paying high deposit rates required credit unions to engage in riskier lending. In 2010, one million depositors were affected by the bankruptcy of two medium-sized credit unions. The run stopped when the CBI provided a credit line to a bank that agreed to absorb the failed institutions.

Waqf Properties

The financing tools and schemes that have been adopted in Iran for the development of endowed properties are summarized as follows: the ACO has formed a Development and Rehabilitation Fund to survey the *Waqf* properties all over the country. Furthermore, ACO diversifies financing avenues for investment projects by resorting to the issuance of *Waqf* certificates, *Musharakah Sukuk*, *Qard Hasan* certificates and Waqf shares. For instance, the construction of cancer specialist hospitals in three provinces of Shiraz, Tehran, and Araak was started through the issuance of *Waqf* shares. It also initiates the "Endowment Investment Fund" by allocating it to part of the income that is gained from down payments of the rented properties, available liquidity, and other small income receipts. Further, by participation in income-generating projects and investing the Fund's resources, both old *Waqf* projects will be revived and the Fund's income will be sustained. In addition, ACO is contemplating to initiate *Waqf* properties stock exchange and auction for both physical properties and the *Waqf* securities (Sorush, 2013; Musavian, et.al, 2009). To implement the above programs, the potential Waqf enterprises were identified over 31 provinces of the country in the year 2014. Overall, 352 corpus were identified for renovation and new investment. They are listed in table 2. The values stand at an estimated IRR of 12,298 billion. The financing is to be made either by the income obtained from *Waqf* properties or by participation with the private sector. Waqf shares were valued with three rates of USD 15, 30, and 60, in order to enable contributors with different financial capabilities participate in these investments (Sadr and Sorush, 2013; Musavian, et.al, 2009).

Hazrat Masoumeh (AS) Trustees' trustee has taken a series of initiatives to increase the productivity of the endowed properties. The rest are commercial projects that have been established through participatory contracts with private investors who finance the construction. In all concluded *Musharakah* contracts, the share of the endowed corpus is 50 percent or more, indicating the successful efforts of the trustee to increase the collectible revenues and to invest them further to renovate the old *Waqf* properties (Astan Quds Hazrat Maoumeh, n.d.).

The innovation made by Namazi hospital in the method of finance is that a part of non-government shares is going to be paid by issuing "*Waqf* certificates" (Sorush, 2013), an initiative which is relatively new for financing *Waqf* activities. The benevolent heritage of the late Namazi and the valuable continued services of Namazi hospital have created a scenario where many people at different levels of income are willing to participate in this new *Waqf* project. Also, this example illustrates that new methods of financing *Waqf* projects are approved by *Shari'ah* and legal authorities (Sorush, 2013).

Performances

Upon introduction of the Usury (Interest) Free Banking Law in 1983, all facilities were extended to the non-public sector within the framework of transactions and PLS (profit and loss sharing) contracts. According to table 1, during the period 1984-2000, on average, 39.5 percent of the Islamic contracts were in the form of PLS and 60.5 percent were transaction contracts. Among PLS contracts, the highest shares belonged to the civil partnership, 40 percent and *Mudarabah*, 27 percent, while installment sale (77 percent) and *Qard Hasan* (11 percent) had respectively the greatest shares among transactions contracts (Komeijani, 2010).

During the first four years of the third FYDP (2000-2005), non-PLS contracts held 79.1 percent share in the total change in outstanding Islamic contracts and PLS contracts 20.9 percent. The share of non-PLS contracts had an increasing trend. Nevertheless, in the last year of the third Plan; this share decreased from 30.9 percent in 2001 to 20.9 percent. Iranian banks and credit institutions extended financing to their customers; installment sale (33.2%), civil partnership (7.7, forward transaction (6.61%), and *qard hasan* loans (5.29%). In addition, 33.12% of the facilities were in the form of installation sales (Column 3. Table 1).

During the first four years of the fourth FYDP (2006-2011), the share of non-PLS outstanding facilities allocated by banks and credit institutions to the private sector exceeded the PLS ones. The share of PLS contracts in the total change in outstanding extended facilities surpassed that of non-PLS contracts, reaching 79.9 percent in 2010. This was mainly due to the approval of the Law for Rationalization of Banks' Deposit and Lending Rates in 2007 and fixing of the lending rate for non-PLS contracts at 12 percent during 2007-2010. Iranian banks and credit institutions extended financing to their customers as follows: installment sale (42.41%), civil partnership (16.57), *Mudarabah* (7.07%0), *qard hasan* loans (3.79%), and so on (Column 4. Table 1).

During the fifth FYDP (2010-2015) Iranian banks and credit institutions extended financing to their customers through installment sale (29.58%), civil partnership (39.44), *Mudarabah* (3.27%) and *qard hasan* loans (4.99%) (Column 5, Table 1).

During the first two years of the sixth FYDP (2016-2021), Iranian banks and credit institutions extended financing to their customers using predominantly civil partnership (41.36%), followed by installment sale (25.56%) and *qard hasan* loans (5.20%) (Column 6. Table 1).

Table 1.
Shares of the Outstanding Facilities extended by the banking system to non – public sector during the Five-year Development Plans.

FYP	FIRST	SECOND	THIRD	FOURTH	FIFTH	SIXTH
Banks and Non-Bank Credit Institutions (billion Rials)	100.00	100.00	100.00	100.00	100.00	100.00
Qard Hasan	5.13	4.76	5.29	3.79	4.99	5.20
Mudarabah	9.34	6.58	5.95	7.07	3.27	1.93
Salaf (Forward Transactions)	6.10	5.80	6.61	3.67	0.50	0.43
Civil Partnership	16.01	14.79	7.73	16.57	39.44	41.36
Jo'aleh	6.15	4.15	1.65	3.80	4.57	3.97
Installment Sale	46.86	46.07	33.12	42.41	29.58	25.56
Ijarah (lease-purchase or Hire Purchase)	0.57	0.82	1.02	1.94	0.61	0.30
Housing	0.00	5.24	29.25	5.18	0.00	0.00
Legal Partnership	5.02	3.44	1.82	1.75	2.43	3.33
Direct Investment	1.68	2.12	0.95	0.89	0.90	0.91
Other	0.23	1.03	6.61	10.01	14.61	17.92

Source: Author's calculation based on C.B.I data

Monetary Policy

The banking system in Iran is regulated by the Central Bank of Iran (CBI, 1980). The Money and Credit Council is the highest policy making body of the bank. Its permanent members are the CBI Governor, the Finance and Economy Minister, two Ministers chosen by the Cabinet, The Head of the Chamber of Commerce, the General Prosecutor and two lawmakers. Each year, after approval of the government's annual budget, the CBI presents a detailed monetary and credit policy to the Money and Credit Council for approval. Thereafter, major elements of these policies are incorporated into the five-year economic development plan. According to Money and Banking Law (1960), monetary policy has traditionally been implemented in order to achieve several objectives, including curbing inflation, enhancing production and employment, and maintaining the value of Iran's national currency. The Iranian banking system followed the same route, with intensive government intervention. After the Islamic Revolution in 1979 and ratification of the RFBA in 1983, the Central Bank of Iran designed monetary and banking policy by using two kinds of monetary policy instruments i.e. direct and indirect instruments (Law for Usury (Interest) Free Banking 1983, Art. 20)

Direct Instruments

Central Bank based on its regulatory powers employs Direct Instruments in two ways as follows:

Profit Rates Management: The Money and Credit Council is responsible for the regulation of profits and the expected rate of return on banking facilities as well as maximum and minimum profit rates based on the RFBA. Moreover, the Central Bank is authorized to determine the possible minimum return on investment or partnership schemes and, when necessary, the minimum and maximum profit rates on banking facilities. As Table 2 shows, during (1981-2001), deposit and lending rates on facilities extended to various economic sectors were confronted with numerous changes, but due to higher inflation rates, the tendency was towards increasing the rates. After the Islamic revolution until the course of the third FYDP, lending rates on facilities extended to various economic sectors were set within a range. During the third FYDP, as a result of reduction in the inflation rate, increase in banks' credit capacity due to reduced reserve requirement ratio, and improved economic condition, banks' lending rates were also reduced.

Table 2.
Profit rates or expected rate of return for the short term, special, one year, and two year investment projects.

Year	Short term	Special	One year	Two year
1985	6	NA	8	8
1986-90	6	NA	8/5	8/5
1991	6/5	NA	9	10
1992	6/5	NA	9	10/5
1993	7/5	NA	10	11/5
1994-95	8	NA	11/5	13/5
1996-2001	8	10	14	15
2002-6	7	9	13	13-17
2007-8	7	7-16	7-16	7-16
2009	9	9	15	16
2010	9	12	14.5	15.5
2011	6	8-11	14	14.5
2012	7-15	10-15	17	18-18.5
2013	7-15	10-19	17	18-18.5
2014	7-20	10-23	17-21.5	18-21.75
2015	10-22.2	11-23	22-24	_
2016	10-18	11-18	18-20	_
2017	10	11-15	15-15/5	_
2018	10	_	15	_

Source: Calculated from the C.B.I data

Since the inception of the fourth plan, lending rates have been unified for all economic sectors. In the initial year of the fourth FYDP, with the Money and Credit Council's approval, and based on the Plan Law, the minimum expected rate of return on facilities extended by public banks to all economic sectors were unified. Based on Article 10 of the fourth FYDP Law, the allocation of banking facilities by the government (in the sectorial or regional form) shall be carried out through subsidy payments and administered funds. During the course of the plan, lending rates on facilities extended by public and private banks to various economic sectors (within the framework of non-PLS contracts) decreased and stood at 12 percent during the last year of the plan.

The weighted real deposit rates were negative except for a few years (1984-1986 and 1990-91). This indicates that depositors were taxed and credit recipients enjoyed the advantage of lending rates. Unfortunately, this approach toward the administrative setting of deposit rates is still taken by the government and the parliament. Enactment of the Law on Rationalization of Banks' Deposit and Lending Rates by the parliament in 2006/07 indicates that the mentioned rates were not reasonable and monetary policy making is not optimal.

Table 3.

Expected rate of return on facilities by sector (percent).

Year	Exports	Trade, Services and Miscellaneous	Construction and Housing	Manufacturing and Mining	Agriculture (percent)
1985-90	8-12	8-12	8-12	6-12	4-8
1991	17-19	17-19	12-14	11-13	6-9
1992-3	18 (less than or equal)	18 (less than or equal)	12-16	11-13	6-9
1994	18	18-24	12-16	16-18	12-16
1995	18	18-24	15	16-18	12-16
1996-02	18	22-25	15-16	17-19	13-16
2003	17	22 (less than or equal)	14-15	15-17	13-14
2004	15	21 (less than or equal)	15 16	16	13.5
2005	14	21 (less than or equal)	15 15	15	13.5
2006	16	16 (less than or equal)	15 14	16	16
2007-10	14	14	13 12	14	14
2011-14	12,14	12,14	11,14 12,14		12,14
2015	22 (greater than or equal)	22 (greater than or equal)	14-16 (greater than or equal) 22		22 (greater than or equal)
2016	20,21	20-21	14-16 21-20	21-20	21-20
2017-18	18	18	8-17/5 18	18	18-15

Source: Calculated on the basis of C.B.I data

With the steady fall in inflation and in accordance with the macroeconomic requirements of the economy, nominal deposit rates were decreased gradually and in stages in the fifth FYDP (2011-2016). As a result, the profit rate for one-year deposits declined from a maximum of 22 percent in 2014 to 15 percent in the last year of the fifth FYDP. Moreover, the maximum lending rates on non-PLS and PLS contracts concluded between banks and credit institutions and their clients decreased from 22% and 21% respectively in 2014 to a maximum of 18% in 2016 (the last year of the 5th FYDP).

In the first year of the sixth FYDP, maximum profit rate was 15.0 % for one-year term investment deposits; maximum lending rate was 18.0 percent on non-PLS contracts as well as for expected profit rate on PLS contracts of banks and non-bank credit institutions as explicitly expressed in the concluded contracts of banks and non-bank credit institutions with clients.

Credit Ceiling: Limitations on credit and direct facilities and giving priority to certain economic sectors act as a policy instrument to direct credit toward target sectors. Furthermore, empowered by the Money and Banking Act, the Central Bank of Iran may intervene through restricting banks by determining the application of deposit funds, and specifying the maximum amount of loans for various sectors. Based on the monetary, credit, and regulatory policies of the Iranian banking system, all fund suppliers i.e. public and private banks as well as credit institutions licensed by the Central Bank should give priority to productive sectors. Money and Credit Council recommends the banks to allocate 80% of their excess reserve to priority sectors (allocated as follows: 37% to manufacturing and mining, 25% to agriculture, 20% to construction and housing, 10% to trade, and 8% to export). The remaining 20% of the excess reserve could be used freely. Nevertheless, there are sub-limits on credit for consumer durables or home improvement. The limits concerning credit allocation support job creation as the economy's access to foreign capital became more restricted (IMF, 2011b, pp. 4-7). Since the approval of the third FYDP, this practice is no longer valid.

Indirect Instruments

Indirect instruments depend on market conditions. The Central Bank indirectly influences market conditions as the issuer of high-powered money. The indirect investment could be classified as follows:

The Reserve Requirement Ratio (RRR): RRR is one of the CBI's indirect instruments for implementing the monetary policy. Banks are required to preserve a certain portion of their deposits in the Central Bank. By changing this ratio, the Central Bank is able to manage the facilities granted by the banking system. According to the Money and Banking Act, the legal reserve portion is set by the Central Bank in the range of 10 to 30 percent.

During 1981-2002 period, the utilization of RRR was among the limited central bank instruments. Raising the RRR for commercial banks continued during the 1981-1991 period, and reached its maximum level in years 1991-2001. At the beginning of 1993, in order to decrease the liquidity growth, the RRR was set at 30 percent for commercial banks, and 10 percent for specialized banks. These payments were not previously subject to RRR.

Since the commencement of the third FYDP (2005-2010) and reduction of inflationary threats, as well as to strengthen the lending operations of banks, the RRR was decreased and set at 17 percent for commercial banks and 10 percent for specialized banks. During the first three years of the fourth FYDP, RRR remained unchanged. However, in 2009-2010, in order to increase the sustainability of banking deposits and encourage banks to hold more long-term deposits, the RRR was reduced and determined according to the maturity date of banking deposits. Despite the decrease in RRR, the weighted average was around 15 percent.

Over the course of the fifth FYDP (2010-15), RRR for the specialized banks on average was 10 percent. The RRR for the deposits in commercial banks and non-bank credit institutions was set at 17% during the four years of the plan and was decreased to 13.5% in 2015. Based on paragraph (3) of the mentioned approval, from 2016, the RRR for the deposits in commercial banks and non-bank credit institutions was set within a range of 10 to 13 percent. It was also decided that the ratios set by the CBI should be revised every three months, based on banks' and credit institutions' performance in this regard. The RRR applied to commercial banks and credit institutions (state-owned and private) is unified at 13.0 percent. The RRR for specialized banks and banks' and credit institutions' branches in free trade zones is set at 10.0 percent. The RRR for the Housing Savings Fund program of Bank Maskan remains unchanged. The release of funds to banks as a result of the execution of current regulation (lowering of banks' reserve requirement ratios) will be utilized first for the debt settlement of banks with CBI. RRR on *Qard hasan* savings deposits held with banks and credit institutions is determined at 10.0 percent.

Open Deposit Account (ODA): One of the bold measures taken for the efficient utilization of indirect monetary instruments in the framework of the Usury-free Banking Law is to allow banks to open a special deposit account with the CBI. Regulation on ODA was approved by the Money and Credit Council at the end of 1998/99. The main objective of this plan was the adoption of appropriate monetary policies to control liquidity through the absorption of banks' excess resources. The CBI pays profit to these deposits on the basis of specific rules. Unlike the legal reserve deposit, this account is not mandatory, and banks may choose to deposit their excess funds with the Central Bank and receive remuneration.

Central Bank Securities (Open Market Operation): After the Islamic revolution, open market operations, which involve buying and selling of bonds, were stopped. Because of the usury nature of this instrument, the open market operations as a monetary policy instrument were not used until the commencement of the third FYDP. Upon that time, in order to activate the participation of the investors in economic activities, utilization of participation papers instead of bonds as well as payment of real profit rates was put on the Central Bank's agenda. Since *riba*-based bonds are prohibited in Islam, the utilization of profit-sharing instruments is encouraged. Two types of securities were issued.

CBI Participation Papers: The first type of security that was issued by the Central Bank, subject to the approval of the Money and Credit Council, aims at absorbing the volume of liquidity in the hands of the public and blocking the funds raised by issuing securities. It also acts as a contractionary policy instrument in open market operations. According to the third FYDP Law, the CBI was authorized to issue participation papers through the Money and Credit Council's approval. However, based on the fourth FYDP Law, the issuance of Participation Papers by the CBI is authorized upon the approval of the parliament. By using this instrument, the CBI could affect broad money (M2) through the monetary base, thereby controlling the rate of inflation. Therefore, during the third FYDP and the first three years of the fourth FYDP, Central Bank issued participation papers as an instrument to absorb excess liquidity from the market. However, due to several factors including a low preset profit rate and the long process of issuance approval by the parliament, this instrument was not effective. Moreover, the burden of profit payment on Central Bank's balance sheet as well as the government expansionary fiscal policies made this instrument ineffective.

According to the Monetary, Credit, and Supervisory Policy Package for 2011, the general conditions for the issuance, maturity, and provisional profit rate of CBI participation papers were left at the discretion of the CBI governor. Nevertheless, due to the proportionate growth of liquidity, the CBI authorities decided not to issue participation papers in 2011.

Participation Papers (Sukuk): The second type of securities are called participation papers. Article 1 of the Law for the Issuance of Participation Papers states that, "in order to increase public participation in implementation of government's profitable development projects included in government annual budget laws, as well as profitable productive, construction and services projects, the government, public corporations, municipalities, non-public institutions and entities, public utility corporations, and their affiliates, joint-stock and public joint-stock companies and producers' cooperatives are allowed, in line with this law, to finance part of the financial resources required for the implementation through issuance and public offerings of participation papers. Participation papers are registered or bearer securities with a specified nominal value issued for a specific period of time and are assigned to investors for the implementation of the projects mentioned in Article 1. Holders of these papers are entitled to their shares of profit, proportionate to the nominal value and the period of their participation. These papers are transacted directly or through the stock exchange" (CBI, 2018). Regulations that govern the issuance of these securities-including the trustee, duration, collateral, and involvement of banks-are set by the Money and Credit Council at the Central Bank of Iran.

Since its first issuance in 1994 till year 2011, *Musharakah Sukuk* was the dominant *Sukuk* type in Iran's financial system (Wilson, 2011). These participation bonds were supposed to be demanded from the issuing agent and at face value. Since they could not be sold in the secondary market, in 2009-2010 the amount of *Musharakah Sukuk* issuance was less than 1% of GDP.

Sukuk market in Iran has diversified with the emergence of *Ijarah Sukuk*, the 2nd notable *Sukuk* type, on the stage. The Law for Development of New Financial Instruments and Institutions (Articles 11 and 12), which was ratified in 2009, was the main factor that facilitated the issuance of *Ijarah Sukuk*. Under this law, Special Purpose Vehicles were recognized as one of the financial institutions under the Securities Market Act. Article 11 of this law outlines the tax exemptions for Special Purpose Vehicles. The article further spells out tax advantage to investors where "no tax whatsoever shall be claimed for the transfer, issuance, and redemption of the foregoing securities". Article 12, on the other hand, states that proceeds gained from selling assets to the Special Purpose Vehicles shall be exempted from tax and no tax and charges whatsoever shall be levied on the transfer of such securities.

In 2012, the Securities and Exchanges Organization adopted the regulation governing the Issue of *Murabaha Sukuk*. The first *Murabaha Sukuk* was issued to finance Butan Company in 2013. A year later, the Iranian capital market issued the fourth type of *Sukuk - Salam Sukuk*, which was used primarily to finance oil exploration and deployment projects by the National Iranian Oil Company. This was thought to be the region's first Islamic instrument in the Energy Market. From July 2014 until December 2016, the value of outstanding Salam *Sukuk* was over US$800 million, accounting for around 9% of total *Sukuk* outstanding in Iran's capital market as at the end of 2016. *Istisna Sukuk* first made its debut in Iran in 2015. Novin Investment Bank subscribed to the first *istisna Sukuk* in the Iranian capital market on behalf of national development Mining and Industries Company for collecting US$ 45.8 million at the market exchange rate. In September 2015, the first treasury bills after the 1979 Islamic revolution were issued with a face value of US$ 33.16 per bill and a maturity of 5.5 months. The first government *Sukuk* issuance in the form of Al-ljara (rent) was in 2015 and Murabaha (cost-plus) *Sukuk* in 2016. These securities carry maturities of two to five years and their return/profit is set around 20 percent. The Planning and Budget Organization provides the guarantee for repayment through budget resources. In 2016, Bank Maskan issued a US $86 million mortgage-backed security.

This marked another effort by the Securities and Exchanges Organization to introduce regulated debt instruments in the country.

Table 4. illustrates the Iranian capital market. It is a deep market for *musharakah Sukuk* but it is very small for ijara, *Murabaha, Salam, Iistisna* and mortgage-backed securities (IICM, 2016). However, the *Musharakah Sukuk* market was the dominant kind of *Sukuk* in Iran.

Table 4.
The value of outstanding *sukuk* issued by kind.

	2005 - 2008	2010	2011	2012	2013	2014	2015	2016
Islamic Treasury Bills	0	0	0	0	0	0	318	2484
Salam Sukuk	0	0	0	0	0	32	345	1259
MBS								98
Istisna Sukuk	0	0	0	0	0	0	54	54
Murabaha *Sukuk*	0	0	0	0	12	20	63	561
Murabaha Sukuk	0	0	303	449	665	959	936	1128
Musharakah Sukuk	444	800	2285	2566	2156	2667	1610	3546

Source: IICM (2016)

Figure 13 illustrates the growing pattern of issuing *Sukuk* in the capital market of Iran during 2005 -2016. The value of *Musharakah Sukuk* reached 3546 million dollars.

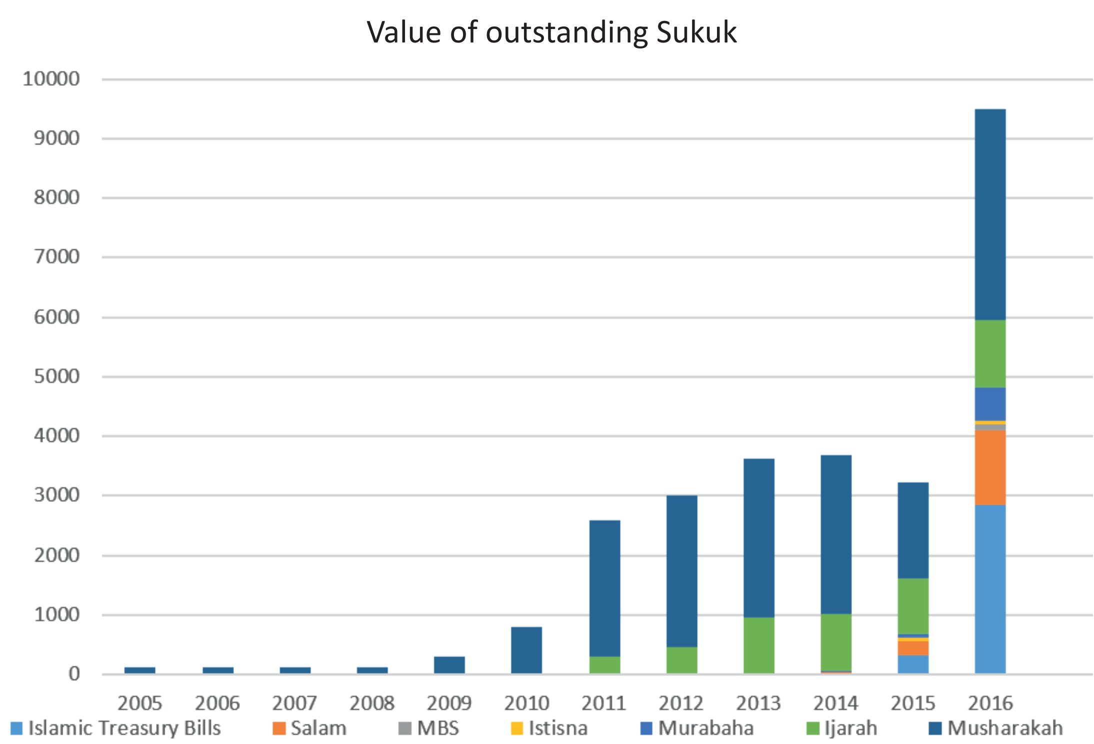


Figure 13. Value of outstanding sukuk issued in the capital market.

Source: IICM (2016)

In 2016, the maximum provisional profit rate on participation papers was set at 21.0 percent per annum. The issuing institutions are obligated to calculate the final profit rate of the projects and adjust the profit payment to the paper holders. The repurchase of Participation Papers by banks is not allowed prior to the maturity date of papers. However, these papers can be transacted in the secondary market in banks and on the Stock Exchange (IICM, 2016).

Discussion

Implementing *riba*-free banking for more than three decades, Iran has made substantial achievements. Iran has completely transformed legally its banking system to comply with the accepted Islamic principles. Nevertheless, Islamic banking progress is affected by several peculiar circumstances related to the country. Each phase of this progress i.e. nationalization, Islamization, and state dominance, has meant a significant jump in the utilization of the banking system to achieve the economic goals of the revolution and each phase has been prompted by impatience of the government authorities with the pace of Islamization. Before 1986, the Central Bank was implicitly a quasi-independent economic institution and revealed extensive control over the operation of the banking system. But in the third phase, the banking system is being rapidly integrated with the rest of the government and the central bank's independence has weakened.

Although Islamic banking in Iran from legal and theoretical aspects is well designed and is expected to be an effective tool for achieving economic objectives, in practice the efficiency of the system is questionable. The efficiency of Islamic banking is related to specific economic, political, and institutional factors of Iran. The burden of low efficiency of the banking system put on the shoulder of the real sector and its outcomes were the poor macroeconomic performances. This outcome can be explained partly by the shortcomings of implementing Islamic banking in Iran that put the future of the banking system in danger. These issues can be classified as follows:

Macroeconomic Performance

The first decade after the revolution was associated with a war with Iraq, and a rapidly growing population, hence a remarkable rise in the role of government in the economy and a dramatic decline in people's income (CBI, 2014). Iran accepted the United Nations proposal (UNSC Resolution 598) to end the war but the costs of war and heavy subsidies left behind a legacy of massive public debt from this time period.

After the economic contraction of wartime, Iran (1989-1997) adopted core policy changes that consist of various degrees of price liberalization, exchange rate unification, and industrial privatization. Within the first few years of utilization of the unused production capacity, increased public and private investments helped the economy end its downward trend. However, despite modest initial success, because of the maturity of accumulated foreign debts, new US sanctions, falling oil prices, and a high rate of liquidity growth, the economy gradually moved into stagflation (Salehi Esfahan and Pesaran, 2009; Nili et al., 2009). Khatami's presidency (1997–2005) concentrated on better governance. Because of the reduction of tension with the West and the gradual rise of oil prices, the economy expanded steadily. Real GDP per capita rose from $1,200 to $3,800 and inflation decreased from 20% to 10% (CBI, 2014). During Ahmadinejad's presidency (2005–13) the oil revenue was more than all oil revenue that Iran had earned after the revolution. Severe sanctions imposed in 2012 directly targeted the CBI and major banks accelerated the downward trend of the financial system and an increase in bank vulnerabilities was witnessed (Zahedi and Azadi, 2018). The real GDP per capita growth was the lowest compared to the previous era (2.5%) and the inflation rate was 19.2%. When Rouhani took office in 2013, the crude oil exports which were already cut by half along with the fall of oil prices further reduced Iran's oil export revenue to about a quarter of its pre-sanctions level. But after the implementation of the JCPOA in January 2016, due to the increase in oil exports, the economic growth rate increased. In parallel, high-interest rates along with what was seen as a better economic expectation tended to decrease inflation from 35% in 2013 to about 10% in 2015 (Zahedi and Azadi, 2018). The lack of implementing structural reforms and resuming of sanctions in 2018 have had the most negative impact on the growth outlook with oil shipments dropping at least by 2.5 million BPD. As a result, there was an economic contraction of 3.9 percent in real GDP, and a decline of 6 percent was expected for 2019 (IMF, 2019a). In addition, the real interest rate and currency exchange rate also affected inflation by changing the velocity of money and the prices of imported goods, respectively. Iran's real GDP per capita growth stood at -2.6% in 2018, annual average inflation at 31.2%, and the unemployment rate at 13.9% (IMF, 2019a). In addition, from the end of 2017, there has been a drop of about 70 percent in the value of the Iranian rial against the U.S. dollar.

Nevertheless, the sanctions can explain part of the poor macroeconomic performance, and the rest can be explained by internal factors. The real sector in Iran is highly dependent on bank credit i.e. more than 90% of corporates on external finance (Mahmoudzadeh, Nili and Nili, 2018). Because of the crucial role of banks in the financial market, any deficiency in the banking system directly transfers to the real sector. Despite rapid growth in the broad money supply, the real sector has consistently faced liquidity and cash flow problems. A recent study estimated that over 80% of companies listed on the Tehran Stock Exchange face credit constraints (Mahmoudzadeh, Nili and Nili, 2016). The cause of the problems is rooted in fiscal dominance, institutional weakness of the CBI, endemic corruption, and general misconducting.

Instability of the Banking System

Iran's banking system is suffering from several crucial problems, both external and internal, that make the country's financial sector unstable. Iran has been subject to a variety of external sanctions since 1979, but perhaps the strictest were put in place in 2012. A key component of the sanctions were restrictions on Iranian banks that helped isolate them from the global banking system, especially by curbing transactions in US dollars and correspondent relations with foreign banks. The number of correspondent banks fell from 306 in 2012 to only 4 in 2014 and access to the Brussels-based SWIFT1 banking platform was stopped (IMF, 2016). These restrictions raised the cost of banking, lowered banks' income from financing international trade, and pushed some financial transactions outside the regulated banking system. Banks' profits were also hurt by the CBI's raising of interest rates to cover the inflation that resulted from the sharp exchange rate depreciation following the sanctions. Profit rates on one-year deposits were raised from 17 to 24 percent (Keimasi, Rezaii, and Ghaffarinejad, 2016). Those sanctions decreased Iran's oil exports and imposed restrictions on Iranian banks that further cut them off from the global banking system, creating a currency crisis and a deep recession in Iran.

Resuming sanctions in 2018 again has accelerated the country's banking system problems. By the end of 2018, the SWIFT electronic payments system had disconnected Iranian banks. All of these sanctions led to further isolation of the Iranian banking system. Besides the external factors, the banking system of Iran suffers from several internal problems that can be classified as follows: *The Public Sector Dominance:* The banking system has a complex ownership structure involving extensive, nontransparent interconnections with various public or semi-public institutions and corporations and weak internal controls. These features have made the system very difficult to supervise and vulnerable to mismanagement and corruption. Iran's banking crisis is rooted in part in heavy state dominance and controls over banks.

Nonperforming Loans (NPLs): Loans were nonperforming for a number of reasons including country's venerable macroeconomic conditions; pervasive government arrears to public enterprises which in turn cannot service their bank loans; lending directed to public enterprises and selected economic activities; and challenges in evaluating the creditworthiness of borrowers because of weak corporate governance and accounting practices (CBI, 2018). One key policy change during the Ahmadinejad presidency was energy price reform, which finances partly the cash transfer scheme as well as other poverty relief programs. The remaining is part-financed through the banking system hence the banks' claims on the government increased from 1.7% to 7.8% of the GDP. Because of the direct lending to the government and government-owned corporations, the frozen assets in the banks' balance sheets increased. There was no choice but to borrow heavily from the central bank. As a result of these developments, Iran's financial sector confronted profound changes. The balance sheets due to rising non-performing loans (NPLs) and contraction of cash flow-generating assets were impaired. When Rouhani took office in 2013a, large amounts of toxic assets had brought the banking system to the verge of a major crisis (Nili and Mahmoudzadeh, 2014). As a result, in order to fill the gaps in their balance sheets, banks by offering higher interest rates began to compete to attract more deposits. Paying high-interest rates on the liability side amplified balance sheet imbalances. Competition to attract new deposits led to a price war and a Ponzi scheme. Meanwhile, with higher interest rates, the cost of borrowing in the real sector increased and, through the adverse selection effect, put more pressure on the banks' balance sheets (Mahmoudzadeh, Nili and Nili, 2016). This situation resulted in a downward spiral of higher interest rates and a further rise of NPLs. According to figure 15, in the last decade, the CBI claims on banks have increased on average by 13% per year, placing it as the main driver of the monetary base growth (Mahmoudzadeh, Nili and Nili, 2016). IMF estimates placed NPLs in June 2017 at 11.4 percent (IMF, 2018). The IMF has also reported a broader measure of NPLs that includes banks' illiquid assets; this second measure was 28 percent in June 2017. Provisioning for NPLs is low-only 43.6 percent of official NPLs in June 2017-partly because of the pressure to pay dividends to shareholders (IPRC, 2017/18, 2018; IMF, 2018; Mazarei, 2019). Officially, over one in ten bank loans were nonperforming (Islamic Parliament Research Center of the Islamic Republic of Iran, 2018).

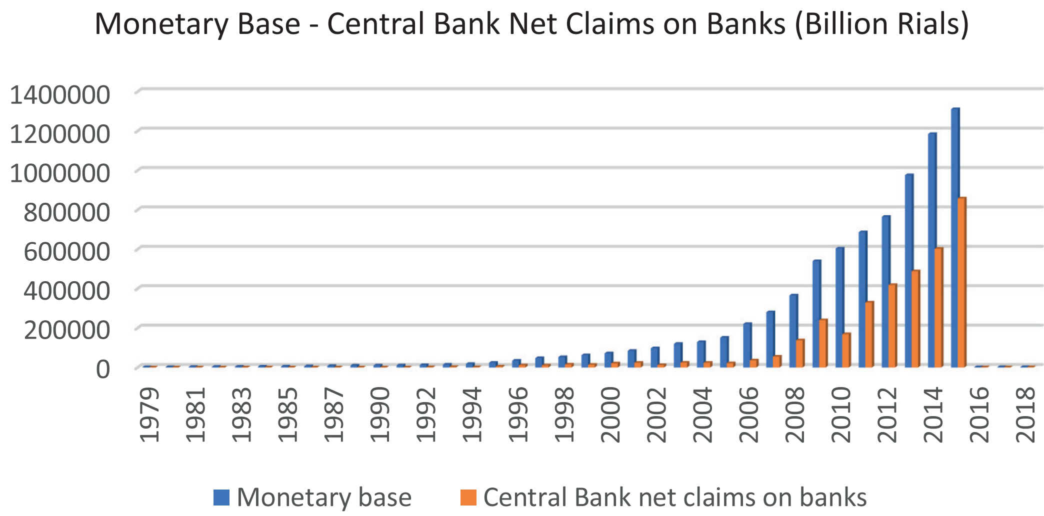


Figure 14. Central Bank of Iran's net claims on banks, 1980–2017.

Source: IMF (2019b), Mazarei (2019)

Unhealthy Financial Soundness Indicators (FSI): The key FSI of the Iranian banks have changed between 2005 and 2017. A marked deterioration of the banking sector's health in terms of accumulation of non-income-generating assets (NPLs and claims on government), the build-up of debt to the central bank, decline in banks' ability to absorb losses (CAR), and lower profitability (ROA) is witnessed. The banks' debt to the CBI (9.2% of total loans) is approaching their required reserves (11.6% of total loans). The high growth rate of liquidity (M2) led to an expansion in size of banks without a corresponding increase in their required capital, causing the capital adequacy ratio in the system-wide banking system to reach less than 4.9%, which is far below the Basel II and Basel III international standards that recommend minimum CAR levels of 8% and 10.5%, respectively (IMF, 2018). This problem developed over several years of weak profitability in the banking system due to the high amount of NPLs, high cost of funds, and high operating costs.

The Large Shadow Banking System: These unregulated financial institutions have competed aggressively with regulated banks for deposits by offering interest rates considerably higher than the CBI's maximum interest rates paid by regulated banks. In the absence of supervision and adequate internal controls, some of these institutes have faced difficulties (including runs on two of them in 2017), requiring the CBI to bail out depositors and merge or close many of them (IMF, 2018).

Bailing Out Banks: Banks have faced chronic liquidity problems from high levels of NPLs, their holding of illiquid real estate and equity, and the lack of cross-border correspondent banking and trade financing due to sanctions. As figure 15 shows, CBI has been actively bailing out banks for many years by providing large liquidity injections. The CBI's willingness to inject resources into banks through its emergency liquidity window-at high-interest rates (34 percent) but without collateral—has turned it into a lender of first resort and has used up its control over monetary conditions. Monetary policy has become increasingly guided by the liquidity needs of banks, especially private banks. Private Banks had the highest average NPL ratio (about 13%). This can be explained by the fact that the weaker borrowers with riskier projects borrow from private banks (Nili and Mahmoudzadeh, 2014). The reaction of the CBI to the abovementioned issues was limited to attempts to play a more effective role in the interbank market, prohibit dividend distribution in loss-making banks, and push for more transparency and compliance with the Anti-Money Laundering.

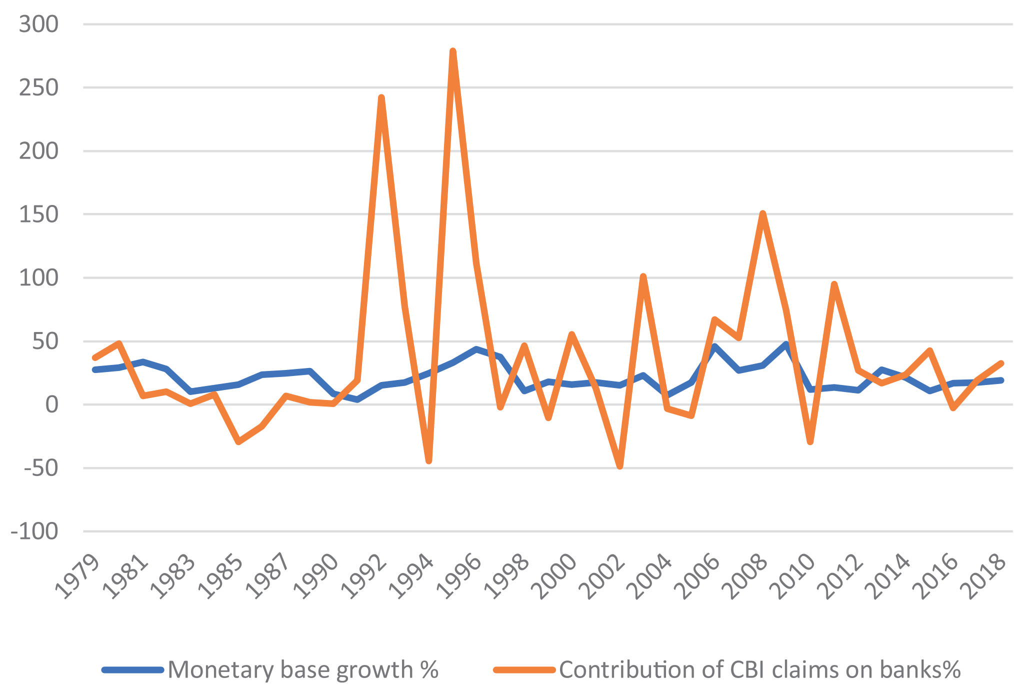


Figure 15. Central Bank of Iran's liquidity lifeline to banks. .
Source: IMF (2019b), Mazarei (2019)

Inefficient Monetary Policy

The performance of the monetary policy in Iran reveals that despite applying several direct instruments (such as managing the profit rates and putting the credit ceiling) and indirect instruments (the required reserve and the issuance of participation papers); since none of the legally approved instruments have been used efficiently, the Central Bank was successful neither to curb inflation nor to maintain the value of the currency. Iran has persistently experienced high (average 20%) and volatile (9%) inflation over the past three decades. Furthermore, since 1989, the rial has depreciated at an average annual rate of 18%. The depreciation has occurred in both forms of crawling (2002–2010) and bouts (2012 and 2018), the latter of which could possibly be attributed to speculative attacks. For decades, the de jure exchange rate regime of Iran has been managed floating while the de facto policy was a fixed exchange rate (2002–2010) and soft peg (crawl-like arrangement) (2010–present) with an anchor to a composite currency. Another important characteristic of Iran's currency exchange policy has been its multiple currency practices and various forms of restrictive measures on imports. The multiple exchange rate regimes of the past few decades not only have resulted in suboptimal allocation of Iran's scarce resources but have also allowed for the growth of powerful rent-seeking groups and corruption. The reasons behind the inefficient monetary policy can be classified as follows:

1. Iran is as an oil-exporting country hence its monetary policy is under fiscal dominance. In other words, the central bank is not independent. Because of the volatility of oil and gas revenues and insufficient measures taken by the government, the volatility of the net foreign assets and government debts to the Central Bank balance sheet was severe.
2. Since the monetary policy instruments available in Iran are limited, the authorities tried to control the monetary base through complementary approaches such as foreign exchange policies. The exchange rate is the main nominal anchor and liquidity management and the control over the systemic liquidity is a key determinant of the effectiveness of the monetary policy and the sustainability of the exchange rate (El Hamiani Khatat, 2016).
3. Another consequential factor in central bank performance is the poor quality of governance, independence, transparency and accountability. Therefore, fiscal dominance, lack of proper monetary instruments at the CBI's disposal, inefficient use of the available instruments, as well as exogenous uncontrollable factors are responsible for the poor outcome of Iran's monetary policy.

Shortcomings of Islamic Banking

In more than three decades of experiencing *riba*-free banking, Iran has made substantial achievements in absorbing deposits and allocating them to the real sector. However, there are several shortcomings.

1. Banks involved in Islamic finance cannot be expected to subsidize officially inspired ideas such as offering below-inflation rate loans and at the same time remain profitable. The business of Islamic banking and finance cannot be seen as a source of social good and in the interest of the banking sector concurrently. In Iran, remarks by the politicians appear to suggest an ambition to turn banks into providers of subsidized loans for the poor (Sadeghi Shahdani, 2007). What they can be reasonably expected to do is to follow a genuine Islamic policy set by the central bank, without influence from politicians. For instance, delayed payments of debts are a problem in the Iranian banking system for which no economic solution consistent with jurisprudence has yet been found. The legitimate way of imposing fines for delays in repayment has been a matter of debate since the Islamic Revolution.
2. Lack of public awareness about Islamic banking: Any kind of fixed profit is considered as a form of *riba* (usury). If one looks at the whole business from outside, it becomes clear that such vital knowledge is rare and that fund transfers are based only on signing a few contracts.
3. Lack of accounting and auditing standards: Proper implementation of *riba* free banking in Iran requires a revision of conventional accounting standards so that they match the requirements of Islamic banks. For example, most deposits in Iranian banks are subject to the wakalah and not a qard contract. However, such deposits are dealt with as qard contracts, and their principal and interest are registered as costs of capital in the records. Furthermore, there are no easy solutions with weak a system of accountability, where borrowers could declare a loss at the end of a pre-agreed time-frame even if they actually make a profit. Some contracts are sham; they appear one way on paper and contain some significant de facto differences when they are implemented. The

de jure aspects of *riba*-free banking are somehow different from the de facto aspects. Auditing systems lack the same standards, too. To tackle this deficiency, it is necessary to learn from the experiences of other Islamic banks and institutions (Nili, 2014).

4. The legal system does not distinguish between current accounts and *qard hasan*. Therefore, all current and some savings accounts are defined based on *qard hasan*, which is a kind of benevolent charitable activity that requires intention and sacrifice. Opening an account for the purpose of winning a prize or access to financial services does not count as *qard hasan*, regardless of whether interest is being paid or not (Nili, 2014).

5. Since 1983, Iranian banks' operations have been set de jure in the context of Islamic financial principles that proscribe fixed interest rate deposits and loans in favor of equity-based profit- and loss-sharing arrangements. In theory, Islamic finance should be less prone to crisis because its risk-sharing feature reduces leverage and encourages better risk management on the part of the banks and their customers (El-Gamal, 2006; Kammer. et al. 2015; Mazarei, 2019). In practice, however, banks in Iran operate very much like conventional banks. They treat loans and deposits as conventional banks do, with fixed interest rates that are not connected with the return on deposit/profit sharing. The CBI sets credit allocation guidelines and maximum deposit and lending rates, but banks do not always adhere to the interest rate ceilings. In fact, the CBI has frequently changed the maximum allowable interest rates depending on macroeconomic pressures (interest rates were raised sharply after the 2012 sanctions but have remained unchanged since the reinstatement of sanctions in 2018). While banks operate similar to conventional banks, the Islamic financial framework has hindered the development of a government debt market and has limited the tools available to the CBI for conducting monetary policy. In addition, banks are authorized to pay an on-account monthly profit to depositors before actual profits accrue at the end of the fiscal year. These on-account rates are being misused as a competition tool among banks. Although the Central Bank intervenes and determines the rates, banks sometimes find loopholes in the regulations.

6. The *Shari'ah* supervisory board of the Central Bank is the sole body in charge of supervising the *Shari'ah* compliance of Iranian banks. As a result, some banking activities fail to comply with *Shari'ah* principles because their associated contracts are not supervised. It seems that the banks themselves should step forward and make provisions for this purpose. With sole reliance on jurisprudence; one big challenge in the Iranian *riba*-free banking system is the dominance of jurisprudence in setting regulations, guidelines, directives, and contracts. This approach, which resorts solely to fiqh for resolving *Shari'ah*-related issues, turns a blind eye to the goals, principles, and foundations of Islamic economics and finance (Nili and Mahmoudzadeh, 2014).

7. The Iranian banking system has so far failed to maintain constructive cooperation with world's Islamic banks. Standardizing Islamic banking is not only necessary for running Islamic banks efficiently, but can also help in religious unity in the Islamic world to support each other in the wake of economic and financial crises. Deeper and wider cooperation in scientific and administrative fields is crucial.

Concluding Remarks

Iran legally has completely transformed its banking activities to comply with the accepted Islamic principles. Incorporating Islamic banks in the monetary policy framework is a complex task not only because of the need for compliance with Islamic finance's core principles but also due to the heterogeneity of financial systems and monetary policy frameworks. Several layers of difficulties are confronted with while implementing monetary policy, including shallow financial markets, pegged exchange rate regimes, fiscal dominance, interest rate controls and directed lending. In addition, the poor outcome of Iran's monetary policy is rooted in lack of proper monetary instruments at the CBI's disposal, inefficient use of the available instruments, the poor quality of governance, dependency, transparency, and accountability, as well as exogenous uncontrollable factors, importantly severe unfair sanctions against Iran. Although the banking system of Iran is being perceived as an effective tool in pursuance of Islamic economic objectives, the sector is suffering from several deficiencies that make the system vulnerable to external and internal shocks and real sector growth is impeded. In order to decrease the vulnerability of the banking system to the external and internal shocks and make it more effective in obtaining the financial needs of the real sector, there is a serious need for major reforms on the level of banks as well as on the macro level.

At the bank level, the design of effective liquidity management frameworks for Islamic banks is required to be based on the orderly development of Islamic domestic *Shari'ah*-compliant interbank, government *Sukuk* markets and exchange rate sustainability. Those markets cannot develop without coordination and strong commitment of the Central Bank and the fiscal authority as well as the necessary regulatory change needed to facilitate their development. The importance of domestic government *Sukuk* markets is not only needed for the implementation of an Islamic monetary policy but the profitability and viability of Islamic banks also calls for a more proactive role of Central Bank in the development of these markets. Furthermore, there is a need for the introduction of new products and instruments for the banking system in line with innovations in modern banking.

On the macro level, macroeconomic and financial stability will be critical to building an efficient Islamic banking system in Iran. Islamic banking of Iran will definitely contribute to the welfare of their community as well as to the welfare of the world as a whole in the presence of effective corporate governance, more transparency, accountability, and better interaction with the relevant international, regional and national institutions, as well as with political and economic stability.

Iran at a Glance[2]

Official Name:	Iran (officially the Islamic Republic of Iran)
Capital	Tehran
Location	Located in Southwestern Asia. Northern border: Armenia, Azerbaijan and Turkmenistan. Western border: Turkey and Iraq. Eastern border: Afghanistan and Pakistan. Southern border: The Persian Gulf and Oman Sea.
Surface area (1000 sq. km)	1,745.2
Language:	Persian (Farsi)
Religion:	99.4 % Moslem,90–95% Shia, remaining 0.6% non-Islamic, Zoroastrians, Jews, and Christians
The official unit of currency	1 Toman (super unit) = 10 Iranian rial (IRR)
Population, total[3]	81.16 million
Population growth (annual %)	1.4
Life expectancy at birth, total (years)	76
Net migration (thousands)	-275
Human Development Index[4]	0.798 high (2017) (60th)
Fertility rate, total (births per woman)	2.1
Iran's economic freedom score[5]	51.1, the 155th freest (2019)
Ease of doing business index[6]	128th (2019)
Total literacy rate (above 6 years old)[7]	87.6 (2016)
Gini Coefficient	0.40 (2016)
Poverty headcount ratio at $1.90 a day (2011 PPP) (% of population)	.3

Notes

1 SWIFT stands for Society for Worldwide Interbank Financial Telecommunications

2 Sources include data from Statistical Center of Iran and Central Bank of the Isalmic Republic of Iran.

3 Sources include World Bank data and Eurostat.

4 Data obtained from www.hdi.undp.org.

5 Data obtained from https://freedomhouse.org

6 Data obtained from www.Doingbusiness.org

7 Statistical Center of Iran

List of Figures

List of Tables

Glossary

ACO Auqaf and Charity Organization

CAR Capital Adequacy Ratio

CBI Central Bank of Iran

CPI Consumer Price Index

FSI Financial Soundness Indicators

FYDP Five-Year Development Plan

GDP Gross Domestic Product

IMF International Monetary Fund

JCPOA Joint Comprehensive Plan of Action

Mmbbl/d Million barrels per day

M1 Narrow Money Supply (sum of currency and demand deposits)

M2 Liquidity (sum of currency, demand deposits, and time deposits)

MB Monetary Base (high-powered money)

NPLs Non-performing Loans

ODA Open deposit account

PLS Profit and Loss Sharing

RFBA Riba Free Banking Act

ROA Return on Assets

RRR Reserve Requirement Ratio

SWIFT Society for Worldwide Interbank Financial Telecommunications

U.S.A United States of America

References

Ashraf, H. & Alizadeh Giashi, A. (2011). Islamic Banking in Iran - Progress and challenges. *Kuwait Chapter of Arabian Journal of Business and Management Review, 1*(2), 31.

Auqaf and Charity Organization. (2002). *Report on developments in Waqf and charity affairs during the last 20 years*. Auqaf & Charity Organization, Public Relations Office. Retrieved from http//www.razemandegari.com

Astan Quds Razavi. (2013). *A 33 Years Performance Report* (Vol. 1). Mashhad: The Central Official Complex.

Behdad, S. (1988 OR 1989 or 1987?). The Political Economy of Islamic Planning in Iran. In H. Amirahmadi and M. Parvin (Eds.), *Post-Revolutionary Iran*. Boulder, Colo.: Westview Press, Inc.

CBI (1978). *Annual Report*. Central Bank of Iran.

CBI (1980). *Annual Report*. Central Bank of Iran.

CBI (1983). *Law for Usury (Interest) Free Banking*. Tehran: Central Bank of the Islamic Republic of Iran. Retrieved from www.cbi.ir/simplelist/1457.aspx

CBI (1984). Analysis of post-revolutionary economic change. Tehran: Central Bank of the Islamic Republic of Iran.

CBI (1997). *Law for the Issuance of Participation Papers*. Tehran: Central Bank of the Islamic Republic of Iran. Retrieved from www.cbi.ir/page/2560.aspx

CBI (2014). *Monetary Policy Instruments in Iran*. Tehran: Central Bank of the Islamic Republic of Iran. Retrieved from http://www.cbi.ir/page/1465.aspx.

CBI (2018). *Economic Report and Balance Sheet for 2016/17*. Tehran: Central Bank of the Islamic Republic of Iran.

Cizakca, M. (2000). *A History of Philanthropic Foundations: The Islamic World from the Seventh Century to the Present*. Istanbul: Bogazici University.

Curzon, G. N. (1892). *Persia and the Persian Question* (Vol. 1 & 2). London.

El-Gamal, M. (2006). *Islamic Finance, Law, Economics, and Practice*. Cambridge: Cambridge University Press.

El Hamiani Khatat, M. (2016). *Monetary Policy in the Presence of Islamic Banking* (Working Paper No. WP/16/72). International Monetary Fund.

Fars Province (2011). *Annual Statistical Report*. Shiraz: Fars Province.

Global Islamic Finance Report (2017). *Leadership in Islamic Finance*. Islamic Bankers Association.

Guillaume, D., & Sensenbrenner, G. (2011). *Staff Report for the 2011 Article IV Consultation: Selected Issues*. International Monetary Fund.

Hassani, M. (2010). Islamic Banking and Monetary policy: Experience of Iran. *International Review of Business Research Papers, 6*(4).

Idem, A. (1982) The Role of Financial Intermediaries in Economic Development: The Case of Iran, 1888-1978 (Doctoral dissertation). George Washington University.

IICM (2016). *Musharakah Sukuk in Iran* (Vol. 8/1). Securities & Exchange Organization (SEO).

IMF (2011a). *Islamic Republic of Iran: Selected Issues Paper* (Country Report No. 11/242). Washington: International Monetary Fund.

IMF (2011b) . *Staff Report for the 2011 Article IV Consultation*. Washington: International Monetary Fund.

IMF (2016). *The Islamic Republic of Iran—Staff Report for the 2016 Article IV Consultation*. Washington: International Monetary Fund.

IMF (2018). *The Islamic Republic of Iran—Staff Report for the 2018 Article IV Consultation*. Washington: International Monetary Fund.

IMF (2019a*). Regional Economic Outlook Update, Middle East, North Africa, and Pakistan (Statistical Appendix)*. Washington: International Monetary Fund.

IMF (2019b). *World Economic Outlook*. Washington: International Monetary Fund.

IPRC (2017/18). *The Iranian Economy in 2016/17* (in Persian). Tehran: Islamic Parliament Research Center of the Islamic Republic of Iran.

IPRC (2018). *Assessment of the Performance of the Central Bank Regarding the Organization of Unlicensed Credit Institutions* (in Persian). Tehran: Islamic Parliament Research Center of the Islamic Republic of Iran.

Iqbal, Z. & Mirakhor, A. (1987). *Islamic Banking*. International Monetary Fund.

Issawi, C. (1972). The Economic History of Iran: 1800-1914, Center for Middle Eastern Studies. *American Political Science Review, 66*(4), 1383-1384.

Kabesee, O. (1975). *Ahkam al Waqf, Moasseseh al Nashr lel Idarah alAuqaf*. Baghdad.

Kammer, A., Norat, M., Pinon, M., Prasad, A., Towe, C., & Zeidan, Z. (2015). *Islamic Finance: Opportunities, Challenges, and Policy Options* (IMF Staff Discussion Note No. 15/05). Washington: International Monetary Fund.

Keimasi, Rezaii, & Ghaffarinejad. (2016). Effects of Sanctions of the. Iranian Banking System on Profitability. *Journal of Money and Economy, 12*(4), 369-388.

Khan, M. S. & Mirakhor, A. (1990). Islamic Banking: Experiences in the Islamic Republic of Iran and in Pakistan. *Economic Development and Cultural Change, 38*(2), 353-375.

Komeijani, A. (2010). Performance of Monetary Policy under the Interest-Free Banking Law in Iran, (1972-2010). Paper presented at the International Conference on Experiences of the Monetary Policy in Islamic Countries: Policy Dialogues. Money and Banking Research Institute and Islamic Research and Training Institute of the IDB, Tehran, Iran.

Mahmoudzadeh, A., Nili, M., & Nili, F. (2016). *Evaluation of the Performance and Perspective of the Financial Markets in Iran*. Monetary and Banking Research Institute, Central Bank of Iran (in Farsi).

Mahmoudzadeh, A, Nili, M & Nili, F (2018). Real Effects of Working Capital Shocks: Theory and Evidence from Micro Data. *The Quarterly Review of Economics and Finance.*

Mazarei, A. (2019). *Iran Has a Slow Motion Banking Crisis*. Peterson Institute for International Economics.

Mirakhor, A. & Zaidi, I. (1988). *Stabilization and Growth in An Open Islamic Economy* (IMF Working Paper Vol. 22, No. 88), (pp. 1-37). International Monetary Fund.

Musavian, A. et al., (2009). *Tarrahi Auraq Waqf Designing Waqf Certificates, Do Faslname Motaleat Eqtesad Islamic*.

Nili, M., Dargahi, H., Kordbacheh, H., & Nili, F. (2009). *Government and Economic Growth in Iran*. Nashre Ney (in Farsi).

Nili, F. (2014), *Islamic Finance Handbook, Iran Islamic Banking and Finance,* Ch. 13. Wiley Finance Series.

Nili, F., & Mahmoudzadeh, A. (2014). *Banks' Noncurrent Claims and Toxic Assets* (in Persian). Tehran: Money and Banking Research Institute.

Parveen, T., Zadeh, E. L., & Muzakkir, S. A. (2015). Evolution of Islamic Banking in IRAN: Prospects and Problems. *IOSR Journal of Business and Management (IOSR-JBM), 17*(9), 61-66.

Razzaghi, A. (1988). *Eghtedad-e Iran (The Iranian Economy)*.Tehran: Nashre Ney.

Sadeghi Shahdani, M. (2007). Islamic Banking In Iran From Theory To Practice. In *Proceedings of the 2nd Islamic Conference 2007 (iECONS2007)*. Faculty of Economics and Muamalat, Islamic Science University of Malaysia.

Sadr, S. K. and Souri, H., (2010). The Role of Management of Commercial Waqf Properties on Their Corresponding Generated Revenues. *Iranian Economic Review, 14*(25), 20-31.

Salehi Esfahan, H., & Pesaran, M. H. (2009). The Iranian Economy in the Twentieth Century: A Global Perspective. *Iranian Studies, 42*.

Sorush, A. (2013). *Waqf Certificates*. Tehran: Towe'eh Mondegar.

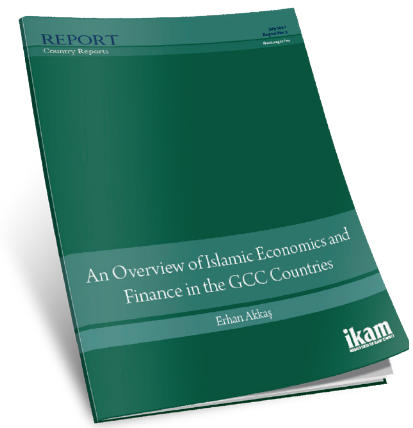
Thiagaraja, S., Morgan, A., & Tebbutt, A. (2014). *The Islamic Finance Handbook*. John Wiley & Sons Singapore Pte. Ltd.

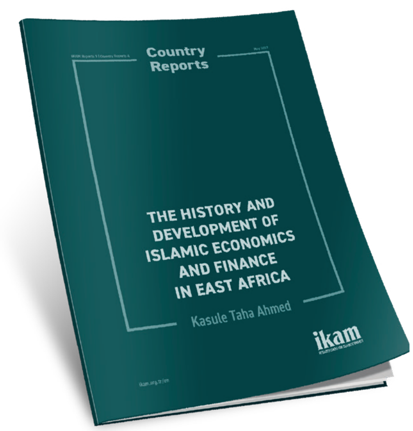
Valibeigi, M. (1993). Islamic Economics and Economic Policy Formation in Post-Revolutionary Iran: A Critique. *Journal of Economic Issues, XXVII*(3).

Wilson, R. (2011). *Approaches to Islamic Banking in the Gulf*. Dubai: Gulf Research Center.

Zahedi, R., & Azadi, P. (2018). *Central Banking in Iran* (Stanford Iran 2040 Project Working Paper No. 5). Stanford University.

Country Reports





Research Reports

ikam
RESEARCH CENTER FOR ISLAMIC ECONOMICS
Aziz Mahmut Hüdayi Mh. Türbe Kapısı Sk. No:13 Üsküdar İstanbul
ikam.org.tr info@ikam.org.tr ikamorgtr ikamorgtr

İLKE
ilim kültür eğitim vakfı