

## Effect of Interest-Based Debt Financing on Sustainable Development of Residents of Pakistan

### Implikasi Pembiayaan Hutang Berasaskan Faedah Terhadap Pembangunan Mampan Penduduk di Pakistan

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#### ABSTRACT

*Interest-based debt harms the country's financial, social, and economic structure, undermining the sustainable development of the masses. In Pakistan, for example, the state's reliance on interest-based debt at both international and national levels influences the nation's socio-economic framework, thus impeding the sustainable progress of its citizens. The study's objective is to analyse the effect of interest-based debt financing on the well-being of the masses in Pakistan. It is worth considering whether interest-based debt financing negatively impacts the sustainable development of Pakistan's masses. The method used in this study is part of a qualitative approach that involves the analysis of secondary data obtained through documents, research results or writings that have been highlighted. Moreover, a qualitative research methodology is employed to develop a conceptual framework using an inductive approach. It is expected that interest-based debt, whether acquired from foreign or national institutions by the government of Pakistan, undermines the country's sustainable economic growth. The study's findings suggest that the Government of Pakistan should develop strategies or policies to lessen the nation's reliance on interest-based debt. Nevertheless, Pakistan is constitutionally obliged to achieve sustainable development for its citizens in accordance with Islamic Shariah, ensuring the elimination of interest from its economy thereby enhancing both the tangible and intangible socio-economic well-being of its residents.*

*Keywords: Socio-economic well-being; residents; sustainable development; interest-based debt*

#### ABSTRAK

*Hutang berasaskan faedah mengganggu struktur kewangan, sosial, dan ekonomi negara, yang menyebabkan pembangunan mampan bagi rakyat terjejas. Seperti di Pakistan, kebergantungan negara terhadap hutang berasaskan faedah (baik dari peringkat luar negara mahupun dalam negara) mempengaruhi struktur sosio-ekonomi negara, dengan itu menggugat pembangunan mampan penduduknya. Objektif kajian ini adalah untuk menganalisis kesan pembiayaan hutang berasaskan faedah terhadap kesejahteraan rakyat di Pakistan. Persoalan timbul apakah pembiayaan hutang berasaskan faedah menggugat pembangunan mampan rakyat Pakistan atau tidak. Kaedah yang digunakan dalam penyediaan kajian ini adalah sebahagian daripada pendekatan kualitatif yang melibatkan penyorotan dan analisis data sekunder yang diperolehi melalui dokumen, hasil penyelidikan, atau penulisan yang telah ditekankan. Selain itu, metodologi penyelidikan kualitatif dijalankan untuk membina kerangka konseptual dengan menggunakan paradigma induktif. Dijangkakan bahawa hutang berasaskan faedah sama ada diperolehi dari institusi luar negara atau dalam negeri oleh kerajaan Pakistan menggugat pertumbuhan ekonomi mampan negara. Hasil kajian menunjukkan bahawa implikasi dasar masa depan bagi Kerajaan Pakistan adalah untuk merancang mekanisme atau dasar-dasar bagi*

*mengurangkan kebergantungan negara kepada hutang berasaskan faedah. Walau bagaimanapun, Negara Pakistan berkewajipan perlembagaan untuk mencapai pembangunan mampan penduduknya dengan mematuhi syariah Islam agar penghapusan faedah dari ekonomi Pakistan dapat dilihat, seterusnya penduduk Pakistan mampu mencapai kesejahteraan sosio-ekonomi secara langsung mahupun tidak langsung.*

*Kata kunci: Kesejahteraan sosio-ekonomi; penduduk; pembangunan mampan; hutang berasaskan faedah*

## INTRODUCTION

The economic problems of Pakistan lie in country's dependence mainly upon interest-based debt. The foreign interest-based debt availed by third world countries acts as the major barrier towards sustainable development of humans in their territories. The quality of life for the residents of the Country has been compromised as a cost to avail foreign debt on interest basis. Third world countries for their serious indebtedness towards rich countries has resulted in the creation of other economic issues. The country's reliance upon foreign interest-based debts has been resulted to handicap sustainable human development, also contributed in security, political and economic issues of the territories owing debt of rich countries (Shah 2007). Thus, is the case with Pakistan due to its reliance upon interest-based debt mainly upon foreign debt, which has created a vicious debt trap and blocked the way of country's economic success as Pakistan was on the way towards setting example for the world that economic development can be pursued by implementation of Islamic principles of Shariah with respect to national and economic affairs of the country. However, the country's dependency upon interest-based debt is the root cause of all economic problems in Pakistan (Ghutai & Bahari 2020). To protect Pakistan from debt crisis it is urgent need of time to abandoned interest-based debt acquisition policy to attain socioeconomic development. The subtopic of the study is comprised of background, followed by literature review, methodology, discussion, and conclusion.

## BACKGROUND

The vision of Pakistan to be an independent and sovereign Islamic ideological state was proposed by Iqbal in 1930 (Saeed 2002) and led by founding father Muhammad Ali Jinnah to be realized in 1947. The father of the nation in 1948 ordered State Bank of Pakistan to incorporate Islamic principles shariah in financial and economic affairs of the country (Mujahid, 2001). Pakistan was created by the name of Islam thus, for the reasons millions of

people sacrificed their lives, homes, well established businesses to live their lives according to the enlightened principles of Islamic Shariah (Ghutai & Bahari 2020). All the constitutions (1956, 1962, 1973) of Pakistan consented upon the abolishment of interest as early as possible. The existing constitution of Pakistan with respect to Article 38 (f) firmly asserts that the interest must be exterminated as early as possible. The present constitution of Pakistan asserts that the State is under constitutional responsibility to enable its residents both individually and collectively to comply with Islamic principles of Shariah in their lives (Pakistan 2004).

Moreover, the state will help to facilitate the residents of Pakistan to understand the meaning of life according to Quran and Sunnah of Prophet Muhammad PBUH (Haq, 2017). The existing Prime minister of Pakistan also vowed to make Pakistan alike first Islamic state of medina led by the last Prophet Muhammad (PBUH), (Farzana 2018). The holy book Quran clearly disclosed the decree of Almighty Allah (SWT) with respect to forbiddance of riba-interest upon Muslims. Moreover, all divine books has declared that interest is prohibited as it is based upon injustice and exploitation with respect to other fellow human beings (Ghutai & Bahari 2019). In today's era interest-based debt acts as the tool of capitalism due to which nations are enslaved with respect to racism and imperialism, oppressed, widens gaps between poor and rich thus, results in giving rise to injustice (Foster 2019). Moreover, due to adoption of free market capitalism the world has witnessed status structure, oppression, debt-based banking and warfare against the weaker nations of the world. It is possible to gather large amount of liquidity, this is because the interest-based debt as basic instrument of financial intermediation, pursual of derivatives, short selling assures profit maximization and concentration of wealth in fewer hands (Rebello, 2009). Therefore, the Shariah of Prophet Muhammad (PBUH) rejects riba-interest based economic endeavors and interest is clearly prohibited for Muslims no matter wherever they are. The divine decree is applicable to all Muslims since the Quranic revelations regarding the prohibition of interest-based dealings. Thus, it is the constitutional

as well as religious duty of Government of Pakistan to carry forth financial and economic endeavors of the State without interest to assure socio-economic wellbeing of residents of Pakistan.

Since April 2019, a bill regarding interest free financial and economic setup of Pakistan is under process, presented by a parliamentarian in National assembly of Pakistan. Since 1947 to date all the political parties along with forefathers of the nation supported the notion of leading economy of Pakistan without interest and in compliance to Islamic Shariah so that sustainable financial and economic regimes can be established but to date has not been realized in effect. Moreover, interest based financial and economic regimes has showed the world that this system is unstable therefore more often results in frequent financial crisis throughout the world while during and post global financial crisis world has witnessed that interest free Islamic banking showed comparatively great resilience against financial crisis. To stabilize financial regimes, the developed world is reducing interest rates but not getting desired outcome because their efforts to adopt unconventional monetary policy is without any.

#### LITERATURE REVIEW

The pursual of interest based economic setup prevailing in modern world is badly failed to address human, economic and financial crisis (Foster 2019). The adherence to man-made laws and economic yet financial concepts such as interest (Riba) based debts, speculative endeavors, in one way or the other way give rise to exploitation and socio-economic injustice. All such economic, financial, and business endeavors are opposite to divine decree and when carried forth to solve one economic problem creates another economic and financial issues in the economy (Ascarya 2017). The economic setup prevailing in the modern world has given rise to enslave countries by using interest-based debts and destabilizes employment and production levels in their economies (Shabbir 2016). Whereas, Muslims are having Enlightened era of implementing shariah compliant economic setup in the first Islamic State of Madina 1400 years back. Islamic economic system which rejects interest-based debts, speculative based, gambling based economic endeavors can be applicable in today's world and is equally capable to solve economic, social yet financial ills of the world. Islam prohibits interest-Riba because it gives rise to exploitation tyranny and oppression (Ahmadi 2016).

Islam prohibits interest-based debt because of its exploitative attribute but also guides about interest free economic alternatives to solve economic and humanistic problems of the world (Saiti & Abdullah, 2016). For Muslims, the decree against involvement of interest based economic, financial conduct as revealed in Quran and Hadiths of Prophet Muhammad (PBUH) is final. Thus, interest based economic and financial conducts according to Quran acts as a supreme constitution for Muslims, will be subjected to severe punishments hereafter as well as in worldly affairs. Therefore, Muslim countries particularly in Pakistan efforts to pursue interest free financial, economic setup started soon after independence regarding submit for religious and constitutional obligation (SBP 2018). For the revival of interest free economic setup in Pakistan particularly as were practiced 1400 years ago in Islamic welfare State of Madina, the State of Pakistan is in urgent need of abduction of interest-based debt both at foreign and national level by devising interest free economic and financial avenues so that sustainable development of residents of Pakistan can be witnessed. Muslims in the world are in declining status as compared to developed world because they rely upon interest-based debt. The Muslims in the world can rise in status only if they will be a practicing Muslims as asserted by senator Choudhary Tanvir Khan (Amin 2018). For sustainable development of the masses refers to ensuring wellbeing of the humans in the economy.

In Islam sustainable economic development of the masses refers to the wellbeing of humans throughout the world however, according to Islam, sustainable economic development refers not only to increase collective income or wealth to safeguard the basic need of residents of the country but also, to satisfy spiritual needs of the residents of the economy (M Umer Chapra, 2008). Interest upon debt is an evil idea as it is tied up with exploitation and injustice. By acquiring debt upon interest, the evilistic relationship exists between debtor and creditor. Interest based economic endeavors need to be abolished because it creates not only economic problems but also affects society in multifaced dimensions (Shockley 2015).

In Islam there is only one form of acquiring debt which is without interest basis and delivered as *Qard-e-hasanah* apart from it any increase upon the amount of debt will give rise to interest or riba. As stated by last holy Prophet Muhammad (PBUH) that riba arises in lending (Iqbal 2006). However, interest whether in the form of simple interest or

Compound interest serves to accumulate collective wealth in few individual hands. In an approximation around 88 percent of global wealth is concentrated in hands of only 10 percent richest people however, out of this 50% the global wealth is concentrated in hands of 1% population controlling not only the wealth but also power throughout world. As a result, a vicious cycle of inequality arises amongst dwellers of the world. Moreover, people living below the poverty line throughout the world hold less than 1% wealth in this regard (Schwab 2017). Sustainable development is the process leading to enhancing as well as improving socio-economic opportunities and potential of every resident of the country over specific period so that quality of life in the economy could be improved. For sustainable development with respect to socio-economic and environmental approach a focused and pro-active yet feasible strategy is needed so that strategies not sustainable in approach to progress and development with respect to improving quality of life needs to be abolished (Munasinghe 2013).

Due to industrialization climate change, health and living standards deteriorated particularly in developing countries. To counter effect, the challenges the United Nations has developed sustainable development goals (2030) so that quality of life, poor health and climate de-stability shall be addressed. However, debt and sustainable development look alike as debt is employed to improve living conditions of people as well as to improve income and create entrepreneurship. Debt must be paid by evaluating borrowers' debt paying ability after satisfying his living expenditures (Júnior & Bertran 2021). Borrowings help economies to finance their developmental projects. However, the overhead level of debt in low-income economies along with emerging economies are unable to sustain its level of debt repayment which leads to imperil the growth and economic sustainability. Sustainable level of public debt is the level attained by government in their respective territories if able to pay off all its debt along with associated interest payment without any financial help to service its debt burden partially (Hakura 2020). If interest rates in the economy surpasses economic growth, then debt to GDP ratio will enhance which could lead to economic severity even financial crisis in Canada. If the government will borrow to service its debt, the country's debt upon interest will enhance respectively. If the economy grows swiftly than the interest rates upon debt then country's debt to GDP ratio will fall (Robson 2021).

Public debt in Pakistan has been increased since 2018 as Government has paid 7.5 trillion interest amounts to service its public debt (General 2021). Debt to GDP ratio of Pakistan has been increased from 85.9% in 2019 to 87.6% in June 2021. The Government of Pakistan has allocated 3.060 trillion for fiscal year 2021-2022 for debt servicing (Asad 2021). Foreign dependency undermines development in the dependent country as dependent country follows policies of foreign country or its representatives which undermines growth in the economy, speed up environmental deterioration, thus overall affects economic sustainability and development in the economic setup of dependent country (Britannica, n.d). Due to Pakistan's reliance upon debt to assure economic stability in the country is projecting / accelerating different problems such as inflation, lowest most public expenditure, no or lesser innovation and productivity. The debt to GDP ratio of Pakistan in 2021 has been witnessed to 84% which is very alarming to realize that solution of Pakistan does not lie in debt creation instead we have to change the policies from debt to be productive economy. Pakistan is facing highest most inflation in 48 years due to which the prices of the essential commodities are very high (Dilawar 2023).

#### METHODOLOGY

The research design is qualitative through approach content analysis (content analysis) (Bryman, 2012). This qualitative selection factor is appropriate with research specifications that aim to comprehensively understand the strategy clarification. This step is in line with the characteristics of the data qualitative that focuses on description descriptively, verbal, and based notes documentation information (Piaw 2011).

Qualitative methodology is applied to pursue subjective study upon foreign debt undermining sustainable development of residents of Pakistan. The conceptual framework is built by using inductive paradigm to discuss about Pakistan's reliance upon foreign debt which in counteract undermines the sustainable development of the masses of Pakistan. Whilst it is the constitutional and religious obligation of the State to develop human capacity of the country in compliance to Islamic Shariah so that they can be able to lead economic, financial and social affairs of the country without interest basis so that sustainable development can be witnessed. Nevertheless, due to exceedingly large volume of interest-based debt

burden the government of Pakistan is unable to invest in developing its residents, public infrastructure and achieve sustainable development goals for the country.

## DISCUSSION

There is unanimous consent amongst all Muslims of world with respect to interest-riba abolition through all financial and economic endeavors in Islamic Shariah. Thus, State's indulgence in riba-based debt for carrying economic and financial affairs of the country goes against constitutional clauses particularly becomes void as per Islamic ideology of Pakistan. However, the standing committee of the senate with complete agreement passed bill against interest charged upon debt at individual or private level in capital territory of Islamabad (Haq 2018). Now question arises that interest-based debt at individual level in Pakistan cannot be dealt but at State level can be legitimated to be dealt in. While, in Islam shariah rulings against any economic, social, financial ill applies not only individually but also collectively. In Islam, basic reasons against prohibition of interest based-debt is due to the reason that it affects society in terms of increasing poverty by reducing purchasing power of residents of country also, results in increase of unlawful activities due to which inequitable distribution of wealth takes place (Ahmed, Siddiqui & Immamuddin 2013).

Under Islamic jurisprudence financial pursuits are important for sustainable economic development but considers interest based economic endeavors useless thus, allows many alternate forms of financial instruments which can help Muslims to avoid interest and can be carried by the State (Alharbi 2015). In the beginning era of Islamic history, Muslims have developed financial system which was operative without interest basis. They have pursued successfully financial system where they carried their business transactions on the basis of participative mode of financing by sharing profit and loss through *Mudarabah*, *Musharakah* instruments and without interest-based loans to fulfil consumers' needs (Muhammad Umer Chapra & Khan 2000). However, interest based economic and financial setup established in Muslim territories has taken place in the reign of western colonization (Habib, Mohieldin, Verbeek & Aboulmagd 2015).

The objective resolution of Pakistan was passed in 1949 which affirms that Islam is the State religion of Pakistan also, is the preamble of Pakistan's

existing constitution declares that no law would be pursued in Pakistan if in conflict with the injunction of Quran and Islamic Shariah (Mukhtar 2016). Then how come State of Pakistan along with its statutory organizations undertakes interest based economic and financial endeavors in lieu of Islamic Shariah.

However, due to adherence of State in pursual of interest based financial dealings, the Government is indulged in wagging war against divine powers according to Quranic revelations thus as an outcome of such practices *barakah* is devolved from economy of Pakistan. Such as people of Pakistan time to time faces shortages of wheat and sugar while Pakistan is an agricultural country (Sehgal 2020). Purchasing power of majority segment of population is lowered due to increase in the prices of every commodity also, the value of Pakistani currency depreciated 35% since 2018 (Business, 2020). The example of descendance in the virtue of Barakah from the economy can be described by the growth in real GDP of the country which is 0.5% while it had been 1.0% in 2019 (CEIC 2020). Growth in real GDP in October has been witnessed -0.4% (IMF 2020). Almost 6.65 million people are unemployed in 2020 while previously in 2019 almost 5.80 million people were jobless. It is expected that for coming year the rate for unemployment will increase 9.56% approximately (Mian 2020). Debt to GDP ratio of Pakistan has reached 84.80% of GDP (economics, 2020a). In the history of Pakistan growth rate has never been reached to negative figure, corruption has been doubled, inflation is at the highest (Naz Baloch 2020).

As interest based financial setup is operative in the country through conventional banking and mainly through external debt acquired through foreign regulatory agencies, financial institutions, and foreign investors. The sovereignty of the country is at stake due to the heavy burden of interest upon debt and its repayments. Such as gross domestic debt of Pakistan is USD 33,711.7 Billion which comprises of government public debt and IMF debt (Arifeen 2019). However, total reserves of country in USD are 18,105.1 million as per 20<sup>th</sup> March 2020 consisted of mainly borrowed money than earned money. The total debt and liabilities of Pakistan consists of government domestic debt and external debt as per December 2019 accounts for USD 40, 993.5 billion (Arifeen 2019). Each year Pakistan has to borrow more debt in order to balance its budget deficit and refinancing of interest payments owed against interest-based debt.

Moreover, Inflation in Pakistan has increased from 3.93% in 2018's to 7.64% in 2019. In presence of budget and trade deficit along with foreign loans upon interest, the Government expenditure upon Public of Pakistan towards making hospitals, educational institutes, Dams is affected badly while People of Pakistan are heavily burdened to pay off the taxes (Baloch 2019). However, in February 2020 the debt of Pakistani population has been increased to Rs. 153689 due to increase in per capita debt amount to 28% respectively and as a result funds for development in the country has been recorded the lowest within 11 years (Today 2020). Country's reliance upon interest-based debts around 84% has hijacked the Government's financial decisions in favor of its residents instead the country's sovereignty is at the stake. Inflation has been the highest most in Pakistan as yearly inflation in Pakistan is recorded at 40% this week which is basically due to IMF demand to levy higher taxes as well as petroleum prices for releasing USD 1.1 billion dollars (Times 2023). Dependency theory presumes that developed countries have been involved even to date in exploitation of poor countries or underdeveloped countries and they do it through debts, unfair trade ventures, and by the name of foreign aid (Andersen & Taylor 2007). The rich economies grant their loans upon interest to poor countries so that they can extract resources from those underdeveloped, developing or poor countries. (Hassan 2019). Riba based debts not only harms borrowers in a negative way but also the socio-economic structure of society. Interest is against establishing justice based financial structure of the society. Thus, the need arises that the Government of Pakistan fulfills its constitutional and religious responsibility by abandoning interest-based loans towards sustainable development of its masses respectively. Pakistan has increased policy rate the highest since 1996 which is 20.5 % (Bokhari 2023). The debt to GDP ratio of Pakistan in 2021 has been witnessed to 84% which is very alarming to realize that solution of Pakistan does not lie in debt creation instead change in policies is needed to shift from debt to productive economy.

### CONCLUSION

It is the constitutional responsibility of Government of Pakistan to assure sustainable development of the residents of Pakistan by the eradication of interest with respect to all economic and financial affairs of the country respectively. Interest based debt

widens socio-economic gap amongst the residents of the same economy where affluent becomes more affluent while poor get poorer. That is why Islam, and all divine religions prohibits interest in all its forms because it creates economic injustices and inequalities amongst the masses. According to Islam sustainable development of humans in an economy refers towards attainment of both tangible outcomes of productivity such as increase in Gross Domestic Product, Gross National Product, National Income for creation and equitable distribution of wealth along with satisfying intangible wellbeing of its residents such as developing human capacity of an economy spiritually to attain eternal success hereafter. Due to dependence upon interest based foreign debt Pakistan cannot fulfill its constitutional obligations regarding eradication of interest also, due to adherence upon interest based foreign debt, the State is unable to exercise its constitutional responsibility of developing human capacity of the country according to Quran and Islamic principles of Shariah to lead without interest based economic, financial, and social avenues. Also, the State is unable to perform its duty of safeguarding socio-economic wellbeing of the residents of Pakistan. Moreover, interest upon debt undermines economic growth of the country whether interest rates are higher or lower it affects sustainable development as it enhances country's dependence upon foreign policy institutions or countries thus, welfare of common man in Pakistan is undermined. Future policy implication for Government of Pakistan is to devise mechanism or policies to reduce Country's dependence upon interest-based debts so that constitutional obligation towards interest (riba) eradication can be realized in full effect also, to foster sustainable socio-economic development in Pakistan.

### AUTHOR'S CONTRIBUTIONS

Conceptualization, Dr. Gul Ghutai, Nouman Khan Kakar; methodology, Nauman Khan, Dr. Gul Ghutai, Dr. Iqbal, Nurfahiratul Azlina; validation, Nauman Khan, Dr. Gul Ghutai, Dr. Iqbal and Nurfahiratul Azlina; formal analysis, Dr. Gul Ghutai, Nouman Khan; investigation, Nouman Khan, Dr. Gul Ghutai; writing and original draft preparation, Nauman Khan, Dr. Gul Ghutai; writing, review and editing, Nauman Khan, Dr. Gul Ghutai, Dr. Iqbal, Nurfahiratul Azlina; supervision, Dr. Gul Ghutai. All authors have read and agreed to the published version of the manuscript.

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